0. EXECUTIVE SUMMARY

0.1. OBJECTIVES

The European Charter for Small Enterprises, endorsed at the Feira European Council in June 2000, considers that "some failure is concomitant with responsible initiative and risk-taking and must be mainly envisaged as a learning opportunity" and called for assessing national bankruptcy laws in the light of good practice.

The project ‘Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy’ was launched by the European Commission to identify the issues with regard to business restructuring, bankruptcy and fresh start in the European Union.

The objectives of the study were, in summary, to obtain current reliable information on the attitude of the public, the business community and financial institutions to business failure and bankruptcy and to analyse the legal consequences of insolvency.

The result of this study should allow a comparison of the situation in Europe and the United States and the drawing of policy conclusions on business failure and its consequences on entrepreneurship.

The project was conducted by the team of experts, specialised in EU law and reorganisation, set up by Philippe & Partners and Deloitte & Touche.

0.2. METHODOLOGY

The project consists of two parts:

- Part 1: Stigma on failure: this part analyses the attitude of the public, the business community and financial institutions towards business failure and bankruptcy.

- Part 2: Legal consequences of insolvency: this part analyses:
  - The existing procedures in the Member States and the US aimed at detecting businesses with financial difficulties at an early stage;
  - The possibilities, in the different Member States and the US, for economically viable businesses to continue economic activities;
  - The legal consequences of bankruptcy and the possibilities for a fresh start.

With respect to the methodology implemented, within the section related to Stigma on failure, in order to assess the extent of the Stigma, we conceived a questionnaire to send to targeted communities (general, business and financial) and organisations.

The targeted communities and organisations have been selected using the database of Deloitte & Touche (a partner of the consortium), and its international network. The list of the targeted organisations has been communicated to the European Commission before sending the questionnaire by fax.
9. CONCLUSIONS

Legal Consequences of Bankruptcy and a Fresh Start

Early intervention is a key component to business preservation. It is important that national bankruptcy-related legislation supports procedures that aim at detecting and warning businesses with difficulties at an early stage. The implementation and imposition of tools to detect businesses in distress would increase the chances of success in business recoveries. For example, independent organisations or departments within commercial courts could systematically screen companies and warn these entities at any first indications of financial difficulties. These groups should initially encourage and eventually obligate businessmen to take the appropriate steps to recover their businesses.

The European organisations that participated in this study typically mentioned late recognition of businesses in distress as the underlying causes of business failure. In the past, this has meant that once financial difficulties are recognised in a company and appropriate action is taken to remedy those, the company is beyond stages of recovery. In the event of late detection of a business in distress, in which case a business might be forced to enter bankruptcy proceedings, these proceedings should still aim at rehabilitation of the business.

It appears that most EU Member States do have legal procedures aimed at rehabilitation of distressed businesses. However, they appear to be unsuccessful and unpopular within the business community. Their unpopularity and unsuccessfulness could be attributed to the following:

- Negative Publicity. Businesses generally regard them as unnecessarily harming their reputation.
- Procedures are complex and high in cost.
- Creditors are highly protected.
- Thresholds for entry are high.
- Lack of awareness. A lot of companies seem to not be aware of all legal possibilities available to them in situations of distress.
- Slow adaptation. By the time many companies take the initiative to consult an expert, they are often beyond the stage of recovery.

In addition, there is a general sentiment among EU Member States that certain obstacles prevent a business or businessman from starting fresh once it has been previously bankrupt. Automatic restrictions and long discharge periods after bankruptcy were the main obstacles cited throughout this study. Restrictions, disqualification and prohibitions have an adverse effect on entrepreneurial activity. Most Member States believe that an early discharge for non-fraudulent debtors could stimulate the possibilities for a fresh start. For fraudulent debtors, there should be more severe restrictions placed on such businesses and individuals before they can benefit from a discharge. However, most Member States agreed that restrictions should only be placed on fraudulent debtors.
**Stigma**

Regarding the stigma associated with bankruptcy, there was a clear difference in opinion between the various types of organisations that participated in this study.

A strong stigma seems to exist within the general community, or the consumer public. The public is generally not aware about the specific concepts, the technical aspects and the legal system of bankruptcy, including the notions of cessation of payments and restructuring tools to assist in turnaround of distressed businesses. Consumer awareness about bankruptcy seems generally to be limited to individual and consumer bankruptcy cases, for which the stigma is high. However, consumer protection organisations interviewed for this study and that represent the general public also seem to have no link to the entrepreneurial culture, as their perception of business reality is filtered through the protection of consumers.

Stigma associated with bankruptcy seems to be divided within the business community. Non-fraudulent bankruptcies seem to carry very little stigma and are regarded more or less as “accidents” and the honest debtor is more or less a victim of circumstances. On the other hand, a strong stigma is associated with the fraudulent bankruptcy and the dishonest debtor.

Nevertheless, there appears to be a strong reluctance in both the business and the financial communities to dealing with a business facing difficulties. However, the business community is much more tolerant towards a business that has recovered from such difficulties.

It is possible that the stigma associated with bankrupt businesses and individuals could be diffused through availability of good and transparent information to the public. As of now, there exists a huge amount of information on the financial and legal status of entrepreneurs. However, often this information does not specify the cause of the difficulties or the bankruptcy. These reports are not very clear in helping the general community to really understand what the situation is and how to be involved within the business context. Lastly, the information is usually quite expensive, which is possibly a deterrent in providing consumers and the general public access to such information.

The organisations that participated in this study expressed a clear need for increasing external control aimed at preventing business failures. The control could be carried either by crisis managers or by judicial authorities, but without the interference of national authorities.
8. RECOMMENDATIONS

In this section we developed possible recommendations to improve the situation of entrepreneurs facing failure and previously failed entrepreneurs who wish to make a fresh start on the following levels:

- General public, business and financial community
- National authorities
- The European Union

8.1. STIGMA

8.1.1 General public, business and financial community

- General knowledge of bankruptcy / insolvency

The general public, the business and financial communities have different level of knowledge of the concepts of bankruptcy / insolvency and its consequences. The general public has limited awareness on the matter whereas the business and financial communities have a more in-depth knowledge of these concepts.

Developing informational and education programs on bankruptcy / insolvency could help reduce the stigma surrounding business failure, for example, by defining the difference between fraudulent and non-fraudulent bankrupts.

- Dealing with bankrupt businesses

A business in financial difficulties usually encounters a resistance from its business partners, financiers, creditors (who typically require guarantees) and the general public (who prefer to buy from another company) in continuing to do business.

This mentality and negative reaction against businesses in distress should be changed into a more positive perception of the situation, since the continued support from business partners, financiers, creditors and consumers could contribute in a company avoiding bankruptcy.

8.1.2. National authorities

- Information on business failure

The information on business failure influences the public’s notion and attitude towards bankruptcy. National authorities should provide for clearer, more in-depth information to the general public who usually receives this information from the media, which may lack objectivity.

- Promotion of fresh start

The national authorities should promote the fresh start of previously failed businesses, by enabling and empowering them to begin new activities without being hindered by restrictions. However, this should not apply to fraudulent bankruptcies.

8. Recommendations
8. Recommendations

- **External control**

National legislation should provide for a greater control over the business activities of an entrepreneur facing difficulties or previously involved in bankruptcy. This control would reassure customers and the business and financial community. It could be either of a judicial or administrative nature, or the entrepreneur’s creditors or an external manager could carry it out (preferably).

8.1.3. The European Union

The European Union should assist the national authorities to promote the informing and education of the general public and, to a lesser extent, the business and financial communities, on knowledge of bankruptcy, insolvency, the consequences, and the difference between fraudulent and non-fraudulent bankruptcies.

8.2. **EARLY WARNING**

8.2.1 General public, business and financial community

- **Earlier recognition:**

Entrepreneurs, who sometimes have difficulties to admit that their business is in financial difficulty, should be “pushed” by external advice (accountant, detection authority, etc.) to initiate recovery measures. This external advice would assist the business to analyse the situation more objectively and should intervene at an early stage in order to allow the widest range of possibilities of recovery measures.

- **Information:**

Not only should this external body intervene and provide advice at an early stage, but should also provide the debtors with a clear understanding of the various options available to him and with sufficient information regarding these options.

8.2.2. National authorities

- **Formal detection proceedings**

Special detection procedures should be implemented, whereby neutral organisations or institutions (e.g. special division of the court) have the task to systematically screen and monitor warning lights to detect businesses in financial difficulties. Such businesses should be informed of their position and be encouraged or obliged to take appropriate steps.

The fact that entrepreneurs would be confronted with an external third party was monitoring the company might have a positive effect in rescuing the company.

- **Information with regard to the legal possibilities to rescue businesses**
Entrepreneurs should be better informed of all legal possibilities offered by the legislation to enterprises in distress. Informed entrepreneurs would then be able to take the necessary steps at an earlier stage. We believe the national authorities should implement programs in order to promote reorganisation through a chamber of commerce and/or a trade register, thus providing information on the financial status of entrepreneurs.

8.2.3. The European Union

The European Union should provide the national authorities with an impetus to organise coherent and efficient detection measures, by way of uniform legislative requirements. It should also promote a control of these detection measures in order to ensure that these goals are satisfied.

8.3. BUSINESS SURVIVAL

8.3.1. General public, business and financial community

From our surveys, it became apparent that financial institutions require the appointment of a ‘crisis-manager’ to assist the enterprise in distress. According to the French experience, crisis-managers or “mandataires ad hoc” and could be appointed either by the court or the involved financial institution. An independent crisis-manager could act as a neutral party between creditors and the debtor.

The business and general communities indicated that a crisis-manager should be a third party or external expert under the control of the judiciary authorities, whereas the financial community indicated that this third party should be independent. According to the interviews, the financial community believes that the appointing a third party should be done in the strictest confidentiality, in order to avoid all potential stigmas.

A solution could be to promote the intervention of the crisis-managers or mandataires ad hoc under the control of a judiciary body operating under confidentiality. This intervention would protect not only the interest of creditors, but also the right of the entrepreneur.

8.3.2. National authorities

- Promotion of entrepreneurial culture according to European trends

National authorities should set-up special programmes in order to promote the entrepreneurial culture at a national level in accordance with and supported by the European authorities.

- Enterprises should be obliged to take action in a timely manner.

An obligation to take action in a timely manner may substantially increase the chances of rescuing an enterprise in financial difficulties. The law could therefore impose on the debtor the obligation to petition for an insolvency procedure if it can reasonably foresee that it will no longer be able to pay its debts. With regard to debtors that have
reasonable doubt as to the question of whether or not they will be able to continue paying their debts, the law could stipulate the obligation to consult with an external accountant.

- **Simplification of existing proceedings**

Recovery proceedings can be very complex and external specialised advice is usually required to guide the enterprises towards and through the process. To make this kind of proceedings more successful and popular, the proceedings should be simplified.

- **Lower requirements for entry**

Certain Member States could lower their thresholds for entry to recovery proceedings. The condition of insolvency and a possibility of recovery should be enough and could lead to more accessible proceedings.

- **Confidentiality**

Confidentiality of the proceedings could benefit the potential survival of the company. This would avoid stakeholders customers being influenced by negative and unnecessary publications in official gazettes, newspapers etc. Court hearings should only be accessible to directly involved parties (creditors, administrator etc.).

- **Costs**

The cost of recovery proceedings is sometimes an obstacle in initiating the rehabilitation process and costs should therefore be reduced.

- **Control of information to disclose**

During the reorganisation process, a debtor has to provide a lot of information (e.g. rescue plan). Control of this information by a neutral third party could increase the confidence of the creditors in their debtor.

- **New deliveries**

Once a company is in financial difficulties and is in a process of reorganisation, the company should be allowed to identify those suppliers that are critical to the business operations and continue to pay those suppliers with available cash. At the same time a plan is being formulated to rescue the company and to repay debt incurred before starting the reorganisation.

- **Specialised insolvency sections of courts**

All insolvency matters should be assigned to specialised insolvency sections of a restricted number of courts (and courts of appeal), rather than charging all courts and courts of appeal with issues relating to insolvency law. Judges specialised in insolvency issues should preside over the bankruptcy court.
• **Preferential creditors should not be kept completely out of proceedings**

A major reason for the lack of successful rehabilitation proceedings is that the procedure is sometimes only binding on unsecured creditors. We believe that there is insufficient ground for such restriction. A regulation of the scheme of arrangement should obviously take into account the difference between common unsecured creditors and preferential creditors, in the sense that the percentage to be spent on preferential creditors could exceed the percentage to be spent on common unsecured creditors. But there is insufficient reason to keep preferential creditors completely out of the scheme of arrangement.

**8.3.3. The European Union**

At the European Union, the promotion of the information to entrepreneurs of the existing possibilities for businesses in temporary distress could have an encouraging effect towards entrepreneurial activity and business survivals.

Since the various existing proceeding seem to be very complex and for that reason unpopular and unsuccessful, harmonisation of the legislation should be a long term objective.

**8.4. FRESH START**

**8.4.1. General public, business and financial community**

According to the results of the survey, there is an evident stigma affecting entrepreneurs in difficulty (namely within the general community) and entrepreneurs previously bankrupt. Therefore, even if the legislator at European and at domestic level adopts legal measures in order to promote the fresh start, there is a need to introduce a European cultural campaign promoting the fresh start and a new entrepreneurship. In Latin countries, the word “faillite” (“fallimento”, “quiebra”…) holds a very negative connotation. It seems that these cultural elements would also require a sound reflection in order to involve the three communities.

**8.4.2. National authorities**

• **Reducing stigmatising effects of bankruptcy: distinction between fraudulent and non-fraudulent debtors**

Some legislators create stigmatising effects by imposing various automatic restrictions, disqualifications or prohibitions for debtors. These kinds of measures can unnecessarily harm the image of an honest entrepreneur who failed due to, for example, an economic crisis or an illness. A clear distinction should be made between measures or regulations that apply to non-fraudulent bankruptcies and those that apply to fraudulent bankruptcies. By creating such a distinction, the attitude of third parties towards the debtor could change. Non-fraudulent debtors would not be stigmatised through association with fraudulent ones.
Furthermore, it is necessary to adopt legislation aimed at forcing the information provider (media or other) to give a clear description of the status of the entrepreneur. If the entrepreneur has previously failed, the information provider should be obliged to distinguish between fraudulent bankruptcy and non-fraudulent bankruptcy. The legislator should be capable to define the minimum threshold of information that the information provider must respect. This legislation should be conceived in order to promote information that adds value to the existing content.

**Early discharge for non-fraudulent debtors**

Early and automatic discharge from remaining debts is mandatory to promote fresh starts and entrepreneurial activity. However, tougher and more restrictive legislation should be applied to fraudulent debtors.

**8.4.3. The European Union**

At a European level, information towards entrepreneurs and the public could be provided in order to persuade people of the ‘positive’ effects a bankruptcy experience can have. Potential entrepreneurs should be informed of the discharge possibilities in order to promote entrepreneurial activity.
7. **INDICATORS TO ASSESS TO WHAT EXTENT NATIONAL BANKRUPTCY LAWS ACT AS DETERRENT TO BUSINESS SURVIVAL AND FRESH START**

In this section we have developed indicators to assess to what extent national bankruptcy laws act as deterrent to early warning, business survival and to fresh start.

We then made a comparison of these various indicators in the EU Member States and the U.S., in order to determine national best practice.

7.1. **INDICATORS**

7.1.1. Early warning

Our study reveals that formal early warning procedures are very rare, and often fail to intervene in time. Our study highlights that the underlying causes for the failure of the various early warning procedures may, among others, be as follows:

- **Late recognition:**

Entrepreneurs can sometimes have difficulties in recognising that their business is in financial difficulty. They cannot believe that ‘their’ business is in trouble and quietly hope for recovery or are persuaded that they have discovered the hole in the market. Under this pretext they put off or delay commencing rehabilitation proceedings, which leads to irretrievably lost businesses, for which liquidation becomes the only option. Speed is the essence in rescue proceedings and fast action is required in order to safeguard the assets of the enterprise.

- **Disclosure of information**

Certain laws fail to prescribe the substance of the information to be disclosed and how and when that information is to be provided. Many jurisdictions do not provide for a means of control or review of this information. A lack of transparency and accurate information regarding the financial statement of the debtor can lead to misconceptions and the inaccurate assessment of the viability of the business by creditors. As a result the early warning process fails.

7.1.2. Business survival

Our study reveals that formal rehabilitation proceedings aimed at rescuing viable businesses have been introduced in many jurisdictions. Examples are the ‘redressement judiciaire’ in France, the ‘concordat judiciaire’ in Belgium, the ‘examinership’ in Ireland. It seems however that these forms of rescue are not successful everywhere. In some countries they are rarely used and often do not achieve their aim of preventing bankruptcy proceedings. Our research highlights that

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1 Trends, 6 september 2001, “De bloedkamer gaat on line”.
2 In the year 2001, 126 procedures of ‘concordat judiciaire’ were ordered against 7.062 bankruptcy orders.
the underlying (legal) causes of the failure of these rescue proceedings could, amongst others be the following:

- **Ignorance surrounding and complexity of the legal possibilities to rescue businesses**

Rehabilitation proceedings, in contrast to bankruptcy, are in some jurisdictions not well known. The proceedings can be very complex and external specialised advice is mandatory to guide the enterprises towards and through the proper process. In some cases it is then too late to initiate rehabilitation proceedings, where the enterprise is beyond salvage.

- **Requirements for entry**

High thresholds for entry result are not conducive to the use of rehabilitation proceedings. This is the case if the proceedings can only be initiated by guaranteeing the creditors immediate payment. For example, in Austria, in addition to the conditions of insolvency, a certain percentage of unsecured debts must be paid to benefit from the procedure (see table).

- **Publicity**

The vast majority (see table) of jurisdictions require publication of the court order granting the rehabilitation process in the official gazette of the court, which results in panic or at least negative publicity and therefore loss of customers. The fact that court hearings (and meeting of creditors) are public and that parties who are not directly affected can follow the proceedings can have a negative impact on the course of the process. The surrounding publicity can unnecessarily damage the business.

It is therefore recommended that confidential procedures be provided for, based on the agreement of the major creditors, who would have a duty of confidentiality regarding the process.

- **Costs**

Rehabilitation proceedings are often too expensive for small and medium sized companies. The proceedings can be relatively complex and external advice and assistance to commence and follow the process is unavoidable. Additionally the costs associated with external advice, where the enterprise has to bear the fees of the administrator(s) is prohibitive. The cost of rehabilitation proceedings is in some cases a stumbling block to the initiation of the rehabilitation process. Most Member States have stressed that out-of-court proceedings are usually cheaper, even though the fees and expenses of the third party appointed must be paid.

- **Administration of the regime**

The long delay and the formalism of the procedure were criticised by many experts from the Member States, as a factor that deters the enterprise to initiate reorganisation proceedings.
7. Indicators to assess to what extent national bankruptcy laws act as deterrent to business survival and fresh start

- **Degree of protection against creditors during the procedures**

  A clear factor in the lack of success of reorganisation proceedings in certain EU Member States is the level of protection given to secured creditors (i.e.: the rights of secured creditors’ are not affected by the reorganisation procedure). In fact the rights of secured creditors generally take priority over all other interests: VAT, social security… Without the consent of these creditors to the reorganisation procedure, without a reduction of credit or delays to pay, the procedure has no chance of success!

- **Knowledge and functioning of the relevant courts**

  **7.1.3. Fresh start**

  In many Member States, there is an unmistakable negative attitude towards entrepreneurs who have failed. Bankruptcy law sometimes contributes to this stigma by imposing various kinds of restrictions, disqualifications or prohibitions on bankrupts. We have developed in our report a number of possible underlying (legal) causes of this stigma. It appears that many Member States are reluctant to give a second chance to those who have failed (even honestly).

  In this section a number of indicators to assess those insolvency laws which contain obstacles to a fresh start, are described.

- **Effects of bankruptcy**

  Stigmatisation can be created by the particular legal effects of a bankruptcy as such. In Belgium for example the bankrupt is to some extent limited in his freedom of action: possible interrogation by the Administrator; obligation to inform the administrator of changes of address. Belgian bankruptcy law also stipulates, as in Italy, that correspondence addressed to the bankrupt is handed over to and opened by the administrator. In a majority of countries, the bankrupt is automatically divested of control of (almost) all of his assets. This measure exists to ensure that he will not dispose of his assets and by doing so, breaching the equality between the creditors. In Italy, the bankrupt cannot abandon his domicile without the permission of the judge to whom he shall report whenever requested. In Portugal, the bankrupt’s residence is fixed in the bankruptcy declaratory sentence and he may not stay away from this assigned residence for more than 5 days without notification to the court.

  These effects tend to stigmatise the bankrupt and moreover can cause an adverse attitude towards entrepreneurial activity because of the possible financial and social costs of a failure.

- **Restrictions, disqualifications and prohibitions**

  Bankruptcy laws can sometimes impose automatic restrictions, disqualifications or prohibitions on those who are subject to bankruptcy proceedings. This results in stigmatisation and leads to an aversion towards entrepreneurial activity. In Italy for example, a bankrupt cannot pursue an occupation as a lawyer or statutory auditor.
• Distinction between honest and dishonest bankrupts

If no clear distinction is made between honest but unlucky and dishonest or fraudulent bankrupts, honest bankrupts will be stigmatised through association with the dishonest. As long as honest and dishonest bankrupts remain subject to the same bankruptcy regime, third parties are unable to see a distinction and the negative attitude will persist.

• Discharge from remaining debts

Bankruptcy legislation that has a conservative approach in its application to discharge of debts, that remain after the bankruptcy proceedings are closed, can also have a negative effect on a fresh start. In Italy for example discharge can only be obtained by the bankrupt producing evidence of good behaviour during a period of 5 years. In Germany discharge is allowed only after 6 years of good behaviour and in Greece, it will be granted only after 10 years. Long discharge periods obstruct the possibility of a fresh start. However, it is not only the discharge period that gives us an indication of the obstacles, but also the requirements necessary to obtain the discharge. In some Member States discharge is automatic but in others certain criteria must be fulfilled (for example the need to obtain an agreement with the creditors in Denmark or Italy) or opposition to the discharge is possible. Early and automatic discharge for honest bankrupts is vital to encouraging fresh starts.

For directors of a bankrupt company discharge is also important. The director of an undercharged company can be stigmatised when his mandate as director of an undischarged company is disclosed.

7.2. NATIONAL COMPARISON OF THESE INDICATORS

7.2.1. Early warning

a) Performance indicator: “Timely recognition of financial difficulties”

Objective: To detect at an early enough stage a business or entrepreneur’s financial difficulties, in order to set up adequate prevention procedures.

b) Performance indicator: “Disclosure of information by debtor”.

Objective: To assess whether the debtor is subject to an efficient supervision process for the disclosure of information regarding his own situation.

Example of best practice: Belgium

7.2.1. Business survival

a) Performance indicator: ”ignorance and complexity”
**Objective:** to determine to what extent the ignorance of legal possibilities to rescue a business and the complexity of these procedures might impede the debtor from benefiting from such rescue opportunities.

**Example of best practice:** None

**b) Performance indicator:** “requirements for entry”

**Objective:** to assess the level of requirements established by national legislation in order to benefit from rehabilitation proceedings, which, if too high, may impede the debtor from benefiting from such procedures.

**Example of best practice:** Denmark, France, UK (receivership), USA

**Comparative table:**

<table>
<thead>
<tr>
<th>CONDITIONS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
</tr>
</tbody>
</table>
| Ordinary reorganisation | • illiquidity, impending illiquidity or over indebtedness
|                      | • 40 % of the unsecured debts shall be paid
|                      | • within 2 years
| Compulsory reorganisation | • illiquidity, impending illiquidity or over indebtedness
|                      | • 20 % of the unsecured debts shall be paid
|                      | • within 2 years
|                      | • in the course of a bankruptcy proceeding
|                      | • Agreement of creditors
| Out-of-court proceedings |
| Belgium |
|          | • Temporary inability to pay debts
|          | • Continuity of the trader is threatened by problems that may lead to cessation of payments
| Denmark |
| Suspension of payments | • inability to fulfil its obligations
| Compulsory composition | • no particular conditions
| Out-of-court proceeding | • agreement of creditors
| Finland |
| Restructuring of enterprises | • Financial difficulties

7. Indicators to assess to what extent national bankruptcy laws act as deterrent to business survival and fresh start
7. Indicators to assess to what extent national bankruptcy laws act as deterrent to business survival and fresh start

<table>
<thead>
<tr>
<th></th>
<th>Indebtedness</th>
<th>viability of the enterprise</th>
<th>Agreement of creditors</th>
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<tbody>
<tr>
<td><strong>Out-of-court proceedings</strong></td>
<td></td>
<td></td>
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<tr>
<td><strong>France</strong></td>
<td></td>
<td></td>
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<tr>
<td>Independent preliminary bankruptcy</td>
<td>No default of payment</td>
<td></td>
<td></td>
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<tr>
<td>Amicable settlement procedure</td>
<td>No default of payment</td>
<td></td>
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<tr>
<td><strong>Germany</strong></td>
<td></td>
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<tr>
<td>Reorganisation based on insolvency plan</td>
<td>No default of payment</td>
<td>In the course of a bankruptcy proceeding</td>
<td></td>
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<tr>
<td>Out-of-court proceedings</td>
<td></td>
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<tr>
<td><strong>Greece</strong></td>
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<tr>
<td></td>
<td>Suspension or discontinuation of operations</td>
<td>Cessation of payments</td>
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<td></td>
<td>Bankrupt trader or trader under administration of the creditors or under provisional order of liquidation</td>
<td>Total of debts five times more than the sum of their share</td>
<td></td>
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<tr>
<td></td>
<td>Cessation of payments</td>
<td>Bankrupt trader or trader under administration of the creditors or under provisional order of liquidation</td>
<td>Total of debts five times more than the sum of their share</td>
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<tr>
<td></td>
<td>Total of debts five times more than the sum of their share</td>
<td>Capital and the reserves</td>
<td></td>
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<td></td>
<td>Inability to pay debts</td>
<td></td>
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<tr>
<td><strong>Ireland</strong></td>
<td></td>
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<tr>
<td>Examinership</td>
<td>Inability to pay debts</td>
<td>No resolution of winding up</td>
<td>Reasonable prospect of survival</td>
</tr>
<tr>
<td>** Scheme of arrangement **</td>
<td></td>
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<td></td>
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<tr>
<td><strong>Italy</strong></td>
<td></td>
<td></td>
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<tr>
<td>Controlled administration procedure</td>
<td>no bankruptcy or composition in the prior five years</td>
<td>no bankruptcy offence or other specified crimes</td>
<td></td>
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<tr>
<td>Preventive creditors' settlement procedure</td>
<td>no bankruptcy or composition in the prior five years</td>
<td>no bankruptcy offence or other specified crimes</td>
<td>possibility to rescue the trader</td>
</tr>
<tr>
<td></td>
<td>no bankruptcy or composition in the prior five years</td>
<td>no bankruptcy offence or other specified crimes</td>
<td>difficulties to meet its obligations</td>
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<tr>
<td></td>
<td>no bankruptcy or composition in the prior five years</td>
<td>no bankruptcy offence or other specified crimes</td>
<td>trader shall offer guarantees to pay all secured debts and</td>
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7. Indicators to assess to what extent national bankruptcy laws act as deterrent to business survival and fresh start

<table>
<thead>
<tr>
<th>Country</th>
<th>Indicators</th>
</tr>
</thead>
</table>
| **Luxembourg** | · 40 % of unsecured debts  
                    · trader offers to sell its assets |
| Reprieve from payment | · Temporary cessation of payments because of  
                      · Extraordinary circumstances  
                      · sufficient assets to satisfy all creditors  
                      · strong potential of survival  
                      · lost of creditworthiness  
                      · difficulties to meet its obligations  
                      · no bankruptcy decision |
| Controlled management |                                                                                         |
| **The Netherlands** | · Anticipation of inability to pay due and payable debt  
                          · Agreement of the creditors |
| Suspension of payments |                                                                                         |
| Out-of-court proceedings |                                                                                         |
| **Portugal** | · Difficult economic situation or insolvency  
                   · Economic viability and financial possibility to recover |
| **Sweden** |                                                                                         |
| Reorganisation | · Inability to pay debts as they fall due or anticipation of  
                      · Such inability |
| Composition | · Inability to pay debts as they fall due or anticipation of  
                      · Such inability  
                      · Reasonable prospect of survival  
                      · In the course of a bankruptcy proceeding |
| **Spain** | · Temporary financial distress |
| **UK** |                                                                                         |
| Receivership | · No particular conditions |
| Administration | · Inability to pay debts as they fall due or anticipation of  
                    · Such inability  
                    · The survival of the company, or an arrangement or  
                    · Composition, or a better realisation than in a winding-up,
7. Indicators to assess to what extent national bankruptcy laws act as deterrent to business survival and fresh start

<table>
<thead>
<tr>
<th>Company voluntary arrangement</th>
<th>USA</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>May be expected</td>
</tr>
<tr>
<td></td>
<td>No particular conditions</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Chapter 11</th>
<th>If filed by the debtor: no requirement</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>If filed by creditors: proof that debtor is not paying debts as they become due</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Out-of-court proceedings</th>
<th>Called a “workout” – consensual agreement between debtor and major creditors</th>
</tr>
</thead>
</table>

c) Performance indicator: “publicity”

Objective: to identify whether the publicity obligations provided by the national legislation will have a harmful effect on the rehabilitation process.

Example of best practice: France, USA

Comparative table:

<table>
<thead>
<tr>
<th>PUBLICITY OF THE PROCEDURE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
</tr>
<tr>
<td>· publication through Internet</td>
</tr>
<tr>
<td>Belgium</td>
</tr>
<tr>
<td>· official gazette</td>
</tr>
<tr>
<td>· newspapers</td>
</tr>
<tr>
<td>Denmark</td>
</tr>
<tr>
<td>· official gazette</td>
</tr>
<tr>
<td>Finland</td>
</tr>
<tr>
<td>· official gazette</td>
</tr>
<tr>
<td>· newspapers</td>
</tr>
<tr>
<td>· trade register</td>
</tr>
<tr>
<td>· public access to court files</td>
</tr>
<tr>
<td>France</td>
</tr>
<tr>
<td>Procedure</td>
</tr>
<tr>
<td>--------------------</td>
</tr>
<tr>
<td>Independent preliminary Bankruptcy</td>
</tr>
<tr>
<td>Amicable settlement Procedure</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>Germany</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>Greece</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>Ireland</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
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<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>Italy</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>Luxembourg</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>The Netherlands</td>
</tr>
<tr>
<td></td>
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<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>Portugal</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>Spain</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
</tbody>
</table>
7. Indicators to assess to what extent national bankruptcy laws act as deterrent to business survival and fresh start

<table>
<thead>
<tr>
<th>Country</th>
<th>Indicators to assess to what extent national bankruptcy laws act as deterrent to business survival and fresh start</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sweden</td>
<td>- other measures of publicity decided by the court</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td>UK</td>
<td>- official gazette</td>
</tr>
<tr>
<td></td>
<td>- newspapers</td>
</tr>
<tr>
<td></td>
<td>- trade register</td>
</tr>
<tr>
<td></td>
<td>- mention of the reorganisation procedure on every invoice, order of goods and business letters</td>
</tr>
<tr>
<td>USA</td>
<td>- publication through Internet</td>
</tr>
<tr>
<td></td>
<td>- newspapers, TV</td>
</tr>
<tr>
<td></td>
<td>- public access to court files</td>
</tr>
</tbody>
</table>

d) Performance indicator: “costs”

Objective: to determine whether the level of costs required for the rehabilitation proceedings - in particular for small and medium enterprises - provided by the national legislation will have a harmful effect on the rehabilitation process.

Example of best practice: None

e) Performance indicator: “administration of the regime”

Objective: to assess whether the formalism and delays of the procedure set up under national legislation will be such as to deter an enterprise from initiating reorganisation proceedings.

Example of best practice: Portugal

Comparative table:

<table>
<thead>
<tr>
<th>ADMINISTRATION OF THE PROCEDURE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
</tr>
<tr>
<td>Ordinary reorganisation</td>
</tr>
<tr>
<td>------------------------</td>
</tr>
<tr>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Compulsory reorganisation</th>
<th>Bankruptcy administrator retains control</th>
</tr>
</thead>
</table>

<table>
<thead>
<tr>
<th>Belgium</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Debtor retains control</td>
</tr>
<tr>
<td></td>
<td>Supervision of administrator</td>
</tr>
<tr>
<td></td>
<td>Authorisation of administrators required for certain operations</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Denmark</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Debtor retains control</td>
</tr>
<tr>
<td></td>
<td>Supervision of the administrator</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Finland</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Debtor retains control</td>
</tr>
<tr>
<td></td>
<td>Supervision of the administrator</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>France</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Independent preliminary</td>
<td>Debtor retains control</td>
</tr>
<tr>
<td>Bankruptcy</td>
<td>Supervision of independent receiver</td>
</tr>
<tr>
<td>Amicable settlement</td>
<td>Debtor retains control</td>
</tr>
<tr>
<td>Procedure</td>
<td>Conciliator prepares the plan</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Germany</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Trustee in insolvency retains control (except if self-management ordered)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Greece</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Debtor retains control</td>
</tr>
<tr>
<td></td>
<td>Supervision of administrator</td>
</tr>
<tr>
<td></td>
<td>If debtor fails to comply with the agreement: administrator shall retain control</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Ireland</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Examinership</td>
<td>Debtor retains control on business</td>
</tr>
<tr>
<td>Scheme of arrangement</td>
<td>Examiner retains control on the procedure</td>
</tr>
<tr>
<td></td>
<td>Debtor retains control</td>
</tr>
<tr>
<td></td>
<td>No administrator</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Italy</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Debtor retains control</td>
</tr>
</tbody>
</table>
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

<table>
<thead>
<tr>
<th>Supervision of the administrator</th>
</tr>
</thead>
<tbody>
<tr>
<td>Luxembourg</td>
</tr>
<tr>
<td>Debtor retains control, BUT</td>
</tr>
<tr>
<td>Authorisation of administrator</td>
</tr>
<tr>
<td>The Netherlands</td>
</tr>
<tr>
<td>Debtor and administrator retain control jointly</td>
</tr>
<tr>
<td>Portugal</td>
</tr>
<tr>
<td>Composition</td>
</tr>
<tr>
<td>Entrepreneurial</td>
</tr>
<tr>
<td>Reconstitution</td>
</tr>
<tr>
<td>Financial restructuring</td>
</tr>
<tr>
<td>Controlled management</td>
</tr>
<tr>
<td>Debtor retains control, BUT</td>
</tr>
<tr>
<td>Sweden</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>UK</td>
</tr>
<tr>
<td>Administration</td>
</tr>
<tr>
<td>Company voluntary</td>
</tr>
<tr>
<td>Arrangement</td>
</tr>
<tr>
<td>USA</td>
</tr>
<tr>
<td></td>
</tr>
</tbody>
</table>

f) Performance indicator: “degree of protection against creditors during the procedures”

7. Indicators to assess to what extent national bankruptcy laws act as deterrent to business survival and fresh start
Objective: to identify whether the national legislation provides a particularly protective regime for secured creditors, which might be a factor of failure for a reorganisation procedure.

Example of best practice: Belgium, Finland, France, Germany, Greece, Ireland, Luxembourg, Portugal, USA

Comparative table:
## DEGREE OF PROTECTION OF CREDITORS

<table>
<thead>
<tr>
<th>Country</th>
<th>Privilege of debts arising after initiation of the procedure</th>
<th>Unsecured creditors are bound by the agreement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>•</td>
<td>•</td>
</tr>
<tr>
<td>Belgium</td>
<td>•</td>
<td>•</td>
</tr>
<tr>
<td>Denmark</td>
<td>•</td>
<td>•</td>
</tr>
<tr>
<td>Finland</td>
<td>•</td>
<td>•</td>
</tr>
<tr>
<td>France</td>
<td>•</td>
<td>•</td>
</tr>
<tr>
<td>Germany</td>
<td>•</td>
<td>•</td>
</tr>
<tr>
<td>Greece</td>
<td>• Privilege of debts arising after initiation of the procedure</td>
<td>• all creditors are bound by the agreement (except the employees)</td>
</tr>
<tr>
<td>Ireland</td>
<td>•</td>
<td>•</td>
</tr>
<tr>
<td>Italy</td>
<td>•</td>
<td>•</td>
</tr>
</tbody>
</table>
7. Indicators to assess to what extent national bankruptcy laws act as deterrent to business survival and fresh start

### Luxembourg

<table>
<thead>
<tr>
<th>Reprieve from payments</th>
<th>Privilege of debts arising after initiation of the procedure</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Unsecured creditors are bound by the agreement</td>
</tr>
<tr>
<td>Controlled management</td>
<td>Privilege of debts arising after initiation of the procedure</td>
</tr>
<tr>
<td></td>
<td>All creditors are bound by the agreement</td>
</tr>
</tbody>
</table>

### The Netherlands

- Privilege of debts arising after initiation of the procedure
- Unsecured creditors are bound by the agreement

### Portugal

- Privilege of debts arising after initiation of the procedure
- All creditors are bound by the agreement

### Spain

- Privilege of debts arising after initiation of the procedure
- Unsecured creditors are bound by the agreement

### Sweden

- Privilege of debts arising after initiation of the procedure
- Unsecured creditors are bound by the agreement

### UK

- Privilege of debts arising after initiation of the procedure
- Unsecured creditors are bound by the agreement

### USA

- Privilege of debts arising after initiation of the procedure
- All creditors are bound by the agreement

### g) Performance indicator: “knowledge and functioning of the relevant courts”

**Objective:** to determine whether the competent courts have the adequate knowledge and training in order to favour the success of rehabilitation proceedings.

**Example of best practice:** all except Spain

**Comparative table:**
7. Indicators to assess to what extent national bankruptcy laws act as deterrent to business survival and fresh start

7.2.3. Fresh start

a) Performance indicator: “effects of bankruptcy”

Objective: to assess to what extent the effects of bankruptcy as such may result in the stigmatisation of the debtor

Example of best practice: all countries

b) Performance indicator: “restrictions, disqualification and prohibitions”

Objective: to determine whether national legislation imposes automatic restrictions, disqualifications and prohibitions that result in the stigmatising of the bankrupt person.

Example of best practice: Greece

Comparative table:

<table>
<thead>
<tr>
<th>Country</th>
<th>Status</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>Specialised court, or specialised section or unit of civil courts</td>
</tr>
<tr>
<td>Belgium</td>
<td>Specialised court, or specialised section or unit of civil courts</td>
</tr>
<tr>
<td>Denmark</td>
<td>Specialised court, or specialised section or unit of civil courts</td>
</tr>
<tr>
<td>Finland</td>
<td>Specialised court, or specialised section or unit of civil courts</td>
</tr>
<tr>
<td>France</td>
<td>Specialised court, or specialised section or unit of civil courts</td>
</tr>
<tr>
<td>Germany</td>
<td>Specialised court, or specialised section or unit of civil courts</td>
</tr>
<tr>
<td>Greece</td>
<td>Specialised court, or specialised section or unit of civil courts</td>
</tr>
<tr>
<td>Ireland</td>
<td>Specialised court, or specialised section or unit of civil courts</td>
</tr>
<tr>
<td>Italy</td>
<td>Specialised court, or specialised section or unit of civil courts</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>Specialised court, or specialised section or unit of civil courts</td>
</tr>
<tr>
<td>The Netherlands</td>
<td>Specialised court, or specialised section or unit of civil courts</td>
</tr>
<tr>
<td>Portugal</td>
<td>Specialised court, or specialised section or unit of civil courts</td>
</tr>
<tr>
<td>Spain</td>
<td>Neither specialised court, nor specialised section or unit of civil courts</td>
</tr>
<tr>
<td>Sweden</td>
<td>Specialised court, or specialised section or unit of civil courts</td>
</tr>
<tr>
<td>UK</td>
<td>Specialised court, or specialised section or unit of civil courts</td>
</tr>
<tr>
<td>USA</td>
<td>Specialised court, or specialised section or unit of civil courts</td>
</tr>
</tbody>
</table>

POSSIBLE PROHIBITION OF CARRYING OUT COMMERCIAL ACTIVITIES AND CONDITIONS THEREFORE
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

7. Indicators to assess to what extent national bankruptcy laws act as deterrent to business survival and fresh start

<table>
<thead>
<tr>
<th>Country</th>
<th>Stigma on failure and legal consequences of bankruptcy</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>Prohibition from engaging in an independent trade or business (with exemptions)</td>
</tr>
<tr>
<td>Belgium</td>
<td>Prohibition from carrying out certain professions (auditor) or mandate (management of insurance company) under certain conditions (fraud...)</td>
</tr>
<tr>
<td>Denmark</td>
<td>Business prohibitions (if illegal removal of company’s assets)</td>
</tr>
<tr>
<td>Finland</td>
<td>Possible business prohibitions</td>
</tr>
<tr>
<td>France</td>
<td>Prohibition to practice certain activities (in case of fraudulent bankruptcy)</td>
</tr>
<tr>
<td>Germany</td>
<td>Prohibition to practice for 5 years for directors who committed criminal offenses.</td>
</tr>
<tr>
<td>Greece</td>
<td>Individual bankrupts are excluded from any commercial or industrial profession, and from certain functions (civil servant, lawyer...)</td>
</tr>
<tr>
<td>Ireland</td>
<td>Restriction from being appointed director of a company or incorporating a new company for a term of five years (unless proof of good conduct)</td>
</tr>
<tr>
<td>Italy</td>
<td>Prohibition against carrying out certain professions (lawyer, stockbroker) or charges (trustee, director...)</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>Under certain conditions (gross and indisputable mistake that lead to bankruptcy), prohibition from performing business activity</td>
</tr>
<tr>
<td>The Netherlands</td>
<td>Prohibition unless “declaration of non-objection” obtained with the Ministry of Justice</td>
</tr>
<tr>
<td>Portugal</td>
<td>Prohibition from carrying out any business, unless judge provides that they may and if no criminal proceedings</td>
</tr>
<tr>
<td>Spain</td>
<td>Prohibition from engaging in any business, unless rehabilitated.</td>
</tr>
<tr>
<td>Sweden</td>
<td>Prohibition from carrying out a business if in public interest and if severe negligence</td>
</tr>
<tr>
<td>UK</td>
<td>Prohibition from being a director, receiver or incorporating a company under certain conditions (if criminal offense, wrongful trading...)</td>
</tr>
<tr>
<td>USA</td>
<td>None, except where directors are criminally prosecuted</td>
</tr>
</tbody>
</table>

**c) Performance indicator:** “distinction between honest and dishonest bankrupts”

**Objective:** to identify whether a national legislation distinguishes between fraudulent bankruptcy and honest bankruptcy, so as to avoid stigmatising the honest bankrupt.

**Example of best practice:** Spain

**d) Performance indicator:** “discharge from remaining debts”

**Objective:** to assess whether national legislation provides for the possibility of discharge from remaining debts once the bankruptcy is closed.

**Example of best practice:** Austria, Belgium, France, Germany, Spain, UK, US

**Comparative table:**

<table>
<thead>
<tr>
<th>Liability for the Remaining Debts and Possibility of Discharge</th>
<th>Austria, Belgium, France, Germany, Spain, UK, US</th>
</tr>
</thead>
</table>

7. Indicators to assess to what extent national bankruptcy laws act as deterrent to business survival and fresh start
7. Indicators to assess to what extent national bankruptcy laws act as deterrent to business survival and fresh start

| Country   | Directors liable if committed a fault (e.g. did not file for judicial insolvency on time) | Discharge if reorganization or in the course of private bankruptcies (non-traders) | Directors liable if committed a serious fault that led to bankruptcy or if did not declare bankruptcy on time | Discharge if excusability is granted by the court (in case of innocent bankruptcy) | Directors liable after bankruptcy/winding-up procedure but not after compulsory composition | Discharge in case of release after 5 or 20 years or in case of debt rescheduling | Directors liable if did not file for bankruptcy on time or did not convene shareholders on time | Discussion on discharge | Directors liable in case of mismanagement | Yes, unless specific offenses committed | Directors liable if failed to petition for bankruptcy on time | Discharge under customer insolvency procedure | Directors liability if committed tort or did not notify creditors of cessation of payments | Discharge for individual bankrupts after 10 years or in case of judicial composition | Directors liable if do not respect their duty to protect the company’s creditors | Discharge for individual bankrupts if good behavior or creditors' settlement | Directors liable for misconduct in management or fault that led to company’s bankruptcy | Discharge if composition after bankruptcy or rehabilitation | Directors liable if their failure contributed to bankruptcy | Discharge if scheme of arrangement reached with creditors | Directors liable if significantly contributed to the company’s bankruptcy | Discharge | Directors liable if did not file for bankruptcy on time | Discharge if rehabilitation is granted (in case of non-fraudulent bankruptcy) | Directors liable if deliberately or negligently caused damage to company | Discharge | Directors liable if misfeasance, fraudulent / wrongful trading | Discharge if non-fraudulent insolvency | Individual debtor discharged from debt, except certain debts (e.g. alimony, taxes, damages for fraud…) | Corporate debtor discharged from debts |
6. **INDICATORS TO ASSESS THE INFLUENCE OF THE STIGMA OF FAILURE**

In this section we have developed indicators to assess the influence of the stigma of failure on the potential of previously failed entrepreneurs to start again and on entrepreneurship in general.

6.1. **GENERAL KNOWLEDGE AND SILENCE**

We draw attention to the fact that within the business and financial communities, the organisations targeted have an understanding of the technical notions of “bankruptcy”, “insolvency” and/or “cessation de paiements”, and the applicable legal regimes. The answers given to question 3 of the respective questionnaires reveals that most of the targeted communities have a knowledge of these notions and of the distinction between a business in distress and a business that has recovered from distress.

According to the answers received to the first question, and the interviews carried-out, the situation is totally different for those targeted organisations dealing with the general public, and consumers. Indeed, within the general (consumer) community, the answers given in the questionnaires showed that their general knowledge is limited to the notion of bankruptcy/business failure, but does not extend to the difference between insolvency and bankruptcy.

The relationship existing between the financial and business community can be considered as osmotic and transparent. However the situation is not the same in the case of those organisations dealing with general interests and consumers’ protection as they have no real link with the entrepreneurial culture. This situation prevents both consumers and small investors from being informed about “bankruptcy” and business in difficulty. Several organisations pointed out that consumers are only aware of bankruptcy when they are a direct victim of a bankruptcy case.

Often, within the general public community, the organisations targeted failed to respond to the questionnaires and interviews: 20 responses were received. During the interviews (most of which were carried out in the local language), the organisations were shown not to have a understanding or general awareness about the potential implications of bankruptcy in the consumer context. The silence or the lack of information should be considered as a strong indicator of ignorance of the implications of the bankruptcy and stigma for the general public. Unfortunately, these factors cannot be evaluated or considered scientifically or statistically. On the other hand, the business community appears to be the most “concerned” community with the issue and the survey: the questionnaires were answered with less reluctance and more ‘input’. All the organisations interviewed expressed an interest in providing input.

6.2. **THE STIGMA.**

Within the three targeted communities, in the vast majority of the Member States there is a strong stigma attached to the bankrupt entrepreneur. However, it is impossible to define national trends.
Both the financial and the business community indicated that a stigma surrounds the failure of a business (see answer 2 in the respective questionnaires). Indeed, both communities also observed that a distinction is made between a business in distress and a business that has recovered from distress. This has been underlined during the interviews and it is the official position they adopted in the questionnaires (see answer 3).

According to the answers to questions 5 and 7, the situation is quite different within the general community, where the distinction is not so clear, and where the stigma is as strong against the entrepreneur in difficulty or against the entrepreneur, who has previously failed.

During the interviews, the impression emerged that within the business community there is a kind of class complicity between entrepreneurs, namely within the crafters’ communities: financial difficulties, and eventually honest bankruptcy, are considered as expected the normal risks of business life accidents during the business life. Therefore, there is no strong stigma vis-à-vis entrepreneurs having faced difficulties and / or honest bankrupts. This is confirmed by the answers given to question 15.

A difference in approach could be identified with regard to the issue of fraudulent bankruptcy as opposed to non-fraudulent bankruptcy (see answers 4, and 7 of respective questionnaires).

Both the business (within answer 25) and the financial community (within answer 35) considered the presence of stigmas in case of fraud, and further stated that these stigmas in case of fraudulent bankruptcy should not be eliminated.

In this context, it is worth noting that the public in general mentions fraud among the four most common reasons for failure, whereas it does not appear in the reasons expressed by the business and financial communities.

6.3. THE INFORMATION

According to answer 6 of respective questionnaires, within the business and the financial community, there is a large amount of information on the financial and legal status of entrepreneurs. The vast majority of the targeted organisation within the business community consider that this is information relevant for the business sector (answer 11 of the business community questionnaire). This could also be viewed an evidence of stigma. “Why do we need so much information if we do not fear facing an entrepreneur in difficulty?” this indicator, however, cannot be considered as entirely relevant given the ease of collecting and storing such information using modern technologies (please note the sources of information mentioned by the targeted organisations within the questionnaire relating to the business community in answer 6). The organisations confirmed that information regarding the financial status of entrepreneur has always been important in terms of quantity. Potentially, currently, the information is also closer to hand.

In terms of content, the organisations confirmed that in many cases, the sources of information do not specify the cause of the difficulties or the bankruptcy, and do not often differentiate between fraudulent bankruptcy, and non-fraudulent bankruptcy, as
stated by the targeted organisations of the business community within answers 10, and 11 of the questionnaires. Therefore, prudentially, the entrepreneur could cease any commercial relationship with an entrepreneur facing difficulties, whose status is recalled by private databanks.

Within the financial community, the majority of targeted organisations (please note answer 6 of the questionnaire) considered that the financial community does keep precise data (mainly accounting and general credit information) on the history of their clients and on their eventual financial difficulties.

With respect to the general community, the organisations attach a stigma merely because of the weakness of consumers vis-à-vis the entrepreneur and because the consumer does not generally consult this kind of information (see answers 12, and 13 of the questionnaire). Some organisations pointed out that often the price of this information discourages the single consumer. In addition to the questionnaires surveyed, the general ignorant attitude of the general community was further noted by the observation that their members rely almost exclusively on the media as a source of information on business failure. The non-availability of information was confirmed by the fact that targeted organisations do not keep any specific databank on bankruptcies/business failures.

6.4. THE REASONS FOR FAILURE

The answers received are not homogeneous and are inconsistent (please note answer 22 for the financial community, answer 13 for the business community, and answer 14 for the general community). All organisations stated that in many cases the reason for the bankruptcy of a single entrepreneur is not relevant to the level of stigma attached, because the reason is not known. Conversely, it was also stressed that information on the specific reasons for failure increasing the organisations’ knowledge would provide an indispensable basis for an enlightened attitude towards these businesses.

It should be observed that the comparative analysis of the answers received from the business community with regard to large enterprises highlights that the most common highly ranked reason for business failure is management skills and poor management (please note answer 13 of the business community questionnaire). Obviously, these reasons are linked to the individual entrepreneur/ business management. Therefore, the stigma linked to business failure might follow the entrepreneur/ the business more closely than in cases of failure caused by external conditions.

Somewhat differently, the financial community (please note answer 22 for the financial community) mentioned causes for failure linked to the individual entrepreneur in the context of medium, small and micro enterprises, where the issue of management skills, relative youth or lack of experience of the entrepreneur were given high importance. On the other hand, the reasons for failure of large enterprises were more equally divided between management skills, financial causes, and external business conditions. Therefore, the stigma attached to the failure of a medium to micro enterprises seems stronger within the financial community – and may have an impact at the level of obtaining financial assistance. This position should be addressed in contrast to that of the business community, which tends to justify business failure...
by financial difficulties of medium to micro enterprises, together with negative external business conditions.

6.5. THE ROLE OF THE ORGANISATIONS IN THE PREVENTION OF FAILURE

The general community does not have enough knowledge of the prevention measures. During the interviews, 2 Italian organisations declared themselves to be in favour of strengthening the control of the judicial bodies on business.

The financial community consider that an effective means for the detection of companies in possible financial difficulties, was achieved by their members both through overall control over the management of the target company/ presence of representatives at the management bodies of the target company, and through the close follow-up of the financial state of the company (see answer n° 23 of the questionnaire).

The position of the business and financial generally favour limiting the level of public intervention in business and promoting the banking intervention in the venture (see answer 37 of the questionnaire relating to the financial community; and answer 29 of the questionnaire referring to the business community). The business community generally appeared to regret the fact that the financial community does not provide the entrepreneurs with more support, whereas the financial community appeared to desire an increase in control over businesses, while rejecting both judicial and the financial control.

Within the business community, the targeted organisations answered (answer 33) in favour of placing the external control under the judicial authority and in many cases complementing this solution with additional solutions.

We would like to add that a Dutch organisation stressed that that the legislator could just decide to provide more assistance to business facing difficulties. Therefore, according to this organisation the legislator should encourage businesses in distress to ask for technical and legal assistance (answer 31 of the questionnaire relating to the business community).

6.6. DEALING WITH A BUSINESS FACING DIFFICULTIES / PREVIOUSLY FAILED

A reluctance appears in both the business (see answer n° 14 of the business questionnaires) community where the attitude of those organisations appears to be almost fifty/fifty ...: several targeted organisations pointed out that dealing with a business facing difficulties would normally be subject to the provision of guarantees, or even cash payments) and the financial communities with regard to the idea of dealing with a business facing difficulties, expressing the stigma that is attached to this situation (see answer 28 of the questionnaire relating to the financial community).

However, the business community is much more tolerant towards a business that has recovered from such difficulties. Indeed, according to the answers (see answer n° 14 of the business community) to the surveys, it appears that the attitude adopted by the
business community towards businesses facing difficulties would often depend upon the current economic situation, the importance of the customer relationship, the nature and level of difficulties encountered, and would be decided on a case by case basis. Although the general reluctance to deal with a business facing difficulties appears quite strong, all the targeted organisations unanimously agreed that their members would be willing to deal with a business that has recovered after failure.

All the targeted financial organisations agreed that the provision of new credit to a client facing business failure is subject to a case-by-case evaluation of the situation (see answer 28 of the questionnaire relating to the financial community). This unanimous attitude reflects the reluctance of the financial community towards businesses having faced financial difficulties, and the stigma being linked to these businesses.

The general community’s approach is characterised by the consumers’ indecision as to the attitude they should adopt.

6.7. THE FRESH START

On the whole, within the general community, there is a stigma attached to the entrepreneur who has previously failed (see answer 5 of the questionnaire relating to the general community). Within the business and financial communities, the stigma is relevant. However, it should be noted that according to the interviews carried-out within the crafters’ sector the stigma is not as apparent, due to the kind of sector complicity that exists.

According to the interviews carried out and the result highlighted by the answer 23, and 24, a majority of the targeted organisations from the business community appear to be favourable to the idea of the promotion, by the legislator, of the opportunities for a fresh start for a business previously involved in bankruptcy, and to the correlative elimination of the stigma surrounding the business life of an entrepreneur previously involved in a bankruptcy. However, this is not the case in relation to the stigma surrounding fraudulent bankruptcy. Almost all of the targeted organisations agreed with the idea that failed entrepreneurs often learn from their mistakes and that they will be more successful in the future, thus expressing a positive “second chance” attitude, although such entrepreneurs would have to deal with the burden of the stigma of bankruptcy, making it more difficult to achieve good results (see answer 26 of the questionnaire relating to the business community).

The financial organisations appeared to have more reservations on the elimination of stigma with a view to a fresh start (see answer 34 of the questionnaire relating to the financial community). Most of the targeted financial organisations seem to be in favour of the promotion, by the legislator, of the opportunities for a fresh start for a business previously involved in bankruptcy. The targeted financial organisations seem to be divided on the issues of whether the legislator should work to eliminate the stigma affecting the business life of an entrepreneur previously involved in a bankruptcy, and of whether the legislator should promote a fresh start and eliminate stigma for fraudulently bankrupt persons. However, most targeted organisations positively answered that their members do believe that failed entrepreneurs often learn...
from their mistakes and that they will be more successful in the future, thus expressing a certain degree of trust in failed entrepreneurs.

The financial community nevertheless almost unanimously agreed that banks (see answer 37 of the questionnaire relating to the financial community) do have an important role to play in the restart of a failed entrepreneur, and that their members would agree to the provision of new credit to an entrepreneur that has previously faced bankruptcy/failed – although the latter would be subject to the provision of adequate securities and guarantees, and to the meeting of fixed goals expressed in the business plan.

6.8. THE EXTERNAL CONTROL

The targeted organisations expressed the need for a general increase in the level of preventative external control on businesses facing difficulties and on business in bankruptcy.

According to the interviews carried out the targeted organisations of the general community, solely the intervention of the judicial powers could limit the stigma and guarantee the respect of creditors rights.

According to the survey, the business community generally speaking does not appear to believe that the legislator should strengthen the level of control over the business life of an entrepreneur previously involved – as opposed to “actually facing difficulties” - in a bankruptcy experience. The majority of the targeted organisations assessed that the external control over a business facing difficulties should not be under the power of the judicial authorities, and even less under the control of creditors (see answers 33, and 34 of the questionnaire relating to the business community). The suggestion in favour of the appointment of a crisis manager was generally well received by the business community, which agreed that it would be considered an appropriate measure both by creditors and by employees of the business facing difficulties (see answer 35 of the questionnaire relating to the business community). German organisations pointed out that the appointment of the crisis manager is already possible.

According to answer 43 of the questionnaire relating to financial community, within the financial community, external control could work to limit the stigma. The control should be carried out by crisis managers, without the intervention of the judiciary authorities. In the course of the survey, the majority of the targeted organisations in the financial community appeared to believe that the entrepreneur does consider that the external manager can reduce the stigma on business facing difficulties. The majority of the financial targeted organisations rejected the idea of judicial supervision of the external control, to which several organisations seemed to prefer the control of creditors. The targeted organisations almost unanimously agreed that creditors of a business facing difficulties would consider the appointment of a crisis manager an appropriate measure.

An UK organisation underlined the fact that businesses do not consider that a crisis manager, appointed by the court (so called court-appointed administrator), actually works to reduce the stigma.
All communities associate the external control with the protection of the rights of creditors. Therefore, it should be concluded that the Stigma will exist if the rights of creditors are not satisfied.

6.9. **LIST OF RELEVANT PERFORMANCE INDICATORS**

- **“awareness”**

  *Definition*: General knowledge in a particular community on basic distinctions associated with bankruptcy: what is bankruptcy/ business failure/insolvency, fraudulent/ non-fraudulent bankruptcy…

  *Objective*: To determine to what extent the ignorance of a particular community around the notions associated with bankruptcy might result in particularly stigmatising attitudes in the situations.

  **Most striking answers by the three communities:**
  - **General community**: Knowledge does not extend to the difference between insolvency and bankruptcy. Limited awareness on the matter.
  - **Business community**: Aware of the stigma that surrounds business failure. A distinction is made between business in distress and business that has recovered from distress.
  - **Financial community**: Ibid.

- **“attitudes”**

  *Definition*: General trends described by the targeted communities in reaction to situations of bankruptcy/ insolvency, specific case by case attitudes, for instance in the case of fraudulent bankruptcy.

  *Objective*: To determine whether the reaction is in general positive or negative, whether it differs according to the community, whether it attaches a stigma to the failure and whether it might deter a failed business/ entrepreneur from starting a new business.

  **Most striking answers by the three communities:**
  - **General community**: Stigma attached to failure in general.
  - **Business community**: More moderated: distinction is made between business in distress/ business having recovered from distress, and between fraudulent/ non-fraudulent bankruptcy.
  - **Financial community**: Ibid.

- **“information”**

  *Definition*: The sources of information relied on by the different communities.

  *Objective*: How do the sources of information on business failure used by each community influence their knowledge on bankruptcy and their attitude towards bankrupt businesses.
Most striking answers by the three communities:
- **General community**: Media (no specific databanks); not well informed.
- **Business community**: Varied sources of information (colleagues, competitors, the business sector, media, credit/financial institutions).
- **Financial community**: Specific and efficient databanks.

**“role in prevention”**

**Definition**: Whether the targeted community feels it has a role to play in the prevention of business failure.

**Objective**: To determine what this role would be, and whether it consists in an active approach: for the prevention of failure on the one hand, and for a fresh start on the other hand.

Most striking answers by the three communities:
- **General community**: Very limited role.
- **Business community**: Yes but generally not in favour of the following forms of intervention: to become involved in the management of a bankrupt person, to sell shares to a bankrupt person.
- **Financial community**: Yes. It could involve the presence of representatives of the organisation at the board of directors, overall control over management of the target company, and surveillance of the financial state of the company.

**“dealing with bankrupt businesses”**

**Definition**: Whether the members of the targeted communities generally continue to deal with businesses that are facing difficulties/ bankruptcy, including: continuing business, continuing to provide credit, etc.

**Objective**: To determine on the one hand, whether businesses facing difficulties are provided with support from their business partners, from banks, etc, and on the other hand, whether a stigma is attached to a previously failed business, which would be revealed by its partners’ reluctance to continue to deal with it.

Most striking answers by the three communities:
- **General community**: High deterrent effect: most consumer organisations would discourage their members from dealing with a business in difficulties, and would warn their members of the previous failure of a business.
- **Business community**: Relative willingness to deal with bankrupt businesses, depending on the specific case. Requirement of strong additional guarantees. Generally tolerant/open to dealing with a business in insolvency status.
- **Financial community**: Reluctance.

**“fresh start”**

**Definition**: Whether previously failed/ bankrupt businesses are given a “second chance” and are provided with the possibility to start a new business.
**Objective:** To identify any stigma linked to the start of a new business by a previously failed/ bankrupt business.

**Most striking answers by the three communities:**
- **General community:** High deterrent effect: most consumer organisations would warn their members of the previous failure of a business. However, a favourable attitude was shown to legislative promotion of opportunities.
- **Business community:** Generally favourable to legislative promotion of the opportunities for a fresh start and the correlative elimination of stigma. Limit: in the case of fraudulent bankruptcy.
- **Financial community:** Generally favourable to legislative promotion of the opportunities for a fresh start but more reluctant to the correlative elimination of stigma. Banks’ important role: provision of credit (subject to the provision of adequate securities).

- **“external control”**

**Definition:** Control which is/ could/ should be provided by domestic legislation on the business life of an entrepreneur either facing difficulties or previously involved in bankruptcy.

**Objective:** To identify the position of the three targeted communities with respect to the various forms of external control. This analysis involves the assessment of existing legislation in the area, including the level of satisfaction of the targeted communities in the member states, and the choice of the preferred form of external control (by the judicial authorities, by creditors…).

**Most striking answers by the three communities:**
- **General community:** N/A.
- **Business community:** Generally not in favour of legislative strengthening of the control over the business life of an entrepreneur previously involved in bankruptcy – as opposed to “actually” facing difficulties. In the latter case, the business community is generally reluctant to place the external control in the hands of the judicial authorities or under the control of creditors: the appointment of a crisis manager is preferred.
- **Financial community:** According to the financial community, the entrepreneur in many cases would consider that the external manager could reduce the stigma. The majority of the targeted organisations rejected judicial supervision, over which several organisations preferred the control of creditors. The appointment of a crisis manager was considered almost unanimously as an appropriate measure for the protection of creditors.
5. PRINCIPLES AND GUIDELINES FOR EFFECTIVE INSOLVENCY AND CREDITOR RIGHTS SYSTEM: ASSESSMENT TEST IN EU MEMBER STATES AND US

The Principles and Guidelines for Effective Insolvency and Creditor Rights Systems were developed by the World Bank to promote international consensus on a uniform framework to assess the effectiveness of insolvency and creditor rights systems. The Principles and Guidelines offer guidance to policymakers on their policy choices. They are a distillation of international best practice in the design of effective insolvency systems.

For the purpose of our study, we thought that it could be useful to mention the World Bank principles as a tool to get a general view of the current practices throughout the European Union and in the U.S. regarding effective insolvency and creditors rights systems.

In order to assess to what extent the principles are adopted in the different Member States and in the U.S., we designed a questionnaire based on the key elements of the 35 Principles and Guidelines. Experts were asked to mention for each principle whether the principle is: 1) fully adopted 2) almost fully adopted 3) partially adopted 4) not adopted in his/her national insolvency system.

Our approach and conclusions do not pretend to be exhaustive or to reflect the full reality of the practice. It is based on multiple choice questionnaires that we sent to our national experts, who gave us answers based on their own experience and opinion, which is necessarily personal and subjective. Our national experts being high-specialised and well-experienced practitioners, we consider their answers as highly reliable and reflective of the general practices.

The charts below compare the responses of the experts per country and per principle. The last chart shows the average of all responses for each principle per country. Preceding the charts the key elements of the relevant principles are quoted.

5.1. LEGAL FRAMEWORK FOR CREDITOR RIGHTS

Principle 1 Compatible Enforcement Systems

A modern credit-based economy requires predictable, transparent and affordable enforcement of both unsecured and secured credit claims by efficient mechanisms outside of insolvency, as well as a sound insolvency system. These systems must be designed to work in harmony.

- This principle is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of Greece and Spain where it is only partially adopted.

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1 The Principles and Guidelines can be accessed in the Best Practice directory on the Global Insolvency Law Database at www.worldbank.org/gild.
### Principle 2 Enforcement of Unsecured Rights

A regularized system of credit should be supported by mechanisms that provide efficient, transparent, reliable and predictable methods for recovering debt, including seizure and sale of immovable and movable assets and sale or collection of intangible assets such as debts owed to the debtor by third parties.

*This principle is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of Greece and the UK where it is only partially adopted.*

### Principe 3 Security Interest Legislation

The legal framework should provide for the creation, recognition, and enforcement of security interests in movable and immovable (real) property, arising by agreement or operation of law. The law should provide for the following features:

- Security interests in all types of assets, movable and immovable, tangible and intangible, including inventory, receivables, and proceeds; future or after-acquired property, and on a global basis; and based on both possessory and non-possessory interests;
- Security interests related to any or all of a debtor's obligations to a creditor, present or future, and between all types of persons;
- Methods of notice that will sufficiently publicize the existence of security interests to creditors, purchasers, and the public generally at the lowest possible cost;
- Clear rules of priority governing competing claims or interests in the same assets, eliminating or reducing priorities over security interests as much as possible.

- This principle is fully or almost fully adopted in all EU Member States. Unfortunately, we did not get any answer from our U.S. expert on this topic.

### Principle 4 Recording and Registration of Secured Rights

There should be an efficient and cost-effective means of publicizing secured interests in movable and immovable assets, with registration being the principal and strongly preferred method. Access to the registry should be inexpensive and open to all for both recording and search.

- *This principle is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of Italy and The Netherlands where it is only partially adopted.*

### Principle 5 Enforcement of Secured Rights

Enforcement systems should provide efficient, inexpensive, transparent and predictable methods for enforcing a security interest in property. Enforcement procedures should provide for prompt realization of the rights obtained in secured assets, ensuring the maximum possible recovery of asset values based on market values. Both non-judicial and judicial enforcement methods should be considered.
This principle is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of Greece, Italy and Luxembourg where it is only partially adopted.
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

Legal Framework for Creditor Rights

0 = N/A
1 = Fully Adopted
2 = Almost Fully Adopted
3 = Partially Adopted
4 = Not Adopted

Principle 1
Principle 2
Principle 3
Principle 4
Principle 5

Austria
Belgium
Denmark
Finland
France
Germany
Greece
Ireland
Italy
Luxembourg
Portugal
Spain
Sweden
The Netherlands
UK
USA
### Principle 6  Key Objectives and Policies

Though country approaches vary, effective insolvency systems should aim to:
- Integrate with a country's broader legal and commercial systems.
- Maximize the value of a firm's assets by providing an option to reorganize.
- Strike a careful balance between liquidation and reorganization.
- Provide for equitable treatment of similarly situated creditors, including similarly situated foreign and domestic creditors.
- Provide for timely, efficient and impartial resolution of insolvencies.
- Prevent the premature dismemberment of a debtor's assets by individual creditors seeking quick judgments.
- Provide a transparent procedure that contains incentives for gathering and dispensing information.
- Recognize existing creditor rights and respect the priority of claims with a predictable and established process.
- Establish a framework for cross-border insolvencies, with recognition of foreign proceedings.

*This principle is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of Germany and Greece where it is only partially adopted. In addition, principle 6 is not adopted in Spain.*

### Principle 7  Director and Officer Liability

Director and officer liability for decisions detrimental to creditors made when an enterprise is insolvent should promote responsible corporate behavior while fostering reasonable risk taking. At a minimum, standards should address conduct based on knowledge of or reckless disregard for the adverse consequences to creditors.

*This principle is fully or almost fully adopted in the U.S. and in all EU Member States.*

### Principle 8  Liquidation and Rehabilitation

An insolvency law should provide both for efficient liquidation of nonviable businesses and those where liquidation is likely to produce a greater return to creditors, and for rehabilitation of viable businesses. Where circumstances justify it, the system should allow for easy conversion of proceedings from one procedure to another.

*This principle is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of Germany, Greece, Italy and Spain where it is only partially adopted.*
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

5. Principles and guidelines for effective insolvency and creditor rights system: assessment test in EU member states and US

Legal Framework for Corporate Insolvency (1)

- Principle 6
- Principle 7
- Principle 8

0 = N/A
1 = Fully Adopted
2 = Almost Fully Adopted
3 = Partially Adopted
4 = Not Adopted

Austria  Belgium  Denmark  Finland  France  Germany  Greece  Ireland  Italy  Luxembourg  Portugal  Spain  Sweden  The Netherlands  UK  USA

2 2 2 2 2 2 2 2 2 2 2 2 2 2 2
Principle 9  Commencement: Applicability and Accessibility

A. The insolvency process should apply to all enterprises or corporate entities except financial institutions and insurance corporations, which should be dealt with through a separate law or through special provisions in the insolvency law. State-owned corporations should be subject to the same insolvency law as private corporations.

- This part of principle 9 is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of Greece, Italy and Spain where it is partially adopted. It is not adopted in Belgium.

B. Debtors should have easy access to the insolvency system upon showing proof of basic criteria (insolvency or financial difficulty). A declaration to that effect may be provided by the debtor through its board of directors or management. Creditor access should be conditioned on showing proof of insolvency by presumption where there is clear evidence that the debtor failed to pay a matured debt (perhaps of a minimum amount).

- This part of principle 9 is fully or almost fully adopted in the U.S. and in all EU Member States

C. The preferred test for insolvency should be the debtor's inability to pay debts as they come due—known as the liquidity test. A balance sheet test may be used as an alternative secondary test, but should not replace the liquidity test. The filing of an application to commence a proceeding should automatically prohibit the debtor's transfer, sale or disposition of assets or parts of the business without court approval, except to the extent necessary to operate the business.

- This part of principle 9 is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of Finland and The Netherlands where it is only partially adopted.

Principle 10  Commencement: Moratoriums and Suspension of Proceedings

A. The commencement of bankruptcy should prohibit the unauthorized disposition of the debtor's assets and suspend actions by creditors to enforce their rights or remedies against the debtor or the debtor's assets. The injunctive relief (stay) should be as wide and all embracing as possible, extending to an interest in property used, occupied or in the possession of the debtor.

- This part of principle 10 is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of Finland where it has not been adopted.

B. To maximize the value of asset recoveries, a stay on enforcement actions by secured creditors should be imposed for a limited period in a liquidation proceeding to enable higher recovery of assets by sale of the entire business or its productive units, and in a rehabilitation proceeding where the collateral is needed for the rehabilitation.

- This part of principle 10 is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of Spain where it has not been adopted and the UK where it is only partially adopted.
Principle 11 Governance: Management

A. In liquidation proceedings, management should be replaced by a qualified court-appointed official (administrator) with broad authority to administer the estate in the interest of creditors. Control of the estate should be surrendered immediately to the administrator except where management has been authorized to retain control over the company, in which case the law should impose the same duties on management as on the administrator. In creditor-initiated filings, where circumstances warrant, an interim administrator with reduced duties should be appointed to monitor the business to ensure that creditor interests are protected.

- This part of principle 11 is fully or almost fully adopted in all EU Member States with the exception of Ireland and Spain where it is only partially adopted. In the U.S. it is partially adopted.

B. There are two preferred approaches in a rehabilitation proceeding: exclusive control of the proceeding by an independent administrator or supervision of management by an impartial and independent administrator or supervisor. Under the second option complete power should be shifted to the administrator if management proves incompetent or negligent or has engaged in fraud or other misbehavior. Similarly, independent administrators or supervisors should be held to the same standard of accountability to creditors and the court and should be subject to removal for incompetence, negligence, fraud or other wrongful conduct.

- This part of principle 11 is fully or almost fully adopted in all EU Member States with the exception of Finland, Italy, The Netherlands and Spain where it is only partially adopted. In the U.S. it is not adopted.
5. Principles and guidelines for effective insolvency and creditor rights system: assessment test in EU member states and US
Principle 12 Governance: Creditors and the Creditors' Committee

Creditor interests should be safeguarded by establishing a creditors committee that enables creditors to actively participate in the insolvency process and that allows the committee to monitor the process to ensure fairness and integrity. The committee should be consulted on non-routine matters in the case and have the ability to be heard on key decisions in the proceedings (such as matters involving dispositions of assets outside the normal course of business). The committee should serve as a conduit for processing and distributing relevant information to other creditors and for organizing creditors to decide on critical issues. The law should provide for such things as a general creditors assembly for major decisions, to appoint the creditors committee and to determine the committee's membership, quorum and voting rules, powers and the conduct of meetings. In rehabilitation proceedings, the creditors should be entitled to select an independent administrator or supervisor of their choice, provided the person meets the qualifications for serving in this capacity in the specific case.

- Principle 12 is fully or almost fully adopted in the U.S. and in 8 EU Member States. It is only partially adopted in France, Ireland, Italy, Sweden, The Netherlands and the UK. It is not adopted in Belgium.

Principle 13 Administration: Collection, Preservation, Disposition of Property

The law should provide for the collection, preservation and disposition of all property belonging to the debtor, including property obtained after the commencement of the case. Immediate steps should be taken or allowed to preserve and protect the debtor's assets and business. The law should provide a flexible and transparent system for disposing of assets efficiently and at maximum values. Where necessary, the law should allow for sales free and clear of security interests, charges or other encumbrances, subject to preserving the priority of interests in the proceeds from the assets disposed.

- This principle is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of Denmark, Greece and Spain where it is only partially adopted.

Principle 14 Administration: Treatment of Contractual Obligations

The law should allow for interference with contractual obligations that are not fully performed to the extent necessary to achieve the objectives of the insolvency process, whether to enforce, cancel or assign contracts, except where there is a compelling commercial, public or social interest in upholding the contractual rights of the counter-party to the contract (as with swap agreements).

- This principle is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of France and Spain where it is only partially adopted.
Principle 15 Administration: Fraudulent or Preferential Transactions

The law should provide for the avoidance or cancellation of pre-bankruptcy fraudulent and preferential transactions completed when the enterprise was insolvent or that resulted in its insolvency. The suspect period prior to bankruptcy, during which payments are presumed to be preferential and may be set aside, should normally be short to avoid disrupting normal commercial and credit relations. The suspect period may be longer in the case of gifts or where the person receiving the transfer is closely related to the debtor or its owners.

- This principle is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of Greece where it is only partially adopted. Member States
Principle 16  Claims Resolution: Treatment of Stakeholder Rights and Priorities

A. The rights and priorities of creditors established prior to insolvency under commercial laws should be upheld in an insolvency case to preserve the legitimate expectations of creditors and encourage greater predictability in commercial relationships. Deviations from this general rule should occur only where necessary to promote other compelling policies, such as the policy supporting rehabilitation or to maximize the estate's value. Rules of priority should support incentives for creditors to manage credit efficiently.

- This part of principle 16 is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of France and Greece where it is only partially adopted.

B. The bankruptcy law should recognize the priority of secured creditors in their collateral. Where the rights of secured creditors are impaired to promote a legitimate bankruptcy policy, the interests of these creditors in their collateral should be protected to avoid a loss or deterioration in the economic value of their interest at the commencement of the case. Distributions to secured creditors from the proceeds of their collateral should be made as promptly as possible after realization of proceeds from the sale. In cases where the stay applies to secured creditors, it should be of limited specified duration, strike a proper balance between creditor protection and insolvency objectives, and provide for the possibility of orders being made on the application of affected creditors or other persons for relief from the stay.

- This part of principle 16 is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of France and Portugal where it is only partially adopted.

C. Following distributions to secured creditors and payment of claims related to costs and expenses of administration, proceeds available for distribution should be distributed pari passu to remaining creditors unless there are compelling reasons to justify giving preferential status to a particular debt. Public interests generally should not be given precedence over private rights. The number of priority classes should be kept to a minimum.

- This part of principle 16 is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of Belgium, Ireland, Sweden and Greece where it is only partially adopted. It is not adopted in Spain.
5. Principles and guidelines for effective insolvency and creditor rights system: assessment test in EU member states and US
5.3. FEATURES PERTAINING TO CORPORATE REHABILITATION

**Principle 17  Design Features of Rehabilitation Statutes**

To be commercially and economically effective, the law should establish rehabilitation procedures that permit quick and easy access to the process, provide sufficient protection for all those involved in the process, provide a structure that permits the negotiation of a commercial plan, enable a majority of creditors in favor of a plan or other course of action to bind all other creditors by the democratic exercise of voting rights (subject to appropriate minority protections and the protection of class rights) and provide for judicial or other supervision to ensure that the process is not subject to manipulation or abuse.

- This principle is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of France, Greece and Spain where it is only partially adopted.

**Principle 18  Administration: Stabilizing and Sustaining Business Operations**

The law should provide for a commercially sound form of priority funding for the ongoing and urgent business needs of a debtor during the rescue process, subject to appropriate safeguards.

- Principle 18 is fully or partially adopted in the U.S. and in 8 EU Member States. It is partially adopted in Belgium, France, Germany, Greece, Ireland, Italy and Luxembourg. It is not adopted in Spain.

**Principle 19  Information: Access and Disclosure**

The law should require the provision of relevant information on the debtor. It should also provide for independent comment on and analysis of that information. Directors of a debtor corporation should be required to attend meetings of creditors. Provision should be made for the possible examination of directors and other persons with knowledge of the debtor's affairs, who may be compelled to give information to the court and administrator.

- This principle is fully or almost fully adopted in the U.S. and in 9 EU Member States. It is partially adopted in Austria, Belgium, France and Greece. It is not adopted in Italy and Spain.
Principle 20  Plan: Formulation, Consideration and Voting

The law should not prescribe the nature of a plan except in terms of fundamental requirements and to prevent commercial abuse. The law may provide for classes of creditors for voting purposes. Voting rights should be determined by amount of debt. An appropriate majority of creditors should be required to approve a plan. Special provision should be made to limit the voting rights of insiders. The effect of a majority vote should be to bind all creditors.

- This principle is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of France, Greece, Austria and Ireland where it is only partially adopted.

Principle 21  Plan: Approval of Plan

The law should establish clear criteria for plan approval based on fairness to similar creditors, recognition of relative priorities and majority acceptance. The law should also provide for approval over the rejection of minority creditors if the plan complies with rules of fairness and offers the opposing creditors or classes an amount equal to or greater than would be received under a liquidation proceeding. Some provision for possible adjournment of a plan decision meeting should be made, but under strict time limits. If a plan is not approved, the debtor should automatically be liquidated.

- This principle is fully or almost fully adopted in the U.S. and in 10 EU Member States. It is partially adopted in Belgium, France, Greece and the UK. It is not adopted in Spain.

Principle 22  Plan: Implementation and Amendment

The law should provide a means for monitoring effective implementation of the plan, requiring the debtor to make periodic reports to the court on the status of implementation and progress during the plan period. A plan should be capable of amendment (by vote of the creditors) if it is in the interests of the creditors. The law should provide for the possible termination of a plan and for the debtor to be liquidated.

- This principle is fully or almost fully adopted in 9 EU Member States. It is partially adopted in Belgium, Denmark, Ireland, Spain, the UK and Greece. Unfortunately, we did not get any answer from our U.S. expert on this topic.

Principle 23  Discharge and Binding Effects

To ensure that the rehabilitated enterprise has the best chance of succeeding, the law should provide for a discharge or alteration of debts and claims that have been discharged or otherwise altered under the plan. Where approval of the plan has been procured by fraud, the plan should be subject to challenge, reconsidered or set aside.

- This principle is fully or almost fully adopted in the U.S. and in 11 EU Member States. It is partially adopted in Germany and Greece. It is not adopted in Italy and France.

5. Principles and guidelines for effective insolvency and creditor rights system: assessment test in EU member states and US
Principle 24 International Considerations

Insolvency proceedings may have international aspects, and insolvency laws should provide for rules of jurisdiction, recognition of foreign judgments, cooperation and assistance among courts in different countries, and choice of law.

- This principle is fully or almost fully adopted in the U.S. and in 6 EU Member States. It is partially adopted in Austria, Belgium, and Ireland. It is not adopted in Italy, Denmark, Germany, France, Spain and Greece. The question is however no more relevant under a European perspective, because of the adoption of the Council Regulation No 1346/2000 of 29 May 2000 on insolvency proceedings, which is directly applicable in all EU Member States with the exception of Denmark.
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

5. Principles and guidelines for effective insolvency and creditor rights system: assessment test in EU member states and US

Features Pertaining to Corporate Rehabilitation

0 = N/A
1 = Fully Adopted
2 = Almost Fully Adopted
3 = Partially Adopted
4 = Not Adopted

Austria  Belgium  Denmark  Finland  France  Germany  Greece  Ireland  Italy  Luxembourg  Portugal  Spain  Sweden  The Netherlands  UK  USA

### 5.4. INFORMAL CORPORATE WORKOUTS AND RESTRUCTURINGS

**Principle 25  Enabling Legislative Framework**

Corporate workouts and restructurings should be supported by an enabling environment that encourages participants to engage in consensual arrangements designed to restore an enterprise to financial viability. An enabling environment includes laws and procedures that require disclosure of or ensure access to timely, reliable and accurate financial information on the distressed enterprise; encourage lending to, investment in or recapitalization of viable financially distressed enterprises; support a broad range of restructuring activities, such as debt writeoffs, reschedulings, restructurings and debt-equity conversions; and provide favorable or neutral tax treatment for restructurings.

- *This principle is fully or almost fully adopted in the U.S. and in 7 EU Member States. It is partially adopted in Denmark, Germany, Finland, Luxembourg and Portugal. It is not adopted in Italy, Austria and Spain.*

<table>
<thead>
<tr>
<th>Principle 26  Informal Workout Procedures</th>
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<td>A country's financial sector (possibly with the informal endorsement and assistance of the central bank or finance ministry) should promote the development of a code of conduct on an informal out-of-court process for dealing with cases of corporate financial difficulty in which banks and other financial institutions have a significant exposure—especially in markets where enterprise insolvency has reached systemic levels. An informal process is far more likely to be sustained where there are adequate creditor remedy and insolvency laws. The informal process may produce a formal rescue, which should be able to quickly process a packaged plan produced by the informal process. The formal process may work better if it enables creditors and debtors to use informal techniques.</td>
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- *This principle is fully or almost fully adopted in the U.S. and in 5 EU Member States only. It is partially adopted in Denmark, France, Finland, Luxembourg and Ireland. It is not adopted in Italy, Austria, Belgium, Germany and Spain*
5. Principles and guidelines for effective insolvency and creditor rights system: assessment test in EU member states and US
5.5. IMPLEMENTATION OF THE INSOLVENCY SYSTEM

**Principle 27 Role of Courts**

Bankruptcy cases should be overseen and disposed of by an independent court or competent authority and assigned, where practical, to judges with specialized bankruptcy expertise. Significant benefits can be gained by creating specialized bankruptcy courts. The law should provide for a court or other tribunal to have a general, non-intrusive, supervisory role in the rehabilitation process. The court/tribunal or regulatory authority should be obliged to accept the decision reached by the creditors that a plan be approved or that the debtor be liquidated.

- *This principle is fully or almost fully adopted in the U.S. and in 9 EU Member States. It is partially adopted in Austria, France, Italy, Spain and Portugal. It is not adopted in Sweden.*

**Principle 28 Performance Standards of the Court, Qualification and Training of Judges**

Standards should be adopted to measure the competence, performance and services of a bankruptcy court. These standards should serve as a basis for evaluating and improving courts. They should be enforced by adequate qualification criteria as well as training and continuing education for judges.

- *This principle is fully or almost fully adopted in the U.S. and in 5 EU Member States. It is partially adopted in Belgium, France, Greece, Ireland, Italy and Sweden. It is not adopted in Denmark, Austria, Finland and Spain.*

**Principle 29 Court Organization**

The court should be organized so that all interested parties—including the administrator, the debtor and all creditors—are dealt with fairly, objectively and transparently. To the extent possible, publicly available court operating rules, case practice and case management regulations should govern the court and other participants in the process. The court's internal operations should allocate responsibility and authority to maximize resource use. To the degree feasible the court should institutionalize, streamline and standardize court practices and procedures.

- *This principle is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of France, Austria and Spain where it is only partially adopted.*

**Principle 30 Transparency and Accountability**

An insolvency systems should be based on transparency and accountability. Rules should ensure ready access to court records, court hearings, debtor and financial data and other public information.

- *This principle is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of Belgium, Denmark and Germany where it is only partially adopted. In addition, it is not adopted in Spain.*

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5. Principles and guidelines for effective insolvency and creditor rights system: assessment test in EU member states and US
Principle 31 Judicial Decision making and Enforcement

Judicial decision making should encourage consensual resolution among parties where possible and otherwise undertake timely adjudication of issues with a view to reinforcing predictability in the system through consistent application of the law. The court must have clear authority and effective methods of enforcing its judgments.

- This principle is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of France, Germany, Belgium and Spain where it is only partially adopted.

Principle 32 Integrity of the Court

Court operations and decisions should be based on firm rules and regulations to avoid corruption and undue influence. The court must be free of conflicts of interest, bias and lapses in judicial ethics, objectivity and impartiality.

- This principle is fully or almost fully adopted in the U.S. and in all EU Member States.

Principle 33 Integrity of Participants

Persons involved in a bankruptcy proceeding must be subject to rules and court orders designed to prevent fraud, other illegal activity or abuse of the bankruptcy system. In addition, the bankruptcy court must be vested with appropriate powers to deal with illegal activity or abusive conduct that does not constitute criminal activity.

- This principle is fully or almost fully adopted in the U.S. and in all EU Member States.

Principle 34 Role of Regulatory or Supervisory Bodies

The body or bodies responsible for regulating or supervising insolvency administrators should be independent of individual administrators and should set standards that reflect the requirements of the legislation and public expectations of fairness, impartiality, transparency and accountability.

- This principle is fully or almost fully adopted in the U.S. and in 9 EU Member States. It is partially adopted in Austria, Finland, Germany, Ireland and Spain. It is not adopted in Belgium.

Principle 35 Competence and Integrity of Insolvency Administrators

Insolvency administrators should be competent to exercise the powers given to them and should act with integrity, impartiality and independence.

- This principle is fully or almost fully adopted in the U.S. and in all EU Member States.
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

5. Principles and guidelines for effective insolvency and creditor rights system: assessment test in EU member states and US

Implementation of the Insolvency System (2)

0 = N/A
1 = Fully Adopted
2 = Almost Fully Adopted
3 = Partially Adopted
4 = Not Adopted

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Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

1 = Fully Adopted
2 = Almost Fully Adopted
3 = Partially Adopted
4 = Not Adopted
The graph above shows the EU and U.S. average degree of implementation for each principle. A majority of principles are on average almost fully or fully adopted. The least adopted principles are principles 26, and 28 whereas principles 9/B, 15 and 32 are adopted in most Member States.

The graph below illustrated the degree of implementation for all principles or parts of principles per country. Luxembourg, Denmark and Sweden have fully adopted a majority of principles (respectively 28 principles fully adopted in Luxembourg, 24 in Sweden and 23 in Denmark).

Portugal, whilst showing a majority of 38 fully adopted or almost fully adopted answers has the largest number of principles “almost fully adopted”.

Luxembourg, showing the largest number of principles fully adopted, totals 37 principles or parts of principles fully or almost fully adopted. Only 3 principles are partially adopted in Luxembourg as opposed to Spain, which has fully adopted or almost fully adopted 18 principles. Spain also has the largest number of principles not adopted (11). Finally, Greece shows the largest number of principles partially adopted (18).

As we already underlined, the results of the 16 questionnaires that we received from our experts are to be taken carefully and to be considered as nothing more than what they really reflect: the opinion of 16 national experts regarding the implementation of the World Bank principles in their own legal systems, based on their high experience in the matter of insolvency.

Accordingly, we believe that it is interesting to show and to describe practices throughout the EU Member States and the U.S. regarding the World Bank principles, as they are perceived by the national experts. Nevertheless, we are aware that their results cannot necessarily be extended or generalized, and that is the reason why we would not affirm that Member States that have the highest rate of implementation should be showed as examples of best practice.

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2 It should be noted that these statistics are calculated on the basis of all principles and their subdivision since each subdivision was also the object of a separate question. This gives a total of 41 questions.
5. Principles and guidelines for effective insolvency and creditor rights system: assessment test in EU member states and US

Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

Degree of implementation per country

- Number of principles not adopted
- Number of principles partially adopted
- Number of principles almost fully adopted
- Number of principles fully adopted

Austria: 3 (not adopted), 2 (partially adopted), 2 (almost fully adopted), 1 (fully adopted)
Belgium: 4 (not adopted), 5 (partially adopted), 2 (almost fully adopted), 2 (fully adopted)
Denmark: 1 (not adopted), 14 (partially adopted), 0 (almost fully adopted), 0 (fully adopted)
Finland: 1 (not adopted), 15 (partially adopted), 0 (almost fully adopted), 0 (fully adopted)
France: 1 (not adopted), 10 (partially adopted), 2 (almost fully adopted), 0 (fully adopted)
Germany: 21 (not adopted), 10 (partially adopted), 7 (almost fully adopted), 0 (fully adopted)
Greece: 7 (not adopted), 10 (partially adopted), 2 (almost fully adopted), 0 (fully adopted)
Ireland: 10 (not adopted), 18 (partially adopted), 1 (almost fully adopted), 0 (fully adopted)
Italy: 10 (not adopted), 10 (partially adopted), 0 (almost fully adopted), 0 (fully adopted)
Luxembourg: 5 (not adopted), 5 (partially adopted), 0 (almost fully adopted), 0 (fully adopted)
Portugal: 3 (not adopted), 10 (partially adopted), 0 (almost fully adopted), 0 (fully adopted)
Spain: 9 (not adopted), 10 (partially adopted), 0 (almost fully adopted), 0 (fully adopted)
Sweden: 24 (not adopted), 11 (partially adopted), 0 (almost fully adopted), 0 (fully adopted)
The Netherlands: 12 (not adopted), 12 (partially adopted), 1 (almost fully adopted), 0 (fully adopted)
UK: 5 (not adopted), 5 (partially adopted), 0 (almost fully adopted), 0 (fully adopted)
4. LEGAL CONSEQUENCES OF INSOLVENCY

4.1. DETECTION OF BUSINESSES IN DISTRESS AND WARNING LIGHTS

Early intervention of a business with potential financial problems is a key component to business preservation. Likewise, late recognition of these problems is an underlying cause of business failure. By the time the problems are recognised and appropriate action is taken, it is often too late to save the business. This title explains and compares the existing procedures in the Member States and the US that serve as warning lights for businesses in distress at an early stage and the provide tools for detecting these warning lights.

4.1.1. INTRODUCTION: THE CONCEPT OF WARNING LIGHTS AND THE ISSUE AT STAKE

The phrase “warning lights and prevention of insolvency” relates to the detection of problems within a company at a pre-critical stage and the adoption of measures to prevent further deterioration of the company’s financial situation. Warning lights can help to detect troubled companies and limit the damages that normally occur in the case of bankruptcy. Independent organisations or institutions and/or ad hoc bodies can serve greatly to facilitate the process of screening and monitoring of warning lights.

Procedures and tools for detecting financially distressed companies at an early stage and warning outsiders of these imminent problems vary from country to country. These detection tools could be formal or informal, internal or external to a company. Important questions in addressing the above are as follows: Are businesses systematically screened? By whom and how? What is the effect of such procedures in practice? Does it lead to timely liquidations or successful rescue operations?

Although warning lights and detection procedures may enable early detection of financial difficulties and thus provide a basis for their eventual rescue, these are often carried out through national provisions and procedures that favour publicity of a business’ deteriorating financial situation. The marketplace is likely to react negatively by placing a stigma of failure on the distressed business. This might deter creditors from granting credits to the business and cause the public and business partners to lose trust in the business, causing a downward spiral of the company’s financial situation and jeopardising its any potential rescue.

4.1.2. OVERVIEW OF THE NATIONAL PROCEDURES

The European law provides for numerous directives and other acts relating to financial reporting and account obligations of companies. These acts are applicable in and addressed to all Member States. It is not the purpose of our study to deal with the acquis communautaire in the matter.

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1 As examples of this acquis communautaire: Regulation 2002/3626 requiring listed companies to use International Accounting Standards by 2005; Directive of the European Parliament and of the Council amending Directives 78/660/EEC, 83/349/EEC as regards the valuation rules for the annual and consolidated accounts of certain types of companies as well as of banks and other financial institutions; Fourth Council directive 78/660/EEC of 25 July 1978 based on Article 54 (3) (g) of the Treaty on the
With respect to the mandatory publication of the annual accounts, or the obligation to call the general meeting of the shareholders in case of serious loss of the subscribed capital, these are susceptible to reveal the distress status of the concerned company. However, they cannot be qualified as “warning lights” for bankruptcy in each Member State.

Therefore, the report will reconsider these obligations or other acts of the acquis communautaire as “warning lights” just where this definition is in line with the domestic law or case law, or just legal best practice of the Member State in question.

The present section focuses primarily on specific legislative detection procedures mandated by law. Therefore, the obligation to file audited financial statements, which is mandatory and standard for all companies in the EU (because of the mentioned acquis communautaire) and public companies in the U.S., shall not be described extensively, except to the extent it plays a significant role according to its use by courts, authorities or practitioners. We attempt to identify, through a comparative approach, which countries have legislation put in place to monitor and identify distressed companies and to what extent such legislation is justified despite the potential stigmas such monitoring of companies may create.

A. AUSTRIA

A national law, the Business Reorganisation Act, introduced by the Insolvency Law Reform Act of 1997, aims at enabling businesses that are only in temporary financial difficulties, but are basically healthy, to continue to exist after having undergone a reorganisation procedure. This Act provides for a “continuation forecast”, which includes an evaluation of the anticipated yield of the company. Only the debtor can initiate this procedure by filing of an application with the court. If the application brings sufficient proof that the business needs reorganisation, the court will appoint the temporary reorganisation auditor to assist the company in its restructuring efforts. Such proceedings are not made public.

Apart from this specific procedure, the Austrian legislation provides for a general accounting obligation requiring companies to publish financial statements to the Trade Register of the registered office of the corporation. Large stock corporations also have the obligation to publish their statements in an official journal. Both

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annual accounts of certain types of companies; Seventh Council Directive 83/349/EEC of 13 June 1983 based on the article 54 (3) (g) of the Treaty on consolidated accounts; Eleventh Council Directive 89/666/EEC of 21 December 1989 concerning disclosure requirements in respect of branches opened in a Member States by certain types of company governed by the law of another State; Council Directive 91/674/EEC of 19 December 1991 on the annual accounts and consolidated accounts of insurance undertakings; Council directive 89/117/EEC of 13 February 1989 on the obligations of branches established in a Member States of credit institutions and financial institutions having their head offices outside that Member States regarding the publication of annual accounting documents; Council directive 86/635/EEC of 8 December 1986 on the annual accounts and consolidated accounts of banks and other financial institutions; Second Council Directive 77/91/EEC of 13 December 1976 on co-ordination of safeguards which, for the protection of the interest of members and others, are required by Member States of companies within the meaning of the second paragraph of Article 58 of the Treaty, in respect of formation of public limited liability companies and maintenance and alteration of their capital, with a view to making such safeguards equivalent.

4.1. Detection of businesses in difficulties and warning lights
publicly-held corporations and large private limited companies are subject to mandatory external audits of their financial statements and management reports.

The Austrian association for the protection of creditors’ rights plays a major role in assessing the economic status of the businesses (KSV, AKV). The KSV collects financial data for both companies and consumers. KSV provides opinions on the economic situation of companies or individuals.

Lastly, a helpful warning tool in detecting distressed companies is Austrian companies’ obligation to call a shareholders’ meeting according to the Article 17 of the “Second Council Directive 77/91/EEC of 13 December 1976 on co-ordination of safeguards which, for the protection of the interest of members and others, are required by Member States of companies within the meaning of the second paragraph of Article 58 of the Treaty, in respect of formation of public limited liability companies and maintenance and alteration of their capital, with a view to making such safeguards equivalent”: in the case of a serious lost of the subscribed capital, a general meeting of shareholders must be called within the period laid down by the laws of the Member States, to consider whether the company should be wound up or any other measures taken. The amount of a loss deemed to be serious within the meaning of the paragraph may not be set by the laws of Member States at a figure higher than half the subscribed capital.

B. BELGIUM

In Belgium the amended law on Judicial Composition of 1997 introduced a procedure aimed at detecting financial difficulties at an early stage. The Commercial Court systematically gathers data concerning businesses facing financial difficulties, including tax arrears, court orders, seizures, etc. A file containing this data is kept at the clerk of the Commercial Court and can be accessed by the concerned business and the public prosecutor, but not by creditors or other third parties. On the basis of the gathered information, special divisions within the Commercial Court may start an inquiry. The business pleads its case to the court and has the right to defend itself with assistance from its consultant (e.g. accountant or lawyer). Such inquiry can lead to Bankruptcy or Judicial Composition in so far as the conditions for these insolvency proceedings are fulfilled.

The objective of this system of “data collection” and subsequent “business enquiry” by the court is to monitor the financial situation of businesses in order to detect businesses in difficulties and to guide them towards the right type of insolvency procedure. The court’s duty is not to consult the business on its financial difficulties, but to monitor it and investigate the seriousness of these difficulties. The decision to petition for Bankruptcy or Judicial Composition remains a responsibility of the enterprise or, ultimately, the Public Prosecutor.

Forcing a business to answer to a competent neutral third party or a judge regarding its financial difficulties can have positive effects on the business’ managers, to the extent they may be forced to admit the existence of difficulties and the necessity to reorganise the business. To benefit from this guidance by the Commercial Court,

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2 The ‘Kreditschutzverband’ and the ‘Alpenländische Kreditorverband’

4.1. Detection of businesses in difficulties and warning lights
businesses are urged to take precautionary measures on a timely basis, so that they do not have to be heard by the court.

C. DENMARK

Apart from the common procedures and standard requirements provided by the acquis communautaire in terms of accounting and disclosures, the Danish legislator does not provide any specific measure referring to warning lights.

D. FINLAND

Finnish law requires companies to deliver their annual financial statements to the Trade Register.

In addition, the Official Journal publishes essential informations with respect to the financial status on companies.

E. FRANCE

Two main types of early warning mechanisms can be identified.

French businesses have the general accounting obligation to provide file annual accounts and annual reports. These reports are filed with the Trade Register. In addition, the Clerk of the Commercial Court keeps the following information in special registries: the register of protests for non-payment (“Registre des Protêts”), the general company lien index (“nantissements du fonds de commerce”), a specific lien index for equipment, vendor’s liens and liens on public companies and leaseback agreements on movable property, and the tax and social security lien index. These various indexes are freely accessible by the public and by the courts.

Warning procedures to detect any difficulties that could compromise the ongoing business of the company include:

a) Warnings made by the Statutory Auditor. Auditors are required by law to provide such warnings and are subject to criminal penalties in the event that these are not respected.

b) The Works Council\(^3\) warning procedure. The works council may only request information and may draft a report addressed to the concerned company. Such procedure is optional. It however enables the employees to play an important role if the company faces difficulties.

Warning procedure of the Chief Judge of the Commercial Court. The chief judge is alerted by directors of a distressed company, if the statutory auditor was not successful in commencing a warning procedure. The chief judge then calls a meeting with the directors. He cannot force the directors to cooperate with the procedure. If the directors participate in the meeting and the judge is not satisfied with their responses, he can request further information from the statutory auditor, employee

\(^3\) ‘Comité d’entreprise’: body representing the interests of the salaried.

4.1. Detection of businesses in difficulties and warning lights
representatives, public authorities, social security administration and other governmental bodies.

Such an external tool supports other mechanisms aimed at detecting a company’s difficulties without imposing on it the stigmas linked to publicity. However, its effectiveness is dependent on the will of a company’s directors.

**F. GERMANY**

In Germany, Companies are subjected to the standard internal auditing and reporting to the executive committee, as well as external auditing and submission of annual reports, which can be accessed either through the Industrial Chamber of Commerce and through private monitoring organisations.

The introduction of corporate governance, which appears as an adequate internal detection tool, in so far as employees are involved in the business internal control, but which may also incur stigmatising the business’ difficulties if the internal “transparency” is rendered public.

**G. GREECE**

In Greece, company law dictates that a significant decrease in the share capital must be reported and explained to the General Assembly, accompanied by a report of a chartered auditor.

In addition, corporate information regarding the limited liability companies is filed with the respective Registry and published in the Official Gazette. In addition, this information is made available through the several Chambers operating in Greece. Corporate information on limited liability companies is filed with the First Instance Court, is published in the Official Government Gazette and made available through the Chambers. Corporate information on general partnerships and on limited partnerships is available through the respective files kept with the First Instance Court and the Chambers. However, no financial data is available through the Chambers or through the files kept with the Court.

Financial information about businesses may be available to the public through private companies specialised in the monitoring of business to banks (only) through a company called “TIRESSIAS S.A.,” which collects data concerning any individual or legal entity that defaults on payments.

Companies limited by shares are systematically screened by their supervising authority, the Ministry of Development, but with little success. The systematic screening of companies limited by shares by the Ministry of Development – Division of Companies Limited by Shares, which operates at the Prefecture where the registered office of the company is located, consists of:

(i) The ascertainment of the payment of the share capital, the value of contributions in kind and the compliance with the relevant provisions of the law in general in the case of the establishment of a company, of an increase of its capital or a modification of its articles of association.
(ii) The observance of the provisions of the law, the company’s articles of association and the resolutions of the general meetings, the verification of the balance sheet through verification and examination of the company books, cash, portfolio and all other movable or immovable property owned by the company and the attendance at the general meetings, whenever the Minister of Development considers it expedient, of an official of the Ministry of Development representing the Minister. The aforesaid representative is entitled to supervise the control exercised by the shareholders during a general meeting.

(iii) Furthermore, the Minister of Development is entitled to demand an inspection of a company limited by shares whenever substantial reasons exist by applying to the Court. In this case, the Court is obliged to order the inspection.

The scope for such screening is for the supervising authority to ensure that the companies comply and operate in accordance with the law, the articles of association and the resolutions of their internal bodies. To that aim, Law 2190/1920 on companies limited by shares provides for penalties and fines (up to the revocation of the company’s license) in case of non-compliance of the company with the above-mentioned provisions.

Furthermore, under certain conditions, an inspection of the company can be ordered by the Court of First Instance upon an application submitted by:

(i) shareholders (representing at least 1/20 of the paid up capital),
(ii) the Stock Exchange Committee, if the shares of the company are listed on the Stock exchange,
(iii) (as already described here above) the Minister of Development whenever substantial reasons exist,
(iv) the Supervising Minister in the case of companies limited by shares carrying out public utility operations.

H. IRELAND

According to the EU Acquis, Ireland has a general accounting obligation for its companies.

In addition, directors of a company are required to call a meeting in the case that the assets of the company are half or less than half of the amount of the company’s called up share capital.

The Company Law Enforcement Act, 2001 created the Office of the Director of Corporate Enforcement, an independent state-funded agency that monitors compliance with company provisions and may investigate suspected offences. The Director has various statutory functions, including the enforcement of the Companies Acts (including criminal prosecution of summary offences), the encouragement of compliance with the Companies Acts and the investigation of suspected offences under the Companies Acts. As the Office has only recently been set up, it is difficult to evaluate the extent to which it will actually intervene in the process of checking.
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

4.1. Detection of businesses in difficulties and warning lights

businesses. Indictable (serious) offences against this Act are prosecuted by the Director of Public Prosecutions.

I. ITALY

The Italian legislation provides for a general accounting obligation and requires companies to file financial statements, accessible by the public. This is not the case, however, for individual entrepreneurs and partnerships, which are not required to make financial statements publicly available. The financial statements are centralised at the Chamber of Commerce data bank and are accessible on line to the public. However, the up-dating system is not very efficient and might prevent timely detection of difficulties.

Companies’ credit lines and credit records are registered in a data bank, which is available only to financial institutions, but the public has access to the roll of injunctions of payment and to the roll of attachment procedures kept by Courts.

In addition, some rules that may help in detecting corporate entities with financial difficulties include:
- the call of a general meeting by directors when the company’s capital is reduced by more than one third as a result of losses;
- the supervision of certain companies by a board of internal auditors (however the independence of such board is not always assured, in so far as it is appointed by the shareholders’ meeting and its fees are paid by the company);
- the entrusting of the supervision of certain companies whose shares are listed on the stock exchange to an external auditing firm: where such auditing firm renders an adverse opinion or a disclaimer, CONSOB (equivalent to the US Securities and Exchange Commission) must immediately be informed;
- the supervision of financial intermediary firms by the CONSOB and the Bank of Italy to ensure transparent and proper conduct and management of authorised entities.

The national report stressed that the timely intervention of the supervised entities has drastically reduced the number of compulsory liquidation procedures and has permitted many successful rescue operations for the benefit of the investors and the financial market itself.

J. LUXEMBOURG

Luxembourg companies are subject to the protest list, a solemn declaration before notary on behalf of the holder of an instrument of payment that it has not been paid, which compels the company, by order of the court, to make payments of its debts.

In addition, companies are required to publish accounts annually in the Trade Register. However, the Trade Register is not easily accessible to the public and there is no strict control over maintaining this register. Businesses that do not respect or follow the requirements of publishing financial statements in a timely manner do not face strict penalties.
K. THE NETHERLANDS

In the Netherlands, a company is legally obligated to notify the tax authorities, social insurance board and pension funds of its inability to pay taxes/premiums. A timely notification is within two weeks after the date the debt to the tax authorities, social insurance board and/or pension fund has become due. If the inability of payment has not been notified in time, the directors of the company could be held personally liable for the unpaid claims. However, this procedure is of practical use only for the authorities that are to be notified under these rules. Other creditors are not notified. This procedure serves as a warning light to an extent, but does not lead necessarily lead to timely liquidation or successful rescue operations.

Dutch companies have a general accounting obligation and all companies registered at the Dutch stock and options exchanges are required to submit interim reports and to make public statements in case of poor financial performance.

L. PORTUGAL

It must be observed that Portugal does not have any specific early detection system, apart from the standards accounting obligations provided by EU Acquis.

M. SPAIN

Apart from the standards accounting obligations provided by EU Acquis, Spain does not provide for specific early detection tools.

Nevertheless, several ways of noticing a company’s bad financial situation exist, such as obtaining information regarding a business, which can be either through official information sources (the Trade Register; the Property Registry; the Unpaid Acceptances Registry) or through private information sources, which have developed due to the limitations of the Official information sources (few databases and Private Investigation Agencies).

N. SWEDEN

There are several ways to detect Swedish companies facing financial difficulties.

First of all, Swedish law requires that limited companies be registered at the Patent and Registration Office. The Register contains information on the articles of association of the company, the board, auditor(s), share capital and other matters but not including ownership. The Office must be informed of any changes to this information and it can give information on whether the company has registered any floating charges. Copies of the financial year annual accounts must be filed with the Office. The Patent and Registration Office exercises a control over companies on a regular basis. It checks whether the limited companies are fulfilling all their obligations above. It can initiate an automatic compulsory liquidation procedure if the company does not fulfil its information duty toward the Trade Register (see Chapter 4.3, paragraph 2 of the Swedish report). Indeed, if these obligations are found not to have been fulfilled the company may be involuntary wound up as a result.
This information, including annual financial statements, is contained in the Trade Register, which is accessible to the public.

The state authority “enforcement service” executes judgements with respect to financial obligations. This authority provides information on companies’ unpaid debts to the state. It is possible for the public to access such information from the enforcement service.

There are also several private credit reference agencies that sell information on late payers and non-payers of debt, as well as official publications on bankruptcies and cancellations of payments related to public debt.

**O. UNITED KINGDOM**

Prevention of insolvency in the UK is mainly based on the general accounting obligation, a company’s constitution and financial status being available to the public. This policy of openness and transparency enables anyone who is interested in the affairs of a company to have access to information they need to make an informed judgement on the company’s financial affairs and the abilities of the company’s management. The official publication, consisting in the notification by the Trade Register to the Gazette of certain pieces of information, applies to all companies. The Trade Register also keeps copies of the information supplied by the company and this is made available for public inspection. Furthermore, limited companies are required by law to prepare a set of final accounts. This process is limited only to the extent that the accounts and financial statements published are fraudulent and/or are considerably out-of-date by the time they are published.

In addition to these general reporting requirements there are also statutory obligations on company directors providing penalties for those who carry on trading knowing that a company is or may become insolvent. These measures can in some cases provide a strong incentive for directors to blow the whistle at an early stage when rescue seems possible.

A number of organisations (both governmental and non-governmental) also seek to provide advice, guidance and assistance to individuals and companies experiencing financial difficulties. In recent years, there has been a particular effort made by banks to identify borrowers’ problems at an earlier stage and to provide support to resolve these issues.

In addition to formal “rescue” proceedings there are many informal “workouts” of situations in which companies have got into financial difficulties. Other strategies have been developed to informally rescue a business by reaching a consensual arrangement between a company and its major creditors. An obvious example is the banks’ “intensive care” strategies, which encompass both small and publicly quoted companies, of which the best known is the so-called “London Approach.” This involves very large, multi-banked companies. The Bank of England has sponsored the framework for this approach in the UK.

**P. USA**

4.1. Detection of businesses in difficulties and warning lights
The U.S. does not have specific legislation or “company law” that aims at monitoring if a company is in financial distress. However, the United States capital markets provide extensive procedures, both formal and informal, that monitor and gauge the financial health of companies and provide a substantial amount of data to forecast a company’s financial health and the potential for insolvency. As mentioned previously, most of these are applicable to publicly-held companies in debt.

The U.S. Securities and Exchange Commission (SEC) requires public companies to disclose meaningful financial and other information to the public, which provides a common pool of knowledge for all investors to use to judge for themselves if a company’s securities are a good investment. An example of some disclosure requirements is the filing of quarterly (10-Q) and annual (10-K) audited financial statements. The essential content of these form 10-K and registration statement information packages includes audited financial statements, a summary of selected financial data appropriate for trend analysis, and a meaningful description of the registrant’s business and financial condition. The SEC also oversees other key participants in the securities world, including stock exchanges, broker-dealers, investment advisors, mutual funds, and public utility holding companies, all which monitor companies and report those findings to the public. Therefore, indirectly the SEC is the governmental authority that regulates and monitors a public company’s financial status.

Both large and mid-sized companies and their debt are routinely and strictly evaluated and rated in financial reports produced by investment banking, brokerage houses, and other financial institutions and research groups, such as Standard & Poor’s, Moody’s Investor Services, Fitch’s, Forrester, IDC, etc. There are even specific investment banks and financial institutions that monitor companies for the purpose of investing and trading in their distressed debt and claims. Furthermore, the financial health of a company is extensively reported through various business newspapers, magazines and financial television networks.

In addition, a number of analyses and ratio tests have been created to determine financial health of a company. The Altman Z-score is the best known of these. The Altman Z-Score (developed in the 1960s by Professor Edward Altman) combines 5 financial ratios to predict specifically how close a company is to bankruptcy.

Management and turnaround consultants and financial advisors use these various detection mechanisms to monitor and identify companies that appear distressed. These advisors then approach distressed companies they have identified and offer services to assist management in reorganising their companies. This is an established and thriving practice for lawyers, accountants and turnaround/workout managers and widely accepted in the United States.

All of the above-mentioned factors and procedures interact to create a system that works efficiently to detect and monitor distressed companies.

4.1.3. COMPARATIVE ANALYSIS
This analysis compares the various systems existing in each country. It distinguishes between a) those that apply the most stringent measures and b) those that do not strictly monitor companies facing difficulties.

The issues are broken down in the following sections:

1. Preliminary analysis

2. Comparison of national systems for detecting and warning of distressed companies and potential insolvency

3. Specific weaknesses of the various systems

1. Preliminary comparative analysis:

a. Special legally mandated detection procedures

With the exception of Belgium and France, the rest of the countries analysed do not have specific and formal legislatively-mandated investigation/warning procedures for detecting businesses in distress or potential insolvencies. However, all countries do have general accounting obligations and public disclosure requirements.

Both Belgium and France have governmental, legislatively-mandated systems for detecting distressed businesses. For example, the French Works Council monitors potential companies in distress and has the authority to request a company to provide information about its financial situation. The Works Council then warns the distressed company’s directors and allows them to react to the situation without any external interference. Additionally, the law on 1997 Judicial Composition gave the Belgian Commercial Court power to detect, investigate and collect data from businesses with potential financial difficulties. Special divisions within the Commercial Court may start an inquiry and require company management to plead its case in court.

b. Public access to information

Based on the responses from the report participants, financial data on distressed companies should be made available to the public. However, the resulting publicity generated by making information publicly available might deter creditors, business partners, or the public in general from dealing with the business facing financial difficulties. This, of course, depends on the country’s individual attitude to such publicity requirements.

Our analysis shows that access to information relating to businesses can be identified through two primary means: through public sources, such as the French publicity files for liens, protests, tax and social security liens, or through private sources, such as data sold to the public by third parties at a cost. It is not clear whether either way is preferable. It seems that any public access to information might lead to future stigmas for the business. However, it depends on if the interests and protection of creditors or that of the debtors is considered.
c. **External v. internal warning lights**

Generally, procedures exist both internally and externally (to a business) that can provide a means of detecting any warning signals of financial deterioration and subsequent intervention. Some of these external procedures include business monitoring under state supervision, judicial control or intervention of judicial authorities in the detection process, private monitoring and data collection by specialised firms that then sell such data to the public, control by banks at the loan renewal stage, and other creditor checks.

Certain procedures for detecting and warning of company financial distress are also put in place internally in a company. Some of these include the internal audit function; specific company law procedures, for example the requirement of reporting changes in share capital in countries such as Finland, Greece, Italy, the U.S.; or more specific provisions, such as the introduction of corporate governance in Germany or the possibility for French shareholders to ask questions to the Board of Directors.

These provisions may be quite efficient for the detection of difficulties, but their impact may not be very significant where no mandatory measure is imposed (e.g. French Works Council; questions to Board of Directors; internal auditing), or may adversely affect the debtor in a stigmatising way where the internal measures are made known publicly (e.g. reporting of significant changes, such as a decrease in share capital).

As a concluding remark, efficient detection and warning of financially distressed companies may be ensured by granting external bodies (government, Commercial Court, etc.) the power to systematically screen and warn companies in distress at an early stage and subsequently implement a timely rescue operation.

**d. Mandatory v. optional procedures**

As previously addressed, some detection procedures are imposed by national legislation, others, such as the idea of ‘recommendations’ for the creation of liquidity plans and of the statement of assets and liabilities in Germany or the French works council procedure are not mandatory.

**2. Comparison of national systems for detecting and warning of distressed companies and potential insolvency**

Based on the analysis of national provisions, we have identified two main categories of warning lights and detection tools.

The first category (2.1) consists of tools that are created by national legislation to enable the collection and public accessibility of financial data and that might provide a basis for the detection of potential difficulties to creditors and the outside public.

The second category (2.2) describes tools aimed at monitoring businesses both internally and externally.
We will also focus on the strengths and weaknesses of these detection tools and warning lights, in light of preventing financial difficulties and distress versus preventing stigmas that might arise by enabling these tools.

2.1. Data collection tools

Data collection tools appear as the most generally used tools for the double objective of creditors information and warning light for the prevention of insolvency through early detection of difficulties.

As already mentioned previously, data collection tools include those provided under national legislation in order to collect financial data concerning businesses, such as (a) general accounting obligations and publication of financial statements, (b) the degree of specialisation of such files and (c) the impact on publicity of the company through such data collection.

The tables below provide an overview of the procedures in each country followed by an explanation of each aspect of data collection.

### DATA COLLECTION TOOLS

<table>
<thead>
<tr>
<th></th>
<th>General Accounting Obligation, Delivering financial statements</th>
<th>Publicity of financial statements</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>Exemption provided for certain traders</td>
<td>Yes</td>
</tr>
<tr>
<td>Belgium</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Denmark</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Finland</td>
<td>Yes (stricter obligation for public limited liable companies)</td>
<td>Yes</td>
</tr>
<tr>
<td>France</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Germany</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Greece</td>
<td>Yes</td>
<td>Yes for public companies, and for limited liability companies</td>
</tr>
<tr>
<td>Ireland</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Italy</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>Yes, but no control</td>
<td>No</td>
</tr>
<tr>
<td>Netherlands</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Portugal</td>
<td>Yes</td>
<td></td>
</tr>
<tr>
<td>Spain</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Sweden</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>UK</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>USA</td>
<td>Yes</td>
<td>Yes</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th></th>
<th>General centralised files (public info)</th>
<th>Specialised files</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td></td>
<td>Data collected by the association for the protection of creditors’ rights, Internet page (enforcement proceedings levied against the goods of a company/person)</td>
</tr>
<tr>
<td>Belgium</td>
<td>Yes</td>
<td>File at clerk of Commercial Court (ex. Tax arrears) Access limited to trader and public prosecutor</td>
</tr>
<tr>
<td>Denmark</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Finland</td>
<td>Yes</td>
<td></td>
</tr>
</tbody>
</table>
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

<table>
<thead>
<tr>
<th>Country</th>
<th>Detection of businesses in difficulties and warning lights</th>
</tr>
</thead>
<tbody>
<tr>
<td>France</td>
<td>Yes</td>
</tr>
<tr>
<td>Germany</td>
<td>Yes</td>
</tr>
<tr>
<td>Greece</td>
<td>Yes (Land including pledges)</td>
</tr>
<tr>
<td></td>
<td>No public access to tax data</td>
</tr>
<tr>
<td>Ireland</td>
<td>Yes</td>
</tr>
<tr>
<td></td>
<td>Yes, no public access to tax data</td>
</tr>
<tr>
<td>Italy</td>
<td>Yes</td>
</tr>
<tr>
<td></td>
<td>Yes: credit lines / records available to financial institutions only; Roll of injunctions of payment/attachment procedures: public access</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>No</td>
</tr>
<tr>
<td></td>
<td>No</td>
</tr>
<tr>
<td>Netherlands</td>
<td>No</td>
</tr>
<tr>
<td></td>
<td>No</td>
</tr>
<tr>
<td>Portugal</td>
<td>Yes</td>
</tr>
<tr>
<td>Spain</td>
<td>Yes</td>
</tr>
<tr>
<td></td>
<td>Yes: Trade Register; Unpaid acceptances Registry; Property Registry</td>
</tr>
<tr>
<td>Sweden</td>
<td>Yes</td>
</tr>
<tr>
<td></td>
<td>Yes: register; enforcement service (unpaid debts); Official publication of bankruptcies/public cancellations of payments</td>
</tr>
<tr>
<td>UK</td>
<td>Yes</td>
</tr>
<tr>
<td>USA</td>
<td>Yes</td>
</tr>
</tbody>
</table>

(a) General accounting obligation

Legislation in most countries requires companies to produce annual audited financial statements publicly.

The general accounting obligation may be, therefore, an effective tool for monitoring companies and providing warning signals for companies in financial distress, but this will not be discussed any further, as this is not in the framework of this report.

(b) Specialised files

Most countries have centralised files for collecting information that are sometimes available to the general public.

For example, France provides specialised files for centralising information with regard to liens, protests, tax and social security liens, which are accessible to the public. Similar data with regard to liens, protests, land, pledges, and property is publicly available in Greece, Italy, Spain, and the U.S. However, access to such information is limited to such information in Belgium (where access to these files is limited to the business and to the public prosecutor) and Greece. In Italy, access to files related to credit lines and credit records is limited to financial institutions, although the public nevertheless has access to the roll of injunctions of payment and attachment procedures. However, these limitations sometimes protect a business from the publicity harmful information early on by avoiding large diffusion of data concerning the business.

In the U.S., a vast amount of information related to business and individuals, including quarterly and annual financial statements, various liens, court records, bankruptcy filings and all related documents, etc., are available to anyone. However, an outsider is usually required to pay a nominal amount to access such information.
However, such specialised centralised files are not provided in some countries, such as Luxembourg and in the Netherlands.

(c) Publicity

As previously stated, most countries provide for availability of financial statements and other financial records through centralised files. The effect of such publicity on the status of businesses depends on the country’s general economic and sociological background and on the attachment to such publicity. In some Member States, it is viewed that transparency of information leads to investor confidence. However, if the information is negative, there is a risk that investor confidence will decrease and a business might carry with it a stigma of failure. The U.S. is an example of a system whereby information is extremely transparent and almost always made available to the public. It is possible that a business in the U.S. might develop a negative reputation or investor confidence might decrease due to its financial distress. However, the information serves to warn creditors, outside shareholders and other third parties of the company’s financial distress early on and allows those parties to take appropriate action to attempt to turnaround the company through reorganisation instead of liquidation. The harmful effect of negative information is therefore mitigated by the potential upside of avoiding liquidation and rescuing the company.

2.2. Business monitoring

The monitoring of businesses is one of the primary ways to actively identify companies in distress and to engage preventative measures early on. Such monitoring may be achieved through the use of internal or external detection tools available to the company or investor.

Internal detection tools

Businesses in most countries are subject to one form or another of internal detection tools, serving to detect financial difficulties within a company. Such detection and warning systems are achieved by internal company checks and through specific company law procedures.

Detection tools are more prevalent and extensive in specific forms of companies (e.g. public or regulated companies) rather than individual businesses. The extent of the detection of difficulties is thus limited to those forms of companies to which the procedure specifically applies.

(a) Internal company checks

General accounting typically leads to companies creating internal checks to act as warning signs. These checks, which are usually not mandated by law, typically include budgeting procedures, forecasting, business plans and strategic plans. This section is not intended to discuss the various types of internal checks management puts in place to detect if the company is in financial difficulty, but rather on internal company checks that is mandated by legislation.
Internal company checks are legislated in some countries, most often in particular types of companies, such as France, Germany, Greece, Ireland, Italy, the Netherlands, Spain and the US. There are however differences in the details behind the mandatory provisions required by law in each country.

These tools cover the presence of auditors and accountants and optional internal company checks.

- **Internal auditors and accountants**

  Auditors and accountants are sometimes required by legislation to warn a company when certain financial criteria are met. This section does not intend to provide an exhaustive description of such procedures. However, the role of internal auditors/accountants is worth mentioning with respect to the early identification of financial difficulties.

  In Italy, a board of internal auditors supervises public companies and certain limited liability companies (SRL). A company is considered a SRL if the SRL capital is equal or higher than € 100,000 or in the event that for two years the company does not provide for the duly publication of the required balance sheets. This board has the task to control the management of the company in order to safeguard the interests of the shareholders and of the creditors of the company. The board comprises of professionals registered with the Roll of Certified Accountants and are appointed by the shareholders. It exercises its control over the company’s management, compliance with applicable rules, accounts and financial situation. However, the independence of the board, who is appointed by the shareholders’ meeting and whose fees are paid by the company, is not always assured. Accordingly, the board’s intervention is not always punctual and does not avoid the bankruptcy.

  In the U.S., the SEC requires the companies’ accountants to maintain proper accounting records and internal controls. Although the SEC does not mandate all companies to employ internal auditors, the Blue Ribbon Committee report, which reports on good corporate governance, recommends that public companies (depending on the size) do so.

  These procedures, which must be followed on a regular and mandatory basis, provide clear warning lights for the individual business. The efficiency of these procedures may be questioned where no sanctions are provided or where the independence of the regulating body is not guaranteed.

  The use of ad hoc bodies designed to detect difficulties, although they may not per se provide warning lights, are mainly based on their preventive aim and on their confidential nature.
(b) **Specific company legal procedures**

In some Member States the company law provides for specific procedures as a means of detecting businesses in distress. However, such legislative procedures are not provided in some countries, for instance in the Netherlands, in Luxembourg or in Spain.

In Finland, Greece and Italy, these procedures are mainly based on the event that the capital decreases by a certain proportion.

France provides for the mandatory procedure where shareholders or partners submit written questions to the Board of Directors in case of knowledge of “any fact that could compromise the ongoing business of the company”.

Such internal procedures ensure identification of financial difficulties early on; searching for and identifying solutions; not disclosing the information publicly that the company is in distress; and at the same time avoiding the perceived stigmatising.

Similar to the above, is the German internal procedure by which internal audit and internal control, pass on recommendations to the executive committee of a corporation, who is obligated by law to take suitable steps to detect events that might endanger the survival of the company.

US companies are not governed by a specific company law, as many Member States, but monitored by the SEC, who enforces the securities acts (e.g. Securities Act of 1933 and Securities Exchange Act of 1934). As a result of companies’ compliance with SEC disclosure requirements and other third party data requests, enough information is made available to the public to identify companies in distress at an early stage.

**MONITORING OF BUSINESS: Internal tools**

<table>
<thead>
<tr>
<th></th>
<th>Internal company check</th>
<th>Specific company law procedures</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>No mandatory internal auditors</td>
<td>Audit and management report</td>
</tr>
<tr>
<td>Belgium</td>
<td></td>
<td>Yes</td>
</tr>
<tr>
<td>Denmark</td>
<td></td>
<td>Yes, collection by employees Stock exchange introduction</td>
</tr>
<tr>
<td>Finland</td>
<td></td>
<td>Yes, for limited liability company Liquidation if equity has decreased &lt; ½ its capital</td>
</tr>
<tr>
<td>France</td>
<td>Yes: Works Council (O) Statutory Auditor (M, in limited</td>
<td>M: questions by shareholders/partners to Board of directors</td>
</tr>
<tr>
<td>Germany</td>
<td>Yes, internal auditor, Or, creation of liquidity and of statement of assists and liabilities</td>
<td>Recommendations by the internal audit and controlling to the executive committee of corporation → must take suitable measures (M); Corporate governance</td>
</tr>
<tr>
<td>Greece</td>
<td>Yes, monitoring by auditor</td>
<td>Yes, if decrease in share capital of public company: specify purpose</td>
</tr>
<tr>
<td>Ireland</td>
<td>Or, inspection of books,</td>
<td>Yes, directors of a company must convey</td>
</tr>
</tbody>
</table>

*O: optional  
M: mandatory*
(2) External tools

For the purpose of this report, external tools must be understood as tools used to exercise a control over the financial state of businesses by an external supervisory source/entity.

External tools basically include the monitoring of the business by (a) a state authority; (b) judicial control or intervention; (c) monitoring of businesses by private specialised businesses. Most countries mandate the audit of public companies and in some cases also private enterprises. Although external auditors have valuable insight into a company, they usually only provide an audit opinion based on historical information. Auditors are typically limited to issuing a going concern warning if substantial doubt exists that the company will continue as a going concern for the next twelve months. However, this kind of warning is not usually sufficient for identifying a company in the early stages of financial distress.

(a) State authority monitoring

Most Member States lack a legislated monitoring system governed by a national authority to detect early warning signs of distressed companies. The efficiency of early detection of financial difficulties in companies may be hampered if no other detection takes place. However, some countries have limited state authorised monitoring, discussed below:

- Informing the competent authorities.

Information may take the form of notification of difficulties to competent authorities. For example, the Netherlands provides a legal obligation to timely notify the tax authorities, social insurance board, and the pension fund if the company is no longer able to pay its taxes and/or premiums (within 2 weeks the claim has become due). This procedure guarantees detection of difficulties.

The information is achieved in Belgium by allowing access to the Public Prosecutor, along with the trader, to the financial data that is collected in the file kept at the clerk of the Commercial Court. The limited access to the said data guarantees that the potentially harmful information is not made public.
Portugal has set an original out-of-court conciliation procedure, which is conducted through the mediation of a public entity, the IAPMEI. However, this institution has not been granted any sanctioning nor enforcement powers. This procedure aiming at the prevention of bankruptcy involves the intervention of creditors and business partners, but it cannot be considered strictly speaking as a warning light. Nevertheless, in so far as it is based on reaching a consensus, it does work in favour of the idea of avoiding stigmatising a business facing difficulties.

In the US, the external auditor is required to inform the SEC and the public, through the audit report, if there exists substantial doubt that the company will continue to be a going concern for the next twelve months.

- **Direct monitoring by certain authorities**

Direct monitoring consists of the supervision of particular businesses by competent authorities.

In Finland, businesses are subject to the direct monitoring by the tax authorities and by the government guarantee authority.

In Greece, the supervising authority, the Ministry of Development systematically screens limited companies – though in practice, the screening procedures offer very little to avoid insolvency. The scope for such screening is for the supervising authority to ensure that the companies do comply and operate in accordance with the law, the articles of association and the resolutions of their internal bodies. The Irish Office of the Director of Corporate Enforcement, which is an independent state-funded agency, may play a role in the checking of businesses, in so far as it monitors compliance with company provisions and may investigate suspected offences. The Director has various statutory functions, including the enforcement of the Companies Acts (including criminal prosecution of summary offences), the encouragement of compliance with the Companies Acts and the investigation of suspected offences under the Companies Acts.

In Italy, financial intermediaries for instance are subject to the supervision of CONSOB in order to ensure transparent and proper conduct and sound and prudent management. In Italy the timely intervention of the supervisory entities has drastically reduced the recourse to the compulsory administration liquidation procedure and has permitted many successful rescue-operations.

In Sweden, the state authority for execution of judgements in respect of financial obligations (the “enforcement service”) provides information relating to companies’ unpaid debts to the state. Information may be obtained as to enforcements that have been started, such as levied distress on a company’s goods.

The French Works Council warning procedure may be initiated in case of “knowledge of any fact which could compromise the ongoing status of the
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

4.1. Detection of businesses in difficulties and warning lights

This is performed in two steps, (1) the Works Council requests the company to provide information about the situation; (2) if the council is not satisfied with the response, it drafts a report addressed to the company. The Works Council however has no authority to call a shareholders’ meeting.

This procedure is optional and does not guarantee the detection of companies in distress. Furthermore, the procedure is fairly cumbersome (based on the calling of several meetings) and has been criticised for delaying the potential preventive reactions. This procedure allows for limited publicity of the company in the case of its financial distress.

In the US, all public companies and other companies with public debt, are monitored by the SEC. Although the SEC does not per se review company filings (e.g. 10K) for the purpose to identify distressed companies, but rather ensures that the full disclosure requirements are met. The result is that sufficient information is made public, together with other third party data, so that the investor pool is in a position to identify any companies in financial difficulties.

(b) Judicial control or intervention

Less than one third of the Member States provide for some form of judicial intervention as a means to detect or prevent business difficulties, which include Austria, Belgium, France, and Sweden.

In Belgium, the Commercial Court systematically collects data concerning businesses facing financial difficulties, such as tax arrears, court orders, and seizures. Special divisions of the Commercial Court may start an inquiry at their own initiative based on the information gathered. In France, the chief judge of the Commercial Court may be alerted of a company in distress by the board of directors, the statutory auditor who was unsuccessful commencing a warning procedure or by public information. He has the power to call a meeting with the board of directors. If the judge is unsatisfied with the responses given to him, he can request further information from the statutory auditor, employee representatives, public authorities, social security administration and other governmental bodies. The judicial role is therefore quite efficient at the stage of detection and prevention, though not stigmatising the business situation, as the information collected will remain in the hands of the court. These procedures are to be assessed as successful both in terms of detection and in terms of avoiding stigmatising the business at stake.

In Austria, the Trade Register Court intervenes in the process of reviewing whether the documentation submitted to the Trade Register is complete with regard to the extent required by law. There is no systematic screening process, and the Court does not review whether the content of the submitted documentation is correct.

In Sweden, the Patent and Registration Office exercises a control over companies on a regular basis. It checks whether the limited companies are fulfilling all their obligations. It can initiate an automatic compulsory liquidation procedure if the company does not fulfil its information duty toward the Trade Register.
4.1 Detection of businesses in difficulties and warning lights

In a limited number of countries is there an authority that has been set up to specifically screen and monitor companies with the intention of warning the debtor and creditor in order to attempt a rescue.

<table>
<thead>
<tr>
<th>MONITORING OF BUSINESS: External tools</th>
<th>State authority monitoring</th>
<th>Judicial control/ intervention</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>Yes, appointment of reorganisation auditor; Review of documentation: financial statements; the Trade Register court (completeness)</td>
<td></td>
</tr>
<tr>
<td>Belgium</td>
<td>Yes, Commercial Court</td>
<td>Yes, specific data collection by the commercial company</td>
</tr>
<tr>
<td>Denmark</td>
<td>Tax authority, government guarantee authority</td>
<td></td>
</tr>
<tr>
<td>Finland</td>
<td>Yes, Commercial Court</td>
<td></td>
</tr>
<tr>
<td>France</td>
<td>Yes, investigation by the chief judge of the Commercial Court</td>
<td></td>
</tr>
<tr>
<td>Germany</td>
<td>No</td>
<td>No</td>
</tr>
<tr>
<td>Greece</td>
<td>For limited co., screening by minister of development</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Not ex officio but the First Instance Court may order the control of the business where shareholders representing 1/20 of the paid-up capital of a company limited by shares request so</td>
<td></td>
</tr>
<tr>
<td>Ireland</td>
<td>Yes, office of the director of corporate enforcement (independent state-funded agency)</td>
<td></td>
</tr>
<tr>
<td>Italy</td>
<td>Supervision of CONSOB</td>
<td>Upon request of board of statutory auditors, appointment of a judicial administrator upon request shareholders representing 10% of the assets.</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>Limited (public prosecutor has insufficient means)</td>
<td></td>
</tr>
<tr>
<td></td>
<td>No</td>
<td></td>
</tr>
<tr>
<td>Netherlands</td>
<td>Notification of inability to pay to tax, social insurance, pension fund</td>
<td></td>
</tr>
<tr>
<td></td>
<td>No</td>
<td></td>
</tr>
<tr>
<td>Portugal</td>
<td>IAPMEI co-ordinates the conciliation debtor/creditors</td>
<td></td>
</tr>
<tr>
<td></td>
<td>No</td>
<td></td>
</tr>
<tr>
<td>Spain</td>
<td>No</td>
<td>No</td>
</tr>
<tr>
<td>Sweden</td>
<td>The state authority for execution of judgements in respect of financial obligations</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Patent and registration office control</td>
<td></td>
</tr>
<tr>
<td>UK</td>
<td>Yes</td>
<td>No</td>
</tr>
<tr>
<td>USA</td>
<td>Yes</td>
<td>No</td>
</tr>
</tbody>
</table>

(c) Private monitoring of businesses

Most countries allow private businesses to carry out the monitoring of companies and to sell the information and analysis gathered relating to businesses’ financial state.

In Finland, several companies are specialised in providing companies a monitoring service of other companies. The monitoring informs of the changes in companies’ clientele at desired intervals. Companies can immediately react to the improved or...
weakened financial standing, for instance by following the payment pattern of the clients, the changes of business names, creditworthiness or the rating classification. In Spain, private information sources have arisen due to the limitations of the official information sources, and include a few databases as well as Private Investigator Agencies. In Sweden, private credit reference agencies sell information on late payers and non-payers of debt. Credit rating information can be received directly via computer communication (Internet). However, banks and finance companies are not obliged to release such information about their customers without their consumers’ consent.

It is interesting to mention that in Belgium, certain courts have subscribed a membership with such providers in order to monitor the companies and to receive warning lights on line (see ‘Trends, 6 September 2001, De Bloedkamer gaat on line’).

In the US, the information and analysis that can be obtained from third parties include bond and credit ratings, analyst reports on individual companies and industries, and peer reviews in different sectors. For the American investor, whether individuals, banks, brokers, insurance companies etc., this information is valuable in order to detect companies or industries in distress early on.

Although some may consider that such sources of information on the financial difficulties of businesses may either be harmful or endanger the company’s potential rescue, the U.S. bankruptcy system has proven that such publicly available information actually enhances the chances of successful reorganisation and is critical in the early identification of companies in distress.

2.3. Specific Weaknesses:

The comparative analysis reveals the following weaknesses with respect to the national tools used as means of detection and/or prevention of difficulties.

The main weakness is considered to be a lack of efficient use of existing mechanisms to identify financial difficulties in companies, mainly due to the fact that some procedures are optional rather than mandatory, and to the lack of penalties. The analysis shows that few legislative prevention mechanisms appear to be implemented in a majority of countries.

In Austria although the continuation-forecast procedure might be quite helpful as a prevention tool, the fact that the debtor may only initiate it is a particular weakness, and practically results in its inefficiency. It is nevertheless worth observing that granting the debtor the initiative of the prevention procedure provides an adequate shield against the harmful effects of a public procedure.

In Germany, some mechanisms are in place to detect financial difficulties, both internal and external. However, medium sized companies rarely use these control mechanisms. As a result, third parties discover crises much more frequently.

Similarly, in Luxembourg, the lack of transparency, partly due to the lack of penalties if the accounts are not timely deposited – or even not deposited at all – increases the risk not to be able to rescue businesses facing difficulties.
In Italy, the lack of efficiency of the specific internal tool of the board of statutory auditors is due to the latter’s lack of independence. By contrast, the timely intervention of supervisory entities – external to the business – have led to successful rescue operations.

4.1.4. CONCLUSION

There seems to be little legislative and judicial procedures in both the EU and the U.S. to detect and warn businesses in distress. Although warning lights in the form of the accounting obligations and publication of financial statements, judgements, tax debts, etc. do exist, companies are generally not systematically and effectively screened by independent governmental bodies or other regulatory commissions.

However, it must be pointed out that several domestic legislations are undergoing changes to reform the bankruptcy and insolvency laws. Such legislation includes the 1997 amended law on Judicial Composition in Belgium, the 1997 Insolvency Law Reform Act in Austria, the Irish legislation amended in 1999 and 2001, the Italian 1998 Legislative Decree, the Portuguese Decree-Law of 1998, creating the mediation procedure. Furthermore, several legislative projects are planned in Greece, in Luxembourg, and in the Netherlands with the Dutch committee on Modernisation of Bankruptcy Law. These changes in national legislations reflect the general national concern for the matter. However, it appears that these legislations do not focus on the implementation of specific screening and warning procedures. The recent Irish Company Law Enforcement Act, 2001 creating the Office of the Director of Corporate Enforcement, which is an independent state-funded agency, may provide an example of legislation in favour of the development of screening procedures. The harmonisation of a detection process would ensure the efficiency of existing tools for warning businesses facing difficulties and would increase the chances of success of potential rescue operations.

It seems that due to the lack of such detection procedures and early warning of distressed businesses, opportunities for timely rescue operations of failing businesses are substantially diminished in most European Union countries.

It should be noted, however, that while the U.S. does not have any governmental or judicial bodies that monitor and regulate the financial health of companies with the specific intention of identifying companies in distress, there still exists a lot of distressed companies that are successfully reorganised. This is mainly due to strict disclosure requirements and the extensive monitoring of and reporting on companies to the public by independent third parties. It should also be noted that there seems to be a much more tolerant view of business failure in the U.S. society than in Europe, so adoption of the U.S. system in Europe might not have the same outcome as in the U.S.

The mechanisms used to detect and prevent business financial difficulties should perhaps strike a balance between public transparency of information that might enable a business in distress to be identified early on and subsequently rehabilitated, and confidentiality and discretion of information that might protect a business from the unnecessary harm and stigma that often arises with the publicity of failure.

4.1. Detection of businesses in difficulties and warning lights 180
4.2. LEGAL POSSIBILITIES TO CONTINUE ECONOMIC ACTIVITIES

4.2.1. INTRODUCTION

This title explores the various legal possibilities in the EU Member States and the United States that allow a business (individual or a legal entity) encountering economic or financial difficulties to continue operating and attempt a recovery instead of liquidating its assets.

Section 4.2.2. provides a descriptive summary of the legal possibilities available in each country for a distressed business to avoid bankruptcy. Our analysis is based on the national reports that are annexed and attempts to outline the most important aspects of each of the national systems.

Section 4.2.3. aims to compare the national systems, identifying and underlying their similarities and dissimilarities. Finally we try to assess and criticise these systems, focusing on the relevant aspects regarding the stigma on failure.

4.2.2. OVERVIEW OF THE NATIONAL PROCEDURES

It appears that in every EU Member State, as well as in the U.S., there exist legal procedures that allow for the reorganisation or rehabilitation of businesses encountering difficulties.

In most of the countries, with the exception of the U.S., only the debtor is entitled to initiate the procedure. This requirement is based on the principle that the co-operation of the debtor is an essential condition to the success of any recovery and the procedure should not be imposed on it.

Most of these legal procedures are based on the realisation of a rescue plan. This “plan” may consist of proposals and counter-proposals, or a “scheme of arrangement,” depending on the terminology used. However it is referred to, the function of a plan of reorganisation is to provide the creditors with a single document containing all information regarding the business and its plan for going forward. The goal of the plan is to provide creditors with the necessary information to decide whether or not they should choose to vote on and confirm the submitted plan.

The success of any recovery depends on the will of the creditors to give the debtor a chance to reorganise. Creditors have the choice to participate in voting on the plan and have the right to confirm or reject the proposed plan. Details regarding creditor participation and voting percentages vary from country to country. A plan must then usually be confirmed by the court once it is accepted by the legally required majority of creditors. Upon execution of the plan, remedies are usually provided to creditors if the debtor fails to comply with its obligations under the plan.

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1 The term “bankruptcy” in the above sentence actually implies a company trying to prevent liquidation or insolvency. However, for the purposes of the U.S. section, the distinction between “bankruptcy” and insolvency should be made. Bankruptcy in the U.S. does not necessarily imply insolvency (loosely defined as the sum of all debts being greater than the sum of all property). Bankruptcy for a company refers to Chapter 11 (Reorganisation) or Chapter 7 (Liquidation) of the Bankruptcy Code. A company in the U.S. can be “bankrupt” but not insolvent. In fact, Chapter 11 “bankruptcy” in the U.S. can also be a method of preventing insolvency. In most of this report, however, bankruptcy is referring to insolvency of a company.
The majority of EU Member States’ legislation regarding reorganisation or restructuring of businesses involves a high degree of information towards creditors and provides important publicity as to the initiation, progress and ending of the procedures. Practitioners consider such information necessary to protect creditors and to prevent association of a stigma with the debtor, which is often created by the publicity surrounding such a procedure (i.e., publication in the official gazette, in newspapers, in registers, and any other means of communication). In the eyes of European practitioners, potential creditors, investors, clients and partners may be deterred from doing business with an enterprise that has been publicly recognised as being distressed. This often results in the irreversible failure of the business.

On the contrary, the high degree of confidentiality characteristic to unofficial (out-of-court) recovery proceedings often allows for the maximum chances of recovery of a business. Moreover, out-of-court proceedings are usually less costly, assuming creditors can reach agreements in a timely manner. This is generally the case in most EU Member States and the U.S., the exception being France, as reorganisations in France are conducted under the supervision of the courts but still guarantee confidentiality.

Creditors and other partners or other entities related to a company in the United States are generally not as reluctant as their European counterparts to trust a business facing financial difficulties. Accordingly, publicity surrounding the reorganisation of a debtor is not considered as detrimental to the reputation of the distressed business as in Europe. Furthermore, publicity of a distressed debtor in the U.S. can even be beneficial. A Chapter 11 (referring to Chapter 11 of the U.S. Bankruptcy Code entitled “Reorganisation”) filing in the U.S. allows a business to obtain credit more readily than before filing. This allows the business to continue operating and signals to creditors that it is open for business and able to pay for goods and services. It encourages vendors to provide terms to the debtor. Thus, the availability of what is called “post petition financing” reduces the stigma associated with a distressed business.

Whilst it is possible to state that all EU Member States provide reorganisation procedures close to the “judicial composition”, obviously these procedures may vary from each other a great deal, not only with respect to their name but also to their conditions, effects, administration, and any other aspect.

A. AUSTRIA

The Austrian legislation provides court proceedings and out-of-court proceedings.

The court proceedings are called Ordinary Reorganization and Compulsory Reorganization, which are governed by the Settlement and Recomposition of Debts Act of 10th December 1914 (“Ausgleichsordnung”), and the Bankruptcy Act of 10th December 1914 (“Konkursordnung”).

A.1. Court proceedings

a) The Ordinary Reorganization (“Ausgleich”)
Definition

This reorganisation proceeding attempts to rescue the debtor through a partial discharge of its debt. It is based on an agreement between the debtor and its creditors, under which the debtor is obligated to pay a certain percentage of its debt within a specified time period, in exchange for a discharge of the residual debt.

Initiators

Only the debtor (whether an individual or a legal entity) may initiate the procedure.

Conditions

The procedure is available to debtors who are illiquid (including impending illiquidity) or over-indebted. This is similar to the conditions that apply to a bankruptcy procedure.

Although this procedure is based on a consensual agreement between the parties, minimum requirements are legally imposed:

- 40% of the unsecured debts shall be paid under an Ordinary Reorganization;
- The payment, of the above, is to be completed within a maximum period of two years.

Administration

Once the procedure has been initiated, the court appoints a reorganization administrator. The management retains control of the enterprise, while the administrator only has a supervisory function.

b) The Compulsory Reorganization (“Zwangsausgleich”)

Definition

Similar to the Ordinary Reorganization, it is based on an agreement between the debtor and its creditors, which attempts to rescue the debtor’s business through a partial discharge of debt.

Initiators

Only the debtor (whether an individual or a legal entity) may initiate the procedure.

Conditions

The procedure is available to debtors who are illiquid or over-indebted. The main difference between the Ordinary and Compulsory Reorganization procedures are that the latter may only be initiated in the course of a bankruptcy proceeding.

4.2 Legal possibilities to continue economic activities

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The following minimum requirements apply:

- 20% of the unsecured debts shall be paid under a Compulsory Reorganization;

- The payment, of the above, is to be completed within a maximum period of two years.

The Ordinary Reorganization is rather unsuccessful, mainly due to the high minimum legal requirements. Accordingly, most insolvent businesses prefer to initiate bankruptcy proceedings, which then allows them to apply for a Compulsory Reorganization.

♦ Administration

As this procedure must be initiated in the course of bankruptcy proceedings, the appointed bankruptcy administrator retains control of the business; however, there is no reorganization administrator.

A.2. Out-of-court proceedings

Out-of-court proceedings are also referred to “informal workouts”, “out-of-court reorganization” or “silent reorganization”. Since these proceedings are conducted out of court, there are no minimum requirements and is based on the agreement between the debtor and its creditors.

Out-of-court proceedings prove to have a growing success rate as it avoids any detrimental publicity effect that is attached to court reorganizations. However, such proceedings require the consent of all creditors, which is not always easy to attain.

B. BELGIUM

Belgian law provides a specific legal procedure, that being the Judicial Composition, to assist enterprises to continue activities. The Judicial Composition Act of 17th July 1997 (“Loi du 17 juillet 1997 relative au Concordat judiciaire”) regulates the procedure. Two procedures that may also help enterprises that face difficulties are the Provisional administrator and the Independent preliminary bankruptcy.

B.1. Judicial Composition (“Le concordat judiciaire”)

♦ Definition

This procedure attempts to recover a debtor in distress, through the court granting a moratorium on payments to creditors, during which time a recovery plan must be formulated and submitted to the creditors, including ultimately the court.

♦ Initiators

Either the debtor (whether an individual or a legal entity) or the Public Prosecutor may initiate the procedure, however usually the debtor initiates the procedure.
4.2 Legal possibilities to continue economic activities

Conditions

This procedure can be initiated if the debtor is temporarily unable to pay its debts or faces temporary financial difficulties.

Judicial Composition is granted on condition that there is a reasonable chance of achieving recovery.

Administration

Once the procedure has been initiated, the court appoints one or more administrator. The debtor retains control of its business under supervision of the administrator. Certain operations can require the authorization of the administrator(s).

B.2. Provisional administrator (“Administrateur provisoire”)

Although this legal procedure is not intended to be a recovery procedure, it allows any interested party to request the appointment of a temporary administrator, to replace the current management, when it is feared that the business is potentially bankrupt.

This legal procedure attempts to prevent the management from acting in such a way that would be prejudicial to creditors in case of a subsequent bankruptcy.

B.3. Independent Preliminary Bankruptcy (“Mandat ad hoc”)

Although this mechanism is not legally regulated, it has already been used by courts. It is based on the appointment, by the court, of an independent “receiver” with a very limited and specific assignment.

The management retains control of the business, but with the efficient assistance of the independent “receiver”.

C. DENMARK

Danish law provides court proceedings and out-of-court proceeding.

Court proceedings, called the Suspension of Payments and the Compulsory Composition are regulated by the Bankruptcy Act 1975. Out of court proceedings are referred to as Unannounced Suspension of Payments.

C.1. Court proceedings

a) Suspension of Payments

Definition

Suspension of Payments is a procedure offered to a debtor having difficulty in meeting its obligations. It aims at examining whether there is any possibility of
continuing operations and to establish an arrangement with the creditors, possibly in connection with a reorganisation of the business.

♦ Initiators

Only the debtor may initiate the procedure.

♦ Conditions

The debtor must be or must foresee that he is unable to fulfil his obligations.

♦ Administration

Once the procedure has been initiated, the court appoints an administrator. The debtor retains control of its business; however, he acts under supervision of the administrator whose consent is required in all important transactions.

b) Compulsory Composition

♦ Definition

Compulsory Composition is a procedure whereby an agreement is reached between the debtor and the creditors under which a specified proportion of the creditors decides between either:
- a percentage reduction of the non-preferential debt and a distribution of the debtor's property or part thereof, in exchange for the release of the debtor from part of the debt not settled, or
- an extension of payment.

♦ Initiators

Only the debtor may initiate this procedure, however the procedure is often caused by pressure from the creditors.

♦ Conditions

No particular conditions are required.

♦ Administration

The debtor retains control of its business. However, in some cases, the court may subordinate the granting of the measure to the appointment of an administrator, who will have the same function as in a Suspension of Payments procedure.

C.2. Out-of-court proceeding

The Unannounced Suspension of Payment is an informal procedure, based on a private agreement between the debtor and its major creditors. It includes an arrangement to allow the continuation of the business.
D. FINLAND


D.1. Restructuring of Enterprises ("Yrityssaneeraus")

♦ Definition

Restructuring of Enterprises can be utilised by debtors (with debt) experiencing financial difficulties with an aim to preserve its operational requirements and restructure its debts and to prevent bankruptcy.

♦ Initiators

Either the debtor (whether an individual or a legal entity), a creditor or a potential creditor may initiate the procedure.

♦ Conditions

The procedure is applicable to viable enterprises that is experiencing financial difficulties.

♦ Administration

After initiation of the procedure, the court appoints one or several administrators. The role of the administrator is to formulate a plan and to supervise the activities of the enterprise, however, the debtor retains control of the business.

D.2. Out-of-court proceeding

It is based on a voluntary arrangement between the debtor and its creditors. In order to achieve success through this type of restructuring, it is necessary to obtain at least the consent of the major creditors; the agreement cannot however be opposed to the creditors who did not consent to the arrangement.

This procedure has the advantage of being less costly and to avoid the detrimental publicity of an official procedure.

E. FRANCE

French law provides for two procedures, namely the Independent Preliminary Bankruptcy ("Le mandat ad hoc") and the Amicable Settlement Procedure ("La procédure de règlement amiable"). These procedures are legally defined by the law of 1st March 1984 ("Loi du 1er mars 1984 relative à la procédure du règlement amiable") (articles L.611-3 and L.612-1 of the French Commercial Code) and require the intervention of a judge.
E.1. The Independent Preliminary Bankruptcy (“Le mandat ad hoc”)

♦ Definition

This procedure applies to debtors in financial difficulty, through the appointment of an objective third party, whose function is to assist the debtor and its creditors to reach an agreement in order for the debtor to continue its activities. The advantage of the procedure is its flexibility and confidentiality, since, even though the law does not address confidentiality, in practice the procedure is not public knowledge.

♦ Initiators

Only the debtor (whether an individual or legal entity) may initiate the procedure.

♦ Conditions

Debtor in financial difficulty, but not yet in default of payments (otherwise they must file for bankruptcy), may benefit from the procedure.

♦ Administration

Once the procedure has been initiated, the court appoints an independent receiver. The objective of the independent receiver is of a supervisory role, but also includes a wide range of activities, for example assisting management, negotiating payment terms with banks and business partners. However, the debtor still retains control of its business.

E.2. The Amicable Settlement Procedure (“La procédure de règlement amiable”)

♦ Definition

Similar to the Independent Preliminary Bankruptcy procedure, this procedure is based on an agreement between the debtor and its creditors, concluded under the auspices of a conciliator and under supervision of the court. This procedure is strictly confidential, the breach of the duty of confidentiality being criminally punishable.

♦ Initiators

Only the debtor (whether an individual or a legal entity) may initiate the procedure.

♦ Conditions

The procedure is offered to enterprises that experience legal, economic, or financial difficulties but that are not yet in default of payments.

♦ Administration
The conciliator does not have the right to participate in the management of the business; the debtor retains control of its business. The conciliator is appointed to prepare a reorganization plan that will be submitted to the creditors and the court.

**F. GERMANY**

German law provides for court proceedings, the Reorganization based insolvency plan that must be initiated in the course of insolvency proceedings, as well as out-of-court proceedings. The German legislation on insolvency has been modified significantly since the German Insolvency Act (“Insolvenzordnung”) came into force on 1st January 1999. It is aimed at eliminating the overlap between the Bankruptcy Act and the Composition Act.

**F.1. Reorganization based on insolvency plan (“Unternehmenssanierung”)**

♦ **Definition**

This procedure is based on the formulation of a reorganization plan in the course of insolvency proceedings (in a restrictive way, meaning compulsory liquidation proceedings), aimed at rescuing the business.

♦ **Initiators**

This procedure can be initiated either by the debtor (only legal entities) or the insolvency trustee. The creditors’ assembly (not a single creditor) may instruct the insolvency trustee to compile a reorganization plan.

♦ **Conditions**

The procedure can be utilised by debtors that are unable to pay their debts as they fall due and/or where it can be established that the value of the assets is less than the liabilities (over-indebtedness) and may only be initiated in the course of insolvency proceedings.

♦ **Administration**

An insolvency trustee manages the enterprise; the court may however order self-management, on request of the debtor or its creditors (but in the later case, the debtor has to agree).

**F.2. Out-of-court proceeding**

This procedure is based on an agreement between the debtor and its creditors. Either the debtor or the creditors may start the negotiations; in practice, creditors are very often the initiators. The procedure has the advantage to be less costly and more confidential than court proceedings.

**G. GREECE**
Greek law provides reorganisation procedures regulated by the Law 3562/1956 on the placing of companies limited by shares under the administration and management of creditors and the placing under special winding-up, and the Law 1892/1990 on modernization and development and other provisions (articles 44, 45, 46, 46a, 46b).

**G.1. Restructuring as per article 44 and winding-up or special liquidation as per article 46 a of Law 1892/1990, of companies in financial crisis**

a) **Restructuring**

- **Definition**

Restructuring is based on an agreement between the debtor and its creditors, with the objective to restructure the business and a plan of debt settlement or reduction of its debt.

- **Initiators**

Either the debtor (whether an individual or a legal entity) or the majority of its creditors (as legally defined) may initiate the procedure.

- **Conditions**

This procedure is available to debtors:

- That have suspended or discontinued their operations for financial reasons;
- That have ceased making payments;
- That are bankrupt, or under the administration of the creditors or under provisional order, or liquidation;
- The total of their debt is 5 times more than the sum of their share capital and the reserves, and are unable to pay their debts.

- **Administration**

After initiating the procedure, an administrator is appointed by the court. However, the debtor retains control of its business. If the debtor fails to comply with the agreement concluded with the creditors, the administrator will manages the business.

b) **Winding-up**

In case the restructuring fails, the trustee has the possibility to sell the company’s assets under the usual procedure of compulsory auction. Another way of proceeding is to sell the business as a whole, under the procedure of public tender.

We do not consider such a procedure as a possibility to continue business.

**G.2. Placing of companies limited by shares, general partnerships and limited partnerships under administration of its creditors or under special liquidation**
This procedure is not used anymore, since it was historically justified by the post-war efforts to rescue the Greek economy and will not be further discussed.

H. IRELAND

Irish law provides for two legal possibilities to continue economic activities for companies in distress: the Examinership, introduced by the 1990 Companies Amendment Act, and the Scheme of Arrangement, which is regulated by the 1963 Companies Act.

H.1. Examinership

♦ Definition

This is a procedure whereby the court appoints an independent third-party, to assess the operations, activities and assets of the debtor’s business, consider whether rescue is possible or not, and if so, propose a scheme that must be adopted by certain classes of creditors, under supervision of the court. Some aspects of this procedure is based on the U.S. Bankruptcy Code Chapter 11, further discussed in Section P.

♦ Initiators

Either the debtor (only legal entities), a creditor, or a potential creditor may initiate the procedure. However, in the vast majority of cases, the debtor initiates it.

♦ Conditions

This procedure can be utilised by a debtor, with a reasonable prospect of recovery, that is or will become unable to pay its debt, but who is not yet under a resolution to wind up.

♦ Administration

Once the procedure has been initiated, the court appoints an examiner. The examiner is responsible for the conduct of the administration of the procedure; however, the debtor retains control of the business.

H.2. Scheme of Arrangement

♦ Definition

A Scheme of Arrangement is a compromise or arrangement, which a debtor negotiates with its creditors or members, regarding the payment of its debt (reduction and delays).

♦ Initiators

The debtor (only legal entities), the creditors, the shareholders of the company or the liquidator, if the company is being wound-up, may initiate the procedure.
The Scheme of Arrangement is rarely used, since the Examinership is effectively a sophisticated version of it.

- **Conditions**

This procedure is available to companies, even if the company is going through a winding-up procedure, on condition of the approval of a qualified majority of creditors and of the High Court.

- **Administration**

Unlike the Examinership procedure, no external administrator is appointed. The debtor retains control on its business.

**I. ITALY**

Italian law provides two procedures: the Controlled Administration procedure, and the Preventive Creditors Settlement procedure, both regulated by the Royal Decree of 16th March 1942 on Discipline of the bankruptcy, of the preventive creditors settlement procedure, of the controlled administration procedure and of the compulsory administrative liquidation procedure (“Disciplina del fallimento, del concordato preventivo, dell’administrazione controllata e della liquidazione coatta amministrativa”).

**I.1. The Controlled Administration procedure (“administrazione controllata”)**

- **Definition**

This procedure allows the debtor in temporary financial distress a way to continue its operations through placing the management of the business and administration of the assets under the supervision of the court, in order to find a solution to its financial woes and pay all debt.

- **Initiators**

Only the debtor (only legal entities) may initiate the procedure.

- **Conditions**

The major conditions to initiate this procedure are:

- in the prior five years, the debtor shall not have been declared bankrupt or benefited from a judicial creditors composition procedure;

- it has not been found guilty of a bankruptcy offence or other specified crimes;

- it is possible to rescue the debtor;

- the debtor has difficulties in meeting its obligations.
The success of the procedure depends on the ability of the debtor to finally pay all of its debt.

♦ **Administration**

Once the procedure has been initiated, the court appoints an administrator. His function is to evaluate the plan proposed by the debtor and to supervise the procedure. The debtor retains control of its business.

**I.2. The Preventive Creditors' Settlement procedure ("concordato preventivo")**

♦ **Definition**

This procedure is available to a debtor that is insolvent and that wants to avoid to be adjudicated into bankruptcy.

♦ **Initiators**

Only the debtor (only legal entities) may initiate the procedure.

♦ **Conditions**

The conditions in order to benefit from the procedure are the following:

- in the prior five years, the debtor shall not have been declared bankrupt or benefited from a judicial creditors composition procedure;
- he has not been found guilty of a bankruptcy offence or other specified crimes
- the debtor will offer guarantees or securities of his capacity to pay:
  - the secured creditors in its entirety;
  - 40% of the value of the unsecured creditors;
- the debtor will offer to sell his assets.

♦ **Administration**

Once the procedure has been initiated, the court appoints one or more administrators. The debtor retains control of its business, under supervision of the administrators.

**J. LUXEMBOURG**

Luxembourg law provides for two principal procedures, namely the Reprieve of Payment, regulated by the Grand Ducal Decree of 4th October 1934, and the Controlled Management, regulated by the Grand Ducal Decree of 24th May 1935. The Law of 5th April 1993 and of 30th March 1988 has enacted a procedure specific to banks and financial institutions.
Another Luxembourg procedure is the “Composition in order to avoid bankruptcy”, regulated by the Law of 14th April 1886 relating to compositions in order to avoid bankruptcy (Loi du 14 avril 1886 relative aux concordats préventifs de faillite). However, this procedure has fallen into disuse.

J.1. The Reprieve from Payment (Le “sursis de payement”)

♦ **Definition**

This procedure allows a debtor to suspend payment to creditors for a limited period of time, based on an agreement between the debtor and its creditors that is confirmed by the court.

♦ **Initiators**

Only the debtor may initiate the procedure.

♦ **Conditions**

The conditions to initiate the procedure are the following:

- The debtor is forced by extraordinary and unforeseeable events to cease his payments temporarily and has sufficient assets and funds according to its duly verified balance sheet in order to satisfy all creditors, in principal and interests;

- The financial situation of the debtor, although currently in deficit, shows strong potential that could allow a restoration of the financial situation.

♦ **Administration**

Once the procedure has been initiated, the court appoints one or more administrators. The debtor loses the right to solely manage the assets of the company. The administrators must approve all operations.

J.2. The Controlled Management

♦ **Definition**

This procedure is a remedy, granted by the court, to protect a debtor, in order to allow it to reorganize its business or to convert its assets into cash.

♦ **Initiators**

Only the debtor may initiate the procedure.

♦ **Conditions**
The debtor has **lost its creditworthiness** or **has difficulties in satisfying all its commitments**. The procedure is **not** available to debtors that have already been declared **bankrupt** by a final decision.

**Administration**

Once the procedure has been initiated, the court appoints one or more **administrators**. The **debtor loses** the right to **solely manage** the assets of the company. The **administrators must approve** all operations.

**J.3. Composition in order to avoid bankruptcy** (Le “Concordat préventif de faillite”)

This procedure is based on an **agreement** between the **debtor** and its **creditors**. The agreement may rearrange debt payments or plan a reduction of debts, however the procedure is no longer used and therefore not further discussed.

**K. THE NETHERLANDS**

Dutch law provides a number of possibilities for debtors that face financial distress. This include activities where the debtor may continue on the basis of a **Scheme of Arrangement**, to give the enterprise some time to put its financial affairs in order and to grant it a **Suspension of Payments**. The reorganization procedures are regulated by the **Bankruptcy act of 1st September 1896**.

**K.1. Suspension of Payment** (“Surseance van betaling”)

**Definition**

The suspension of payment is a **temporary relief** granted by the court to the debtor towards its unsecured creditors, in order to **attempt the continuation** of the business and, ultimately, the **satisfaction of all or part of the creditors**. Secured creditors are not affected by the suspension of payments, which may frustrate the success of the procedure.

The debtor may use this delay in various way; it may either use the suspension of payments to reorganize its activities, creditors being kept at distance, or to propose to its creditors a judicial scheme of arrangement, or to sell part or all of its assets.

**Initiators**

Only the **debtor** (whether an individual or a legal entity) may **initiate** the procedure, except in the case of a financial institution, the **Dutch Central Bank** may initiate the procedure without being a creditor.

**Conditions**

This procedure is available to an enterprise that expects to be **unable to continue payment** of its **due and payable** debt and as long as the court grants it.
4.2 Legal possibilities to continue economic activities

♦ Administration

Once the procedure has been initiated, the court appoints one or more administrators. During the suspension, the debtor and the administrator(s) jointly manage and dispose of the debtor’s estate.

K.2. Out-of-court scheme of arrangement (“Akkoord”)

An out-of-court scheme of arrangement is a procedure that offers the debtor in distress an option to pay its creditors a certain percentage of the outstanding debt and the debtor being discharged of the remaining debt. The procedure is dependant on the agreement of all the creditors. This could be frustrating to the debtor and under special circumstances a judge may impose an unwilling creditors to cooperate in an out-of-court settlement (for example on the basis of abuse of power or unreasonableness).

Usually, secured creditors participate in the scheme of arrangement to the extent that they have claims that are not secured.

L. PORTUGAL

Portuguese law provides for various possibilities for the recovery of debtors that face financial difficulties. They are regulated by the Code of Special Procedures for Company Recovery and Bankruptcy (Código dos Processos Especiais de Recuperação da Empresa e de Falência”), introduced by the Decree-Law nº132/93 of 23rd April 1993.

♦ Definition


♦ Initiators

The debtor (only legal entities), a creditor, or the Public Prosecutor may request the adoption of an appropriate recovery measure.

♦ Conditions

A debtor in a difficult economic situation or that is insolvent, but that is considered to be economically viable and could be financially recovered, may apply for one of the following recovery measures:

L.1. Composition

The procedure allows for a reduction or modification of all or part of the debt of the business. Depending on the terms of the approved agreement, the debtor may retain control of its business.

L.2. Entrepreneurial reconstitution
The procedure allows for the **creation of one or more new companies** for exploiting new establishments of the debtor company, provided the creditors are ready to undertake or boost the respective activities.

In this procedure, the **directors of the new company** exercise control on the debtor’s establishment.

**L.3. Financial restructuring**

The procedure provides for creditors a mean to adopt plans to restructure the **company’s liabilities** or to **change its share capital structure**, which places the company into a solvent position and generate a positive working capital.

Similar to the composition procedure, the **debtor** may retain **control** over its business.

**L.4. Controlled management**

The procedure applies a **global action plan**, orchestrated between creditors, and executed through **a new board of directors**, which provides proper supervision. The **new board of directors controls** the business.

**M. SPAIN**

Spanish legislation provides one legal possibility to continue business: the **Suspension of Payments** (“Suspensión de pagos”), regulated by the **Suspension of Payments Act of 1922**.

- **Definition**

  The procedure grants a **compulsory moratorium** on all the debtor’s debt with the objective of reaching a **judicially controlled arrangement** or **composition** between the **debtor** and its **creditors** in order to **restore its finances**. This is accomplished by negotiating **changes to the terms and conditions** governing the debt. The agreement may include a postponement in debt payment, a reduction of debts, or both. The majority of creditors must consent to the composition.

- **Initiators**

  Only the **debtor** (whether an individual or a legal entity) may **initiate** the procedure.

- **Conditions**

  To benefit from the procedure, the debtor must be **in temporary financial distress**.

- **Administration**

  Once the procedure has been initiated, the court appoints one or more **administrators**. The **debtor** retains **control** of its business, on **condition of approval**.
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

by the administrator. A decision taken without the authorization of the administrators is criminally punishable.

N. SWEDEN

Swedish law provides two legal possibilities to continue business: the Reorganization procedure and the Judicial Composition, both regulated by the Company Reorganization Act of 1996.

N.1. Reorganisation ("Företagsrekonstruktion")

♦ Definition

Reorganisation aims at reorganizing the business of a debtor in financial distress by making various reforms and/or initiating a financial settlement with its creditors.

♦ Initiators

Either the debtor (whether an individual or a legal entity) or a creditor, with the consent of the debtor, initiates the procedure.

♦ Conditions

This procedure is available to debtors that are or will become unable to pay their debts. It must be established that there is reasonable chance that a successful reorganization can be achieved.

♦ Administration

Once the procedure has been initiated, the court appoints an administrator, who will propose a reorganization plan. This must be submitted to the creditors and the court. The debtor retains control over its business; however, the debtor cannot sell or otherwise dispose of property that is of importance to the operation of business without the authorization of the administrator.

N.2. Judicial composition ("Ackord")

♦ Definition

The procedure is based on a financial arrangement, concluded in the course of reorganization proceedings, between an insolvent debtor and its unsecured creditors, aiming at relieving the debtor of part of its debts.

♦ Initiators

Only the debtor (whether an individual or a legal entity) may initiate the procedure, even though the administrator (appointed in the Reorganization) usually drafts the documents.
Conditions

The criteria is similar to those applicable to reorganization, however, there is no need to prove bankruptcy. Judicial Composition can only be initiated in the course of a reorganization procedure.

Administration

Since the Judicial Composition can only be initiated in the course of a Reorganization procedure, an administrator is already appointed. The debtor retains control over its business; although, the debtor cannot sell or otherwise dispose over property that is of importance to the operation of business without the authorization of the administrator.

O. UNITED KINGDOM

UK law provides three procedures available to companies facing difficulties: the Receivership, the Administration, and the Company Voluntary Arrangement, all regulated by the Insolvency Act 1986 and the Companies Act 1985 and 1989.

O.1. Receivership

Definition

Receivership is a procedure available to companies (only legal entities), whereby a receiver is appointed with a charge to recover a debenture holder’s claim or a creditor’s funding (usually a bank).

Initiators

A debenture holder (if the debenture so provides) or the court may initiate the procedure, by appointing a receiver.

Conditions

No specific conditions apply.

Administration

The debenture holder or the court appoints an administrative receiver who effectively replaces the management of the debtor (the company). He is authorised and empowered by the debenture holder and also attain specific powers listed in the Insolvency Act 1986.

O.2. Administration

Definition
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

Administration is a court-approved scheme whereby the business obtains protection from the creditors’ claims during a period where creditors approve a scheme for the sale or restructuring of the business. It is similar to the U.S. Bankruptcy Code Chapter 11 procedure.

✶ Initiators

Either the debtor (only legal entities) or one or more creditors may initiate the procedure.

✶ Conditions

The procedure is offered to a company that is unable to pay its debt or is likely to become unable to pay its debt.

The petitioner must satisfy the court that issuing an administration order would be likely to achieve one or more of the following objectives:

- the survival of the company, and the whole or any part of its undertaking as a going concern;
- the approval of a voluntary arrangement or composition in satisfaction of the company’s debts, or a compromise or arrangement between the company and some or all of its members;
- a more advantageous realization of the company’s assets than it could be effected in a winding-up.

✶ Administration

Once the procedure has been initiated, the court appoints an administrator. The administrator retains control over the business.

O.3. Company Voluntary Arrangement

✶ Definition

The company voluntary arrangement is a contractual agreement between the company and its creditors, under which the company reaches a compromise with creditors over its outstanding debts.

✶ Initiators

The debtor (only legal entities), or if the company is under administration, the administrator, or if the company is being wound-up, the liquidator, may initiate the procedure.

✶ Conditions

No specific conditions apply.
Once the procedure has been initiated, the creditors appoint “nominees”. The debtor retains control over its business, under supervision of the nominees.

P. UNITED STATES OF AMERICA

The law governing bankruptcy in the United States is called the Bankruptcy Code. The Bankruptcy Code is administered by Federal judges presiding over specialised tribunals called “Bankruptcy Courts” that are located throughout the United States and that, for the most part, have national jurisdiction. The Bankruptcy Code is structured in several chapters, including Chapter 11 (entitled “Reorganization”) and Chapter 7 (entitled “Liquidation”). Whether a debtor is in liquidation or restructuring proceedings, it is considered to be legally in “bankruptcy.” A business has the option to liquidate or reorganize itself both in-court by filing Chapter 7 or Chapter 11, or out-of-court through receivership, assignment or “workout.”

P.1. Chapter 11

Chapter 11 is the cornerstone of sophisticated bankruptcy practice in the United States and sets forth a structure for the rehabilitation of a corporate or (rarely) an individual debtor. The commencement of a Chapter 11 proceeding is not necessarily perceived in a negative way. Even though it is never easy to start such a procedure, it does not imply that the debtor has failed. The stigma of such a reorganisation is weaker than in European Member States and the commencement of a Chapter 11 case even has the effect of making the financing of a distressed debtor’s operations easier than if it had never filed.

Definition

Chapter 11 of the Bankruptcy Code (entitled “Reorganization”) provides a financially troubled business with an opportunity to restructure its finances to enable the continuation of its operations. To promote this goal, chapter 11 enables a debtor to remain in control of its assets and business (as a “debtor in possession”) while negotiating a restructuring of its affairs.

Initiators

Either the debtor (whether an individual or a legal entity) or the creditors that meet certain criteria may initiate a Chapter 11 proceeding. Initiation by the debtor is called a “voluntary” proceeding, while initiation by the creditor is called an “involuntary” proceeding. Control of the Chapter 11 process is critically important to the debtor, permitting the debtor to choose the exact date it wishes to file and the venue it wishes to file in, to stockpile cash, to negotiate post-petition financing or the use of cash collateral, to control the dissemination of information to the public, and to adequately alert and prepare its employees, vendors and suppliers of the bankruptcy filing. On the contrary, the commencement of involuntary proceedings signals to third parties that the company’s financial stability is in jeopardy and threatens the control debtor’s
management has over its company. This forces the debtor to co-operate and negotiate with its creditors and may be used by creditors precisely for this purpose.

♦ Conditions

There is no requirement for a debtor to initiate the voluntary proceeding.

An involuntary proceeding can be commenced only on the condition that the petitioning creditors show that the debtor is generally not paying its debts as they become due.

It should be noted that the filing of an involuntary petition with the bankruptcy court by petitioning creditors does not automatically lead to the debtor’s entry into Chapter 11. The debtor has 20 days to answer or contest the involuntary petition or file its own voluntary petition. The period of time between the filing of the involuntary petition and the entry for an order for relief is known as the “gap period” during which the debtor continues its normal business operations. The debtor may continue to operate its business and can use, acquire or dispose of property as if the involuntary case had not been commenced until the bankruptcy court requires otherwise. In the event that the debtor fails to timely contest the involuntary petition, the bankruptcy court may officially commence the chapter 11 case. If the debtor does contest the involuntary petition during the gap period, then the bankruptcy court will conduct a trial to determine the validity of the involuntary petition.

♦ Administration

The commencement of a chapter 11 reorganisation case does not usually result in the appointment of a chapter 11 trustee. Rather, the chapter 11 debtor remains in possession of its assets and becomes known as a debtor in possession. A chapter 11 debtor in possession generally may exercise all powers granted to a chapter 11 trustee under the Bankruptcy Code.

On request of a party in interest or the United States Trustee, the court may order the appointment of a chapter 11 trustee for cause, including fraud, dishonesty, incompetence or gross mismanagement of the affairs of the debtor by current management. However, bankruptcy courts are usually very reluctant to install a trustee unless there is truly gross mismanagement or fraud. Furthermore, where the court has not appointed a trustee, on request of any party in interest or of the US trustee, the court may order the appointment of an examiner to conduct such investigation of the undertaking as appropriate.

Under the Bankruptcy Code, the trustee or the debtor in possession may sell or use property in the ordinary course of business without a court order. Use or sale of property out of the ordinary course of business requires the court’s permission.

The goal of the Chapter 11 reorganisation is the filing and confirmation by the court of a Chapter 11 Plan of Reorganization (“plan”). A plan is basically a detailed term

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2 The US Trustee is an official of the US Department of Justice, appointed for each federal judicial district or group of districts, to monitor the progress of local bankruptcy cases and to represent the interest of the US Government in the expeditious and efficient prosecution of such bankruptcy cases. His function may be compared to the role of the Public Prosecutor in certain EU Member States.

4.2 Legal possibilities to continue economic activities
sheet that sets forth the treatment to be accorded to parties in interest under the plan and the means for effectuating that treatment.

Unless a trustee has been appointed, the undertaking has the exclusive right to propose a Plan of Reorganization for 120 days after the commencement of the proceeding, called the “*exclusivity period*.” After the exclusivity period, any creditor or equity security holder may propose a competing plan. Many judges view this as chaotic and expensive and often extend the exclusivity period of the debtor’s right to propose the plan. However, if the debtor proposes a plan within this period, no other plan can be proposed.

**P.2. Out-of-court proceeding**

The *workout* is a consensual restructuring outside chapter 11 through which a debtor and its significant creditors attempt to reach an agreement to restructure and adjust the debtor’s debt obligations. This includes the adjustment of payment schedules, the maturity date of the debt, and the issuance of new and additional debt instruments.

Both debtors and creditors may initiate the workout in an attempt to avoid bankruptcy under chapter 11.

The debtor’s creditors who participate in the workout should at least include significant creditors to be successful.

If an agreement is reached (a *composition* or *workout*), it is only binding on the consenting creditors. Usually, a composition agreement provides that the agreement will be effective on the condition that it is accepted by a certain percentage of creditors whose acceptance is solicited.

The mere existence of an informal workout is generally not kept confidential. However, it is common and standard for parties to a workout to execute a confidentiality agreement with respect to the use and dissemination of financial and other non-public information provided by the company. In addition, the parties to a workout usually agree not to issue any publicity unless mutually agreed to.

**4.2.3. COMPARATIVE ANALYSIS**

This section considers and compares only the most relevant procedures in each country aimed strictly at rescuing a business in distress to insolvency. Section 4.3 focuses on the legal consequences of bankruptcy, or insolvency, and the ability to have a “fresh start.” Our analysis was exclusively based on the national reports drafted by our EU and US correspondents annexed to the present report.

1) General description of the possibilities in the EU to continue economic activities

Due to the fact that each of the EU Members States and the U.S. have unique and varied in-court proceedings and out-of-court options for restructuring, comparing and contrasting these on an overall basis is a difficult task.
Overall, it can be said that all countries (EU Member States and the United States) offer one or several legal possibilities for a business in distress to stage a recovery. This is usually either by obtaining a temporary stay from or suspension of payments to creditors or by consensual agreements with creditors. This is usually done under supervision of an appointed administrator and/or court authority, with the degrees of authority of the court varying depending on the country.

However, we cannot conclude that the publicity and disclosure of information surrounding a debtor in distress necessarily engender stigma. A country’s sociological perception of failure plays a huge role in the development of a stigma surrounding a distressed debtor. Strong publicity and availability of information to the public may not create stigma in a society where business partners, consumers and investors do not attach any importance to the potential failure of an enterprise. This is generally the case in the U.S. where commencement of reorganisation procedures is not perceived negatively and can even have a positive effect on the outcome of the debtor. On the other hand, in the EU Member States, where society generally distrusts businesses facing financial difficulties, even limited publicity may be a strong factor in generating a stigma. It is difficult to determine which aspect – the protection of the debtor from negative publicity of the procedure versus the protection of the creditors and the right of interested parties to access information – plays the dominant role in business recovery.

2) Nature of the procedure

In all Member States of the EU, insolvency law is a part of private law, as opposed to public law or criminal law. In the U.S., insolvency law is governed nationally by the “Bankruptcy Code,” which is administered by Federal judges presiding over specialised tribunals called “Bankruptcy Courts.”

The vast majority of Member States and the United States provide for informal procedures conducted out of the court’s authority. These procedures are based on consensual agreements between debtors and creditors regarding the future of the business. In Europe, these agreements fall within the scope of private law, especially the law of contracts, and the common principle of the freedom of the parties. In the U.S., informal “workouts” do not fall under the Bankruptcy Code, but any agreements made are legally binding.

3) Legal conditions of reorganisation proceedings

a) Out-of-court proceedings

Out-of-court proceedings are not restrictive and refer to all contractually binding informal agreements, informal workouts and unofficial arrangements concluded between a debtor and its creditors. They are primarily based on the freedom of contracts, and may include any kind of arrangement, on condition that they comply with national law.

There is no specific or strictly defined criteria that regulates these procedures.
As the success of the “procedure” depends on the agreement between the debtor and its creditors, or of some creditors, to grant delays for payment, or reduction of debts, the only condition to fulfil is to obtain the consent of the creditors, or at least of most significant creditors.

Generally, a debtor can choose to arrange out-of-court proceedings, so long as the creditors consent. However, legislation in some countries obligates a debtor ceasing payments to petition for bankruptcy in court. In such cases, the possibility for a debtor to come to an informal arrangement with its creditors is limited to the debtor not yet being in default. For example, Belgian, French, German, and Luxembourg law oblige the debtor that ceases payments to its creditors to file for bankruptcy within a legally defined period.

Even though these procedures are by nature informal, and conducted out-of-court, it occurs in certain countries that the legislator intervenes in some way, or that the court has the power to ratify the agreement. In Finland, confirmation by the court of the informal arrangement gives to the parties a basis for executing their plan, or agreement. In the U.S., the interested parties generally use the Chapter 11 procedures and stipulations as a guideline for conducting an informal plan of reorganisation. In most countries, courts interfere in these agreements only in cases where disputes arise, as they would have intervened to ensure the respect of any other agreement, under contract law.

b) Court proceedings

Court proceedings and the details surrounding a company’s entry into bankruptcy vary among the various EU Member States and the U.S. However, we have identified the following four factors that are, for the most part, inherent to proceedings in the countries analysed:

1. Financial and economical difficulties

A business must be facing a difficult economic and financial situation, either through a cessation of payments to its creditors (as in Austria, Belgium, Germany, Luxembourg, Ireland, Netherlands, Portugal, Sweden, the United Kingdom), or through over-indebtedness (Austria, Finland, Germany). In Denmark and Italy, the debtor must be facing difficulties in meeting its obligations in order to file for reorganisation proceedings.

In a United States Chapter 11 case, one needs to distinguish between voluntary and involuntary proceedings. A business that files for Chapter 11 voluntarily does not have to meet any requirement in order to obtain court relief. However, the Court might dismiss a voluntary petition in case of bad faith of the debtor. On the other hand, creditors who initiate involuntary proceedings carry the burden of showing that the business is generally not paying its debts as they become due. The U.S. involuntary chapter 11 can therefore be compared to a procedure of its European counterparts that requires the cessation of payments to be established.

2. Viability of the enterprise
Only Belgium, Finland, Ireland, Italy, Luxembourg, Portugal and to a certain extent, the United Kingdom (Administration), formally require that an enterprise be viable or present a strong potential to recover from its distress. Spanish law, even though not strictly requiring the viability of the enterprise, states that the enterprise must face temporary financial difficulties to benefit for the regime. We may thus conclude from this condition that the situation of the enterprise cannot be irreversible and that a prospect of survival exists.

In the United States, there is no such specific requirement for the introduction of the chapter 11 proceeding except that the debtor must be in the “zone of insolvency.”

3. Conditions with respect to bankruptcy and/or winding-up

Several countries require that the debtor is not yet in default of payment or has not yet been declared bankrupt (insolvent) or put under a winding-up procedure in order to be put into reorganisation procedures. This is the case in Belgium, France, Germany, Ireland, Luxembourg and in the United Kingdom for at least one of the procedures available.

In Italy, both the Controlled administration procedure and the Preventive creditors’ settlement procedure are offered to corporate debtors having difficulties meeting their obligations. However, these companies may only apply on the condition that they have not been declared bankrupt or benefited from a judicial creditors composition procedure in the prior five years. In addition to the legal effects attached to the declaration of bankruptcy (see Title 5) that may prevent the debtor to start a new activity, there are severe conditions to benefit from the Controlled administration procedure and for the Preventive creditors’ settlement that may create stigma.

On the other hand, Austria, Denmark, Finland, Greece, Italy, Netherlands, Portugal, Sweden, Spain, the United Kingdom and the U.S. offer the possibility to benefit from the recovery procedures while the debtor is already in a situation of cessation of payment.

Belgium, France, Ireland (Examinership), Luxembourg (Controlled management) and the United Kingdom (Company voluntary arrangement) prohibit the introduction of a recovery procedure when a judicial decision declaring the undertaking bankrupt or wound-up has already been made.

Austria, Germany, Greece and Sweden provide procedures that can only be initiated in the course of insolvency proceedings, respectively the Compulsory reorganisation, the Reorganisation based on an insolvency plan, the Restructuring of enterprises and the Composition.

In the U.S. there is no legal stipulation regarding multiple Chapter 11 filings. In fact, if a debtor is unable to comply with the provisions of a plan of reorganisation which has become effective, the debtor may file a new chapter 11 petition in a renewed effort to reorganise its affairs. Some companies have gone through chapter 11 bankruptcy several times and multiple filings have become so common that they are sometimes referenced as “Chapter 22.”
Regarding the stigma on failure and the fresh start, it is noticeable that certain EU Member States provide the possibility to businesses that are already under a bankruptcy or liquidation proceeding to benefit from a reorganisation procedure in order to finally recover from such insolvent situation. In these procedures, the initiation of bankruptcy, winding-up, or liquidation proceedings does not necessarily engender failure, since a recovery procedure may be initiated in the course of these procedures. Bankruptcy proceedings may thus be converted into reorganisation proceedings.

Austria, Germany, Greece, and Sweden even provide procedures that may only be initiated in the course of insolvency proceedings (we mean bankruptcy or liquidation proceedings), as stated above. It may be a strategy of the debtor to first be declared bankrupt and then to apply for recovery procedures, if this way allows him to obtain more time to prepare a plan, or to benefit from less restrictive conditions.

4. Conditions with respect to creditors’ reimbursement

In addition to one or more criteria described above, certain countries impose conditions regarding the distribution of the debtor’s assets to creditors.

In Austria, for instance, the Reorganisation procedure requires the agreement that 40 percent of unsecured debts shall be paid, if it is an ordinary reorganisation, initiated out of any insolvency proceeding. This quota is reduced to 20 percent if the reorganisation is a compulsory one, initiated in the course of bankruptcy proceedings. As a consequence, many insolvent businesses opt rather for bankruptcy proceedings and try subsequently to convert it into a Compulsory reorganisation. These quotas may certainly deter the debtor from initiating the proceedings.

Moreover, in both cases, the payment of these quotas is due within a maximum time period of two years.

Similarly, in Italy, with respect to the Preventive creditors’ settlement procedure, the debtor shall offer guarantees that he will pay all secured debts and 40 % of the unsecured debts to benefit from the procedure.

In Luxembourg, the granting of a Reprieve of payments is conditional upon the existence of sufficient assets to satisfy all creditors.

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<th>CONDITIONS</th>
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<td><strong>Austria</strong></td>
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<tr>
<td><strong>Ordinary reorganisation</strong></td>
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<tr>
<td>- illiquidity, impending illiquidity or over indebtedness</td>
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<tr>
<td>- 40 % of the unsecured debts shall be paid within 2 years</td>
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<tr>
<td><strong>Compulsory reorganisation</strong></td>
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<tr>
<td>- illiquidity, impending illiquidity or over indebtedness</td>
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<tr>
<td>- 20 % of the unsecured debts shall be paid within 2 years</td>
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<td>- in the course of a bankruptcy proceeding</td>
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</table>
### 4.2 Legal possibilities to continue economic activities

<table>
<thead>
<tr>
<th>Country</th>
<th>Description</th>
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<tbody>
<tr>
<td><strong>Belgium</strong></td>
<td>• Agreement of creditors&lt;br&gt;• Temporary inability to pay debts&lt;br&gt;• Continuity of the business is threatened by problems that may lead to cessation of payments</td>
</tr>
<tr>
<td><strong>Denmark</strong></td>
<td><strong>Suspension of payments</strong>&lt;br&gt;• inability to fulfil its obligations&lt;br&gt;<strong>Compulsory composition</strong>&lt;br&gt;• no particular conditions&lt;br&gt;<strong>Out-of-court proceeding</strong>&lt;br&gt;• agreement of creditors</td>
</tr>
<tr>
<td><strong>Finland</strong></td>
<td><strong>Restructuring of enterprises</strong>&lt;br&gt;• Financial difficulties&lt;br&gt;• Indebtedness&lt;br&gt;• viability of the enterprise&lt;br&gt;<strong>Out-of-court proceedings</strong>&lt;br&gt;• Agreement of creditors</td>
</tr>
<tr>
<td><strong>France</strong></td>
<td><strong>Independent preliminary bankruptcy</strong>&lt;br&gt;• No default of payment&lt;br&gt;<strong>Amicable settlement procedure</strong>&lt;br&gt;• No default of payment</td>
</tr>
<tr>
<td><strong>Germany</strong></td>
<td><strong>Reorganisation based on insolvency plan</strong>&lt;br&gt;• No default of payment&lt;br&gt;<strong>Out-of-court proceedings</strong>&lt;br&gt;• In the course of a bankruptcy proceeding&lt;br&gt;• No default of payment</td>
</tr>
<tr>
<td><strong>Greece</strong></td>
<td>• Suspension or discontinuation of operations&lt;br&gt;• Cessation of payments&lt;br&gt;• Bankrupt business or business under administration of the creditors or under provisional order of liquidation&lt;br&gt;• Total of debts five times more than the sum of their share capital and the reserves&lt;br&gt;• Inability to pay debts</td>
</tr>
<tr>
<td><strong>Ireland</strong></td>
<td><strong>Examinership</strong>&lt;br&gt;• Inability to pay debts&lt;br&gt;• No resolution of winding up</td>
</tr>
</tbody>
</table>
4.2 Legal possibilities to continue economic activities

<table>
<thead>
<tr>
<th>Scheme of arrangement</th>
<th>Italy</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
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</tr>
<tr>
<td>· Reasonable prospect of survival</td>
<td></td>
</tr>
<tr>
<td>· Agreement of the creditors</td>
<td></td>
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</tbody>
</table>

<table>
<thead>
<tr>
<th>Controlled administration procedure</th>
<th></th>
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<tbody>
<tr>
<td>Preventive creditors' settlement procedure</td>
<td></td>
</tr>
<tr>
<td>Italy</td>
<td></td>
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<tr>
<td>· no bankruptcy or composition in the prior five years</td>
<td></td>
</tr>
<tr>
<td>· no bankruptcy offence or other specified crimes</td>
<td></td>
</tr>
<tr>
<td>· possibility to rescue the business</td>
<td></td>
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<tr>
<td>· difficulties to meet its obligations</td>
<td></td>
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<tr>
<td>· no bankruptcy or composition in the prior five years</td>
<td></td>
</tr>
<tr>
<td>· no bankruptcy offence or other specified crimes</td>
<td></td>
</tr>
<tr>
<td>· debtor shall offer guarantee to pay all secured debts and 40 % of unsecured debts</td>
<td></td>
</tr>
<tr>
<td>· debtor offers to sell its assets</td>
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</tbody>
</table>

<table>
<thead>
<tr>
<th>Reprieve from payment</th>
<th>Luxembourg</th>
</tr>
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<tbody>
<tr>
<td>Controlled management</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td>· Temporary cessation of payments because of extraordinary circumstances</td>
<td></td>
</tr>
<tr>
<td>· sufficient assets to satisfy all creditors</td>
<td></td>
</tr>
<tr>
<td>· strong potential of survival</td>
<td></td>
</tr>
<tr>
<td>· lost of creditworthiness</td>
<td></td>
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<tr>
<td>· difficulties to meet its obligations</td>
<td></td>
</tr>
<tr>
<td>· no bankruptcy decision</td>
<td></td>
</tr>
</tbody>
</table>

| Suspension of payments | The Netherlands |
| Out-of-court proceedings |                |
| · Anticipation of inability to pay due and payable debt |                |
| · Agreement of the creditors |                |

| Portugal |            |
|          |            |
| · Difficult economic situation or insolvency |            |
| · Economic viability and financial possibility to recover |            |

| Reorganisation | Sweden |
|               |        |
| Composition   |        |
|               |        |
| · Inability to pay debts as they fall due or anticipation of such inability |        |
| · Inability to pay debts as they fall due or anticipation of such inability |        |
| · Reasonable prospect of survival |        |

Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy
4.2 Legal possibilities to continue economic activities

4) Initiators of the procedure

a) Out-of-court proceedings

Out-of-court proceedings may be initiated by any party confronted with the financial and economical difficulties of the enterprise, since it is based on an agreement between all consenting parties and on the freedom of contract. The debtor as well as the creditor may initiate negotiations. However, usually the debtor starts the negotiation, since it wants to delay lawsuits and procedures of execution over the enterprise’s assets.

b) Court proceedings

Since recovery procedures aim at the survival of the business, the cooperation of the debtor is a necessary ingredient to their success. Several EU Member States make the debtor the only possible initiator of the procedure. This will be discussed further in section 1.

However, our analysis of the national reports seems to attribute the failure of the recovery procedure to the lack of action taken by the debtor. Entrepreneurs and company management are often reluctant to recognise their difficulties and consequently delay the initiation of the proceeding. Once the procedure is finally initiated, the recovery of their business is no longer possible. Based on this concept,
several EU Member States and the United States allow debtors, as well as creditors to initiate a bankruptcy proceeding. This will be discussed further in section 2.

Specificsally of the in- and out-of-court proceedings in the EU Member States and the United States will be discussed in section 3.

1. **Only the debtor** (i.e. the individual or, if it is a legal entity, its competent body)

In Austria, France, Greece (but only with regard to the Reforming procedure), Italy, Luxembourg, Netherlands, Spain, and Sweden (but only with regard to the Composition procedure) the debtor is the only possible initiator of the procedure. In Belgium, in addition to debtor initiation of the proceeding, the Public Prosecutor, to the exclusion of creditors, is also allowed to initiate recovery proceedings. However, in practice the Public Prosecutor never uses his power of initiation.

As stated above, this option is understandable as the success of the reorganisation of the enterprise depends mostly on the will of the debtor, and on its willingness to co-operate with the administrator that is usually appointed by the court.

On the other hand, experts throughout Member States stress that the failure of a reorganisation proceeding is often due to the fact that the debtor waits too long before initiating the adequate proceeding.

2. **The debtor and/or its creditors** (any creditor or the majority of creditors)

Finland, Greece (except for in regards to the Reforming Procedure), Ireland, Portugal, Sweden (but only with regard to the Reorganisation), the United Kingdom (but only with regard to the Administration) and the United States allow both the debtor and the creditors to initiate the proceeding.

However, in Greece, only the majority of creditors may initiate the procedure, whereas in the other countries, any creditor, and even a potential creditor, as in Finland and Ireland, may initiate the procedure.

We should add that in Ireland and in Sweden, in the vast majority of cases, the debtor usually makes the application, even though the creditors are entitled to do so.

3. **Particularities**

As discussed previously, Chapter 11 in the United States allows for both the debtor and the creditors, who meet the threshold requirements, to initiate the proceeding. Both types of initiation (voluntary in case of debtor initiation and involuntary in case of creditor initiation) leave the debtor in control of its assets (except for in cases of fraud whereby the court appoints a trustee to administer the proceeding). However, the voluntary proceeding allows the debtor to choose the exact date and the venue in which it wishes to file, to conduct the negotiations of the post petition financing and use of cash collateral, to control the dissemination of publicity, and to adequately alert and prepare its employees, vendors and suppliers of the pending filing.
In Germany, as the *Reorganisation based on insolvency plan* can only be initiated in the course of insolvency proceedings, both the debtor and the trustee in insolvency can petition for the commencement of the procedure.

In Greece, regarding the *Placing of companies limited by shares, general partnerships and limited partnerships under the administration and management of their creditors or under special liquidation*, only the majority of creditors may initiate the procedure, to the exclusion of the debtor. As we previously stated, this procedure fell into disuse.

In Ireland, in addition to the debtor and the creditor, any member of the company, and, if the company is in the course of being wound-up, the liquidator, may initiate the procedure.

In Portugal, in addition to the debtor and the creditor, the Public Prosecutor is entitled to initiate the procedure, like in Belgium. However, we remind that in Belgium, creditors are not granted that right.

In the United Kingdom, the *Receivership* may only be initiated by a debenture holder (if the debenture provides so), or by the court. The *Company voluntary arrangement* can be initiated by the debtor, by the administrator if the company is under *Administration* and by the liquidator if the company is under winding-up.

Overall, we have concluded that whether the debtor or creditor initiates the procedure has few consequences regarding the stigma on failure. Indeed, the eventual stigma attached to the introduction of a recovery procedure is first of all caused by the notification that is made to all creditors; whether the procedure had been initiated by the debtor or by one or several creditors has no significance. In the vast majority of procedures granted to debtors in difficulties, the decision that grants the procedure is public and the existence of the recovery procedure is notified to the creditors.

It should be noted, however, that in the U.S., a debtor who puts itself into bankruptcy often angers the creditors. If the debtor initiates the proceeding, the debtor chooses the time and control over notifying creditors and appeasing their worries. This is not necessarily the case if a creditor initiates the proceeding, in which case the debtor’s control over the business is truly threatened.

Almost all procedures are based on the consent among creditors to reduce or rearrange the debts of the business, suggesting that creditors are all involved in the procedure and informed of its evolution individually or, for example, through a creditors’ assembly.

It is difficult to strike the balance between the protection of creditors’ interests, through transparency and availability of information on the debtor, and the protection of the debtor, through confidentiality of proceedings. It seems that current European national legislation places higher emphasis on and importance to the protection of creditors. However, there are exceptions to this general rule and those will be further developed in points 7, 9 and 12 of this title.
## INITIATORS OF THE PROCEDURE

<table>
<thead>
<tr>
<th>Country</th>
<th>Initiators of the Procedure</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>· Debtor (whether an individual or a legal entity)</td>
</tr>
<tr>
<td>Belgium</td>
<td>· Debtor (whether an individual or a legal entity)</td>
</tr>
<tr>
<td></td>
<td>· Public prosecutor</td>
</tr>
<tr>
<td>Denmark</td>
<td>· Debtor</td>
</tr>
<tr>
<td>Finland</td>
<td>· Debtor (whether an individual or a legal entity)</td>
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<tr>
<td></td>
<td>· Creditor</td>
</tr>
<tr>
<td></td>
<td>· Potential creditor</td>
</tr>
<tr>
<td>France</td>
<td>· Debtor (whether an individual or a legal entity)</td>
</tr>
<tr>
<td>Germany</td>
<td>· Debtor (only legal entities)</td>
</tr>
<tr>
<td></td>
<td>· Trustee in insolvency (whether instructed by the creditors' assembly or not)</td>
</tr>
<tr>
<td>Greece</td>
<td>· Debtor (whether an individual or a legal entity)</td>
</tr>
<tr>
<td></td>
<td>· Majority of creditors</td>
</tr>
<tr>
<td>Ireland</td>
<td>Examinership</td>
</tr>
<tr>
<td></td>
<td>· Debtor (only legal entities)</td>
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<tr>
<td></td>
<td>· Creditor</td>
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<tr>
<td></td>
<td>· Potential creditor</td>
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<tr>
<td></td>
<td>Scheme of arrangement</td>
</tr>
<tr>
<td></td>
<td>· Debtor (only legal entities)</td>
</tr>
<tr>
<td></td>
<td>· Creditors</td>
</tr>
<tr>
<td></td>
<td>· Members of the company</td>
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<tr>
<td></td>
<td>· Liquidator</td>
</tr>
</tbody>
</table>
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

<table>
<thead>
<tr>
<th>Country</th>
<th>Details</th>
</tr>
</thead>
<tbody>
<tr>
<td>Italy</td>
<td>Debtor (only legal entities)</td>
</tr>
<tr>
<td></td>
<td><strong>Luxembourg</strong></td>
</tr>
<tr>
<td></td>
<td>Debtor (whether an individual or a legal entity)</td>
</tr>
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<td></td>
<td><strong>The Netherlands</strong></td>
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<tr>
<td></td>
<td>Debtor</td>
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<tr>
<td></td>
<td>If the debtor is a financial institute: the Dutch Central Bank</td>
</tr>
<tr>
<td></td>
<td><strong>Portugal</strong></td>
</tr>
<tr>
<td></td>
<td>Debtor (only legal entities)</td>
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<tr>
<td></td>
<td>Creditor</td>
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<tr>
<td></td>
<td>Public prosecutor</td>
</tr>
<tr>
<td></td>
<td><strong>Spain</strong></td>
</tr>
<tr>
<td></td>
<td>Debtor (whether an individual or a legal entity)</td>
</tr>
<tr>
<td></td>
<td><strong>Sweden</strong></td>
</tr>
<tr>
<td></td>
<td>Reorganisation</td>
</tr>
<tr>
<td></td>
<td>Debtor (whether an individual or a legal entity)</td>
</tr>
<tr>
<td></td>
<td>Creditor, with the consent of the debtor</td>
</tr>
<tr>
<td></td>
<td>Judicial composition</td>
</tr>
<tr>
<td></td>
<td>Debtor (whether an individual or a legal entity)</td>
</tr>
<tr>
<td></td>
<td><strong>UK</strong></td>
</tr>
<tr>
<td></td>
<td>Receivership</td>
</tr>
<tr>
<td></td>
<td>Debenture holder</td>
</tr>
<tr>
<td></td>
<td>Court</td>
</tr>
<tr>
<td></td>
<td>Administration</td>
</tr>
<tr>
<td></td>
<td>Debtor (only legal entities)</td>
</tr>
<tr>
<td></td>
<td>Creditor</td>
</tr>
<tr>
<td></td>
<td>Company voluntary arrangement</td>
</tr>
<tr>
<td></td>
<td>Debtor (only legal entities)</td>
</tr>
<tr>
<td></td>
<td>Administrator (companies under administration)</td>
</tr>
<tr>
<td></td>
<td>Liquidator (companies under winding-up)</td>
</tr>
<tr>
<td></td>
<td><strong>USA</strong></td>
</tr>
<tr>
<td></td>
<td>Debtor</td>
</tr>
<tr>
<td></td>
<td>Creditor</td>
</tr>
</tbody>
</table>

5) Administration of the procedure

a) Out-of-court proceedings

4.2 Legal possibilities to continue economic activities
In all countries analysed, unofficial proceedings are by nature regulated according to the will of the contracting parties. As a consequence, courts have no role and no administrator is appointed. The debtor retains its powers over its business, and the scope of the agreement is limited to the granting of delays of payment or of reductions of debts. Nevertheless, parties may for example, jointly appoint a third party to assist or to replace the management, on the condition of reaching consensus with all parties involved, or they may decide that the debtor will manage the business under the supervision of the creditors.

b) Court proceedings

In most EU Member States, once the procedure has been introduced, the court appoints an objective third party, whose function is primarily to assist and supervise the conduct of business operations during the proceedings. The U.S. chapter 11 procedure does not, however, necessarily involve the appointment of a trustee; actually, courts are even reluctant to appoint a trustee unless there is gross mismanagement or fraud.

Most EU regimes are based on the following hypothesis: the debtor has temporary financial difficulties, as a consequence of exceptional circumstances. Accordingly, the debtor is not necessarily considered a bad manager. This explains why most national procedures allow the debtor to keep the management of the enterprise, for example to make decisions relating to the disposal of the assets. Usually, these procedures, however, require a guarantee to the creditors. For the operations that might impair their rights, an authorisation of the third party (an administrator, or the trustee where the procedure has been initiated in the course of an insolvency proceeding) is required. Such procedures exist in Belgium, Luxembourg, Netherlands and Spain.

In the United States, management powers are usually left to the debtor, which officially becomes a “debtor in possession”. The trustee, if any, or the debtor are entitled to sell or use property in the ordinary course of business without a court order. Use of or sale of property out of the ordinary course of business, however, requires the court’s authorisation. The key point is to determine whether the operation is in the ordinary course of business or not.

In other procedures, the role of the appointed administrator is limited to the assistance and supervision of the operations that the debtor conducts. They may report to the court, for example, but are not allowed to prevent the debtor from acting. Austria, Finland, France, Ireland, Italy, Sweden and the United Kingdom (but only with regard to the Company voluntary arrangement) provide such procedures.

We already mentioned that Austria, Germany and Sweden provide the possibility to introduce a reorganisation procedure in the course of insolvency proceedings. In these cases, a trustee in insolvency is appointed to manage the bankrupt’s assets. In Austria and in Germany, the control of the business remains with the trustee; no administrator is specifically appointed for the conduct of the reorganisation procedure. During the procedure, the debtor is deprived of his right to manage. In Sweden, on the other hand, the function of the administrator is limited to investigation and negotiation with the creditors in order to conclude the composition.
Portugal provides an interesting panel of recovery measures, as we mentioned in section II. In principle, the debtor keeps management powers. Actually, no third party is appointed to assist it, but the creditors may supervise its operations, depending on the measure granted and its terms.

The United Kingdom also provides procedures where a third party retains control over the business: this is the case in the *Administration* and in the *Receivership*.

As for the effects of court proceedings on stigma, it is unclear as to whether the interference of an administrator in conducting the affairs makes creditors more confident with respect to the issue of the proceedings, and thus more willing to continue business.

On the one hand, creditors may perceive this third party as a protector of their rights, who will prevent the debtor from making any decision that would be unfavourable to their interests. But on the other hand, the sole existence of an administrator who assists or controls the management of the debtor may render its difficult situation even more serious from a creditor’s point of view.

Still, the presence of an administrator (instead of the debtor or even assisting him) may have a psychological effect, due to the impression that the transfer of the management of the debtor to a third party may show the inability and inaptitude of its management. This may engender a stigma, since such an impression may deter co-contractors from entering or from continuing business with this debtor.

### ADMINISTRATION OF THE PROCEDURE

<table>
<thead>
<tr>
<th></th>
<th>Austria</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Ordinary reorganisation</strong></td>
<td>Debtor retains control</td>
</tr>
<tr>
<td></td>
<td>Supervision of the administrator</td>
</tr>
<tr>
<td><strong>Compulsory reorganisation</strong></td>
<td>Bankruptcy administrator retains control</td>
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<thead>
<tr>
<th></th>
<th>Belgium</th>
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<tbody>
<tr>
<td></td>
<td>Debtor retains control</td>
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<tr>
<td></td>
<td>Supervision of administrator</td>
</tr>
<tr>
<td></td>
<td>Authorisation of administrators required for certain operations</td>
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</tbody>
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<table>
<thead>
<tr>
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<th>Denmark</th>
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<tbody>
<tr>
<td></td>
<td>Debtor retains control</td>
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<td></td>
<td>Supervision of the administrator</td>
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<thead>
<tr>
<th></th>
<th>Finland</th>
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<tbody>
<tr>
<td></td>
<td>Debtor retains control</td>
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<tr>
<td></td>
<td>Supervision of the administrator</td>
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<tr>
<td>Country</td>
<td>Legal possibility</td>
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</tr>
<tr>
<td>France</td>
<td>Independent preliminary bankruptcy</td>
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<td></td>
<td>Debitors retains control</td>
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<td></td>
<td>Supervision of independent receiver</td>
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<td></td>
<td>Amicable settlement procedure</td>
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<td></td>
<td>Conciliator prepares the plan</td>
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<tr>
<td>Germany</td>
<td>Trustee in insolvency retains control (except if self-management ordered by the court)</td>
</tr>
<tr>
<td>Greece</td>
<td>Debtor retains control</td>
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<tr>
<td></td>
<td>Supervision of administrator</td>
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<tr>
<td></td>
<td>If debtor fails to comply with the agreement: administrator shall retain control</td>
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<tr>
<td>Ireland</td>
<td>Examinership</td>
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<tr>
<td></td>
<td>Examiner retains control on the procedure</td>
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<td></td>
<td>Scheme of arrangement</td>
</tr>
<tr>
<td></td>
<td>No administrator</td>
</tr>
<tr>
<td>Italy</td>
<td>Debtor retains control</td>
</tr>
<tr>
<td></td>
<td>Supervision of the administrator</td>
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<tr>
<td>Luxembourg</td>
<td>Debtor retains control, BUT</td>
</tr>
<tr>
<td></td>
<td>Authorisation of administrator required</td>
</tr>
<tr>
<td>The Netherlands</td>
<td>Debtor and administrator retain control jointly</td>
</tr>
<tr>
<td>Portugal</td>
<td>Composition</td>
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<tr>
<td></td>
<td>Entrepreneurial reconstitution</td>
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<td>Entrepreneurial reconstitution: the board of the new company retains control</td>
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<td>Financial restructuring</td>
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<td></td>
<td>Controlled management</td>
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<tr>
<td></td>
<td>The new board of directors retains control</td>
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</table>
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

4.2 Legal possibilities to continue economic activities

<table>
<thead>
<tr>
<th></th>
<th>Spain</th>
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<tbody>
<tr>
<td></td>
<td>Debtor retains control, BUT</td>
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<tr>
<td></td>
<td>Authorisation of administrator required</td>
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<thead>
<tr>
<th></th>
<th>Sweden</th>
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<tbody>
<tr>
<td></td>
<td>Debtor retains control</td>
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<tr>
<td></td>
<td>Supervision of the administrator</td>
</tr>
<tr>
<td></td>
<td>Authorisation of administrators required for certain operations</td>
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<table>
<thead>
<tr>
<th></th>
<th>UK</th>
</tr>
</thead>
<tbody>
<tr>
<td>Receivership</td>
<td>Receiver maintains control</td>
</tr>
<tr>
<td>Administration</td>
<td>Administrator maintains control</td>
</tr>
<tr>
<td>Company voluntary arrangement</td>
<td>Debtor maintains control</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th></th>
<th>USA</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Debtor maintains control</td>
</tr>
<tr>
<td></td>
<td>Chapter 11 trustee or US trustee appointed by court only on request of an interested party or in case of fraud</td>
</tr>
</tbody>
</table>

6) Restructuring plan

Almost all procedures are based on the drafting of a plan to reorganise the business. The plan can take the form of an agreement or proposal and can be the result of an in-court or out-of-court proceeding.

Approval of the plan, including distribution of the debtor’s assets to the various classes of creditors is conditional upon the viability of the enterprise and upon each creditor’s chances to recover a profitable activity. A reliable plan is therefore an essential tool in convincing creditors that the debtor still has chances to recover.

a) The drafting of a plan

Legislation in all EU Member States and the United States provides for at least one type of bankruptcy proceeding that requires a restructuring plan, or proposal, whether that be prepared by the debtor or by the appointed administrator.

In Greece and in Luxembourg, however, legal reorganisation procedures that may be conducted without a plan also exist, including the Restructuring or winding-up of enterprises and the Reprieve of payments.
With the exception of these procedures, all legal procedures include the drafting of a plan that is subject to the vote and approval by the creditors, and to the subsequent ratification by the court.

\textit{b) The recovery measures}

Approval by the creditors is essential to the success of a recovery, as they must approve the submitted plan.

The plan must, therefore, contain a clear description of the estate of the debtor’s business, including a statement of assets and liabilities, and a complete view of the proposed recovery measures to be taken and their potential effect on the survival of the enterprise. These measures should detail proposals on restructuring the debts of the enterprise, payment schedules to the creditors, and the role of the management.

Overall, the plan should provide creditors with a clear understanding of the current and future state of the business, so they can decide whether or not the plan is in their best interests and should be approved.

\textit{c) Adoption of the plan}

Confirmation by creditors is always necessary in the adoption of a plan, but minimum requirements for approval of the plan vary in each country. In all countries analysed, the power of the court is very broad, including the right to reject a plan that has been approved by the necessary majority of creditors. Such a rejection should be based, depending on the various legal systems, on the protection of the interest of creditors or of the public.

As already mentioned, the competent court in most Member States has the power to authorise (‘ratify’) the plan accepted by the creditors. However, in the United Kingdom (\textit{Company voluntary arrangement}), the court is not entitled to approve the proposals submitted by the nominees. The \textit{Administration} procedure gives wide powers to the court regarding the proposals, under certain circumstances.

In Belgium, France, and Luxembourg, the court can authorise the plan on the condition that the required majorities have been reached. However, even in such a case, the court has the power to reject the plan.

In Austria, Finland, Germany and Ireland, law provides several conditions under which the court must reject the plan, and other conditions under which the court may reject it.

In Denmark, the court has no influence regarding the \textit{Suspension of payments}; however, with regard to the \textit{Compulsory composition}, the plan is an integral part of the composition proposal and dependent upon the acceptance of the court.

In Germany (in the \textit{reorganisation based on insolvency plan}), the court has strong discretionary powers, which allows it to decide whether or not to confirm the plan.
Whilst Spain considerably limits the powers of the court. Once the plan has been adopted by the legally required majority of creditors, the court takes 8 days to announce the approval of the composition after the date of the creditors meeting. Within this period, certain legally defined creditors are entitled to oppose the composition. In the even that there is no opposition within this period of delay, the court must approve the composition. In the same way, in Portugal, powers of the court are strictly limited to a control of the respect of the applicable legal rules, to the exception of any opportunity control.

It seems that in Europe creditor protection is one of the main legislative objectives with the court guaranteeing such protection. In the U.S., however, bankruptcy judges consider the primary purpose of a chapter 11 proceeding to be preservation of the value of the debtor and its operations and avoidance of economic disruption and employee dislocation that occurs upon the piecemeal liquidation of a business. With this perspective, bankruptcy courts make decisions based on the overall goal of reorganising the business, even over strong creditors’ objections. In fact, if the creditors reject the plan, the bankruptcy judge can overrule this and confirm the plan if the court finds the plan “fair and equitable.”

The U.S. approach towards the creditors’ rights contrasts with that of some of its European counterparts. For example, legal systems influenced by the Germanic tradition aim first at the protection of the creditors instead focusing on the recovery of the debtor.

<table>
<thead>
<tr>
<th>RESTRICTURING PLAN</th>
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<tbody>
<tr>
<td><strong>Austria</strong></td>
</tr>
<tr>
<td>· plan drafted</td>
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<tr>
<td>· vote of creditors</td>
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<tr>
<td>· if legal majorities reached: confirmation by court (non-discretionary power)</td>
</tr>
<tr>
<td><strong>Belgium</strong></td>
</tr>
<tr>
<td>· plan drafted</td>
</tr>
<tr>
<td>· vote of creditors</td>
</tr>
<tr>
<td>· confirmation by the court (discretionary power)</td>
</tr>
<tr>
<td><strong>Denmark</strong></td>
</tr>
<tr>
<td><strong>Suspension of payments</strong></td>
</tr>
<tr>
<td>· plan drafted</td>
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<tr>
<td>· vote of creditors</td>
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<tr>
<td><strong>Composition</strong></td>
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<tr>
<td>· plan drafted</td>
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<td>· confirmation by the court (non-discretionary power)</td>
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<td>Finland</td>
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<td>Luxembourg</td>
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<tr>
<td>The Netherlands</td>
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</tbody>
</table>
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

<table>
<thead>
<tr>
<th>Country</th>
<th>Process Details</th>
</tr>
</thead>
</table>
| Portugal | - plan drafted  
            - vote of creditors  
            - if legal majorities reached: confirmation by court (non-discretionary power) |
| Spain    | - plan drafted  
            - vote of creditors  
            - confirmation by the court (non-discretionary power) |
| Sweden   | - plan drafted  
            - vote of creditors  
            - confirmation by the court (discretionary power) |
| UK       | - plan drafted  
            - vote of creditors |
| USA      | - plan drafted  
            - vote of creditors  
            - confirmation by the court (discretionary power) |

7) **Degree of protection of creditors**

a) **Out-of-court proceedings**

Informal, out-of-court proceedings are based on the agreement or plan made between the debtor and its creditors, which usually requires the consent of a defined percentage of creditors. Since the agreement is only binding upon consenting creditors, the success of the plan is highly dependent on the treatment and protection of those creditors.

In some countries like Austria and Germany, legal principles, such as the principle of the equality of treatment and the protection of secured creditors’ claims, must still be complied with in the informal proceedings.
In the U.S., a consensual restructuring outside of chapter 11 is known as a “workout.” Although the restructuring of the company’s debt must be consensual in order to effectively implement a workout, a factor that strongly influences the extent to which creditors are willing to compromise on a position is the chapter 11 process itself. The debtor may even threaten the commencement of a chapter 11 case in order to exact a compromise from its creditors.

b) Court proceedings

In the vast majority of Member States, the procedure is based on a reorganisation plan. In these cases, on the condition that it has been approved by the required majorities, the court may or must confirm the reorganisation plan or arrangement. Where the plan violates the interests of all or part of the creditors (even those who voted for the plan), the court may, and sometimes must, reject the plan, which is an important feature of creditor protection. Spanish bankruptcy law dictates, however, that the court must approve the plan in cases where no creditors oppose it within a specified period of time.

The process as described above is similar in the U.S., except that there is perhaps less focus on the protection of the creditors. In the U.S., if the debtor is unable to obtain the acceptance of an impaired class of creditors for approval of the plan, he may nevertheless obtain confirmation of the plan if the bankruptcy court finds that the plan is “fair and equitable” and does not discriminate unfairly against any class of claims or interests that is impaired and has not accepted, the plan.

Most EU Member States distinguish between secured and unsecured creditors, in voting on and confirming the plan, while some countries’ legislation calls for equal treatment of creditors in confirmation of the plan.

1. Post-petition debts

In all EU Member States and in the Unites States, post-petition debts are considered super-privileged, and are cured before all other debts. These creditors are, therefore, not subject to the plan of reorganisation.

2. Secured and unsecured debts

In Austria, Denmark, Italy, Luxembourg (in the Reprieve of payment), the Netherlands, Sweden (in the Composition), Spain, and the United Kingdom, secured creditors benefit from a particular protection. They can choose whether or not they want to participate in the plan and are not obligated to it if they choose not to.

On the other hand, Belgium, Finland, France, Germany, Greece (except for employees), Ireland, Luxembourg (for the Controlled management), Portugal and the United States provide procedures for all creditors to vote on the agreement or the plan. If the legally required majorities are reached, all creditors are bound by it, even those who voted against it. It may occur, however, that the plan must comply with the legal sequence of creditors, as in Finland.
<table>
<thead>
<tr>
<th>DEGREE OF PROTECTION OF CREDITORS</th>
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<tbody>
<tr>
<td><strong>Austria</strong></td>
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<tr>
<td>· Privilege of debts arising after initiation of the procedure</td>
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<tr>
<td>· Unsecured creditors are bound by the agreement</td>
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<tr>
<td><strong>Belgium</strong></td>
</tr>
<tr>
<td>· Privilege of debts arising after initiation of the procedure</td>
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<tr>
<td>· All creditors are bound by the agreement</td>
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<tr>
<td><strong>Denmark</strong></td>
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<tr>
<td><strong>Finland</strong></td>
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<td><strong>France</strong></td>
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<tr>
<td>· Privilege of debts arising after initiation of the procedure</td>
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<tr>
<td>· All creditors are bound by the agreement</td>
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<tr>
<td><strong>Germany</strong></td>
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<tr>
<td>· Privilege of debts arising after initiation of the procedure</td>
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<tr>
<td>· All creditors are bound by the agreement</td>
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<tr>
<td><strong>Greece</strong></td>
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<tr>
<td>· Privilege of debts arising after initiation of the procedure</td>
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<tr>
<td>· All creditors are bound by the agreement (except the employees)</td>
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<tr>
<td><strong>Ireland</strong></td>
</tr>
<tr>
<td>· Privilege of debts arising after initiation of the procedure</td>
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<tr>
<td>· All creditors are bound by the agreement</td>
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</table>
### Legal possibilities to continue economic activities

<table>
<thead>
<tr>
<th>Country</th>
<th>Details</th>
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<tbody>
<tr>
<td>Italy</td>
<td>- Privilege of debts arising after initiation of the procedure&lt;br&gt;</td>
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<tr>
<td></td>
<td>- Unsecured creditors are bound by the agreement</td>
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<tr>
<td>Luxembourg</td>
<td><strong>Reprieve from payments</strong>&lt;br&gt;- Privilege of debts arising after initiation of the procedure&lt;br&gt;- Unsecured creditors are bound by the agreement</td>
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<tr>
<td></td>
<td><strong>Controlled management</strong>&lt;br&gt;- Privilege of debts arising after initiation of the procedure&lt;br&gt;- All creditors are bound by the agreement</td>
</tr>
<tr>
<td>The Netherlands</td>
<td>- Privilege of debts arising after initiation of the procedure&lt;br&gt;</td>
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<td></td>
<td>- Unsecured creditors are bound by the agreement</td>
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<tr>
<td>Portugal</td>
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<td>- All creditors are bound by the agreement</td>
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<tr>
<td>Spain</td>
<td>- Privilege of debts arising after initiation of the procedure&lt;br&gt;</td>
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<td>Sweden</td>
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<tr>
<td>UK</td>
<td>- Privilege of debts arising after initiation of the procedure&lt;br&gt;</td>
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<td></td>
<td>- Unsecured creditors are bound by the agreement</td>
</tr>
<tr>
<td>USA</td>
<td>- Privilege of post-petition debts&lt;br&gt;- All creditors are bound by the agreement</td>
</tr>
</tbody>
</table>

#### 8) Termination of the procedure

Confirmation and implementation of the plan adopted ordinarily discharges the debtor from liability for all debts arising prior to the effective date of the plan of reorganisation, except to the extent that the plan of reorganisation does not apply to certain categories of them. This is the case in Austria, Belgium, Finland, France,
Germany, Greece, Ireland, Italy, Luxembourg (for the Controlled management), the Netherlands, Sweden, Spain, and in the U.S.. The Portuguese Composition, which usually includes a clause “return to better fortune,” obliges the undertaking to pay its creditors proportionally as soon as its economic situation improves.

If the case of a breach of agreement by the debtor, the possibility to terminate the plan and proceeding is provided by most Member States’ bankruptcy law. In this case, creditors recover their individual rights of execution against the debtor, or eventually bankruptcy or winding-up proceedings are commenced.

The Irish procedure of “Examinership” is terminated seventy days from the date of the petition or on the withdrawal or refusal of the petition, whichever first happens. The court may extend that period by no more than 30 days. The procedure may also cease by the coming into effect of the compromise or the scheme of arrangement or on such an earlier date that the court may direct. If no plan is confirmed by the given date, the court terminates the procedure, causing the debtor to inevitably go into liquidation.

The Suspension of payments under Dutch law may be terminated by the fulfilment of the restructuring plan, but it may also end on expiry of the term fixed by the court or upon request of the court, the creditors, the administrator or the debtor.

We noted earlier that the Luxembourg Reprieve of payment does not involve the elaboration of a plan, but only grants the undertaking of a moratorium of payments. The Reprieve of payments consequently expires after a certain duration fixed by the court. Moreover, the undertaking has the possibility to withdraw the application, and one or more creditors, or the appointed commissioners, may request its revocation, under certain conditions.

Apart from the Composition, which is based on a reorganisation plan, Portugal provides for original solutions, based on a very broad variety of recovery measures that may be granted. The Entrepreneurial reconstitution ends by the setting up of a new company, which determines the instantaneous extinction of the legal entity holding the company, whenever the agreement comprises all the assets of the company or the removal of the sole entrepreneur involved in the agreement. The Financial restructuring ends upon the decision of the judge, as soon as the full execution of the measure has been secured, but no later than 60 days after resolution of the assembly. The Controlled management ends on expiry of the term fixed by the plan, which cannot last more than 2 years. The company then recovers its normal activity and creditors whose claims have not been satisfied recover their rights of execution.

9) Degree of information

The degree of information accessible to creditors varies from one country to the next.

Most EU Member States and the U.S. require notifying creditors of the initiation of recovery proceedings.

However, in Finland, only the most significant creditors (regarding the amount of their claims,) as well as those the court requires, are notified of the debtor’s
Restructuring petition. Other creditors are not personally contacted about the petition, except through the publication at the onset of the proceedings, that will be addressed under section 12). Only these most significant creditors are thus involved in the process and kept informed, since their consent is required to achieve a successful result.

Similarly, the French *Amicable settlement procedure* requires only the most important creditors to be invited to participate in the proceeding (i.e. those who are owed most significant amounts or those who hold important guarantees); other creditors are not advised of the commencement of the procedure, since it is strictly confidential.

In Luxembourg, the *Controlled management* is confidential until the court decides to appoint one or more administrators. Creditors are thus only consulted at the stage of the submission of the reorganisation plan, which is after the start of the *Controlled management* of the company. Creditors have a right of appeal against the decision of the court, but this right is theoretical since the decision is not published and the delay to appeal is short. Although the creditors’ participation in the proceeding is limited, the prospects for debtor recovery might be substantially improved, since the debtor is protected from the negative publicity that is often generated in a recovery attempt.

In addition to the information relating to the initiation of the procedure, creditors are usually kept informed of the progress of the proceedings. They are invited to the court hearings, and have knowledge of all information contained in the plan, since they are supposed to vote on it. Austria, Belgium, Germany, Ireland, Italy, Luxembourg (with regard to the *Reprieve of payments*), the Netherlands, Portugal, Sweden, Spain and the United Kingdom provide such a system. Greek law provides a system that ensures information of participating creditors, others being informed through the general publicity.

In France, however, only creditors who agreed to participate in the *Independent preliminary bankruptcy* are kept informed of the progress of the proceeding. Although this duty of confidentiality is not legally sanctioned, it is in practice respected. The French *Amicable settlement procedure* is interesting with regard to stigma: it provides a duty of confidentiality imposed on all persons involved in the procedure, breach of which is a criminal offence. This improves the chances of success, since it is based on the implication of only the most significant creditors, and guarantees confidentiality, which might reduce the stigma.

We believe both procedures should be used as examples of a successful reorganisation procedure. Limiting access to information, including reports on the progress of the procedure, to participating creditors, would considerably improve the chances for the enterprise to recover without suffering the stigma generated by too much general publicity.

Access to the court files is guaranteed to creditors in countries, such as Austria, Belgium, Greece (with regard to the procedure of *Placing of companies limited by shares, general partnerships, and limited partnerships either under the administration and management of their creditors, or under special liquidation*), Italy (upon authorisation of the delegated judge), the Netherlands (Dutch law provides for a right of access to a very large number and variety of documents), Portugal, and Spain.
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

We should underline that creditors who are not personally informed may, where such publicity is required by law, be informed of this through the use of general publicity (see point 12).

The availability of information of creditors is an essential element to the success of the procedure. Only an informed creditor who has clear insight into the prospects for the debtor to reorganise is going to accept a proposal, scheme of arrangement, restructuring plan, or any sort of agreement. No creditor will support an attempt to continue business despite temporary difficulties if it is not ‘proven’ that the chance of the undertaking to recover is realistic. Indeed, recovery procedures are unanimously considered as expensive; administrator’s fees, as well as procedure’s costs, must be paid first, reducing the guarantees of those who were creditors at the time of the commencement of the proceedings. In order to commence recovery procedure, it is necessary to convince all or at least the majority of creditors that they will receive more by supporting the procedure than they would receive upon liquidation.

To assess the real chances of a debtor to recover from its difficulties, it is necessary for the creditors to be guaranteed minimum information relating to the assets and liabilities of the undertaking. This right of information must however be balanced with the potential detrimental effect of publicity on the continuation of business operations.

The disclosure of the economic and financial situation of the debtor to its potential partners, its creditors, and its consumers, may indeed be an important factor of stigma.

To that extent, we recollect however that the disclosure of information does not automatically generate stigma, depending on the sociological perception of failure. As already mentioned, in the United States, the initiation of a reorganisation procedure has no effect to that point, and may even have beneficial effects.

However, we agree with our correspondents that in the EU Member States, business partners, investors and consumers are traditionally reluctant to trust a debtor who is in a difficult financial situation. The legislator itself shows reluctance to trust the debtor in such a case, since in general, national legislation provides for the appointment of an administrator to supervise, assist, and approve the decisions of the debtor. In the United States, on the other hand, the legislator provides for the appointment of a third party only where there was gross mismanagement and fraud.

We assume that the legislator’s view reflects the society’s opinion on that point. We thus think that it may be confirmed that in EU Member States, the commencement of reorganisation proceedings is perceived in a negative way rather than in a neutral or positive way. Accordingly, information and publicity may then generate stigma since it brings the existence of this procedure to the attention of the public.

DEGREE OF INFORMATION

4.2 Legal possibilities to continue economic activities 228
4.2 Legal possibilities to continue economic activities

<table>
<thead>
<tr>
<th>Country</th>
<th>Notification of the initiation of the procedure</th>
<th>Access to court files</th>
<th>Information contained in the plan</th>
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<tbody>
<tr>
<td>Austria</td>
<td>Notification of the initiation of the procedure to all creditors</td>
<td>Access to court files</td>
<td>Information contained in the plan</td>
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<td>Belgium</td>
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<td>Access to court files</td>
<td>Information contained in the plan</td>
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<tr>
<td>Finland</td>
<td>Notification of the initiation of the procedure only to significant creditors</td>
<td>Access to court files</td>
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<tr>
<td>France</td>
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<tr>
<td>Greece</td>
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<td>Ireland</td>
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<td>Access to court files</td>
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<tr>
<td>Italy</td>
<td>Notification of the initiation of the procedure to all creditors</td>
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<td>Information contained in the plan</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>Notification of the initiation of the procedure to all creditors</td>
<td>Access to court files</td>
<td>Information contained in the plan</td>
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</tbody>
</table>
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

4.2 Legal possibilities to continue economic activities

| Controlled management | · Notification of the initiation of the procedure after |
| Reprieve from payments | · Appointment of the administrator |
|                        | · Notification of the initiation of the procedure to all creditors |

| The Netherlands |
| · Notification of the initiation of the procedure to all creditors |
| · Access to court files |
| · Information contained in the plan |

| Portugal |
| · Notification of the initiation of the procedure to all creditors |
| · Access to court files |
| · Information contained in the plan |

| Spain |
| · Notification of the initiation of the procedure to all creditors |
| · Access to court files |
| · Information contained in the plan |

| Sweden |
| · Notification of the initiation of the procedure to all creditors |
| · Information contained in the plan |

| UK |
| · Notification of the initiation of the procedure to all creditors |
| · Information contained in the plan |

| USA |
| · Notification of the initiation of the procedure to all creditors |
| · Information contained in the plan |

10) Costs

In all EU Member States and in the United States, out-of-court proceedings are generally less expensive than in-court proceedings.

In-court proceedings include judicial costs and the fees of the third party appointed by the judge, expert costs and all costs regarding the creditors’ meetings, the notifications to creditors, correspondence, and all other expenses, which are usually high. In addition, in all EU Member States and in the U.S. in-court proceedings, these fees are treated as privileged claims and paid first, before all pre-petition debts.

The high cost of official proceedings can be seen as an obstacle that may prevent and discourage the debtor to initiate rehabilitation proceedings. This is one of the reasons...
that the decision by the debtor to initiate reorganisation proceedings is often made too late.

Likewise, unless the debtor shows strong recovery potential, creditors, knowing that an official proceeding will subordinate their claims to the fees related to the proceedings, will be more likely to object to the proceeding. They take on the added risk that in the event that the recovery fails, creditors will often obtain less in value than what they would have obtained through liquidation.

11) Structure of the bankruptcy courts

In European Member States, reorganisation proceedings are a matter of private law. These proceedings are done under civil law courts (commercial courts). In certain EU Member States, these courts have (specialised) units or sections for insolvency matters, which are sometimes called “reorganisation courts” or “bankruptcy courts,” depending on their function in a specific case. These units and sections have exclusive jurisdiction over reorganisation cases (complying with territorial competence). In Finland for example, there are 19 specific district courts that deal with restructuring matters. This results in a high degree of expertise. The Irish Examinership and Scheme of arrangement are matters that are dealt with by the High Court. Since the High Court is not divided into units, Irish law states that the President of the High Court shall assign three judges to deal with reorganisation matters. These assigned judges accordingly have the requisite specific expertise.

The restructuring function is entrusted to well-experienced judges who make overall decisions in the interest of the general public and the national economy. The experience and reputation of the judges presiding over a case may serve to reassure potential co-contractors, suppliers, consumers, and the public in general. The idea of judicial proceedings under the surveillance of specialised courts with judges experienced in the field of reorganisation provides a sort of protection of the rights of all parties involved and of general public interest.

Unlike in all EU Member States and the U.S., in Spain there are neither special courts nor special units of civil law courts in charge of insolvency or reorganisation procedures. Civil courts hear Suspension of payments cases. Judges of this court do not receive specialised education on business law or insolvency matters. Their qualification in insolvency matters is consequently sometimes considered as unsatisfactory. Nevertheless, we should mention that in practice these judges usually tend to entrust the handling of the procedure to the supervising auditors that they appoint. The most significant decisions that the judge makes in the course of the proceeding are based on the reports issued by the auditors. In practice it is quite unusual that the decision of the judge differs from the opinion expressed by the auditors.

While this practice compensates for the judges’ lack of specialised knowledge, it should be emphasised that supervising auditors are selected from a reduced circle of accounting experts. This situation brings into question the independence and objectivity of the auditors. Furthermore, it reduces the possibilities to enhance the qualifications of the persons acting as supervising auditors.
Spanish insolvency practitioners severely criticise the current Spanish insolvency procedure.

<table>
<thead>
<tr>
<th>STRUCTURE OF THE COURT</th>
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<tbody>
<tr>
<td>Austria</td>
</tr>
<tr>
<td>Specialised court, or specialised section or unit of civil courts</td>
</tr>
<tr>
<td>Belgium</td>
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<tr>
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Publicity refers to both official, court documents submitted in relation to the reorganisation proceeding, as well as any printed, published or reported news about a company’s reorganisation proceedings through official gazettes, newspapers, magazines, the Internet, TV, or any other official or unofficial news source.

In this report, we are concerned about the impact publicity of a proceeding might have on the debtor’s overall chance of recovery. It seems that such publicity often results in a stigma being placed on a distressed debtor by potential investors, business partners and consumers. A debtor in distress is perceived as having failed. This can often result in investors being reluctant to finance new or ongoing activities, business partners being reluctant to enter into or continue relationships and consumers being reluctant to buy the services or products offered by the company. Instead of helping the debtor, this attitude of clients, creditors, partners and investors further precipitates the company’s failure. The more publicly known the debtor’s problems are, the higher the potential a negative stigma against the debtor.

Court proceedings usually provide at least a public announcement of the initiation of the procedure and of its ending. This can cause irreversible damage to the debtor right from the onset of the proceeding.

Out-of-court procedures, however, are based on agreements between the debtor and all or part of the creditors that are kept confidential. Only participating parties are kept informed of the process, according to the terms of the agreement. It can be said that this mitigates the effect such proceedings have on the stigma of the debtor.

The degree of publicity varies depending on how information is made public and on what kind of information is publicly revealed.
In most EU Member States, the commencement and termination of reorganisation or winding-up proceedings is published in official national gazettes and on one or two national newspapers, determined by either the court or by law. This is the case in Belgium, Denmark, Finland, Germany, Ireland, Luxembourg, the Netherlands, Portugal, Sweden and the United Kingdom.

In Austria, commencement of a reorganisation is made public on the Internet (http://www.edikte.justiz.gv.at). The announcement contains the essential data on the proceeding, resulting in the proceeding being highly publicised.

Irish law and UK law are severe regarding publicity of the initiation of the reorganisation procedures. As soon as a debtor is under Examinership (Irish law), or Administration or Receivership (UK law), every invoice, every order for goods and every business letter by the debtor or on behalf of it shall mention that the debtor is being put under these procedures. Furthermore, in Ireland the failure to comply with this obligation is an offence that may lead to a conviction for a fine of up to 12,700 €.

In addition, Finland, Germany, Ireland, Italy, Spain, and the United Kingdom require commencement of the proceedings to be published in the Trade Register and other related registers.

In the UK, company voluntary arrangement is not made public.

Powers of the Spanish judges are really strong regarding the publicity to be given to a reorganisation procedure. The judge has the freedom to give the necessary publicity to the situation of the debtor for the general knowledge, taking into account the importance of the suspension granted, the number of creditors and the extension of the business. Usually such publicity is made through a publication in the national official gazette and/or in the regional official gazettes.

In Italy, it is sometimes the case that modern ways of communication and advertisement are used (instead of by personal registered mail) in the largest and most important procedures that concern a large number of creditors difficult to attain. Of course, such a possibility may engender a detrimental publicity to the debtor.

In addition to the publication of the opening of the procedure, certain countries provide for a public access to court files, notably the plan, as in Finland and the Netherlands (where the drafted plan is published in the official gazette).

Regarding prevention of stigma, French law provides for a very interesting procedure, as we already mentioned it in § 9. In the Independent preliminary bankruptcy, there is no legal requirement for publication. Confidentiality is not legally guaranteed however, but in practice only creditors who agree to participate in the process are kept informed of its evolution. The Amicable settlement procedure goes even further, since there is a duty of confidentiality imposed on all involved parties, and violation of which is criminally punishable. As a result, if the reorganisation is successful, no one will ever know that the debtor had difficulties at one time and that it has been reorganised.
The Greek *Restructuring of enterprises* is not publicly announced. Only a notification is made to creditors.

Information on a Chapter 7 or Chapter 11 filing is generally widely available and easily accessible to the public, especially depending on the size of the filing. When a business files for Chapter 11 with the court, it must submit certain schedules related to the business, operations and financials of the company to the court. Thereafter, a company’s actions are monitored by the court in the form of official schedules that must be submitted to the court regularly. Among reports that a debtor must submit to the court includes cash flow forecasts, biweekly income statements, etc.

Any schedules or documents that are submitted to the court are accessible to the public through the federal court that the case was filed in. The federal courts have a number of electronic public access systems available, including Voice Case Information System (VCIS) (toll free number for ordering), Public Access to Court Electronic Records (PACER) (modem-based access), the U.S. Party/Case Index (USPCI), Electronic Case Filing (ECF), which also provides electronic access to filings and related documents, but is simply a different source than PACER.

All bankruptcy court websites are accessible free of charge through [www.uscourts.gov](http://www.uscourts.gov).

In addition, there are a number of other non-court related services available to the public for retrieving the bankruptcy documents filed with the courts. Usually, these are available instantly online on a pay-per-report basis. One of these services is called [www.bankruptcydata.com](http://www.bankruptcydata.com).

Other information sources that are dedicated to reporting news on bankruptcies, but do not provide access to the actual documents filed by a debtor to the court, include:

- [www.bankruptcydata.com](http://www.bankruptcydata.com)
- [www.fedfil.com/bankruptcy/](http://www.fedfil.com/bankruptcy/)
- [www.uscourts.gov](http://www.uscourts.gov)
- [www.bankrupt.com](http://www.bankrupt.com)
- [www.abiworld.org](http://www.abiworld.org)
- [www.turnaround.org](http://www.turnaround.org)
- [www.turnarounds.com](http://www.turnarounds.com)

In the United States as well as in all EU Member States, the initiation of a reorganisation procedure will be published in all major online and printed business newspapers and magazines, and through television, depending on the size of the enterprise involved.

### PUBLICITY OF THE PROCEDURE

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4.2 Legal possibilities to continue economic activities
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<td>UK</td>
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<td>USA</td>
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#### 4.2.4. CONCLUSION

Analysis of each of the national reports reveals that EU Member States legislation is not harmonised at this point. Many EU Member States and the U.S. have several in-court and out-of-court options for reorganisation.
It appears that every country analysed has a similar legal framework for reorganisation of a distressed business. All proceedings seem to focus heavily on participation of creditors in the process, which suggests that the success of reorganisation proceedings depends strongly on the best protection of the creditors’ interests.

Analysis of the EU Member reports indicates a strong preference by all participants for informal agreements and a strong belief that formal reorganisation proceedings attach too much negative publicity to the creditor. Debtors fear this publicity, knowing or fearing that it will precipitate their failure, and consequently delay initiation of any reorganisation to the point that their businesses are beyond recovery.

Two countries appear to offer slightly different options. France developed a confidential procedure based on the sole participation of the major creditors. The confidentiality of this procedure protects the debtor from negative publicity, while offering possibilities for restructuring. Portugal offers the possibility for a business in distress to be granted recovery measures among a large panel of measures.

In examining the influence of the reorganisation proceedings in the EU Member States on the launching of new commercial activities, it is necessary to discuss the US Chapter 11 procedure.

In the United States, consumers, business partners and investors do not fear entering into or continuing business relationships with a debtor in distress. Even though the initiation of a Chapter 11 case is publicly announced (and this publicity is strong in the United States: Internet, access to court files), the debtor’s reputation does generally not get destroyed. This is perhaps due to the more tolerant attitude toward failure and failed companies in the US.

In fact, initiation of such a procedure is even seen positively, as it indicates to creditors and other related parties that the business is addressing its problems and taking steps to solve those and start over in a financially strong position than before. This is the case even though Chapter 11 sometimes ends up in the company’s winding-up or liquidating. Management is not afraid of petitioning for such a procedure and therefore reacts with enough time to increase its chances of recovery.

Procedures in the EU Member States lean toward a traditional pro-creditors approach, while in the United States practice favours recovery of the debtor, even at the expense of the creditors. All EU Member States provide procedures based on the agreement of creditors, and these would definitely not give their consent to a reorganisation procedure except if it is more advantageous than a liquidation. The court’s confirmation, if any, is conditional upon the reaching of legally required majorities and complying with the interests of the creditors.

This is also the case in the U.S. system. However, U.S. courts also consider that the interest of preserving the going concern value of an operating enterprise and avoiding a disastrous liquidation should prevail over the interests of creditors that might be opposed to reorganisation. As a consequence, a plan that has not been adopted by the legally required majorities of creditors may be confirmed by the court anyway; if it is deemed to be “fair and equitable,” this concept being legally defined.
Critical analysis provided by the EU national reports showed that unpopularity of reorganisation procedures and their too frequent failure may be a consequence of the reluctance of many managers or individual businesses, undertakings or debtors to consider taking advice from insolvency experts at an early stage of distress, in order to determine whether they should petition for insolvency or reorganisation procedures.

This may be due, among other reasons:

- to a lack of understanding of what options are available, or
- to the desire to maintain their own positions and income for as long as possible, or
- to a reluctance to accept how serious the situation really is, or
- to the fear to be classified as a business that failed, whereas that is not (or maybe not yet) the case.

These managers or individual businesses, undertakings or debtors may also be reluctant to alert creditors at an early stage, as this might result in them taking actions to execute their rights instead of allowing the business to attempt a recovery.

On the contrary, in the U.S., there is an established and extensive practice surrounding corporate recovery and turnaround. Many independent experts are dedicated solely to corporate turnaround and prevention of insolvency and any actions taken by companies to hire such experts is kept fully confidential.

For all these reasons, the legal possibilities to continue economic activities throughout EU Member States are generally perceived as unsuccessful and unsatisfactory. The number of procedures initiated and successful reorganisations is very low. In a downward spiralling trend, the more reorganisations fail, the less creditors, suppliers, and customers will gain confidence in such proceedings. In other words, more proof that rehabilitation can be successful is necessary to change the existing negative attitude towards entrepreneurs facing financial difficulties.
4.3. LEGAL CONSEQUENCES OF BANKRUPTCY AND POSSIBILITIES FOR A FRESH START

This title summarises the bankruptcy procedures organised in the EU Member States and in the U.S. (hereafter “targeted Countries”). A thorough comparison between the different procedures is presented, in order to emphasise their particularities and to evaluate their degree of adequacy.

This title also describes the legal consequences arising from such procedures as well as the stigma that may result therefrom. These consequences will then be compared in order to highlight the general causes of a stigma of failure and develop the possibilities for a fresh start.

4.3.1. INTRODUCTION

Contrary to restructuring procedures aimed at rescuing a business (see section 4.2 of this report), bankruptcy is a formal judicial or administrative procedure that aims principally at realising the bankrupt’s assets for the purpose of distributing the net proceeds to its creditors, usually as a result of its insolvency. In some countries however, the initiation of bankruptcy proceedings may result in the reorganisation of the business.

Bankruptcy procedures have important consequences regarding the liability of management and entrepreneurs, the prohibition from practising certain professions, criminal offences, etc. Currently the bankruptcy procedures create a stigma on failure, prohibiting entrepreneurs from starting new businesses.

4.3.2. INITIATION OF BANKRUPTCY PROCEDURES AND DIRECT EFFECT OF THESE PROCEDURES

4.3.2.1. OVERVIEW OF THE NATIONAL PROCEDURES

A. AUSTRIA

In Austria, bankruptcy (“konkurs”) is governed by the Bankruptcy Act of 1914.

Austrian bankruptcy law is primarily creditor oriented and mainly aims at liquidating the debtor’s assets instead of trying to rescue the business.

1. Initiation of the proceedings

Bankruptcy applies to companies only, unlike the “private bankruptcy” (or “privatkonkurs”) for which only individuals may petition. The latter will not be further considered in this report.

Bankruptcy can be petitioned by:

- the debtor
- or a creditor
- or the court (only when the court has rejected an application by the business) for
the opening of reorganisation proceedings or when such proceedings did not lead
to a successful settlement).

2. **Criteria for the petition:**

The ground for initiating bankruptcy proceedings is the *illiquidity* of the debtor (i.e.
when he can no longer meet his financial obligations for a certain period of time). He
must also be in a situation of *over-indebtedness* (i.e. his liabilities must exceed his
assets. A pre-bankruptcy balance sheet must be established to determine whether the
debtor is overly indebted).

The debtor must also have sufficient assets to cover the costs of the proceedings.

3. **Effects:**

A bankruptcy order is made by the court. The main effects of the judgement of
Bankruptcy are:
- creditors must declare their claim within a specific deadline;
- a *bankruptcy administrator* is appointed, in order to continue, if possible, the
debtor’s business, inventory and liquidate the assets;
- a *creditors’ committee* is appointed by the court. Such committee is composed of
three to seven members, for the purpose of checking the cash management,
assisting the bankruptcy administrator and approving certain transactions;
- a *creditors’ assembly* supervises the bankruptcy administrator and the creditors’
committee
- a peculiar body is the *Association for the Protection of Creditors’ Rights*: there are
in Austria 3 associations, created upon approval of the Federal Ministry of Justice,
that represent and secure creditors in the course of insolvency proceedings.
- the assets can be distributed following the distribution plan drafted by the
bankruptcy administrator and approved by the creditors’ committee.

4. **Publicity:**

Since 2000, the court’s bankruptcy judgement must be published on the Internet.

In general, the bankrupt’s name is not mentioned in a specific register but only on the
Internet, except for companies registered in the Commercial Register, for which the
opening of bankruptcy proceedings will be published in this Register.

5. **End of the procedure:**

The procedure ends:
- When all assets of the bankrupt have been distributed;
- Or when it appears that that the assets are not sufficient to cover the costs of the
proceedings;
- Or with the consent of all creditors;
- Or when the bankruptcy proceedings are converted into “compulsory reorganisation” proceedings (see Title 4), after the reorganisation plan has been accepted by the creditors and confirmed by the court.

B. Belgium

In Belgium, bankruptcy (“faillite” or “faillissement”) is governed by the Belgian law of August 8, 1997 on bankruptcy.

1. Initiation of the proceedings

Bankruptcy proceedings apply to traders (individuals or companies) only.

They are initiated by the debtor (who is obliged to do so within one month of the cessation of his payments), a creditor or the Public Prosecutor.

2. Criteria for the petition:

The law requires that the debtor:
- has ceased its payments, and
- has lost its creditworthiness.

3. Effects:

The main effects of the bankruptcy order are:
- a receiver in bankruptcy (“Curateur/Curator”) is appointed to recover and realise the debtor’s assets, and to distribute the net proceeds to the creditors;
- creditors must declare their claim within a specific period of time;
- the debtor is automatically divested from the control of its assets;
- all claims against the bankrupt become due;
- a stay of legal proceedings and execution measures against the debtor or his property.

4. Publicity:

The court’s bankruptcy order must be published in the Official Belgian Gazette and in two newspapers.

A file relating to the bankrupt will be kept at the clerk of the commercial court and any interested party may consult it for free.

5. End of the procedure:

The procedure ends when all assets are distributed and the company’s liquidation is achieved or if the assets are not sufficient.

C. Denmark

Under Danish law, bankruptcy (“Konkurs”) is governed by the Danish Bankruptcy Act of June 8, 1977 (consolidated in September 1986).
An insolvent debtor’s property is liquidated and its proceeds are distributed among its creditors following the bankruptcy/winding-up procedure (“konkurs”) or the Liquidation Composition procedure (“likvidationsakkord”). The difference between these procedures is that, in case of liquidation composition as opposed to bankruptcy/winding-up, the trader is discharged for his remaining debts.

Liquidation composition may be carried out voluntarily by agreement or as a compulsory composition (see Title 4 for the description of this procedure). In this section we will only address the bankruptcy/winding up proceedings.

1. Initiation of the proceedings:

Bankruptcy/winding-up proceedings, which apply to both natural and legal entities (company), are initiated either by the debtor or his creditors.

2. Criteria for the petition:

In order to apply for bankruptcy/winding-up, a company must be insolvent. Under Danish law, insolvency is defined as a state of “illiquidity”, i.e. the debtor is not able to meet his financial obligations as they fall due.

3. Effects:

The purpose of this procedure is to ensure that the creditors receive an equal treatment in the distribution of their debtor’s assets, with priority to secured or preferential creditors.

After a bankruptcy/winding-up order is issued by the court, trustees/liquidators will be appointed who will take over the business management and realise its assets.

There is a stay of all legal proceedings and executions of enforcement against the bankrupt’s property: creditors may no longer levy execution or attachment, they must wait for the assets’ distribution by the liquidator.

4. Publicity:

Publicity is generated by the bankruptcy proceedings.

5. End of the procedure:

The procedure ends when all assets are distributed among the creditors and, if the debtor is a company, when it is dissolved.

D. FINLAND

In Finland, bankruptcy (“konkurssi”) is governed by the Finish Bankruptcy Act of 1968, the Act on the Recovery of the Bankruptcy Estate of 1991, the Act on the Priority of Claims of 1992 and the Act on the Supervision of the Administration of Bankruptcy Estates of 1995. A proposal for a government bill has recently been
approved which will result in a new Bankruptcy Act that clarifies the existing legislation. It is expected to become law in 2003.

1. **Initiation of the proceedings:**

Bankruptcy applies both to individuals and companies. It is initiated by the debtor (voluntary) or a creditor (involuntary).

2. **Criteria for the petition:**

A particularity of the Finish system is that a debtor may voluntarily file for bankruptcy, *without regard* to any preconditions of its financial status.

However, in case of involuntary bankruptcy, creditors must prove one of the six conditions set out in the Bankruptcy Act (e.g. an unsuccessful attempt of execution, negligence to satisfy creditors eight days after receiving a certified request for payment from a bailiff, etc…).

After proceedings are initiated voluntarily, a provisional administrator is appointed, for the purpose of submitting an inventory of the debtor’s estate in order to check if it is sufficient to merit full bankruptcy proceedings.

3. **Effects:**

Various actors intervene in the procedure:

- a *provisional administrator* (see above) who will be replaced, when bankruptcy is accepted, by:

  - a *trustee*: his role is to take care of the procedure of acceptance of creditors’ claims and to act as executor after the expiration of the time limit for the proof of claims.

- The *creditors’ meeting* plays an important role in the bankruptcy estate’s administration, while the administrator and trustee must comply with all of its major decisions.

- A bankruptcy *ombudsman* supervises all actions of the administrator and trustee. It is an independent and impartial authority, who may not prejudice the rights of the debtor nor the creditors.

Other effects are:

- Execution of the debtor’ assets are suspended;
- Interest on a debtor’s debt continues to accrue, unlike in other countries;
- The debtor loses all control over its property and assets. This authority is taken over by the body of creditors;
- After the creditors’ claims have been lodged and accepted, the assets will be distributed among the creditors. Secured creditors will receive payment prior to the other creditors. Claims secured by a floating charge (security not attached to a particular asset but to a category of assets that may be modified through the evolution of the business. In the case of bankruptcy, the “floating charge” becomes a “fixed charge”) also enjoy a priority of payment.
4. **Publicity:**

Bankruptcy judgements are made public in newspapers. There is no specific bankruptcy register.

5. **End of the procedure:**

The procedure ends when all assets have been distributed and the company is liquidated.

**E. FRANCE**

French bankruptcy ("faillite") is governed by the Law of January 25, 1985 on restructuring and judicial liquidation of companies, as modified by the law of June 10, 1994.

The French bankruptcy is not favorable to creditors, for its main priority is to save the company and not only to settle its debts.

Judicial liquidation (or "liquidation judiciaire") of a company may however be ordered by the court either:
- after an observation period (that lasts from 4 to 20 months) during which the company may continue its business, and at the end of which the judge must decide between a reorganisation or a liquidation procedure; or
- immediately, when the business has ceased all activities or when its restructuring is clearly impossible.

1. **Initiation of the proceedings:**

Bankruptcy proceedings are open for both:
- companies (practising commercial activities or not);
- individuals (merchants, registered craftsmen and farmers).

Proceedings may be initiated by:
- the debtor itself (it is obliged to declare its default of payment within 15 days of cessation of payments);
- a creditor, regardless of the amount of its claim;
- the Public Prosecutor (seldom);
- the Court.

2. **Criteria for the petition:**

A Bankruptcy order can be made by the court, on the following grounds:
- default of payment, i.e. when the debtor’s available capital (defined as the assets that can be liquidated within a few days) does not meet its debt obligations (debts due and payable);
- breach of the terms of the amicable settlement or of the continuation plan (see Title 4);
- penalties against managerial misconduct (i.e. bankruptcy opened against the
director of a company if he was found liable for the company’s debts and did not
pay them, or if he misappropriated corporate funds, signed interested
transactions...).

3. **Effects:**

The Bankruptcy order governing the company’s liquidation has the following main
effects:
- a liquidator is appointed for the purpose of selling the business’ assets and
  dividing them among the creditors;
- an ‘insolvency judge’ is appointed, in order to supervise the liquidation and to
  ensure the protection of the interests of all parties;
- in case an observation period precedes the liquidation, it has the following effects
  upon the creditors:
  a) all court proceedings involving debts that arose prior to the commencement of
     the bankruptcy proceedings are suspended, as well as the enforcement of any
     judgement;
  b) the debtor is prohibited from paying any debt that arose prior to the
     commencement of the bankruptcy proceedings;
  c) interest accrual on prior debts is suspended;
  d) any acceleration of payment of outstanding debt is prohibited.
- Creditors are paid following specific rules (e.g. waged workers first, then legal
  expenses, creditors with pledges or mortgages...).

4. **Publicity:**

The judgement initiating the liquidation procedure must be published in the
Commercial Registry for companies and entrepreneurs, in the Professions Registry for
craftsmen and in a newspaper.

5. **End of the procedure:**

The liquidation procedure ends either when all the company’s debts are settled, or
when its assets are insufficient to settle all of its debts (which is mostly the case).

**F. GERMANY**

German insolvency proceedings (“insolvenzverfahren”) are governed by the German

They do not regulate only a bankrupt’s compulsory winding-up. These proceedings
may also lead to reorganisation measures.

They apply to companies or individuals (“customer insolvency procedures”).

For the purposes of this report, we will consider these proceedings as far as they
govern compulsory winding-up of companies.
1. **Initiation of the proceedings:**

“Insolvenzverfahren” procedure can be initiated by:
- the debtor himself
- a creditor;
- against any individual or company (except the Federal or State government or any company subject to the latter’s supervision).²

2. **Criteria for the petition:**

The criteria for commencement are quite flexible and include the following:
- A debtor’s inability (or imminent inability) to pay its debts as they fall due. Even an inability to balance minor outstanding payments can justify the commencement of insolvency proceedings, or
- bankrupt’s liabilities exceeding its assets (excessive indebtedness).

3. **Effects:**

A petition for “insolvenzverfahren” has the following effects:

**a) Preliminary measures:** in order to secure the bankrupt’s property, the court will appoint a preliminary trustee who will run the bankrupt’s business until the opening of insolvency proceedings.

**b) Insolvency proceedings:** if the court agrees to open insolvency proceedings:
- A final trustee in insolvency is appointed to manage the company. He will dispose of the debtor’s assets instead of the bankrupt, unless the court orders self-management (i.e. the bankrupt continues to manage its business under supervision of the trustee);
- Creditors register their claim, within a specified period of time;
- The trustee collects the bankrupt’s claims and realises the assets. In this regard, like in most countries, he is required to respect certain rules, notably:
  a) the assets of creditors with a right of ownership against the bankrupt (owners with a retention title, landlord, lessor…) will be segregated out of the insolvency’s estate.
  b) Other creditors (having security on movable or immovable property) will have a privileged claim against the insolvent estate at its realisation.

4. **Publicity:**

The court resolution over the initiation of the insolvency proceedings is made public by the office of the insolvency court in the German Federal Gazette (“Bundesanzeiger”).

The public announcement takes the form of an entry in the publication for official notices of the court. The insolvency court can arrange further and repeated

² They however do not apply against individuals who are not self-employed or have been self-employed, to whom a simplified insolvency procedure applies.
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

publications. In particular, the court resolution should serve the interests of the creditors and debtors of the company.

Furthermore the initiation of insolvency proceedings must be recorded in the land register ("Grundbuch").

5. End of the procedure:

The procedure will end:
- when all assets have been realised and distributed among the creditors;
- after the preliminary measures are taken, investors may show interest in the insolvent company.

G. GREECE

In Greece, bankruptcy is governed by Articles 525 to 596 of the Greek Commercial Code and Act of 12 December 1878, amended by the Law of 22 February 1910 and the N.L. 635 of 1937.

1. Initiation of the proceedings:

Bankruptcy proceedings apply only to traders, whether individuals or companies.

They can be initiated by the debtor (who is obliged to do so by the law), a creditors or the court (exceptionally).

2.Criteria for the petition:

Cessation of payments is a pre-condition for bankruptcy. It refers to the permanent inability for the debtor to pay its due and entitled debts. It does not depend on the financial situation of the debtor but on the non-payment of his debts.

3.Effects:

The main effects of a bankruptcy judgement can be summarised as follows:

- a ‘Judge Rapporteur’ is appointed for the purposes of verifying the creditors’ claims and calling the general meeting of shareholders, that will protect the creditors’ interests during the proceedings;
- an Administrator is appointed for the purpose of representing, assisting and monitoring the debtor during the bankruptcy procedure, and to draw up a list of assets and liabilities in order to be distributed to the creditors;
- all proceedings based on ordinary claims are suspended (not claims secured by pledge, mortgage or lien);
- as regards the distribution of assets, secured creditors will be satisfied by preference and may only participate in the creditors’ meetings for the unsatisfied portion of their claims. The creditors’ meeting will attempt to reach a settlement with the debtor by means of a contract, on how to distribute the assets.

4.Publicity:

4.3. Legal consequences of bankruptcy and possibilities for a fresh start
The declaration of bankruptcy must be published in the Lawyers’ Pension Fund Bulletin and the bankrupt’s name should be mentioned in a special registry.

5. End of the procedure:

The procedure is terminated when the bankrupt’s estate is liquidated, when the court decides to end it for lack of assets, or if a judicial composition is reached.

H. IRELAND

In Ireland, “compulsory liquidation” is governed by the Irish Companies (Consolidation) Act of 1908, the Companies Act of 1913, the Companies Act of 1963, the Companies Act of 1990 and the Company Law Enforcement Act of 2001.

1. Initiation of the proceedings:

The liquidation of an Irish company may result from a compulsory liquidation, ordered by the court, following the petition of the company itself, any creditor or the Director of Corporate Enforcement (an independent, state-funded agency, responsible for the enforcement of the Companies Act).

2. Criteria for the petition:

A petition for ‘compulsory liquidation’ may be initiated when a company is unable to pay its debts (e.g. when a creditor has obtained a judgement for debts but has been unsuccessful in attempting to execute it).

3. Effects:

The court will appoint a liquidator who will take over the management, wind up the company’s business, realise and distribute its assets (with a priority to preferential creditors or creditors whose claims are secured by a floating charge).

Once the company is declared to be liquidated there is a stay of all legal proceedings and executions of enforcement against the bankrupt’s property.

4. Publicity:

The application for liquidation proceedings must be published in local newspapers.

5. End of the procedure:

The procedure ends when the assets of the company have been completely wound up and the company is dissolved.

I. ITALY

In Italy, bankruptcy is governed by the Italian Royal Decree n° 267 of March 16, 1942 (also referred to as the Bankruptcy Act).
As the aim of the Italian legislator was clearly to protect the interest of creditors and to eliminate insolvent companies from the market by liquidating them, Italy has developed several insolvency procedures, whereas the restructuring of companies has not captured much of its attention.

The three major insolvency procedures in Italy will briefly be described, i.e. the liquidation bankruptcy (“fallimento”), the compulsory administrative liquidation (“liquidazione coatta amministrativa”) and the extraordinary administration (“amministrazione straordinaria”). These procedures are often linked, as one procedure may lead to another.

I.1. Liquidation Bankruptcy

1. Initiation of the proceedings:

This procedure may only be initiated by private entrepreneurs with a substantial business organisation in terms of capital, work force and equipment. It excludes companies, public entities, agricultural entrepreneurs and small individual entrepreneurs from the application of liquidation bankruptcy.

It can be initiated by:
- the debtor
- a creditor
- the Public Prosecutor
- the Court.

2. Criteria for the petition:

In order to apply for this procedure, the private entrepreneur must be in a state of “functional impotence”, i.e. it is impossible to meet its financial obligations regularly and through normal business practices, due to a lack of liquidity and credit.

3. Effects:

As soon as the Court renders a judgement adjudicating the debtor bankrupt:
- a ‘bankruptcy trustee’ is appointed to realise the bankrupt’s property and to distribute it among the creditors;
- a ‘delegated judge’ is appointed to supervise the procedure;
- the creditors must lodge their claim;
- no execution measure may be taken against the bankrupt;
- Preferred and secured creditors (e.g. claims for the trustee’s fees, costs of judicial proceedings, employees’ wages…) will be paid prior to unsecured creditors.

4. Publicity:

The adjudication in “fallimento” is published in the Public Record kept by the court and the proceedings are published in the Register kept by the Chamber of Commerce accessible on line.
5. **End of the procedure:**

This procedure may lead to a creditors’ settlement\(^3\) and the bankrupt will then recover the possession and management of its assets.

Or, if such settlement could not be reached, the bankrupt’s business will be wound-up.

### 1.2. Compulsory administration liquidation

1. **Initiation of the proceedings:**

This is an administrative procedure that only applies to certain categories of companies owned partially by the State or subject to the control of administrative authorities (e.g. banks, insurance companies...).

It is initiated by the company itself.

2. **Criteria for the petition:**

The company has a discretionary power to decide whether it needs to be removed from the market, not only in case of financial distress, but also for any problems that may jeopardise its ability to carry on business. In order to protect the rights of creditors and third parties, the Court may however check the insolvent status of the company.

3. **Effects:**

When the company has declared that it wishes to initiate this procedure (and unless the court rejects such action):

- a ‘*liquidating commissioner*’ (an administrative entity) is entrusted with the power to evaluate and liquidate the assets, and to distribute them amongst the creditors;
- this commissioner is appointed and controlled by a public administrative body with the same powers and functions as the bankruptcy court.
- the creditors will be reimbursed (secured and favoured creditors first) and they may appeal to the court against the distribution of the assets.

4. **Publicity:**

The proceedings are carried out under the control of the Industry and Trade Ministry, whose decisions and orders are rendered by a Decree which is duly published in the *Gazetta Ufficiale della Republica*.

The proceedings are also published in the Register kept by the Chamber of Commerce, which is accessible on line.

5. **End of the procedure:**

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\(^3\) See above, Title 4. In such case, the bankrupt must have offered full payment of secured creditors and a pro-rata payment to unsecured creditors. A majority of creditors and the court must also have approved the bankrupts’ offer.

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4.3. Legal consequences of bankruptcy and possibilities for a fresh start
Again, this procedure may result in a settlement by the creditors, or in a liquidation of the company.

I.3. Extraordinary administration

This procedure aims not only at satisfying creditors’ rights but also at reducing the negative effects of bankruptcy on a company’s work force, by trying to find an alternative solution to bankruptcy.

1. Initiation of the proceedings:

The extraordinary administration applies only to major companies (of at least 200 employees).

It can be triggered by:
- the debtor
- a creditor
- the Public Prosecutor
- the court.

2. Criteria for the petition:

In order for the court to accept the application for this procedure, the liabilities of the failing business must amount to at least one third of the total of its assets and its sales and services profits of the last financial year.

3. Effects:

The procedure starts with an observation period (of max. 2 months), during which a ‘judicial commissioner’ may be appointed to manage the company, under the supervision of the court; or the entrepreneur may keep its management power.

After this observation period, if it appears that no reorganisation procedure is possible, the procedure is converted into a liquidation bankruptcy procedure (see point I.1)

4. Publicity:

We refer to the compulsory administrative procedure. (point I.II)

5. End of the procedure:

See the liquidation bankruptcy procedure (point I.I).

J. LUXEMBOURG

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4.3. Legal consequences of bankruptcy and possibilities for a fresh start
In Luxembourg, bankruptcy ("faillite") is governed by articles 437 to 592 of the Luxembourg Commercial Code.

1. **Initiation of the proceedings:**

Bankruptcy only applies to traders (whether companies or individuals).

It may be initiated by creditors, the court or the debtor himself (who is obliged to do so within one month from the cessation of payments).

2. **Criteria for the petition:**

Both of the following conditions must be met in order for bankruptcy to be ordered by the court:
- suspension of payments (the debtor can no longer pay his liquid and due debts ‘illiquidity’);
- Loss of credit worthiness (the debtor’s business is not trustworthy anymore).

3. **Effects:**

As soon as the court orders bankruptcy:
- he will appoint a judge to supervise the bankruptcy proceedings as well as a trustee who will take over the management of the business and who will draw up a state of the bankrupt’s assets;
- creditors must lodge and prove their claims;
- no individual action or execution may be taken against the debtor;
- interests on claims that are not secured stop accruing;
- the assets are distributed among the creditors in accordance with the distribution plan voted by them and signed by the court.

4. **Publicity:**

The bankruptcy judgement must be published in newspapers and displayed in the hearing rooms of the commercial court for a period of three months.
The public may also consult the company’s file at the commercial court.

5. **End of the procedure:**

The procedure is brought to an end when all assets are distributed and the company is liquidated.

It may also be closed if the assets are not sufficient to cover the administration and liquidation costs of the bankruptcy or if a composition after bankruptcy is reached.

**K. THE NETHERLANDS**

In the Netherlands, bankruptcy (or “faillissement”) is governed by the Dutch Bankruptcy Act of September 1, 1896 and its numerous amendments.
The Dutch legislation provides for three different legal procedures in relation to insolvency. The suspension of payment was discussed above (see Title 4), whereas the debt restructuring involves private individuals only and will not be further considered in this report. We will briefly describe the bankruptcy procedure that applies to companies and individuals.

1. **Initiation of the proceedings:**

The proceedings can be initiated both against individuals and companies, by:
- the debtor himself;
- creditors (case law has established that there should be more than one creditor);
- the Public Prosecutor, in case the public interest is involved.

2. **Criteria for the petition:**

A declaration for bankruptcy requires the existence of facts and circumstances evidencing:
- that the debtor has ceased to pay, and
- that the debtor has several creditors.

3. **Effects:**

The opening of bankruptcy proceedings has the following effects:
- the court appoints a ‘trustee’ charged with the administration and liquidation of the bankruptcy estate. The bankrupt loses all free disposal and administration of its property;
- the court also appoints a ‘bankruptcy judge’ to supervises the administration and liquidation;
- creditors lodge their claim;
- secured creditors (mortgagees and pledges) may exercise their security rights as if bankruptcy had not taken place. If they wish to sell the secured goods, they must however do so through a public sale (which is likely to generate less proceeds than a private sale), or through a private sale but with the co-operation of the trustee;
- however, secured creditors (as well as third parties) are not allowed to exercise their rights if a “cooling down period” (i.e. period of up to one month (with a possible extension to two months) is ordered by the bankruptcy judge, during which claims of third parties or secured creditors against assets belonging to the bankruptcy estate may only be executed with the trustee’s authorisation);

4. **Publicity:**

The publicity surrounding insolvency proceedings consists of:
- the publication of the declaration of insolvency and the termination of the insolvency proceedings;
- the public register held by the court;
- notification with the Trade Registry.

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5 See the Dutch report, p. 32-34.

4.3. Legal consequences of bankruptcy and possibilities for a fresh start
5. **End of the procedure:**

The bankruptcy ends by:
- closing due to lack of assets;
- closing if the bankrupt is in a position to resume payment of its debts;
- a scheme of arrangement with the creditors.

**L. PORTUGAL**

In Portugal, bankruptcy ("insolvência") is governed by the Bankruptcies Code of 1935 and the Decree-law of January 3, 1990

1. **Initiation of the proceedings:**

Bankruptcies apply only to “debtors holding an entrepreneurial organisation” (individuals or companies).

They are initiated by the debtor, a creditor, the Department of Public Prosecution or the court (if an opposition to the recovery procedure is lodged by creditors representing at least 51% of the recognised outstanding debts).

2. **Criteria for the petition:**

The company must be unable to meet its financial obligations in time because its available assets are insufficient to satisfy its current liabilities.

3. **Effects:**

Once bankruptcy has been ordered by the court:
- a ‘judicial liquidator’, in charge of the recovery and sale of the debtor’s assets, is appointed;
- ‘creditors’ committees’ are appointed to supervise the liquidator;
- suspension of execution measures;

4. **Publicity:**

Bankruptcy judgements are published.

5. **End of the procedure:**

The procedure ends when the company is liquidated (after all assets have been distributed) or where the creditors have agreed a recovery plan.

**M. SPAIN**

In Spain, bankruptcy (or “quiebra”) is governed by various legislation: the Spanish Commercial Code of 1885, the Civil Procedural Rules of 1881 and articles 1001 to 1177 of the former Commercial Code of 1829, which remains in force for the specific provisions on bankruptcy.
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

4.3. Legal consequences of bankruptcy and possibilities for a fresh start

1. Initiation of the proceedings:

Bankruptcy proceedings apply to traders (whether individuals or companies).

They can be initiated by:
- the debtor himself ((following a legal obligation, when he is facing a situation of stay of payment of his debts);
- any legitimate creditor.

2. Criteria for the petition:

The business must be in a situation of “generalised stay of payments”, which is a broad concept defined case-by-case by the court, that corresponds to an economic imbalance whereby the business’ liabilities exceed its assets.

Examples of facts that have led to the opening of bankruptcy proceedings are:
- unsuccessful seizure of assets by a creditor;
- suspension of a payment if this suspension indicates that the business is insolvent;
- non-compliance by the business of a convention reached with its creditors, within the procedure of suspension of payments.

3. Effects:

The main effect of a bankruptcy order are:

- the appointment of several ‘mandatories’ (more than in foreign bankruptcy procedures):
  a) a ‘Depository’: responsible for the recovery of the bankrupt’s assets and for the management of its business until Receivers are appointed;
  b) a Creditors’ Meeting: that will vote on any proposal submitted by the debtor and approve the classification and ranking of debts. Receivers are appointed at this meeting;
  c) Receivers: creditors that represent the main body of creditors, manage and liquidate the bankruptcy estate. Unlike most bankruptcy procedures, the debtor’s assets are therefore managed by the creditors themselves;
  d) a ‘Commissioner’: delegate of the court who supervises the function of the Receivers;
- the creditors must declare their claim within a specific period of time;
- the assets are, after being recovered by the Depository, distributed among the creditors, following the ranking approved by the Creditors’ Meeting;
- secured creditors may however enforce their security separately.

4. Publicity:

The declaration of bankruptcy must be published in the Official Gazette and in certain newspapers, and registered in the Civil, Commercial and Property Registry.

5. End of the procedure:

The procedure is brought to an end when:

4.3. Legal consequences of bankruptcy and possibilities for a fresh start 256
- all assets are distributed and the company is liquidated;
- the application for bankruptcy is dismissed for lack of assets or absence of creditors;
- a composition agreement is reached between the debtor and its creditors, within the bankruptcy procedure.

N. SWEDEN

In Sweden, bankruptcy ("konkurs") is governed by the Bankruptcy Act of 1987 and the Preferential Rights of Creditors Act (1979).

1. Initiation of the proceedings:

The Swedish *konkurs* applies to companies and individuals, traders or non traders.

It can be initiated either by the debtor or its creditors. When the debtor petitions for bankruptcy, it will be declared bankrupt the same day, whereas if the procedure is initiated by creditors, the company will be considered bankrupt only when the court declares it.

2. Criteria for the petition:

The debtor must be unable to pay its debts as they fall due and such inability must not be merely temporary.

3. Effects:

The court will appoint a receiver who will recover and realise the company’s assets, and distribute the proceeds among to the creditors. He will also take over the company’s management.

A dividend is distributed to preferential and secured creditors first. A particularity is that non-preferred creditors are not required to automatically declare and prove their claim. The receiver will ask them to lodge a proof of their claim only if it appears that they will receive a dividend after the preferential and secured creditors have been paid (this seldom occurs).

4. Publicity:

The declaration of bankruptcy is announced in the Swedish Official Gazette (the *Post- och Inrikes Tidningar*).

The bankruptcy is also recorded in an official register where all Swedish bankruptcies are gathered. The Patent and Registration office keeps this Register and the information is public and is open to inquiries by members of the general public.

5. End of the procedure:

The procedure is brought to an end when the receiver submits his final report and his dividend proposal to the court.
O.  UNITED KINGDOM

In the United Kingdom, the Insolvency Act 1986 and the Insolvency Rules 1986, amended by the Insolvency Bill 2000, govern insolvent companies’ proceedings.

The term “bankruptcy” refers to the procedure applied only to individuals unable to pay their debts, and not to companies. It will not be discussed in this report.

In order to bring the existence of a company to an end and to distribute its assets, a compulsory or voluntary (not discussed here) liquidation may take place, sometimes through the mechanism of receivership.

0.1. Compulsory liquidation

1. Initiation of the proceedings:

Compulsory liquidation is initiated by the failing company itself, any creditor, a shareholder of the company and, in very limited circumstances, by the Department of Trade and Industry.

2. Criteria for the petition:

A petition for compulsory liquidation may be presented to the court on a number of grounds, usually on the ground that a company is unable to pay its debts (e.g. if it has neglected a demand of payment for more than £750 or if it is proved that the value of the company’s assets is less the amount of its liabilities).

3. Effects:

When a winding-up order is made, the official receiver of the court becomes the liquidator of the company until meetings of creditors decide to appoint someone else. The directors’ powers will cease as from that moment.

No action can be started unless the leave of the court is obtained and any execution started after the commencement of a compulsory liquidation is void.

The liquidator will apply the proceeds of the realised assets and pay creditors, who are required to submit their claims (by sending particulars of it to the liquidator by way of a proof of debt) in the following order:

(a) creditors secured by a fixed charge or mortgage, out of the proceeds of the asset subject to the fixed charge or mortgage;
(b) the liquidator's costs and remuneration;
(c) preferential creditors (e.g. Inland Revenue, the Department of Social Security, occupational pension schemes and employees who are owed remuneration up to a set amount);
(d) creditors secured by a floating charge, out of the proceeds of the assets subject to the floating charge;
(e) unsecured creditors; and
(f) any claims arising from post-liquidation interest.

4. **End of the procedure:**

The procedure ends when all assets are liquidated and the company’s existence is brought to an end.

5. **Publicity:**

Once a winding up order has been made by the court, the official receiver (who is the liquidator until another liquidator is appointed) will file a copy of the order with the Registrar of Companies, ensure that the order is published in the government gazette and will advertise the order in a newspaper of his choice.

6. **Receivership:**

This procedure, discussed above in section 4.2, by which a creditor may appoint a receiver in order to realise his security, may also lead to a company’s liquidation.

**P. UNITED STATES**

U.S. companies can be either liquidated under Chapter 7 (usually smaller companies) or under Chapter 11 (typically large companies) of the Bankruptcy Code of 1978.

**P.1. Chapter 7 Liquidation**

1. **Initiation of the proceedings:**

The liquidation procedure under Chapter 7 applies to individuals, partnerships and corporations, excluding railroads, domestic or foreign insurance companies or banks.

The debtor can initiate the procedure (voluntary case) or by three or more of its creditors (holders of a claim against the debtor that is not a contingent liability or subject to a bona fide dispute) where the company has more than 12 creditors or a trustee representing such creditors. After a creditor group has filed a petition for a Chapter 7 case, the debtor has the right to oppose the petition in court, to either change it to a Chapter 11 case or dismiss the case.

2. **Criteria for the petition:**

The basis for filing a petition under Chapter 7 is similar to the filing of a petition under Chapter 11 and has been discussed under title 4.2.

3. **Effects:**

Under Chapter 7, the company stops all operations and goes completely out of business. A trustee is appointed to pursue any estate claim, liquidate the debtor’s assets, and distribute it to the creditors in order of priority; secured creditors first, then holders of administrative expense claims, holders of priority claims, employee claims, tax obligations, etc. and lastly holders of unsecured claims. A creditors committee
could be appointed, representing the unsecured creditor group, if the creditor group so decides.

4. **Publicity:**

The publicity generated from a bankruptcy filing is dependant on the size of the company and not on the type of chapter filing. Therefore, since most companies filing under Chapter 7 are smaller companies, the publicity generated is not as much as when a large company files under Chapter 11. Pleadings are filed with the Bankruptcy court and maintained by the clerk of the court in a docket that may be viewed by the public.

5. **End of the procedure:**

The procedure ends when all assets have been liquidated and distributed.

**P.2. Chapter 11**

A company can also liquidate its business under Chapter 11. During a liquidating Chapter 11 case, the debtor in possession attempts to sell or dispose of all or substantially all the assets of the debtor's estate, ordinarily as a going concern. The plan of reorganisation provides for the liquidation of any remaining assets and for the distribution of the proceeds of the liquidation.

Refer to Title 4.2 of the report regarding proceedings under Chapter 11 and the effects.

**P.3. Choice between Chapter 7 and Chapter 11**

A debtor may prefer liquidation in a chapter 11 case over liquidation in a chapter 7 case because (unless a chapter 11 trustee is appointed), the debtor will remain in control of its business and property may continue to operate while the liquidation is conducted. This may make it more likely to obtain going concern values rather than liquidation values.

Creditors may agree to a chapter 11 liquidation in order to avoid chapter 7 expenses, because they believe the debtor will be able to maximise the value of the its property better than a trustee unfamiliar with the debtor's business and property, or because the creditors committee plays a more important role in chapter 11 and tends to surrender its powers to a chapter 7 trustee.

**4.3.2.2. COMPARATIVE ANALYSIS**

The common aim of most countries’ bankruptcy procedures is to liquidate insolvent businesses. A comparison of the various bankruptcy procedures and its direct effect is discussed under the following sections:

A. Objective of the procedure:
B. Nature of the procedure
C. Quality of the debtor
D. Potential triggers for bankruptcy procedures
E. Possible initiators
F. Main effects of bankruptcy
G. Key players involved in the procedure
H. Creditors’ role and distribution of the assets
I. End of the procedure.

A. Objective of the procedures:

Traditionally, the objective of bankruptcy procedures was to sanction failing businesses that betrayed its creditors’ trust. The civil and criminal sanctions resulting from this betrayal, will be discussed in the next chapter (Chapter 4.3.3).

Three major trends have been observed:

- bankruptcy should only achieve one goal: maximum reimbursement of the debtor’s creditors;
- the desire to liquidate failing businesses as soon as possible, to ensure a stable market;
- it is more advantages to the stakeholders of the company (i.e. creditors and employees) that a failing business be saved and reorganised, rather than be liquidated. This help people realise that failing companies are not always liquidated and the stigma of bankruptcy could therefore be reduced.

These trends do not only result from policies followed by national governments, but also from historical considerations and from the date of the national legislation (bankruptcies in Austria, Greece, Italy and Spain are still based on rather old legal sources). Traditional legislation tends to punish failing businesses, whereas recent developments promote restructuring.

The majority of the countries analysed favour the first two trends (i.e. reimbursement of creditors and efficient liquidation of failing businesses).

In other countries, however, (such as France and Germany), the initiation of bankruptcy procedures begins with an observation period in order to determine the business’ best outcome: a traditional (liquidation) procedure or a restructuring procedure. Such perspective seems a good way to reduce the stigma on bankruptcy. That is, the announcement that a company has entered into bankruptcy proceedings should not be perceived that the company is to be liquidated, but rather that there is a chance of reorganisation. However, it is not clear whether the French and German citizens are aware of this aspect, or if to them, any bankruptcy procedure is assimilated as the end of a company. In line with countries such as France and Germany, the U.S. Bankruptcy code specifically makes a distinction between a reorganisation bankruptcy (Chapter 11) and a liquidation bankruptcy (Chapter 7). This distinguishes between a company that still has a chance to reorganise versus a company that is going out of business.

In other countries, (such as Austria, Italy, and the Netherlands) a creditors’ settlement or scheme of arrangement may be reached at the end of the procedure in which case the company will not be liquidated.
4.3. Legal consequences of bankruptcy and possibilities for a fresh start

**B. Nature of the procedure:**

A similarity between the various procedures results from the desire, in every country, to dispose of a regulated, formal and controlled procedure.

All procedures are of a judicial nature (except for Italy which also provides for an administrative procedure, that applies to State-owned companies only, which is controlled by administrative authorities). The courts responsible for bankruptcy proceedings are often specialised courts (such as in Germany, Italy and the U.S.). A special judge may even be appointed for every bankruptcy case. The court’s role varies: sometimes its only task is to provide a general control of the procedure, namely in bankruptcy proceedings where the creditors play an important role in the proceedings (Finland, Spain, Greece, Portugal), whereas in other countries (Germany, France, Italy, United Kingdom and mostly Austria), the court’s decisions strongly influence the outcome of the procedure.

Although it is important to have judiciary control and to allow the judge to decide on some issues, giving creditors the possibility to intervene and to propose a plan may be favorable to a positive outcome for the company. Their intervention and their
concessions could help save the company and therefore reduce the stigma on bankruptcy.

In all Member States and the U.S., a bankruptcy order is made by the court, in which it determines the moment of cessation of payments and appoints the persons (e.g. trustee, administrator, liquidator) responsible for the follow-up of the bankruptcy.

<table>
<thead>
<tr>
<th>JUDICIARY OR ADMINISTRATIVE PROCEDURE</th>
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<tbody>
<tr>
<td>Austria</td>
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<tr>
<td>- Judiciary.</td>
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<td>- Court very powerful.</td>
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<td>Belgium</td>
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<td>- Judiciary.</td>
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<td>Denmark</td>
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<td>- Judiciary.</td>
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<td>Finland</td>
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<tr>
<td>- Judiciary.</td>
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<tr>
<td>France</td>
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<tr>
<td>- Mostly judiciary (two periods: observation period and liquidation or reorganisation procedure)</td>
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<tr>
<td>Germany</td>
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<tr>
<td>- Judiciary (two periods: preliminary measures and liquidation or reorganisation)</td>
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<td>Greece</td>
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<td>- liquidation bankruptcy and extraordinary administration : judiciary compulsory administrative liquidation : administrative</td>
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<td>Luxembourg</td>
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<td>- Judiciary.</td>
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<td>The Netherlands</td>
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<td>USA</td>
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<td>- Judiciary.</td>
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C. Recognised types of debtor

The various country bankruptcy systems/regimes are not consistent with respect to the debtors that may initiate bankruptcy proceedings.

Most countries (Belgium, the Netherlands, Greece, Luxembourg, Portugal, Spain…) provide for a different procedure for traders and non-traders.

Some countries’ procedures apply either to companies or to individuals, whereas other countries’ procedures apply to both (e.g. Belgium, Finland, France, Germany, Greece). However, none of the countries’ bankruptcy proceedings apply to a state or to government institutions.
4.3. Legal consequences of bankruptcy and possibilities for a fresh start

D. Criteria to initiate bankruptcy procedures

A debtors’ poor financial condition is the most common reason for companies going into bankruptcy. However, the bankruptcy procedures can only be initiated if certain criteria have been met. The strictness of the criteria differs significantly from country to country as discussed. The criteria can be generally summarised into the following categories:

- A cessation or suspension of payments, (France, Greece, Spain); or
- Insolvency/Over-indebtedness (Germany, Portugal, Italy); or
- Lost of creditworthiness; or
- Debtor unable to meet its obligations.

Some countries are quite strict and require that two conditions be met (Austria: illiquidity and over-indebtedness, Belgium: cessation of payments and lost of creditworthiness), whereas the criteria is applied more liberally in other countries, e.g. Germany, UK, U.S. and Ireland.
France provides that judicial liquidation may also be initiated as penalty against managerial misconduct (e.g. director found liable for all the debts of the company or for misappropriation of corporate funds).

It seems that the requirement of a strict criteria has a negative consequence, since it prohibits the debtor or its creditors from petitioning for bankruptcy. The debtor’s business will continue, with the possibility that its financial situation might worsen, resulting in diminishing value to creditors. However, petitioning for bankruptcy is an act filled with important consequences (the negative publicity being one of them) and it is therefore essential that the introduction of such procedure be controlled.

**CRITERIA TO INITIATE PROCEDURE**

<table>
<thead>
<tr>
<th>Country</th>
<th>Criteria</th>
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<tbody>
<tr>
<td>Austria</td>
<td>Illiquidity and over-debtessness</td>
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<td>Belgium</td>
<td>Cessation of payments and lost of creditworthiness</td>
</tr>
<tr>
<td>Denmark</td>
<td>Illiquidity (not being able to meet obligations as they fall due)</td>
</tr>
<tr>
<td>Finland</td>
<td>Voluntary: no criteria required</td>
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<tr>
<td></td>
<td>Involuntary: proof of one out of 6 legal conditions</td>
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<tr>
<td>France</td>
<td>Default of payment</td>
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<td>Or breach of amicable settlement</td>
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<tr>
<td></td>
<td>Or penalties against managerial misconduct</td>
</tr>
<tr>
<td>Germany</td>
<td>Flexible: inability to pay any (minor) debt or liabilities exceeding assets</td>
</tr>
<tr>
<td>Greece</td>
<td>Cessation of payments only (financial situation not relevant)</td>
</tr>
<tr>
<td>Ireland</td>
<td>Flexible: debtor unable to pay its debts</td>
</tr>
<tr>
<td>Italy</td>
<td>Liquidation bankruptcy: functional impotence</td>
</tr>
<tr>
<td></td>
<td>Compulsory administrative liquidation: discretionary power of debtor</td>
</tr>
<tr>
<td></td>
<td>Extraordinary administration: liabilities equal to a third of the assets, sales and profits</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>Suspension of payments and exhaustion of commercial debts</td>
</tr>
<tr>
<td>The Netherlands</td>
<td>Cessation of payments and other conditions</td>
</tr>
<tr>
<td>Portugal</td>
<td>Inability to meet obligations on time because assets are insufficient to satisfy liabilities</td>
</tr>
<tr>
<td>Spain</td>
<td>Flexible: generalised stay of payments</td>
</tr>
<tr>
<td>Sweden</td>
<td>Permanent inability to pay debts</td>
</tr>
<tr>
<td>UK</td>
<td>Flexible: inability to pay debts (in general) or other criteria</td>
</tr>
<tr>
<td>USA</td>
<td>Voluntary: no specific criteria</td>
</tr>
<tr>
<td></td>
<td>Involuntary: Flexible - debtor unable to meet its obligation</td>
</tr>
</tbody>
</table>

**E. Possible initiators**

The debtor, its creditor(s), the court or the Public Prosecutor can initiate bankruptcy procedures in most countries. However, in Belgium, Finland, Germany, Spain, U.S. and Sweden, the court alone do not initiate bankruptcy proceedings.
### INITIATORS OF THE PROCEDURE

<table>
<thead>
<tr>
<th>Country</th>
<th>Initiators</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>Debtor, Creditor, Court</td>
</tr>
<tr>
<td>Belgium</td>
<td>Debtor, Creditor, Court, Public Prosecutor</td>
</tr>
<tr>
<td>Denmark</td>
<td>Debtor, Creditor</td>
</tr>
<tr>
<td>Finland</td>
<td>Debtor, Creditor</td>
</tr>
<tr>
<td>France</td>
<td>Debtor, Creditor, Court, Public Prosecutor</td>
</tr>
<tr>
<td>Germany</td>
<td>Debtor, Creditor</td>
</tr>
<tr>
<td>Greece</td>
<td>Debtor, Creditor, Court</td>
</tr>
<tr>
<td>Ireland</td>
<td>Debtor, Creditor, Director of corporate enforcement</td>
</tr>
<tr>
<td>Italy</td>
<td>Debtor, Creditor, Court, Public Prosecutor, <em>liquidation bankruptcy</em>: debtor, creditor, court, Public Prosecutor, <em>compulsory administrative liquidation</em>: debtor only, <em>extraordinary administration</em>: debtor, creditor, court, Public Prosecutor</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>Debtor, Creditor, Court</td>
</tr>
<tr>
<td>The Netherlands</td>
<td>Debtor, Creditor (more than one), Public Prosecutor</td>
</tr>
<tr>
<td>Portugal</td>
<td>Debtor, Creditor, Court, Public Prosecutor</td>
</tr>
<tr>
<td>Spain</td>
<td>Debtor, Creditor</td>
</tr>
<tr>
<td>Sweden</td>
<td>Debtor, Creditor</td>
</tr>
<tr>
<td>UK</td>
<td>Debtor, Creditor, Contributor, Department of Trade and industry</td>
</tr>
<tr>
<td>USA</td>
<td>Debtor, Three or more creditors or their trustee</td>
</tr>
</tbody>
</table>

**F. Main effects of bankruptcy:**

4.3. Legal consequences of bankruptcy and possibilities for a fresh start
As regards the debtor:

In most of the countries’ bankruptcy systems⁶, the debtor looses control over its assets and a special person (trustee, receiver, administrator, or liquidator) assumes control of the estate and assets.

In Finland, where the creditors play an important role, the trustee is required to submit important decisions for the approval by the creditors’ meeting. Similarly in the U.S., since the trustee represents the unsecured creditors, the creditors committee has the right to consult with the trustee, make recommendations and submit questions regarding the liquidation of the debtor’s estate.

<table>
<thead>
<tr>
<th>MANAGEMENT OF THE BUSINESS DURING BANKRUPTCY</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
</tr>
<tr>
<td>Bankruptcy administrator</td>
</tr>
<tr>
<td>Creditors’ committee</td>
</tr>
<tr>
<td>Belgium</td>
</tr>
<tr>
<td>Receiver</td>
</tr>
<tr>
<td>Denmark</td>
</tr>
<tr>
<td>Trustee</td>
</tr>
<tr>
<td>Finland</td>
</tr>
<tr>
<td>Creditors’ meeting</td>
</tr>
<tr>
<td>France</td>
</tr>
<tr>
<td>Trustee (during observation period ) then liquidator</td>
</tr>
<tr>
<td>Germany</td>
</tr>
<tr>
<td>Trustee or debtor (if court allows self-management)</td>
</tr>
<tr>
<td>Greece</td>
</tr>
<tr>
<td>Administrator</td>
</tr>
<tr>
<td>Ireland</td>
</tr>
<tr>
<td>Liquidator</td>
</tr>
<tr>
<td>Italy</td>
</tr>
<tr>
<td>liquidation bankruptcy : bank, trustee</td>
</tr>
<tr>
<td>compulsory administrative liquidation : liquidation commissioner</td>
</tr>
<tr>
<td>extraordinary administration : judicial commissioner</td>
</tr>
<tr>
<td>Luxembourg</td>
</tr>
<tr>
<td>Trustee</td>
</tr>
<tr>
<td>The Netherlands</td>
</tr>
<tr>
<td>Trustee</td>
</tr>
<tr>
<td>Portugal</td>
</tr>
<tr>
<td>Judicial liquidator</td>
</tr>
<tr>
<td>Spain</td>
</tr>
<tr>
<td>Depository then receiver</td>
</tr>
<tr>
<td>Sweden</td>
</tr>
<tr>
<td>Receiver</td>
</tr>
<tr>
<td>UK</td>
</tr>
<tr>
<td>Liquidator</td>
</tr>
<tr>
<td>USA</td>
</tr>
<tr>
<td>Trustee</td>
</tr>
</tbody>
</table>

As regards the creditors:

One of the main goals of bankruptcy procedures is to provide a means to equally distribute the assets among the creditors (depending on priority). Therefore a creditor that seeks execution of its claim before other creditors is not in line with the above

⁶ In Germany the court may order the debtor to self-management his business.
stated objective. In some countries, secured creditors typically receive payment on its claims before other creditors.

This is an automatic effect of all bankruptcy procedures, except for the Netherlands, where execution measures will be suspended only if the court has ordered a “cooling down period”.

In some countries (e.g. Finland), interest on the debtor’s debts continues to accrue, whereas in others (e.g. Belgium or France) such interest is suspended.

Other rules, regarding the compensation between debts-claims, the continuity of contractual commitments etc. vary from country to country.

**G. Key players involved in the procedure**

A number of key players are involved when a company enters into bankruptcy, which includes:

- A trustee (also known as receiver, administrator or liquidator)
- A specialised judge or court (see point B.)
- Creditors Committees
- Other creditor group (e.g. secured or preferential creditors)

In the majority of the countries, these persons are court appointed; however in some countries, like Spain, the creditors have the authority to make these appointments.

The trustee is usually responsible for managing the debtor’s estate, liquidating the assets and the distribution to creditors. Some countries require that this trustee be a lawyer or an accountant.

In order to protect the creditors’ rights, some countries make provision that specific organisations represent the creditors: Austria - presence of a creditors’ assembly and control by the Association for the Protection of Creditors’ Rights; Finland, Greece, Spain, U.S. and Portugal - creditors’ committee. In other countries (e.g. Belgium, Luxembourg, Ireland), the creditors are not protected through such committees.

A particular appointed authority in Finland is the ‘Bankruptcy Ombudsman’, whose specific duty is to control the bankruptcy procedure. It is an independent and impartial authority that does not represent the creditors or the debtor.

| KEY PLAYERS INVOLVED IN THE PROCEDURE |
|-----------------|-------------------------------------------------|
| **Austria**     | Bankruptcy administrator                        |
|                 | Creditors’ committee                            |
|                 | Creditors’ assembly                             |
|                 | Association for the protection of creditors’ rights |
| **Belgium**     | Receiver                                         |
|                 | Court                                            |
### H. Creditors’ role and distribution of the assets

In most countries creditors are usually requested, after the commencement of bankruptcy, to declare their claim within a specific period of time. These claims will then be accepted or partially/totally rejected, following a review by the court, the trustee (France and U.S.), the debtor (Chapter 11 in the U.S.) or the creditors (Italy, Spain, Germany, and the Netherlands).

Generally the proceeds of the estates’ recovered assets (transformed into cash) is distributed to the creditors following a special priority:

- The debts arising after the introduction of the procedure (e.g. the procedural costs) are usually paid before any other debt.
- In most countries, the law determines the order of payment, usually based on a system of prior payment to owners of securities, privileges, floating charges or

<table>
<thead>
<tr>
<th>Country</th>
<th>Role or office</th>
</tr>
</thead>
<tbody>
<tr>
<td>Denmark</td>
<td>Trustee</td>
</tr>
<tr>
<td>Finland</td>
<td>Provisional administrator (becomes trustee)</td>
</tr>
<tr>
<td></td>
<td>Creditors' meetings</td>
</tr>
<tr>
<td></td>
<td>Ombudsman</td>
</tr>
<tr>
<td>France</td>
<td>Liquidator</td>
</tr>
<tr>
<td></td>
<td>Insolvency judge</td>
</tr>
<tr>
<td>Germany</td>
<td>Preliminary trustee (becomes final trustee)</td>
</tr>
<tr>
<td></td>
<td>Court</td>
</tr>
<tr>
<td>Greece</td>
<td>Judge rapporteur</td>
</tr>
<tr>
<td></td>
<td>Administrator</td>
</tr>
<tr>
<td></td>
<td>Creditors’ meeting</td>
</tr>
<tr>
<td>Ireland</td>
<td>Liquidator</td>
</tr>
<tr>
<td></td>
<td>Court</td>
</tr>
<tr>
<td>Italy</td>
<td>Liquidation bankruptcy : bankruptcy trustee, judge</td>
</tr>
<tr>
<td></td>
<td>compulsory administrative liquidation : liquidating commissioner and</td>
</tr>
<tr>
<td></td>
<td>administrative control</td>
</tr>
<tr>
<td></td>
<td>extraordinary administration : judicial commissioner</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>Trustee</td>
</tr>
<tr>
<td></td>
<td>Judge</td>
</tr>
<tr>
<td>The</td>
<td>Bankruptcy judge</td>
</tr>
<tr>
<td>Netherlands</td>
<td>Creditors' committees</td>
</tr>
<tr>
<td>Portugal</td>
<td>Judicial liquidator</td>
</tr>
<tr>
<td></td>
<td>Creditors’ committees</td>
</tr>
<tr>
<td>Spain</td>
<td>Depository</td>
</tr>
<tr>
<td></td>
<td>Creditors’ meeting</td>
</tr>
<tr>
<td></td>
<td>Receivers</td>
</tr>
<tr>
<td></td>
<td>Commissioner</td>
</tr>
<tr>
<td>Sweden</td>
<td>Receiver</td>
</tr>
<tr>
<td>UK</td>
<td>Liquidator</td>
</tr>
<tr>
<td></td>
<td>Creditors’ meeting</td>
</tr>
<tr>
<td></td>
<td>Contributors’ meeting</td>
</tr>
<tr>
<td>USA</td>
<td>Trustee</td>
</tr>
<tr>
<td></td>
<td>Judge</td>
</tr>
<tr>
<td></td>
<td>Creditors Committee</td>
</tr>
</tbody>
</table>

4.3. Legal consequences of bankruptcy and possibilities for a fresh start
rights of ownership; followed by a pro rata payment to the other non-preferential creditors. The latter sometimes receive no payment after the preferred creditors have been paid. The Swedish system provides, in contrary to other countries, that non-preferential creditors are not even required to declare their claim except if it appears that they will receive a dividend. Similar to the Swedish system, in a Chapter 7 liquidation in the U.S., where a company has no unsecured assets, the unsecured creditor also is not required to file a claim.

This inability for unsecured creditors to be paid after secured creditors is an essential point in the stigma surrounding bankruptcy. Who would wish to have contractual relationship with a company, knowing that if this company went bankrupt, all debts which are outstanding would be lost? All creditors would accordingly try to have a security but it is impossible to provide securities to everyone. In other countries (Austria, Greece), the distribution to creditors results from a bankruptcy plan or settlement submitted for the creditors’ approval. However, even in this case, secured creditors have a right to be paid first, the same problem still subsists.

<table>
<thead>
<tr>
<th>Country</th>
<th>Declaration of claim</th>
<th>Distribution Order</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>Declaration of claim</td>
<td>Distribution: following the distribution plan drafted by the bankruptcy administrator and approved by the creditors’ committee</td>
</tr>
<tr>
<td>Belgium</td>
<td>Declaration of claim</td>
<td>Distribution: secured claims prior to others</td>
</tr>
<tr>
<td>Denmark</td>
<td>Declaration of claim</td>
<td>Distribution following a specific order</td>
</tr>
<tr>
<td>Finland</td>
<td>Declaration of claim</td>
<td>Secured claims prior to others</td>
</tr>
<tr>
<td>France</td>
<td>Declaration of claim</td>
<td>Distribution following a specific order (waged workers, then legal expenses, then creditors with pledges or mortgages…)</td>
</tr>
<tr>
<td>Germany</td>
<td>Declaration of claim</td>
<td>Special rules of distribution: right of ownership first, secured creditors and others afterwards</td>
</tr>
<tr>
<td>Greece</td>
<td>Declaration of claim</td>
<td>Distribution: priority to secured creditors and settlement with creditors on distribution</td>
</tr>
<tr>
<td>Ireland</td>
<td>Declaration of claim</td>
<td>Distribution following a specific order (preferential and secured creditors first)</td>
</tr>
<tr>
<td>Italy</td>
<td>Declaration of claim</td>
<td>Distribution: specific order (preferred and secured creditors first)</td>
</tr>
<tr>
<td></td>
<td>liquidation bankruptcy:</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Compulsory administrative liquidation:</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Extraordinary administration:</td>
<td></td>
</tr>
<tr>
<td>Luxembourg</td>
<td>Declaration of claim</td>
<td>Distribution: specific order</td>
</tr>
<tr>
<td></td>
<td>Distribution: specific order</td>
<td></td>
</tr>
</tbody>
</table>

4.3. Legal consequences of bankruptcy and possibilities for a fresh start
I. End of the procedure

The Bankruptcy process is usually concluded after all assets have been liquidated and distributed and administration of the liquidation of the company is completed; or, when a restructuring plan has been successfully adopted; or, as in most countries, when it becomes evident that the assets of the business are insufficient to cover the procedural costs.

4.3.3. FURTHER CONSEQUENCES OF BANKRUPTCY AND CAUSES OF THE STIGMA ON FAILURE AND POSSIBILITIES FOR A FRESH START?

Apart from the liquidation and distribution of the debtor’s assets as a result from bankruptcy procedures, the management of a bankrupt company may also be held civilly or criminally liable. In some cases, special prohibitions will refrain entrepreneurs from starting a new business.

However, in circumstances, described hereunder, that varies in every country, debtors may benefit from “excusability” (i.e. a procedure that will provide for the discharge of payment of their remaining debts and/or the release of certain prohibitions). This excusability will make it easier for the debtor to initiate a “fresh start” of a business.

4.3.3.1. OVERVIEW OF NATIONAL PROCEDURES

Every national system applies specific restrictions to debtors and provide for various conditions in order to grant “excusability”.

The negative consequences resulting from bankruptcy are analysed in light of the following topics:
- liability for remaining debts (bankrupts are not always discharged from unpaid debts. Such debts may sometimes be satisfied with the assets or income that the bankrupt may acquire in the future.)
- criminal offences or

<table>
<thead>
<tr>
<th>The Netherlands</th>
<th>Declaration of claim</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Distribution: secured creditors may exercise their rights as if there were no bankruptcy.</td>
</tr>
<tr>
<td></td>
<td>Suspension of creditors’ execution measures only if “cooling-down” period ordered</td>
</tr>
<tr>
<td>Portugal</td>
<td>Declaration of claim</td>
</tr>
<tr>
<td></td>
<td>Distribution: specific order</td>
</tr>
<tr>
<td>Spain</td>
<td>Declaration of claim</td>
</tr>
<tr>
<td></td>
<td>Secured creditors first and proposal by the debtor on ranking and classification of debts (to be approved by the creditors’ meeting)</td>
</tr>
<tr>
<td>Sweden</td>
<td>No automatic declaration of claim (only if it appears that non-secured creditors will receive something)</td>
</tr>
<tr>
<td></td>
<td>Distribution: secured creditors first</td>
</tr>
<tr>
<td>UK</td>
<td>Declaration of claim</td>
</tr>
<tr>
<td></td>
<td>Distribution: creditors secured by a fixed charge or mortgage first, then liquidator, preferential creditors…</td>
</tr>
<tr>
<td>USA</td>
<td>Declaration of claim</td>
</tr>
<tr>
<td></td>
<td>Distribution: by priority starting at secured creditors and ending with unsecured claims</td>
</tr>
</tbody>
</table>
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

4.3. Legal consequences of bankruptcy and possibilities for a fresh start

The analysis will focus on sole proprietors and the directors of the companies, because the negative consequences have no practical relevance to the legal entities, since it usually is dissolved at the end of the process. The founders or partners of a limited liability company are usually liable only to the amount of capital invested.

A. AUSTRIA

1. Negative consequences of bankruptcy

   a) Director’s liability for the remaining debts

   An important effect of bankruptcy is that creditors may continue to bring individual actions against the directors of a bankrupt company. This is the case, for example, if the directors did not file for judicial insolvency proceedings in due time, where they can be held liable for part/ the total of the company’s debts.

   b) Criminal offences

   Directors may be held criminally liable if they did not respect the essential principle of equal treatment of equal creditors.

   c) Professional interdictions

   Directors may also be prohibited from engaging in an independent trade or business, after a bankruptcy. Exemptions are however applicable (upon proof that they are likely to fill their obligations as regards the intended business and the settlement of previous debts).

   Directors are, however, not excluded from being director of another company.

2. Excusability and possibility for a fresh start

   A discharge from these negative consequences of bankruptcy may be obtained only:
   - if the bankruptcy proceedings are converted into reorganisation proceedings;
   - or in the course of private bankruptcies (that apply to individual non-traders only).

   The Austrian system seems to be quite severe as regards the limitations to excuse bankrupt entrepreneurs. If no reorganisation is possible, they may not be excused. This is quite unfair for “innocent” bankrupts who were lead to bankruptcy by misfortune.

   This could be an important cause of the stigma on bankruptcy: why start a business knowing that if you fail and become bankrupt, your creditors may continue to sue you forever?

   However, this negative effect will concretely not always affect the directors of bankrupt companies, for bankrupt companies are usually liquidated after the proceedings, so there is no company left for the payment of debts preceding
bankruptcy (unless the directors are held civilly or criminally liable for the company’s debts, as mentioned above).

B. BELGIUM

1. Negative consequences of bankruptcy

a) Directors’ liability for the remaining debts

A bankrupt company’s directors responsibility may be invoked, and they can be declared liable for all or part of the company’s debts in several circumstances, such as:
- if they committed a serious fault that led to the bankruptcy,
- if they did not declare bankruptcy on time (or failed to convene a meeting of shareholders to deliberate, when the net assets of the company had fallen down below half of its share capital).

Such responsibility may go far, in situations where the bankrupt company is only a screen, hiding the “real master” of the company (i.e. the person or company owning most of the bankrupt company’s shares and taking important decisions, and whose assets and activities are mixed with those of the bankrupt company). In such cases, the liability may be extended to the “real master” of the business.

If their company’s bankruptcy has caused a damage to a third party, the liability of its directors could be engaged, which may lead to serious financial sanctions.

The founders of a bankrupt company may be held liable for part or all the liabilities of the company, in case its registered capital was manifestly insufficient to ensure its normal activities during at least two years.

b) Criminal offences

Entering into contractual relations without sufficient counterpart, misappropriating or concealing assets, and fraudulently organising an insolvency… are some of the possible criminal offences sanctioned by Belgian law.

c) Professional interdictions

Directors of a bankrupt company may be banned from the exercise of certain professions (such as the profession of auditor) or certain mandates (e.g. the management of an insurance company).

2. Excusability and possibility of a fresh start:
Excusable bankrupts are those that failed because of misfortune or because of certain circumstances in life, and that co-operated during the bankruptcy procedures. Excusability is decided by the court that has a wide margin of interpretation.

If a bankrupt is excused, he will be discharged from his remaining debts. None of his creditors may institute proceedings against him, except for his future debts (that arise after the bankruptcy procedure).

This procedure seems to be a good way to reduce the stigma on bankruptcy and to favour fresh starts, especially since Belgian courts are usually ready to grant excusability to those who “deserve” it, those who failed because of misfortune or because of certain circumstances of life.

C. DENMARK

1. Negative consequences of bankruptcy

   a) Directors’ liability for the remaining debts

   After bankruptcy/winding-up proceedings, creditors regain their right against the bankrupt to the part of the claim that was not paid through distribution, unlike in compulsory composition where the bankrupt is released of all debts not accepted in the composition.

   Directors of a bankrupt company face several civil sanctions:
   - they may be forced to repay up to five years’ of bonuses granted while the company was insolvent;
   - the liquidator may bring an action for damage against them, even if they were discharged, within 2 years after the date of the discharge;
   - creditors who did not receive payment and who prove that the directors had foreseen the company’s impending liquidation, may claim reimbursement of his loss.

   Creditors may also sue them if the assets have not been distributed equally.

   b) Criminal offences

   They may also be convicted of economic crime if they illegally removed the company’s assets from a company bought for the purpose of preventing assets being recovered, after which the company may be dissolved.

2. Excusability and possibility for a fresh start

   Bankrupts still liable for the remaining debts not paid through bankruptcy proceedings, may obtain discharge of debt if they are excused after 5 or 20 years (depending on the type of debt and whether special legal steps were taken to secure it).
Directors may also obtain debt rescheduling if they can prove that they are not able and not expected to be able to fulfil their debt obligations in the next few years, and that their circumstances speak in favour hereof.

D. FINLAND

1. Negative consequences of bankruptcy

a) Directors’ liability for the remaining debts

Directors may be held liable for part or all of the company’s debts if they did not file for bankruptcy on time or if they did not convene a meeting of shareholders when the company’s equity decreased below half of its share capital.

They may also be held liable to compensate a loss caused through an error or negligence while performing their duties.

b) Criminal offences

Directors intentionally acting to the detriment of the interest of their creditors (destroying their property, transferring it abroad in order to make it unreachable to their creditors…) may be criminally sanctioned.

c) Professional interdictions

Prohibition on certain business activities may result from bankruptcy.

2. Excusability and possibility for a fresh start

Approximately three-quarters of all persons who have been involved in bankruptcy are still in business⁷, for directors who have not committed the above-mentioned faults will not be liable for the remaining debts. As for other entrepreneurs, they remain liable for their remaining debts, which may cause a long and vicious circle of debt collection. There has been a vivid discussion about the excusability of debts after 10 or 15 years, but to date there does not exist such provisions.

E. FRANCE

1. Negative consequences of bankruptcy

a) Directors’ liability for the remaining debts

A. Reimbursement of debt:

In case of mismanagement that contributed to the insufficiency of assets of their company, the directors may be ordered to reimburse all or part of the company’s debts.

⁷ According to the author of the Finish report.

4.3. Legal consequences of bankruptcy and possibilities for a fresh start
B. Involuntary bankruptcy:
Directors not respecting the above-mentioned reimbursement of debts or who misappropriated corporate funds, committed self dealing, may be sued in an involuntary bankruptcy procedure, independent from the company’s bankruptcy proceedings.

C. Personal bankruptcy:
If the directors do not reimburse debts imposed to them by the court, if the court decides to include their assets for the reimbursement of creditors, or if they violate a restriction on management imposed to them, a declaration of personal bankruptcy could apply to them. The consequences of this declaration is that they will be prohibited from managing companies with a commercial purpose, lose civil rights and be ineligible for positions before the commercial courts.

b) Criminal offences
Criminal penalties may apply to individuals who organised fraudulent bankruptcies, e.g. who fraudulently obtained funding or sold assets below their value in order to avoid bankruptcy.

c) Professional interdictions
The court may decide that persons subject to fraudulent bankruptcy may no longer practice certain activities.

2. Excusability and possibility of a fresh start:
Directors of a bankrupt company may, although pecuniary penalties have been imposed on them, continue their activities within the entity or the ongoing entity itself, if restructuring resulted from bankruptcy proceedings. This will not be the case if civil or criminal sanctions were imposed on them.

They are usually discharged from payment of the debts not satisfied by the liquidator, unless, for example, they committed criminal offences or fraud with respect to creditors, or in the case of personal bankruptcy

The French system therefore makes a distinction between “innocent” and “voluntary or fraudulent” bankruptcy, as regards the consequences that such bankruptcies may have on the possibility for entrepreneurs or directors to continue their activities or to start new businesses.

F. GERMANY

1. Negative consequences of bankruptcy

a) Director’s liability for the remaining debts
Directors who failed to petition for bankruptcy proceedings when they should have (within three weeks as from the date on which the company became
b) **Criminal offences:**

The German Criminal Code specifically provides for criminal insolvency offences: directors who fail to exercise the diligence expected from responsible businessmen or who committed fraudulent insolvencies may be liable to a prison term.

Directors who did not call a shareholders’ meeting when half or more of the company’s capital was eroded, may be liable to a prison term of up to three years or a fine.

c) **Professional interdictions**

Directors who committed a criminal offence are prohibited to practice for 5 years.

2. **Excusability and possibility of a fresh start:**

Individual customers may, under the customer insolvency procedure, benefit from a debt release granted by the insolvency court, if they have shown their good behavior during 6 years. Such judicial debt release does not exist for bankrupt companies which are usually wound up and whose directors will only be held liable in the above mentioned circumstances.

**G. GREECE**

A particularity of the Greek system is that, in some aspects, it is much more severe towards individual bankrupts than towards the directors of a bankrupt company.

1. **Negative consequences of bankruptcy**

   a) **Directors’ liability for the remaining debts**

   A. If a director’s conduct causes damage to the bankrupt company, the Board of directors (and not the company’s creditors or shareholders) may sue him. In case of bankruptcy, this possibility will be transferred to the administrator of the bankruptcy (who seldom pursue the director, due to the difficulty of finding evidence and the high costs resulting from judicial proceedings, and mostly because such proceedings do not affect the status of the director);

   B. Creditors may however sue directors following the general rules of tort (proof of a damage may be based on the fact that directors have intentionally violated the rules imposed on them by bankruptcy law.)

   C. They may also sue them if they prove that they have suffered damage because the directors did not notify them of their company’s cessation of payment, which is a legal obligation.

   b) **Criminal offences**
Directors may be convicted of plain bankruptcy, when they provoked bankruptcy through their faulty behaviour.

In case of a fraudulent bankruptcy, the court may order the bankrupt’s physical detention or house confinement, in order to ensure his physical availability during the bankruptcy procedure.

c) Professional interdictions

Only individual bankrupt lose their trading capacity and are therefore excluded from any commercial or industrial profession. They also face the prohibition of exercising certain functions (i.e. civil servant in the administrative, judicial and public sector, custodian, lawyer or official administrative, employees in a company of public law);

2. Excusability and possibility for a fresh start

Under Greek law, directors are not considered as merchants and may therefore never be declared personally bankrupt. They merely represent a company and although most of the time, due to their wrong judgements, they are responsible for a company’s bankruptcy, they are not professionally affected since they are free to start a new business, be appointed as directors or work as independent entrepreneurs.

Individual bankrupts are, however, as mentioned above, deprived from their status of merchant and incapable of starting a new commercial business. In order to obtain discharge of bankruptcy and to recover their status of merchant, one of the following conditions must be filled:

- a lapse of 10 years from the date of the bankruptcy’s declaration (long period of time);
- a judicial composition amongst the creditors, validated by the court, not subject to appeal and not declared void;
- full satisfaction of all creditors (unlikely to occur, since the entrepreneur who is declared bankrupt does not usually have enough assets to satisfy his creditors).

If one of these conditions is fulfilled (which rarely is the case), the court has the obligation to discharge the individual bankrupt. No discharge may however be granted in case of fraudulent bankruptcy.

As a conclusion, it appears that the Greek system creates a very important stigma on bankruptcy as regards individual entrepreneurs, who have little chance of starting a commercial business again (even though they are considered as “innocent bankrupts”). To the contrary, the directors are not very affected by their company’s bankruptcy, for their status is unchanged and they will be forced to reimburse their creditors only if the latter prove that they have suffered damage because of their acts. Such conception stimulates the trend to practice business activities through a company, and not as individual entrepreneurs.
**H. IRELAND**

1. **Negative consequences of bankruptcy**

   **a) Directors’ liability for the remaining debts**

   Directors may be made personally liable for all or part of the company’s debts, in case of:
   - **Fraudulent trading**: acting with the intent to defraud creditors (civil and criminal offence);
   - **Reckless trading**: carrying out a company’s business in a reckless manner (i.e. with “gross carelessness”);
   - **Misfeasance proceedings**: retaining the company’s money or property, being guilty of misfeasance or breach of duty or trust in relation to the company;
   - **Return of improperly transferred assets**: obligation to return company’s property that was disposed of in order to perpetrate a fraud on the company, its creditors or members;
   - **Failure to keep proper books and records**: contravention to the obligation to keep proper books of accounts, that resulted to the company’s inability to pay all its debts (or its winding up) or caused a substantial uncertainty as to its assets and liabilities.

   **b) Criminal offences**

   Directors of a bankrupt company may be criminally sued if they committed fraud, dishonesty, …

   **c) Professional interdictions**

   - **Restriction of directors**
     Any person who was a director of an insolvent company within twelve month of its winding up, may not be appointed as a directors of a company or take part in the incorporation of a new company for a term of five years, unless:
     - such company has a share capital of a certain amount,
     - or unless that person proves that it has acted honestly and responsibly or that he was director of the company solely by reason of his nomination and without taking part of the management.

   - **Disqualification of directors**
     Directors who were convicted of an indictable offence (see above) in relation to a company, may not be appointed as a directors of a company or take part in the incorporation of a new company for a term of five years.

2. **Excusability and possibility for a fresh start**

**I. ITALY**

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8 EUR 63.487 (or EUR 317.435 for public limited companies).

4.3. Legal consequences of bankruptcy and possibilities for a fresh start
1. **Negative consequences of bankruptcy**

   a) **Directors liability for the remaining debts**

   Under Italian law, directors have a special duty to act in protection of the company’s creditors. The breach of such duty will automatically trigger their liability.

   In the context of a bankruptcy, such breach of duty could arise from:
   - the payment with preference to certain creditors;
   - negligence, imprudence or technical incompetence that lead to the reduction of the company’s assets, to detriment of the creditors’ interests.

   Claims for damages could also be grounded on the breach of a specific rule (i.e. the duty to convene a shareholders’ meeting in the event of severe loss).

   b) **Criminal offences**

   Directors of a bankrupt company may be applied “bankruptcy crimes”, such as:
   - fraudulent bankruptcy offence (when the directors have concealed property, made false statements, fraudulent disposal of assets in favour of some creditors...);
   - obtaining credit in order to conceal the insolvency;
   - concealing bankruptcy assets, making false statements...

   c) **Professional interdictions**

   Bankrupts are unable to exercise certain professions (i.e. attorney at law or stockbroker), or to assume certain charges (trustee, tax collector, director, statutory auditor and liquidator of a company). If bankruptcy crimes have been applied, they may be prohibited from exercising entrepreneurs’ activities for ten years.

2. **Excusability and possibility for a fresh start**

   Directors of a bankrupt company may usually continue business activities, unless that have been applied the professional activities.

   Bankrupts could benefit from a judicial discharge. Such discharge may be obtained only if the bankrupt:
   - has integrally paid his debts;
   - or has regularly fulfilled its obligations from the creditor’s settlement procedure;
   - or has effectively and continuously proved his good behaviour for at least five years from the end of the bankruptcy procedure.

   This discharge may never be granted if the bankrupt was found guilty of bankruptcy crimes or crimes against the patrimony, the public faith, the industry and the commerce.
4.3. Legal consequences of bankruptcy and possibilities for a fresh start

J. LUXEMBOURG

1. Negative consequences of bankruptcy

   a) Directors liability for the remaining debts

   Directors of a bankrupt company may be held civilly liable for any misconduct in their management (the company may sue them in order to obtain reimbursement) or for the non-compliance of the law of August 10, 1915 or the company’s statutes (the company, the trustee or any third party may sue them jointly, e.g. in case of failure to convene a general meeting when needed, to publish the annual accounts…).

   If they committed a gross and indisputable mistake that contributed to the company’s bankruptcy, they may be ordered to pay all or part of the company’s debts.

   They may also be declared personally bankrupt under certain conditions (if they dispose of the company’s assets in their personal interest, continue a deficient exploitation…).

   b) Criminal offences:

      - in case of simple bankruptcy:
        the bankrupt may be sanctioned by imprisonment for a term between one month and two years, if it is discovered during the bankruptcy procedure, that he has committed a criminal offence, such as: payment to a favoured creditor to the detriment others, not declaring bankruptcy when required to, not keeping regular accountancy…
      - in case of fraudulent bankruptcy:
        the crime of fraudulent bankruptcy may be imposed if the bankrupt has removed records or falsified their content, if he has concealed part of his assets or if he states that he was debtor of sums while he was not. He will be sentenced to imprisonment for a term of five to ten years.

   c) Professional interdictions

   The bankrupt may be prohibited from performing a business activity (including being director of a company), for a period of one to twenty years, if:

   - the trustee or public prosecutor request it within three years from the judgement declaring bankruptcy;
   - the bankrupt has contributed by a gross and indisputable mistake to the bankruptcy, mistake that no diligent and careful director would commit.

   It automatically applies to any person convicted of fraudulent bankruptcy.

2. Excusability and possibility for a fresh start

   If the debtor’s assets were insufficient to cover the liquidation costs of bankruptcy, this procedure is closed and the creditors may still sue the insolvent entrepreneur. This constitutes an important obstacle to the possibility to start a new business.
Another element is that a bankrupt could continue its business or start new commercial activities only in the following circumstances:

- if he manages to negotiate a composition after bankruptcy with his creditors (and if he was not sentenced for fraudulent bankruptcy)
- if he is rehabilitated by the court, (i.e. if he has totally paid his debts and if he is not a fraudulent bankrupt nor has been sentenced for robbery, speculation or breach of trust).

It seems difficult for individual bankrupts who have lost all their assets to obtain a composition after bankruptcy or to pay all of their debts! Therefore, entrepreneurs/directors who were sanctioned through by prohibiting further commercial activities may seldom be rehabilitated and start a new business again… Luckily, this sanction is not automatic and does not apply to “innocent” bankrupts, who did not commit any gross and indisputable mistake.

K. THE NETHERLANDS

1. Negative consequences of bankruptcy

a) Director’s liability for the remaining debts

The directors may be jointly liable towards the company if they failed to properly perform their duty and if this failure contributed to the bankruptcy of the company (e.g. acts contrary to the company’s object, disproportionately large securities provided to banks in order to obtain credits…).

Certain creditors (tax authorities, social insurance and pension funds) may sue the directors of a bankrupt company for any outstanding tax, if the latter failed to notify these creditors in a timely manner, as legally required, of the company’s inability to pay them.

Creditors may also sue them for other unlawful acts (e.g. undertaking an obligation on behalf of the company knowing that the company would not be able to fulfil it).

b) Criminal offences

Directors who do not, during the bankruptcy proceedings, respect their obligation to provide the trustee, the bankruptcy judge and the creditors’ committee with the required information may be criminally sanctioned. Other criminal offences linked to bankruptcy are:

- prejudicing one creditor above the others;
- transferring assets below their value;
- not taking account of certain assets or withdrawing assets from the estate.

c) Professional interdictions

In order to start a new business, individual bankrupts and directors must obtain a “declaration of non-objection” by the Ministry of Justice, with regard to the
incorporation of a new company. Such declaration is difficult to obtain if the founders were previously involved in fraudulent businesses/bankruptcies or if they leave behind a trail of bankruptcies. This declaration will also be refused if there is reasonable doubt with regard to the reliability or the integrity of the individual.

2. Excusability and possibility for a fresh start

Bankrupts do not benefit from an automatic discharge of payment of their remaining debts, at the end of the bankruptcy procedure. They will only be released from their debts if they have reached a scheme of arrangements with their creditors. The Debt Restructuring of Private Individuals Act aims at helping them liquidate their assets in such a way that they will negotiate with creditors to obtain full discharge of their debts. This arrangement may include the transfer of their business to a third party.

As regards the possibility to start a new business, both individual bankrupts and directors are confronted with the requirement of obtaining a “declaration of non-objection” as explained above.

L. PORTUGAL

1. Negative consequences of bankruptcy

a) Directors’ liability for the remaining debts

Directors who have significantly contributed to the bankruptcy of their company through actions performed within the last two years previous to the declaration of bankruptcy, may be declared responsible for the bankrupt’s debts (if requested by the public prosecutor or any creditor).

b) Criminal offences

- Crime of fraudulent bankruptcy: committed by directors who, with the intention to cause detriment to their creditors, destroy or hide their assets, artificially aggravate losses…
- Crime of negligent insolvency: committed by directors who created a state of insolvency through serious negligence or imprudence and failed to apply for any recovery measures on time.
- Crime of favouring creditors: committed by directors, aware of their state of insolvency, who favoured certain creditors to the detriment of others.

c) Professional interdictions

As from the declaration of bankruptcy (and if no agreement was found to satisfy its creditors), individual bankrupts and directors of bankrupt companies are prohibited from carrying on any business, unless the judge recognises that they acted correctly and with normal diligence in the exercise of their activity, and if no criminal proceedings have been started.

2. Excusability and possibility for a fresh start
The possibility to start a new business is limited by the above-mentioned prohibition that may apply to bankrupts. This prohibition can however be set aside if the judge expressly authorises the bankrupt to practice a business in order for him to earn the indispensable means of sustenance and if such practice does not adversely prejudice the liquidation of the bankrupt’s estate.

M. SPAIN

Spanish bankruptcies are qualified by the judge, according to the bankrupt’s conduct, as follows:
- **Fortuitous** bankruptcy: accidental bankruptcy, produced by the misfortune of a debtor with good commercial management of his business.
- **Tortuous** bankruptcy: caused by a negligent debtor who lacked diligence in the administration of its business and the respect of basic commercial rules.
- **Fraudulent** bankruptcy: caused by the debtor’s intentional illegal acts (e.g. concealment of all or part of its assets, abuse of confidence to the detriment of third parties…).

Only fortuitous bankruptcies are exempted from criminal liabilities. Fortuitous and tortuous bankruptcies allow the bankrupt to reach agreements with his creditors and to request rehabilitation.

1. Negative consequences of bankruptcy

a) **Directors’ liability for the remaining debts**

In cases where the directors did not file for bankruptcy when they should have, the bankruptcy will be qualified as tortuous and the management will be held liable.

b) **Criminal offences**

Insolvency due to negligent conduct, tort, provoking, hiding or aggravation one’s bankruptcy are criminal offences. Directors can therefore be imposed criminal sanctions if they have caused the insolvency or provided false information regarding the company’s accounts. Should they wish to start a new business or manage another company, they will have to comply with their criminal sanction before starting it.

c) **Professional interdictions**

After the bankruptcy proceedings, bankrupts are barred from engaging in any business in the future, unless they are rehabilitated (see above).

2. **Excusability and possibility for a fresh start:**

After the closing of fortuitous or tortuous bankruptcy proceedings, the bankrupt may request its rehabilitation, in order to engage into business again.
This rehabilitation is not automatic. The latter must request it to the judge, under the following conditions:
- all debts must be paid or an arrangement with the creditors must be obtained
- in the event the bankrupt is also charged with criminal sanctions, these penalties must be complied with.

A fraudulent bankrupt may never be rehabilitated, even if all his debts are paid.

The Spanish system is based on a coherent distinction between the nature of the bankruptcy, based on the innocent, negligent or fraudulent character of the bankrupt. However, it does seem difficult for bankrupts to obtain an arrangement with their creditors if they have nothing left, and it would therefore seem fair to adjudicate automatic rehabilitation to the fortuitous bankrupt.

N. SWEDEN

1. Negative consequences of bankruptcy

   a) Directors’ liability for the remaining debts

   Directors who deliberately or negligently cause loss or damage to the company, its shareholders or third parties, are liable to pay damages.

   If a distribution of dividends is made without respecting the law, then the beneficiary must repay what he has received. If he is unable to do so, the directors involved in the decision of distribution may be liable for repayment.

   b) Criminal offences

   Depriving the creditors of assets of considerable value, not keeping the company’s books correctly, etc. is a criminal offence.

   c) Professional interdictions

   According to Swedish law, directors of a bankrupt company should be prohibited from carrying on a business, if:
   - it is in the public’s interest
   - and if they have severally neglected his business duties or its creditors’ interests.

2. Excusability and possibility for a fresh start

   Although the above-mentioned rules on prohibition seem quite strict, bankrupts are seldom really prohibited from trading9. The idea is to refrain only persons who were involved in several bankruptcies from trading.

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9 According to the authors of the Swedish Report.
As regards the numerous sanctions that may apply to directors in case of their company’s bankruptcy, it seems that it does not frighten them. At the contrary, most of them continue their business for as long as possible, in the hope of finding new investors to turn around the business and even improve the company’s business.

In that sense, Swedish bankruptcy legislation works well to facilitate a fresh start of bankrupt businesses.

O. UNITED KINGDOM

1. Negative consequences of liquidation

a) Directors’ liability for the remaining debts

Management of a liquidated company can be held personally liable for the company’s remaining debts in case of:
- misfeasance or breach of any fiduciary or other duty
- fraudulent trading (carrying out a company’s business with the intent to defraud creditors or for any other fraudulent purpose)
- wrongful trading (continuing to trade when the director knew or ought to have known that there was no reasonable prospect of the company avoiding liquidation).

b) Criminal offences

Fraud, misconduct, falsification of the company’s books, material omissions from statements and false representations are criminally sanctioned.

c) Professional interdictions

Under the Company Directors Disqualification Act of 1986, directors may be disqualified from being a director, acting as receiver of a company’s property or being concerned with the promotion, formation or management of a company, in the following circumstances:
- criminal offences connected with the Companies Acts legislation
- wrongful trading
- failure to comply with filing requirements
- unfit conduct in insolvent companies.

The minimum period of disqualification is 2 years and the maximum 15 years.

2. Excusability and possibility for a fresh start

The UK system seems to distinguish between fraudulent and non-fraudulent insolvency, providing a wide range of sanctions and prohibitions for directors that have acted unlawfully or against the company’s or creditors’ interests. Should this not be the case, directors are apparently free to start a new business again.
P. UNITED STATES

1. Negative consequences of bankruptcy

a) Directors’ liability for the remaining debts

The confirmation of a plan of reorganisation in a Chapter 11 case ordinarily discharges the corporate debtor from liability for all debts arising prior to the effective date of the plan of reorganisation, except to the extent that the plan of reorganisation otherwise provides.

If the liquidation of the business was achieved through Chapter 7, the company ceases to exits and typically all pre-petition debts are discharged. Technically the Bankruptcy Code stipulates that a corporate debtor in Chapter 7 will not discharged of pre-petition debt, however since the entity ceases to exits, granting a discharge is irrelevant. However, a creditor can object to the discharge by filing a complaint in the bankruptcy court, called an “adversary proceeding”. A discharge may also be denied entirely if the individual debtor has engaged in bankruptcy-related wrongs (e.g. concealing assets from creditors).

Certain debts of an individual debtor are not discharged based on the nature of the debt or the fact that the debts were incurred due to improper behaviour of the debtor. The most common types of non-discharged debt are typically related to individual debtor rather than the corporate debtor, and include certain types of tax claims, child support, alimony, debts for wilful and malicious injuries to person or property, debt to government units for fines and penalties. In general the directors and officers of a corporate debtor, will not be responsible for any debts from the estate.

Outside of bankruptcy, directors and officers have a duty of care (applying the same care as an ordinary prudent person) and a duty of loyalty (prohibits faithlessness and self-dealing), referred to as a fiduciary duty, towards the company’s shareholders.

When a company moves into the “zone of insolvency”, the fiduciary duty shifts from the stockholders to the creditors. Zone of insolvency refers to when a company becomes insolvent. A company is typically considered insolvent when it is unable to pay its obligations or the company’s liabilities exceed the assets.

Directors and officers can be held personally liable for certain actions that are in breach of their fiduciary duty to creditors, during the time the company is insolvent. Usually this fiduciary duty towards creditors stops when the company files for bankruptcy, because most significant decisions are subject to review by interested parties and approval by the court. There is no uniform rule governing the releases and indemnification for directors and officers. However, the Business Judgement rule provides a safe harbour for directors, which operates from the presumption that directors’ actions are in good faith.

Traditionally, large companies carry director and officer insurance which protects officers and directors for any actions taken in derogation of their twin duties of
loyalty and care generally to the extent such actions are not the result of gross negligence or wilful misconduct. In Chapter 7 cases, the trustee directly replaces the management.

b) Criminal offences

Directors and officers in a Chapter 7 or Chapter 11 case may be criminally indicted for fraud or gross negligence in performing duties and responsibilities.

c) Professional interdictions

After a company emerges from chapter 11, there are no penalties assessed on management. Absent a release, a management member may be held civilly liable if a creditor successfully prosecutes a cause of action against such individual. Unless management is subject to a non-compete agreement, individuals are free to engage in new enterprises. The only deterrent is whether such individual’s reputation is adversely impacted by an unsuccessful reorganisation.

2. Excusability and possibility for a fresh start

The commencement of a Chapter 7 liquidation is an admission that the business enterprise has failed. Although the public may perceive such liquidation negatively, it does not necessarily mean that the directors and officers are stigmatised to be able to start new business.

The initiation of Chapter 11 proceedings, although newsworthy, does not necessarily create negative publicity, since the outcome of the proceedings is not always liquidation, but usually reorganisation. Even if the case is a “liquidating” Chapter 11, the debtor attempts to dispose the assets, as a going concern, which usually creates more value to the creditor if the assets are sold at liquidation values.

Rather than chilling new investments in the company, the procedure encourages and facilitates mergers and acquisitions by providing a mechanism for the debtor to identify parties interested in acquiring its assets. The latter are sold free and clear of liens, claims, and other interests, including secured claims.

During a Chapter 11 case, management is often rewarded through retention bonus and incentive compensation programs (subject to Bankruptcy Court approval) and is proposed to ensure that key management does not leave the company during its reorganisation. These programs are another way to mitigate the stigma of chapter 11 by encouraging management to remain with the company.

In general, the American system regards bankruptcies in a much more positive manner than in Europe, as further discussed hereunder.

4.3.3.2. COMPARATIVE ANALYSIS

Bankruptcy affects the debtor in many ways; his reputation may be prejudiced (depending on the publicity made regarding the bankruptcy); he may be faced with
creditors still requesting reimbursement or encounters difficulty in starting a new business because of restrictions resulting from the bankruptcy.

We shall describe hereunder, the major restrictions applied to debtors (individual entrepreneurs and directors of a company), sanctions that may constitute major obstacles to a new start.

We shall then discuss the possibilities offered by the European Member States to allow for the fresh start of new businesses and contrast it to the U.S. system.

I. Restrictions applied as a result of bankruptcy:

Restrictions that generally apply to bankrupt individuals or directors of bankrupt companies are:

- of a pecuniary nature (liable for all or part of the company’s debts to the estate or creditors);
- of a civil nature (e.g. obligation to provide repair of damage suffered as a consequence of the bankruptcy);
- of a criminal nature (in case of fraudulent bankruptcy, concealing assets...);
- of a prohibitive nature (i.e. prohibited to exercise certain functions or to assume certain charges).

• Individual entrepreneurs vs. directors:

In some countries, the sanctions that apply to individuals and to directors of companies are quite similar, except of course for legal specificities that result from the fact that directors have, unlike individual entrepreneurs, the duty to answer for their acts to the company’s shareholders.

The Greek system imposes stricter sanctions to individual entrepreneurs than to directors (only individuals automatically lose their trading capacity and are prohibited from exercising certain functions). This concept promotes the use of corporations for launching a new business rather than a sole proprietary.

• pecuniary or civil sanctions vs. prohibitions:

All countries apply pecuniary or civil sanctions (that do not necessarily result from bankruptcy legislation but from general principles of tort or the obligation to repair a damage caused to others).

The automatic prohibition of exercising certain functions or assuming certain charges after bankruptcy does not exist in all countries or is seldom applied. It is mostly in Greece or in Portugal that they are applied.

It seems that, among these various sanctions, the sanction of prohibition constitutes a greater obstacle to the possibility of a fresh start.
sanctions in the interest of creditors vs. in the interest of the “society” in general

A common feature is the duty to protect the creditors and to respect the creditors’ equality in the distribution of assets. Directors of bankrupt companies are often sued in this regard, if they favoured creditors to the detriment of others, before bankruptcy proceedings were initiated.

The objective of other sanctions lies within the idea of “purifying” the market: expunging incapable entrepreneurs or making sure that they will not be able to launch a new business again (e.g. through the prohibition sanction).

“innocent” bankruptcy vs. fraudulent bankruptcy:

After having observed the various sanctions resulting from bankruptcies, one can not refrain from considering that some appear to be “normal” whereas others seem “unfair”. Such consideration results from the fact that one tends to accept more easily sanctions applied as a result of wilfully fraudulent bankruptcies than the sanctions applied to “innocent” bankrupts, that suffered misfortune or following certain circumstances of life. It is easier to accept that fraudulent bankrupts be held liable for their remaining debts, or be prohibited from launching a new business again.

Although this appears to be an essential element to consider when providing for post-bankruptcy sanctions, it seems that not all countries make a clear distinction between innocent or honest and fraudulent bankruptcies. Belgium, France, Luxembourg and mostly Spain tend to apply different sanctions to innocent bankrupts and fraudulent bankrupts. The Spanish system seems to be an example to follow in that regard, with its qualification of bankruptcies as fortuitous, tortuous or fraudulent.

It is essential that a distinction is made between the two kinds of bankruptcies, so that honest bankrupts do not continue to be stigmatised through association with the dishonest.

II. Possibilities for a fresh start and stigma on bankruptcy:

What exactly is meant by “fresh start”? Fresh start is the possibility of continuing or starting a new business after a bankruptcy. Fresh start is rendered possible where the stigma on bankruptcy is low (i.e. the negative attitudes and barriers for entrepreneurs that discourage them from risk-taking and entrepreneurship).

Concretely, the stigma on bankruptcy can result from:
- the importance of sanctions applied to bankrupts;
- the prohibition to carry out economic activities;
- the negative publicity (e.g. mention of the bankrupt’s name on a special list with the commercial jurisdiction, publication in local or national newspapers…);
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

- the possibility to invoke the directors’ liability and the importance of the insurance coverage they may benefit from
- the confusion between fraudulent and non fraudulent bankruptcy.

In order for a bankrupt to bypass this stigma and to start a new business again, two important elements must be considered:

a) Discharge of the remaining debts:

As described above, a consequence of bankruptcy applied in almost all countries is the bankrupt’s liability for his remaining debts.

In order to allow fresh start, the notion of discharge of debt is essential, but for individual entrepreneurs only. Bankrupt companies are usually, after the bankruptcy procedure is finished, totally liquidated so that their creditors no longer have anyone to turn to for the reimbursement of their claims (unless they can sue the company’s directors at fault).

As for individual bankrupts, how could they possibly envisage the possibility of starting a new business if, as soon as they make any profit, their previous creditors will come knocking on their door in order to obtain satisfaction of their claims?

Some countries allow a total or a partial discharge of debts.

Very few countries provide for an automatic discharge of debts (e.g. Greece, but this advantage is strongly counterbalanced by the deprivation of the individual bankrupt’s status of trader).

Most countries accept such discharge, but only following a special procedure (e.g. rehabilitation in Austria, Belgium, Germany, or Spain). This rehabilitation is often linked to the notion of “innocent” bankruptcy, which seems quite logical.

Some countries (Denmark, Italy) allow such discharge, but only upon fulfilment of strict conditions, e.g.:
  - the total satisfaction of creditors (which seems almost impossible to achieve for a small bankrupt with nothing left), or
  - the expiration of a certain period of time during which the bankrupt has proved his good behaviour.

Other countries (Austria or Finland) are very strict. They provide that discharge may only be granted if the debtor manages to obtain a reorganisation plan with its creditors (which is clearly difficult in a “traditional” bankruptcy where there are hardly no assets left, but might appear easier in countries where the initiation of bankrupt does not necessarily lead to the company’s winding-up but may result in its reorganisation and continuity of its business).

In the countries where release of debts exists, such release is sometimes never granted if the bankrupt has been convicted with criminal offences (e.g. Italy, Luxembourg).
### Liability for the Remaining Debts and Possibility of Discharge

<table>
<thead>
<tr>
<th>Country</th>
<th>Directors liable conditions</th>
<th>Discharge conditions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>- Directors liable if committed a fault (e.g. did not file for judicial insolvency on time)</td>
<td>- Discharge if reorganisation or in the course of private bankruptcies (non-traders)</td>
</tr>
<tr>
<td>Belgium</td>
<td>- Directors liable if committed a serious fault that led to bankruptcy or if did not declare bankruptcy on time</td>
<td>- Discharge if excusability is granted by the court (in case of innocent bankruptcy)</td>
</tr>
<tr>
<td>Denmark</td>
<td>- Directors liable after bankruptcy/winding-up procedure but not after compulsory composition</td>
<td>- Discharge in case of release after 5 or 20 years or in case of debt rescheduling</td>
</tr>
<tr>
<td>Finland</td>
<td>- Directors liable if did not file for bankruptcy on time or did not convene shareholders on time</td>
<td>- Discussion on discharge</td>
</tr>
<tr>
<td>France</td>
<td>- Directors liable in case of mismanagement</td>
<td>- Yes, unless specific offences committed</td>
</tr>
<tr>
<td>Germany</td>
<td>- Directors liable if failed to petition for bankruptcy on time</td>
<td>- Discharge under customer insolvency procedure</td>
</tr>
<tr>
<td>Greece</td>
<td>- Directors liability if committed tort or did not notify creditors of cessation of payments</td>
<td>- Discharge for individual bankrupts after 10 years or in case of judicial composition</td>
</tr>
<tr>
<td>Ireland</td>
<td>- Directors liable if fraudulent/reckless trading, misfeasance proceedings…</td>
<td>- Discharge: possible</td>
</tr>
<tr>
<td>Italy</td>
<td>- Directors liable if do not respect their duty to protect the company’s creditors</td>
<td>- Discharge for individual bankrupts if good behaviour or creditors’ settlement</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>Directors liable for misconduct in management or fault that led to company’s bankruptcy</td>
<td>- Discharge if composition after bankruptcy or rehabilitation</td>
</tr>
<tr>
<td>The Netherlands</td>
<td>Directors liable if their failure contributed to bankruptcy</td>
<td>- Discharge if scheme of arrangement reached with creditors</td>
</tr>
<tr>
<td>Portugal</td>
<td>- Directors liable if significantly contributed to the company’s bankruptcy</td>
<td>- Discharge</td>
</tr>
<tr>
<td>Spain</td>
<td>- Directors liable if did not file for bankruptcy on time</td>
<td>- Discharge if rehabilitation is granted (in case of non-fraudulent bankruptcy)</td>
</tr>
<tr>
<td>Sweden</td>
<td>- Directors liable if deliberately or negligently caused damage to company</td>
<td>- Discharge</td>
</tr>
<tr>
<td>UK</td>
<td>- Directors liable if misfeasance, fraudulent / wrongful trading</td>
<td>- Discharge if non-fraudulent insolvency</td>
</tr>
<tr>
<td>USA</td>
<td>- Individual debtor discharged from debt, except certain debts (e.g. alimony, taxes, damages for fraud…)</td>
<td>- Corporate debtor discharged from debts</td>
</tr>
</tbody>
</table>
b) Non-prohibition of carrying-out commercial activities:

Having obtained discharge of the remaining debts is not the only condition for a successful fresh start. How could the entrepreneur/director be able to launch a new business if he has been subject to a prohibition from exercising certain commercial activities or professions?

As mentioned above, Greece seems to have the strictest regime in that regard, for bankrupt entrepreneurs will immediately lose their trading capacity and are therefore excluded from any commercial or industrial profession.

Some professions (e.g. trustee, lawyer, employee in a company of public law, auditor...) may not be exercised by individuals previously bankrupt, either automatically as a result of the bankruptcy, either under certain conditions, as illustrated hereafter.

France bases such prohibition on the existence of criminal sanctions and applies it only to the activities for which the bankrupt was subject to fraudulent bankruptcy, which appears to be a sound limitation.

The Netherlands have a specific regime: bankrupt entrepreneurs and directors of a bankrupt company must, before incorporating a new company, obtain a “declaration of non-objection” by the Ministry of Justice. The granting of such declaration is mainly based on the distinction innocent vs. fraudulent bankruptcy.

In contrast, the U.S. Bankruptcy Code provides for a complete discharge of debt, subject to litigation involving objections by creditors and other limited exceptions. The discharge constitutes a permanent statutory injunction prohibiting creditors from taking any action designed to collect the discharged debt.

In general, the US Bankruptcy Code does not place any restrictions on the directors or individual entrepreneur subsequent to the discharge of the debt, which allows them to enter freely into other business ventures thereafter. However, restrictions will be placed on any individual that has been convicted to a criminal offence related to any fraud, gross negligence or wilful misconduct that led to the bankruptcy.

<table>
<thead>
<tr>
<th>Country</th>
<th>Possible Prohibition of Carrying-out Commercial Activities and Conditions Therefore</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>Prohibition from engaging in an independent trade or business (with exemptions)</td>
</tr>
<tr>
<td>Belgium</td>
<td>Prohibition from carrying out certain professions (auditor) or mandate (management of insurance company) under certain conditions (fraud…)</td>
</tr>
<tr>
<td>Denmark</td>
<td>Business prohibitions (if illegal removal of company’s assets)</td>
</tr>
</tbody>
</table>

4.3. Legal consequences of bankruptcy and possibilities for a fresh start 293
### 4.3. Legal consequences of bankruptcy and possibilities for a fresh start

<table>
<thead>
<tr>
<th>Country</th>
<th>Possible Business Prohibitions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Finland</td>
<td>Possible business prohibitions</td>
</tr>
<tr>
<td>France</td>
<td>Prohibition to practice certain activities (in case of fraudulent bankruptcy)</td>
</tr>
<tr>
<td>Germany</td>
<td>Prohibition to practice for 5 years for directors who committed criminal offences.</td>
</tr>
<tr>
<td>Greece</td>
<td>Individual bankrupts are excluded from any commercial or industrial profession, and from certain functions (civil servant, lawyer...)</td>
</tr>
<tr>
<td>Ireland</td>
<td>Restriction from being appointed director of a company or incorporating a new company for a term of five years (unless proof of good conduct)</td>
</tr>
<tr>
<td>Italy</td>
<td>Prohibition to carry out certain professions (lawyer, stockbroker) or charges (trustee, director..)</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>Under certain conditions (gross and indisputable mistake that lead to bankruptcy), prohibition from performing business activity</td>
</tr>
<tr>
<td>The Netherlands</td>
<td>Prohibition unless “declaration of non-objection” obtained with the Ministry of Justice</td>
</tr>
<tr>
<td>Portugal</td>
<td>Prohibition from carrying out any business, unless judge provides that they may and if no criminal proceedings</td>
</tr>
<tr>
<td>Spain</td>
<td>Prohibition from engaging in any business, unless rehabilitated.</td>
</tr>
<tr>
<td>Sweden</td>
<td>Prohibition from carrying out a business if in public interest and if severe negligence</td>
</tr>
<tr>
<td>UK</td>
<td>Prohibition from being a director, receiver or incorporating a company under certain conditions (if criminal offences, wrongful trading...)</td>
</tr>
<tr>
<td>USA</td>
<td>None, except if directors were criminally prosecuted</td>
</tr>
</tbody>
</table>

#### 4.3.4. CONCLUSION

A comparison of the various bankruptcy systems in the EU Member States indicates that the common goal of these procedures is to provide for the efficient liquidation of businesses in distress and the reimbursement of its creditors.

The various country systems follow a similar theme:

- Judiciary procedure initiated by the debtor or its creditors or other party;
- Creditors declare their claim in order to obtain reimbursement;
- A specific authority (trustee, receiver, liquidator, etc.) replaces the directors of the company;
- Distribution to creditors of the remaining assets, following a specific priority.

In order to benefit from such procedures, various criteria’s are required that all have to do with the impossibility for a business to recover. Some criteria’s are quite flexible (e.g. Germany and Ireland: inability to pay any minor debt), whereas others are more strict (e.g. Austria where the company must suffer illiquidity and over-indebtedness.)
Although all countries’ procedures seem to reach their goal, i.e. the liquidation of a company, some countries’ systems (e.g. Germany, France and U.S.) also emphasis the restructuring of companies in order to (1) continue the business, (2) continue the employment of employees and (3) maximising the return to creditors and other stakeholders.

Most EU Member States’ systems impose certain restrictions, whether of a pecuniary or criminal nature, on individual debtors or directors, or certain prohibition to perform certain activities or to be appointed in certain functions. This has the potential to create negative stigma, since these restrictions creates an environment that deters entrepreneurs to make a fresh start.

These restrictions are considered to be justified where the individual debtor and directors committed fraud or willingly caused the company’s bankruptcy. However, in bone fide cases of bankruptcy, some of the restrictions could be considered excessive and prohibits entrepreneurs to make a fresh start. Not all countries make a clear distinction between bone fide and fraudulent bankruptcies and the restrictions related to a bone fide versus fraudulent bankruptcy.

According to our study, it appears that two conditions are required in order to allow for a new fresh start:

a) the total discharge of the debtors’ remaining debts;

b) limited restrictions should be imposed on the individual debtor or director in a bone fide bankruptcy.

Under these circumstances, previously bankrupt entrepreneurs may find the motivation to launch a new business again.
4.3. LEGAL CONSEQUENCES OF BANKRUPTCY AND POSSIBILITIES FOR A FRESH START

This title summarises the bankruptcy procedures organised in the EU Member States and in the U.S. (hereafter “targeted Countries”). A thorough comparison between the different procedures is presented, in order to emphasise their particularities and to evaluate their degree of adequacy.

This title also describes the legal consequences arising from such procedures as well as the stigma that may result therefrom. These consequences will then be compared in order to highlight the general causes of a stigma of failure and develop the possibilities for a fresh start.

4.3.1. INTRODUCTION

Contrary to restructuring procedures aimed at rescuing a business (see section 4.2 of this report), bankruptcy is a formal judicial or administrative procedure that aims principally at realising the bankrupt’s assets for the purpose of distributing the net proceeds to its creditors, usually as a result of its insolvency. In some countries however, the initiation of bankruptcy proceedings may result in the reorganisation of the business.

Bankruptcy procedures have important consequences regarding the liability of management and entrepreneurs, the prohibition from practising certain professions, criminal offences, etc. Currently the bankruptcy procedures create a stigma on failure, prohibiting entrepreneurs from starting new businesses.

4.3.2. INITIATION OF BANKRUPTCY PROCEDURES AND DIRECT EFFECT OF THESE PROCEDURES

4.3.2.1. OVERVIEW OF THE NATIONAL PROCEDURES

A. AUSTRIA

In Austria, bankruptcy ("konkurs") is governed by the Bankruptcy Act of 1914.

Austrian bankruptcy law is primarily creditor oriented and mainly aims at liquidating the debtor’s assets instead of trying to rescue the business.

1. Initiation of the proceedings

Bankruptcy applies to companies only, unlike the “private bankruptcy” (or “privatkonkurs”) for which only individuals may petition. The latter will not be further considered in this report.

Bankruptcy can be petitioned by:

- the debtor

1 See the Austrian Bankruptcy Act of 1914
2. **Criteria for the petition:**

The ground for initiating bankruptcy proceedings is the *illiquidity* of the debtor (i.e. when he can no longer meet his financial obligations for a certain period of time). He must also be in a situation of *over-indebtedness* (i.e. his liabilities must exceed his assets. A pre-bankruptcy balance sheet must be established to determine whether the debtor is overly indebted).

The debtor must also have sufficient assets to cover the costs of the proceedings.

3. **Effects:**

A bankruptcy order is made by the court. The main effects of the judgement of Bankruptcy are:

- creditors must declare their claim within a specific deadline;
- a *bankruptcy administrator* is appointed, in order to continue, if possible, the debtor’s business, inventory and liquidate the assets;
- a *creditors’ committee* is appointed by the court. Such committee is composed of three to seven members, for the purpose of checking the cash management, assisting the bankruptcy administrator and approving certain transactions;
- a *creditors’ assembly* supervises the bankruptcy *administrator* and the creditors’ committee;
- a peculiar body is the *Association for the Protection of Creditors’ Rights*: there are in Austria 3 associations, created upon approval of the Federal Ministry of Justice, that represent and secure creditors in the course of insolvency proceedings.
- the assets can be distributed following the distribution plan drafted by the bankruptcy administrator and approved by the creditors’ committee.

4. **Publicity:**

Since 2000, the court’s bankruptcy judgement must be published on the Internet.

In general, the bankrupt’s name is not mentioned in a specific register but only on the Internet, except for companies registered in the Commercial Register, for which the opening of bankruptcy proceedings will be published in this Register.

5. **End of the procedure:**

The procedure ends:

- When all assets of the bankrupt have been distributed;
- Or when it appears that that the assets are not sufficient to cover the costs of the proceedings;
- Or with the consent of all creditors;
- Or when the bankruptcy proceedings are converted into “compulsory reorganisation” proceedings (see Title 4), after the reorganisation plan has been accepted by the creditors and confirmed by the court.

**B. BELGIUM**

In Belgium, bankruptcy (“faillite” or “faillissement”) is governed by the Belgian law of August 8, 1997 on bankruptcy.

1. **Initiation of the proceedings**

   Bankruptcy proceedings apply to traders (individuals or companies) only.

   They are initiated by the debtor (who is obliged to do so within one month of the cessation of his payments), a creditor or the Public Prosecutor.

2. **Criteria for the petition:**

   The law requires that the debtor:
   - has ceased its payments, and
   - has lost its creditworthiness.

3. **Effects:**

   The main effects of the bankruptcy order are:
   - a receiver in bankruptcy (“Curateur/Curator”) is appointed to recover and realise the debtor’s assets, and to distribute the net proceeds to the creditors;
   - creditors must declare their claim within a specific period of time;
   - the debtor is automatically divested from the control of its assets;
   - all claims against the bankrupt become due;
   - a stay of legal proceedings and execution measures against the debtor or his property.

4. **Publicity:**

   The court’s bankruptcy order must be published in the Official Belgian Gazette and in two newspapers.

   A file relating to the bankrupt will be kept at the clerk of the commercial court and any interested party may consult it for free.

5. **End of the procedure:**

   The procedure ends when all assets are distributed and the company’s liquidation is achieved or if the assets are not sufficient.

**C. DENMARK**

Under Danish law, bankruptcy (“Konkurs”) is governed by the Danish Bankruptcy Act of June 8, 1977 (consolidated in September 1986).
An insolvent debtor’s property is liquidated and its proceeds are distributed among its creditors following the bankruptcy/winding-up procedure (“konkurs”) or the Liquidation Composition procedure (“likvidationsakkord”). The difference between these procedures is that, in case of liquidation composition as opposed to bankruptcy/winding-up, the trader is discharged for his remaining debts.

Liquidation composition may be carried out voluntarily by agreement or as a compulsory composition (see Title 4 for the description of this procedure). In this section we will only address the bankruptcy/winding up proceedings.

1. Initiation of the proceedings:

Bankruptcy/winding-up proceedings, which apply to both natural and legal entities (company), are initiated either by the debtor or his creditors.

2. Criteria for the petition:

In order to apply for bankruptcy/winding-up, a company must be insolvent. Under Danish law, insolvency is defined as a state of “illiquidity”, i.e. the debtor is not able to meet his financial obligations as they fall due.

3. Effects:

The purpose of this procedure is to ensure that the creditors receive an equal treatment in the distribution of their debtor’s assets, with priority to secured or preferential creditors.

After a bankruptcy/winding-up order is issued by the court, trustees/liquidators will be appointed who will take over the business management and realise its assets.

There is a stay of all legal proceedings and executions of enforcement against the bankrupt’s property: creditors may no longer levy execution or attachment, they must wait for the assets’ distribution by the liquidator.

4. Publicity:

Publicity is generated by the bankruptcy proceedings.

5. End of the procedure:

The procedure ends when all assets are distributed among the creditors and, if the debtor is a company, when it is dissolved.

D. FINLAND

In Finland, bankruptcy (“konkurssi”) is governed by the Finish Bankruptcy Act of 1968, the Act on the Recovery of the Bankruptcy Estate of 1991, the Act on the Priority of Claims of 1992 and the Act on the Supervision of the Administration of Bankruptcy Estates of 1995. A proposal for a government bill has recently been
approved which will result in a new Bankruptcy Act that clarifies the existing legislation. It is expected to become law in 2003.

1. **Initiation of the proceedings:**

Bankruptcy applies both to individuals and companies. It is initiated by the debtor (voluntary) or a creditor (involuntary).

2. **Criteria for the petition:**

A particularity of the Finish system is that a debtor may voluntarily file for bankruptcy, *without regard* to any preconditions of its financial status.

However, in case of involuntary bankruptcy, creditors must prove one of the six conditions set out in the Bankruptcy Act (e.g. an unsuccessful attempt of execution, negligence to satisfy creditors eight days after receiving a certified request for payment from a bailiff, etc…).

After proceedings are initiated voluntarily, a provisional administrator is appointed, for the purpose of submitting an inventory of the debtor’s estate in order to check if it is sufficient to merit full bankruptcy proceedings.

3. **Effects:**

Various actors intervene in the procedure:

- a *provisional administrator* (see above) who will be replaced, when bankruptcy is accepted, by:
- a *trustee*: his role is to take care of the procedure of acceptance of creditors’ claims and to act as executor after the expiration of the time limit for the proof of claims.
- The *creditors’ meeting* plays an important role in the bankruptcy estate’s administration, while the administrator and trustee must comply with all of its major decisions.
- A bankruptcy *ombudsman* supervises all actions of the administrator and trustee. It is an independent and impartial authority, who may not prejudice the rights of the debtor nor the creditors.

Other effects are:

- Execution of the debtor’s assets are suspended;
- Interest on a debtor’s debt continues to accrue, unlike in other countries;
- The debtor loses all control over its property and assets. This authority is taken over by the body of creditors;
- After the creditors’ claims have been lodged and accepted, the assets will be distributed among the creditors. Secured creditors will receive payment prior to the other creditors. Claims secured by a floating charge (security not attached to a particular asset but to a category of assets that may be modified through the evolution of the business. In the case of bankruptcy, the “floating charge” becomes a “fixed charge”) also enjoy a priority of payment.
4. Publicity:

Bankruptcy judgements are made public in newspapers. There is no specific bankruptcy register.

5. End of the procedure:

The procedure ends when all assets have been distributed and the company is liquidated.

E. FRANCE

French bankruptcy (“faillite”) is governed by the Law of January 25, 1985 on restructuring and judicial liquidation of companies, as modified by the law of June 10, 1994.

The French bankruptcy is not favorable to creditors, for its main priority is to save the company and not only to settle its debts.

Judicial liquidation (or “liquidation judiciaire”) of a company may however be ordered by the court either:
- after an observation period (that lasts from 4 to 20 months) during which the company may continue its business, and at the end of which the judge must decide between a reorganisation or a liquidation procedure; or
- immediately, when the business has ceased all activities or when its restructuring is clearly impossible.

1. Initiation of the proceedings:

Bankruptcy proceedings are open for both:
- companies (practising commercial activities or not);
- individuals (merchants, registered craftsmen and farmers).

Proceedings may be initiated by:
- the debtor itself (it is obliged to declare its default of payment within 15 days of cessation of payments);
- a creditor, regardless of the amount of its claim;
- the Public Prosecutor (seldom);
- the Court.

2. Criteria for the petition:

A Bankruptcy order can be made by the court, on the following grounds:
- default of payment, i.e. when the debtor’s available capital (defined as the assets that can be liquidated within a few days) does not meet its debt obligations (debts due and payable);
- breach of the terms of the amicable settlement or of the continuation plan (see Title 4);
- penalties against managerial misconduct (i.e. bankruptcy opened against the
director of a company if he was found liable for the company’s debts and did not
pay them, or if he misappropriated corporate funds, signed interested
transactions...).

3. Effects:

The Bankruptcy order governing the company’s liquidation has the following main
effects:
- a liquidator is appointed for the purpose of selling the business’ assets and
dividing them among the creditors;
- an ‘insolvency judge’ is appointed, in order to supervise the liquidation and to
ensure the protection of the interests of all parties;
- in case an observation period precedes the liquidation, it has the following effects
upon the creditors:
  a) all court proceedings involving debts that arose prior to the commencement of
the bankruptcy proceedings are suspended, as well as the enforcement of any
judgement;
  b) the debtor is prohibited from paying any debt that arose prior to the
commencement of the bankruptcy proceedings;
  c) interest accrual on prior debts is suspended;
  d) any acceleration of payment of outstanding debt is prohibited.
- Creditors are paid following specific rules (e.g. waged workers first, then legal
expenses, creditors with pledges or mortgages...).

4. Publicity:

The judgement initiating the liquidation procedure must be published in the
Commercial Registry for companies and entrepreneurs, in the Professions Registry for
craftsmen and in a newspaper.

5. End of the procedure:

The liquidation procedure ends either when all the company’s debts are settled, or
when its assets are insufficient to settle all of its debts (which is mostly the case).

F. GERMANY

German insolvency proceedings (“insolvenzverfahren”) are governed by the German

They do not regulate only a bankrupt’s compulsory winding-up. These proceedings
may also lead to reorganisation measures.

They apply to companies or individuals (“customer insolvency procedures”).

For the purposes of this report, we will consider these proceedings as far as they
govern compulsory winding-up of companies.
1. **Initiation of the proceedings:**

   “Insolvenzverfahren” procedure can be initiated by:
   - the debtor himself
   - a creditor;
   - against any individual or company (except the Federal or State government or any company subject to the latter’s supervision).²

2. **Criteria for the petition:**

   The criteria for commencement are quite flexible and include the following:
   - A debtor’s inability (or imminent inability) to pay its debts as they fall due. Even an inability to balance minor outstanding payments can justify the commencement of insolvency proceedings, or
   - bankrupt’s liabilities exceeding its assets (excessive indebtedness).

3. **Effects:**

   A petition for “insolvenzverfahren” has the following effects:

   a) **Preliminary measures:** in order to secure the bankrupt’s property, the court will appoint a preliminary trustee who will run the bankrupt’s business until the opening of insolvency proceedings.

   b) **Insolvency proceedings:** if the court agrees to open insolvency proceedings:
      - A final trustee in insolvency is appointed to manage the company. He will dispose of the debtor’s assets instead of the bankrupt, unless the court orders self-management (i.e. the bankrupt continues to manage its business under supervision of the trustee);
      - Creditors register their claim, within a specified period of time;
      - The trustee collects the bankrupt’s claims and realises the assets. In this regard, like in most countries, he is required to respect certain rules, notably:
         a) the assets of creditors with a right of ownership against the bankrupt (owners with a retention title, landlord, lessor…) will be segregated out of the insolvency’s estate.
         b) Other creditors (having security on movable or immovable property) will have a privileged claim against the insolvent estate at its realisation.

4. **Publicity:**

   The court resolution over the initiation of the insolvency proceedings is made public by the office of the insolvency court in the German Federal Gazette (“Bundesanzeiger”).

   The public announcement takes the form of an entry in the publication for official notices of the court. The insolvency court can arrange further and repeated

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² They however do not apply against individuals who are not self-employed or have been self-employed, to whom a simplified insolvency procedure applies.
publications. In particular, the court resolution should serve the interests of the creditors and debtors of the company.

Furthermore the initiation of insolvency proceedings must be recorded in the land register (“Grundbuch”).

5. End of the procedure:

The procedure will end:
- when all assets have been realised and distributed among the creditors;
- after the preliminary measures are taken, investors may show interest in the insolvent company.

G. GREECE

In Greece, bankruptcy is governed by Articles 525 to 596 of the Greek Commercial Code and Act of 12 December 1878, amended by the Law of 22 February 1910 and the N.L. 635 of 1937.

1. Initiation of the proceedings:

Bankruptcy proceedings apply only to traders, whether individuals or companies.

They can be initiated by the debtor (who is obliged to do so by the law), a creditors or the court (exceptionally).

2. Criteria for the petition:

Cessation of payments is a pre-condition for bankruptcy. It refers to the permanent inability for the debtor to pay its due and entitled debts. It does not depend on the financial situation of the debtor but on the non-payment of his debts.

3. Effects:

The main effects of a bankruptcy judgement can be summarised as follows:

- a ‘Judge Rapporteur’ is appointed for the purposes of verifying the creditors’ claims and calling the general meeting of shareholders, that will protect the creditors’ interests during the proceedings;
- an Administrator is appointed for the purpose of representing, assisting and monitoring the debtor during the bankruptcy procedure, and to draw up a list of assets and liabilities in order to be distributed to the creditors;
- all proceedings based on ordinary claims are suspended (not claims secured by pledge, mortgage or lien);
- as regards the distribution of assets, secured creditors will be satisfied by preference and may only participate in the creditors’ meetings for the unsatisfied portion of their claims. The creditors’ meeting will attempt to reach a settlement with the debtor by means of a contract, on how to distribute the assets.

4. Publicity:
The declaration of bankruptcy must be published in the Lawyers’ Pension Fund Bulletin and the bankrupt’s name should be mentioned in a special registry.

5. **End of the procedure:**

The procedure is terminated when the bankrupt’s estate is liquidated, when the court decides to end it for lack of assets, or if a judicial composition is reached.

**H. IRELAND**

In Ireland, “compulsory liquidation” is governed by the Irish Companies (Consolidation) Act of 1908, the Companies Act of 1913, the Companies Act of 1963, the Companies Act of 1990 and the Company Law Enforcement Act of 2001.

1. **Initiation of the proceedings:**

The liquidation of an Irish company may result from a compulsory liquidation, ordered by the court, following the petition of the company itself, any creditor or the Director of Corporate Enforcement (an independent, state-funded agency, responsible for the enforcement of the Companies Act).

2. **Criteria for the petition:**

A petition for ‘compulsory liquidation’ may be initiated when a company is unable to pay its debts (e.g. when a creditor has obtained a judgement for debts but has been unsuccessful in attempting to execute it).

3. **Effects:**

The court will appoint a liquidator who will take over the management, wind up the company’s business, realise and distribute its assets (with a priority to preferential creditors or creditors whose claims are secured by a floating charge).

Once the company is declared to be liquidated there is a stay of all legal proceedings and executions of enforcement against the bankrupt’s property.

4. **Publicity:**

The application for liquidation proceedings must be published in local newspapers.

5. **End of the procedure:**

The procedure ends when the assets of the company have been completely wound up and the company is dissolved.

**I. ITALY**

In Italy, bankruptcy is governed by the Italian Royal Decree n° 267 of March 16, 1942 (also referred to as the Bankruptcy Act).
As the aim of the Italian legislator was clearly to protect the interest of creditors and to eliminate insolvent companies from the market by liquidating them, Italy has developed several insolvency procedures, whereas the restructuring of companies has not captured much of its attention.

The three major insolvency procedures in Italy will briefly be described, i.e. the liquidation bankruptcy ("fallimento"), the compulsory administrative liquidation ("liquidazione coatta amministrativa") and the extraordinary administration ("amministrazione straordinaria"). These procedures are often linked, as one procedure may lead to another.

I.1. Liquidation Bankruptcy

1. Initiation of the proceedings:

This procedure may only be initiated by private entrepreneurs with a substantial business organisation in terms of capital, work force and equipment. It excludes companies, public entities, agricultural entrepreneurs and small individual entrepreneurs from the application of liquidation bankruptcy.

It can be initiated by:
- the debtor
- a creditor
- the Public Prosecutor
- the Court.

2. Criteria for the petition:

In order to apply for this procedure, the private entrepreneur must be in a state of “functional impotence”, i.e. it is impossible to meet its financial obligations regularly and through normal business practices, due to a lack of liquidity and credit.

3. Effects:

As soon as the Court renders a judgement adjudicating the debtor bankrupt:
- a ‘bankruptcy trustee’ is appointed to realise the bankrupt’s property and to distribute it among the creditors;
- a ‘delegated judge’ is appointed to supervise the procedure;
- the creditors must lodge their claim;
- no execution measure may be taken against the bankrupt;
- Preferred and secured creditors (e.g. claims for the trustee’s fees, costs of judicial proceedings, employees’ wages…) will be paid prior to unsecured creditors.

4. Publicity:

The adjudication in “fallimento” is published in the Public Record kept by the court and the proceedings are published in the Register kept by the Chamber of Commerce accessible on line.
5. **End of the procedure:**

This procedure may lead to a creditors’ settlement\(^3\) and the bankrupt will then recover the possession and management of its assets.

Or, if such settlement could not be reached, the bankrupt’s business will be wound-up.

### 1.2. Compulsory administration liquidation

1. **Initiation of the proceedings:**

   This is an administrative procedure that only applies to certain categories of companies owned partially by the State or subject to the control of administrative authorities (e.g. banks, insurance companies...).

   It is initiated by the company itself.

2. **Criteria for the petition:**

   The company has a discretionary power to decide whether it needs to be removed from the market, not only in case of financial distress, but also for any problems that may jeopardise its ability to carry on business. In order to protect the rights of creditors and third parties, the Court may however check the insolvent status of the company.

3. **Effects:**

   When the company has declared that it wishes to initiate this procedure (and unless the court rejects such action):
   - a ‘liquidating commissioner’ (an administrative entity) is entrusted with the power to evaluate and liquidate the assets, and to distribute them amongst the creditors;
   - this commissioner is appointed and controlled by a public administrative body with the same powers and functions as the bankruptcy court.
   - the creditors will be reimbursed (secured and favoured creditors first) and they may appeal to the court against the distribution of the assets.

4. **Publicity:**

   The proceedings are carried out under the control of the Industry and Trade Ministry, whose decisions and orders are rendered by a Decree which is duly published in the *Gazetta Ufficiale della Republica*.

   The proceedings are also published in the Register kept by the Chamber of Commerce, which is accessible on line.

5. **End of the procedure:**

\(^3\) See above, Title 4. In such case, the bankrupt must have offered full payment of secured creditors and a pro-rata payment to unsecured creditors. A majority of creditors and the court must also have approved the bankrupts’ offer.

4.3. Legal consequences of bankruptcy and possibilities for a fresh start
Again, this procedure may result in a settlement by the creditors, or in a liquidation of the company.

I.3. Extraordinary administration

This procedure aims not only at satisfying creditors’ rights but also at reducing the negative effects of bankruptcy on a company’s work force, by trying to find an alternative solution to bankruptcy.

1. Initiation of the proceedings:

The extraordinary administration applies only to major companies (of at least 200 employees).

It can be triggered by:
- the debtor
- a creditor
- the Public Prosecutor
- the court.

2. Criteria for the petition:

In order for the court to accept the application for this procedure, the liabilities of the failing business must amount to at least one third of the total of its assets and its sales and services profits of the last financial year.

3. Effects:

The procedure starts with an observation period (of max. 2 months), during which a ‘judicial commissioner’ may be appointed to manage the company, under the supervision of the court; or the entrepreneur may keep its management power.

After this observation period, if it appears that no reorganisation procedure is possible, the procedure is converted into a liquidation bankruptcy procedure (see point I.1)

4. Publicity:

We refer to the compulsory administrative procedure. (point I.II)

5. End of the procedure:

See the liquidation bankruptcy procedure (point I.1).

J. LUXEMBOURG

4.3. Legal consequences of bankruptcy and possibilities for a fresh start
In Luxembourg, bankruptcy ("faillite") is governed by articles 437 to 592 of the Luxembourg Commercial Code.

1. **Initiation of the proceedings:**

Bankruptcy only applies to traders (whether companies or individuals).

It may be initiated by creditors, the court or the debtor himself (who is obliged to do so within one month from the cessation of payments).

2. **Criteria for the petition:**

Both of the following conditions must be met in order for bankruptcy to be ordered by the court:
- suspension of payments (the debtor can no longer pay his liquid and due debts ‘illiquidity’);
- Loss of credit worthiness (the debtor’s business is not trustworthy anymore).

3. **Effects:**

As soon as the court orders bankruptcy:
- he will appoint a judge to supervise the bankruptcy proceedings as well as a trustee who will take over the management of the business and who will draw up a state of the bankrupt’s assets;
- creditors must lodge and prove their claims;
- no individual action or execution may be taken against the debtor;
- interests on claims that are not secured stop accruing;
- the assets are distributed among the creditors in accordance with the distribution plan voted by them and signed by the court.

4. **Publicity:**

The bankruptcy judgement must be published in newspapers and displayed in the hearing rooms of the commercial court for a period of three months.

The public may also consult the company’s file at the commercial court.

5. **End of the procedure:**

The procedure is brought to an end when all assets are distributed and the company is liquidated.

It may also be closed if the assets are not sufficient to cover the administration and liquidation costs of the bankruptcy or if a composition after bankruptcy is reached.

**K. THE NETHERLANDS**

In the Netherlands, bankruptcy (or “faillissement”) is governed by the Dutch Bankruptcy Act of September 1, 1896 and its numerous amendments.
The Dutch legislation provides for three different legal procedures in relation to insolvency. The *suspension of payment* was discussed above (see Title 4), whereas the *debt restructuring* involves private individuals only and will not be further considered in this report⁵. We will briefly describe the *bankruptcy* procedure that applies to companies and individuals.

1. **Initiation of the proceedings:**

The proceedings can be initiated both against individuals and companies, by:
- the debtor himself;
- creditors (case law has established that there should be more than one creditor);
- the Public Prosecutor, in case the public interest is involved.

2. **Criteria for the petition:**

A declaration for bankruptcy requires the existence of facts and circumstances evidencing:
- that the debtor has ceased to pay, and
- that the debtor has several creditors.

3. **Effects:**

The opening of bankruptcy proceedings has the following effects:
- the court appoints a ‘*trustee*’ charged with the administration and liquidation of the bankruptcy estate. The bankrupt loses all free disposal and administration of its property;
- the court also appoints a ‘*bankruptcy judge*’ to supervises the administration and liquidation;
- creditors lodge their claim;
- secured creditors (mortgagees and pledges) may exercise their security rights as if bankruptcy had not taken place. If they wish to sell the secured goods, they must however do so through a public sale (which is likely to generate less proceeds than a private sale), or through a private sale but with the co-operation of the trustee;
- however, secured creditors (as well as third parties) are not allowed to exercise their rights if a “cooling down period” (i.e. period of up to one month (with a possible extension to two months) is ordered by the *bankruptcy judge*, during which claims of third parties or secured creditors against assets belonging to the bankruptcy estate may only be executed with the trustee’s authorisation);

4. **Publicity:**

The publicity surrounding insolvency proceedings consists of:
- the publication of the declaration of insolvency and the termination of the insolvency proceedings;
- the public register held by the court;
- notification with the Trade Registry

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⁵ See the Dutch report, p. 32-34.
5. **End of the procedure:**

The bankruptcy ends by:
- closing due to lack of assets;
- closing if the bankrupt is in a position to resume payment of its debts;
- a scheme of arrangement with the creditors.

**L. PORTUGAL**

In Portugal, bankruptcy ("insolvencia") is governed by the Bankruptcies Code of 1935 and the Decree-law of January 3, 1990

1. **Initiation of the proceedings:**

Bankruptcies apply only to “debtors holding an entrepreneurial organisation” (individuals or companies).

They are initiated by the debtor, a creditor, the Department of Public Prosecution or the court (if an opposition to the recovery procedure is lodged by creditors representing at least 51% of the recognised outstanding debts).

2. **Criteria for the petition:**

The company must be unable to meet its financial obligations in time because its available assets are insufficient to satisfy its current liabilities.

3. **Effects:**

Once bankruptcy has been ordered by the court:
- a ‘judicial liquidator’, in charge of the recovery and sale of the debtor’s assets, is appointed;
- ‘creditors’ committees’ are appointed to supervise the liquidator;
- suspension of execution measures;

4. **Publicity:**

Bankruptcy judgements are published.

5. **End of the procedure:**

The procedure ends when the company is liquidated (after all assets have been distributed) or where the creditors have agreed a recovery plan.

**M. SPAIN**

In Spain, bankruptcy (or “quiebra”) is governed by various legislation: the Spanish Commercial Code of 1885, the Civil Procedural Rules of 1881 and articles 1001 to 1177 of the former Commercial Code of 1829, which remains in force for the specific provisions on bankruptcy.
1. Initiation of the proceedings:

Bankruptcy proceedings apply to traders (whether individuals or companies).

They can be initiated by:
- the debtor himself ((following a legal obligation, when he is facing a situation of stay of payment of his debts);
- any legitimate creditor.

2. Criteria for the petition:

The business must be in a situation of “generalised stay of payments”, which is a broad concept defined case-by-case by the court, that corresponds to an economic imbalance whereby the business’ liabilities exceed its assets.

Examples of facts that have led to the opening of bankruptcy proceedings are:
- unsuccessful seizure of assets by a creditor;
- suspension of a payment if this suspension indicates that the business is insolvent;
- non-compliance by the business of a convention reached with its creditors, within the procedure of suspension of payments.

3. Effects:

The main effect of a bankruptcy order are:

- the appointment of several ‘mandatories’ (more than in foreign bankruptcy procedures):
  a) a ‘Depository’: responsible for the recovery of the bankrupt’s assets and for the management of its business until Receivers are appointed;
  b) a Creditors’ Meeting: that will vote on any proposal submitted by the debtor and approve the classification and ranking of debts. Receivers are appointed at this meeting;
  c) Receivers: creditors that represent the main body of creditors, manage and liquidate the bankruptcy estate. Unlike most bankruptcy procedures, the debtor’s assets are therefore managed by the creditors themselves;
  d) a ‘Commissioner’: delegate of the court who supervises the function of the Receivers;
- the creditors must declare their claim within a specific period of time;
- the assets are, after being recovered by the Depository, distributed among the creditors, following the ranking approved by the Creditors’ Meeting;
- secured creditors may however enforce their security separately.

4. Publicity:

The declaration of bankruptcy must be published in the Official Gazette and in certain newspapers, and registered in the Civil, Commercial and Property Registry.

5. End of the procedure:

The procedure is brought to an end when:
- all assets are distributed and the company is liquidated;
- the application for bankruptcy is dismissed for lack of assets or absence of creditors;
- a composition agreement is reached between the debtor and its creditors, within the bankruptcy procedure.

**N. SWEDEN**

In Sweden, bankruptcy ("konkurs") is governed by the Bankruptcy Act of 1987 and the Preferential Rights of Creditors Act (1979).

1. **Initiation of the proceedings:**

The Swedish *konkurs* applies to companies and individuals, traders or non traders.

It can be initiated either by the debtor or its creditors. When the *debtor* petitions for bankruptcy, it will be declared bankrupt the same day, whereas if the procedure is initiated by *creditors*, the company will be considered bankrupt only when the court declares it.

2. **Criteria for the petition:**

The debtor must be unable to pay its debts as they fall due and such inability must not be merely temporary.

3. **Effects:**

The court will appoint a receiver who will recover and realise the company’s assets, and distribute the proceeds among to the creditors. He will also take over the company’s management.

A dividend is distributed to preferential and secured creditors first. A particularity is that non-preferred creditors are not required to automatically declare and prove their claim. The receiver will ask them to lodge a proof of their claim only if it appears that they will receive a dividend after the preferential and secured creditors have been paid (this seldom occurs).

4. **Publicity:**

The declaration of bankruptcy is announced in the Swedish Official Gazette (the *Post- och Inrikes Tidningar*).

The bankruptcy is also recorded in an official register where all Swedish bankruptcies are gathered. The Patent and Registration office keeps this Register and the information is public and is open to inquiries by members of the general public.

5. **End of the procedure:**

The procedure is brought to an end when the receiver submits his final report and his dividend proposal to the court.
0. UNITED KINGDOM

In the United Kingdom, the Insolvency Act 1986 and the Insolvency Rules 1986, amended by the Insolvency Bill 2000, govern insolvent companies’ proceedings.

The term “bankruptcy” refers to the procedure applied only to individuals unable to pay their debts, and not to companies. It will not be discussed in this report.

In order to bring the existence of a company to an end and to distribute its assets, a compulsory or voluntary (not discussed here) liquidation may take place, sometimes through the mechanism of receivership.

0.1. Compulsory liquidation

1. Initiation of the proceedings:

Compulsory liquidation is initiated by the failing company itself, any creditor, a shareholder of the company and, in very limited circumstances, by the Department of Trade and Industry.

2. Criteria for the petition:

A petition for compulsory liquidation may be presented to the court on a number of grounds, usually on the ground that a company is unable to pay its debts (e.g. if it has neglected a demand of payment for more than £750 or if it is proved that the value of the company’s assets is less then the amount of its liabilities).

3. Effects:

When a winding-up order is made, the official receiver of the court becomes the liquidator of the company until meetings of creditors decide to appoint someone else. The directors’ powers will cease as from that moment.

No action can be started unless the leave of the court is obtained and any execution started after the commencement of a compulsory liquidation is void.

The liquidator will apply the proceeds of the realised assets and pay creditors, who are required to submit their claims (by sending particulars of it to the liquidator by way of a proof of debt) in the following order:

(a) creditors secured by a fixed charge or mortgage, out of the proceeds of the asset subject to the fixed charge or mortgage;
(b) the liquidator's costs and remuneration;
(c) preferential creditors (e.g. Inland Revenue, the Department of Social Security, occupational pension schemes and employees who are owed remuneration up to a set amount);
(d) creditors secured by a floating charge, out of the proceeds of the assets subject to the floating charge;
(e) unsecured creditors; and
(f) any claims arising from post-liquidation interest.

4. **End of the procedure:**

The procedure ends when all assets are liquidated and the company’s existence is brought to an end.

5. **Publicity:**

Once a winding up order has been made by the court, the official receiver (who is the liquidator until another liquidator is appointed) will file a copy of the order with the Registrar of Companies, ensure that the order is published in the government gazette and will advertise the order in a newspaper of his choice.

6. **Receivership:**

This procedure, discussed above in section 4.2, by which a creditor may appoint a receiver in order to realise his security, may also lead to a company’s liquidation.

**P. UNITED STATES**

U.S. companies can be either liquidated under Chapter 7 (usually smaller companies) or under Chapter 11 (typically large companies) of the Bankruptcy Code of 1978.

**P.1. Chapter 7 Liquidation**

1. **Initiation of the proceedings:**

The liquidation procedure under Chapter 7 applies to individuals, partnerships and corporations, excluding railroads, domestic or foreign insurance companies or banks.

The debtor can initiate the procedure (voluntary case) or by three or more of its creditors (holders of a claim against the debtor that is not a contingent liability or subject to a bona fide dispute) where the company has more than 12 creditors or a trustee representing such creditors. After a creditor group has filed a petition for a Chapter 7 case, the debtor has the right to oppose the petition in court, to either change it to a Chapter 11 case or dismiss the case.

2. **Criteria for the petition:**

The basis for filing a petition under Chapter 7 is similar to the filing of a petition under Chapter 11 and has been discussed under title 4.2.

3. **Effects:**

Under Chapter 7, the company stops all operations and goes completely out of business. A trustee is appointed to pursue any estate claim, liquidate the debtor’s assets, and distribute it to the creditors in order of priority; secured creditors first, then holders of administrative expense claims, holders of priority claims, employee claims, tax obligations, etc. and lastly holders of unsecured claims. A creditors committee
could be appointed, representing the unsecured creditor group, if the creditor group so decides.

4. **Publicity:**

The publicity generated from a bankruptcy filing is dependant on the size of the company and not on the type of chapter filing. Therefore, since most companies filing under Chapter 7 are smaller companies, the publicity generated is not as much as when a large company files under Chapter 11. Pleadings are filed with the Bankruptcy court and maintained by the clerk of the court in a docket that may be viewed by the public.

5. **End of the procedure:**

The procedure ends when all assets have been liquidated and distributed.

**P.2. Chapter 11**

A company can also liquidate its business under Chapter 11. During a liquidating Chapter 11 case, the debtor in possession attempts to sell or dispose of all or substantially all the assets of the debtor's estate, ordinarily as a going concern. The plan of reorganisation provides for the liquidation of any remaining assets and for the distribution of the proceeds of the liquidation.

Refer to Title 4.2 of the report regarding proceedings under Chapter 11 and the effects.

**P.3. Choice between Chapter 7 and Chapter 11**

A **debtor** may prefer liquidation in a chapter 11 case over liquidation in a chapter 7 case because (unless a chapter 11 trustee is appointed), the debtor will remain in control of its business and property may continue to operate while the liquidation is conducted. This may make it more likely to obtain going concern values rather than liquidation values.

**Creditors** may agree to a chapter 11 liquidation in order to avoid chapter 7 expenses, because they believe the debtor will be able to maximise the value of the its property better than a trustee unfamiliar with the debtor's business and property, or because the creditors committee plays a more important role in chapter 11 and tends to surrender its powers to a chapter 7 trustee.

**4.3.2.2. COMPARATIVE ANALYSIS**

The common aim of most countries’ bankruptcy procedures is to liquidate insolvent businesses. A comparison of the various bankruptcy procedures and its direct effect is discussed under the following sections:

A. Objective of the procedure:
B. Nature of the procedure
C. Quality of the debtor
D. Potential triggers for bankruptcy procedures
E. Possible initiators
F. Main effects of bankruptcy
G. Key players involved in the procedure
H. Creditors’ role and distribution of the assets
I. End of the procedure.

4.3. Objective of the procedures:

Traditionally, the objective of bankruptcy procedures was to sanction failing businesses that betrayed its creditors’ trust. The civil and criminal sanctions resulting from this betrayal, will be discussed in the next chapter (Chapter 4.3.3).

Three major trends have been observed:

- bankruptcy should only achieve one goal: maximum reimbursement of the debtor’s creditors;
- the desire to liquidate failing businesses as soon as possible, to ensure a stable market;
- it is more advantages to the stakeholders of the company (i.e. creditors and employees) that a failing business be saved and reorganised, rather than be liquidated. This help people realise that failing companies are not always liquidated and the stigma of bankruptcy could therefore be reduced.

These trends do not only result from policies followed by national governments, but also from historical considerations and from the date of the national legislation (bankruptcies in Austria, Greece, Italy and Spain are still based on rather old legal sources). Traditional legislation tends to punish failing businesses, whereas recent developments promote restructuring.

The majority of the countries analysed favour the first two trends (i.e. reimbursement of creditors and efficient liquidation of failing businesses).

In other countries, however, (such as France and Germany), the initiation of bankruptcy procedures begins with an observation period in order to determine the business’ best outcome: a traditional (liquidation) procedure or a restructuring procedure. Such perspective seems a good way to reduce the stigma on bankruptcy. That is, the announcement that a company has entered into bankruptcy proceedings should not be perceived that the company is to be liquidated, but rather that there is a chance of reorganisation. However, it is not clear whether the French and German citizens are aware of this aspect, or if to them, any bankruptcy procedure is assimilated as the end of a company. In line with countries such as France and Germany, the U.S. Bankruptcy code specifically makes a distinction between a reorganisation bankruptcy (Chapter 11) and a liquidation bankruptcy (Chapter 7). This distinguishes between a company that still has a chance to reorganise versus a company that is going out of business.

In other countries, (such as Austria, Italy, and the Netherlands) a creditors’ settlement or scheme of arrangement may be reached at the end of the procedure in which case the company will not be liquidated.
4.3. Legal consequences of bankruptcy and possibilities for a fresh start

<table>
<thead>
<tr>
<th>Country</th>
<th>Nature of the procedure</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>Creditor-oriented</td>
</tr>
<tr>
<td>Belgium</td>
<td>Creditor-oriented</td>
</tr>
<tr>
<td>Denmark</td>
<td>Creditor-oriented</td>
</tr>
<tr>
<td>Finland</td>
<td>Creditor-oriented</td>
</tr>
<tr>
<td>France</td>
<td>Creditor-oriented (unless it becomes a reorganisation</td>
</tr>
<tr>
<td></td>
<td>procedure: debtor-oriented)</td>
</tr>
<tr>
<td>Germany</td>
<td>Creditor-oriented (unless it becomes a reorganisation</td>
</tr>
<tr>
<td></td>
<td>procedure: debtor-oriented)</td>
</tr>
<tr>
<td>Greece</td>
<td>Creditor-oriented</td>
</tr>
<tr>
<td>Ireland</td>
<td>Creditor-oriented</td>
</tr>
<tr>
<td>Italy</td>
<td>liquidation bankruptcy and compulsory administrative</td>
</tr>
<tr>
<td></td>
<td>liquidation: creditor-oriented</td>
</tr>
<tr>
<td></td>
<td>extraordinary administration: debtor-oriented</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>Creditor-oriented</td>
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<tr>
<td>The Netherlands</td>
<td>Creditor-oriented</td>
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<tr>
<td>Portugal</td>
<td>Creditor-oriented</td>
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<tr>
<td>Spain</td>
<td>Creditor-oriented</td>
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<tr>
<td>Sweden</td>
<td>Creditor-oriented</td>
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<tr>
<td>UK</td>
<td>Creditor-oriented</td>
</tr>
<tr>
<td>USA</td>
<td>Creditor-oriented</td>
</tr>
</tbody>
</table>

B. Nature of the procedure:

A similarity between the various procedures results from the desire, in every country, to dispose of a regulated, formal and controlled procedure.

All procedures are of a judicial nature (except for Italy which also provides for an administrative procedure, that applies to State-owned companies only, which is controlled by administrative authorities). The courts responsible for bankruptcy proceedings are often specialised courts (such as in Germany, Italy and the U.S.). A special judge may even be appointed for every bankruptcy case. The court’s role varies: sometimes its only task is to provide a general control of the procedure, namely in bankruptcy proceedings where the creditors play an important role in the proceedings (Finland, Spain, Greece, Portugal), whereas in other countries (Germany, France, Italy, United Kingdom and mostly Austria), the court’s decisions strongly influence the outcome of the procedure.

Although it is important to have judiciary control and to allow the judge to decide on some issues, giving creditors the possibility to intervene and to propose a plan may be favorable to a positive outcome for the company. Their intervention and their
concessions could help save the company and therefore reduce the stigma on bankruptcy.

In all Member States and the U.S., a bankruptcy order is made by the court, in which it determines the moment of cessation of payments and appoints the persons (e.g. trustee, administrator, liquidator) responsible for the follow-up of the bankruptcy.

<table>
<thead>
<tr>
<th>JUDICIARY OR ADMINISTRATIVE PROCEDURE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
</tr>
<tr>
<td>Court very powerful.</td>
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<tr>
<td>Belgium</td>
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<tr>
<td>Judiciary.</td>
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<tr>
<td>Denmark</td>
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<tr>
<td>Judiciary.</td>
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<tr>
<td>Finland</td>
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<tr>
<td>Judiciary.</td>
</tr>
<tr>
<td>France</td>
</tr>
<tr>
<td>Mostly judiciary (two periods: observation period and liquidation or reorganisation procedure)</td>
</tr>
<tr>
<td>Germany</td>
</tr>
<tr>
<td>Judiciary (two periods: preliminary measures and liquidation or reorganisation)</td>
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<tr>
<td>Greece</td>
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<tr>
<td>Judiciary.</td>
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<tr>
<td>Ireland</td>
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<tr>
<td>Judiciary.</td>
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<tr>
<td>Italy</td>
</tr>
<tr>
<td>liquidation bankruptcy and extraordinary administration : judiciary compulsory administrative liquidation : administrative</td>
</tr>
<tr>
<td>Luxembourg</td>
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<tr>
<td>Judiciary.</td>
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<td>The Netherlands</td>
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<td>Judiciary.</td>
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<td>Judiciary.</td>
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<td>Spain</td>
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<td>Judiciary.</td>
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<td>UK</td>
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<tr>
<td>Judiciary.</td>
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<tr>
<td>USA</td>
</tr>
<tr>
<td>Judiciary.</td>
</tr>
</tbody>
</table>

C. Recognised types of debtor

The various country bankruptcy systems/regimes are not consistent with respect to the debtors that may initiate bankruptcy proceedings.

Most countries (Belgium, the Netherlands, Greece, Luxembourg, Portugal, Spain…) provide for a different procedure for traders and non-traders.

Some countries’ procedures apply either to companies or to individuals, whereas other countries’ procedures apply to both (e.g. Belgium, Finland, France, Germany, Greece). However, none of the countries’ bankruptcy proceedings apply to a state or to government institutions.
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

4.3. Legal consequences of bankruptcy and possibilities for a fresh start

<table>
<thead>
<tr>
<th>RECOGNISED TYPES OF DEBTOR</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
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<tr>
<td>Belgium</td>
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<td>Denmark</td>
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<tr>
<td>Finland</td>
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<td>France</td>
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<td>Germany</td>
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<td>Greece</td>
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<td>Italy</td>
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<td>Luxembourg</td>
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<td>The Netherlands</td>
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<td>Portugal</td>
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<td>Spain</td>
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<td>Sweden</td>
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<td>UK</td>
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<tr>
<td>USA</td>
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</tbody>
</table>

**D. Criteria to initiate bankruptcy procedures**

A debtors’ poor financial condition is the most common reason for companies going into bankruptcy. However, the bankruptcy procedures can only be initiated if certain criteria have been met. The strictness of the criteria differs significantly from country to country as discussed. The criteria can be generally summarised into the following categories:

- A cessation or suspension of payments, (France, Greece, Spain); or
- Insolvency/Over-indebtedness (Germany, Portugal, Italy); or
- Lost of creditworthiness; or
- Debtor unable to meet its obligations.

Some countries are quite strict and require that two conditions be met (Austria: illiquidity and over-indebtedness, Belgium: cessation of payments and lost of creditworthiness), whereas the criteria is applied more liberally in other countries, e.g. Germany, UK, U.S. and Ireland.
France provides that judicial liquidation may also be initiated as penalty against managerial misconduct (e.g. director found liable for all the debts of the company or for misappropriation of corporate funds).

It seems that the requirement of a strict criteria has a negative consequence, since it prohibits the debtor or its creditors from petitioning for bankruptcy. The debtor’s business will continue, with the possibility that its financial situation might worsen, resulting in diminishing value to creditors. However, petitioning for bankruptcy is an act filled with important consequences (the negative publicity being one of them) and it is therefore essential that the introduction of such procedure be controlled.

<table>
<thead>
<tr>
<th>CRITERIA TO INITIATE PROCEDURE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
</tr>
<tr>
<td>Illiquidity and over- indebtedness</td>
</tr>
<tr>
<td>Belgium</td>
</tr>
<tr>
<td>Cessation of payments and lost of creditworthiness</td>
</tr>
<tr>
<td>Denmark</td>
</tr>
<tr>
<td>Illiquidity (not being able to meet obligations as they fall due)</td>
</tr>
<tr>
<td>Finland</td>
</tr>
<tr>
<td>Voluntary: no criteria required</td>
</tr>
<tr>
<td>Involuntary: proof of one out of 6 legal conditions</td>
</tr>
<tr>
<td>France</td>
</tr>
<tr>
<td>Default of payment</td>
</tr>
<tr>
<td>Or breach of amicable settlement</td>
</tr>
<tr>
<td>Or penalties against managerial misconduct</td>
</tr>
<tr>
<td>Germany</td>
</tr>
<tr>
<td>Flexible: inability to pay any (minor) debt or liabilities exceeding assets</td>
</tr>
<tr>
<td>Greece</td>
</tr>
<tr>
<td>Cessation of payments only (financial situation not relevant)</td>
</tr>
<tr>
<td>Ireland</td>
</tr>
<tr>
<td>Flexible: debtor unable to pay its debts</td>
</tr>
<tr>
<td>Italy</td>
</tr>
<tr>
<td>Liquidation bankruptcy : functional impotence</td>
</tr>
<tr>
<td>Compulsory administrative liquidation : discretionary power of debtor</td>
</tr>
<tr>
<td>Extraordinary administration : liabilities equal to a third of the assets, sales and profits</td>
</tr>
<tr>
<td>Luxembourg</td>
</tr>
<tr>
<td>Suspension of payments and exhaustion of commercial debts</td>
</tr>
<tr>
<td>The Netherlands</td>
</tr>
<tr>
<td>Cessation of payments and other conditions</td>
</tr>
<tr>
<td>Portugal</td>
</tr>
<tr>
<td>Inability to meet obligations on time because assets are insufficient to satisfy liabilities</td>
</tr>
<tr>
<td>Spain</td>
</tr>
<tr>
<td>Flexible: generalised stay of payments</td>
</tr>
<tr>
<td>Sweden</td>
</tr>
<tr>
<td>Permanent inability to pay debts</td>
</tr>
<tr>
<td>UK</td>
</tr>
<tr>
<td>Flexible: inability to pay debts (in general) or other criteria</td>
</tr>
<tr>
<td>USA</td>
</tr>
<tr>
<td>Voluntary: no specific criteria</td>
</tr>
<tr>
<td>Involuntary: Flexible - debtor unable to meet its obligation</td>
</tr>
</tbody>
</table>

E. Possible initiators

The debtor, its creditor(s), the court or the Public Prosecutor can initiate bankruptcy procedures in most countries. However, in Belgium, Finland, Germany, Spain, U.S. and Sweden, the court alone do not initiate bankruptcy proceedings.
### INITIATORS OF THE PROCEDURE

<table>
<thead>
<tr>
<th>Country</th>
<th>Initiators</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>Debtor, Creditor, Court</td>
</tr>
<tr>
<td>Belgium</td>
<td>Debtor, Creditor, Public Prosecutor</td>
</tr>
<tr>
<td>Denmark</td>
<td>Debtor, Creditor</td>
</tr>
<tr>
<td>Finland</td>
<td>Debtor, Creditor</td>
</tr>
<tr>
<td>France</td>
<td>Debtor, Creditor, Court, Public Prosecutor</td>
</tr>
<tr>
<td>Germany</td>
<td>Debtor, Creditor</td>
</tr>
<tr>
<td>Greece</td>
<td>Debtor, Creditor, Court</td>
</tr>
<tr>
<td>Ireland</td>
<td>Debtor, Creditor, Director of corporate enforcement</td>
</tr>
<tr>
<td>Italy</td>
<td>Debtor, creditor, court, Public Prosecutor (liquidation bankruptcy), debtor only (compulsory administrative liquidation), debtor, creditor, court, Public Prosecutor (extraordinary administration)</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>Debtor, Creditor, Court</td>
</tr>
<tr>
<td>The Netherlands</td>
<td>Debtor, Creditors (more than one), Public Prosecutor</td>
</tr>
<tr>
<td>Portugal</td>
<td>Debtor, Creditor, Court, Public Prosecutor</td>
</tr>
<tr>
<td>Spain</td>
<td>Debtor, Creditor</td>
</tr>
<tr>
<td>Sweden</td>
<td>Debtor, Creditor</td>
</tr>
<tr>
<td>UK</td>
<td>Debtor, Creditor, Contributor, Department of Trade and industry</td>
</tr>
<tr>
<td>USA</td>
<td>Debtor, Three or more creditors or their trustee</td>
</tr>
</tbody>
</table>

**F. Main effects of bankruptcy:**

4.3. Legal consequences of bankruptcy and possibilities for a fresh start
As regards the debtor:

In most of the countries’ bankruptcy systems, the debtor loses control over its assets and a special person (trustee, receiver, administrator, or liquidator) assumes control of the estate and assets.

In Finland, where the creditors play an important role, the trustee is required to submit important decisions for the approval by the creditors’ meeting. Similarly in the U.S., since the trustee represents the unsecured creditors, the creditors committee has the right to consult with the trustee, make recommendations and submit questions regarding the liquidation of the debtor’s estate.

<table>
<thead>
<tr>
<th>MANAGEMENT OF THE BUSINESS DURING BANKRUPTENCY</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
</tr>
<tr>
<td>· Bankruptcy administrator</td>
</tr>
<tr>
<td>· Creditors’ committee</td>
</tr>
<tr>
<td>Belgium</td>
</tr>
<tr>
<td>· Receiver</td>
</tr>
<tr>
<td>Denmark</td>
</tr>
<tr>
<td>· Trustee</td>
</tr>
<tr>
<td>Finland</td>
</tr>
<tr>
<td>· Creditors’ meeting</td>
</tr>
<tr>
<td>France</td>
</tr>
<tr>
<td>· Trustee (during observation period) then liquidator</td>
</tr>
<tr>
<td>Germany</td>
</tr>
<tr>
<td>· Trustee or debtor (if court allows self-management)</td>
</tr>
<tr>
<td>Greece</td>
</tr>
<tr>
<td>· Administrator</td>
</tr>
<tr>
<td>Ireland</td>
</tr>
<tr>
<td>· Liquidator</td>
</tr>
<tr>
<td>Italy</td>
</tr>
<tr>
<td>· liquidation bankruptcy: bank, trustee</td>
</tr>
<tr>
<td>· compulsory administrative liquidation: liquidation commissioner</td>
</tr>
<tr>
<td>· extraordinary administration: judicial commissioner</td>
</tr>
<tr>
<td>Luxembourg</td>
</tr>
<tr>
<td>· Trustee</td>
</tr>
<tr>
<td>The Netherlands</td>
</tr>
<tr>
<td>· Trustee</td>
</tr>
<tr>
<td>Portugal</td>
</tr>
<tr>
<td>· Judicial liquidator</td>
</tr>
<tr>
<td>Spain</td>
</tr>
<tr>
<td>· Depository then receiver</td>
</tr>
<tr>
<td>Sweden</td>
</tr>
<tr>
<td>· Receiver</td>
</tr>
<tr>
<td>UK</td>
</tr>
<tr>
<td>· Liquidator</td>
</tr>
<tr>
<td>USA</td>
</tr>
<tr>
<td>· Trustee</td>
</tr>
</tbody>
</table>

As regards the creditors:

One of the main goals of bankruptcy procedures is to provide a means to equally distribute the assets among the creditors (depending on priority). Therefore a creditor that seeks execution of its claim before other creditors is not in line with the above

---

6 In Germany the court may order the debtor to self-management his business.
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

stated objective. In some countries, secured creditors typically receive payment on its claims before other creditors.

This is an automatic effect of all bankruptcy procedures, except for the Netherlands, where execution measures will be suspended only if the court has ordered a “cooling down period”.

In some countries (e.g. Finland), interest on the debtor’s debts continues to accrue, whereas in others (e.g. Belgium or France) such interest is suspended.

Other rules, regarding the compensation between debts-claims, the continuity of contractual commitments etc. vary from country to country.

**G. Key players involved in the procedure**

A number of key player or parties are involved when a company enters into bankruptcy, which includes:

- A trustee (also known as receiver, administrator or liquidator)
- A specialised judge or court (see point B.)
- Creditors Committees
- Other creditor group (e.g. secured or preferential creditors)

In the majority of the countries, these persons are court appointed; however in some countries, like Spain, the creditors have the authority to make these appointments.

The trustee is usually responsible for managing the debtor’s estate, liquidating the assets and the distribution to creditors. Some countries require that this trustee be a lawyer or an accountant.

In order to protect the creditors’ rights, some countries make provision that specific organisations represent the creditors: Austria - presence of a creditors’ assembly and control by the Association for the Protection of Creditors’ Rights; Finland, Greece, Spain, U.S. and Portugal - creditors’ committee. In other countries (e.g. Belgium, Luxembourg, Ireland), the creditors are not protected through such committees.

A particular appointed authority in Finland is the ‘Bankruptcy Ombudsman’, whose specific duty is to control the bankruptcy procedure. It is an independent and impartial authority that does not represent the creditors or the debtor.

<table>
<thead>
<tr>
<th>KEY PLAYERS INVOLVED IN THE PROCEDURE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
</tr>
<tr>
<td></td>
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<tr>
<td></td>
</tr>
<tr>
<td>Belgium</td>
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<td></td>
</tr>
</tbody>
</table>

4.3. Legal consequences of bankruptcy and possibilities for a fresh start

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H. Creditors’ role and distribution of the assets

In most countries creditors are usually requested, after the commencement of bankruptcy, to declare their claim within a specific period of time. These claims will then be accepted or partially/totally rejected, following a review by the court, the trustee (France and U.S), the debtor (Chapter 11 in the U.S.) or the creditors (Italy, Spain, Germany, and the Netherlands).

Generally the proceeds of the estates’ recovered assets (transformed into cash) is distributed to the creditors following a special priority:

- The debts arising after the introduction of the procedure (e.g. the procedural costs) are usually paid before any other debt.
- In most countries, the law determines the order of payment, usually based on a system of prior payment to owners of securities, privileges, floating charges or

<table>
<thead>
<tr>
<th>Country</th>
<th>Role(s)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Denmark</td>
<td>Trustee</td>
</tr>
<tr>
<td>Finland</td>
<td>Provisional administrator (becomes trustee)</td>
</tr>
<tr>
<td></td>
<td>Creditors’ meetings</td>
</tr>
<tr>
<td></td>
<td>Ombudsman</td>
</tr>
<tr>
<td>France</td>
<td>Liquidator</td>
</tr>
<tr>
<td></td>
<td>Insolvency judge</td>
</tr>
<tr>
<td>Germany</td>
<td>Preliminary trustee (becomes final trustee)</td>
</tr>
<tr>
<td></td>
<td>Court</td>
</tr>
<tr>
<td>Greece</td>
<td>Judge rapporteur</td>
</tr>
<tr>
<td></td>
<td>Administrator</td>
</tr>
<tr>
<td></td>
<td>Creditors’ meeting</td>
</tr>
<tr>
<td>Ireland</td>
<td>Liquidator</td>
</tr>
<tr>
<td></td>
<td>Court</td>
</tr>
<tr>
<td>Italy</td>
<td>Trustee</td>
</tr>
<tr>
<td></td>
<td>Bankruptcy judge</td>
</tr>
<tr>
<td></td>
<td>Creditors’ committees</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>Trustee</td>
</tr>
<tr>
<td></td>
<td>Judge</td>
</tr>
<tr>
<td>The Netherlands</td>
<td>Bankruptcy judge</td>
</tr>
<tr>
<td></td>
<td>Creditors’ committees</td>
</tr>
<tr>
<td>Portugal</td>
<td>Judicial liquidator</td>
</tr>
<tr>
<td></td>
<td>Creditors’ committees</td>
</tr>
<tr>
<td>Spain</td>
<td>Depository</td>
</tr>
<tr>
<td></td>
<td>Creditors’ meeting</td>
</tr>
<tr>
<td></td>
<td>Receivers</td>
</tr>
<tr>
<td></td>
<td>Commissioner</td>
</tr>
<tr>
<td>Sweden</td>
<td>Receiver</td>
</tr>
<tr>
<td>UK</td>
<td>Liquidator</td>
</tr>
<tr>
<td></td>
<td>Creditors’ meeting</td>
</tr>
<tr>
<td></td>
<td>Contributors’ meeting</td>
</tr>
<tr>
<td>USA</td>
<td>Trustee</td>
</tr>
<tr>
<td></td>
<td>Judge</td>
</tr>
<tr>
<td></td>
<td>Creditors Committee</td>
</tr>
</tbody>
</table>

4.3. Legal consequences of bankruptcy and possibilities for a fresh start
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

4.3. Legal consequences of bankruptcy and possibilities for a fresh start

Rights of ownership; followed by a pro rata payment to the other non-preferential creditors. The latter sometimes receive no payment after the preferred creditors have been paid. The Swedish system provides, in contrary to other countries, that non-preferential creditors are not even required to declare their claim except if it appears that they will receive a dividend. Similar to the Swedish system, in a Chapter 7 liquidation in the U.S., where a company has no unsecured assets, the unsecured creditor also is not required to file a claim.

This inability for unsecured creditors to be paid after secured creditors is an essential point in the stigma surrounding bankruptcy. Who would wish to have contractual relationship with a company, knowing that if this company went bankrupt, all debts which are outstanding would be lost? All creditors would accordingly try to have a security but it is impossible to provide securities to everyone. In other countries (Austria, Greece), the distribution to creditors results from a bankruptcy plan or settlement submitted for the creditors’ approval. However, even in this case, secured creditors have a right to be paid first, the same problem still subsists.

<table>
<thead>
<tr>
<th>Country</th>
<th>Declaration of claim</th>
<th>Distribution</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>Declaration of claim</td>
<td>Distribution: following the distribution plan drafted by the bankruptcy administrator and approved by the creditors’ committee</td>
</tr>
<tr>
<td>Belgium</td>
<td>Declaration of claim</td>
<td>Distribution: secured claims prior to others</td>
</tr>
<tr>
<td>Denmark</td>
<td>Declaration of claim</td>
<td>Distribution following a specific order</td>
</tr>
<tr>
<td>Finland</td>
<td>Declaration of claim</td>
<td>Secured claims prior to others</td>
</tr>
<tr>
<td>France</td>
<td>Declaration of claim</td>
<td>Distribution following a specific order (waged workers, then legal expenses, then creditors with pledges or mortgages…)</td>
</tr>
<tr>
<td>Germany</td>
<td>Declaration of claim</td>
<td>Special rules of distribution: right of ownership first, secured creditors and others afterwards</td>
</tr>
<tr>
<td>Greece</td>
<td>Declaration of claim</td>
<td>Distribution: priority to secured creditors and settlement with creditors on distribution</td>
</tr>
<tr>
<td>Ireland</td>
<td>Declaration of claim</td>
<td>Distribution following a specific order (preferential and secured creditors first)</td>
</tr>
<tr>
<td>Italy</td>
<td>liquidation bankruptcy: Declaration of claim</td>
<td>Distribution: specific order (preferred and secured creditors first) Compendious administrative liquidation: Declaration of claim</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>Declaration of claim</td>
<td>Distribution: specific order</td>
</tr>
</tbody>
</table>
Bankruptcy process is usually concluded after all assets have been liquidated and distributed and administration of the liquidation of the company is completed; or, when a restructuring plan has been successfully adopted; or, as in most countries, when it becomes evident that the assets of the business are insufficient to cover the procedural costs.

### 4.3.3. FURTHER CONSEQUENCES OF BANKRUPTCY AND CAUSES OF THE STIGMA ON FAILURE AND POSSIBILITIES FOR A FRESH START?

Apart from the liquidation and distribution of the debtor’s assets as a result from bankruptcy procedures, the management of a bankrupt company may also be held civilly or criminally liable. In some cases, special prohibitions will refrain entrepreneurs from starting a new business.

However, in circumstances, described hereunder, that varies in every country, debtors may benefit from “excusability” (i.e. a procedure that will provide for the discharge of payment of their remaining debts and/or the release of certain prohibitions). This excusability will make it easier for the debtor to initiate a “fresh start” of a business.

### 4.3.3.1. OVERVIEW OF NATIONAL PROCEDURES

Every national system applies specific restrictions to debtors and provide for various conditions in order to grant “excusability”.

The negative consequences resulting from bankruptcy are analysed in light of the following topics:
- liability for remaining debts (bankrupts are not always discharged from unpaid debts. Such debts may sometimes be satisfied with the assets or income that the bankrupt may acquire in the future.)
- criminal offences or
- exclusion from certain professional activities.

The analysis will focus on sole proprietors and the directors of the companies, because the negative consequences have no practical relevance to the legal entities, since it usually is dissolved at the end of the process. The founders or partners of a limited liability company are usually liable only to the amount of capital invested.

A. AUSTRIA

1. Negative consequences of bankruptcy

   a) Director’s liability for the remaining debts

   An important effect of bankruptcy is that creditors may continue to bring individual actions against the directors of a bankrupt company. This is the case, for example, if the directors did not file for judicial insolvency proceedings in due time, where they can be held liable for part/ the total of the company’s debts.

   b) Criminal offences

   Directors may be held criminally liable if they did not respect the essential principle of equal treatment of equal creditors.

   c) Professional interdictions

   Directors may also be prohibited from engaging in an independent trade or business, after a bankruptcy. Exemptions are however applicable (upon proof that they are likely to fill their obligations as regards the intended business and the settlement of previous debts).
   Directors are, however, not excluded from being director of another company.

2. Excusability and possibility for a fresh start

   A discharge from these negative consequences of bankruptcy may be obtained only:
   - if the bankruptcy proceedings are converted into reorganisation proceedings;
   - or in the course of private bankruptcies (that apply to individual non-traders only).

   The Austrian system seems to be quite severe as regards the limitations to excuse bankrupt entrepreneurs. If no reorganisation is possible, they may not be excused. This is quite unfair for “innocent” bankrupts who were lead to bankruptcy by misfortune.

   This could be an important cause of the stigma on bankruptcy: why start a business knowing that if you fail and become bankrupt, your creditors may continue to sue you forever?

   However, this negative effect will concretely not always affect the directors of bankrupt companies, for bankrupt companies are usually liquidated after the proceedings, so there is no company left for the payment of debts preceding
bankruptcy (unless the directors are held civilly or criminally liable for the company’s debts, as mentioned above).

B. BELGIUM

1. Negative consequences of bankruptcy

a) Directors’ liability for the remaining debts

A bankrupt company’s directors responsibility may be invoked, and they can be declared liable for all or part of the company’s debts in several circumstances, such as:

- if they committed a serious fault that led to the bankruptcy,
- if they did not declare bankruptcy on time (or failed to convene a meeting of shareholders to deliberate, when the net assets of the company had fallen down below half of its share capital).

Such responsibility may go far, in situations where the bankrupt company is only a screen, hiding the “real master” of the company (i.e. the person or company owning most of the bankrupt company’s shares and taking important decisions, and whose assets and activities are mixed with those of the bankrupt company). In such cases, the liability may be extended to the “real master” of the business.

If their company’s bankruptcy has caused a damage to a third party, the liability of its directors could be engaged, which may lead to serious financial sanctions.

The founders of a bankrupt company may be held liable for part or all the liabilities of the company, in case its registered capital was manifestly insufficient to ensure its normal activities during at least two years.

b) Criminal offences

Entering into contractual relations without sufficient counterpart, misappropriating or concealing assets, and fraudulently organising an insolvency… are some of the possible criminal offences sanctioned by Belgian law.

c) Professional interdictions

Directors of a bankrupt company may be banned from the exercise of certain professions (such as the profession of auditor) or certain mandates (e.g. the management of an insurance company).

2. Excusability and possibility of a fresh start:
Excusable bankrupts are those that failed because of misfortune or because of certain circumstances in life, and that co-operated during the bankruptcy procedures. Excusability is decided by the court that has a wide margin of interpretation.

If a bankrupt is excused, he will be discharged from his remaining debts. None of his creditors may institute proceedings against him, except for his future debts (that arise after the bankruptcy procedure).

This procedure seems to be a good way to reduce the stigma on bankruptcy and to favour fresh starts, especially since Belgian courts are usually ready to grant excusability to those who “deserve” it, those who failed because of misfortune or because of certain circumstances of life.

C. DENMARK

1. Negative consequences of bankruptcy

a) Directors’ liability for the remaining debts

After bankruptcy/winding-up proceedings, creditors regain their right against the bankrupt to the part of the claim that was not paid through distribution, unlike in compulsory composition where the bankrupt is released of all debts not accepted in the composition.

Directors of a bankrupt company face several civil sanctions:
- they may be forced to repay up to five years’ of bonuses granted while the company was insolvent;
- the liquidator may bring an action for damage against them, even if they were discharged, within 2 years after the date of the discharge;
- creditors who did not receive payment and who prove that the directors had foreseen the company’s impending liquidation, may claim reimbursement of his loss.

Creditors may also sue them if the assets have not been distributed equally.

b) Criminal offences

They may also be convicted of economic crime if they illegally removed the company’s assets from a company bought for the purpose of preventing assets being recovered, after which the company may be dissolved.

2. Excusability and possibility for a fresh start

Bankrupts still liable for the remaining debts not paid through bankruptcy proceedings, may obtain discharge of debt if they are excused after 5 or 20 years (depending on the type of debt and whether special legal steps were taken to secure it).
Directors may also obtain debt rescheduling if they can prove that they are not able and not expected to be able to fulfil their debt obligations in the next few years, and that their circumstances speak in favour hereof.

D. FINLAND

1. Negative consequences of bankruptcy

   a) Directors’ liability for the remaining debts

   Directors may be held liable for part or all of the company’s debts if they did not file for bankruptcy on time or if they did not convene a meeting of shareholders when the company’s equity decreased below half of its share capital.

   They may also be held liable to compensate a loss caused through an error or negligence while performing their duties.

   b) Criminal offences

   Directors intentionally acting to the detriment of the interest of their creditors (destroying their property, transferring it abroad in order to make it unreachable to their creditors…) may be criminally sanctioned.

   c) Professional interdictions

   Prohibition on certain business activities may result from bankruptcy.

2. Excusability and possibility for a fresh start

   Approximately three-quarters of all persons who have been involved in bankruptcy are still in business\(^7\), for directors who have not committed the above-mentioned faults will not be liable for the remaining debts. As for other entrepreneurs, they remain liable for their remaining debts, which may cause a long and vicious circle of debt collection. There has been a vivid discussion about the excusability of debts after 10 or 15 years, but to date there does not exist such provisions.

E. FRANCE

1. Negative consequences of bankruptcy

   a) Directors’ liability for the remaining debts

       A. Reimbursement of debt:

       In case of mismanagement that contributed to the insufficiency of assets of their company, the directors may be ordered to reimburse all or part of the company’s debts.

---

\(^7\) According to the author of the Finish report.
B. Involuntary bankruptcy:
Directors not respecting the above-mentioned reimbursement of debts or who misappropriated corporate funds, committed self dealing, may be sued in an involuntary bankruptcy procedure, independent from the company’s bankruptcy proceedings.

C. Personal bankruptcy:
If the directors do not reimburse debts imposed to them by the court, if the court decides to include their assets for the reimbursement of creditors, or if they violate a restriction on management imposed to them, a declaration of personal bankruptcy could apply to them. The consequences of this declaration is that they will be prohibited from managing companies with a commercial purpose, lose civil rights and be ineligible for positions before the commercial courts.

b) Criminal offences
Criminal penalties may apply to individuals who organised fraudulent bankruptcies, e.g. who fraudulently obtained funding or sold assets below their value in order to avoid bankruptcy.

c) Professional interdictions
The court may decide that persons subject to fraudulent bankruptcy may no longer practice certain activities.

2. Excusability and possibility of a fresh start:
Directors of a bankrupt company may, although pecuniary penalties have been imposed on them, continue their activities within the entity or the ongoing entity itself, if restructuring resulted from bankruptcy proceedings. This will not be the case if civil or criminal sanctions were imposed on them.

They are usually discharged from payment of the debts not satisfied by the liquidator, unless, for example, they committed criminal offences or fraud with respect to creditors, or in the case of personal bankruptcy.

The French system therefore makes a distinction between “innocent” and “voluntary or fraudulent” bankruptcy, as regards the consequences that such bankruptcies may have on the possibility for entrepreneurs or directors to continue their activities or to start new businesses.

F. GERMANY

1. Negative consequences of bankruptcy

a) Director’s liability for the remaining debts
Directors who failed to petition for bankruptcy proceedings when they should have (within three weeks as from the date on which the company became bankrupt)
bankruptcy), could be held personally liable for the resulting losses incurred by the company.

b) Criminal offences:

The German Criminal Code specifically provides for criminal insolvency offences: directors who fail to exercise the diligence expected from responsible businessmen or who committed fraudulent insolvencies may be liable to a prison term.

Directors who did not call a shareholders’ meeting when half or more of the company’s capital was eroded, may be liable to a prison term of up to three years or a fine.

c) Professional interdictions

Directors who committed a criminal offence are prohibited to practice for 5 years.

2. Excusability and possibility of a fresh start:

Individual customers may, under the customer insolvency procedure, benefit from a debt release granted by the insolvency court, if they have shown their good behavior during 6 years. Such judicial debt release does not exist for bankrupt companies which are usually wound up and whose directors will only be held liable in the above mentioned circumstances.

G. GREECE

A particularity of the Greek system is that, in some aspects, it is much more severe towards individual bankrupts than towards the directors of a bankrupt company.

1. Negative consequences of bankruptcy

a) Directors’ liability for the remaining debts

A. If a director’s conduct causes damage to the bankrupt company, the Board of directors (and not the company’s creditors or shareholders) may sue him. In case of bankruptcy, this possibility will be transferred to the administrator of the bankruptcy (who seldom pursue the director, due to the difficulty of finding evidence and the high costs resulting from judicial proceedings, and mostly because such proceedings do not affect the status of the director;

B. Creditors may however sue directors following the general rules of tort (proof of a damage may be based on the fact that directors have intentionally violated the rules imposed on them by bankruptcy law.)

C. They may also sue them if they prove that they have suffered damage because the directors did not notify them of their company’s cessation of payment, which is a legal obligation.

b) Criminal offences

4.3. Legal consequences of bankruptcy and possibilities for a fresh start
Directors may be convicted of plain bankruptcy, when they provoked bankruptcy through their faulty behaviour.

In case of a fraudulent bankruptcy, the court may order the bankrupt’s physical detention or house confinement, in order to ensure his physical availability during the bankruptcy procedure.

c) Professional interdictions

Only individual bankrupt lose their trading capacity and are therefore excluded from any commercial or industrial profession. They also face the prohibition of exercising certain functions (i.e. civil servant in the administrative, judicial and public sector, custodian, lawyer or official administrative, employees in a company of public law);

2. Excusability and possibility for a fresh start

Under Greek law, directors are not considered as merchants and may therefore never be declared personally bankrupt. They merely represent a company and although most of the time, due to their wrong judgements, they are responsible for a company’s bankruptcy, they are not professionally affected since they are free to start a new business, be appointed as directors or work as independent entrepreneurs.

Individual bankrupts are, however, as mentioned above, deprived from their status of merchant and incapable of starting a new commercial business. In order to obtain discharge of bankruptcy and to recover their status of merchant, one of the following conditions must be filled:
- a lapse of 10 years from the date of the bankruptcy’s declaration (long period of time);
- a judicial composition amongst the creditors, validated by the court, not subject to appeal and not declared void;
- full satisfaction of all creditors (unlikely to occur, since the entrepreneur who is declared bankrupt does not usually have enough assets to satisfy his creditors).

If one of these conditions is fulfilled (which rarely is the case), the court has the obligation to discharge the individual bankrupt. No discharge may however be granted in case of fraudulent bankruptcy.

As a conclusion, it appears that the Greek system creates a very important stigma on bankruptcy as regards individual entrepreneurs, who have little chance of starting a commercial business again (even though they are considered as “innocent bankrupts”). To the contrary, the directors are not very affected by their company’s bankruptcy, for their status is unchanged and they will be forced to reimburse their creditors only if the latter prove that they have suffered damage because of their acts. Such conception stimulates the trend to practice business activities through a company, and not as individual entrepreneurs.
H. IRELAND

1. Negative consequences of bankruptcy

a) Directors’ liability for the remaining debts

Directors may be made personally liable for all or part of the company’s debts, in case of:
   - *Fraudulent trading*: acting with the intent to defraud creditors (civil and criminal offence);
   - *Reckless trading*: carrying out a company’s business in a reckless manner (i.e. with “gross carelessness”);
   - *Misfeasance proceedings*: retaining the company’s money or property, being guilty of misfeasance or breach of duty or trust in relation to the company;
   - *Return of improperly transferred assets*: obligation to return company’s property that was disposed of in order to perpetrate a fraud on the company, its creditors or members;
   - *Failure to keep proper books and records*: contravention to the obligation to keep proper books of accounts, that resulted to the company’s inability to pay all its debts (or its winding up) or caused a substantial uncertainty as to its assets and liabilities.

b) Criminal offences

Directors of a bankrupt company may be criminally sued if they committed fraud, dishonesty, …

c) Professional interdictions

   - *Restriction of directors*
     Any person who was a director of an insolvent company within twelve month of its winding up, may not be appointed as a directors of a company or take part in the incorporation of a new company for a term of five years, unless:
     - such company has a share capital of a certain amount,\(^8\)
     - or unless that person proves that he has acted honestly and responsibly or that he was director of the company solely by reason of his nomination and without taking part of the management.

   - *Disqualification of directors*
     Directors who were convicted of an indictable offence (see above) in relation to a company, may not be appointed as a directors of a company or take part in the incorporation of a new company for a term of five years.

2. Excusability and possibility for a fresh start

I. ITALY

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\(^8\) EUR 63.487 (or EUR 317.435 for public limited companies).
1. Negative consequences of bankruptcy

a) Directors liability for the remaining debts

Under Italian law, directors have a special duty to act in protection of the company’s creditors. The breach of such duty will automatically trigger their liability.

In the context of a bankruptcy, such breach of duty could arise from:
- the payment with preference to certain creditors;
- negligence, imprudence or technical incompetence that lead to the reduction of the company’s assets, to detriment of the creditors’ interests.

Claims for damages could also be grounded on the breach of a specific rule (i.e. the duty to convene a shareholders’ meeting in the event of severe loss).

b) Criminal offences

Directors of a bankrupt company may be applied “bankruptcy crimes”, such as:
- fraudulent bankruptcy offence (when the directors have concealed property, made false statements, fraudulent disposal of assets in favour of some creditors…);
- obtaining credit in order to conceal the insolvency;
- concealing bankruptcy assets, making false statements…

c) Professional interdictions

Bankrupts are unable to exercise certain professions (i.e. attorney at law or stockbroker), or to assume certain charges (trustee, tax collector, director, statutory auditor and liquidator of a company).
If bankruptcy crimes have been applied, they may be prohibited from exercising entrepreneurs’ activities for ten years.

2. Excusability and possibility for a fresh start

Directors of a bankrupt company may usually continue business activities, unless that have been applied the professional activities.

Bankrupts could benefit from a judicial discharge. Such discharge may be obtained only if the bankrupt:
- has integrally paid his debts;
- or has regularly fulfilled its obligations from the creditor’s settlement procedure;
- or has effectively and continuously proved his good behaviour for at least five years from the end of the bankruptcy procedure.

This discharge may never be granted if the bankrupt was found guilty of bankruptcy crimes or crimes against the patrimony, the public faith, the industry and the commerce.
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

J. LUXEMBOURG

1. Negative consequences of bankruptcy

   a) Directors liability for the remaining debts

   Directors of a bankrupt company may be held civilly liable for any misconduct in their management (the company may sue them in order to obtain reimbursement) or for the non-compliance of the law of August 10, 1915 or the company’s statutes (the company, the trustee or any third party may sue them jointly, e.g. in case of failure to convene a general meeting when needed, to publish the annual accounts…).

   If they committed a gross and indisputable mistake that contributed to the company’s bankruptcy, they may be ordered to pay all or part of the company’s debts.

   They may also be declared personally bankrupt under certain conditions (if they dispose of the company’s assets in their personal interest, continue a deficient exploitation…).

   b) Criminal offences:

   - in case of simple bankruptcy:
     the bankrupt may be sanctioned by imprisonment for a term between one month and two years, if it is discovered during the bankruptcy procedure, that he has committed a criminal offence, such as: payment to a favoured creditor to the detriment others, not declaring bankruptcy when required to, not keeping regular accountancy…
   - in case of fraudulent bankruptcy:
     the crime of fraudulent bankruptcy may be imposed if the bankrupt has removed records or falsified their content, if he has concealed part of his assets or if he states that he was debtor of sums while he was not. He will be sentenced to imprisonment for a term of five to ten years.

   c) Professional interdictions

   The bankrupt may be prohibited from performing a business activity (including being director of a company), for a period of one to twenty years, if:
   - the trustee or public prosecutor request it within three years from the judgement declaring bankruptcy;
   - the bankrupt has contributed by a gross and indisputable mistake to the bankruptcy, mistake that no diligent and careful director would commit.

   It automatically applies to any person convicted of fraudulent bankruptcy.

2. Excusability and possibility for a fresh start

   If the debtor’s assets were insufficient to cover the liquidation costs of bankruptcy, this procedure is closed and the creditors may still sue the insolvent entrepreneur. This constitutes an important obstacle to the possibility to start a new business.
Another element is that a bankrupt could continue its business or start new commercial activities only in the following circumstances:
- if he manages to negotiate a composition after bankruptcy with his creditors (and if he was not sentenced for fraudulent bankruptcy)
- if he is rehabilitated by the court, (i.e. if he has totally paid his debts and if he is not a fraudulent bankrupt nor has been sentenced for robbery, speculation or breach of trust).

It seems difficult for individual bankrupts who have lost all their assets to obtain a composition after bankruptcy or to pay all of their debts! Therefore, entrepreneurs/directors who were sanctioned through by prohibiting further commercial activities may seldom be rehabilitated and start a new business again… Luckily, this sanction is not automatic and does not apply to “innocent” bankrupts, who did not commit any gross and indisputable mistake.

K. **THE NETHERLANDS**

1. **Negative consequences of bankruptcy**

   a) **Director’s liability for the remaining debts**

   The directors may be jointly liable towards the company if they failed to properly perform their duty and if this failure contributed to the bankruptcy of the company (e.g. acts contrary to the company’s object, disproportionately large securities provided to banks in order to obtain credits…).

   Certain creditors (tax authorities, social insurance and pension funds) may sue the directors of a bankrupt company for any outstanding tax, if the latter failed to notify these creditors in a timely manner, as legally required, of the company’s inability to pay them.

   Creditors may also sue them for other unlawful acts (e.g. undertaking an obligation on behalf of the company knowing that the company would not be able to fulfil it).

   b) **Criminal offences**

   Directors who do not, during the bankruptcy proceedings, respect their obligation to provide the trustee, the bankruptcy judge and the creditors’ committee with the required information may be criminally sanctioned.

   Other criminal offences linked to bankruptcy are:
   - prejudicing one creditor above the others;
   - transferring assets below their value;
   - not taking account of certain assets or withdrawing assets from the estate.

   c) **Professional interdictions**

   In order to start a new business, individual bankrupts and directors must obtain a “declaration of non-objection” by the Ministry of Justice, with regard to the
incorporation of a new company. Such declaration is difficult to obtain if the founders were previously involved in fraudulent businesses/bankruptcies or if they leave behind a trail of bankruptcies. This declaration will also be refused if there is reasonable doubt with regard to the reliability or the integrity of the individual.

2. **Excusability and possibility for a fresh start**

Bankrupts do not benefit from an automatic discharge of payment of their remaining debts, at the end of the bankruptcy procedure. They will only be released from their debts if they have reached a scheme of arrangements with their creditors. The Debt Restructuring of Private Individuals Act aims at helping them liquidate their assets in such a way that they will negotiate with creditors to obtain full discharge of their debts. This arrangement may include the transfer of their business to a third party.

As regards the possibility to start a new business, both individual bankrupts and directors are confronted with the requirement of obtaining a “declaration of non-objection” as explained above.

**L. PORTUGAL**

1. **Negative consequences of bankruptcy**

   a) **Directors’ liability for the remaining debts**

   Directors who have significantly contributed to the bankruptcy of their company through actions performed within the last two years previous to the declaration of bankruptcy, may be declared responsible for the bankrupt’s debts (if requested by the public prosecutor or any creditor).

   b) **Criminal offences**

   - Crime of fraudulent bankruptcy: committed by directors who, with the intention to cause detriment to their creditors, destroy or hide their assets, artificially aggravate losses…
   - Crime of negligent insolvency: committed by directors who created a state of insolvency through serious negligence or imprudence and failed to apply for any recovery measures on time.
   - Crime of favouring creditors: committed by directors, aware of their state of insolvency, who favoured certain creditors to the detriment of others.

   c) **Professional interdictions**

   As from the declaration of bankruptcy (and if no agreement was found to satisfy its creditors), individual bankrupts and directors of bankrupt companies are prohibited from carrying on any business, unless the judge recognises that they acted correctly and with normal diligence in the exercise of their activity, and if no criminal proceedings have been started.

2. **Excusability and possibility for a fresh start**
The possibility to start a new business is limited by the above-mentioned prohibition that may apply to bankrupts. This prohibition can however be set aside if the judge expressly authorises the bankrupt to practice a business in order for him to earn the indispensable means of sustenance and if such practice does not adversely prejudice the liquidation of the bankrupt’s estate.

**M. SPAIN**

Spanish bankruptcies are qualified by the judge, according to the bankrupt’s conduct, as follows:

- **fortuitous** bankruptcy: accidental bankruptcy, produced by the misfortune of a debtor with good commercial management of his business.
- **tortuous** bankruptcy: caused by a negligent debtor who lacked diligence in the administration of its business and the respect of basic commercial rules.
- **fraudulent** bankruptcy: caused by the debtor’s intentional illegal acts (e.g. concealment of all or part of its assets, abuse of confidence to the detriment of third parties…).

Only fortuitous bankruptcies are exempted from criminal liabilities. Fortuitous and tortuous bankruptcies allow the bankrupt to reach agreements with his creditors and to request rehabilitation.

1. **Negative consequences of bankruptcy**

   a) **Directors’ liability for the remaining debts**

   In cases where the directors did not file for bankruptcy when they should have, the bankruptcy will be qualified as tortuous and the management will be held liable.

   b) **Criminal offences**

   Insolvency due to negligent conduct, tort, provoking, hiding or aggravation one’s bankruptcy are criminal offences. Directors can therefore be imposed criminal sanctions if they have caused the insolvency or provided false information regarding the company’s accounts. Should they wish to start a new business or manage another company, they will have to comply with their criminal sanction before starting it.

   c) **Professional interdictions**

   After the bankruptcy proceedings, bankrupts are barred from engaging in any business in the future, unless they are rehabilitated (see above).

2. **Excusability and possibility for a fresh start:**

   After the closing of fortuitous or tortuous bankruptcy proceedings, the bankrupt may request its rehabilitation, in order to engage into business again.
This rehabilitation is not automatic. The latter must request it to the judge, under the following conditions:
- all debts must be paid or an arrangement with the creditors must be obtained
- in the event the bankrupt is also charged with criminal sanctions, these penalties must be complied with.

A fraudulent bankrupt may never be rehabilitated, even if all his debts are paid.

The Spanish system is based on a coherent distinction between the nature of the bankruptcy, based on the innocent, negligent or fraudulent character of the bankrupt. However, it does seem difficult for bankrupts to obtain an arrangement with their creditors if they have nothing left, and it would therefore seem fair to adjudicate automatic rehabilitation to the fortuitous bankrupt.

N. SWEDEN

1. Negative consequences of bankruptcy

a) Directors’ liability for the remaining debts

Directors who deliberately or negligently cause loss or damage to the company, its shareholders or third parties, are liable to pay damages.

If a distribution of dividends is made without respecting the law, then the beneficiary must repay what he has received. If he is unable to do so, the directors involved in the decision of distribution may be liable for repayment.

b) Criminal offences

Depriving the creditors of assets of considerable value, not keeping the company’s books correctly, etc. is a criminal offence.

c) Professional interdictions

According to Swedish law, directors of a bankrupt company should be prohibited from carrying on a business, if:
- it is in the public’s interest
- and if they have severally neglected his business duties or its creditors’ interests.

2. Excusability and possibility for a fresh start

Although the above-mentioned rules on prohibition seem quite strict, bankrupts are seldom really prohibited from trading\(^9\). The idea is to refrain only persons who were involved in several bankruptcies from trading.

\(^9\) According to the authors of the Swedish Report.
As regards the numerous sanctions that may apply to directors in case of their company’s bankruptcy, it seems that it does not frighten them. At the contrary, most of them continue their business for as long as possible, in the hope of finding new investors to turn around the business and even improve the company’s business.

In that sense, Swedish bankruptcy legislation works well to facilitate a fresh start of bankrupt businesses.

**O. UNITED KINGDOM**

1. **Negative consequences of liquidation**

   a) **Directors’ liability for the remaining debts**

   Management of a liquidated company can be held personally liable for the company’s remaining debts in case of:
   - misfeasance or breach of any fiduciary or other duty
   - fraudulent trading (carrying out a company’s business with the intent to defraud creditors or for any other fraudulent purpose)
   - wrongful trading (continuing to trade when the director knew or ought to have known that there was no reasonable prospect of the company avoiding liquidation).

   b) **Criminal offences**

   Fraud, misconduct, falsification of the company’s books, material omissions from statements and false representations are criminally sanctioned.

   c) **Professional interdictions**

   Under the Company Directors Disqualification Act of 1986, directors may be disqualified from being a director, acting as receiver of a company’s property or being concerned with the promotion, formation or management of a company, in the following circumstances:
   - criminal offences connected with the Companies Acts legislation
   - wrongful trading
   - failure to comply with filing requirements
   - unfit conduct in insolvent companies.

   The minimum period of disqualification is 2 years and the maximum 15 years.

2. **Excusability and possibility for a fresh start**

   The UK system seems to distinguish between fraudulent and non-fraudulent insolvency, providing a wide range of sanctions and prohibitions for directors that have acted unlawfully or against the company’s or creditors’ interests. Should this not be the case, directors are apparently free to start a new business again.
P. **UNITED STATES**

1. **Negative consequences of bankruptcy**

   - **a) Directors’ liability for the remaining debts**

   The confirmation of a plan of reorganisation in a Chapter 11 case ordinarily discharges the corporate debtor from liability for all debts arising prior to the effective date of the plan of reorganisation, except to the extent that the plan of reorganisation otherwise provides.

   If the liquidation of the business was achieved through Chapter 7, the company ceases to exits and typically all pre-petition debts are discharged. Technically the Bankruptcy Code stipulates that a corporate debtor in Chapter 7 will not discharged of pre-petition debt, however since the entity ceases to exits, granting a discharge is irrelevant. However, a creditor can object to the discharge by filing a complaint in the bankruptcy court, called an “adversary proceeding”. A discharge may also be denied entirely if the individual debtor has engaged in bankruptcy-related wrongs (e.g. concealing assets from creditors).

   Certain debts of an individual debtor are not discharged based on the nature of the debt or the fact that the debts were incurred due to improper behaviour of the debtor. The most common types of non-discharged debt are typically related to individual debtor rather than the corporate debtor, and include certain types of tax claims, child support, alimony, debts for wilful and malicious injuries to person or property, debt to government units for fines and penalties. In general the directors and officers of a corporate debtor, will not be responsible for any debts from the estate.

   Outside of bankruptcy, directors and officers have a duty of care (applying the same care as an ordinary prudent person) and a duty of loyalty (prohibits faithlessness and self-dealing), referred to as a fiduciary duty, towards the company’s **shareholders**.

   When a company moves into the “zone of insolvency”, the fiduciary duty shifts from the stockholders to the **creditors**. Zone of insolvency refers to when a company becomes insolvent. A company is typically considered insolvent when it is unable to pay its obligations or the company’s liabilities exceed the assets.

   Directors and officers can be held personally liable for certain actions that are in breach of their fiduciary duty to creditors, during the time the company is insolvent. Usually this fiduciary duty towards creditors stops when the company files for bankruptcy, because most significant decisions are subject to review by interested parties and approval by the court. There is no uniform rule governing the releases and indemnification for directors and officers. However, the Business Judgement rule provides a safe harbour for directors, which operates from the presumption that directors’ actions are in good faith.

   Traditionally, large companies carry director and officer insurance which protects officers and directors for any actions taken in derogation of their twin duties of
loyalty and care generally to the extent such actions are not the result of gross negligence or wilful misconduct. In Chapter 7 cases, the trustee directly replaces the management.

b) Criminal offences

Directors and officers in a Chapter 7 or Chapter 11 case may be criminally indicted for fraud or gross negligence in performing duties and responsibilities.

c) Professional interdictions

After a company emerges from chapter 11, there are no penalties assessed on management. Absent a release, a management member may be held civilly liable if a creditor successfully prosecutes a cause of action against such individual. Unless management is subject to a non-compete agreement, individuals are free to engage in new enterprises. The only deterrent is whether such individual’s reputation is adversely impacted by an unsuccessful reorganisation.

2. Excusability and possibility for a fresh start

The commencement of a Chapter 7 liquidation is an admission that the business enterprise has failed. Although the public may perceive such liquidation negatively, it does not necessarily mean that the directors and officers are stigmatised to be able to start new business.

The initiation of Chapter 11 proceedings, although newsworthy, does not necessarily create negative publicity, since the outcome of the proceedings is not always liquidation, but usually reorganisation. Even if the case is a “liquidating” Chapter 11, the debtor attempts to dispose the assets, as a going concern, which usually creates more value to the creditor if the assets are sold at liquidation values.

Rather than chilling new investments in the company, the procedure encourages and facilitates mergers and acquisitions by providing a mechanism for the debtor to identify parties interested in acquiring its assets. The latter are sold free and clear of liens, claims, and other interests, including secured claims.

During a Chapter 11 case, management is often rewarded through retention bonus and incentive compensation programs (subject to Bankruptcy Court approval) and is proposed to ensure that key management does not leave the company during its reorganisation. These programs are another way to mitigate the stigma of chapter 11 by encouraging management to remain with the company.

In general, the American system regards bankruptcies in a much more positive manner than in Europe, as further discussed hereunder.

4.3.3.2. COMPARATIVE ANALYSIS

Bankruptcy affects the debtor in many ways; his reputation may be prejudiced (depending on the publicity made regarding the bankruptcy); he may be faced with
creditors still requesting reimbursement or encounters difficulty in starting a new business because of restrictions resulting from the bankruptcy.

We shall describe hereunder, the major restrictions applied to debtors (individual entrepreneurs and directors of a company), sanctions that may constitute major obstacles to a new start.

We shall then discuss the possibilities offered by the European Member States to allow for the fresh start of new businesses and contrast it to the U.S. system.

I. Restrictions applied as a result of bankruptcy:

Restrictions that generally apply to bankrupt individuals or directors of bankrupt companies are:

- of a pecuniary nature (liable for all or part of the company’s debts to the estate or creditors);
- of a civil nature (e.g. obligation to provide repair of damage suffered as a consequence of the bankruptcy);
- of a criminal nature (in case of fraudulent bankruptcy, concealing assets...);
- of a prohibitive nature (i.e. prohibited to exercise certain functions or to assume certain charges).

Individual entrepreneurs vs. directors:

In some countries, the sanctions that apply to individuals and to directors of companies are quite similar, except of course for legal specificities that result from the fact that directors have, unlike individual entrepreneurs, the duty to answer for their acts to the company’s shareholders.

The Greek system imposes stricter sanctions to individual entrepreneurs than to directors (only individuals automatically lose their trading capacity and are prohibited from exercising certain functions). This concept promotes the use of corporations for launching a new business rather than a sole proprietary.

pecuniary or civil sanctions vs. prohibitions:

All countries apply pecuniary or civil sanctions (that do not necessarily result from bankruptcy legislation but from general principles of tort or the obligation to repair a damage caused to others).

The automatic prohibition of exercising certain functions or assuming certain charges after bankruptcy does not exist in all countries or is seldom applied. It is mostly in Greece or in Portugal that they are applied.

It seems that, among these various sanctions, the sanction of prohibition constitutes a greater obstacle to the possibility of a fresh start.
sanctions in the interest of creditors vs. in the interest of the “society” in general

A common feature is the duty to protect the creditors and to respect the creditors’ equality in the distribution of assets. Directors of bankrupt companies are often sued in this regard, if they favoured creditors to the detriment of others, before bankruptcy proceedings were initiated.

The objective of other sanctions lies within the idea of “purifying” the market: expunging incapable entrepreneurs or making sure that they will not be able to launch a new business again (e.g. through the prohibition sanction).

“innocent” bankruptcy vs. fraudulent bankruptcy:

After having observed the various sanctions resulting from bankruptcies, one can not refrain from considering that some appear to be “normal” whereas others seem “unfair”. Such consideration results from the fact that one tends to accept more easily sanctions applied as a result of wilfully fraudulent bankruptcies than the sanctions applied to “innocent” bankrupts, that suffered misfortune or following certain circumstances of life. It is easier to accept that fraudulent bankrupts be held liable for their remaining debts, or be prohibited from launching a new business again.

Although this appears to be an essential element to consider when providing for post-bankruptcy sanctions, it seems that not all countries make a clear distinction between innocent or honest and fraudulent bankruptcies. Belgium, France, Luxembourg and mostly Spain tend to apply different sanctions to innocent bankrupts and fraudulent bankrupts. The Spanish system seems to be an example to follow in that regard, with its qualification of bankruptcies as fortuitous, tortuous or fraudulent.

It is essential that a distinction is made between the two kinds of bankruptcies, so that honest bankrupts do not continue to be stigmatised through association with the dishonest.

II. Possibilities for a fresh start and stigma on bankruptcy:

What exactly is meant by “fresh start”? Fresh start is the possibility of continuing or starting a new business after a bankruptcy. Fresh start is rendered possible where the stigma on bankruptcy is low (i.e. the negative attitudes and barriers for entrepreneurs that discourage them from risk-taking and entrepreneurship).

Concretely, the stigma on bankruptcy can result from:
- the importance of sanctions applied to bankrupts;
- the prohibition to carry out economic activities;
- the negative publicity (e.g. mention of the bankrupt’s name on a special list with the commercial jurisdiction, publication in local or national newspapers…);
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

4.3. Legal consequences of bankruptcy and possibilities for a fresh start

- the possibility to invoke the directors’ liability and the importance of the insurance coverage they may benefit from
- the confusion between fraudulent and non fraudulent bankruptcy.

In order for a bankrupt to bypass this stigma and to start a new business again, two important elements must be considered:

a) Discharge of the remaining debts:

As described above, a consequence of bankruptcy applied in almost all countries is the bankrupt’s liability for his remaining debts.

In order to allow fresh start, the notion of discharge of debt is essential, but for individual entrepreneurs only. Bankrupt companies are usually, after the bankruptcy procedure is finished, totally liquidated so that their creditors no longer have anyone to turn to for the reimbursement of their claims (unless they can sue the company’s directors at fault).

As for individual bankrupts, how could they possibly envisage the possibility of starting a new business if, as soon as they make any profit, their previous creditors will come knocking on their door in order to obtain satisfaction of their claims?

Some countries allow a total or a partial discharge of debts.

Very few countries provide for an automatic discharge of debts (e.g. Greece, but this advantage is strongly counterbalanced by the deprivation of the individual bankrupt’s status of trader).

Most countries accept such discharge, but only following a special procedure (e.g. rehabilitation in Austria, Belgium, Germany, or Spain). This rehabilitation is often linked to the notion of “innocent” bankruptcy, which seems quite logical.

Some countries (Denmark, Italy) allow such discharge, but only upon fulfilment of strict conditions, e.g.:

- the total satisfaction of creditors (which seems almost impossible to achieve for a small bankrupt with nothing left), or
- the expiration of a certain period of time during which the bankrupt has proved his good behaviour.

Other countries (Austria or Finland) are very strict. They provide that discharge may only be granted if the debtor manages to obtain a reorganisation plan with its creditors (which is clearly difficult in a “traditional” bankruptcy where there are hardly no assets left, but might appear easier in countries where the initiation of bankrupt does not necessarily lead to the company’s winding-up but may result in its reorganisation and continuity of its business).

In the countries where release of debts exists, such release is sometimes never granted if the bankrupt has been convicted with criminal offences (e.g. Italy, Luxembourg).
### LIABILITY FOR THE REMAINING DEBTS AND POSSIBILITY OF DISCHARGE

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<th>Liability Conditions</th>
<th>Possibility of Discharge</th>
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<td>Austria</td>
<td>Directors liable if committed a fault (e.g. did not file for judicial insolvency on time)</td>
<td>Discharge if reorganisation or in the course of private bankruptcies (non-traders)</td>
</tr>
<tr>
<td>Belgium</td>
<td>Directors liable if committed a serious fault that led to bankruptcy or if did not declare bankruptcy on time</td>
<td>Discharge if excusability is granted by the court (in case of innocent bankruptcy)</td>
</tr>
<tr>
<td>Denmark</td>
<td>Directors liable after bankruptcy/winding-up procedure but not after compulsory composition</td>
<td>Discharge in case of release after 5 or 20 years or in case of debt rescheduling</td>
</tr>
<tr>
<td>Finland</td>
<td>Directors liable if did not file for bankruptcy on time or did not convene shareholders on time</td>
<td>Discussion on discharge</td>
</tr>
<tr>
<td>France</td>
<td>Directors liable in case of mismanagement</td>
<td>Yes, unless specific offences committed</td>
</tr>
<tr>
<td>Germany</td>
<td>Directors liable if failed to petition for bankruptcy on time</td>
<td>Discharge under customer insolvency procedure</td>
</tr>
<tr>
<td>Greece</td>
<td>Directors liability if committed tort or did not notify creditors of cessation of payments</td>
<td>Discharge for individual bankrupts after 10 years or in case of judicial composition</td>
</tr>
<tr>
<td>Ireland</td>
<td>Directors liable if fraudulent/reckless trading, misfeasance proceedings…</td>
<td>Discharge: possible</td>
</tr>
<tr>
<td>Italy</td>
<td>Directors liable if do not respect their duty to protect the company’s creditors</td>
<td>Discharge for individual bankrupts if good behaviour or creditors’ settlement</td>
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<td>Luxembourg</td>
<td>Directors liable for misconduct in management or fault that led to company’s bankruptcy</td>
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<td>The Netherlands</td>
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<td>Sweden</td>
<td>Directors liable if deliberately or negligently caused damage to company</td>
<td>Discharge</td>
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<td>UK</td>
<td>Directors liable if misfeasance, fraudulent / wrongful trading</td>
<td>Discharge if non-fraudulent insolvency</td>
</tr>
<tr>
<td>USA</td>
<td>Individual debtor discharged from debt, except certain debts (e.g. alimony, taxes, damages for fraud…)</td>
<td>Corporate debtor discharged from debts</td>
</tr>
</tbody>
</table>
b) **Non-prohibition of carrying-out commercial activities:**

Having obtained discharge of the remaining debts is not the only condition for a successful fresh start. How could the entrepreneur/director be able to launch a new business if he has been subject to a prohibition from exercising certain commercial activities or professions?

As mentioned above, Greece seems to have the strictest regime in that regard, for bankrupt entrepreneurs will immediately lose their trading capacity and are therefore excluded from any commercial or industrial profession.

Some professions (e.g. trustee, lawyer, employee in a company of public law, auditor...) may not be exercised by individuals previously bankrupt, either automatically as a result of the bankruptcy, either under certain conditions, as illustrated hereafter.

France bases such prohibition on the existence of criminal sanctions and applies it only to the activities for which the bankrupt was subject to fraudulent bankruptcy, which appears to be a sound limitation.

The Netherlands have a specific regime: bankrupt entrepreneurs and directors of a bankrupt company must, before incorporating a new company, obtain a “declaration of non-objection” by the Ministry of Justice. The granting of such declaration is mainly based on the distinction innocent vs. fraudulent bankruptcy.

In contrast, the U.S. Bankruptcy Code provides for a complete discharge of debt, subject to litigation involving objections by creditors and other limited exceptions. The discharge constitutes a permanent statutory injunction prohibiting creditors from taking any action designed to collect the discharged debt.

In general, the US Bankruptcy Code does not place any restrictions on the directors or individual entrepreneur subsequent to the discharge of the debt, which allows them to enter freely into other business ventures thereafter. However, restrictions will be placed on any individual that has been convicted to a criminal offence related to any fraud, gross negligence or wilful misconduct that led to the bankruptcy.

<table>
<thead>
<tr>
<th align="left">POSSIBLE PROHIBITION OF CARRYING-OUT COMMERCIAL ACTIVITIES AND CONDITIONS THEREFORE</th>
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<tbody>
<tr>
<td align="left"><strong>Austria</strong></td>
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</table>
| **Belgium** | Prohibition from carrying out certain professions (auditor) or mandate (management of insurance company) under certain conditions (fraud…)
| **Denmark** | Business prohibitions (if illegal removal of company’s assets) |

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<td>Possible business prohibitions</td>
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<tr>
<td>Germany</td>
<td>Prohibition to practice for 5 years for directors who committed criminal offences.</td>
</tr>
<tr>
<td>Greece</td>
<td>Individual bankrupts are excluded from any commercial or industrial profession, and from certain functions (civil servant, lawyer…).</td>
</tr>
<tr>
<td>Ireland</td>
<td>Restriction from being appointed director of a company or incorporating a new company for a term of five years (unless proof of good conduct).</td>
</tr>
<tr>
<td>Italy</td>
<td>Prohibition to carry out certain professions (lawyer, stockbroker) or charges (trustee, director…).</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>Under certain conditions (gross and indisputable mistake that lead to bankruptcy), prohibition from performing business activity</td>
</tr>
<tr>
<td>The Netherlands</td>
<td>Prohibition unless “declaration of non-objection” obtained with the Ministry of Justice</td>
</tr>
<tr>
<td>Portugal</td>
<td>Prohibition from carrying out any business, unless judge provides that they may and if no criminal proceedings</td>
</tr>
<tr>
<td>Spain</td>
<td>Prohibition from engaging in any business, unless rehabilitated.</td>
</tr>
<tr>
<td>Sweden</td>
<td>Prohibition from carrying out a business if in public interest and if severe negligence</td>
</tr>
<tr>
<td>UK</td>
<td>Prohibition from being a director, receiver or incorporating a company under certain conditions (if criminal offences, wrongful trading…).</td>
</tr>
<tr>
<td>USA</td>
<td>None, except if directors were criminally prosecuted</td>
</tr>
</tbody>
</table>

4.3.4. **CONCLUSION**

A comparison of the various bankruptcy systems in the EU Member States indicate that the common goal of these procedures is to provide for the efficient liquidation of businesses in distress and the reimbursement of its creditors.

The various country systems follow a similar theme:

- Judiciary procedure initiated by the debtor or its creditors or other party;
- Creditors declare their claim in order to obtain reimbursement;
- A specific authority (trustee, receiver, liquidator, etc.) replaces the directors of the company;
- Distribution to creditors of the remaining assets, following a specific priority.

In order to benefit from such procedures, various criteria’s are required that all have to do with the impossibility for a business to recover. Some criteria’s are quite flexible (e.g. Germany and Ireland: inability to pay any minor debt), whereas others are more strict (e.g. Austria where the company must suffer illiquidity and over-indebtedness...
Although all countries’ procedures seem to reach their goal, i.e. the liquidation of a company, some countries’ systems (e.g. Germany, France and U.S.) also emphasis the restructuring of companies in order to (1) continue the business, (2) continue the employment of employees and (3) maximising the return to creditors and other stakeholders.

Most EU Member States’ systems impose certain restrictions, whether of a pecuniary or criminal nature, on individual debtors or directors, or certain prohibition to perform certain activities or to be appointed in certain functions. This has the potential to create negative stigma, since these restrictions creates an environment that deters entrepreneurs to make a fresh start.

These restrictions are considered to be justified where the individual debtor and directors committed fraud or willingly caused the company’s bankruptcy. However, in bone fide cases of bankruptcy, some of the restrictions could be considered excessive and prohibits entrepreneurs to make a fresh start. Not all countries make a clear distinction between bone fide and fraudulent bankruptcies and the restrictions related to a bone fide versus fraudulent bankruptcy.

According to our study, it appears that two conditions are required in order to allow for a new fresh start:

a) the total discharge of the debtors’ remaining debts;
b) limited restrictions should be imposed on the individual debtor or director in a bone fide bankruptcy.

Under these circumstances, previously bankrupt entrepreneurs may find the motivation to launch a new business again.
3. STIGMA ON FAILURE

3.1. QUESTIONNAIRE FOR THE GENERAL (CONSUMER) COMMUNITY AT NATIONAL LEVEL

The present comparative analysis is based on answers to the questionnaires received from targeted organisations in Belgium, Finland, France, Greece, Italy, Luxembourg, Portugal, the Netherlands, Spain, and the UK.

No responses were received from the targeted organisations in the following countries: Austria, Denmark, Germany, Ireland, Sweden, and USA.

“Yes” and “No” answers are illustrated in graphical form.

**KEY:**
1 = Yes
2 = No
3 = Yes and No/ according to the specific case

A number of questions were not answered or answered “we do not know”: These will be displayed as blank.

Additional comments provided by the targeted organisations will be referred to alongside the comparative analysis.

The name of the targeted organisations is confidential, their answers will not be personally identified in the present report, but will be assessed using a country trend.
1. Do the members of your organisation/community know the difference between insolvency and bankruptcy?

The responses received from the targeted organisations highlight that a significant number of those organisations are not aware of the difference between bankruptcy and/or insolvency.

According to the telephone interviews carried out, the vast majority of the organisations targeted do not deal with that specific field. The Italian organisations interviewed did not consider consumers to be directly affected by bankruptcy. Indeed, according to them, within the field of the consumer protection, there are other priorities to deal with. The same organisations pointed out that in many cases they are subject to budget restrictions, and are therefore obliged to work solely within the fields of consumer health or protection of consumers in commercial and financial transactions.
2. Are your members familiar with the notion of bankruptcy/business failure?

The majority of the targeted organisations stated that their members (regional organisations) and consumers are familiar with the notion of bankruptcy / business failure. The vast majority of those organisations interviewed also stated that the consumer has only very general views on, or knowledge of business failure. The French organisations noted that in their experience consumers are aware as a number of them have been placed under a procedure for excessive debt.
3. Do your members often have questions regarding bankruptcy/business failure?

The majority of consumers were found not to have questions relating to bankruptcy or business failure. According to those organisations interviewed, there is also a cultural issue to face: consumers generally think that consumer organisations deal exclusively with consumer protection and not with commercial matters. They also explained that there are no national publicity or other campaigns highlighting the implications of business failure for consumers.
4. If yes, is this generally because they:
- are facing financial difficulties
- deal with bankrupt/failing businesses and are unsure whether they should continue to do so

In view of the limited number of responses received, it is impossible in this instance to highlight a trend. Those targeted organisations, which provided feedback confirmed that in the majority of cases consumers only show an interest in bankruptcy legislation when they face financial difficulties or are dealing with a business in crisis.
5. Do your members attach a stigma to a bankrupt business?

7 organisations out of 13 organisations stated that their members attached a Stigma to a bankrupt business. However, no common trend could be identified among the responses received. Additionally, on a national level, organisations adopted different approaches. Organisations in Belgium, Italy and Spain expressed opposite positions. This situation was not altered during the telephone interviews. The interviewed organisations underlined the fact that their answers were given without consulting their members.

More interesting input was given by a French organisation. According to this organisation, stigma exists because consumers have such a low degree of protection in these circumstances. Indeed, this organisation added that increased public and external control over a business in financial difficulty would reduce the stigma if the controller were acting in the name of the creditor/consumer protection.
6. Why?

Unfortunately, only a limited response to this question was received from the targeted organisations. According to a Belgian organisation stigma exists due to cultural reasons. The answer did not provide any further comments. During the interview, the same organisation highlighted that from a lexical point of view, the word “faillite” (bankruptcy in French) has a very negative connotation. According to this organisation there is a kind of “stigma per se”.

A Finnish organisation stated that stigma does not exist because it is not considered morally justified.

The French, Spanish and Luxembourg organisations declared that stigma existed because of the negative experiences of consumers and minor investors in these situations.
7. In your experience, do your members make a distinction between a business in distress and a business that has recovered from distress?

We are not in position to define a common trend.

The targeted organisations stated that in general their respective members do not see a difference between the stated categories of businesses. Once a company knows that a counterpart is in difficulties, commercial relationships are immediately halted.
8. In your experience, do your members differentiate between a fraudulent bankrupt business and a non-fraudulent bankrupt business?

The vast majority of the targeted organisations stated that the general public does not know whether there is a difference between fraudulent and non-fraudulent bankruptcy. In doubt, they attach a strong stigma to a bankrupt business. Furthermore, according to a Finnish organisation, the knowledge of the public varies according to the information provided by the media. Therefore, the consumer pays attention just to the content of the information and not to the legal nuances.
9. Is your community more tolerant towards a young IT start-up in difficulty than towards an established firm with a significant number of employees?

The majority of the targeted organisations stated that the general public is not more tolerant vis-à-vis start-ups. The one exception was provided by a Finnish organisation. According to this organisation, the Finnish consumer is very tolerant vis-à-vis a business with a significant number of employees. During the interview, the same organisation confirmed that safeguarding the work force appeared to be the most important value for the Finnish citizen and consumer.
Availability of information

10. Apart from the general media, do your members have any other way of being informed of a business failure?

According to the questionnaires received and interviews carried out, the targeted organisations are of the view that the general public relies on the information provided by media.

The French and Luxembourg organisations interviewed provided exceptions to this. These organisations stated that consumer can have access to this information at “guichets” (desks), which are set up within the courts.

11. If yes, how?

The exception is represented by both a French and a Luxembourg organisation. These organisations declared that consumer can have access to this information thanks to guichets (desks), set up within the courts.
12. Does your association keep a specific databank on bankruptcies/business failures?

All the targeted organisations stated that they do not retain this type of information.

One exception was provided by a French organisation. This organisation retains data where that information refers to businessmen who have been involved in bankruptcy on several occasions.

13. If yes, how and under what circumstances is it used?

The French organisation is the only organisation to hold such data. The data is used in litigation procedures initiated in order to defend the consumer.
Reasons for failure

14. According to your experience, and according to your members, what are the most common reasons for business failure?

According to the questionnaires received and the interviews carried out, the vast majority of organisations stated that the causes of the business failure are:

1. financial difficulties
2. lack of management skills
3. fraud
4. taxation.

The majority of interviewed organisations stated that within the credit sector, business failure is due to financial problems. Within the horeca (hotels, restaurants, café’s) sector, business failure is usually caused by a lack of management skills. These sectors would appear to be the most sensitive for consumer protection. Please note that the activities of the majority of targeted consumer organisations are focused on the credit and health sectors.
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

- **Consequences of failure**

15. Do you usually discourage your members from dealing with a company whose financial difficulties have been revealed?

From the 13 organisations questioned, 7 were found not to discourage their members from having dealings with a business in difficulty.

16. Why?

A French organisation, during the interview, taking a conservative approach, stated that the protection of the consumer would be beneficial in a market where the offers for consumers have no limit and the degree of competition is very high.
17. **What is the reaction of the majority of your members towards a failing company?**

The questionnaires received highlighted two major trends: firstly that their members decide to cease all commercial relationships immediately or they request advice from a third party.

5 organisations (F – 2 orgs, P/Fin/S) consider that their members would discontinue business with a failing company.

5 organisations (S – 2 orgs, L/Gr/B) consider that their members would request advice from a third party.
A fresh start

18. If a failed entrepreneur has started a new business, would your members be influenced by his previous failure?

According to the questionnaires received, only one organisation out of 13 stated that their members would not be influenced by the previous failure of an entrepreneur.
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

19. Would you warn them of this previous failure?

The overall majority of organisations questioned stated that they would warn their members about the previous failure of a business.

A Spanish organisation stated that it preferred not to intervene in the commercial conduct of its members. The same organisation, however, declared during the interview that it is impossible not to exert to a certain extent an influence their members if you provide them with this kind of information.

20. Why?

We are not in a position to identify any general trend due to the lack of information provided by the questionnaires received.

However, during the interviews 3 Italian organisations stated that their role is to ensure that the consumer is not involved in financial difficulties. Therefore, on the basis that the consumer is generally the weakest party, these organisations preferred to warn their members. A Greek organisation stated that it would suggest to its members to make further inquiries about the causes of the failure in order to evaluate the desirability to stop business.
21. Do you think that the legislator should promote the opportunities available for a business previously involved in bankruptcy?

8 organisations out of 13 were favourable to the idea of promoting new business opportunities for businesses that previously went bankrupt.

50% of the targeted organisations that responded stated during interview that the legislator should promote new business opportunities for all entrepreneurs in a safe legal and economic environment.
22. Do you think that the legislator should work to eliminate the stigma affecting the business life of an entrepreneur previously involved in a bankruptcy?

8 organisations out of 13 declared that the legislator should work to eliminate the stigma affecting the business life of an entrepreneur previously involved in a bankruptcy. We can state that this answer is in line with the previous question.

3.1 Questionnaire for the general community at national level
23. Should the legislator promote a fresh start and eliminate stigma for fraudulent bankrupt persons?

The majority of the targeted organisations considered that the legislator should not work to promote the elimination of stigma in cases of fraudulent bankruptcy.

The position adopted in the questionnaire was also confirmed during the interviews.
24. Do your members agree with the idea that failed entrepreneurs often learn from their mistakes and that they will be more successful in the future?

7 out of the 12 organisations responding were convinced that failed entrepreneurs generally learn from their mistakes and will be more successful in the future.

The Italian organisations questioned considered that bankruptcy should be considered as an accident in business life, therefore, it is normal that the entrepreneur can become more experienced.
On the basis of the information received, it appears the risk of bankruptcy can discourage the creation of new businesses.

The statement of a Belgian organisation that was expressed during an interview and was confirmed in question n° 26 is very clear: the reason for not starting a new business, is the stigma of possible bankruptcy.

26. Why?

We received just 2 answers (Gr/B). Both state that bankruptcy can be considered as a deterrent to the creation of a new business.
27. Do your previously failed entrepreneur members, if any, continue to be entrepreneurs afterwards?

The targeted organisations are not in position to provide this information. The data is not available. The organisations that replied to the questionnaires declared that the information provided was solely the personal opinion of the representative.
28. If yes, does the stigma of bankruptcy make it more difficult for them to achieve good results?

Unfortunately, only 2 responses to this question were received. The vast majority of targeted organisations interviewed refused to give any official feedback, as it did not relate to consumer protection.

29. How?

Only three responses to this question were received.

According to one Belgian and one Finnish organisation, an entrepreneur who had previously failed would not be able to find new sources of credit to continue his activities.

A Greek organisation pointed out that the entrepreneur would not find a commercial partner.
3.2. QUESTIONNAIRE FOR THE BUSINESS COMMUNITY AT NATIONAL LEVEL

The present comparative analysis is based on answers to the questionnaires received from targeted organisations in Austria, Belgium, Finland, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Spain, and the UK.

No responses were received from targeted organisations in Denmark, France, Norway, Portugal, Sweden, and the USA.

“Yes” and “No” answers are illustrated under the form of graphs.

A number of questions were not answered/answered “we do not know”: they will appear as blank.

Additional comments were occasionally provided by the various organisations questioned and will be referred to alongside the comparative analysis.

The identities of the targeted organisations are confidential; their answers will not, therefore, be personally identified in the present report, but will be assessed on a country by country basis.
1. Does your association/community represent:

<table>
<thead>
<tr>
<th>Category</th>
<th>Number in figures</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Large enterprises (+250)</td>
<td>___</td>
<td>___ %</td>
</tr>
<tr>
<td>Medium sized enterprises (50-250)</td>
<td>___</td>
<td>___ %</td>
</tr>
<tr>
<td>Small enterprises (10-50)</td>
<td>___</td>
<td>___ %</td>
</tr>
<tr>
<td>Micro enterprises (-10)</td>
<td>___</td>
<td>___ %</td>
</tr>
<tr>
<td>Total</td>
<td>___</td>
<td>100 %</td>
</tr>
</tbody>
</table>

This question was designed in order to assess the degree of representation of the targeted organisations.

The targeted organisations were asked to identify whether they generally represented large enterprises (employing more than 250 persons), medium sized enterprises (employing between 50 and 250 persons) small enterprises (employing 10 to 50 persons) or micro enterprises (employing less than 10 persons).

The targeted organisations for the business community represented business (approximately) in the following proportions:
- Mainly micro and small enterprises: 5/8 (of which more than half mainly represented micro enterprises)
- Mainly medium enterprises: 1/8
- Mainly large enterprises: 2/8

The number of enterprises represented by the targeted organisations, in numbers, varied from 55 to 379,300, thus guaranteeing a wide range of representation.

The sample therefore represented all types of enterprises.
2. Within the business community, is there a stigma surrounding the failure of a business and/or bankruptcy?

Within the business community, it appears that a stigma does surround the failure of a business and/or bankruptcy.

- A Belgian organisation justified this statement with the idea that business failure is considered to reflect badly on the management of the underperforming company.

- A Greek organisation indicated that such stigmas consist in negative incentives, high taxation, financial difficulties, and failure in facing competition.

- In Luxembourg, it was stated that bankruptcy is always considered as something negative, and often implies the notion of fraud.

- A Dutch organisation observed that a business failure is generally regarded as a personal failure of the owner/manager.

- A British organisation pointed out to the negative consequences of failure in terms of both creditworthiness and trust.
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

- A Finnish organisation nevertheless pointed out that such a statement is true only to some extent: during the recession of early 1990’s, bankruptcy became so common that today, there is less stigma than 15 years ago.

- The existence of such stigma was denied both by a German organisation and by a Spanish organisation.
3. According to your experience, do entrepreneurs make a distinction between a business in distress and a business that has recovered from distress?

The majority of targeted organisations of the business community believe that entrepreneurs distinguish between a business in distress and a business that has recovered from distress.

The general consensus was that any negative associations attached to a business previously in distress were mitigated by later recovery of that business.

- A Dutch organisation explained that trading with a company in distress is stressful on both sides. When a business has recovered from a distressed situation whereby the creditors were aware of the problems – and possibly even informed of and asked to cooperate in dealing with the problems – there seems to be a sense of relief in the market. This organisation further observed that a company that has recovered from distress is respected as long as the creditors did not have to “bleed.”

- As pointed out by a British organisation, recovering from distress demonstrates acute management abilities.

- However, several organisations in Greece, Luxembourg, and Spain indicated that businessmen do not make a distinction between a business in distress and a business that has recovered from distress.
4. Does your business community differentiate between a fraudulent bankrupt business and a non-fraudulent bankrupt business?

All targeted organisations of the business community unanimously agreed that a fraudulent bankrupt business is not viewed in the same way as a non-fraudulent bankrupt business.

- A Spanish organisation further pointed out the distinction is made by the law.

- A Dutch organisation observed that in many cases where there is or might be a case of fraud, management of the company is not legally prosecuted, but held emotionally accountable for a lack of control or plain lack of “healthy suspicion” in dealing with third parties.

- A British organisation mentioned a general lack of trust of a bankrupt business.

- A German organisation observed that in a case of outright fraud not revealed by the auditor, the latter may be held liable.

- Several organisations suggested that the case of fraud is often difficult to establish.
5. Is your community more tolerant towards a young IT start-up than towards an established firm with a significant number of employees?

The business community does not hold a significant position in one way or another regarding tolerance towards young IT start-ups in contrast to the attitude towards established firms.

- Targeted organisations from Belgium, Greece, Ireland, Italy, Luxembourg, and Spain indicated a more favourable attitude towards young IT start-ups.
- The organisation in Luxembourg justified its position on the basis of the number of salaried employees.
- Similarly, a Belgian organisation stated that the community can be extremely angry when an established firm employing many staff over a long period of time goes bankrupt and staff are made redundant. The public might therefore be more tolerant towards a young company going bankrupt than towards a more established company.
- An Irish organisation that indicated an attitude of higher tolerance towards young IT start-ups also stressed that the recent downturn in the high technology sector has increased the level of anxiety towards IT start-ups.
- A Greek organisation expressed a general attitude of tolerance towards young start-ups.
Several targeted organisations in Austria, Finland, Germany, Ireland, Greece, Italy, the Netherlands and the United Kingdom expressed attitudes of intolerance toward IT start-ups.

The Dutch organisation stated an attitude of tolerance toward IT start-ups in terms of availability of financing, but anxiety in dealing with these young companies on a business level, as compared with more established companies.

A targeted Finnish organisation stressed that IT enterprises are not favoured, whereas so-called “old enterprises” are.
Availability of information

6. *To the best of your knowledge, how does a business discover that a potential or actual counterpart faces difficulties?*

The targeted organisations were provided with multiple-choice possibilities, and answered as following:

- Media  
  *(Austria x2, Belgium x2, Finland x2, Germany x2, Greece, Ireland x2, Italy x3, Luxembourg x2, Spain)*

- Databanks  
  *(Austria, Belgium, Finland, Germany, Greece, Italy (access open only to authorised bodies) x4, Spain x3)*

- Information provided by colleagues, competitors or the business sector  
  *(Austria, Belgium x2, Finland x2, Germany x2, Greece x2, Ireland, Italy x4, Luxembourg x2, Spain x2, Netherlands, UK)*

- Credit and/or financial institutions  
  *(Belgium, Finland x2, Germany x2, Greece, Ireland x2, Italy x3, Luxembourg, Spain, Netherlands, UK)*

- The counterpart  
  *(Austria x2, Belgium (obs: late info: when difficulties have become severe) x2, Finland, Germany, Greece, Ireland, Luxembourg)*

- Creditors  
  *(Belgium, Finland, Germany x2, Greece x2, Ireland x2, Italy x3, Luxembourg x2, UK)*

- Other  
  *(Germany: supervisory authority  
  Ireland: through contacts in business networks and socially, ie at social events etc)*

It appears from the information provided by the study participants that all sources of information are used in detecting a business (actual or potential counterpart) facing difficulties. The most commonly used sources seem to be colleagues, competitors, the general business sector, media, and credit/financial institutions. Information provided by creditors is also important, limited by countries with banking secrecy. Lastly, one German organisation pointed to information provided by the supervisory entity as being an important source.
7. Within your community, do your members enquire whether a bankrupt person is fraudulent or not?

It seems that a majority of those organisations targeted agree that their members do enquire as to whether a bankrupt person is fraudulent or not.

- A Belgian organisation observed most people do not actively search to find out whether or not the bankrupt person is fraudulent, but are curious about it anyway.

- The majority of organisations pointed to a significant level of concern by their members on this issue. The information is usually sought out informally.

- However, a small number of those organisations targeted rejected the idea of such an enquiry. Among these were two Luxembourg organisations, one of which stated that such information is difficult to discover, a Greek organisation, Spanish organisations, and a Dutch organisation.
8. Within the business community, are entrepreneurs listed in databanks according to solvency ratings?

A majority of the business organisations targeted stated that within the business community, entrepreneurs and businessmen are listed in databanks according to solvency ratings.

- A Greek organisation provided that the information includes evidence of non-payments by cheques or by notes.

- German, Irish, Italian Dutch and Spanish organisations did not agree with this statement.

- A Dutch organisation stressed that although no public databases on solvency ratings exist, banks and other financial institutions have databases that provide information to departments on certain “entrepreneurs” and how to deal with their future financing requests.

- An Austrian organisation observed that only a small number of entrepreneurs are listed on such databanks according to solvency ratings.

- A Luxembourg organisation observed that the available databanks are not official, but are private sources of information.
9. If yes, please indicate the sources of this information?

Out of the multiple-choice possibilities on solvency ratings of businesses, the organisations answered as follows:

- law firms

- public institutions (courts or other justice bodies)  
  (Belgium x2, Ireland, Italy x2, Spain x2)

- private databanks  
  (Austria, Belgium x2, Finland x2, Germany (voting agencies), Greece, Ireland, Italy x3, Luxembourg x2, Spain, Netherlands, UK)

- your own organisation  
  (Germany, Italy, Spain)

- other organisations (chambers of commerce, professional associations….)  
  (Austria, Italy x2, Spain)

The overwhelming source of information on insolvency ratings of entrepreneurs seems to be private databanks, described as banks and financial institutions with restricted access to this information.

Law firms do not appear to be source of information at all.

Public bodies, other organisations, and several of the participant organisations identified themselves as being sources of information.
10. Do these databanks differentiate fraudulent bankruptcy, and non-fraudulent bankruptcy?

The targeted organisations mainly expressed the opinion that the available databanks of information do not differentiate between fraudulent bankruptcy and non-fraudulent bankruptcy.

- A Greek organisation observed that only justice bodies, as opposed to their community make such distinction.

- The distinction seems to be made primarily in Italy, the Netherlands, and the UK.
11. Do you consider this information relevant for your business sector?

The study participants strongly agreed that information relating to the distinction between fraudulent and non-fraudulent bankruptcies is relevant to the business sector.

- A Belgian organisation observed that when dealing with a potential new client, it needs to know whether the client had previously been in bankruptcy due to circumstances outside of its control or due to fraud, in which case they would not be accepted as a client. This clearly expresses a stigma linked to fraudulent bankruptcy.

- A German organisation noted that in the absence of the above-described sources of information, such a databank would allow statistics to be drawn up, which would be helpful for reorganisation operations.

- A Dutch organisation pointed out that although this information is relevant, they do not mean to suggest that “once a thief always a thief”, and that one should not be stigmatised for the rest of his/ her “business life”…

3.2. Questionnaire for the business community at national level 78
12. According to the practice of your organisation and/or your members, which organisation provides the most reliable information on the solvency rating of a business?

The proposed sources of information with regard to their reliability were ranked as follows by the targeted organisations:

- Law firms
  (Ireland)

- Public institutions (courts or other justice bodies)
  (Germany, Italy x2, Spain x2)

- Private databanks
  (Austria, Belgium x2, Finland, Germany, Greece, Ireland, Italy x2, Luxembourg x2, Spain, UK)

- Your organisation
  (Italy, Spain, Netherlands)

- Other organisations (chambers of commerce, professional associations)
  (Austria, Germany (chamber of commerce), Italy, Spain)

The majority of targeted organisations confirmed that private databanks are the most reliable sources of information in rating the solvency of a business. Generally speaking, the business community is satisfied with the quality and availability of information databanks for solvency ratings. In addition, consulting firms and chambers of commerce were also identified as reliable sources of information.

Only one Irish organisation mentioned law firms as being reliable sources of information.

Credit institutions were referred to by some business organisations as being good sources of information.
3.2. Questionnaire for the business community at national level

Reasons for failure

13. According to your experience and/or your business vision which are the most common reasons for business failure?

The targeted organisations were asked to identify the most common reasons for business failure and distinguish between large enterprises and medium to micro enterprises.

The answers compared hereafter are based on the causes ranked by the targeted organisations as the first three ones.

Highest ranked reasons appear in **bold**.

**Large enterprises**

- Financial (guarantees, securities given to lenders, lack of working capital, poor cash flow, loss of long term finance, bad debts)  
  *(Austria x2, Belgium, Finland, Germany x2, Greece, Ireland, Italy x5, Luxembourg x2, Spain x3, Netherlands, UK)*

- Fraud  
  *(Belgium)*

- Personal extravagance, excessive drawings or remuneration  
  *(Ireland)*

- Management skills, poor management  
  *(Austria x2, Belgium, Finland, Germany x2, Greece, Ireland x3, Italy x5, Luxembourg, Spain, Netherlands, UK)*

- Legal disputes  
  *(Italy)*

- External business conditions (loss of market, main customer, rent review, other increases overhead)  
  *(Austria, Belgium, Finland, Germany x2, Ireland, Italy x5, Luxembourg x2, Spain, Netherlands, UK)*

- Failure to deal with income tax, corporation tax affairs or VAT  
  *(Luxembourg)*

The comparative analysis of the answers received from the business community with regard to large enterprises highlights that the most common highly ranked reason for business failure is management skills and poor management. The two other main reasons (both were very often identified) seem to be linked on the one hand, to financial problems, and on the other hand, to the external business conditions, such as loss of market, main customer, rent review, other increased overheads.
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

Reasons relating to fraud, personal extravagance, and failure to deal with income tax, were exceptionally identified.

**Medium/ Small/ Macro enterprises**

- Relative youth or lack of experience of the entrepreneur
  *(Austria x2, Belgium, Greece, Ireland x2, Italy x5, Luxembourg, Spain, Netherlands, UK)*

- Financial
  *(Austria x2, Belgium x2, Finland, Germany x2, Greece x2, Ireland x2, Italy x5, Luxembourg x2, Spain x3, Netherlands, UK)*

- Fraud
  *(Greece)*

- Management skills
  *(Austria x2, Belgium x2, Germany, Greece, Ireland x2, Italy x5, Luxembourg x2)*

- Personal extravagance
  *(Belgium)*

- Legal disputes
  *(Italy)*

- External business conditions
  *(Austria, Belgium x2, Finland, Germany x2, Ireland, Italy x5, Luxembourg, Spain, Netherlands, UK)*

- Failure to deal with income tax, corporation tax affairs or VAT
  *(Finland, Germany, Italy)*

The comparative analysis of the answers received from the business community with regard to medium, small and macro enterprises shows that the most common highly ranked cause for business failure was financial difficulties followed very closely by external business conditions, youth/lack of experience, and then lack of good management skills. It must be pointed out that contrary to large enterprises, the young age or the lack of experience of the entrepreneur is considered as an important and widely spread reason for medium to micro business failures: it was ranked first only by two targeted organisations, but was identified among the three most important reasons by a majority of targeted organisations.

Fraud, personal extravagance, legal disputes were only exceptionally identified, whereas failure to deal with income tax, corporate tax affairs and VAT was ranked among the first three reasons for failure for smaller businesses by more organisations than with regard to large enterprises.
The targeted organisations were split in their opinion on the willingness within the business community to deal with businesses facing difficulties. The attitude adopted towards the latter would often depend upon the current economic situation and the importance of the customer relationship. However, there appears to be a general reluctance to deal with a business facing difficulties. Several targeted organisations pointed out that dealing with a business facing difficulties would involve stricter control, including provision of guarantees, or even cash payments.
15. Within your business community, are your members willing to deal with a business that has failed but recovered?

Very encouragingly, all the targeted organisations unanimously agreed that their members would be willing to deal with a business that has recovered after failure. Only slight reluctance was expressed, including adopting a precautionary attitude, taking into account the reasons for the failure and asking for guarantees.
16. In your opinion, are the members of your community aware of the restriction regime applicable to a bankrupt business?

The majority of targeted organisations considered that the members of the business community whom they represent are aware of the restriction applicable to a bankrupt business.

- A German organisation observed that due to the particular rules applicable in insolvency matters, specialists should be resorted to.
- However, a Greek, Irish, Italian and a Spanish organisation expressed the opposite opinion.
17. Should the restriction regime prevent other partners from dealing with a business in insolvency status?

A majority of the targeted organisations stated that any restrictions placed on a bankrupt business should not prevent other partners from dealing with a business in insolvency status.

However, several organisations either did not answer, or answered that restrictions placed on a business should prevent partners from dealing with that business.
Organisations were divided on whether or not they would be willing to get involved in the management of a bankrupt person.

Businesses generally seem to be reluctant to getting involved in management of a bankrupt person in the case of fraud or potential fraud.

- Several organisations, including one German organisation in particular, observed that only individuals are willing/allowed to be involved in the management of a bankrupt person.

- A Dutch organisation also pointed out that such management should be entrusted to specialised companies only.
19. Would a business be disposed to sell shares to a bankrupt person?

Most targeted organisations answered that businesses would not be likely to sell shares to a bankrupt individual.

- A Belgian organisation observed that presumably the business would not be paid for the shares and hence would not sell them, and that small companies would not want a bankrupt to be a shareholder.

- Several organisations, which agreed to such an operation, however subjected their position to the absence of any fraud, or provided that it would depend on the reasons for the bankruptcy.

- A German organisation suggested that this would be contingent upon guarantee of the payment of the price.
20. Would an entrepreneur be disposed to employ a bankrupt person in their business? If yes, which position could the bankrupt occupy?

Several targeted organisations admitted that an entrepreneur would agree to employ a bankrupt person in their business. The positions that such a person could occupy in their view would depend on the reasons for the bankruptcy and on the person’s management skills. Some specified that there should not have been any fraud. Some positions such individuals would be likely to fill include adviser or manager, but overall, these persons would be excluded from the highest management levels.
21. Do business request extra guarantees or attach extra conditions when doing business with a person who has failed in the past?

The majority of organisations targeted agreed that businesses generally would request extra guarantees or conditions when doing business with a person who has failed in the past.
22. How does a business facing difficulties secure additional credit?

The targeted organisations indicated that businesses facing difficulties can secure additional credit through insurance, deposits, the use of personal relationships, the provision of personal guarantees over its own assets if it cannot give anymore charges over the business assets, bank guarantees, the requirement of cash payments, real securities, payment terms, or collateral.
A majority of the targeted organisations appear to favour legislative support for granting opportunities for a fresh start to businesses previously bankrupt.

- A Belgian organisation added that 70% of bankrupts already continue later on in leading positions in companies, and that therefore a fresh start is already a possibility, at least for individuals.

- A German organisation observed that a start-up is necessary fragile at first, thus justifying external assistance – which ought however to comply with competition rules.

- A Greek organisation observed that companies should be allowed a fresh start under careful monitoring.

- It was also pointed out by several organisations that in the case of a non-fraudulent bankruptcy, there is no reason to put extra restrictions on businesses wishing to have a fresh start.
The Dutch targeted organisation took a more conservative position on restricting businesses wishing to start fresh. It argued that a lot of entrepreneurs went bankrupt last year because of a lack of realism in their business plans and should therefore not be easily restored.
24. Do you think that the legislator should work to eliminate the stigma affecting the business life of an entrepreneur previously involved in a bankruptcy?

As for the above question, almost all organisations (with the exception of the two Finnish organisations) seem to believe that the legislator should work to eliminate the stigma affecting the business life of an entrepreneur previously involved in a bankruptcy.

- A Finnish organisation observed that this is not a problem that can be solved by legislation.

- A Dutch organisation, preferring elimination of the stigma by the legislator, observed that in general, a failed entrepreneur in the Netherlands is treated as a “loser” (weak management etc). Lifting this stigma would be advisable. However, this organisation also doubted whether the legislator should enforce the elimination, preferring that the Dutch business morale would migrate towards a more positive approach on entrepreneurs in general.

- Similarly, a German organisation pointed out that the stigma stems from society rather than from the legislator.
25. Should the legislator promote a fresh start and eliminate stigma for fraudulent bankrupt persons?

Almost all organisations took the position that the legislator should not promote the fresh start and elimination of stigma for fraudulent bankrupt individuals.

The Dutch targeted organisation expressed a strong intolerance toward bankruptcies involving fraud and towards the elimination of stigma associated with fraudulent bankrupt individuals.
26. Do your members agree with the idea that failed entrepreneurs often learn from their mistakes and that they will be more successful in the future?

Almost all targeted organisations agreed with the idea that failed entrepreneurs often learn from their mistakes and that they will be more successful in the future, thus expressing a positive “second chance” attitude.

- A Dutch targeted organisation proposed distinguishing between the reasons for prior failure in order to adapt the restart strategy by adding additional conditions. *I do not understand this comment?*

- Two Luxembourg organisations however expressed a contrary position. *What contrary position?*

- A Finnish targeted organisation expressed reserves with regard to businesses facing several bankruptcies. *What kinds of reserves?*
27. For entrepreneurs in your business community who failed, but restarted, if any, does the stigma of bankruptcy make it more difficult to achieve good results?

Despite the generally positive attitude under the previous question, most organisations agreed that for entrepreneurs who have failed, the stigma of bankruptcy in their respective business communities does indeed make it more difficult to achieve good results.
Among the proposed answers, the inability to find credit was noted as being the single most important reason for failed entrepreneurs to achieve good results when attempting a fresh start. The second most important reasons included the inability to find commercial partners and, less commonly, the fact that previous clients have turned into their competitors.
29. Do you think that the legislator should strengthen the level of control over the business life of an entrepreneur previously involved in a bankruptcy experience?

According to the answers received from the targeted organisations, the business community generally does not believe that there should be more legislative control over the business affairs of an entrepreneur previously involved in a bankruptcy. Most organisations believe that the present legislation is sufficient in controlling previously bankrupt businesses and individuals.
30. Do you think that the legislator should strengthen the level of control over the business life of an entrepreneur facing difficulties?

Organisations seem to favour strengthening the level of legislative control over the activities of an entrepreneur actually facing difficulties.

Only half of the organisations adopted the above-stated position. Some of the other organisations made the following comments:

- A Dutch targeted organisation observed that in general businesses facing difficulties should be more strongly “encouraged” to ask for assistance (probably enforced by legislation) at an early stage.

- Some organisations pointed out that strengthening the control would impose further delays on the outcome of the process.

- A German organisation observed that the legislator cannot exercise this control and should therefore delegate third parties to do so.
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

31. Do you think that the legislator should encourage the growth of external controls over a business facing difficulties?

A slight majority of the targeted organisations expressed an opinion that the legislator should encourage external controls over a business facing difficulties.

- A Dutch organisation observed that it is helpful for management facing difficulties to be “guided” towards external feedback, including experienced external managers/advisers.

- A German organisation stressed that encouraging such outside assistance would enable earlier detection – and treatment - of insolvency situations.

- Some organisations indicated that the current regime already provides sufficient guarantees and control over businesses facing difficulties.
32. According to your experience, does the entrepreneur consider that an external manager can reduce the level of stigma surrounding a business facing difficulties?

A conclusion to the above issue could not be made, considering the opinions were divided evenly among the participating organisations.

- A Dutch organisation observed that an external manager can mediate between the debtor and angry stakeholders and thereby reduce the negative stigma associated with a business facing difficulties.

- However, an Irish organisation stated that the stubbornness and ego often found in businessmen and company management might result in a general reluctance to allow an external manager to intervene in the company.
3.2. Questionnaire for the business community at national level

33. Do you think that the external control should be under the power of the judicial authorities?

A slight majority of the targeted organisations stated that external control and monitoring of companies should not be under the power of the judicial authorities.

- A Finnish organisation argued that the present legislation regulating business reorganisation is sufficient.
- According to a German organisation, the judicial power does not have a sufficiently good vision of the enterprise’s economic situation.

The targeted organisations that answered in favour of placing the external control under the judicial authority often complemented this solution with additional suggestions. For example,

- An Austrian organisation further suggested additional support by lawyers and chartered accountants.
- Similarly, a Greek organisation observed that the judicial authorities must be assisted by a body of experts.
- Several organisations also observed that the external control should be placed under the power of the judicial authority only in case of bankruptcy.
A Dutch organisation proposed an alternative solution, based on a combined effort of legislation and finance as these two ‘parties’ are the main stakeholders dealing with companies facing difficulties.
34. Do you think that the external control should be under the control of creditors?

The majority of the targeted organisations of the business community seem to be against the idea of placing the external control of companies under the jurisdiction of creditors.

- A Dutch targeted organisation pointed out that in case of the presence of a large number of creditors, it is likely that a few might block any possibility in coping with the problem.

- According to a German organisation, creditors are generally not interested in performing such duties, as this is not their line of business.

However, several organisations agreed to the idea of creditor control.

- A Finnish organisation expressed a preference for creditor control rather than control by public authorities.
35. Would the appointment of a crisis manager be considered an appropriate measure by the creditors of a business facing difficulties?

The questionnaire suggested to the targeted organisations the appointment of a crisis manager to deal with a business facing difficulties. The question was asked, whether this would be considered adequate in view of creditors.

Most organisations added that creditors would encourage the appointment of a crisis manager in distressed situations.

- A German organisation observed that the appointment of such manager is already possible.

- An Irish organisation pointed out that such crisis manager should be endowed with clearly identified and understood powers of accountancy.

- An Italian organisation observed that the appointment of a crisis manager could be considered an appropriate measure by creditors of medium sized enterprises, as opposed to micro enterprises. Nevertheless, according to this organisation, small or medium sized enterprises could play an important role to stimulate a better business dialogue among the interested parts.
36. Would the appointment of a crisis manager be considered an appropriate measure by the employees of a business facing difficulties?

Most of the targeted organisations stated that the appointment of a crisis manager would be considered an appropriate measure in a distressed situation by the employees of a business facing difficulties.

Some however pointed out that this would depend upon the reason for the crisis.

- A Greek organisation observed that hiring a crisis manager is usually considered to be the most effective tool to face the difficulties encountered by a distressed business. However, according to this organisation, employees are concerned that a crisis manager is usually the cause for many dismissals in a distressed company.

- An Italian organisation voiced the opinion that the appointment of a crisis manager would probably be considered an appropriate measure in a distressed situation by the employees of medium size enterprises, but not of small enterprises.

- A British organisation argued that the appointment of such crisis manager would contribute to business recovery and job sustainability.
3.3. QUESTIONNAIRE FOR THE FINANCIAL COMMUNITY AT NATIONAL LEVEL

The present comparative analysis is based on answers to the questionnaires received from targeted organisations in Austria, Finland, Italy, Luxembourg, Portugal, Spain, Sweden, Netherlands and the UK.

No response was received from the targeted organisations in the following countries: Belgium, Denmark, France, Germany, Ireland, Norway, and the USA.

“Yes” and “No” answers are illustrated in graphical from.

A number of questions were not answered or answered “we do not know”: These will be displayed as blank.

Additional comments provided by the targeted organisations will be referred to alongside the comparative analysis.

The name of the targeted organisations is confidential, their answers will not be personally identified in the present report, but will be assessed using a country trend.
1. Do your members represent:

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<tr>
<th>Category</th>
<th>Number in figures</th>
<th>Percentage</th>
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<tbody>
<tr>
<td>Large enterprises (+ 250)</td>
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<tr>
<td>Medium sized enterprises (50-250)</td>
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<td>Small enterprises (10-50)</td>
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<td>Total</td>
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This question was designed to assess the degree of representation of the targeted organisations.

The targeted organisations were asked to identify whether they generally represented large enterprises (employing more than 250 persons), medium sized enterprises (employing between 50 and 250 persons) small enterprises (employing 10 to 50 persons) or micro enterprises (employing less than 10 persons).

Those organisations targeted within the financial community were represented approximately in the following proportions:
Mainly micro enterprises: 1/4
Mainly small enterprises: 1/6
Mainly medium enterprises: 1/4
Mainly large enterprises: 1/3

The number of enterprises represented by the targeted organisations, in numbers, ranged from 11 to 5000, thus guaranteeing a wide range of representation.

The sample therefore represented uniformly all types of enterprises.
2. Within the financial community, is there a stigma surrounding the failure of a business and/or bankruptcy?

It appears that in the majority of Member States, the financial community considers that the failure of a business or its bankruptcy results in stigma.

The targeted organisation in Luxembourg justified the existence of such stigma by the fact that there have been an increasing number of insolvency proceedings and bankruptcy procedures in Luxembourg.

The British targeted organisation observed that the stigma is more specifically attached to bankruptcy, whilst attitudes to business failure are still negative, they are changing slowly. The financial community therefore is relatively aware of the consequences for a business of distress/insolvency.

The only targeted organisations to reject the existence of stigma in cases of business failure were those organisations targeted in Finland.
3. Does your community make a distinction between a business in distress and a business that has recovered from distress?

Most countries appear to make a distinction between a business in distress and a business that has recovered from distress. A UK organisation pointed out that a business that has recovered from distress usually does so because of the introduction of a new and improved management team, which its members sometimes contribute to alongside investment. According to this result, it thus appears that recovering from distress results in an increased level of trust from the financial community towards the business.

However, one of the Spanish targeted organisations replied in the negative.
4. Does your community differentiate between a fraudulent bankrupt business and a non-fraudulent bankrupt business?

All the targeted organisations stated that businesses involved in bankruptcy proceedings are treated differently by the financial community where fraud was involved. An UK organisation stressed that “fraud is regarded as very serious indeed”.
5. Is your community more tolerant towards a young IT start-up in difficulty than towards an established firm with a significant number of employees?

The attitude of the financial community appears to be more varied with regard to the situation of young IT start-ups.

A more tolerant attitude was expressed by the two targeted Austrian organisations, one of the two Finnish organisations, and one of the British organisations.

On the contrary, one of the Finnish targeted organisations, the two Italian organisations, the Luxembourg, Portuguese, the two Swedish and the Dutch targeted organisations did not take such a tolerant approach. One of the Spanish organisations observed that it did not know, while the other observed that a flexible approach is adopted and that the attitude depends on the case in question. The Finnish Bankers’ Association similarly observed that opinions are formed on a case by case basis. The Swedish Bankers’ Association stressed that on the contrary, there is a feeling of solidarity vis-à-vis more established customers, thus expressing a feeling of suspicion towards young IT start-ups facing difficulties.
6. Do your members keep precise data on the history of their clients and on their eventual financial difficulties?

Most targeted organisations replied that the financial community does keep precise data on the history of their clients and on their eventual financial difficulties.

However, a Swedish organisation explained that only original data on credit assessment, limits and annual reports are kept. Otherwise, the financial community relies on local, individual knowledge of customers.

7. What kind of data?

Most targeted organisations focused on general credit information and on accounting information.

More specifically, the Austrian organisations quoted press releases, data about the business situation based on balance sheets, shares in the partnerships, and lists of clients who are a credit risk. The Italian organisations also pointed to balance sheets, income statements, and data concerning customer transactions. In Italy, it is possible to keep accounting documents for ten years. Reports made on transactions larger than €10,329.14 must be kept for 10 years. The Bank of Italy operates a public credit register and there are private registers of data on loan applications, including data on borrowers whose debts will be extremely difficult to recover because they may be
subject to collective bankruptcy procedures or forcible execution. In Luxembourg, data kept by the financial community includes data concerning financial difficulties such as unpaid cheques and bills of exchange and lists of annual bankruptcy judgements… Portuguese organisations pointed to general economic and financial data. The Spanish Bankers’ Association stated that they basically keep data that are related to the relationship with the client and data that appear on the documentation concerning the activities carried out by the clients. A Swedish organisation stated that they kept only original data on credit assessment, limits and annual reports. Otherwise, the available data is based on local, individual knowledge of customers. A Dutch organisation observed that they keep all kinds of data, such as balance sheets etc. In the UK, an organisation pointed out to management accounts while another organisation observed that most UK clearing banks in addition to financial information, track account trends and characteristics and use these to identify businesses in difficulties at an early stage.
### 8. Do these data differentiate between fraudulent bankruptcy and non-fraudulent bankruptcy?

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<th>Country</th>
<th>Yes</th>
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<td>Austria</td>
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The data stored by the financial community does appear to differentiate between fraudulent bankruptcy and non-fraudulent bankruptcy in a (small) majority of countries (Austria, Finland, Italy, Luxembourg, Spain and Sweden).

Examination of the data on customer relationships in general reveals whether the customer’s failure has had penal consequences, such as charges of bankruptcy against the customer.

The Luxembourg targeted organisation however observed that the attitude towards enterprises/traders having caused fraudulent bankruptcy should be more severe. The data are kept in special files, as these activities are followed by criminal prosecution.
9. *How long do you keep those data?*

Although several answers pointed out that the duration would depend on the specific case, an overall assessment can be made that the data are generally kept between 6 to 10 years:

UK: approximately 7 years; Spain: at least 6 years (legal time period for keeping such information); Portugal: a few years; Luxembourg: at least 10 years; Italy: concerning banks’ accounts books or correspondence: 10 years; otherwise, the data is kept for the duration of the participation in the target company; Austria: as long as the business relation is maintained and thereafter, for a period of 5 to 10 years depending on the type of data. A Swedish organisation stated a stricter policy for the retention of data: the information is kept forever.
10. Are these data shared with other financial institutions?

It appears without any doubt from the answers provided by the financial community that in the majority of countries, data on the history of their clients and on their eventual financial difficulties is not shared with other financial institutions.

In Italy for instance, the data are accessible only to those persons directly affected by and involved in the procedures. All financial intermediaries have access to the Central Credit Register kept by the Bank of Italy. Only members have access to private registers. However, access is limited to the amount of the single borrower’s debt with the entire system, not the exposure of individual lenders.

Austria exceptionally answered positively.

Only a small majority of the targeted organisations however expressed the opinion that sharing such information would be useful, an opinion that is also apparent from the responses given to the following question.
11. If not, would your community consider it useful?

Only a small majority of the targeted organisations considered that sharing the data they keep concerning businesses in difficulties might be helpful. A Luxembourg organisation observed that the main reason would be to prevent “bank shopping”.

However, opposite arguments were based on various principles, such as the violation of the principle of confidentiality if third parties were to learn of elements relating to criminal proceedings or of information on individual accounts (an Italian organisation and a UK organisation), bank secrecy legislation (a Swedish organisation), and anti-competition (a UK organisation).
A larger number of targeted organisations belonging to the financial community share the data concerning the history of their clients and their eventual financial difficulties with their business partners than they do with other credit institutions. Thus, an Austrian organisation observed that such data is shared as far as they are not subject to bankers’ discretion. The same observation was made by a Spanish organisation, according to which the data are shared on a case by case basis taking into account whether these data are public or protected by professional secrecy.

However, a majority of the targeted organisations denied sharing such data with their business partners. A UK organisation however admitted that a summary of progress would be passed to investors.
More than half of the targeted organisations that responded to the survey did not provide an answer to this question.

The majority of the answers received relating to this question stated that the financial community does not consider it useful to share the data held on the history of their clients with business partners. The reasons given to the question on sharing these data with other financial institutions were also restated.
14. Are these data shared with your clients?

A majority of the targeted organisations stated that data relating to their clients were not shared with the latter. A Finnish and an Italian organisation explained that customers can view their own files, but not others; the only exception being guarantors, who can view debtors’ data.

An Austrian observed that such data are shared in a limited way, i.e. within the scope of the bankers’ duty of secrecy and only in the form of general information. In Luxembourg, banking secrecy regulation applies. A UK organisation stated that such data would be shared with their clients to the extent that any early warning signs would be discussed with the client.
15. **If not, would your community consider it useful?**

All answers provided by the financial community gave a negative response. The main reason for this was for reasons of confidentiality.
In Austria, the financial community is subject to the obligation to transmit financial data concerning their clients to judicial authorities only when criminal proceedings have been instituted. Such an obligation also applies in Finland, Italy, Luxembourg (a reporting of criminal/illegal activities must be made to judicial authorities by entities having knowledge of those activities), and the Netherlands.

On the contrary, Portugal, Spain, Sweden and the UK do not have such legislation.
17. If not, would your community agree to do so?

Among those countries that do not provide any legal obligation for financial organisations to provide judicial authorities with data on the financial situation of their clients, only the UK organisation stated that it would agree to do so.
18. Is there a national databank of failed entrepreneurs in your country?

The majority of targeted organisations are aware that their country maintains a national databank of failed entrepreneurs. Exceptions include Luxembourg, Sweden, the Netherlands and the UK. A UK organisation added that such a national data bank would not be acceptable, as it would be completely contrary to an entrepreneurial culture.
19. Is this databank open to consultation by financial institutions?

All targeted organisations within the financial community that answered stated that the existing national databank is indeed open to consultation by financial institutions.

A Spanish organisation answered that there was a limit to such a consultation: insofar as it is subject to prior agreement by the entrepreneur.
20. Does your community receive other external information about failed entrepreneurs?

The majority of targeted organisations within the financial community stated that they benefit from external sources of information about failed entrepreneurs: the Mercantile Credit Agency in Austria, several registers in Italy, several insolvency and late payers registers in Spain, through newspapers and by subscribing to material from the Credit Reference Agency in Sweden.

The Dutch and British organisations targeted were not aware of the existence of such external sources of information.
21. If yes, is it useful?

Those targeted organisations who have access to external sources of information about failed entrepreneurs unanimously agreed that it is useful.
22. According to your experience and/or your business vision what are the most common reasons for business failure?

The targeted organisations were asked to choose the most common reasons from a provided list. A distinction was made between large enterprises on the one hand, and medium, small and micro enterprises on the other hand.

A cross-analysis of answers received from the targeted organisations highlights that according to the opinions of the financial community, the most common causes of business failure are:

**For Large enterprises:**

- management skills/poor management  
  (*Austria, Finland, Portugal, Spain, Sweden, Netherlands, UK*)
- financial  
  (*Austria, Finland, Italy, Luxembourg, Portugal, Sweden, UK*)
- external business conditions (loss of market/main customer; rent review/other increase overhead)  
  (*Austria, Finland, Italy, Portugal, Spain, Sweden, UK*)
- legal disputes  
  (*Italy, Luxembourg,*)
- failure to deal with Income Tax/Corporation Tax affairs or VAT  
  (*Luxembourg*)
- personal extravagance/excessive drawings or remuneration  
  (*Spain*)

**For Medium/Small/Macro enterprises:**

- management skills/poor management  
  (*Austria, Finland, Italy, Luxembourg, Portugal, Spain, Sweden, Netherlands, UK*)
- external business conditions (loss of market/main customer; rent review/other increase overhead)  
  (*Austria, Finland, Italy, Portugal, Spain, Sweden, UK*)
- relative youth or lack of experience of the entrepreneur  
  (*Austria, Finland, Italy, Luxembourg, Sweden*)
- failure to deal with Income Tax/Corporation Tax Affairs or VAT  
  (*Finland, Luxembourg*)
Bankruptcy and a fresh start: stigma on failure and the legal consequences of bankruptcy

- financial
  (Finland, Italy, Portugal, Sweden, UK)

- personal extravagance/ excessive drawings or remuneration
  (Portugal, Spain)

It appears from the answers received that the financial community considers a variety of reasons to be responsible for business failure.

The most commonly raised reasons for the failure of large enterprises are management skills/poor management, financial, and external business conditions.

For medium, small and micro enterprises, the reasons for failure appear to focus more on the individual entrepreneur: the issue of management skills was frequently raised. Also of importance important was the issue of the relative youth or lack of experience of the entrepreneur. Subject to those exceptions, the same reasons as for large enterprises seem to apply (financial difficulties, external business conditions). A limited number of countries raised the issue of personal extravagance.

Finally, it should be stressed that only one of the proposed causes was never raised: that of fraud. It therefore appears that within the financial community, fraud is not considered as a major cause of business failure. The financial community in this way appears to be more aware of “structural” problems (financial and management problems) and the positioning of the business on the market (external business conditions) as the main reasons for business failure.
Role of banks in the prevention of failure

23. What would you modify in order to reduce the number of bankruptcies / business failure?

The targeted organisations were asked to choose from among a series of possible measures to reduce the number of bankruptcies/ business failures.

Several organisations failed to respond to this question.

Answers were ranged as follows:

- Use more severe criteria for the attribution of credits to companies (Austria, Portugal, Sweden)

- Provide for a better control of companies (Austria, Italy, Luxembourg, Portugal, Spain, Sweden, UK)

- Negotiations (Portugal)

- Prevention and intervention by judicial organisms (Luxembourg)

- Intervention by financial institutions (Netherlands)

- Others

(Italy: prevention by agreement with creditors. The Italian Bankers Association argued in favour of the adoption of an out-of-court procedure based on the drawing up of an adjustment plan aimed at overcoming the economic difficulties of the business, which may find itself only temporarily unable to discharge its obligations.

A UK organisation provided the survey with a complementary statement of principles issued by the BBA in 2001.)

It appears that for the targeted financial organisations, the preferred way for reducing the number of bankruptcies/ business failures would consist of providing for the better control of companies. However, the answers given highlight that the financial community does not believe that this control should achieved through the use of judicial intervention or via intervention by financial institutions.
24. Do you believe that banks have an important role to play in the prevention of bankruptcy/business failure?

Surprisingly if considered in parallel with the answers to the previous question, the majority of targeted financial organisations agreed that they have an important role to play in the prevention of bankruptcy/business failure.
25. *What are the criteria, used by your members, in order to evaluate whether the entrepreneur represents a risk?*

The most commonly expressed criteria, used by members of the financial community, to assess whether an entrepreneur represents a risk were the following:

- age of the entrepreneur
- lack of experience
- business plan
- sector of activities
- previously failed
- previous external control
- judicial control (concordat/judicial composition)

Several of the targeted organisations chose to stress all criteria, and the majority of them chose at least: the lack of experience, the business plan, and the fact that the entrepreneur had previously failed. These latter three criteria would appear to be the most important reasons for the financial community’s reluctance with regard to an entrepreneur who represents a potential risk.
26. Do your members have internal control mechanisms for the detection of companies that may be approaching distress?

The targeted organisations from all countries, with the exception of Luxembourg, agreed that their members have internal control mechanisms for the detection of companies that may be approaching distress.
27. Which control is most efficient for the detection of companies in possible financial difficulty?

Two primary means of control for the detection of companies in potential financial difficulties were identified by the targeted financial organisations.

First, the presence of representatives of the organisation at the board of directors (Austria and Italy). Linked to this is the overall control over the management of the target company (Finland).

The second way identified by the majority of targeted organisations included: surveillance of the financial state of the company, of its business line and of the economic sector (Austria), regular reporting activity; requiring recent documents from the company (Luxembourg), deep control of balance sheets, accounts (Spain), close follow-up of results and cash flow and general financial situation (Sweden).

Italy also highlighted the constant monitoring of business customers by banks and the use of scoring systems.
Consequences of failure

28. If a client is facing business failure, do your members, before providing new credit, evaluate its situation on a case-by-case basis?

All the targeted financial organisations agreed that the provision of new credit to a client facing business failure is subject to a case-by-case evaluation of its situation. This unanimous attitude reflects the reluctance of the financial community to businesses having faced financial difficulties, and the stigma associated with these businesses.
29. If no, do your members apply a standard procedure?

In view of the limited number of responses received, it is impossible in this instance to highlight a trend.
30. Would your member’s attitudes change if a professional expert assisted a client, facing business failure?

The opinion of the members of the financial community appears relatively divided on whether their attitude would change if an expert assisted the client facing difficulties. Only a small number of organisations (4 out of 13) agreed that they would not change their attitude in such a case, while many of the targeted organisations still stated that such a measure would incur changes of attitude on their part.

31. If yes, which expert do your members trust the most?
   Please rank your choice.
   (lawyer, accountant, auditor, crisis manager, others)

Among the targeted financial organisations that stated that they would react more favourably if the client facing difficulties was assisted by an expert, the crisis manager was the preferred choice, followed by the auditor, the lawyer and the accountant. However, the classification is not sufficiently precise for it to be representative of a definitive trend.
32. What are the consequences of the distinction, if any, between fraudulent and non-fraudulent bankruptcy?

Several targeted financial organisations failed to answer this question.

The Italian and Portuguese organisations pointed to the legal (criminal) consequences of fraudulent bankruptcy.

Some targeted financial organisations mentioned the very harsh consequences for a fraudulent bankruptcy.

A Luxembourg organisation argued that customers having caused fraudulent bankruptcy would not be accepted anymore for new projects. Similarly, a Swedish organisation stated that fraudulent bankruptcy entails exclusion from the bank in the future.

An Austrian organisation argued that in both cases of fraudulent and non-fraudulent bankruptcy, the client is “absolutely unworthy of credit”. This is clear evidence of stigma.

A UK organisation observed that a fraudulent bankruptcy leads to future difficulty in raising credit.
A fresh start

33. Do you think that the legislator should promote the opportunities for a fresh start for a business previously involved in bankruptcy?

The majority of the targeted financial organisations appear to be in favour of the promotion, by the legislator, of opportunities for a fresh start for a business previously involved in bankruptcy. However, they are far from unanimous on this question. No justifications were given either way, and we are forced to conclude that although there is some degree of will to enable businesses to benefit from a fresh start, the degree of reluctance towards such a proposition is still high. In the UK, an organisation supported the proposition, subject to the absence of fraud. Another organisation pointed out that the legislation is already flexible enough to encourage business (as opposed to company/ legal entity) rescue.

An Italian organisation observed that a firm’s insolvency may be caused by a slowdown in the economy, which inevitably affects the solvency of even a sound, and efficient company. The debtor must accordingly be allowed back into the market when the company is in a position to resume normal operations, possibly through new agreements with creditor (usually banks). To this end, the legal system must favour the granting of further finance (indispensable to the firm’s recovery), without running the risk of seeing such claims revoked or incurring other responsibilities, possibly penal ones.
34. Do you think that the legislator should work to eliminate the stigma affecting the business life of an entrepreneur previously involved in a bankruptcy?

The targeted financial organisations seem to be divided on the issue of whether the legislator should work to eliminate the stigma affecting the business life of an entrepreneur previously involved in a bankruptcy.

The most positive answer came from an Italian organisation, which appears to believe that the legislative reform should eliminate the personal restrictions in connection with entry into the public register and provide for their automatic cancellation when the collective procedure is concluded (at present, a court sentence is required). A targeted organisation in Luxembourg stated that the legislator should primarily establish rules in order to “force” liquidators (or other bodies involved) to close and regularise bankruptcy files as soon as possible/within a reasonable period time.

A UK organisation observed that although the stigma exists, it is not so overwhelming as to prevent an entrepreneur starting again with a good business proposition.

A Swedish organisation limited its positive answer by the idea that the entrepreneur should not have been repeatedly involved in bankruptcies. On the contrary, the Swedish Bankers’ Association declared that such measures are not part of the legislator’s competencies.
The financial community therefore seems interested in a very limited way in the stigma affecting the business life of an entrepreneur previously involved in a bankruptcy.
35. Should the legislator promote a fresh start and eliminate stigma for fraudulent bankrupt persons?

The responses received from targeted organisations in the financial community were divided on the issue as to whether the legislator should promote a fresh start and eliminate stigma for fraudulently bankrupt persons. A majority answered in the negative, thus expressing their reluctance to allow fraudulently bankrupt persons to benefit from a “clean” fresh start. Luxembourg observed that favouring such a fresh start should be subject to very severe conditions. A UK organisation indicated that stigma should be reduced, but not in the case of fraudulent bankruptcy.
3.3. Questionnaire for the financial community at national level

36. Do your members agree with the idea that failed entrepreneurs often learn from their mistakes and that they will be more successful in the future?

The majority of targeted organisations answered positively that their members do believe that failed entrepreneurs often learn from their mistakes and that they will be more successful in the future, thus expressing a certain degree of trust in failed entrepreneurs. Two answers provided an opposing opinion, stating that this would depend upon the case in question. Several answers also highlighted that the failed entrepreneur’s new business would “probably” rather than “certainly” benefit from this failure. The financial community’s reluctance towards the failed entrepreneur is in this case again apparent.
37. Do you believe that banks have an important role to play in the restart of a failed entrepreneur?

Despite the above stated reluctance of the financial community towards previously failed entrepreneurs, the almost unanimous agreement - that banks do have an important role to play in the restart of a failed entrepreneur - demonstrates that banks do feel concerned with helping a previously failed entrepreneur to start a new business.

Some limiting comments were however provided, such as playing a role only in so far as the bank takes part in the restart process by disclaiming parts of the given credit, or a Finnish organisation’s statement that “banks do not provide risk capital, they take credit risk”.

3.3. Questionnaire for the financial community at national level
38. Would your members accept to provide new credit to an entrepreneur that has previously faced bankruptcy/failed?

The targeted organisations, consistent with their declared positive attitude towards previously failed entrepreneurs, similarly (almost) unanimously agreed that the members of the financial community would accept to provide new credit to an entrepreneur that has previously faced bankruptcy/failed.

Several organisations however pointed out that such provision of credit is made on a case by case basis, depending on the business potential and on the credibility of the entrepreneur, and subject to more severe criteria and stronger guarantees, as well as insisting on the close scrutiny of the business plan.
3.3. Questionnaire for the financial community at national level

39. If yes, do your members put restrictions on providing credit?

The above positive statements appear to be strongly limited by banks who, in the majority, would indeed put restrictions on the provision of credit to the failed entrepreneur.

40. If yes, what kind of restrictions?

The restrictions referred to by the targeted financial organisations consisted mainly of the following:
- Provision of adequate securities for the debts and reinforced guarantees, collateral (mortgage and pledge),
- the respect of fixed goals expressed in the business plan, more careful assessment.

41. If yes, how long would such restrictions apply?

Very few targeted organisations responded to the question of duration of the application of restrictions – if any - by members of the financial community.

The main answers were: on the one hand, as long as the client is not completely creditworthy, and on the other hand, during the whole investment period, at certain determined scheduled dates.
Bankruptcy and a fresh start: stigma on failure and the legal consequences of bankruptcy

- **External control**

43. According to your experience, does the entrepreneur consider that the external manager can reduce the stigma on business facing difficulties?

The majority of targeted organisations seemed to believe that the entrepreneur considers that the external manager reduces the stigma on business facing difficulties.

A UK organisation made the distinction between the court-appointed administrator, in which case the entrepreneur would not consider the external manager to be able to reduce the stigma, and the crisis manager, who would be better positioned to reduce the said stigma. The same organisation further added that they do not feel that, in general, any stigma is associated with difficulties as opposed to failure.
44. Do you think that the external control should be under supervision of the judicial authority?

The majority of the financial targeted organisations rejected the idea of judicial supervision of the external control.

A UK organisation, which agreed with placing the external control under the supervision of the judicial authority, nevertheless observed that the manager should have a free hand and should not have to resort continually to the court for decisions, thus expressing the same reluctance as other targeted organisations towards judicial supervision.
45. Do you think that the external control should be under the control of creditors?

A number of the targeted organisations appeared to prefer placing the external control under the control of creditors than under the supervision of a judicial authority.

For instance, an Italian organisation was of the opinion that rather than external monitoring, they would prefer to entrust the oversight of the adjustment plan’s implementation to the creditors, as parties that are directly involved and hence interested in the success of the adjustment. It further advocated the institution of a body such as the “Committee of creditors” (with functions different from those envisaged by the current Bankruptcy Law) and which would also be comprised of experts capable of judging the real possibility of restoring the firm to a sound situation.

A UK organisation, rejecting the idea of external control under creditors’ control, argued that this has been the system in the UK in respect of banks holding detention/ floating charges over a company’s assets and has been extremely successful in achieving business rescue. However, it would not agree with the idea of entrusting such control to creditors as a whole.
46. Would creditors of a business facing difficulties consider the appointment of a crisis manager an appropriate measure?

The targeted organisations almost unanimously agreed that the appointment of a crisis manager would be considered an appropriate measure by the creditors of a business facing difficulties.
47. What do you think about the way in which domestic legislation and regulation provide for control on companies in difficulties (very good, satisfactory, unsatisfactory)?

Very good: UK, Finland
Satisfactory: Netherlands, Sweden
Unsatisfactory: Spain, Portugal, Luxembourg, Italy, Austria

It seems that the feeling of dissatisfaction with regard to the way domestic legislation and regulations provide for controls on companies in difficulties takes predominance over the sense of relative/total satisfaction within the financial community.

48. Which type of control is used in your country (external, internal, judicial, others)?

Italy: judicial
Portugal: judicial
Spain: judicial
Luxembourg: internal
UK: external/ internal
Austria: all 3
Sweden: all 3
Netherlands: different

A comparison of the types of control used in the various countries reveals that judicial control is the most common method employed.

Two countries however provide a combination of external, internal and judicial controls.

Internal control therefore also appears as well spread.

A cross comparison of these two questions also reveals that the most common type of control which is not combined with another type of control – the judicial control - is also felt by the financial community to be the least satisfactory form of control of companies in difficulties.
49. What do you think about the way domestic legislation and regulation deal with bankruptcy/business failure in terms of creditors’ interests (very good/ satisfactory/ unsatisfactory)?

*Very good*: Netherlands, UK  
*Satisfactory*: Luxembourg, Sweden  
*Unsatisfactory*: Austria, Finland, Italy, Portugal, Spain (important reform is pending)

From the answers received from the targeted financial organisations, it appears that there is a predominant sense of dissatisfaction towards the way domestic legislation and regulations deal with bankruptcy/business failure in terms of creditors’ interests. Only the Dutch and the British targeted organisations stated that creditors’ interests are very well dealt with.

50. What do you think about the way the domestic legislation and regulation deal with bankruptcy/business failure in terms of debtors’ interests (very good/ satisfactory/ unsatisfactory)?

*Very good*: Austria, Finland  
*Satisfactory*: Italy, Portugal, Sweden, Netherlands, UK  
*Unsatisfactory*: Luxembourg, Spain

It appears that the targeted financial organisations appear to be generally satisfied with the way the domestic legislation and regulations deal with bankruptcy/business failure in terms of the debtors’ interests. There are, however, areas for improvement.
3.4. KEY RESULTS OF THE QUESTIONNAIRES FOR THE COMMUNITIES: A SUMMARY OVERVIEW.

3.4.1. Questionnaire for the general community at national level

General knowledge

The general community seems to be knowledgeable about bankruptcy and business failure in general, but not on the difference between insolvency and bankruptcy. There also seems to be a general lack of interest regarding these matters, as questions from consumers on the issue of bankruptcy are very rare.

Stigma

In general a stigma is attached to bankrupt enterprises, although no clear distinction was evident between the issue of a business in distress and a business that recovered from distress. The majority of the targeted organisations indicated that the general community is not informed or knowledgeable about the difference between fraudulent and non-fraudulent bankruptcy.

Information

The targeted organisations indicated that there is reliance almost completely on media sources for information on failure business. The targeted organisations do not collect any specific data on bankruptcies or business failures.

Reasons for and consequence of failure

With regard to reasons for failure, the most sensitive sectors appeared to be the credit sector (where failure would mainly be caused by financial problems) and the horeca/hospitality/health sector (where business failure would mainly be due to a lack of management skills).

The general attitude of the consumer organisations regarding consequences of failure was mixed, half rather discouraging their members from dealing with a business in difficulties.

The general community generally agree that failed entrepreneurs often learn from their mistakes, which might make them more cautious to enter into new business ventures, and that legislation should be introduced to limit the stigma associated with a bankruptcy.

3.4.2. Questionnaire for the business community at national level

Stigma

Most of the targeted organisations agree that a stigma is created and attached around the failure of a business and/or bankruptcy.
The majority believes entrepreneurs make a difference between a business in distress and a business that has recovered from distress.

All targeted organisations agreed that a fraudulent bankrupt business is not viewed in the same way as a non-fraudulent bankrupt business.

**Information**

The sources most commonly used are: information provided by colleagues, competitors, the business sector, media, credit or financial institutions, except information covered by banking secrecy acts and creditors.

A majority of the organisations indicate that their members enquire whether a bankrupt person was fraudulent. Furthermore, most organisations have databanks listing entrepreneurs according to solvency ratings, the main source of information for such insolvency ratings – generally considered as reliable - being private databanks. However, the latter do not generally differentiate between fraudulent and non-fraudulent bankruptcy. Most of the organisations targeted agreed that information relating to the distinction between fraudulent/ non-fraudulent bankruptcies is relevant to their business sector.

**Reasons and consequences of failure**

Large enterprises indicate that the most common reason for business failure could be attributed to poor management skills, followed by financial problems, and external business conditions, such as loss of market, main customer, rent review, and increased overheads. Fraud, personal extravagance, and failure to deal with income tax, were not considered to be a common reason.

Medium, small and micro enterprises indicate that the reason for business failure could be attributed (in descending order) to financial difficulties, external business conditions, lack of experience, and management skills. Contrary to large enterprises, the young age or the lack of experience of the entrepreneur is considered as an important and common reason for medium to micro business failures. Fraud, personal extravagance, legal disputes were not considered to be one of the most common reasons, whereas failure to properly comply with income tax regulations, corporation tax affairs and VAT were ranked among the first three reasons according to smaller businesses.

With regard to the consequences of failure, there appears to be a general reluctance to deal with a business facing difficulties. It often depends on the current economic situation, the importance of the customer relationship, the nature and extent of difficulties encountered and is considered on a case-by-case basis. However, an encouragingly sign is that all targeted organisations unanimously agreed that their members would be willing to deal with a business who managed to recover from failure.
Restrictions

There is a general awareness of the restrictions applicable to a bankrupt business in terms of the bankruptcy and insolvency laws. Most organisations are reluctant to sell shares to a bankrupt person. Most organisations would employ a bankrupt person; however there seems to be a reluctance to employ such a person at high management levels. Guarantees are required by the organisations when dealing with a person who has failed in the past.

Fresh start

Most targeted organisations are in favour for steps to be implemented that will encourage a fresh start and eliminate any stigma that usually remains with the entrepreneur, except in the case of fraudulent activity. Almost all targeted organisations agreed that failed entrepreneurs often learn from their mistakes and that they will be more successful in the future, expressing a positive “second chance” attitude. However, currently entrepreneurs have to deal with the burden of the stigma of bankruptcy, making it more difficult to achieve positive results.

External control

The business community generally does not want the legislator to strengthen the level of control over the business life of an entrepreneur previously involved in a bankruptcy, as opposed to those entrepreneurs “currently facing difficulties”. The majority of the targeted organisations indicated that external control over a business in distress should not be under the power of the judicial authorities, and even less under the control of creditors. The appointment of a crisis manager was generally considered a step in the right direction both for creditors and the employees of the business in distress.

3.4.3. Questionnaire for the financial community at national level

Stigma

A majority of organisations considers that the failure of a business or its bankruptcy attaches a stigma. Most organisations also distinguish between a business in distress and a business that has recovered from distress, and unanimously admit that businesses failing as a result of fraudulent activity are treated differently.

Information

Most targeted organisations indicated that the financial community collects historical data (mainly accounting and general credit information), including information on any financial difficulties of their clients. The data collected appear to differentiate between fraudulent and non-fraudulent bankruptcy in a few countries. The data is not shared with other financial institutions – though most organisations seemed to believe that sharing the information could prove helpful – but is often shared with their business partners. In several countries a legal obligation exists to submit financial data, concerning their clients, to judicial authorities when criminal proceedings have been
instituted. Furthermore, most targeted organisations are aware that their country provides a national databank of failed entrepreneurs, which is generally available to financial institutions. Most targeted organisations indicated that external sources of information about failed entrepreneurs are useful.

**Reasons and Consequences of Failure**

The main reasons identified for the failure of enterprises were poor management skills, financial difficulties and external business conditions. However, medium, small and micro enterprises specifically identified the lack of experience and the relative young age of the entrepreneur as a main cause for failure.

All targeted financial organisations indicated that there is reluctance in extending further credit to a client in financial distress and is typically subject to a case-by-case evaluation. Although this is perceived as a stigma, most financial organisations are reacting to the situation to manage its exposure to clients in financial distress. There also seems to be a general view that organisations would not change their attitude if an expert, such as a crisis manager, assisted the client. Most organisations indicate that they will act more strictly and severely with companies or individuals associated with a fraudulent bankruptcy.

**Fresh start**

Most of the targeted financial organisations seem to be in favour of the promotion, by the legislator, of opportunities for a fresh start for a business previously involved in bankruptcy. There seems to be a divided opinion as to whether the legislator should work to eliminate the stigma around individuals involved in fraudulent bankruptcies. They do believe that failed entrepreneurs often learn from their mistakes and that they will be more successful in the future. They also believe that banks plays an important role in the restart of a previously failed entrepreneur, and would extend credit to such an individual, subject to providing adequate securities and guarantees, and reaching goals expressed in the business plan.

**External control**

There seems to be a general opinion that the appointment of an external manager can reduce the stigma associated with a business in distress, although they seem to reject the idea of judicial supervision, but rather to place more control in the hands of the creditors. Creditors always view the appointment of a crisis manager in a positive light.
2. PROJECT METHODOLOGY

This section summarises the methodology applied in order to compile this report. It includes our approach, the activities undertaken and the unforeseen events encountered.

2.1. INTRODUCTION

The project “Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy” consists of two parts:

- Part 1: Stigma on Failure: this part analyses the attitude of the public, the business community and financial institutions towards business failure and bankruptcy.

- Part 2: Legal Consequences of Insolvency: this part analyses the following:
  
  - The existing procedures in the Member States and the US aimed at detecting businesses with financial difficulties at an early stage;
  - The possibilities, in the different Member States and the US, for economically viable businesses to continue its activities; and
  - The legal consequences of bankruptcy and the possibilities for a fresh start.

2.2. PART 1: STIGMA ON FAILURE

2.2.1. The Targeted Communities and Organisations

In order to assess the extent of the Stigma, we formulated a questionnaire to send to targeted communities (general, business and financial) and organisations. The targeted communities and organisations have been selected from a database of Deloitte & Touche (a partner of the consortium), and its international network. The European Commission reviewed the list of the targeted organisations before sending the questionnaires.

Initially the list of targeted organisations comprised of 319 enterprises. An introductory phone call was made and during this call we had the opportunity to explain the general purpose of the project, how the project relates to them as targeted organisations and to make them aware of the forthcoming faxed questionnaire. At this point, a number of the targeted organisations, in particular the U.S. organisations, declared that they would not participate in the project due to a variety of reasons and as a result a modified list of targeted organisations was compiled, which reduced the number to 289 enterprises.

A copy of the final list of the targeted organisations, segregated into each of the mentioned communities, is enclosed.

2.2.2. The Questionnaires and the Interviews
From the introductory telephone calls, we realised that there is a significant difference in the perception of bankruptcy between the three defined communities, and as a result we prepared three different questionnaires tailored for each targeted communities (Appendix U). The questionnaires to the business and financial communities were designed to be more technical. A copy of the templates is enclosed.

The aforementioned templates were submitted to the European Commission at the meeting held on 21st December 2001 at the Directorate. Based on valuable input from the European Commission and in order to increase feedback, the templates were simplified. This was mainly achieved through the use of closed (Yes/No) questions, however space was also provided for the targeted enterprise to additional comments with each question. Conservatively estimated the template would take approximately 20 minutes to complete.

The questions to the business and the financial communities were designed to receive clear feedback on the following issues:

- **The Stigma.** The questions evaluate the existence of the Stigma for businesses that failed, business in distress, business recovering from distress, start-up IT businesses in difficulty, and fraudulent and non-fraudulent bankrupt business.
- **The information.** If the Stigma exists, it is usually shared and enhanced through the availability of information. The questions request examples of any available information that is shared by the communities concerning businesses in difficulty.
- **The reasons for failure.** The questions evaluate what the degree of knowledge and awareness of the targeted communities is in respect to the most common reasons for business failure.
- **The role of the organisations in the prevention of failure.** The questions explore whether organisations could adopt special measures to prevent the failure of the business. Furthermore, the questions also explored what criteria is used to evaluate risk, whether there are internal mechanisms to detect that a business is in distress, and who are the most appropriate professionals to assist the business when in difficulty.
- **The fresh start.** The questions focus on whether the enterprises believe that legislation should promote a Fresh Start and eliminate the Stigma of businesses previously involved in bankruptcy and if the enterprises provide credit to businesses that have previously failed.
- **The external control.** The questions evaluate the possibility to introduce an external control over a distressed business and if such a control should be exercised by the public authorities and/or by ad hoc professionals (such as anti-crisis managers and mandataires ad hoc according to the French trend).

The questions to the general community were designed to be less technical, to enhance feedback, even if the subject “Stigma and Fresh Start” often does not represent a priority for them. The questions focused on the following issues:

- **General knowledge.** The questions evaluate the degree of awareness of the targeted organisations within the specific field.
• **The Stigma.** The questions focus on whether the general community distinguishes between a business in distress, a business that has recovered from distress, and a fraudulent bankrupt and non-fraudulent bankrupt entrepreneur.

• **The availability of information.** The questions determine what information is gathered by the general community and to identify its sources.

• **Reasons for failure.** The questions evaluate what the degree of knowledge and awareness of the general community is in respect to the most common reasons for business failure, which is expected to be different from the other communities.

• **Consequences of failure.** The questions should clarify what the commercial attitude of the consumer is vis-à-vis the failed entrepreneur.

• **The fresh start.** The questions evaluate what the perception of the general community and consumers is on the fresh start of an entrepreneur who has previously failed, especially differentiating between a fraudulent bankruptcy and the non-fraudulent bankruptcy. Consumers are often seen as the least important party to a bankruptcy and therefore, important to understand whether the risk of bankruptcy is considered as deterrent to set up a business.

The questionnaires were initially created in English. We contacted the targeted organisations by phone, during which they confirmed their interest to contribute to the survey. A vast majority of the organisations were able to communicate fluently in English. However, in order to have a better communication with the targeted organisations, where possible, we used the language of the contact person.

From the first round faxed questionnaires, we only received 36 replies out of 270 (Of the 36 replies received, just 22 provided a completed questionnaire). It was therefore suggested by the European Commission, following the meeting held on 28 February 2002 in Brussels, that we send a second distribution of faxed questionnaires whilst also making the following improvements to the process in order to increase the potential number of the replies:

1. The questionnaires were translated into French and German.
2. The number of the targeted organisations was increased to 289 enterprises.
3. It was agreed to, not only send the questionnaires to the newly identified organisations, but also re-send the questionnaires to the previously contacted organisations.
4. Further phone calls were made to notify them of the revised faxed questionnaire, explaining again the objective of the project, and requested the targeted organisations to complete and return the questionnaire. Our approach was not rigid; often we completed the questionnaire during a phone interview with the targeted organisations, or communicated with them by email upon request. This flexible approach resulted in increased feedback.

According to the Terms of References of the project and our technical proposal, we interviewed targeted organisations to determine the expectations of their members and the official position adopted by the organisations within the field of the Stigma and the Fresh Start.

The interviews were conducted over the phone with the respective representatives of the organisations, by following the format of the questionnaires. In some cases we
completed the questionnaire based upon the interview responses and additional information received from the targeted organisations.

2.2.3. Methodology Implemented

A task force was created to follow up on the targeted organisations. This was done through a number of telephone calls and faxes. The data collection process are further explained below:

- **First phone call**: a first phone call was made between the 15th and the 25th of January. The additional organisations identified, as mentioned above, were contacted by phone between the 15th and the 21st of March. A brief explanation of the project, carried out on behalf of the European Commission, was made and provided explanatory information to the targeted organisations. The call allowed us to double-check the details of the organisations and, if requested by the organisation, sent a copy of the questionnaire (fax or email).

- **First fax sending session**: following the aforementioned phone call, the questionnaires were fax to the targeted organisations. The questionnaires were sent between the 28th of January and the 6th February. The additional organisations identified, as mentioned earlier, questionnaires were sent between the 15th and the 21st of March. A deadline of one working week was imposed, however we only received 20 replies at the time of the deadline.

- **Second phone call**: the information received was not considered to be a representative sample. Therefore, a second round of phone calls were done. The objective of the project was explained again and assurance was provided that all information will be kept in the strictest confidence. The second phone call was carried out between the 14th and the 15th of February. The additional organisations identified were contacted between the 15th and the 20th of March. After this second phone call in February an additional 16 replies were received. If requested by the organisation, a copy of the questionnaire (fax or email) was sent again.

- **Third phone call**: a third round of telephone calls were done on the 4th of March. Ten lawyers were assisting the targeted organisation to complete the questionnaires. If requested by the organisation, a copy of the questionnaire (fax or email) was sent again. After the third round of phone calls, only three additional replies were received.

- **Fourth phone call**: Ten lawyers were used between the 15th and the 20th of March to make a fourth round of telephone calls and interviews. If requested by the organisation, a copy of the questionnaire (fax or email) was sent again. After the fourth round of phone calls, 24 additional replies were received.

- **Second fax sending session**: according to the suggestion of the European Commission, and our technical proposal, in order to increase the degree of feedback, the questionnaires were translated into French and German and resent to the relevant targeted organisations. The first template of the questionnaire was
Bankruptcy and a fresh Start: stigma on failure and legal consequences of bankruptcy

prepared only in English. Because of the lack of reaction of the targeted organisations, we translated the questionnaire. The template sent to the organisations provided the questions in the 3 languages in order to reduce eventual language barriers. It should be noted that once the new version was revised, we re-sent the questionnaires to all organisations provided in the list. We re-sent the questionnaire also to organisations that had already provided their answer in order in order to grant equal treatment to future answers.

- **The final phone call:** a final phone call was done prior to the 6th of May. This phone call aimed to assist the reluctant organisations to provide a feedback before the completion of the draft of the final report. If requested by the organisation, a copy of the questionnaire (fax or email) was sent again.

### 2.2.4. Degree of contribution of the targeted organisations

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<th>Answers Received</th>
<th>Blank Answers</th>
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<td>&gt;289</td>
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- Degree of participation of the targeted organisations per country

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- Degree of participation of the targeted organisations per country and per community.

**General Attitude**

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<th>Answers Received</th>
<th>% of Participation</th>
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<tr>
<td>DK</td>
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<td>33%</td>
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</table>

1 Please, note that we sent the questionnaires to 289 organisations, but the actual number of the questionnaires sent was more than 289 because during the phone calls, the contact persons often asked us to re-send them an additional copy by fax or email.

2. Project Methodology
Bankruptcy and a fresh Start: stigma on failure and legal consequences of bankruptcy

### Business

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<th>Answers Received</th>
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From the results of the above and analysis of the replies, indicators relating to the Stigma on business failure were developed and recommendations aiming at eliminating or reducing the Stigma attached to failed entrepreneurs were formulated.

2. Project Methodology

39
2.3. PART 2: LEGAL CONSEQUENCES OF INSOLVENCY

Insolvency law specialists in each Member State were asked to prepare comprehensive reports on the legal framework of bankruptcy. To ensure comparability, uniform guidelines for their reports were designed to be followed by each expert (Appendix B). Together with this guideline, a questionnaire based on the “Principles and Guidelines for Effective Insolvency and Creditor Rights Systems” prepared by the World Bank, was sent to the experts (Appendix C).

From these individual country reports, a summary overview and a basic comparison between the insolvency legislation by country was documented. More specifically with respect to:

- Detection of businesses in difficulties and warning lights (Section 4.1);
- Legal possibilities to continue economic activity (Section 4.2);
- Legal consequences of bankruptcy and possibilities for a fresh start (Section 4.3);

During a second phase we developed indicators to assess to what extent national insolvency laws act as a deterrent to business survival and the possibility of a fresh start subsequent to bankruptcy.

Finally recommendations were formulated to improve the situation for failed entrepreneurs who wish to make a fresh start.
1. INTRODUCTION

1.1. BACKGROUND

Recent political and legislative developments at the European Union level call for a positive attitude towards risk-taking and failure. In its Communication on the “Challenges for enterprise policy in the knowledge-driven economy”, the European Commission considers that “Europe must re-examine its attitude to risk, reward and failure. Thus, enterprise policy must encourage policy initiatives that reward those who take risks. Europe is often reluctant to give another chance to entrepreneurs who failed. Enterprise policy will examine the conditions under which failure could acquire a less negative connotation and it could be acceptable to try again. It will encourage Member States to review bankruptcy legislation to encourage risk-taking”.

It is with these key weaknesses in mind that the European Commission aims to promote entrepreneurship and competitiveness, to simplify and improve the regulatory environment for businesses, calls for examining the conditions under which failure could acquire a less negative connotation and proposes to encourage the Member States to review bankruptcy legislation in order to encourage risk-taking. Its strategy is clearly oriented to promote the survival of viable businesses, to enable a smooth exit for not viable businesses and to offer the possibility of a fresh start for entrepreneurs who have tried but failed.

Linked directly to all these economic realities, new aspects of insolvency practice await legal solutions by identification of principles and guidelines for an efficient and effective insolvency and restructuring practice. In this line, an emerging trend in the different national legislative systems is the inclusion of a positive policy of rehabilitation for insolvent debtors, through a variety of procedures designed to assist them in overcoming an economic crisis without experiencing the total impact of bankruptcy or liquidation: various procedures (some adapted from existing provisions for the concluding of controlled compositions with creditors) have been implemented. Under these procedures, the debtor can enjoy the protection of a legal moratorium against acts of enforcement by the creditors singly or collectively, for a defined period during which efforts can be made -under professional guidance or control- to restructure the debtor's affairs so that equilibrium is eventually capable of being restored. The range of insolvency procedures available within each country demonstrates several contrasting approaches to the regulation of the problems of insolvency. U.S.

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1 Charter for Small Enterprises adopted by the General Affairs Council, 13 June 2000 and welcomed by the Feira European Council, 19/20 June 2000
bankruptcy law is characterised as pro-debtor because it allows managers (appointed by equity holders and so thought to be beholden to them) to continue to run the firm while negotiations are under way. In the United Kingdom, an insolvency practitioner would be put in charge, giving to him the exclusive right to propose a reorganisation plan. Entrusting the operation to the existing board of managers or appointing a new overseer could have consequences on the timing and negotiations of the bankruptcy filing. European bankruptcy occurs more quickly, not because of the procedures but because of the negative attitude of the financial parties towards the failing entrepreneur.6

Nevertheless, an entrepreneurship policy at the international level should encourage an effective insolvency and creditor rights systems built on the simple premise that sustainable market development relies on access to affordable credit and capital investment. A policy in favour of the entrepreneurship should rely on quick and easy rehabilitation legal procedures, provide sufficient protection for all those involved in the process, provide a structure that permits the negotiation of a commercial plan, enable a balance between the business and creditor’s interests, offer the necessary standard of protection for the creditors; and provide for judicial or other supervision to ensure that the process is not subject to manipulation or abuse.

Furthermore, although there is widespread agreement that the globalisation of trade and enterprise requires a co-ordinated approach to international bankruptcy, the field of bankruptcy law has remained persistently territorial. The philosophical position occupied by “territorialism” or the “grab rule” has prevailed despite the evolution of modern times. When a person or a company with international operations falls into serious financial trouble, each country employs its insolvency laws to grab local assets and administer them locally according to the procedures and priorities of that country’s laws.

At the European level, insolvency proceedings with cross-border effects within the European Union lacked a general framework governing the interference of the various national laws and jurisdictions applicable to such proceedings. This situation affected the aim of the Single Market and gave way to “forum shopping” by the parties involved in the insolvency proceedings and a lack of legal certainty. With the adoption on May 29, 2000 of the European Council Regulation on Insolvency Proceedings, the European Union acquires a new instrument for dealing with the cross-border insolvency. The common rules on insolvency proceedings laid down in the Insolvency Regulation constitute an important step forward in the ambit of legal and judicial co-operation within the European Union.

Within this new co-ordinated European context, the policy for a bankruptcy as a new learning opportunity should constitute a stimulating factor of particular interest for all Member States and an incentive for them to build effective bankruptcy systems.

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6 S. Ramachandran, "Bankruptcy's Role in Enterprise Restructuring: A Hammer to Turn a Screw?" in "Private sector" n 38, p 1, 1995
1.2. **Recent Initiatives**

The Lisbon European Council (held on March 23 and 24, 2000) set the European Union a goal of becoming the world’s leading economy in the world by 2010. The European Charter for Small Enterprises, endorsed at the Feira European Council in June 2000, considers that "some failure is concomitant with responsible initiative and risk-taking and must be mainly envisaged as a learning opportunity" and called for assessing national bankruptcy laws in the light of good practice.

The European Commission responded to this by undertaking several initiatives to identify issues regarding business restructuring, bankruptcy and a fresh start in the European Union.

In September 2000 the Flash Eurobarometer survey No 83 on ‘Entrepreneurial activity’ was conducted. The aim of the survey was to measure the general public opinion regarding entrepreneurial attitude within the European Union and the U.S. One of the results of the survey showed that most respondents agree that a second chance should be given to entrepreneurs who have tried but failed.

Another initiative was the seminar on business failure, organised by the Dutch Ministry of Economic and the European Commission, on 10 and 11 May 2001 in Noordwijk aan Zee, the Netherlands. This seminar focused on the relation between business failure and promotion of entrepreneurship. Approximately 130 representatives of private businesses (i.e. lawyers, accountants and entrepreneurs), international organisations, business support organisations, ministries and universities participated in the seminar. Topics such as bankruptcy law, support measures and post failure obstacles for a fresh start were discussed. The seminar concluded that bankrupt entrepreneurs are confronted with legal and financial barriers and stigma, which act as a deterrent to a fresh start. They also concluded that prevention is more efficient than healing, that a quick discharge is necessary and no unnecessary restrictions should be imposed.

1.3. **Objectives of the Report**

In light of the above, the European Commission launched this project *Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy*. The objectives of this study were, in summary, to obtain current reliable information on the attitude of the public, the business community and financial institutions to business failure and bankruptcy and to analyse the legal consequences of insolvency.

The results of this study allow a comparison of the situation in Europe and the U.S. and will assist in drawing policy conclusions on business failure and its consequences on entrepreneurship.

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7 [http://europa.eu.int/comm/enterprise/enterprise_policy/survey/eurobarometer83.htm](http://europa.eu.int/comm/enterprise/enterprise_policy/survey/eurobarometer83.htm)

8 [http://www.ez.nl/businessfailure/index.htm](http://www.ez.nl/businessfailure/index.htm)


10 [http://www.ez.nl/businessfailure/index.htm](http://www.ez.nl/businessfailure/index.htm)
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- **LIST OF NETWORK MEMBERS**
FOREWORD

This study was achieved through the efforts of various contributors. It grew out of the collective work of a **core team based in Brussels** and a **network of specialists throughout the European Union and the US**. The core team gathered the necessary information, studied and described the existing attitude to failure among the general public, the financial sectors and business partners in the EU Member States and compared those to the situation in the US., and collected relevant legal information and provided a critical analysis of the legal consequences of bankruptcy, in Europe and the US.

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Bankruptcy and a fresh start: Stigma on failure and legal consequences of bankruptcy

Brussels, July 2002
Under the direction of Philippe & Partners, in collaboration with Deloitte & Touche Corporate Finance, the study, necessary for the drafting of the report, has been conducted by the following experts in insolvency law:

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**NOTICE**

The information and opinions contained in this study do not constitute legal advice nor shall the availability of the information and opinions in this study create a relationship of client and professional adviser between Philippe & Partners or Deloitte & Touche Corporate Finance and any reader. Any reader is asked to seek professional legal advice before relying upon any information contained in this study.
According to the Terms of References of the project and our technical proposal, we carried out also interviews with the targeted organisations in order to gauge the real needs of the members of the communities and to know the official position adopted by the organisations within the field of the Stigma and the Fresh Start.

We contacted the targeted organisations by phone and interviewed the representative. From a practical perspective, we decided to carry out the interview in accordance with the questionnaires.

This system allowed us to gather data and process them within the same statistics relating to the questionnaires received by fax.

The data collection operations were accomplished following these phases and organisation:

- First phone call
- First fax sending session
- Second phone call
- Third phone call
- Fourth phone call
- Second fax sending session
- Final phone call

In a second phase, we developed indicators relating to the Stigma on business failure.

Finally, we formulated recommendations aiming at eliminating or reducing the Stigma attached to failed entrepreneurs.

In order to analyse the legal consequences of bankruptcy, national insolvency law experts prepared comprehensive reports about the legal framework for bankruptcy in the Member States and the US. Together with this guideline, a questionnaire based on the “Principles and Guidelines for Effective Insolvency and Creditor Rights Systems” prepared by the World Bank, was sent to the experts.

The analysis of the collected national reports leads to an overview and a basic comparison of the various insolvency legislations in all Member States and the US.

During a second phase indicators were developed to assess to what extent national insolvency law really does act as a deterrent to business survival and to the possibility of a fresh start after bankruptcy.

Finally recommendations are formulated to improve the situation for failed entrepreneurs who wish to make a fresh start.

0.3. KEY RESULTS OF THE QUESTIONNAIRES FOR THE GENERAL, BUSINESS AND FINANCIAL COMMUNITIES: A SUMMARY OVERVIEW.

0.3.1. Questionnaire for the general community at national level
Within the general (consumer) community, the general knowledge is limited to the notion of bankruptcy/business failure, but does not extend to the difference between insolvency and bankruptcy. Furthermore, the members of the general community do not seem to be generally interested by the matter, as questions from consumers on the issue of bankruptcy are very rare.

The answers received on the issue of stigma attached to bankruptcy and the distinction between a business in distress and a business that recovered from distress did not provide a clear common position. Furthermore, the vast majority of the targeted organisations declared that the general public does not know whether there is a difference between fraudulent and non-fraudulent bankruptcy.

The general ignorant attitude of the general community was further assessed by the observation that their members rely almost exclusively on the media as a source of information on business failure. Non-availability of information was confirmed by the fact that targeted organisations do not keep any specific databank on bankruptcies/business failures.

With regard to reasons for failure, the most sensitive sectors appeared to be the credit sector (where failure would mainly be caused by financial problems) and the horeca/hospitality/health sector (where business failure would mainly be due to a lack of management skills).

The general attitude of the consumer organisations as to the consequences of failure was very divided, half rather discouraging their members from dealing with a business in difficulties. The reaction was even more conservative in the context of the fresh start: most organisations admitted that they would warn their members about the previous failure of a business. This trend was however limited by the positive attitude to the idea of legislative promotion of the opportunities available for a business previously involved in bankruptcy, and correlative elimination of stigma – except for fraudulent bankruptcy. According to the answers received, the members of the general community generally agree with the idea that failed entrepreneurs often learn from their mistakes – although they might also be deterred from creating a new business.

0.3.2. Questionnaire for the business community at national level

Within the business community, it appears that most of the targeted organisations that participated in the survey agree that a stigma does surround the failure of a business and/or bankruptcy.

The majority of the targeted organisations of the business community believe that entrepreneurs do indeed make a difference between a business in distress and a business that has recovered from distress.

All targeted organisations of the business community unanimously agreed that a fraudulent bankrupt business is not viewed in the same way as a non-fraudulent bankrupt business.
However, the business community does not hold a significant position in one way or another with regard to the issue of tolerance towards young IT start-ups in contrast with their attitude towards established firms.

With regard to the issue of availability of information, it appears from the information provided by those organisations targeted that all choices that were provided in the questionnaire are indeed used as sources of information for discovering that a business (actual or potential counterpart) faces difficulties. The sources, which appear to be the most commonly used are: information provided by colleagues, competitors, or the business sector, media, and credit/ financial institutions. Information provided by creditors is however important too. A limit that was highlighted was banking secrecy. Furthermore, a German organisation pointed out the information provided by the supervisory entity.

A majority of those organisations targeted appeared to agree that their members do enquire as to whether a bankrupt person is fraudulent or not.

Furthermore, most organisations in the business community hold databanks listing entrepreneurs according to solvency ratings, the overwhelming source of information for such insolvency ratings -generally considered as reliable- being private databanks. The latter do not generally differentiate between fraudulent and non-fraudulent bankruptcy. All the organisations targeted nevertheless more or less unanimously agreed that information relating to the distinction between fraudulent/ non-fraudulent bankruptcies is relevant to their business sector.

The issue of reasons for failure was answered somewhat differently by large enterprises on the one hand, and medium to micro enterprises on the other.

The comparative analysis of the answers received from the business community with regard to large enterprises highlights that the most common highly ranked reason for business failure is lack of management skills and poor management. The two other main reasons (both were very often identified) seem to be linked on the one hand, to financial problems, and on the other hand, to the external business conditions, such as loss of market, main customer, rent review, other increased overheads. Reasons relating to fraud, personal extravagance, and failure to deal with income tax, were exceptionally identified.

The comparative analysis of the answers received from the business community with regard to medium, small and macro enterprises shows that the most common highly ranked reason for business failure was financial difficulties, followed very closely by external business conditions, youth/ lack of experience, and then management skills. It must be pointed out that contrary to large enterprises, the young age or the lack of experience of the entrepreneur is considered as an important and widely spread reason for medium to micro business failures: it was ranked first only by two targeted organisations, but was identified among the three most important reasons by a majority of targeted organisations. Fraud, personal extravagance, legal disputes were only exceptionally identified, whereas failure to deal with income tax, corporation tax affairs and VAT was ranked among the first three reasons for failure for smaller businesses by more organisations than with regard to large enterprises.
With regard to the consequences of failure, the attitude of those organisations targeted appears to be almost fifty/fifty with regard to the issue of willingness to deal with businesses facing difficulties. The attitude adopted towards the latter would often depend upon the current economic situation and the importance of the customer relationship, depending on the nature and level of difficulties encountered, on a case by case basis. However, a general reluctance to deal with a business facing difficulties appears quite strong. Surprisingly, and encouragingly, all the targeted organisations unanimously agreed that their members would be willing to deal with a business that has recovered after failure.

The business community expressed a general position of awareness as to the restriction regime applicable to a bankrupt business, and of tolerance in dealing with a business in insolvency status. The attitude was however divided as to whether the members of the organisations would be willing to get involved in the management of a bankrupt person, and was strongly reluctant on the issue of selling shares to a bankrupt person. Employment of a bankrupt person in a business would often be possible, though positions at the highest management levels would be excluded. Finally, strong extra guarantees would be required when dealing with a person who has failed in the past.

With regard to the issue of a fresh start, a majority of the targeted organisations appear to be favourable to the promotion, by the legislator, of the opportunities for a fresh start for an entrepreneur previously involved in bankruptcy, and to the correlative elimination of stigma affecting the business life of an entrepreneur previously involved in a bankruptcy, the limit being: fraud. Almost all targeted organisations agreed with the idea that failed entrepreneurs often learn from their mistakes and that they will be more successful in the future, thus expressing a positive “second chance” attitude, although such entrepreneurs would have to deal with the burden of the stigma of bankruptcy, making it more difficult to achieve good results.

Finally, as to the issue of external control, the business community generally speaking does not seem to believe that the legislator should strengthen the level of control over the business life of an entrepreneur previously involved -as opposed to currently facing difficulties - in a bankruptcy experience. The majority of the targeted organisations assessed that the external control over a business facing difficulties should not be under the power of the judicial authorities, and even less under the control of creditors. The suggestion in favour of the appointment of a crisis manager was generally well received by the business community, that agreed that it would be considered an appropriate measure both by creditors and by employees of the business facing difficulties.

0.3.3. Questionnaire for the financial community at national level

It appears that in the majority of Member States, the financial community considers that the failure of a business or its bankruptcy entails stigma. Furthermore, most organisations make the distinction between a business in distress and a business that has recovered from distress, and unanimously admit that businesses having incurred fraudulent bankruptcy are treated differently.
Concerning the issue of availability of information, most targeted organisations assessed that the financial community does keep precise data (mainly accounting and general credit information) on the history of their clients and on their eventual financial difficulties. The data kept by the financial community seem to differentiate between fraudulent bankruptcy and non-fraudulent bankruptcy in a (small) majority of cases. Those data are clearly not shared with other financial institutions - though most organisations seemed to believe that sharing the information could prove helpful - but are often shared with their business partners. Several Member States provide a legal obligation to transmit financial data concerning the clients of financial institutions to judicial authorities when criminal proceedings have been instituted. Furthermore, most targeted organisations are aware that their country provides a national databank of failed entrepreneurs, which is generally open to consultation by financial institutions. Most targeted organisations within the financial community provided that they benefit from external sources of information about failed entrepreneurs, considered as useful.

With regard to the reasons for failure, the most commonly raised reasons for the failure of large enterprises are lack of management skills/poor management, financial, and external business conditions. For medium, small and micro enterprises, the reasons for failure seem to concentrate more on the person of the entrepreneur: very highly raised is the issue of management skills. Also quite important is the problem of relative youth or lack of experience of the entrepreneur. Otherwise, the same reasons as for large enterprises seem to apply (financial difficulties, external business conditions).

It appears that for the targeted financial organisations, the preferred way for reducing the number of bankruptcies/ business failures would consist in providing a better control of businesses. However, the answers do not seem to reflect the wish that this control be achieved through judicial intervention nor through intervention by financial institutions. Yet, most targeted financial organisations agree that they have an important role to play in the prevention of bankruptcy and business failure. The financial community generally assesses whether the entrepreneur represents a risk by using the following criteria: the lack of experience, the business plan, and the fact that the entrepreneur had previously failed. Furthermore, targeted organisations from all Member States, except Luxembourg, agreed that their members have internal control mechanisms for the detection of businesses that may be approaching distress. Efficient controls for the detection of businesses in potential financial difficulties include the presence of representatives of the organisation at the board of directors, overall control over management of the target business, and surveillance of the financial state of the business.

With regard to the consequences of failure, all targeted financial organisations agreed that provision of new credits to a client facing business failure is subject to a case-by-case evaluation of its situation. This unanimous attitude reflects the reluctance of the financial community towards businesses having faced financial difficulties, and the stigma being linked to these businesses. Few organisations agreed that their members’ attitude would change if the client facing difficulties was assisted by an expert such as a crisis manager. Finally, most organisations of the financial community assessed the harsh consequences - including criminal - of fraudulent bankruptcy.
The issue of the fresh start called the following conclusions. Most of the targeted financial organisations seem to be in favour of the promotion, by the legislator, of the opportunities for a fresh start for an entrepreneur previously involved in bankruptcy. The targeted financial organisations seem to be divided on the issues of whether the legislator should work to eliminate the stigma affecting the business life of an entrepreneur previously involved in a bankruptcy, and of whether the legislator should promote a fresh start and eliminate stigma for fraudulently bankrupt persons. However, most targeted organisations positively answered that their members do believe that failed entrepreneurs often learn from their mistakes and that they will be more successful in the future, thus expressing a certain degree of trust in failed entrepreneurs. The financial community nevertheless almost unanimously agreed that banks do have an important role to play in the restart of a failed entrepreneur, and that their members would accept to provide new credit to an entrepreneur that has previously faced bankruptcy or failed, although the latter would be subject to the provision of adequate securities and guarantees, and to the respect of fixed goals expressed in the business plan.

With regard to the issue of external control, most targeted organisations of the financial community seem to believe that the entrepreneur does consider that the external manager can reduce the stigma on business facing difficulties. The majority of the financial targeted organisations seem to reject the idea of judicial supervision of the external control, to which several organisations seemed to prefer the control of creditors. The targeted organisations almost unanimously agreed that the appointment of a crisis manager would be considered an appropriate measure by creditors of a business facing difficulties.

A cross comparison of these of answers received in relation to the way in which the domestic legislation and regulation provide for control on businesses in difficulties shows that the most common type of control which is not combined with another type of control -the judicial control also is felt by the financial community as the least satisfactory control of businesses in difficulties. Furthermore, it appears that there is a predominant sense of dissatisfaction towards the way domestic legislation and regulations deal with bankruptcy/business failure in terms of creditors’ interests - although the targeted financial organisations seem generally satisfied with the way the domestic legislation and regulations deal with bankruptcy/business failure in terms of the debtors’ interests.

0.4. PRINCIPLES AND GUIDELINES FOR EFFECTIVE INSOLVENCY AND CREDITOR RIGHT SYSTEM: ASSESSMENT IN EU MEMBER STATES AND US

The Principles and Guidelines for Effective Insolvency and Creditor Rights Systems were developed by the World Bank to promote international consensus on a uniform framework to assess the effectiveness of insolvency and creditor rights systems. The Principles and Guidelines offer guidance to policymakers on their policy choices.

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1 The Principles and Guidelines can be accessed in the Best Practice directory on the Global Insolvency Law Database at www.worldbank.org/gild.
For the purpose of our study, we thought that it could be useful to mention the World Bank principles as a tool to get a general view of the current practices throughout the European Union and in the U.S. regarding effective insolvency and creditors rights systems.

In order to assess to what extent the principles are adopted in the different Member States and in the US, we designed a questionnaire based on the key elements of the 35 Principles and Guidelines. Experts were asked to mention for each principle whether the principle is: 1) fully adopted 2) almost fully adopted 3) partially adopted 4) not adopted in his/her national insolvency system.

Our approach and conclusions do not pretend to be exhaustive or to reflect the full reality of the practice. It is based on multiple choice questionnaires that we sent to our national experts, who gave us answers based on their own experience and opinion, which is necessarily personal and subjective. Our national experts being high-specialised and well-experienced practitioners, we consider their answers as highly reliable and reflective of the general practices.

0.4.1. Legal Framework for Creditor Rights

PRINCIPLE 1: COMPATIBLE ENFORCEMENT SYSTEMS

A modern credit-based economy requires predictable, transparent and affordable enforcement of both unsecured and secured credit claims by efficient mechanisms outside of insolvency, as well as a sound insolvency system. These systems must be designed to work in harmony.

• This principle is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of Greece and Spain where it is only partially adopted.

PRINCIPLE 2: ENFORCEMENT OF UNSECURED RIGHTS

A regularised system of credit should be supported by mechanisms that provide efficient, transparent, reliable and predictable methods for recovering debt, including seizure and sale of immovable and movable assets and sale or collection of intangible assets such as debts owed to the debtor by third parties.

• This principle is fully or almost fully adopted in the U.S. and in all EU Member States, with the exception of Greece and the UK where it is only partially adopted.

PRINCIPLE 3: SECURITY INTEREST LEGISLATION

The legal framework should provide for the creation, recognition, and enforcement of security interests in movable and immovable (real) property, arising by agreement or operation of law. The law should provide for the following features:

• Security interests in all types of assets, movable and immovable, tangible and intangible, including inventory, receivables, and proceeds; future or after-acquired property, and on a global basis; and based on both possessory and non-possessory interests;
Bankruptcy and a fresh start: stigma on failure and legal consequences of bankruptcy

- Security interests related to any or all of a debtor’s obligations to a creditor, present or future, and between all types of persons;
- Methods of notice that will sufficiently publicise the existence of security interests to creditors, purchasers, and the public generally at the lowest possible cost;
- Clear rules of priority governing competing claims or interests in the same assets, eliminating or reducing priorities over security interests as much as possible.

- This principle is fully or almost fully adopted in all EU Member States. Unfortunately, we did not get any answer from our U.S. experts on this topic.

PRINCIPLE 4: RECORDING AND REGISTRATION OF SECURED RIGHTS

There should be an efficient and cost-effective means of publicising secured interests in movable and immovable assets, with registration being the principal and strongly preferred method. Access to the registry should be inexpensive and open to all for both recording and search.

- This principle is fully or almost fully adopted in the U.S. and in all EU Member States, with the exception of Italy and The Netherlands where it is only partially adopted.

PRINCIPLE 5: ENFORCEMENT OF SECURED RIGHTS

Enforcement systems should provide efficient, inexpensive, transparent and predictable methods for enforcing a security interest in property. Enforcement procedures should provide for prompt realisation of the rights obtained in secured assets, ensuring the maximum possible recovery of asset values based on market values. Both non-judicial and judicial enforcement methods should be considered.

This principle is fully or almost fully adopted in all EU Member States, except for Greece, Italy and Luxembourg where it is only partially adopted.

- This principle is fully or almost fully adopted in the U.S. and in all EU Member States, with the exception of Greece, Italy and Luxembourg where it is only partially adopted.

0.4.2. Legal Framework for Corporate Insolvency

PRINCIPLE 6: KEY OBJECTIVES AND POLICIES

Though country approaches vary, effective insolvency systems should aim to:
- Integrate with a country’s broader legal and commercial systems.
- Maximise the value of a firm’s assets by providing an option to reorganise.
- Strike a careful balance between liquidation and reorganisation.
- Provide for equitable treatment of similarly situated creditors, including similarly situated foreign and domestic creditors.
- Provide for timely, efficient and impartial resolution of insolvencies.
- Prevent the premature dismemberment of a debtor’s assets by individual creditors seeking quick judgements.
- Provide a transparent procedure that contains incentives for gathering and dispensing information.
• Recognise existing creditor rights and respect the priority of claims with a predictable and established process.
• Establish a framework for cross-border insolvencies, with recognition of foreign proceedings.

• This principle is fully or almost fully adopted in the U.S. and in all EU Member States, with the exception of Germany and Greece where it is only partially adopted. In addition, principle 6 is not adopted in Spain.

PRINCIPLE 7: DIRECTOR AND OFFICER LIABILITY

Director and officer liability for decisions detrimental to creditors made when an enterprise is insolvent should promote responsible corporate behaviour while fostering reasonable risk taking. At a minimum, standards should address conduct based on knowledge of or reckless disregard for the adverse consequences to creditors.

• This principle is fully or almost fully adopted in the U.S. and in all EU Member States.

PRINCIPLE 8: LIQUIDATION AND REHABILITATION

An insolvency law should provide both for efficient liquidation of nonviable businesses and those where liquidation is likely to produce a greater return to creditors, and for rehabilitation of viable businesses. Where circumstances justify it, the system should allow for easy conversion of proceedings from one procedure to another.

• This principle is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of Germany, Greece, Italy and Spain where it is only partially adopted.

PRINCIPLE 9: COMMENCEMENT: APPLICABILITY AND ACCESSIBILITY

A. The insolvency process should apply to all enterprises or corporate entities except financial institutions and insurance corporations, which should be dealt with through a separate law or through special provisions in the insolvency law. State-owned corporations should be subject to the same insolvency law as private corporations.

• This part of principle 9 is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of Greece, Italy and Spain where it is partially adopted. It is not adopted in Belgium.

B. Debtors should have easy access to the insolvency system upon showing proof of basic criteria (insolvency or financial difficulty). A declaration to that effect may be provided by the debtor through its board of directors or management. Creditor access should be conditioned on showing proof of insolvency by presumption where there is clear evidence that the debtor failed to pay a matured debt (perhaps of a minimum amount).
• This part of principle 9 is fully or almost fully adopted in the U.S. and in all EU Member States.

C. The preferred test for insolvency should be the debtor's inability to pay debts as they come due—known as the liquidity test. A balance sheet test may be used as an alternative secondary test, but should not replace the liquidity test. The filing of an application to commence a proceeding should automatically prohibit the debtor's transfer, sale or disposition of assets or parts of the business without court approval, except to the extent necessary to operate the business.

• This part of principle 9 is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of Finland and The Netherlands where it is only partially adopted.

PRINCIPLE 10: COMMENCEMENT: MORATORIUMS AND SUSPENSION OF PROCEEDINGS

A. The commencement of bankruptcy should prohibit the unauthorised disposition of the debtor's assets and suspend actions by creditors to enforce their rights or remedies against the debtor or the debtor's assets. The injunctive relief (stay) should be as wide and all embracing as possible, extending to an interest in property used, occupied or in the possession of the debtor.

• This part of principle 10 is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of Finland where it has not been adopted.

B. To maximise the value of asset recoveries, a stay on enforcement actions by secured creditors should be imposed for a limited period in a liquidation proceeding to enable higher recovery of assets by sale of the entire business or its productive units, and in a rehabilitation proceeding where the collateral is needed for the rehabilitation.

• This part of principle 10 is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of Spain where it has not been adopted and the UK where it is only partially adopted

PRINCIPLE 11: GOVERNANCE: MANAGEMENT

A. In liquidation proceedings, management should be replaced by a qualified court-appointed official (administrator) with broad authority to administer the estate in the interest of creditors. Control of the estate should be surrendered immediately to the administrator except where management has been authorised to retain control over the business, in which case the law should impose the same duties on management as on the administrator. In creditor-initiated filings, where circumstances warrant, an interim administrator with reduced duties should be appointed to monitor the business to ensure that creditor interests are protected.
• This part of principle 11 is fully or almost fully adopted in all EU Member States with the exception of Ireland and Spain where it is only partially adopted. In the U.S. it is partially adopted.

B. There are two preferred approaches in a rehabilitation proceeding: exclusive control of the proceeding by an independent administrator or supervision of management by an impartial and independent administrator or supervisor. Under the second option complete power should be shifted to the administrator if management proves incompetent or negligent or has engaged in fraud or other misbehaviour. Similarly, independent administrators or supervisors should be held to the same standard of accountability to creditors and the court and should be subject to removal for incompetence, negligence, fraud or other wrongful conduct.

• This part of principle 11 is fully or almost fully adopted in all EU Member States with the exception of Finland, Italy, The Netherlands and Spain where it is only partially adopted. In the U.S. it is not adopted.

PRINCIPLE 12: GOVERNANCE: CREDITORS AND THE CREDITORS’ COMMITTEE

Creditor interests should be safeguarded by establishing a creditors committee that enables creditors to actively participate in the insolvency process and that allows the committee to monitor the process to ensure fairness and integrity. The committee should be consulted on non-routine matters in the case and have the ability to be heard on key decisions in the proceedings (such as matters involving dispositions of assets outside the normal course of business). The committee should serve as a conduit for processing and distributing relevant information to other creditors and for organising creditors to decide on critical issues. The law should provide for such things as a general creditors assembly for major decisions, to appoint the creditors committee and to determine the committee's membership, quorum and voting rules, powers and the conduct of meetings. In rehabilitation proceedings, the creditors should be entitled to select an independent administrator or supervisor of their choice, provided the person meets the qualifications for serving in this capacity in the specific case.

• This principle is fully or almost fully adopted in the U.S. and in 8 EU Member States. It is only partially adopted in France, Ireland, Italy, Sweden, The Netherlands and the UK. It is not adopted in Belgium.

PRINCIPLE 13: ADMINISTRATION: COLLECTION, PRESERVATION, DISPOSITION OF PROPERTY

The law should provide for the collection, preservation and disposition of all property belonging to the debtor, including property obtained after the commencement of the case. Immediate steps should be taken or allowed to preserve and protect the debtor's assets and business. The law should provide a flexible and transparent system for disposing of assets efficiently and at maximum values. Where necessary, the law should allow for sales free and clear of security interests, charges or other encumbrances, subject to preserving the priority of interests in the proceeds from the assets disposed.
• This principle is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of Denmark, Greece and Spain where it is only partially adopted.

PRINCIPLE 14: ADMINISTRATION: TREATMENT OF CONTRACTUAL OBLIGATIONS

The law should allow for interference with contractual obligations that are not fully performed to the extent necessary to achieve the objectives of the insolvency process, whether to enforce, cancel or assign contracts, except where there is a compelling commercial, public or social interest in upholding the contractual rights of the counter-party to the contract (as with swap agreements).

• This principle is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of France and Spain where it is only partially adopted.

PRINCIPLE 15: ADMINISTRATION: FRAUDULENT OR PREFERENTIAL TRANSACTIONS

The law should provide for the avoidance or cancellation of pre-bankruptcy fraudulent and preferential transactions completed when the enterprise was insolvent or that resulted in its insolvency. The suspect period prior to bankruptcy, during which payments are presumed to be preferential and may be set aside, should normally be short to avoid disrupting normal commercial and credit relations. The suspect period may be longer in the case of gifts or where the person receiving the transfer is closely related to the debtor or its owners.

• This principle is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of Greece where it is only partially adopted.

PRINCIPLE 16: CLAIMS RESOLUTION: TREATMENT OF STAKEHOLDER RIGHTS AND PRIORITIES

A. The rights and priorities of creditors established prior to insolvency under commercial laws should be upheld in an insolvency case to preserve the legitimate expectations of creditors and encourage greater predictability in commercial relationships. Deviations from this general rule should occur only where necessary to promote other compelling policies, such as the policy supporting rehabilitation or to maximise the estate's value. Rules of priority should support incentives for creditors to manage credit efficiently.

• This part of principle 16 is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of France and Greece where it is only partially adopted.

B. The bankruptcy law should recognise the priority of secured creditors in their collateral. Where the rights of secured creditors are impaired to promote a legitimate bankruptcy policy, the interests of these creditors in their collateral should be protected to avoid a loss or deterioration in the economic value of their interest at the commencement of the case. Distributions to secured creditors from the proceeds of their collateral should be made as promptly as
possible after realisation of proceeds from the sale. In cases where the stay applies to secured creditors, it should be of limited specified duration, strike a proper balance between creditor protection and insolvency objectives, and provide for the possibility of orders being made on the application of affected creditors or other persons for relief from the stay.

- This part of principle 16 is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of France and Portugal where it is only partially adopted.

C. Following distributions to secured creditors and payment of claims related to costs and expenses of administration, proceeds available for distribution should be distributed pari passu to remaining creditors unless there are compelling reasons to justify giving preferential status to a particular debt. Public interests generally should not be given precedence over private rights. The number of priority classes should be kept to a minimum.

- This part of principle 16 is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of Belgium, Ireland, Sweden and Greece where it is only partially adopted. It is not adopted in Spain.

0.4.3. Features Pertaining to Corporate Rehabilitation

PRINCIPLE 17: DESIGN FEATURES OF REHABILITATION STATUTES

To be commercially and economically effective, the law should establish rehabilitation procedures that permit quick and easy access to the process, provide sufficient protection for all those involved in the process, provide a structure that permits the negotiation of a commercial plan, enable a majority of creditors in favour of a plan or other course of action to bind all other creditors by the democratic exercise of voting rights (subject to appropriate minority protections and the protection of class rights) and provide for judicial or other supervision to ensure that the process is not subject to manipulation or abuse.

- This principle is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of France, Greece and Spain where it is only partially adopted.

PRINCIPLE 18: ADMINISTRATION: STABILIZING AND SUSTAINING BUSINESS OPERATIONS

The law should provide for a commercially sound form of priority funding for the ongoing and urgent business needs of a debtor during the rescue process, subject to appropriate safeguards.

- This principle is fully or partially adopted in the U.S. and in 8 EU Member States. It is partially adopted in Belgium, France, Germany, Greece, Ireland, Italy and Luxembourg. It is not adopted in Spain.
PRINCIPLE 19: INFORMATION: ACCESS AND DISCLOSURE

The law should require the provision of relevant information on the debtor. It should also provide for independent comment on and analysis of that information. Directors of a debtor corporation should be required to attend meetings of creditors. Provision should be made for the possible examination of directors and other persons with knowledge of the debtor's affairs, who may be compelled to give information to the court and administrator.

- Principle 19 is fully or almost fully adopted in the U.S. and in 9 EU Member States. It is partially adopted in Austria, Belgium, France and Greece. It is not adopted in Italy and Spain.

PRINCIPLE 20: PLAN: FORMULATION, CONSIDERATION AND VOTING

The law should not prescribe the nature of a plan except in terms of fundamental requirements and to prevent commercial abuse. The law may provide for classes of creditors for voting purposes. Voting rights should be determined by amount of debt. An appropriate majority of creditors should be required to approve a plan. Special provision should be made to limit the voting rights of insiders. The effect of a majority vote should be to bind all creditors.

- This principle is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of France, Greece, Austria and Ireland where it is only partially adopted.

PRINCIPLE 21: PLAN: APPROVAL OF PLAN

The law should establish clear criteria for plan approval based on fairness to similar creditors, recognition of relative priorities and majority acceptance. The law should also provide for approval over the rejection of minority creditors if the plan complies with rules of fairness and offers the opposing creditors or classes an amount equal to or greater than would be received under a liquidation proceeding. Some provision for possible adjournment of a plan decision meeting should be made, but under strict time limits. If a plan is not approved, the debtor should automatically be liquidated.

- This principle is fully or almost fully adopted in the U.S. and in 10 EU Member States. It is partially adopted in Belgium, France, Greece and the UK. It is not adopted in Spain.

PRINCIPLE 22: PLAN: IMPLEMENTATION AND AMENDMENT

The law should provide a means for monitoring effective implementation of the plan, requiring the debtor to make periodic reports to the court on the status of implementation and progress during the plan period. A plan should be capable of amendment (by vote of the creditors) if it is in the interests of the creditors. The law should provide for the possible termination of a plan and for the debtor to be liquidated.
• This principle is fully or almost fully adopted in 9 EU Member States. It is partially adopted in Belgium, Denmark, Ireland, Spain, the UK and Greece. Unfortunately, we did not get any answer from the U.S..

PRINCIPLE 23: DISCHARGE AND BINDING EFFECTS

To ensure that the rehabilitated enterprise has the best chance of succeeding, the law should provide for a discharge or alteration of debts and claims that have been discharged or otherwise altered under the plan. Where approval of the plan has been procured by fraud, the plan should be subject to challenge, reconsidered or set aside.

• This principle is fully or almost fully adopted in the U.S. and in 11 EU Member States. It is partially adopted in Germany and Greece. It is not adopted in Italy and France.

PRINCIPLE 24: INTERNATIONAL CONSIDERATIONS

Insolvency proceedings may have international aspects, and insolvency laws should provide for rules of jurisdiction, recognition of foreign judgements, co-operation and assistance among courts in different Member States, and choice of law.

• This principle is fully or almost fully adopted in the U.S. and in 6 EU Member States. It is partially adopted in Austria, Belgium, and Ireland. It is not adopted in Italy, Denmark, Germany, France, Spain and Greece. The question is however no more relevant under a European perspective, because of the adoption of the Council Regulation No 1346/2000 of 29 May 2000 on insolvency proceedings, which is directly applicable in all EU Member States with the exception of Denmark.

0.4.4. Informal Corporate Workouts and Restructurings

PRINCIPLE 25: ENABLING LEGISLATIVE FRAMEWORK

Corporate workouts and restructurings should be supported by an enabling environment that encourages participants to engage in consensual arrangements designed to restore an enterprise to financial viability. An enabling environment includes laws and procedures that require disclosure of or ensure access to timely, reliable and accurate financial information on the distressed enterprise; encourage lending to, investment in or recapitalization of viable financially distressed enterprises; support a broad range of restructuring activities, such as debt write-offs, reschedulings, restructurings and debt- equity conversions; and provide favourable or neutral tax treatment for restructurings.

• This principle is fully or almost fully adopted in the U.S. and in 7 EU Member States. It is partially adopted in Denmark, Germany, Finland, Luxembourg and Portugal. It is not adopted in Italy, Austria and Spain.
PRINCIPLE 26: INFORMAL WORKOUT PROCEDURES

A country's financial sector (possibly with the informal endorsement and assistance of the central bank or finance ministry) should promote the development of a code of conduct on an informal out-of-court process for dealing with cases of corporate financial difficulty in which banks and other financial institutions have a significant exposure—especially in markets where enterprise insolvency has reached systemic levels. An informal process is far more likely to be sustained where there are adequate creditor remedy and insolvency laws. The informal process may produce a formal rescue, which should be able to quickly process a packaged plan produced by the informal process. The formal process may work better if it enables creditors and debtors to use informal techniques.

- This principle is fully or almost fully adopted in the U.S. and in 5 EU Member States only. It is partially adopted in Denmark, France, Finland, Luxembourg and Ireland. It is not adopted in Italy, Austria, Belgium, Germany and Spain.

0.4.5. Implementation of the Insolvency System

PRINCIPLE 27: ROLE OF COURTS

Bankruptcy cases should be overseen and disposed of by an independent court or competent authority and assigned, where practical, to judges with specialised bankruptcy expertise. Significant benefits can be gained by creating specialised bankruptcy courts.

The law should provide for a court or other tribunal to have a general, non-intrusive, supervisory role in the rehabilitation process. The court/tribunal or regulatory authority should be obliged to accept the decision reached by the creditors that a plan be approved or that the debtor be liquidated.

- This principle is fully or almost fully adopted in the U.S. and in 9 EU Member States. It is partially adopted in Austria, France, Italy, Spain and Portugal. It is not adopted in Sweden.

PRINCIPLE 28: PERFORMANCE STANDARDS OF THE COURT, QUALIFICATION AND TRAINING OF JUDGES

Standards should be adopted to measure the competence, performance and services of a bankruptcy court. These standards should serve as a basis for evaluating and improving courts. They should be enforced by adequate qualification criteria as well as training and continuing education for judges.

- This principle is fully or almost fully adopted in the U.S. and in 5 EU Member States. It is partially adopted in Belgium, France, Greece, Ireland, Italy and Sweden. It is not adopted in Denmark, Austria, Finland and Spain

PRINCIPLE 29: COURT ORGANIZATION

The court should be organised so that all interested parties—including the administrator, the debtor and all creditors—are dealt with fairly, objectively and transparently. To the extent possible, publicly available court operating rules, case
practice and case management regulations should govern the court and other participants in the process. The court's internal operations should allocate responsibility and authority to maximise resource use. To the degree feasible the court should institutionalise, streamline and standardise court practices and procedures.

- This principle is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of France, Austria and Spain where it is only partially adopted.

PRINCIPLE 30: TRANSPARENCY AND ACCOUNTABILITY

An insolvency systems should be based on transparency and accountability. Rules should ensure ready access to court records, court hearings, debtor and financial data and other public information.

- This principle is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of Belgium, Denmark and Germany where it is only partially adopted. In addition, it is not adopted in Spain.

PRINCIPLE 31: JUDICIAL DECISION MAKING AND ENFORCEMENT

Judicial decision making should encourage consensual resolution among parties where possible and otherwise undertake timely adjudication of issues with a view to reinforcing predictability in the system through consistent application of the law. The court must have clear authority and effective methods of enforcing its judgements.

- This principle is fully or almost fully adopted in the U.S. and in all EU Member States with the exception of France, Germany, Belgium and Spain where it is only partially adopted.

PRINCIPLE 32: INTEGRITY OF THE COURT

Court operations and decisions should be based on firm rules and regulations to avoid corruption and undue influence. The court must be free of conflicts of interest, bias and lapses in judicial ethics, objectivity and impartiality.

- This principle is fully or almost fully adopted in the U.S. and in all EU Member States.

PRINCIPLE 33: INTEGRITY OF PARTICIPANTS

Persons involved in a bankruptcy proceeding must be subject to rules and court orders designed to prevent fraud, other illegal activity or abuse of the bankruptcy system. In addition, the bankruptcy court must be vested with appropriate powers to deal with illegal activity or abusive conduct that does not constitute criminal activity.
• This principle is fully or almost fully adopted in the U.S. and in all EU Member States.

PRINCIPLE 34: ROLE OF REGULATORY OR SUPERVISORY BODIES

The body or bodies responsible for regulating or supervising insolvency administrators should be independent of individual administrators and should set standards that reflect the requirements of the legislation and public expectations of fairness, impartiality, transparency and accountability.

• Principle 34 is fully or almost fully adopted in the U.S. and in 9 EU Member States. It is partially adopted in Austria, Finland, Germany, Ireland and Spain. It is not adopted in Belgium.

PRINCIPLE 35: COMPETENCE AND INTEGRITY OF INSOLVENCY ADMINISTRATORS

Insolvency administrators should be competent to exercise the powers given to them and should act with integrity, impartiality and independence.

• This principle is fully or almost fully adopted in the U.S. and in all EU Member States.
The graph above shows the EU average degree of implementation for each principle\(^2\). A majority of principles are on average almost fully or fully adopted. The least adopted principles are principles 26, 28 and 24 whereas principles 32, 9/B and 15 are adopted in most Member States.

The graph below illustrated the degree of implementation for all principles per country. Luxembourg, Denmark and Sweden have fully adopted a majority of principles (respectively 28 principles fully adopted in Luxembourg, 24 in Sweden and 23 in Denmark).

Portugal, whilst showing a majority of 38 fully adopted or almost fully adopted answers has the largest number of principles "almost fully adopted".

Luxembourg, showing the largest number of principles fully adopted, totals 37 principles fully or almost fully adopted. Only 3 principles are partially adopted in Luxembourg as opposed to Spain, which has fully adopted or almost fully adopted 18 principles. Spain also has the largest number of principles not adopted (11). Finally, Greece shows the largest number of principles partially adopted (18).

The results of the 16 questionnaires that we received from our experts are to be taken carefully and to be considered as nothing more than what they really reflect: the opinion of 16 national experts regarding the implementation of the World Bank principles in their own legal systems, based on their high experience in the matter of insolvency.

We are aware that these results cannot necessarily be extended or generalised, and that is the reason why for example we would not affirm that Member States that have the highest rate of implementation should be showed as examples of best practice.

\(^2\) It should be noted that these statistics are calculated on the basis of all principles and their subdivision since each subdivision was also the object of a separate question. This gives a total of 41 questions.
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0.5. INDICATORS

0.5.1. Indicators to assess the influence of the stigma of failure

- **“awareness”**

  **Definition:** General knowledge in a particular community on basic distinctions linked to bankruptcy: what is bankruptcy/ business failure/insolvency, fraudulent/ non-fraudulent bankruptcy…

  **Objective:** To determine to what extent the ignorance of a particular community around the notions linked to bankruptcy might incur particularly stigmatising attitudes in the situations.

  **Most striking answers by the three communities:**
  - **General community:** Knowledge does not extend to the difference between insolvency and bankruptcy. Limited awareness on the matter.
  - **Business community:** Aware of the stigma that surrounds business failure. Distinction is made between business in distress and business that has recovered from distress.
  - **Financial community:** idem.

- **“attitudes”**

  **Definition:** General trends described by the targeted communities in reaction to situations of bankruptcy/ insolvency, specific case by case attitudes, for instance in the case of fraudulent bankruptcy.

  **Objective:** To determine whether the reaction is rather positive or negative in general, whether it differs according to the community, whether it attaches a stigma to the failure and whether it might deter a failed business/ entrepreneur from starting a new business.

  **Most striking answers by the three communities:**
  - **General community:** Stigma attached to failure in general.
  - **Business community:** More moderated: distinction is made between business in distress/ business having recovered from distress, and between fraudulent/ non-fraudulent bankruptcy.
  - **Financial community:** idem.

- **“information”**

  **Definition:** What are the sources of information that are relied on by the different communities.

  **Objective:** To determine how the sources of information on business failure which are used by each community influence their knowledge on bankruptcy notions and their attitude towards bankrupt businesses.
Most striking answers by the three communities:
- **General community**: Media (no specific databanks); not well informed.
- **Business community**: Varied sources of information (colleagues, competitors, the business sector, media, credit/financial institutions).
- **Financial community**: Specific and efficient databanks.

**Role in Prevention**

**Definition**: Whether the targeted community feels it has a role to play in the prevention of business failure.

**Objective**: To determine what this role would be, and whether it consists in an active approach: for the prevention of failure on the one hand, and for the fresh start on the other hand.

**Dealing with Bankrupt Businesses**

**Definition**: Whether the members of the targeted communities generally continue to deal with businesses that are facing difficulties/ bankruptcy, including: continuing business, continuing to provide credits, etc.

**Objective**: To determine on the one hand, whether businesses facing difficulties are provided with support from their business partners, from banks, etc, and on the other hand, whether a stigma is attached to a previously failed business, which would be revealed by its partners’ reluctance to continue to deal with it.

**Fresh Start**

**Definition**: Whether previously failed/ bankrupt businesses are given a “second chance” and are provided with the possibility to start a new business.
Objective: To identify any stigma linked to the start of a new business by a previously failed/ bankrupt business.

Most striking answers by the three communities:
- General community: Very deterrent effect: most consumer organisations would warn their members of the previous failure of a business. However, favourable to legislative promotion of opportunities.
- Business community: Generally favourable to legislative promotion of the opportunities for a fresh start and correlative elimination of stigma. Limit: fraudulent bankruptcy.
- Financial community: Generally favourable to legislative promotion of the opportunities for a fresh start but more reluctant to the correlative elimination of stigma. Banks’ important role: provision of credits (subject to the provision of adequate securities).

- “external control”

Definition: Control which is/ could/ should be provided by domestic legislations over the business life of an entrepreneur either facing difficulties or previously involved in bankruptcy.

Objective: To identify the position of the three targeted communities in respect of various forms of external control. This analysis involves the assessment of the existing legislation in the matter, including the level of satisfaction of the targeted communities in the member states, and the choice of the preferred form of external control (by the judicial authorities, by creditors…).

Most striking answers by the three communities:
- General community: N/A.
- Business community: Generally not in favour of a legislative strengthening of the control over the business life of an entrepreneur “previously” involved in bankruptcy – as opposed to “actually” facing difficulties. In the latter case, the business community is generally reluctant to place the external control under the power of judicial authorities or under the control of creditors: the appointment of a crisis manager would be preferred.
- Financial community: According to the financial community, the entrepreneur would consider that the external manager could reduce the stigma. The majority of the targeted organisations rejected judicial supervision, to which several organisations preferred the control of creditors. The appointment of a crisis manager was considered almost unanimously as an appropriate measure for the protection of creditors.

0.5.2. Indicators to assess to what extent national bankruptcy law acts as deterrent to business survival and a fresh start

a) Early warning

- “Recognition of financial difficulties”
Objective: To detect early enough a business or an entrepreneur’s financial difficulties in order to set up adequate prevention procedures.

• “Disclosure of information by debtor”

Objective: To assess whether the debtor is subject to an efficient supervision process for his disclosure of information regarding its own situation.

Example of best practice: Belgium

b) Business survival

• “ignorance and complexity”

Objective: to determine to what extent the ignorance of legal possibilities to rescue business and complexity of these procedures might impede the debtor from benefiting from such rescue opportunities.

Example of best practice: None

• “requirements for entry”

Objective: to assess the level of requirements of a national legislation to benefit from the rehabilitation proceedings, which, if too high, may impede the debtor from benefiting from such procedures.

example of best practice: Denmark, France, UK (receivership), USA.

• “publicity”

Objective: to identify whether the publicity obligations provided by the national legislation will have a harmful effect on the rehabilitation process.

Example of best practice: France, USA

• “costs”

Objective: to determine whether the level of costs required for the rehabilitation proceedings -in particular for small and medium enterprises- provided by the national legislation will have a harmful effect on the rehabilitation process.

Example of best practice: None

• “administration of the regime”

Objective: to assess whether the formalism and delays of the procedure set up under a national legislation will be such as to deter an enterprise to initiate reorganisation proceedings.
Example of best practice: Portugal

- “degree of protection against creditors during the procedures”

Objective: to identify whether the national legislation provides a particularly protective regime for secured creditors, which might be a factor of failure for a reorganisation procedure.

Example of best practice: Belgium, Finland, France, Germany, Greece, Ireland, Luxembourg, Portugal, US.

- “knowledge and functioning of the relevant courts”

Objective: to determine whether the competent courts have the adequate knowledge and training in order to favour the success of rehabilitation proceedings.

Example of best practice: all, except Spain

c) Fresh start

- “effects of bankruptcy”

Objective: to assess to what extent the effects of bankruptcy as such may incur stigmatisation of the debtor

Example of best practice: all Member States

- “restrictions, disqualifications and prohibitions”

Objective: to determine whether a national legislation imposes automatic restrictions, disqualifications and prohibitions that end up stigmatising the bankrupt person.

Example of best practice: Greece

- “distinction between honest and dishonest bankrupts”

Objective: to identify whether a national legislation does distinguish a fraudulent bankruptcy from an honest bankruptcy, so as to avoid stigmatising the honest bankrupt.

Example of best practice: Spain

- “discharge from remaining debts”

Objective: to assess whether a national legislation provides for the possibility to discharge from remaining debts once the bankruptcy is closed.

Example of best practice: Austria, Belgium, France, Germany, Spain, UK and US.
0.6. RECOMMENDATIONS

Possible recommendations were identified, which are summarised below.

0.6.1. Recommendations as regards the stigma on bankruptcy:

a) The general public, the business community and financial institutions
   - General knowledge on bankruptcy / insolvency
   - Dealing with bankrupt businesses

b) National authorities
   - Information on business failure
   - Promotion of fresh start
   - External control

c) The European Union
   - Information of existing insolvency proceedings
   - Reduce stigmatising effects of bankruptcy by stressing distinction between honest and dishonest bankrupts

0.6.2. Recommendations as regards the early warning:

a) The general public, the business community and financial institutions
   - Earlier detection
   - Information

b) National authorities
   - Formal detection proceedings
   - Information with regard to the legal possibilities to rescue businesses

c) The European Union
   - Harmonise legislations
   - Promote a control of the detection measures

0.6.3. Recommendations as regards the business survival:
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The general public, the business community and financial institutions

- Appointment of an external crisis manager

National authorities

- Promotion of entrepreneurial culture according to European trends
- Enterprises should be obliged to take action in a timely manner
- Simplification of existing proceedings
- Lower requirements for entry
- Higher confidentiality
- Reduce costs
- Control of the information to disclose
- New deliveries
- Specialised insolvency courts
- Reduce the number of preferential rights
- Do not keep preferential creditors completely out of proceedings

The European Union

- Promotion of the information
- Harmonisation of the legislation

Recommendations as regards the possibilities for a fresh start:

The general public, the business community and financial institutions

- Promotional campaign in order to launch the Fresh start and a new entrepreneurship

National authorities

- Reduce stigmatising effects of bankruptcy: distinction between honest and dishonest bankrupts
- Early discharge for honest bankrupts

The European Union

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• Information on the “positive” effects of a bankruptcy experience.