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# German Federal Government Outlines Path to Comprehensive Reform in Restructuring and Insolvency Law

***Government draft of law implements EU Restructuring Framework, and introduces new restructuring instruments.***

On 14 October 2020, the German Federal Government published a government draft of the Act on the Further Development of the Restructuring and Insolvency Law (SanInsFoG). This government draft primarily provides for the highly anticipated implementation of Directive (EU) 2019/1023 on Preventive Restructuring Frameworks (Restructuring Directive) into German law. In addition to the adoption of a Law on the Stabilization and Restructuring Framework for Enterprises (StaRUG), which serves to implement the Restructuring Directive, the draft contains several other reforms of German insolvency and restructuring law. In particular, the Insolvency Code shall be adjusted in those areas where the Federal Government saw need for improvement following the evaluation of the Law to Further Facilitate the Restructuring of Enterprises (ESUG) passed in 2011. According to the Federal Government's timetable, the law shall become effective in substantial parts as soon as 1 January 2021.

## Law on the Stabilization and Restructuring Framework for Enterprises

The core of the government draft is the draft of the StaRUG, in which the Federal Government pursues a modern approach to restructuring: The StaRUG's wide catalog of new restructuring instruments offers debtors the opportunity to implement a restructuring concept with the support of a majority of creditors against obstructing creditors, but also involves considerable challenges for the affected stakeholders and the debtor's directors. In any case, the impact of the StaRUG on German restructuring and insolvency practice will be significant.

### Core: Restructuring Plan

A core element of the StaRUG is the option of a pre-insolvency restructuring by way of a restructuring plan. The debtor has the opportunity to submit a restructuring plan to its creditors to provide for the restructuring measures as well as restructuring contributions of the affected creditors. In principal, a majority of the creditor groups defined in the restructuring plan with 75% of the claims in each creditor group is sufficient for the adoption of the plan. If the required majority is not achieved in one class, its approval may be replaced under certain conditions by a so-called “cross-class cram-down”. In this respect, the StaRUG uses concepts and elements that are partly known from the US Chapter 11 proceedings, the English Scheme of Arrangement, and the German insolvency plan proceedings, but overall creates its own, new approach.

The debtor (in agreement with the stakeholders who support the plan) is granted flexibility to adapt the structure of the proceedings to the actual circumstances. Unlike insolvency proceedings, no consolidated overall proceedings are required. For example, a debtor could restructure only the financial liabilities and could keep the involvement of the courts to a minimum to conduct the proceedings largely privately. The StaRUG thus introduces a selective and generally silent restructuring instrument.

Such a procedure will, however, only be successful for all participants if it is professionally prepared and conducted. The draft law contains instruments against unfair use of the proceedings as well as numerous legal protection options, which means that there are also options for safeguarding and asserting interests on the side of the stakeholders who reject the plan.

### Framework for the Restructuring Plan

#### In particular: Moratorium, Restructuring Agents, Contract Adjustments, and Increased Liability

In order for a debtor to be able to prepare and negotiate the restructuring plan, the StaRUG offers the possibility of imposing a moratorium (the draft law calls it a "stabilization order"), whereby measures of individual enforcement of creditors' rights may be restricted. The moratorium may initially be imposed for a period of up to three months, although under certain circumstances follow-up orders to extend the moratorium to a maximum of eight months are permissible.

In certain cases, restructuring officers shall be appointed and will be responsible for monitoring the propriety of the proceedings, and, if necessary, mediating between the parties. The debtor and creditors have certain rights of influence regarding the person and the appointment of the restructuring officer.

The draft of the StaRUG also allows interference with existing contractual relationships (thereby going beyond what the Restructuring Directive requires). Under strict conditions, a debtor can obtain a court order to terminate a contract that has not yet been completely fulfilled by both parties if the other party is not prepared to make the necessary adjustments or termination of the contract necessary for the implementation of the restructuring project. A comparable option is, for example, also foreseen in the Dutch implementation law. A possible field for application can be long-term lease agreements.

Finally, the draft clarifies that with the occurrence of imminent illiquidity, the directors' primary duty shifts to serving the interests of the creditors. From the time of the notification of the restructuring plan at court, a director's breach of duty at the expense of the creditors shall be sanctioned with an external liability towards the affected creditors.

## Extended Suspension of the Obligation to File for Insolvency

Independently from the SanInsFoG, the German Parliament has adopted further amendments to insolvency law in view of the ongoing COVID-19 pandemic: Under the Law to Mitigate the Consequences of the COVID-19 Pandemic in Civil, Insolvency and Criminal Procedure Law, the obligation to file for insolvency was suspended until 30 September 2020. With an Act dated 25 September 2020, the German Parliament extended that suspension until 31 December 2020 for those companies that are over-indebted in the sense of insolvency law as a result of the pandemic, but not cash-flow insolvent.

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