Think Ahead ACCA

TECHNICAL ALERT 03/2023

The European Union (Preventive Restructuring) Regulations 2022 (SI 380/2022) –

Updates to examinership legislation 2022

This publication has been jointly developed by the member bodies of the Consultative Committee of Accountancy Bodies – Ireland (CCAB-I), being the Institute of Chartered Accountants in Ireland, The Association of Chartered Certified Accountants, The Institute of Certified Public Accountants and Chartered Institute of Management Accountants.

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A. Introduction

The European Union (Preventive Restructuring) Regulations 2022 (SI 380/2022) were signed by the Minister for Enterprise Trade and Employment on 27 July 2022.

In the following paragraphs they are referred to as the "Regulations".

The Regulations were issued for the purpose of giving effect to EU Directive 2019/1023 (the Directive). The meaning of certain definitions or phrases used in the Regulations can be found in the Directive.

The aim of the Directive is to establish a framework across the European Union which will ensure that Member States have effective restructuring processes in place at both national and cross border level.

Rather than introducing a separate restructuring regime, which could have been done to implement the Preventive Restructuring Directive, the Regulations modify the examinership process as set out in the Companies Act 2014 (the Act) on the basis that the current examinership regime is aligned with requirements set out in the Preventive Restructuring Directive.

The Irish Government has stated that it is adopting a two phased approach to reviewing and amending Ireland's examinership process with the passing of the Regulations constituting Phase one.

We will outline a number of the key amendments to the 2014 Act below arising from the transposition of the Directive.

B. Early Warning System

Regulation 7 inserts a new section 271A into the Act. This section provides for a new mechanism which alerts directors to circumstances which could give rise to a likelihood that the company will be unable to pay its debts. Section 271A now provides:

a) A director may have regard to early warning tools; and
b) For the purposes of this section, an early warning tool means a mechanism to alert the directors of the company to circumstances that could give rise to a likelihood that the company concerned will be unable to pay its debts (within the meaning of section 509(3)) and can identify the restructuring frameworks available to the company and signal to such directors the need to act without delay.

An early warning system mechanism has been introduced to alert directors to circumstances that could give rise to a likelihood that the company will be unable to pay its debts. The mechanism is set out in Information Note 2023/1 available on the website of the Corporate Enforcement Authority. It is important to note that this provision does not give rise to any mandatory requirement on the part of a company director to take such specific action, however, it will be interesting to see whether the courts take account of this early warning system in the context of directors' duties in due course.

C. Directors' Duties

Regulation 4 of the Regulations amends the Act by the insertion of a new Section 224A which places a new statutory fiduciary duty on a company director "*who believes, or who has reasonable cause to believe, that the company is, or is likely to be, unable to pay its debts (within the meaning of section 509(3)*", to have regard to:

a) the interests of the creditors;
b) the need to take steps to avoid insolvency; and
c) the need to avoid deliberate or grossly negligent conduct that threatens the viability of the business of the company. This duty is in addition to the existing fiduciary duties on the part of directors contained in the Act.

The new Section 224A provides that the duty imposed on a director shall be owed by them to the company (and the company alone) and shall be enforceable in the same way as any other fiduciary duty owed to a company by its directors.

D. Experience of Examiner

The Regulations amend section 509(2) of the Act to require the court, in cases where there is a cross-border element, to consider whether the person to be appointed as Examiner, has "*sufficient expertise and experience to perform the role, having due consideration to the Examiner's experience and to the specific features of the case*".

It is not entirely evident how the amendment of section 509(2) will have any impact in practical terms. An Affidavit of Suitability accompanied a petition prior to the commencement of the Regulations, and accordingly, it may mean that further detail will be required in that regard in order for the court to be satisfied as to the level of experience of the proposed examiner.

E. Notice of Meetings - Creditors and Members

Regulation 14 amends section 534(2) and requires the Examiner to ensure that every impaired member or creditor is invited to attend meetings convened in order to allow those parties to consider proposals for a compromise or scheme of arrangement in relation to a company.

The requirement to ensure that every member or creditor is invited to these meetings is mandatory. As appears from Regulation 17, section 541 of the Act has now been amended to provide that the proposals shall not be binding on any member who was not invited to attend the meetings convened. This mandatory requirement may cause practical difficulties with respect to the identification and location of all relevant parties. To that end, it is suggested that reasonable effort and sufficient care is taken in seeking to locate and identify those parties, or court direction is sought if deemed necessary.

F. Scheme Proposals

Regulation 15 provides for additional information to be included in the Scheme proposals circulated under section 539, including:

- Why the proposals provide a reasonable prospect of facilitating the survival of the company;
- Employee consultation;
- Details of new financing required;
- Value of the assets;
- Description of the economic situation of the company; and
- Description of the causes and extent of the difficulties of the company.

As appears from the above, amendments to section 539 of the Act now mandate a minimum level of information to be included in the proposals and accompanying documents.

G. Impaired Creditors Not Counted for Proposal Voting

One of the most significant amendments to the examinership procedure introduced by the Regulations is to creditor's voting rights for the approval of a Scheme.

Section 540(4) of the Act had provided that proposals for a compromise or Scheme of arrangement shall be deemed to have been accepted by a meeting of creditors or of a class of creditors when a majority in number representing a majority in the value of the claims represented at that meeting voted in favour of the proposals.

Creditors' voting rights have been altered by Regulation 16 which now provides that creditors whose interests or claims will not be impaired by the proposals are not afforded a right to vote on the adoption of same.

Regulation 16 inserts a new subsection (4A) to Section 540 which states:

"Creditors or classes of creditors whose interests or claims will not be impaired by the proposals shall not have voting rights in the adoption of the proposals, and the majority calculated in accordance with subsection (4) shall not take into account the number and value of the claims of any such creditors."

The existing examinership procedure requires the approval of only a single class of creditors for a court to confirm a Scheme.

Regulation 17 provides that in accordance with section 540, the Examiner may not rely on the vote of any creditor who would not receive any payment in seeking to have the court approve the Scheme. For example, if the unsecured creditors would not recover any monies on liquidation their votes in favour of a Scheme cannot be relied upon for the purpose of section 541(3B).

In practical terms, it may now be more difficult for the Scheme to receive the requisite approval, where classes of creditors who the Examiner might previously have relied on for approval, will not now be in a position to vote.

In this regard, an examinership, which under the previous regime may have been sanctioned by the court, could potentially now fail at the voting stage for failure to meet the significantly more stringent voting threshold which has been introduced by the Directive.

H. Best-interests-of-creditors test

Regulation 10 amends section 511(3)(g) of the Act by providing that the independent expert's report shall contain:

"… his or her opinion as to whether an attempt to continue the whole or any part of the undertaking meets the best-interest-of-creditors test and would be likely to be more advantageous to the members as a whole than a winding-up of the company."

The best-interests-of creditors test must be applied at both the beginning and end of the examinership process.

The test appears to require the independent expert to carry out an assessment of whether any dissenting creditor would be worse off under a restructuring plan than such a creditor would be if the normal ranking of liquidation priorities were applied, either in the event of liquidation, whether piecemeal or by sale as a going concern, or in the event of the next-best-alternative scenario if the restructuring plan were not confirmed. This assessment of dissenting creditors must be carried out by the independent expert on an individual basis.

Pursuant to the amendments introduced by Regulation 17, Section 541(5) of the Act provides that the court shall not confirm any proposals in respect of a company if they do not satisfy the best-interests-of-creditors test and where such proposals are challenged by one or more creditors on that basis.

I. Employee Claims Carve Out

Regulation 11 amends section 520 of the Act, which provides for protection from creditors during the period in which the company remains in examinership, by the introduction of section 520(5A). Section 520(5A) provides a specific carve out to the general protection for employees, who can now commence or advance certain actions or proceedings notwithstanding the fact that the company is in examinership. Accordingly, the introduction of this amendment means that companies no longer enjoy complete protection given that employee claims can be advanced during the protection period without any requirement for employees to seek the leave of the court.

J. Restrictions on Certain Contracts During Examinership

The Regulations introduce a new section, section 520A, which precludes creditors who are parties to certain contracts ("executory contracts" i.e., where the parties have obligations to perform) from taking certain actions (withholding performance; terminating; accelerating; modifying) based on the company's examinership. Of note is the fact that certain of the preclusions operate notwithstanding any contractual right to the contrary. Introducing an automatic provision will provide certainty to debtors. However, it will be interesting to see if any aggrieved creditors challenge this section based on unconstitutional interference of (contractual) property rights.

The Directive provides some guidance as to the type of contracts which might fall into the definition of executory contracts including lease and license agreements, term supply contracts and franchise agreements.

K. Treatment of Liabilities Incurred During the Protection Period

An Examiner previously had a discretion to certify certain liabilities if, in their opinion failing to incur them during the protection period would seriously jeopardise the survival of the company as a going concern.

However, Section 529(2) now provides for the certification by the Examiner of liabilities, and for their priority under section 554, which has been amended to include the payment of fees for and costs of negotiating or confirming a Scheme and of seeking professional advice connected with the examinership, the payment of employees' wages for work already carried out and any other payments and disbursements made in the ordinary course of business.

The Regulations introduce a new section 529(2A) which provides that in the event of a company being wound up within 6 months of the end of the protection period, certified liabilities that were incurred during the protection period as a part of transaction that are "*reasonable*" and "*immediately necessary for the Scheme of arrangement*" shall not be declared void, voidable or unenforceable on the ground that the transaction is detrimental to the general body of creditors unless there are other reasons why the transaction should be declared void, voidable or unenforceable.

L. Maximum Protection Period

Regulation 14 (b) provides that the maximum period which a company can remain under the protection of the court is one year. Furthermore, the position remains that the Examiner must present his or her report within the prescribed maximum period (which is currently 100 days, and extendable up to 150 days arising from legislation imposed with respect to Covid-19).

M. Conclusion

In conclusion, whilst many of the amendments to the 2014 Act reflect the legislation already in place with respect to examinerships in Ireland, the Regulations have introduced a number of significant changes to the previous examinership process. It will undoubtedly take time for the courts to take into account the implications of those amendments and how they should be addressed in practical terms.

Comparison of the Irish Processes with those of other Countries

Features	Ireland Examinership	Ireland SCARP (Small Company Administrative Rescue Process)	Ireland Part 9 Scheme	UK Restructuring Plan	UK Part 26 Scheme	US Chapter 11
Court Application	Yes	No	Yes	Yes	Yes	Yes
Does the Debtor remain in possession?	Yes	Yes	Yes	Yes	Yes	Yes
Is there a stay on enforcement actions?	Yes	No (however a debtor may apply to the court to put a stay in place)	No	Yes	No	Yes
Restriction of *Ipso Facto* Clauses?	Yes	No	No	Yes	No	Yes
Is provision made for separate classes of Creditors?	Yes	Yes	Yes	Yes	Yes	Yes
Is a Cram-down required?	Yes	Yes (however, there are provisions that allow for the opt out of certain creditors, such as Revenue)	Yes	Yes	Yes	Yes
Is a Cross-class cram down required?	Yes	Yes	No	Yes	No	Yes
What level of support is needed for the	A simple majority (greater than 50%) in number and in value of	60% in number and a simple majority in value of at least one	75% by value and a simple majority in number of	75% by value of one class of impaired 'in the money' creditors	75% by value and a simple majority in number of	2/3 in value and majority in number of allowed claims in each class

Scheme to be accepted?	one class of impaired *'in the money'* creditors	class of impaired creditors	creditors in each class		creditors in each class	
What is the basis to allow for founding jurisdiction?	Irish COMI or formed and registered under Irish companies acts (if non-EU COMI). Foreign companies without an EU COMI can be brought in as a related company if they have a sufficient connection	Falling within the definition of a Small of Micro Company as defined by the Companies Act 2014	Sufficient Connection	Sufficient Connection	Sufficient Connection	Asset in the US
Is there a provision for Super-priority Debtor In Possession (**DIP**) finance?	No (however an Examiner can certify DIP finance which can in turn prime preferential and floating charge creditors)	No (however a Process Adviser can certify DIP finance which can prime preferential and floating charge creditors)	No	No	No	Yes (to obtain DIP Financing the Debtor must apply to the court for permission)
Will the scheme be recognised in the EU once approved?	Yes Examinership listed under Annex A of European Insolvency Regulation Recast	No - A scheme under SCARP does not fall within the definition of an insolvency proceeding for the purposes of European Union Insolvency Regulation Recast	Yes – Automatic recognition across EU member states under Brussels I Recast Regulation	N/A	N/A	N/A