

IOTA PAPER

20
23 MARCH

PRE-INSOLVENCY PROCEDURES IMPLEMENTED IN HUNGARIAN LAW

how the Restructuring Directive has been transposed into
the Hungarian law,
how it offers innovative solutions for distressed companies

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This Article is an analysis of how the Restructuring Directive has been transposed into the Hungarian law, how it offers innovative solutions for distressed companies, following the main building blocks.

Introduction

The impact on the economy caused by the pandemic that has hit the world and by the energy crisis that is currently taking place has put and could put many businesses in a critical financial situation in the near future. The aim of the Directive (EU) 2019/1023 of the European



Parliament and of the Council, of 20 June 2019 on Restructuring and Insolvency (hereinafter referred to as "the Directive"), is to introduce an instrument to rescue companies that are still viable but in financial difficulty, providing an effective legal tool to help financially distressed companies to recover. The overall aim of the Directive is to reduce the most significant obstacles to the free movement of capital arising from the different restructuring and insolvency frameworks in the Member States and to promote the principle of "second chance" in the European Union throwing the distressed a lifebelt.

The Directive represents a milestone in the development of European insolvency law. The text was the result of long and complex negotiations since the proposal was presented in 2016. In its final form, **the Directive establishes some minimum standards** for preventive debt restructuring mechanisms, debt discharge for entrepreneurs, and a limited subset of other insolvency issues, but its harmonization effect will be limited **given multiple options for implementation**, leading to divergent restructuring models in Europe. These options reveal different policy approaches to the regulation of restructuring and insolvency. The end result is "a puzzling variety of diverging options" (Rotaru, 2019). Member States should carefully design restructuring procedures to avoid the negative economic effects of certain options that could undermine creditors' rights or result in unpredictable outcomes, particularly in cross-border cases.

Pre-insolvency procedures are already known in Western European countries and already exist in most EU Member States.

They can basically be classified into two types:

- A type of procedure supporting debt settlement, where the role of the court is limited, where not all creditors are involved and where there is no requirement to prove that the debtor is not yet insolvent. In this case, usually only a moratorium can be requested, and only if the debtor has a creditor who disagrees with the agreement does the court still have a role to play.
- The other type of procedure is collective, i.e. all creditors are involved, a wide range of restructuring instruments are available: in addition to the moratorium, e.g. the restructuring plan, the right to enforce contracts and the role of the court is more important, it "accompanies" the procedure.

The analysis made in this article aims to illustrate **the specificities of the pre-insolvency procedure transposed into the Hungarian law outlining some relevant building blocks of the Directive and its policy options.**

A new legal institution in Hungarian law

In Hungary, only during the emergency period, the transitional legal instrument introduced by Government Decree 179/2021 (16.IV.) on the **reorganisation procedure**, can be considered as a procedure with similar features to the restructuring procedure, and this Government Decree is **the legislative predecessor of the Act transposing the restructuring procedure** into Hungarian law. The restructuring procedure had many similarities with the reorganization procedure. Although they had similar aims and run in parallel for a period (July 1, 2021 – December 31, 2022), they had different rules. The main difference was that the moratorium was subject to the prior opinion of the expert, and only the National Reorganization Nonprofit Ltd. could act as a reorganization expert during the reorganization. This procedure was not popular, so its case law cannot be analysed.

The "Restructuring Act" Act LXIV of 2021 – on restructuring and amending certain acts for harmonization purposes, implementing Titles I-II of the Directive (**hereinafter referred to as the "Act"**) entered into force on 1 July last year, **thus introducing a procedure of niche importance in the Hungarian legal system.** This new procedure has been adopted to stabilize the financial situation of companies on the verge of insolvency. This transposed the Directive into the Hungarian legal system. Its aim is to keep a company afloat despite its financial difficulties and for the debtor company to adopt and implement a restructuring plan with creditors to prevent a possible bankruptcy or insolvency procedure. It is **of niche importance** because, **until now, the only solution for resolving the debts of companies in financial difficulties was the bankruptcy proceedings**, which, with its formalistic, protracted procedure, limited involvement of creditors in decision-making and the stigma associated to it from the debtor's point of view, actually **provided less effective tools for the parties involved in the procedure.**

The aim of the Directive is to increase the competitiveness of the Member States and the EU, and the Directive seeks to achieve this in two areas: the restructuring of legal entities in financial difficulty but not insolvent and the debt settlement and debt relief procedure for insolvent self-employed individuals. The Act focuses exclusively on the implementation of the former, while the provisions of the Directive are transposed for self-employed individuals by amending Act CV of 2015 on the Debt Settlement of Natural Persons. **The Act regulates the so-called pre-insolvency procedure, which involves judicial competence as well, and is therefore be covered by Regulation (EU) 2015/848 of the European Parliament and of the Council on insolvency proceedings (hereinafter referred to as the "Insolvency Regulation").** As a result of the legislator's decision, the **public restructuring procedure has thus also been brought within the scope of the Insolvency Regulation** with the entry into force of the Act. This also means that these procedures (alongside our liquidation and bankruptcy procedures) are also part of the EU's single legal framework, which provides EU rules on the jurisdiction of insolvency proceedings in the Member States covered, including the universal scope of each procedure, i.e. its scope extends beyond the Member State in which it is brought. This analysis therefore focuses exclusively on the procedures covered by this Act.

Innovations in Hungarian insolvency law

Looking at the features of the new type of insolvency proceedings, which determine their specific nature, and the tools supporting the purpose of the proceedings, as main building blocks, I would highlight the following.

Likelihood of insolvency

As a pre-insolvency procedure, restructuring proceedings can be used when the company is not yet considered insolvent but when an adverse development of its financial situation, i.e. the **likelihood of insolvency**, is already discernible. The term of “likelihood of insolvency” is not defined in the Directive and is left to the discretion of the national implementing law. Member States have to carefully balance the desirability to give debtors in debt distress the ability to save their business, while preventing moral hazard. One way to do so may be to reference a time period prior to insolvency (e.g. where there is a rational basis for the conclusion that the company may not be able to pay its debts within the next six months) or to set up additional barriers to access, such as a history of fraud, past use of procedure, and a test of “viability” to increase creditor protection.

According to the Hungarian Act the “likelihood of insolvency” is a situation in which there are reasonable grounds for believing that the debtor will be unable to meet his outstanding payment obligations when they fall due, without taking further measures. This could be considered as a type of “**viability**” test, let’s see why.

When applying for the restructuring procedure in Hungary the debtor **shall present its assets and financial situation by supporting documents, the facts and circumstances justifying the likelihood of insolvency and that there are no legal obstacles to the decision to restructure.** The debtor’s application must be accompanied by its decision on initiating restructuring, its interim balance sheet, not more than 6 months old and last available financial report under the Accounting Act.

If the application is not rejected, the court shall notify the affected creditors indicated in the debtor’s application of the application itself and of its right to submit a statement of opposition within 10 working days of receipt of its order, contesting the likelihood of the debtor’s insolvency and thus the (pre)conditions for the opening of restructuring proceedings. In such a case, creditors may rely on circumstances that preclude restructuring under the national law, such as i.a. the parallel or past use of insolvency or pre-insolvency procedure within a certain period; the breach of certain accounting and bookkeeping obligations under the national law (although these facts are usually available for the court ex officio); the debtor has outstanding uncontested or recognised debts which are more than 30 days overdue and which together exceed 10% of the debtor’s outstanding claims (whether the liability is short-term or long-term); or the debtor is subject to enforcement proceedings; or criminal proceedings are pending in respect of which the debtor may be subject to criminal sanctions; or concerns claims that cannot be involved in the restructuring proceedings, such as wages and salaries, taxes on them, value added taxes, budgetary aid or aid granted by a body providing EU funding in the context of a grant relationship and claims arising therefrom.

The court shall send the statement submitted by the creditor concerned to the debtor with an invitation to make a statement regarding the contents of the submission and supporting evidence within 5 working days. This procedure shall not be required if the debtor attaches to the application a statement of consent to the opening of the restructuring proceedings from all

the creditors affected. However, in the absence of a statement of consent from the creditors, the debtor must carefully consider the legal conditions to access the restructuring procedure.

Although the Directive leaves the possibility open also for creditors to apply for this procedure, even in the absence of the debtor's consent (except for SMEs), the Hungarian legislation has not made use of this more creditor-friendly approach and allow only voluntary access by debtors.

Early warning systems

Member States should provide businesses with early warning tools that **enable debtors to identify circumstances that make insolvency likely and warn them of the urgent need to act**. Member states have to choose which indicators trigger an alarm or warning regarding the economic health of the enterprise. These indicators can be **methodological guides, economic and financial advice, alerts from accounting services or tax authorities, IT applications** to predict the occurrence of an economic crisis based on specific data provided by businesses. The best practices and manuals collected as a result of the EWE (Early Warning Europe) project have also been published to support the development of systems in Member States. In addition, there are extremely simple, yet helpful, indicators, such as defaults, particularly of tax and social security obligations. Public creditors can therefore play a significant role in an early warning system: since distressed enterprises typically delay their tax and social security payments first, these creditors may perceive the difficulties of enterprises before other creditors. (A good example of the this would be the Hungarian administration practice, where the tax authority may grant a taxpayer to pay his tax debt in instalments in case of temporary payment difficulties, provided that the taxpayer is not responsible for the difficulties.)

Given the variety of instruments to be developed, it is not necessary to describe the specific instruments in the normative text, and this has not been done in the Act itself, which only provides the regulatory framework. For businesses, the Hungarian Government shall publish materials on the **online platform designated to provide government information services, including methodological guidance and other services** that could help the enterprises to identify adverse developments in their financial situation and the likelihood of insolvency especially for SMEs and their members and managers. Early warning tools shall support enterprises to identify financial risks, avoid unjustified business risks and manage financial distress appropriately. The platform provides the debtor and the representatives of the employees with relevant and up-to-date information on the availability of early warning tools including the restructuring procedures and measures.

Access to preventive restructuring

Preventive restructuring procedures represent the main building block of the Directive. In general, Member States will have to incorporate or adapt existing procedures **to allow enterprises to restructure their debt without full intervention of the courts, and before enterprises are insolvent** (hence the term “pre-insolvency procedure”). The overall objective is to maximize the use of hybrid restructuring, **combining judicial actions with debtor-creditors negotiation**.

In Hungarian law, pre-insolvency proceedings have separate place in the insolvency system, and are governed by separate legislation (see point 2). The debtor has a preventive restructuring framework at its disposal to implement restructuring measures to avoid insolvency and ensure the viability of its business, thereby protecting jobs and maintaining business activity. The

decision to initiate the procedure is taken by the debtor's decision-making body (the sole member in the case of a single-member legal entity), but in Hungarian law the **debtor may apply to the Metropolitan Court of Budapest as the court with exclusive jurisdiction to initiate the non-litigious civil procedure** itself, whereby the various frameworks become available. One of the great advantages of restructuring proceedings is that they are mostly controlled by the parties and the court has limited jurisdiction. Furthermore, not all creditors are necessarily involved; **it is up to the debtor to decide who to involve in the procedure. Restructuring proceedings can be conducted as a confidential procedure if the company's interest is better served by not disclosing information about the restructuring, as this may prevent it from continuing to operate because of distrust on the part of the partners.** The Directive allows for both types of procedure, giving Member States relatively wide legislative scope. Those who are involved are granted a moratorium (stay) on payment, if requested, so that they can continue negotiations and prepare a plan, while continuing to perform their contracts with the creditors who are not involved. A confidential stay can support some types of restructuring. In order to maximize chances of restructuring (e.g., by preserving ongoing credit relationships; suppliers' credits, etc.), the stay could be kept confidential so that only those creditors affected by the stay know it exists. This gives the debtors a flexible tool to allow the company to continue its operations while it can start negotiations with the most important creditors on whom its financial stability may depend. The confidential nature of the procedure can be maintained in the case of the request for a limited moratorium (limited stay), but if the debtor requests a general moratorium (general stay), the procedure will become public restructuring procedure and will be published. In such a case, a public procedure and a general moratorium by publication does not harm the interests of the parties, but rather may help to protect the debtor and the interests of creditors. **However, if all creditors are involved, and the moratorium is general, the public procedure increases the jurisdiction of the court.**

In Hungarian law, the **confidential character is a novel solution**, which was not present in our insolvency proceedings so far, such as bankruptcy or liquidation proceedings. In many cases, the very fact of being made public is the reason why bankruptcy proceedings fail, and the debtor is liquidated, even though the debtor may be viable and his business is needed, but he may have borrowed badly in the past and got into trouble. An important difference with liquidation proceedings is that restructuring is based solely on the debtor's decision and cannot be initiated by the creditor.

Restructuring proceedings **may be initiated by any legal entity carrying out economic activity or by an organization** (lacking the legal status of a legal person) **with civil personality, but the law specifies the types of debtors for which the initiation of proceedings is excluded:** the scope of the Act does not extend to, inter alia, financial institutions, private entrepreneurs, and public bodies. The Act also excludes from the scope of the procedure, i.a. taxes and social security contributions related to employment, value added taxes and property subject to criminal coercive measures. The decision to open the proceedings is taken by the debtor's decision-making body (the sole member in the case of a one-person company), but the debtor may apply to the Metropolitan Court of Budapest for the non-litigious civil procedure itself. The National Office for the Judiciary has published on its website the **electronic forms to be filled in** for the restructuring procedure. **Legal representation is mandatory during the procedure.** The debtor's decision-making body must set the starting date for the proceedings and the end date will be the date of full implementation of the measures adopted in the restructuring plan or the date of failure. As a general rule, it is not possible to carry out several restructuring proceedings at the same time.

As mentioned above the restructuring proceedings may be conducted as a confidential (informal) or a public one, depending on the affected creditors involved in the restructuring,

and the type of stay requested by the debtor. The starting date of restructuring means the date shown in the decision on restructuring made by the debtor's decision-making body, but this date may not be earlier than the date of the decision and may not be later than the fifteenth day after the date of the decision. If the court orders a general stay, the restructuring procedure shall be considered a public restructuring procedure from the date of publication of the temporary order of the general stay in the Companies Gazette until the final conclusion or termination of the restructuring proceedings.

Debtor in possession

According to the rules of the Directive, Member States have to ensure that debtors accessing the preventive restructuring procedure remain totally - or at least in part - in control of their assets and the day-to-day operation of the business. In pre-insolvency proceedings, it is a key element, that the debtor generally remains in possession of the business, as debtors will be unlikely to use these proceedings if they will be removed from their business. Moreover, allowing debtor to remain in possession of the business allows for the smooth business management. However, particularly in the application of instruments such as a general stay that limits the creditors' rights, the ability of debtors to remain in control of the business must be balanced with protections against abuse. The Directive provides that **appointment of an insolvency practitioner** is mandatory in certain circumstances, although its role in such cases is limited. Member States shall require the appointment of an insolvency practitioner **at least where (i) a general stay of enforcement actions is granted** by judicial or administrative authority and this authority decides that a practitioner is necessary to safeguard the interest of the parties; (ii) a judge or administrative authority needs to approve a restructuring plan with a **"cross-class" cram down**; or (iii) where **it is requested by the debtor or by a majority of creditors** (who should then bear the cost). However, the role of such an insolvency practitioner in the three above situations is limited to assisting the debtor and creditor in negotiating and drafting the plan. Member States can decide to give the insolvency practitioner greater oversight over the debtor's management, increasing creditor protection while lowering ease of use. In cases where an insolvency practitioner is required to be appointed to assist the debtor to negotiate and draft, the parties could expand the insolvency practitioner's role to supervise the actions of the debtor or take partial control of the daily operations of the business, for example by approving any transactions outside normal business operations. Member States **may also decide on a case-by-case basis to appoint an insolvency practitioner, depending on the circumstances of the case or the debtor's needs**, which may already exist under a Member State's national law (e.g., in cases of fraud or mismanagement).

As a general rule under the Act, **the debtor retains control over its assets and can manage the day-to-day operations and the business** ("debtor in possession"). However, **the insolvency practitioner also has significant powers in the procedure, and his or her duties may include supervision of the debtor's management**. Supervision of the management will be ordered by the court, in principle, on request, if this is indicated in the application for approval or on appointment, if creditors so request. The reason for this is that restructuring proceedings are not insolvency proceedings, so there is no reason why the debtor's discretion in the area of its own management should be limited. However, if creditors still consider it appropriate, they may request the approval or the appointment of an insolvency practitioner to supervise the management. It is not excluded that the debtor's application includes a request to this effect. Supervision of the management may involve both administrative supervision (access to documents, records, requests for clarification) and supervision of the content of economic decisions (granting of consent to certain obligations, economic control of new and temporary

financing). In the case of a contract containing a guarantee, the approval not only of the insolvency practitioner but also of the creditor affected is required if it goes beyond the scope of normal management, i.e. outside the normal course of business, in terms of size or type of transaction. The cases for the appointment of an insolvency practitioner are broader in the Act than the minimum set out in the Directive, e.g. always mandatory in the case of a general stay, not only when required by the interests of the parties [see Article 5(3)(a) of the Directive], i.e. the appointment must be made without any special examination if no insolvency practitioner has been appointed previously (e.g. the same applies in the case of a request for confirmation of a plan applying the rules on “cross-class” cram down.)

Stay of creditor actions

A stay provides debtors who seek to restructure their debts with protection from actions by their creditors that may adversely impact the restructuring while a plan is being negotiated. The Directive provides that **Member States have to ensure that debtors may benefit from a stay to support the negotiation of a restructuring plan**. While a stay allows a restructuring to take place without the possibility that a creditor act may undermine a collective resolution of debt distress, it encroaches upon the contractual rights of creditors and **should therefore be designed to sufficiently protect creditors’ rights**. This is particularly the case given that preventive restructuring are used prior to insolvency: when there is only a likelihood of insolvency. In cases where the debtor is only “likely” to be insolvent, pre-insolvency proceedings must take special care in designing a stay so that debtors do not abuse the proceedings merely to delay creditor action. The Directive gives Member States significant discretion over the scope of the stay, requiring them to make key decisions with regard to debtor versus creditor protection. For example, **Member States can choose whether the stay is general (applying to all creditors) or limited to affected creditors or only certain classes of creditors** (e.g., financial creditors) (Figure 1.)¹.

Figure 1. Options for stay of creditor actions under the Directive

<i>General stay (including secured and preferential creditors)</i>	<i>Limited stay</i>	<i>No stay if unnecessary or ineffective</i>
	<i>Only affected creditors</i>	
	<i>Only certain classes of creditors (e.g. financial creditors)</i>	

In that regard, unaffected creditors should be exempt, as they should be paid in full on their contractual terms and therefore there is no justification to have their enforcement rights against the debtor curtailed by a stay. Moreover, in informal restructurings, it is standard practice to have a standstill agreement among financial creditors, leaving other creditors unaffected. The Directive further provides that national laws may exclude certain claims or categories of claims from the stay in “well-defined” circumstances where such an exclusion is duly justified and where enforcement is not likely to jeopardize the restructuring of the business or where the stay could unfairly prejudice creditors.

¹ IMF Working Papers 2021, 152; <https://doi.org/10.5089/9781513573595.001>

Under the Act, the general stay (moratorium applying for all creditors) or a limited stay (moratorium applying only for affected creditors) can be imposed.

In order to facilitate the negotiation of a restructuring plan as part of a preventive restructuring framework, debtors may benefit from a 'stay of individual enforcement actions' (moratorium). The initial duration of the stay shall be for a maximum period of four months, which may be extended for a maximum period of twelve months in duly justified cases. However, in order to protect creditors' interests, the legislation limits the right to apply for a moratorium.

In Hungary an important difference between bankruptcy and restructuring proceedings is also to be found in the moratorium. In the case of bankruptcy, the moratorium is general, i.e. it applies to all creditors and lasts until 0.00 on the second working day after the 180th day following the publication of the moratorium in the Official Gazette of Companies, unless extended. In contrast, in restructuring, the moratorium may be general or limited. A limited moratorium means that it does not cover all creditors or all claims. In a restructuring, the moratorium is for a limited period of time, up to a maximum of 4 months, and cannot exceed 12 months if extended. In these proceedings, the fact of the moratorium need only be published if it is general, in which case the restructuring proceedings are necessarily public. In the case of bankruptcy, if no agreement is reached or if the restructuring proceedings do not comply with the law, the court terminates the bankruptcy proceedings, and the debtor is declared insolvent ex officio in liquidation proceedings. This automaticity is not present in restructuring proceedings, leaving both the debtor and the creditors greater room for determining the form and manner of settlement of the outstanding debt.

The court may order a 'stay of individual enforcement actions' (moratorium) in order to facilitate negotiations on the restructuring **plan at the request of the debtor, which will constitute a temporary limitation of the creditors' rights in respect of the claims affected. During this moratorium, the creditor to whom the moratorium applies:**

- may not initiate enforcement proceedings against the debtor (ongoing enforcement proceedings initiated after the starting date of the restructuring procedure are suspended);
- may not initiate liquidation proceedings against the debtor;
- may not exercise set-off against the debtor (with the exception of pending judicial proceedings initiated by the debtor, regarding a request for set-off submitted before the starting date of the restructuring);
- shall refrain from making any claims against the debtor that is in breach of the purpose of the moratorium.

In order to protect the interests of creditors, the right to apply for a moratorium or for an extension or renewal of the moratorium is limited.

The moratorium applies only to claims which have fallen due before its commencement, the debtor being obliged to pay all other debts.

It is important to note that the tax authority is not considered as an affected creditor in respect of public charges arising in respect of wages and salaries claims, and value added taxes, which cannot be involved in restructuring proceedings (see point 3.3.), and therefore the moratorium does not preclude the possibility of claiming these creditor claims (these claims are not considered as affected claims).

Restructuring plan

The purpose of restructuring is to enable the debtor to agree a restructuring plan with the affected creditors. Under the new rules of the Act, certain elements must be included in the plan, such as a description of the debtor's financial situation, the identification and classification of the parties involved (affected creditors) including their claims and the terms of the plan. The negotiation process for the plan should not be open-ended, the statutory timeframe must not be exceeded, otherwise the restructuring may be failed. **The Act specifies the time and event limits that lead to the failure of the restructuring.**

The negotiation of a prior restructuring plan is facilitated, in some cases by the appointment or ex-officio secondment of an insolvency practitioner to assist in the preparation of the plan. In the course of the procedure, the court may, at the request of the debtor or the creditor, appoint an insolvency practitioner to assist the debtor, who is responsible, inter alia, in communicating with creditors, drafting, voting on and implementing the restructuring plan and is also responsible for the proper implementation of the plan. **Insolvency practitioner's assistance can ensure that a restructuring plan is prepared that is realistically feasible and can genuinely help the debtor to restore solvency, secure its operations, reduce its debts and meet its obligations.**

The Act respects the basic principle that **affected creditors have a right to vote on the plan.**

A further advantage of the restructuring procedure over a purely contractual agreement between the parties is that, if the restructuring plan did not gain majority support in one or several classes, the debtor may request the court to decide on the approval of the restructuring plan by way of a compulsory agreement between the creditor classes (request for confirmation of a plan **applying the rules on "cross-class" cram down**), subject to strict legal conditions for reasons of guarantee. In this way, the situation that often occurs where a single creditor blocks the agreement and thus the debtor's survival cannot occur.

If the vote on the restructuring plan has not gained the necessary support for its adoption among all classes of creditors, the debtor, the debtor's equity holder with at least a majority interest or, with the debtor's consent, any of the creditors concerned may apply to the court for the approval of the restructuring plan by way of a compulsory agreement among the classes of creditors ("cross-class" cram down).

The effect of "cross-class" cram down is that the disagreeing creditor (class) is also covered by the plan.

Under the Act, the conditions for approval are strict: a majority of the creditor classes must have the requisite creditor support votes and, among these classes, at least one of the creditor classes voting in favor must be a secured creditor class or a creditor class linked to the economic activity. If this failed, it is sufficient if at least one creditor class which would not be likely to be satisfied in the liquidation proceedings supports the restructuring plan. **The restructuring plan must also comply with the relative priority rule laid down as principle in the Directive**, according to which creditor classes of dissenting creditors should be treated at least as favourably as any other class of the same ranking and more favourably than subordinated classes. The Act therefore does not avail itself of the option provided in the Directive to require compliance with the absolute priority rule, whereby dissenting creditors must be fully satisfied if a subordinated class is satisfied, in the plan.

The Act also sets out the policy rule that no class of creditors and no affected creditor should receive more than the full amount of its claim (e.g. additional proceeds as "compensation" for funding the debtor as provided in the plan).

If the court confirms the restructuring plan by means of cross-class cram down, this will have the same legal consequences, effects as the restructuring plan approved by the court.

Safeguards: Best interest of creditors' test

The system of safeguards of the Directive is inspired in modern reorganization frameworks. It incorporates not only class voting and cram-down, but also the key safeguards of reorganization: the best interest of creditors' test and the absolute priority rule. The best interests of creditors' test, as a fundamental creditor protection, can be reinforced by choosing the criteria for determining the baseline liquidation value. The "best interests of creditors' test" protects individual creditors. This safeguard applies to any creditor, and states that no creditor should receive less, under the restructuring plan, than what they would have received in the liquidation of the debtor's estate. This safeguard is embedded in traditional insolvency law as a fundamental protection against the expropriation of creditor rights. The Directive adopts a legal concept rooted in US bankruptcy law, based on the idea that a creditor has no reason to reject a plan if it will get at least as much return under the plan as if the debtor were liquidated.

In modern insolvency procedures, the plan establishes classes of creditors, treating preferred creditors as a separate class. Since each creditor class must approve the plan, these creditors cannot be voted down by other creditor classes. Moreover, even if a creditor remains in the minority in its own class, it can veto the plan under the best interests of creditors methodological test.

Under the Act creditors who vote against the restructuring plan and the debtor's equity holders can file a counterclaim/ objection to have the court also examine whether the voted restructuring plan meets the interests of the creditors as a whole, the so-called best interests of creditors test. In the concept of the best interests of creditors methodological test, the use of plural is normative. In this context, the court should not consider how the relevant creditor filing the counterclaim would fare under a next best alternative, but whether creditors voting 'no' would generally fare better under a different solution.

Duties of directors

The duties of directors in the period approaching insolvency have important relevance for preventive restructuring. These duties importantly aim at protecting the interests of different stakeholders from managerial decisions that may adversely impact the debtor's estate. The Directive sets out steps that directors should take in order to minimize losses and avoid insolvency in cases where a company experiences financial difficulties. . Where there is a likelihood of insolvency, the Directive requires directors to protect the legitimate interests of creditors. Specifically, in these cases, the Directive requires directors to have due regard, as a minimum, to the interest of creditors, other stakeholders and equity holders; the need to take steps to avoid insolvency; and the need to avoid deliberate or grossly negligent conduct that threatens the viability of the business. The Directive does not establish any hierarchy among different stakeholders whose interests need to be given due regard. Instead the Directive leaves this determination for Member States. The duties of directors present an area where restructuring and insolvency rules need to be well coordinated with company law.

The Act lays down among the basic principles that the debtor's directors and equity holders have to cooperate with the insolvency practitioner. The debtor's directors, the equity holders, the creditor affected and the insolvency practitioner have to act in good faith and fairly during

the exercise of their rights and the performance of their obligations during the restructuring procedure.

Once the decision to restructure has been taken, the debtor's directors must take all necessary measures within his or her powers to take account of the creditors' interests and to take decisions within the competence of the debtor's decision-making body or, in the case of a debtor which is a single-member legal person, its founder or sole member, in particular decisions necessary to avoid insolvency, and must refrain from unduly favouring certain creditors or taking business risks which are unjustified in relation to the debtor's financial situation.

It should be noted here that the Directive specifically addresses the interests of stakeholders in the context of restructuring, by stipulating that Member States must ensure that stakeholders cannot unduly prevent the adoption of a restructuring plan that would restore the viability of the debtor. To this end, Article 9(3)(a) also allows Member States to exclude shareholders from voting. The Act does not provide for a specific separate creditor class of equity holder: the equity holder, if he/she is a creditor, may vote on the plan as a creditor in the creditor class according to the classification of its claim.

The Directive may use the term 'equity holder' to refer to a membership relationship where the debtor member is present in the company as an investor rather than as a 'personal contributor' (owner); in practice, the attitude of the member to restructuring in a smaller legal entity in the form of a partnership is obviously different from that in a joint-stock company and therefore the application of certain provisions may have different significance.

The Act also ensure the effective implementation of the restructuring by introducing more favourable rules on decision-making than those in company law, reflecting the Directive's requirement for stakeholders referred to above.

The Act also sets out, as a transposition of Article 19 of the Directive, the basic management and operational framework for the debtor's management, which the debtor must take into account in the event of the likelihood of the debtor's insolvency. Importantly, the provision declares the primacy of creditors' interests over the interests of the equity holders and the parties concerned.

Conclusion

The Directive is a welcome first step in the convergence of EU insolvency frameworks, since it addresses an important and wide range of topics: early warnings, preventive restructuring tools, institutional aspects of insolvency systems, and data collection. It has benefitted from the experience of European systems in the development of restructuring legislation and mechanisms to prevent the insolvency of enterprises. Adequate implementation of the Directive can bring much-needed improvements to national systems, especially in the context of the current crisis. This legal framework has been missing in the Hungarian insolvency law. This new set of rules offers a number of tools to ensure the success of the pre-insolvency cases. It remains to be seen whether the new procedures will change the approach of debtors and creditors, as the restructuring, which aims to introduce a pre-insolvency procedure, opens up completely new perspectives for the parties concerned, which were not present in the bankruptcy and liquidation proceedings available until now.

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