In a letter to the European Commission (EC) from the 25 March, the High Yield Division of the Association for Financial Markets in Europe (AFME) shares its views on developments related to European insolvency laws, and provides a brief response to the EC’s recommendation of 12 March 2014 on a new approach to business failure and insolvency.

European insolvency laws are currently being considered under the Capital Markets Union (CMU) project, and AFME called for greater harmonisation in this area in its Agenda for CMU paper published in November 2014.

In this context, the letter sets out the negative effects of disparities amongst European insolvency regimes and restructuring laws, and suggests alterations which would help to increase the efficiency of, and confidence in, European capital markets. It also provides a comprehensive table of the differences in certain national laws as an appendix.

The AFME High Yield Division's view is that differences between national insolvency and restructuring regimes create uncertainty and increase costs for issuers and investors, discourage cross-border investment and often lead to liquidation rather than providing an opportunity to restructure a company in financial difficulty. Small and medium sized companies are particularly at a disadvantage as they are generally unable to cope with high restructuring costs.

Further harmonisation of European insolvency regimes would help to facilitate more predictable and orderly outcomes for corporate restructurings, and to that end the letter suggests the following areas should be prioritised:

- **Stay.** Although in most EU countries some form of stay exists, the forms of stay deployed by certain European jurisdictions are inadequate and allow customers and suppliers to walk away, or demand punitive amendments, just when their continued commitment is most crucial to the company’s rescue. This makes value destruction an inevitable consequence of filing in certain European jurisdictions.

- **Valuation.** Europe does not have a consistent and clearly established method for valuing companies in a restructuring process, nor a consistent method or platform for solving stakeholders’ disputes on valuations. This makes restructurings more complex and leads to more enterprises entering administration or liquidation proceedings than necessary.

- **Cramdown.** Practices vary on the need for the consent of lower ranking stakeholders – shareholders or junior creditors- to go ahead with restructurings. This leads to uncertainty concerning stakeholders’ rights and make restructurings outside administration more difficult. Cramdown regimes with adequate minimum requirements and protections for affected stakeholders would help address this issue.

- **Creditors’ ability to propose a restructuring plan.** A number of jurisdictions allow creditors to propose their own restructuring plan, or a counter-proposal to a debtor’s plan. Where a debtor is not obliged to put a creditor’s restructuring proposal to a vote, creditors often have to either approve the debtor’s plan or force the company into liquidation. Creditors and, potentially, interested third parties, should have the right to submit a restructuring plan to a debtor and put it to creditor vote.
Funding. In Europe, there are few legislative provisions to prioritise rescue finance and therefore no market exists to provide ongoing funding for distressed companies. Consequently, a distressed company has to rely on existing creditors to meet interim funding requirements whilst a restructuring plan is devised. The procedure can be complicated by the increasing number of financial institutions involved in the process, and their range of different investment and exit strategies. The letter suggests that for court-supervised restructurings, there should be no regulatory restrictions on the provision of interim financing to debtors and there should be automatic priority status for new financing. Court supervision would ensure that the terms of the interim financing (including any priority status over existing financing) are warranted in the context of a particular situation.

The letter also points out that any certainty or efficiency gained through Europe-wide initiatives such as the CMU or the European Commission's attempts to create a "single rulebook" (e.g. MiFID, EMIR, AIFMD, CSDR, MAR) is undermined if investors and other stakeholders remain subject to 28 different European insolvency regimes.

The letter and appendix table are available here: www.afme.eu/Divisions/High-Yield/

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About the Association for Financial Markets in Europe
AFME promotes fair, orderly, and efficient European wholesale capital markets and provides leadership in advancing the interests of all market participants. AFME represents a broad array of European and global participants in the wholesale financial markets. Its members comprise pan-EU and global banks as well as key regional banks, brokers, law firms, investors and other financial market participants. AFME participates in a global alliance with the Securities Industry and Financial Markets Association (SIFMA) in the US, and the Asia Securities Industry and Financial Markets Association (ASIFMA) through the GFMA (Global Financial Markets Association). For more information please visit the AFME website, www.afme.eu
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