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Greek Tragedy

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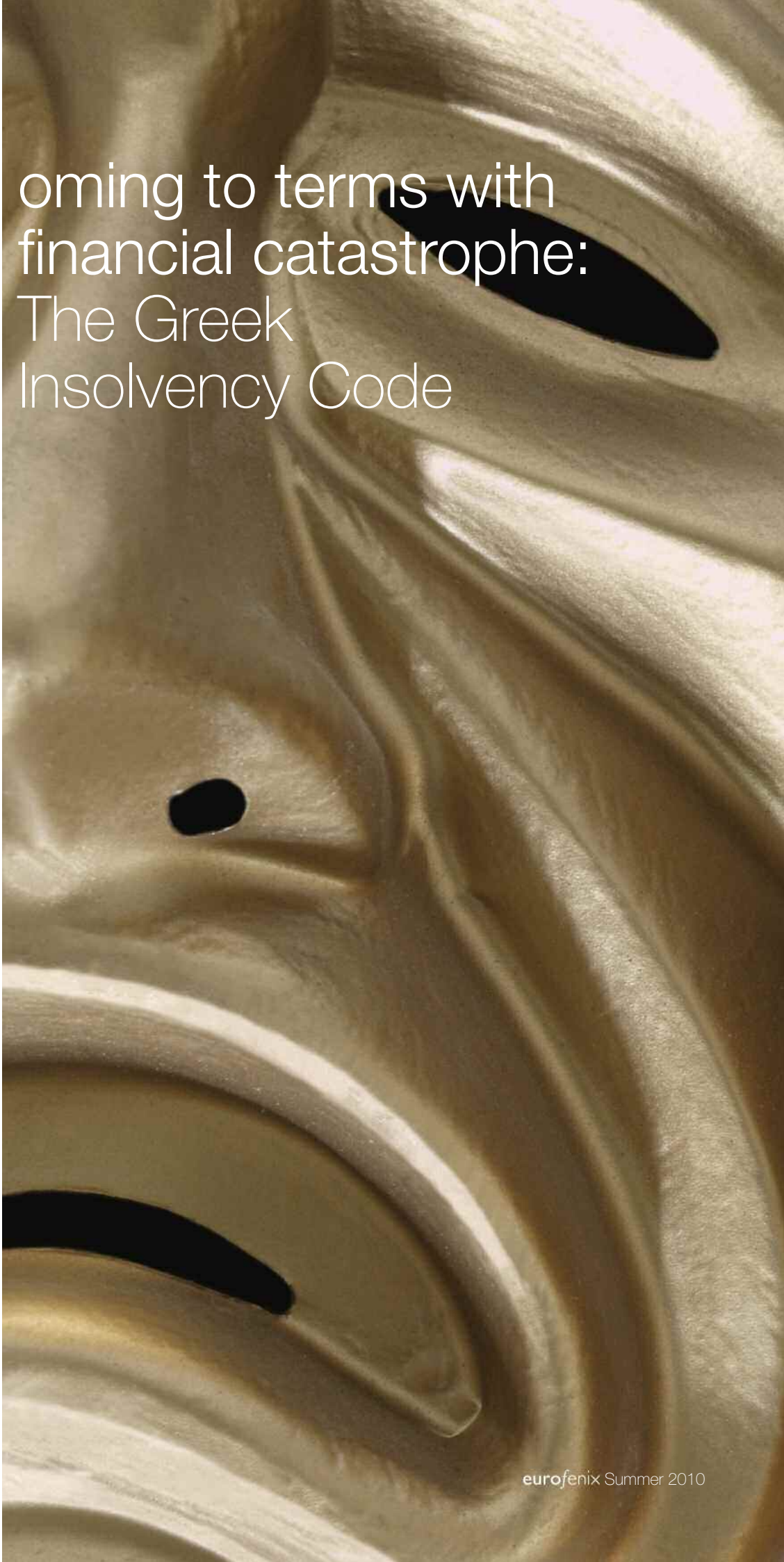
Coming to terms with financial catastrophe: The Greek Insolvency Code



Yiannis G. Sakkas looks at the effects of the recently introduced Insolvency Code in light of the current economic situation

***Quod me nutrit, me distruit* (*"What nourishes me, also destroys me"*). This epitomises in the most profound manner the pragmatic position of the Greek economy. To service the imbroglio of existing debt, Greece had to borrow from the financial markets, which either on account of scepticism, or to excogitate the financial annihilation of the Greek state, demanded punitive rates that propelled the national economy further into the debt trap.**

The EU and IMF rescue mechanism that was agreed, amid a pro European and political populism stance, was inexorably triggered to address liquidity issues in return for drastic budget cuts. In this overall economic environment and in fear that the draconian austerity measures will lead to a decline in consumer spending, debtors and creditors alike see the risk of insolvency materialising for a comprehensive number of Greek companies and assess how their

options under the new insolvency code[1] (the "IC") would make operational the objective of mitigating the calamity of corporate default.

The 2007 reform made this an easier exercise than under erstwhile legislation on two counts. First, the IC has compiled numerous acts and miscellaneous laws relating to the insolvency of private individuals and corporate entities in a single instrument. Therefore, the assessment of legislative options has parted from the complicated procedure that mandated reference to a plethora of legislative instruments. In terms of substance of the law, the reform was established to introduce a modernisation of the legal framework governing insolvency proceedings, always considered in relation to the antediluvian provisions of the repealed legislation. Although the law purports to maintain a balance between debtor's and creditor's rights, it can be characterised as a mildly pro-creditors regime. However, all parties involved are said to benefit from provisions to expedite insolvencies and the rehabilitation mentality of the new code, through the available early recourse and rescue proceedings.

Filing for insolvency is the entry procedure for all institutions available under the IC with the exception of insolvency mediation of article 99, a new voluntary pre-insolvency workout, devoted to enhance the prospect of recovery for underperforming corporate debtors which have not yet crossed the threshold of default. In case of involuntary petitions, there is not a *de lege* demand for debt in excess of a specified amount, but creditors have to observe the principle for prohibition of abuse, akin to the doctrine of estoppel. Filing does not result to an automatic stay and the commencement or continuation of a judicial, administrative or other action against the debtor is only precluded on the inception of proceedings, but provisional measures can be granted on the court's discretion.

Meeting of Creditors

The determination of the manner in which insolvency proceedings will then proceed is entrusted to the *meeting of creditors*. The *meeting* is composed of all creditors and is called to decide on the suspension or continuation of the debtor's business for a period of time, the sale of the business as a going concern or by piecemeal, as well as to vote on a reorganisation plan, if one has been filed and not been rejected in "judicial pre-examination".

The new code reserves an active role for the debtor, almost a protagonist, when it comes to filing a rescue plan, which can be either submitted, exclusively by the company, together with the insolvency petition, or within 120 days from the decision declaring the insolvency. The syndic can also propose a rescue arrangement but not prior to the expiry of the four-month period. Nevertheless, a similar right is not extended to creditors.

Pre-Pack disposals

The new Greek insolvency code does not provide for proceedings analogous to pre-pack administrations available in rescue regimes in other jurisdictions, predominantly Anglo-Saxonic *fora*, which have demonstrated their propensity to grant court ratification to debtor-creditors agreements in fast track pre-pack arrangements, like in the recent example of the English courts which have been scrutinised by aggravated creditors using colourful language, ironically in relation to a Greek telecoms group pre-pack administration, the largest one to date. However, the silence of the Greek insolvency code on the admissibility of pre-pack disposals is not *prima* facie grounds for the idea to be abandoned altogether. Undoubtedly, a pre negotiated rescue plan would deviate from the procedural adherence of the Greek legal order. That should not preclude entirely novel legal arguments, that would seek to attune the paucity of precedence in this field, by fully observing the

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systematic rules imposed to ensure the protection of all parties, namely the *pari passu* treatment of creditors, with emphasis on the unsecured class.

Creditors' rights

This does not insinuate that the rights of secured creditors should be eroded for the benefit of unsecured claims. The bedrock principle underlying secured financing in Greek insolvency law is that the instigation of insolvency proceedings does not preclude a secured creditor from enforcing its security, unless creditors elect otherwise, usually upon tactical considerations pertinent to the circumstances. Secured obligations are exclusively satisfied through the realisation of the nominated collateral in a public auction, in which secured lenders do not have a statutory right to credit bid at a foreclosure sale by using the secured debt as currency in lieu of cash. The order in which the proceeds of disposition shall be applied is statutorily mandated. Senior security holders are satisfied in priority, after the sale expenses and the costs for the preservation of the assets are reimbursed. Greek law does not provide for further impairments by way of a requirement to set aside a percentage of the proceeds for the satisfaction of unsecured debt, like in the case of the prescribed part orders under the UK insolvency Act.

Conflict

However, the collective nature of insolvency proceedings unavoidably precipitates a conflict between secured creditors rights and subordinate claims, especially in the context of judicial reorganisation. To ensure that a corporate recovery attempt will not be futile, certain restrictions have been imposed on the remedies available to secured creditors, namely the prohibition of executionary measures in assets that are vital for the continuation of the business activities. A proposed rescue plan can also cram-down secured creditors interests but security continues to protect the claim as adjusted under the plan. However, the consummation of the plan requires consent from multiple layers of creditors, including the acquiescence of 40% of lenders holding collateral, before it enters the court for ratification. Arguments against an inequitable reduction in the interest of secured creditors are highly persuasive with the court, which in such cases will usually not sanction the plan.

Insolvency mediation

There has not been a significant amount of case law reported on reorganisation proceedings to date. The explanation is in all likelihood related to insolvency mediation, which has gained currency among debtors. However, the code underscores that article 99 proceedings apply only to debtors not technically insolvent but in current or projected financial distress and therefore, *ex vi termini*, insolvency mediation is not an alternative to reorganisation proceedings. Nevertheless, both the predisposition of the judiciary to demonstrate its support to the newly introduced institution of article 99 and the possible incentive of debtors to benefit from measures of early recourse without the abasement of insolvency proceedings, masking to this effect default as financial distress, echoes concern that perhaps some debtors would be better placed in insolvency proceedings.

Debtors' obligations

In the expected deluge of insolvencies, the possibility of less than orthodox business conduct by debtors purporting to avoid the opprobrium of financial default cannot be excluded. This is why an obligation is imposed on debtors to voluntary enter the insolvent status by petitioning the court within maximum fifteen days from the time they have ceased payments in a general and permanent way. For legal entities, this obligation extends to the board of directors members culpable for the delay in the filing of the insolvency, who are also personally liable to compensate creditors for all debts incurred from the time the obligation to file arose. In addition, usual provisions for setting aside preferential transactions and transactions at an under value also apply under Greek law.

The Lydian stone for the determination of debtors and creditors rights is the judiciary's interpretation of the provisions of the new code. In doing so, the courts should view with sympathy approaches that promote the efficient administration of claims and the overall purpose of the insolvency code, even when their mentality deviates from the norms to which insolvency judges are accustomed to, as long as these do not form instrumentalities to promote self interests and do not lessen protection of parties involved in the insolvency procedure. This is a unique opportunity for the Greek insolvency code to be the silver lining in these odious financial circumstances.

Footnotes

1. L. 3588/2007, SG A 153/10.7.07, applying to all proceedings commencing after 16th September 2007.

YIANNIS G. SAKKAS
Associate, Anagnostopoulos-Bazinas (Athens)