

The Second Chance Directive – possible changes in restructuring proceedings from 17 July 2022

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Polish lawmakers have until 17 July 2022 to implement most of the provisions of Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks, on discharge of debt and disqualifications, and on measures to increase the efficiency of procedures concerning restructuring, insolvency and discharge of debt, and amending Directive (EU) 2017/1132 (Directive on restructuring and insolvency), also referred to as **the second chance directive**.

The most important changes that should be implemented into Polish restructuring law in connection with the Second Chance Directive are:

- > the introduction of a preventive restructuring framework;
- > the introduction of early warning systems; and
- > a limit on the period for which enforcement actions may be suspended.

In addition, depending on the assessment of the Polish legislature, the following changes may be introduced:

- > a limit on access to the preventive restructuring framework for debtors at risk of insolvency; and
- > the introduction of a criterion for the protection of creditors' best interests.

Introduction of the preventive restructuring framework

European Union legislation imposes an obligation to ensure that viable enterprises and entrepreneurs that are in financial distress have access to effective national preventive restructuring frameworks which enable them to continue operating.

This means that the relevant Polish legislation may introduce a new restructuring procedure into the Polish legal order which implements the solutions contained in the Second Chance Directive. Another possible scenario is that the provisions of the Second Chance Directive will be implemented by way of the modification of one of the procedures currently provided for in restructuring law.

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Restricting access to the preventive restructuring framework for debtors at risk of insolvency

The EU legislator offers preventive restructuring to debtors that are likely to become insolvent. The concept of insolvency should be understood in accordance with national law. The preventive restructuring framework should be available before the debtor becomes insolvent.

The Polish legislature offers a different approach to the availability of restructuring procedures. The procedures are both for debtors at risk of insolvency and for insolvent debtors. Therefore, the implementation of the Second Chance Directive may entail changes in the rules under which it is possible to commence restructuring proceedings. The Polish legislature may restrict access to preventive restructuring to only those debtors who are at risk of insolvency.

Implementation of early warning systems

The Second Chance Directive requires that early warning systems be put in place. They are intended to signal to the debtor that restructuring measures are needed. The role of early warning systems is to detect circumstances that could raise the likelihood of insolvency.

Among the examples of early warning tools that the EU legislator specified are alert mechanisms in cases where a debtor has not made certain types of payments, advisory services provided by public or private organisations and incentives set forth in national law that encourage third parties that have relevant information concerning debtors to inform such debtors of any negative developments relating thereto.

Polish restructuring law does not offer a solution similar to early warning systems. To date, Polish debtors have not been provided with indications of their financial situation by third parties. The assessment of a debtor's financial situation has rested in its own hands.

Limitation of the length of time during which enforcement actions are suspended

The Polish legislation will need to reflect the length of time for which specific enforcement actions are to be stayed and for which contractual protection is to be granted. Under the Second Chance Directive, this is possible for up to four months, with the possibility of extension. The total period of stay of specific enforcement actions may not exceed 12 months.

Polish restructuring law does not define the maximum length of time for which enforcement proceedings against a debtor's assets may be suspended. Similarly, no limit has been introduced on the length of time for which a debtor's contractual protection is granted. Introducing statutory solutions concerning this issue first requires that the backlog of judgments in restructuring courts be addressed. The introduction of a statutory regulation specifying the period for which protection is granted to a debtor is only one of the elements necessary for implementing the provisions of the Second Chance Directive. The second element is to ensure that the regulation is applied in practice.

Introduction of the best-interests-of-creditors test

Pursuant to the Second Chance Directive, compliance with the best-interests-of-creditors test is assessed if a restructuring plan has been challenged on the grounds that it fails to comply with such test.

Having to comply with the best-interests-of-creditors test means that no objecting creditor will be worse off upon the conclusion of the restructuring plan than such creditor would have been in the event of liquidation – either through gradual liquidation, or the sale of the debtor as a going concern – or in the event that the second-best alternative scenario is applied, if the restructuring plan had not been approved.

Opinions have been voiced that Polish restructuring law does not provide for solutions that could constitute an equivalent of the best-interests-of-creditors test. Therefore, the relevant Polish legislation can be expected to implement comprehensive regulations on this issue.

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