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Droit & Croissance promotes Law & Economics theory in France and beyond, by providing a forum for researchers and encouraging a multidisciplinary approach to study the economic impact of legal norms. Droit & Croissance regularly publishes constructive criticism and actionable propositions for effective reforms of French law in scholarly, professional as well as general interest publications.

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Opening remarks

KEYNOTE SPEAKER

Ana Boata, European Economist, Euler Hermes, Paris

Projections on the economy outlook in Continental Europe

Anna Boata

First, let me introduce my company and myself. Euler Hermes is the world leader in credit insurance. It is a subsidiary of the Allianz group. I am in charge of the macro economic analysis for Western European countries. I will share with you today our expectations for 2016 and forward.

After six years of economic crisis, we have exited the recession and resolved the Greek crisis, at least temporarily, as we still have three years to try to find a sustainable solution to unresolved Greek issues.

It is right to ask ourselves, is this growth enough ? Over the past four quarters, we have been happy to see only 0.4 % GDP growth on a quarterly basis and a little bit over 1 % on an annual basis, in the euro zone. This is good news given the fact that we come from a very strong and long lasting crisis. But we are left to wonder : why can't we do more ?

We have tried to identify, out of a number of outstanding issues, five reasons which can explain this type of steady-to-moderate growth, with no perspective for more.

First, there is the slowdown of the emerging markets. Over the past years, the emerging markets have been the growth engine for global growth and this engine has stalled. On the other side, advanced economies have gained pace. They have entered a recovery mode, albeit a low recovery mode. Even if the United States, the euro zone and Japan are improving, they are still very weak. Overall, you see in our latest forecast that the overall picture is not very bright. We have global GDP growth expectations that have been revised down compared to the beginning of the year and, more importantly, we are still below 3 % global GDP growth. Why do we care about 3 % GDP growth ? Because economists estimate that this is a threshold to reach in order for companies to start investing, to have more employment and more household consumption.

For the moment, even in 2016, we will remain below this threshold, for the sixth consecutive year. And if we take a closer look at the forecast, we also see that we are expecting a recession in Brazil. This may be the worst recession over the past twenty-five years. It may be there next year also even though we now expect stabilization.

Then, unsurprisingly, there is the situation in Russia, currently in a very strong recession, - 4 % this year, - 0.3 % next year. This is the consequence of the sanctions and the lower oil prices.

Then, we have the situation in China, changing its economic model and facing some short-term turbulences and a slowdown in growth. While this is not necessarily unhealthy it is certainly not good for global growth and will increase volatility. We have expectations of 6.5 % growth in China. If you look back, we had 10 % in 2010. This means that China's contribution to global GDP growth will be much reduced.

Then, we have the situation in Latin American countries facing difficulties due to their lack of economic diversification. They depend too much on oil and commodities exports. Today, with lower oil prices and lower demand for commodities, they are facing acute short-term difficulties.

When it comes to the situation in the euro, as you can see, we expect 1.4 % and 1.6 % growth this year and next year. But what you have to keep in mind is that half of this growth will come from Germany and Spain. Therefore, we have a very uneven recovery in the euro zone. Italy is still growing at a very weak pace, 0.7 % slowly emerging from three years of recession and low potential growth. Not to mention Greece, which is still in recession, after seven consecutive years.

Overall, the global picture is not catastrophic, but it is not encouraging either. The consequence of this slow growth is weak global trade. There are volume issues where global demand is still weak, a high level of debt in advanced economies and fast growing debt in emerging markets, especially in foreign currency.

Global trade – how many goods and services are exchanged at the global level – is increasing. There is a positive increase in real terms, in volume terms, even if it is not a significant acceleration. On the other side, this acceleration, while moderate, is compensated by a negative price effect. It means that

companies today face weak global demand and weak demand in the euro zone. It is the case in emerging markets but, more importantly, it is also the case in the euro zone, where demand is so weak that companies are forced to lower their prices in order to sell their product. The consequence is that companies sell their products at lower prices and do not invest because they are not sure to be able to recover investments that they might otherwise have made in innovation or in increasing their production or capacity.

There is a recovery in the euro zone with no investment, and most importantly, with no price increase. At the global level, we see, and expect a decrease of at least some 400 billion dollars in the value of goods and services exchanged. That means that we have lost at least 400 billion dollars in value compared to 2014.

As far as the euro zone is concerned, over the past quarters, we have seen a positive impact from the lower euro. We had been advocating for the implementation of a quantitative easing program by the ECB for a long time. The ECB did it at last but it was a little bit too late. We have indeed seen the positive impact of a lower euro. The euro has decreased by more than 20 % and most of the euro zone countries have benefited. It means that, in real terms, they have managed to boost their exports. There was more demand for the euro zone exports following the depreciation of the euro. But we are wondering what will happen now. Knowing that the euro is at a low level, it never went below 1,1 US dollars. Even if the ECB was to implement more quantitative easing, we doubt, it's almost impossible, that we will see another 20 % fall in the euro. This positive booster has been with us this year, but we don't think that we will see this kind of depreciation next year. One of the positive boosters is already behind us.

We saw low demand in the euro zone as well as globally. This is also true of purchases and prices. Weak demand is still a problem. Low inflation and downside price pressures are still a problem. We have expectations for inflation in the euro zone to reach only 0.9 % next year. The ECB target for inflation is 2 %. So we are not even at half of the target of the ECB.

The ECB was the driver that managed to help the European economy exit the recession over the past year. We saw that the weaker euro had a positive impact on exports. But we had quite a strong credit crunch in the euro zone, mostly in Southern European countries. SMEs in those countries have had to bear very high interest rates for bank loans. They were paying almost 5 %. If you compare this with Germany and France, you see that there is a difference of almost three percentage points.

We saw this fragmentation decrease after the ECB's quantitative easing program, but not enough, in our view. There is an upside trend over the past months but the measures implemented by the ECB are not sufficient to really resorb the financial fragmentation in the euro zone.

We talked about the absence of companies from the euro zone in the investment cycle. While the cost of credit is important we can also wonder if there is sufficient demand. Are there incentives for companies to invest ? If they don't believe so – which is the case today – they won't have any reason to borrow from banks. That is the reason why credit in the euro zone is, in effect, not recovering.

All in all, the quantitative easing program of the ECB has not yet had an impact on the real economy. More importantly, in the euro zone, SMEs or even bigger companies cannot have access to financial markets as much as we would like to and as much as other companies in the rest of the world do. There are a lot of reasons for this, but they are mainly related to regulations regarding capital requirements for banks.

Finally, the fifth reason for slow growth is the counterparty risk. At Euler Hermes, as a credit insurer, we look closely at this risk. We gather data - proprietary data - that we gather from the payment behavior of companies but also from their risk of insolvency.

Looking at payment behavior, we see a negative trend. Emerging countries are paying over longer periods than before. In China and Brazil. It's impressive. We have almost one week of delay compared to last year. On the other side, if we look at the euro zone, we have Italy where companies pay over very long periods, almost one hundred days. In France as well, we have payment terms of almost 80 days. We still have things to improve on this side.

Looking at insolvencies, we see a positive trend. Insolvencies in the euro zone and Western European countries are decreasing at last. For some of the countries this is the first time since the crisis. This is the case for France and Italy. However, mostly all of the Southern European countries, but also countries like France, are still at very high levels of insolvencies. If we compare this to pre-crisis levels, we are still two to three times above pre crisis levels. So, it's not because we have a decrease of 1 % that suddenly everything is getting better for companies and that counterparty risk is improving. There are still things to improve in order to resorb the negative impact of the crisis. The best in class countries, are the Northern European countries, like Germany, the UK, the Netherlands. These countries are on a declining trend in terms of insolvencies and they are also at low levels. This is why we call them "best in class".

In terms of sector risk, you will not be surprised to see that the construction sector is one of the sectors that remain very deteriorated. However, the outlook in the construction sector is improving. So, it's still not good, but it's getting better.

On the other hand we have sectors like the retail sector, or the transportation sector that are benefiting from positive short-term cycles. And, unsurprisingly, this is linked to lower oil prices, which are positively impacting the euro zone. Low oil prices are not positive for every sector of course. Quite naturally, machinery and equipment have deteriorated over the past two quarters.

Finally, we have sectors that are structurally in good shape. They have been so, through the crisis. Sectors like pharmaceuticals, agri-food, chemicals and aeronautics.

Let us have a small focus on the retail sector, because it's a sector that benefits from positive short-term boosters. The low oil prices in the euro zone means that households have had a boost in purchasing power. However, this has not been enough to really improve the outlook for retailers in Western European countries. One of the issues here is their low profitability. Some of them are very in debt, which is even worse. The issue in Western Europe remains the war for prices. We

saw that global trade was decreasing by billions of dollars in value terms. It is a consequence of the low demand, but also of increasing competition and what companies have to do in order to cope with it.

Finally, the third sector that we want to point out today is machinery and equipment. Of course, it is one of the sectors that is on a diverging trend compared to others. Low oil prices have triggered deterioration in the outlook of the sector in most countries. We have seen a constant deterioration in the sector since the third quarter of 2014. This is of course tied to the fact that investment in exploration and production in the energy sector has been cut. We saw a 20 % cut over the past quarters. The outlook is not really bright. We expect Brent oil to reach US$ 60 per barrel next year, on average. But more importantly, we expect Brent oil prices to remain below US$ 100 per barrel by 2020. This is perhaps the key point here that we would like to show you.

In conclusion for this presentation, I would say that while the ECB acted late with a quantitative easing program, we still need to see more. If you compare what the ECB did in Europe with what the Federal Reserve did in the United States or with what the Bank of England dis in the United Kingdom, the ECB actually did only half of what they did. And, especially, it did it late.

Let us consider what the ECB may announce. In any event and irrespective of the measures that they will implement, we are almost certain that it will make an announcement in December, even a small one, that could be continued with further measures in early 2016.

The outlook could improve if the ECB was to act as it should. However the most worrying fact perhaps for the euro zone, is the current lack of investment. Not only from companies. Public investment has fallen a lot in Southern European countries, whereas they were high in 2005. This is normal. They joined the euro zone quite late. They have benefited from the boost of European funds and they need to improve their infrastructure.

Germany is a country that is doing well today. Half of the euro zone growth comes from Germany and Spain. More importantly, Germany does not have a fiscal deficit. Germany could invest more and should invest more. Germany's investments have constantly been lower than that of other countries of the euro zone. The Germans have an investment gap that has accumulated over the years. They should invest in order to boost other countries in the euro zone as well.

So, overall, while it's good news to have a monetary policy program and to boost asset prices and credit. It is not enough. We have seen this over the past quarters. Now the open question is, should this continue ? We hope that it will. And we know what is missing in the euro zone in order to have stronger growth.

First roundtable

New trends and the recent reform in France

- The role played by non-bank buyers of distressed debt
- Exit of historical lenders : a problem or a temporary part of the solution ?
- How can the law affect the "right sizing" of the capital structure with additional liquidity injected as part of equity rather than debt
- The recent reform in France with the "Loi Macron"

KEYNOTE SPEAKER

Thomas Revial, Head of the restructuring arm (CIRI), French ministry of the Economy,

What can we learn from the last reform in France ?

Thomas Revial

I would like to start my speech with a few words about the CIRI and its actions alongside businesses facing financial difficulties. This may be one of France's particularities but the government decided more than thirty years ago to create a light public structure within the French Treasury which aims at offering support services to large companies for early restructuring in order to prevent bankruptcies as much as possible.

This structure was named the CIRI, which stands for *Interdepartmental Committee for Industrial Restructuring*. The CIRI assists private businesses facing economic difficulties and employing more than 400 people in France in the successful running of negotiations with their financial partners on their restructuring plan. Most of the time, the CIRI assists companies, which have initiated pre-insolvency proceedings, and in this context and at the request of the company, the CIRI will conduct mediation proceedings and ensure the coordination of public and private stakeholders. Of course, public authorities have no intention to substitute themselves for private partners, shareholders, bankers and suppliers. It is their very responsibility to participate in the resolution of the difficulties of the company. If necessary, through substantial industrial or financial restructuring measures.

There are generally three main phases in the CIRI's actions. First, a diagnosis phase, to understand the situation of the company and the causes of its difficulties. This phase aims at setting a common understanding of the situation for all stakeholders. Then, a design phase for a restructuring plan, to work on the business model of the company and the way to ensure its long-term economic viability. This phase may demonstrate that strong industrial or financial measures are necessary to ensure the continuation of the business and aims at sharing the company's turnaround strategy with all stakeholders. Lastly, a negotiation phase, which must lead to the conclusion of a unanimous binding agreement, sometimes with the provision of new financing from the company's shareholders or creditors.

The CIRI team seeks to meet three professional standards at all times. First, a neutrality standard. This is perhaps the most important one. The CIRI provides businesses and their partners with a comprehensive approach of operational and financial difficulties and seeks a fair distribution of efforts among all stakeholders. When trust between the parties is no longer present, the presence of an independent third party who has no other interest than contributing to saving jobs may be an asset to bring out fair and consensual agreements. Second, a responsiveness standard. The CIRI teams are fully available for businesses facing financial difficulties. This implies an ability to adapt the timing and the extent of the intervention to the situation of each company. This responsiveness is of course often required by the overstretched cash position of some companies. Lastly, the CIRI is bound by a confidentiality standard, which is necessary to maximize the prospects of success in restructuring.

The CIRI has been a partner of large companies facing difficulties for many years and has acquired a strong practical experience of our legal system to deal with restructuring situations and insolvency.

This brings me to my second point about recent changes in French law. I would like to highlight to you the new law's major breakthroughs, which, I believe, can have an impact on companies facing industrial or financial difficulties. These changes, introduced in the 2014 reform as well as the new law sponsored by our Minister for Economic Affairs – to which the CIRI has contributed most of its structural provisions – seek to draw the consequences of the evolutions we have seen in practice since the financial crisis and make our law more efficient to contribute to the general goal of the government to increase France's attractiveness.

The growing complexity of legal and financial arrangements and the intensity of industrial and financial restructuring needed for some businesses have made it necessary to adapt our law which is sometimes seen abroad as an obstacle to efficient restructuring because of its complexity and the feeling that sometimes stakeholders do not enjoy equal rights. In that respect, there are two main aspects of the recent reform I would like to discuss.

First, the 2014 reform brought changes and substantial improvements in French bankruptcy law in order to strengthen and facilitate out of court pre insolvency proceedings. Our conviction, born of experience, is that anticipation is key to prevent companies facing difficulties from becoming insolvent and to succeed in preserving business and employment as much as possible. To this end, two out-of-court pre-insolvency proceedings have been introduced by the law : ad hoc proceedings and conciliation proceedings.

These proceedings have features that enable strong and credible restructuring prospects, most of the time. They are flexible, voluntary and confidential processes in which the President of the Court appoints an agent to monitor discussions between the company and its major creditors. The Court agent, of course, doesn't have any management responsibilities or any coercive powers. These proceedings aim at reaching a unanimous workout agreement, which sets out terms and conditions for the restructuring of the existing debt and, if any, new financing extended by creditors or shareholders. In these proceedings, the management must cooperate with the Court appointed agent and the creditors to negotiate a solution to the company's difficulties. The major creditors are invited to consider debt rescheduling or even cancellation. In addition, shareholders can be invited to negotiate and potentially recapitalize the company or let other investors in. A debt-rescheduling plan accepted by some creditors cannot be imposed on other dissenting creditors. Unanimity must be reached which is often the best way to maintain confidence in the long run between the company and its financial partners.

Taking into account this element, the 2014 reform has strengthened and extended these pre insolvency proceedings thanks to several provisions.

For instance, obstacles to the opening of an ad hoc or conciliation proceedings have been removed. Any provision of a loan document providing that the election of these proceedings shall trigger an automatic acceleration of the loan is now deemed null and void. Creditors are therefore prohibited from accelerating a loan or terminating an ongoing contract based solely on initiating such proceedings. Furthermore, creditors are better encouraged to extend new financing, which is always very important for businesses in difficulty.

The priority of payment granted to new money facilities has been reinforced. New financing extended in the framework of a Court approved conciliation agreement enjoys a statutory priority of payment should the company subsequently file for insolvency. Since the 2014 reform, the power of the Court to reschedule claims of dissenting creditors over a period of up to ten years during a rehabilitation proceedings no longer applies to lenders who have provided super senior new money financing during a Court approved conciliation agreement.

Also, the efficiency of conciliation proceedings and their follow up review has been strengthened. It is now possible for a debtor to prepare the sale of the company during the pre insolvency proceedings and to implement it in a formal insolvency proceeding. Court agents appointed for conciliation proceedings may be appointed by the President of the Court at the request of the debtor in order to initiate a sale process when it is viewed as the best option to preserve the company's activities and prospects of recovery, to save jobs and pay its creditors.

This extension of conciliation proceedings allows for the formalization of pre-packaged sales and makes the opening of formal proceedings a technical step towards implementing the solution prepared during the conciliation proceedings. This can reduce insolvency proceedings to a few days or a few weeks at most, and therefore strongly reduce the harmful consequences that they can have on the economic environment of the company.

Similarly, if a unanimous agreement cannot be reached during conciliation proceedings, the power of the Court to enforce a majority agreement has been extended and strengthened. The accelerated financial safeguard proceeding introduced in 2009 has been supplemented by an accelerated safeguard procedure which can involve any type of creditors, including suppliers. The purpose of these accelerated safeguard procedures is to restructure the company's debt within a very short timeframe. These proceedings can be opened at the request of a debtor provided that a conciliation procedure is pending where at least a two third majority (in value) of financial creditors and bondholders are likely to approve the restructuring proposals prepared by the company and the Court appointed agent. Expedited safeguard procedures have been initiated where companies have been insolvent for less

than forty five days when the petition for conciliation was filed. This expedited procedure can last from one to three month and offers an opportunity to overcome the opposition of minority dissenting creditors while preserving the business, as much as possible. They are, from experience, a very convincing threat for stakeholders to reach an agreement during pre insolvency proceedings.

As you can see, provisions of the 2014 reform have brought changes and substantial improvements to French insolvency law in order to strengthen and facilitate out of Court pre-insolvency proceedings.

The second main aspect of the 2014 reform and of the recent law sponsored by our Minister for Economic Affairs aims at seeking a better balance between creditors and shareholders, especially in formal insolvency proceedings. Theoretically, creditors and shareholders have a natural interest to negotiate in the framework of pre-insolvency proceedings in order to limit value destruction for failing business entities. Creditors have an interest in avoiding the opening of formal insolvency proceedings where the Court may impose a long term rescheduling of their debt and even, in some cases, the sale of the company's assets, with the risk, for creditors, to lose much of their claims if the proceeds of the sale are too low to cover the liabilities. Similarly, shareholders have an interest in reaching a mutual agreement because the opening of insolvency proceedings can lead to a Court ordered sale of the company or its assets.

In practice, our experience at the CIRI shows that negotiations during pre-insolvency proceedings can be difficult, especially with shareholders. Shareholders normally bear the ultimate risk of the company and, in the event of financial difficulties, have a responsibility, either to recapitalize the company, to finance restructuring measures or alternatively, to transfer shares to third-party investors, often for a symbolic value. When shareholders are not willing to take their responsibilities during pre-insolvency negotiations, which can lead to inequitable solutions between stakeholders, the only way to overcome the obstacle was, until now, to organize a sale. This, however, is a very destructive outcome for all stakeholders and for the economy at large.

The new law has introduced provisions in the insolvency code to achieve a better balance between creditors and shareholders. They should encourage shareholders to accept mutual pre insolvency agreements more easily. In both safeguard and rehabilitation proceedings, any member of the class of financial institutions or the class of major trade creditors may now submit an alternative restructuring plan. This new right should encourage both the debtor and shareholders to reach a mutual agreement with creditors. Otherwise, the Court may accept the plan proposed by creditors to the detriment of shareholders.

In rehabilitation proceedings, the Court appointed administrator may, in a limited set of circumstances, vote on behalf of dissenting shareholders in order to encourage the conversion of debt into equity. This can happen once shareholders have voted against restoring the company's net equity or a share capital increase. In this case, the Court appointed administrator has the power to vote in favor of a recapitalization to restore the company's net equity, which can lead to the dilution of existing shareholders.

In addition to this new provision, the recent law sponsored by our Minister for Economic Affairs even grants the Court the power, in limited circumstances, to force shareholders to sell their shares during rehabilitation proceedings. This power is strictly limited and is a last resort solution but it offers a new option for companies to ensure the continuation of their business. If conditions are met, the Court may appoint an administrator to vote a share capital increase on behalf of a dissenting shareholders or even to transfer, in whole or in part, their shares to a third party investor, subject of course to a fair compensation determined by the Court.

As you can see, the law is pursuing the double objective of restructuring business at an early stage and of removing barriers to an effective restructuring of viable companies. Of course, the goal, here, is to maximize the total value to creditors, employees, owners and the economy as a whole and to increase the prospect of restructuring and therefore the number of viable businesses being rescued.

Some people have said that these reforms have not changed much and are too technical. It is clear that they are not a revolution of our system, but they are making progress in the right direction. While they introduce limited and technical evolutions, they participate in the broader objective of the government to facilitate the survival of viable businesses and to encourage investment in France. In that way, they are in line with the European Commission's 2014 recommendations on a new approach to business failure and insolvency, which aim at promoting restructuring frameworks enabling debtors to address their financial difficulties at an early stage, when their insolvency could be prevented and the continuation of their business assured. In that respect, the fact that the recent reforms have brought changes to French insolvency law in order to strengthen and facilitate out of Court pre-insolvency proceedings and to ensure a better balance between creditors and shareholders is, truly, a step forward.

Now this doesn't mean that there is no more work to do. Quite the contrary. This is why I would like to conclude my speech by highlighting the initiative of the European Commission to build a capital markets union. In that perspective, work is under way to include the question of insolvency law within the scope of the European Commission's action plan to encourage the development of a single market for capital. This initiative could be an opportunity to put forward best practices and the provisions of French law which are proving effective, particularly our pre-insolvency framework. Of course, it could also be an opportunity to compare our system with that of all the Member States, in order to tackle the main remaining obstacles to dealing with business insolvency. It is of course a stimulating perspective for us and we look forward to collecting any good idea that professionals such as yourselves will be willing to share with us.

First panel

Panelists :

Stephen Portsmouth, Managing Director, Société Générale, Paris (Moderator)

Arnaud Joubert, Managing Director, Rothschild, Paris

Cedric Boghanim, Principal, Apollo Management, London

Laurent Benshimon, Managing Director, Houlihan Lokey, Paris

Sophie Vermeille

Now it is time to welcome the first panel and the four distinguished panelists. They are going to comment on what we have discussed, past reforms, but also on the current practice in France. Our four panelists come from different backgrounds and they will share their experience with you for about an hour before taking questions.

Stephen Portsmouth

We are going to focus today on four areas of discussions in the context of a deal which was executed earlier this year, that of the successful restructuring of Latécoère in France, where a major deleveraging was achieved in a company with no major reference shareholder which meant that the discussion was purely based on economics. Our objective today is not to talk about this specific transaction in detail, but really to refer back to it, when discussing the major issues which we see as a result of this latest reform.

Allow me to introduce the members of our panel. On your right is Laurent Benshimon who is with Houlihan Lokey, and who, on this particular transaction, was advising Société Générale, the main lender. On my left is Cedric Boghanim, who works for Apollo Capital Management, one of the reference shareholders and non-bank lender, who came in the transaction and became a major shareholder as a result of the debt equity swap. Myself, I work for Société Générale, in the debt restructuring team, in the risk division. And on my right, I have Arnaud Joubert, who works for Rothschild, who was the advisor to the company.

Perhaps, Arnaud, before we kick off on the discussion, I would ask you to say a few words about the Latécoère case, a before and after picture basically, of what was actually achieved, because there is a lot of French bashing going on, about, you know, deals not being achieved in France and it would be quite useful for everybody to have a reminder of what the company looked like before the deal, and where we got to, after the deal was done.

Arnaud Joubert

All right, thank you, Steve. Latécoère is an aerospace sub contractor. It is a very old company that was set up at the beginning of the 20th century with a very strong brand name which, anecdotally, has contributed to keeping its market cap very high, because there were a lot of retail investors in the company, who thought that a company like Latécoère could never fail. That didn't help, because it didn't help the shareholders understand the situation in which the company really was. To cut a long story short, the reasons for the difficulties of the company is that there was a major shift in the way the aerospace industry has operated over the past ten years and the big manufacturers, like Boeing and Airbus have pushed down more and more CAPEX to their sub contractors, to manufacture parts of the airplanes they were producing. The difficulty, in this industry, is that profit is booked over a very long period of time, because aerospace programs can last fifteen, twenty or even twenty five years. And these companies make a profit only towards the end of the program, once the learning curve has been through and the level and number of products that are being produced finally enable the company to amortize its costs. The challenge is that the company never had a lot of equity, so they have invested a lot in new programs using debt but could not reap the benefits of their investments in the early years. The situation was becoming more and more tense. The company was not generating any cash flow. I am leaving aside a number of programs that the company probably mispriced or programs for which the company didn't have the right industrial tools to make a profit. The situation was also aggravated by the fact that the accounting in that industry is extremely difficult to understand for an outsider, because of the way EBITDA is booked. You book a profit, which is really the average profit that you will make on the program over twenty or twenty-five years. Therefore, it is not the real profit for the year. All of this to say that, the company, from the outside, with a relatively high share price, boosted by a strong brand name and apparent credit ratios that looked OK, didn't make it easy for stakeholders to understand the dire situation of the company. Only the management understood it because they had no cash, basically, and negative cash flows.

The transaction ended up being a massive deleveraging. The company had 280 million euros in debt and approximately 100 million euros of market capitalization, which, to be fair, should have been zero. The transaction consisted in reducing the debt, from 280 to 100 million euros and adding 100 million euros of equity into the company. Our big mantra to the creditors was, "two times a hundred". One hundred of debt and one hundred of new money. Which they ended up accepting. The form it took was a massive 280 million euro capital increase, split between a reserved capital increase for creditors and a rights issue which, ended up, surprisingly, being oversubscribed by shareholders. This resulted in creditors taking over approximately 37 % of the equity of the company, with two lead investors, Apollo and Monarch taking a big chunk of that, and, more importantly, taking over the governance of the company. As Steven said, the company was listed, had no real reference shareholders and therefore no real governance. Only independent directors, which, probably, also, didn't help the company understand how difficult its situation was.

One last comment, to reflect on what Thomas Revial and Steven said. A major issue, in the whole restructuring, was not really the negotiation with creditors and getting them to accept that they needed to reduce the debt to lower levels and to bring in new money. One of the major stumbling blocks was getting the shareholders to agree to the transaction. With such a dispersed pool of capital, with a lot of retail investors, who had lost a lot of money and didn't really understand or didn't really accept that shareholders stand at the bottom of the capital structure and should take the first losses, the major risk was, getting this deal approved in a shareholder's general meeting. This time around, just like in Belvédère, a similar,

well-known case from a few years back, we eventually managed to obtain the approval of two thirds of the shareholders in a shareholder meeting. Had we had a more coercive law to force the shareholders out, it would have been easier.

Stephen Portsmouth

Thank you Arnaud. Now, we really want to talk about the need for shareholders to accept dilution effectively. We have this expression in English, you know, "Getting Turkeys to vote for Christmas". And that's, unfortunately, what you have, or at least what you had, in France, both in principle and in practice. We have moved away from that a little bit but no doubt there is a more work to do on that.

We are going to look at three steps. First, the changes that we have seen over recent years, in France, in restructuring. Then, we will look at some of the issues in the reform itself. And finally, we will look ahead and discuss what we see going forward as potential changes that we could look at.

One of the points on Latécoère that is interesting is that a lot of the banks left the table relatively early on. And that raises the question, you know. Mark Twain was a US author who said that bankers are people who will typically lend you an umbrella when it's sunny and ask for it back as soon as it starts raining. So, I would like to turn to Cedric, because you are the non-banker here. Is that a fair quote ? And, more generally, perhaps, what do you see as the main advantage really, in restructuring processes, of having a non-bank lender around the table ?

Cedric Boghanim

I guess, I mean obviously, the fact that the bank exited, created the opportunity. So it is tough to say that they shouldn't do it, in the first place. But, that said, it was a mixed picture, considering you, as a bank was present and stayed in the process and we worked together as partners, throughout this process. So a very mixed picture, which, is worth noting here. When it comes to the attitude of the banks in general, there are, obviously, limits as to what they can do. Especially in this process which was highly complex due to the fact that the company is publicly traded. This further restricts the ability of certain actors to provide certain instruments, since the company is extremely visible. What we tried to do in this case, was to try and create a dialogue with the company early on and understand the tools that were needed in order to, basically, as you said, provide the liquidity that was needed and therefore, try to essentially fill the gaps, where banks could not be of any help. In this particular case, it obviously involved equity and acting, in a way, as a sponsor and reference shareholder, which, again, simply is not the role of certain banks and not something that they were willing to assume. I think that, in this particular case, that goes back to what is our role and what we can provide. The key to a successful investment is not only financial but also industrial. When it comes to the industrial aspect, it is necessary to have the appropriate governance. That was one of the key objectives ; trying to strike a balanced agreement and make sure that we would be able to, further down the line, implement the changes that were needed to, ultimately, make this a successful investment.

Stephen Portsmouth

Perhaps, Laurent, you could comment, looking, stepping back a little bit, at what has happened over the past few years. Have you seen a trend where banks, perhaps for the reasons that Cedric has outlined, have been reluctant to get involved in some of the governance issues ? Have been reluctant to sell ? Have you seen a bigger trend in French banks in particular, exiting transactions like this ? What is your view ?

Laurent Benshimon

I think what we have seen in the past two to three years and compared to what we had at the very beginning of the cycle, is an increasing trend of banks, and French banks in particular, selling their credit in the secondary market. The drivers for that have really been two-fold. First, Basel III, which has increased the constraints on the balance-sheet of the banks, but also the rise of a secondary market for French credit which has become more liquid and more transparent. This, in turn, has facilitated the entry of secondary buyers like Cedric and resulted in more attractive prices for banks to sell.

All in all, the impact on the French market has been quite positive with the number of debt-to-equity swap transactions significantly increasing over the past two to three years, probably accounting for more than two thirds of the total number of deals completed over the period. If you compare that to four or five years ago or to the beginning of the cycle, I think it was almost a hundred percent of the deals that took the form of amend-and-extend, simply because the banks didn't sell and because the banks cannot ascribe fair value to equity either, their only way to maximize their recoveries was to push maturities down the line.

For borrowers, this has meant a de-levered balance-sheet, new money, not only for liquidity purposes but also for capital expenditures and growth, as well as a change of control with old shareholders exiting and new players able and willing assuming the role of governance.

Stephen Portsmouth

Oftentimes, in the past, we found ourselves trying to define an answer to the problem, before really having defined what the problem is. That is certainly something, which I have seen in the years that I have been working in French restructuring. However, more and more now we are seeing, right from the very beginning, the need for all stakeholders, whether they are the State, or the lenders, or the equity or the different classes of lenders, a need to "negotiate" in inverted commas, a business plan, you know. What is the situation of the company ? What is the business plan going forward ? Is that view shared ? Have you seen a similar move away from basically the "*Village Gaulois*" type of situation, right from day one ? Where we now have this kind of first phase of negotiations, to study the actual position of the company with external advisors and informed investors before having the second phase of negotiation ?

Laurent Benshimon

I think those two phases have always existed but I think they have been of a different nature. In the context of a syndicate dealing primarily with historical lenders, the review and the diagnosis of the company is almost a technical exercise required for internal approval. This is not because banks and CLOs do not need to understand the company. That's because banks and CLOs have been lenders to the company for a long time, so they already understand it. In a syndicate where you have new players, that is, new buyers of the debt, the due diligence phase is by contrast much more thorough and deep,

with more interaction between the new investors and the management because they don't know the company as well as the previous lenders obviously, but also because very often, they are making a new investment in new money, sometimes for a very significant amount.

Stephen Portsmouth

Arnaud, do you have any comment on that particular point ? From the company's perspective ? You oftentimes have been advising companies where sharing the information is, obviously, a very sensitive point, isn't it ?

Arnaud Joubert

I agree with Laurent's comments. There are a number of difficulties indeed, when you are on the company's side, and, I think, more importantly, for listed companies. It is very difficult for a listed company to share any of its prospects with future equity owners because it will have to cleanse that investor vis-à-vis the rest of the market and it is very unusual for a listed company to publish a business plan. So there is always a phase in the negotiations discussing which level of detail will be granted to the subpar investor and future equity owner and therefore what exactly will be cleansed to the broader market.

I think there is also another difficulty. In some instances, the business plan is, people spend hours, and nights, and weeks, negotiating something that nobody really understands and nobody really controls. I think the worst sector for this is retail. Vivarte was a perfect example, where months were spent on a business plan which ended up being dropped. It is a waste of time.

Stephen Portsmouth

Yes, at some point, you have to call time out and move on.

Arnaud Joubert

At some point the investors need to form their own view of what the business plan is, and then the company may have a different business plan, but you have to get on with the restructuring negotiations.

Stephen Portsmouth

And one final point from me on the changes over recent years. One of the key issues in restructurings, wherever you are, is the amount of time that it takes. Because, obviously the longer the company is in distress, the more fragile it is. And the more the objectives that Thomas Revial was talking about, in terms of job creation and in terms of job saving and value creation generally, are at risk. Do you find that the time taken to resolve French restructurings has got better or worse ? I ask this question with an interesting angle because I believe that I am in a position to compare the situation in France with that of other countries as I look at non-French corporates as well. It does seem that it takes an awful lot of time from the moment when you first get involved. And perhaps you could comment on the impact that this has, I mean, the time it takes, the impact it has on the attractiveness of France as a market ? Thomas Revial mentioned that it was one of the key objectives of this new law, trying to make France more attractive for investors.

Cedric Boghanim

That is a big question. Thank you, Steve. To begin with, from a purely financial perspective, and ultimately, it always comes down to liquidity. In other words, as long as the creditors have time and there is no real liquidity threat, they will take the time. That is true to a certain extent, but really, in my experience, people come around the table and find a solution when there is a real liquidity threat. So that's a first point to note and Latécoère was no exception. The second aspect to mention is that the concept of DIP financing (Debtor In Possession) still has some way to go to progress in France. What we have seen in this instance is that it is most of the time very difficult or impossible to implement, depending on the structure obviously, but most of the time, it's a tool that is not as widely used and available as in other jurisdictions and certainly something we can work on and reflect. The key point to keep in mind is that the problem will not go away if you do not have the proper tools. In other words, in most insolvency procedures, there is a liquidity need that needs to be addressed. If we do not have these tools, what we have seen in many instances is that, the company will find tricks to "create" liquidity. This can have an impact for the government or other actors who all need to play with the hand that each has been given around the table. This could be dealt with in a more institutionalized manner, if we had the proper tools.

Stephen Portsmouth

May I just interrupt because you mentioned the word DIP financing and perhaps people in the room aren't familiar with the US terminology of Debtor In Possession, *i.e.* allowing an investor or a lender, in an insolvency situation, to lend money to a company which is already in bankruptcy proceedings in the knowledge that that money will be super senior. Thomas Revial mentioned earlier that measures exist in France, in theory, to achieve this, which is the super seniority available in conciliation proceedings. In practice of course, that doesn't always work despite the reform in 2014. Therefore the lender can still get completely crammed down, in practice if there is an asset sale (*plan de cession*) of the company. I think what Cedric is alluding to, is a need to encourage, or render more attractive, the lending of money to companies who are in distress, because, as you know, sadly, banks are not a very good source of liquidity to companies who are in difficulty. And that's perhaps something, which we could see more of.

Arnaud Joubert

Sorry, just a comment on the time that it takes. I believe that, in France we like to indulge in French bashing. But, to be honest, the time that it takes now to do restructurings in France is not worse than anywhere else, at least from what I have seen. The APCOA restructuring in Germany took over one year and a half. I could mention a Ukrainian deal where we still do not have a standstill in place. It has been negotiated for eight months. To be honest, I believe that the larger deals and the deals where banks sell their stakes to people like Cedric, get done much faster because these funds know that they need to work fast. They are structured to work fast and it is much easier to strike deals. The deals that don't get done fast are the smaller deals, where, a lot of French banks are involved, where it is handled by the "*affaires spéciales*" department and you spend hours negotiating silly points. That is very destructive for the company. I believe that anything that we can continue to do in order to attract investors, change the law and make it more appealing and attractive, especially in terms of DIP financing, will make deals go much faster for hedge funds and distressed credit funds.

Cedric Boghanim

Yes, I would agree with that. I do not believe that time is necessarily the biggest issue. To come back to the issue of super senior and new money. One point that I find interesting in France is that, it is probably one of the only countries, if not the only country, where I have seen the super senior part being the most expensive. It is meant to be the lowest risk part of the capital structure yet we have seen a lot of restructurings where we end up with super senior new money being like, double digit, so, ten percent plus yield, which is, obviously very expensive for the company and makes no sense economically because it turns out to be more expensive than the regular senior debt. I believe this is just a point to keep in mind and probably the best example that, actually, there is an issue since there is a disconnect between what the terms are saying economically and what these facilities should be contractually.

Stephen Portsmouth

You are saying that, in fact, the money that is being put in as super senior is, in effect, economically, equity. We will give you an equity type return, in effect ?

Cedric Boghanim

Yes, at least that's what the terms are, reflecting. Yes.

Stephen Portsmouth

It's interesting that we have now slipped into the second point of our discussion, which is to look at issues that we see with the reforms and areas for improvement. On the Latécoère case, what I find interesting is that we emerged from the process with a very simple capital structure. You have debt and you have equity. That's it. Nice and simple structures that debt can trade at par or as close as possible to par. With a nice clean balance sheet going forward, hopefully, to help the company grow. Laurent, you've had a lot of experience in LBOs and perhaps private companies. Could you react on what Cedric just said about the way new money is put in and injected ? Is there a link, between, the ability to cram down shareholders, if you like, and impose dilution, and the simplicity of the capital structure, when you come out of a restructuring ?

Laurent Benshimon

I would say yes. I think if you have a restructuring framework whereby you have the ability to leave the right amount of debt on the balance sheet, which ultimately, post restructuring will leave enough equity value, then, in principle, a rational investor should have no issue investing new money under the form of equity. As a matter of fact, if he is comfortable with the business plan, the value and the capital structure, he should be more inclined to invest under the form of equity because he will achieve a better return than if he were investing in the form of debt instruments.

Now what we have seen over the past three years, almost exclusively with the exception perhaps of Latécoère, is new money structured under the form of super senior debt. And as Cedric mentioned earlier, that super senior debt often has a yield which is equity yield as opposed to super senior yield. I think that one of the reasons for this is that even if we have more transactions taking the form of debt-to-equity swaps in France, they still remain more levered than what they should be, with a leverage that is often at 6.0x to 6.5x when it should really be at no more than 3.5x to 4.5x for an enterprise value that is probably in a range not exceeding 6.0x to 6.5x at best, upon closing.

How can you improve that ? One way is to improve visibility on how to address holdouts. We talked about shareholders earlier but I think we didn't speak about junior creditors who are out of the money and, because they vote in a separate committee, can absolutely block your process. For instance, if you have mezzanine debt structured under the form of bonds and senior debt under the form of loans, you will need to go and consult the mezzanine debt holders the same way as you will need to go and consult the shareholders. This not only increases time for deal completion, even if, at the end of the day, we are not the worst pupils in Europe, but also, and perhaps more importantly, it increases the cost of doing a restructuring for the parties that are around the table. This ultimately incentivizes in-the-money stakeholders to reinstate more debt on the balance sheet in order to reduce value leakage to out-the-money stakeholders and/or to increase protection on the downside given the higher cost in France of obtaining all the required consents to complete the restructuring. This, in turn, often leaves little equity value post-deal and results in new money injected under the form of super senior debt rather than equity.

Stephen Portsmouth

Yes, thanks. This touches upon the notion of value, which is another issue, which I wanted to raise in the context of this restructuring law, these reforms. You know, in the US and increasingly in Northern Europe, the notion of value is very important. In any restructuring. What we have failed to see here, is the introduction of the concept of value, of enterprise value, as a key factor to decide who should be able to make decisions on what happens, who should retain control and who should lose it. I don't know how to quite phrase my question other than to say, do you all agree that this is an important issues and what is the best way to resolve it going forward ? Perhaps Arnaud, I can turn to you ?

Arnaud Joubert

I agree that French law does not take value into account in the same way as UK law. Yet at the same time, I am still very surprised that you can disenfranchise creditors under UK law at the lowest point in time for the enterprise value of the company. I think the first case was IMO Car Wash, where the mezzanine lenders were not even given the ability to vote and the company rebounded quite quickly thereafter. So I am not sure that having as strict an assessment of the value as under UK law is the right approach. In a way, but I am not sure this has been treated yet, it seems that the way the French *administrateur judiciaire* can decide to split up the votes, between the different classes of creditors, may be a way of trying to put some balance into who can vote and who cannot. I think the major issue, which is the one that Laurent touched upon, is that French law distinguishes bank creditors from bond creditors and does not distinguish between senior lenders and junior lenders. It would make much more sense to stop having this crazy split between bonds and banks and have different classes of creditors according to ranking, because then you could probably give a lower weighing to junior creditors in any vote. That would make things much easier and perhaps approach enterprise value, in a way.

Stephen Portsmouth

I am not sure that I agree with you on the valuation point, Arnaud. Because you can look at the IMO Car Wash case and others and think, oh yes, they recovered really quickly. But the outcome of a restructuring, or the outcome of any decision, is not necessarily a very good measure of how risky that decision was at the time. From my perspective, you value a business at a point in time and you take into account the future prospects through the discount rate that you apply to its cash flows. But I take your point, that tendency is perhaps for one class of stakeholders to profit at the expense of another unduly. Cedric, I would appreciate your comments on that point of valuation and some extra color please on how important this is for somebody coming in from the outside.

Cedric Boghanim

Sure, I guess the point on valuation, essentially, the underlying issue, really, is to have a predictable framework for the actors who come to France. For some of us, who invest in France regularly, we understand some of the principles that will be established. But I would say that for the occasional investor, generally speaking, there is an issue if we don't have a valuation-based framework that can be used as a reference and essentially give enough predictability to make France a creditor friendly jurisdiction. I think, ultimately, to go back to Arnaud's point, do we need to go towards a UK, pure valuation-based system ? I don't know. I guess there are still some improvements to be made from where we are today, that is undeniable. I think what we need to keep in mind, and where we need to go, is to have a much more pragmatic approach, where we cannot stay indefinitely in situations where, you have people around the table who are ready to provide a solution, which usually comes down to providing liquidity for the company and give it a chance to survive and restructure, who are held out of the company by stakeholders who, quite simply, are out of the money. That's the basic issue that we need to deal with. Whether we need pure valuation-based tools where banks essentially provide fairness opinions and say, this class of creditors or shareholders is totally out of the money and therefore is not allowed to vote or whether we simply restrict the influence that they have in the process, I do not know. But I think we should start moving in this direction in order to shorten the process. We are usually stuck in for a number of months, if not years in certain cases. We should allow the company to move on and turn the page.

Stephen Portsmouth

Thanks Cedric. Laurent, would you like to add something to this question of valuation from the point of view of an investment bank or a restructuring.

Laurent Benshimon

It is good for advisors, that much is certain. (Laughter) But, generally speaking, I hear what Arnaud says. I am not sure that the UK system is necessarily the best one. There are some good things in the UK system. There are also some very good things in the French system. The concept of value has definitely been introduced by market participants and practitioners including lenders, be they par lenders or new lenders, even shareholders and also judicial administrators who very early on seek to understand where is the value of the company, who is an in-the-money stakeholder and who is not. Now, surely, it would help to have a binding mechanism within the law that effectively puts that valuation recognition in practice to be able to force a transaction on an out-of-the-money stakeholder who would be blocking or keeping a restructuring process hostage.

Ultimately, we get deals done, as you mentioned earlier. I think that it still takes longer than it should and I that it is more expensive from the perspective of in-the-money stakeholders. For instance, getting the consent of a shareholder or an out-of-the-money junior creditor in France is probably two to three times more expensive than what you would pay in the UK or in the US to obtain their consent. If we can get this extra value back to the company or in-the-money creditors or new players injecting new money, we would reduce the new money yield that we were discussing earlier. That would be a good way forward, I think.

Stephen Portsmouth

I think we have wrapped up on the main points I wanted to raise on the process itself. We talked about confidentiality. We talked about DIP financing. We talked about the need to look at value. Perhaps it's now time to look at where we are going forward. What we see as major trends going forward in France and an opportunity to think about what changes, if any, we see as being most important for us in the next cycle. If I may ask you, Arnaud, to kick off on that ? What do you see as being the new issues arising, and perhaps, I mean, my angle is the prevalence, in recent years, of bond financing which has helped kick the can down the road, in many ways. These massive liquidities have helped companies. But it has, also, perhaps, deferred problems, which, haven't yet been solved, and companies still owe too much debt. It is just a longer tenure, perhaps. What is your view on the restructuring of the debt of companies which have large bond issues ?

Arnaud Joubert

I agree, it is probably going to be a big trend over the next few years. I think that, Laurent, you would agree. The restructurings involving only private-equity are probably behind us. There may be a new wave, but in the short term, I think we will all see more companies going for restructurings, which will be very, very complex, compared to the wave that we have seen. Either because these companies are listed or because they are owned by entrepreneurs and not by professional private equity funds. And also because they are, more and more, financed by bonds. The big issue when restructuring companies with bonds is that, first of all, it is more difficult to identify who are the people you need to speak to. You do not have a register, where you know exactly who your lenders are. Second, the whole cleansing process and the fact that bondholders do not want to be restricted during the negotiations. So, you end up negotiating with someone who represents bondholders and tries to cut a deal on behalf of people that he is not talking to or at least not telling the exact state of the company and the state of the negotiations. This makes negotiations more complex and also opens a whole new point for discussions, including the cleansing process. Having said that, bonds are probably more flexible, during restructurings, when they are not set up with a single bond, as in Belvédère, where you had an intermediary and then all the bondholders sitting behind. This makes things even more complex. When bondholders are direct bondholders, there are numerous ways of getting these bonds to amend their terms, including consent solicitations. Votes, which, sometimes, do not require a two-third majority, as for the bank debt, but only a fifty per cent majority. So there is a wide range of different ways of dealing with it. But, I repeat, the most important problem is that

bondholders can be treated as a separate class from bank creditors even if they are more senior than the banks. And even if there is no reason to treat them differently from bank creditors. Therefore, even in a structure where you have essentially bonds and a very small share of banks, you cannot cram down the banks. Even if they are *pari passu* with bonds, on the basis that you have two different committees in both the *sauvegarde* or the *redressement judiciaire* proceedings.

Stephen Portsmouth

We are circling back to the problem you were discussing earlier.

Arnaud Joubert

One additional point, which is absolutely crazy, in this reform. Banks can, in a *sauvegarde* or a *redressement judiciaire*, come up with their own restructuring plan, in competition with the management's restructuring plan. Whereas bond holders are not entitled to do so. There is no reason for preventing bondholders to do the same as banks. Especially if they are creditors ranking at the same rank or even a more senior ranking than the banks.

Stephen Portsmouth

It is going to be an interesting situation when you have minority banks for security getting crammed down by other types of creditors and banks cannot take that into account at the present time.

Arnaud Joubert

Exactly.

Stephen Portsmouth

Any comments from other members of the panel on that point ?

Cedric Boghanim

Well, I think Arnaud accurately identified the issue. What I would add is that, it's a key priority to try and find a way to get these actors together and be able to work together, since, frankly, as it has been said, the pipeline, if I can say, of companies that are potentially up for restructuring is much more geared towards bond structures than LBOs like we have seen in the past.

Laurent Benshimon

I think I would agree with all of that. I would just add maybe one more thing. Compared to restructurings which are effectively around bank debt, with bonds, given the nature of the instrument, we are likely to see even more trading and an increasing entry of hedge funds into capital structures. This, as we saw earlier, is not necessarily a bad thing from the perspective of the borrower.

Stephen Portsmouth

I had a reaction in my head about what Thomas Revial was saying earlier about the focus in France, historically, on pre-insolvency discussions and I have two points to make about that. One is that, the behavior of people around the table in a pre-insolvency situation, whether it is in a French *conciliation* or an English sitting-around, having tea amongst creditors – which is, basically, the same kind of idea – the behavior of those people around that table will be impacted by what happens down the stream, right ? One of your predecessors in the job, Fanny Lettier, said, when the *sauvegarde financière accelérée* was introduced, that the measure of success of that legislation would be inversely proportional to the number of times it was used, which is a neat way of explaining the point. So, yes, we all agree, it is best to focus on out-of-Court restructurings, but let's not forget what happens downstream. Because that is really the way to keep the focus on the quality of pre insolvency discussions. The other reaction I had to that, and we were discussing this with the group, before we came on, is, what is the actual intention of an insolvency law ? Is it to preserve the status quo and allow extensions of debt and preserve jobs, whatever that means ? Nobody has ever come up with a proper definition of that, from my perspective. Is that the objective ? Or is the objective to help the process of creative destruction, where we actually take the loss and get the company moving forward with a healthy competitive balance sheet. One of the interesting points I noticed from one of the slides that were presented by Anna Boata who introduced today's conference was that France had one of the highest DSO rate (daily sales outstanding) in Europe. This highlighted the French reliance on trade creditors to finance companies, compared to Germany. Why is France not so attractive to finance companies or to banks ? This is one of the issues that *Droit & Croissance* is trying to put on the agenda. Could the structure of our law have something to do with that ? That was the key question I had.

Are there any other points that you want to mention, perhaps as we wrap up ? Looking back over our discussion. The three most important points you would see as being key, moving forward ? What changes would you like to see in the French setup ? Cedric, perhaps I can ask you to just give us your thoughts, one more time ?

Cedric Boghanim

Reflecting on what has been said, the recognition that wider cramdown tools are required, one that we can use earlier in the process, in one form or another, is going to be key to keep a healthy restructuring process going forward. That would be one. The second is the unconditional recognition of priority within the capital structure. Because, again, whether it is secured versus unsecured, or junior versus senior, we are more of an exception than anything else, in France, today. That needs to be clearly addressed, in order to make progress. The final and related point is obviously valuation. But that is more of the nature of an instrument than anything else. The two key principles are these.

Laurent Benshimon

From my standpoint, there have been a lot of new and good developments in the French market, including in the nature of the deals that have taken place over the past two to three years. In my opinion, two issues remain and need to be addressed going forward. How to effectively and efficiently deal with out-of-the-money stakeholders, be they shareholders or junior creditors, in a manner that is both quick and cost effective.

Stephen Portsmouth

Arnaud, is there anything you would like to add to wrap up ?

Arnaud Joubert

On my wish list, maybe one point would be trying to find a way to deal with listed companies. Because the restructurings of

listed companies have not been many and each time we have managed to get the required majority, it was never very satisfactory. On a more detailed point than Cedric or Laurent, regarding the cramdown of junior creditors and shareholders for listed companies specifically, it would make things much easier if at least the voting thresholds or the quorum were reduced, to make votes in an EGM much more predictable.

Cedric Boghanim

The way we approach this is to have, either a chief restructuring officer ("CRO") or other governance items, like a single-tier board structure. These were more condition precedent to the deal than things that we started discussing on day one. That said, I would just add that, obviously, the company had a lot of advisers around the table. Some are not here today but we obviously received a lot of support.

Arnaud Joubert

Before I can reply to your second question. If I can provide the company's view on your first question. I would say, thank God that French corporate law provides for a minimum of protection and, that, as a listed company, the only change in governance that you can implement must go through a shareholder meeting and, thank God, that your creditors are not entitled to sit on your board. It is true that in the Latécoère case, there could have been a CRO but, the governance worked quite well, during that whole phase. Even if it was, at times, difficult for management, who had not gone through this before. I don't think that any change should be made to the law. On your second point. How much was left ? What was the price that was paid by the people taking over, to the shareholders, in order to get the deal agreed ? We came up with this list of precedents to Cedric and Monarch and the other creditors and, what you find out, to be schematic, is that, in French restructurings of listed companies, you have to leave, when the shareholder is absolutely out of the money, between ten and fifteen percent of the upside to the shareholders to obtain their approval. It was the case for Eurotunnel, it was the case for Belvédère and it was the case for Latécoère. I think it was Laurent who said that it is two to three times more expensive to obtain shareholder approval in France than in any other jurisdiction. I must say, that, a hidden price, which is less easy to understand, is the fact that you cannot impose a debt-for-equity swap, where, typically, the creditors would have taken over more than forty seven percent of the equity. The hidden price is that you have to offer to all the shareholders the ability to participate in the recapitalization plan, through a rights issue, rather than a reserved capital increase. And I'm sure that Cedric would have preferred to be able to convert much more of his debt into equity and get a much bigger stake but the way to get the shareholders to approve the deal is to offer them the opportunity to invest on the same terms as the creditors in the rights issue. Hence the oversubscription of the rights issue in this case.

Questions from the audience

Jean-Luc Rensac, Credit Agricole CIB

I have two comments and one question. My first comment is about the DIP financing. I think that it is surprising to see such a high spread but in my view this is just because not all of the lenders wanted to participate. Those who do not want to participate have to be crammed down, one way or the other. If all lenders had participated then prices would have gone down to a logical level. That was my first comment.

My second comment is about the equity. We, at Credit Agricole CIB, were happy to introduce Apollo to the structure, because it proved to be pretty difficult to make this restructuring with only French banks at the table. That is my second comment.

My question now. It was probably difficult to find the right way to make this reserved capital increase, but, my feeling is that the distressed funds are helped by the price they pay for the debt. Because, at the end of the day, more or less, if my recollection is correct about the Latécoère, during the capital increase, Apollo didn't care at all about the price they had to pay for the capital increase on your side. They paid eight, nine, but it might have been ten, twelve. I think they were more interested in the discount that they received by buying debt from the bank, weren't they ?

Arnaud Joubert

Jean-Luc, I'm sorry to disagree. I think the big opportunity for a company that is in such a difficult situation is that there are people accepting to underwrite additional capital and to underwrite the business plan of the company. And it is not going to be banks putting more capital into these companies. It has to be people who can take additional risks and if they can make a lot of money out of it, then it is much better, because then they are attracted to the deal. Had they not bought the debt at a discount, I can promise you, because discussions were very intense, that the price of the reserved capital increase and of the rights issue would have been very different. The dilution of the shareholders would have been different. This means that if we go back to the previous question, we probably would not have had a deal at all, because the shareholders would have rejected it.

Stephen Portsmouth

I would like to comment on that as well, Jean-Luc. I guess, we are all involved in these situations, where pricing the company, valuing the company, well, anybody can do that, I suppose. Valuing the company and therefore the debt. But you also have to value the process. Put a price on how long it is going to take, for the situation to be resolved. And the discount includes an element for that as well, I suppose. And it circles back to what we were saying before about the predictability of the system in France. The more predictable it is, the less the discount, for the banks. If it is a highly risky process then you would expect the buyer to get a fairer return by getting a bigger discount.

Cedric Boghanim

Just to close on this point. I think it is a risk and return discussion. As Arnaud said, it is not about the price we pay for the debt or another instrument. Ultimately this would mean looking at things in isolation. And what we are trying to do, is try and get comfortable with a certain level of risk that would ultimately imply a certain return for us. If we get comfortable, that would mean we can participate. If it is necessary to buy the debt at a certain discount, then it's just what is required for us to get involved, looking at it differently. If we had not bought at a discount we probably would not have been able to underwrite, because it is part of the overall price that we ultimately pay for this risk.

Serge Dominguez, BNP Paribas

Could you say a word about the role played by the *mandataire ad hoc*, the *conciliateur*. What do you expect from them as

advisors or investors ? What could they do better ? Do you think that what they do is fine as it is ?

Stephen Portsmouth

From my perspective, whether it is called a *conciliateur*, a *mandataire ad hoc,* or whether it is called PriceWaterhouse-Coopers, because they have been appointed by banks to assist the process, or even as Thomas Revial said before whether it's a representative of the French government, as sometimes happens in France, what is important is that you have someone who is there to moderate. It is always useful. I am moderating here so that nobody is out there at the back, throwing paper planes, you know. You need to get somebody who is around to make the conversation helpful and my perception is, that although I started off with a very negative perception as an Englishman in France, about the whole idea of conciliation and all that kind of thing, my general view at Société Générale is that they can be helpful. In the same way that PriceWaterhouseCoopers advisers can be helpful. To get different stakeholders, different points of view to focus on the key issues, which are, the company itself and the unleveraged cash flows of the company. Is there anything you want to say to that ?

Arnaud Joubert

I think it is really dependent on the situation. In some instances, it is less required. Because everybody is acting or behaving like a grown-up. Trying to find the best solution for the company. In some instances, it is very useful to have an independent third party who is there, as Thomas said, just to make sure that everybody shares the pain and makes equitable efforts. I think the role of the *mandataire ad hoc* and the *conciliateur* was very useful at the beginning of the crisis in 08, 09 and 10, because all the Anglo-Saxon creditors were afraid of this Court appointed persons and respected them. I think the issue we are having now is that most of the Anglo-Saxon creditors do not really respect them anymore. I am not even talking about the "*affaires spéciales*" departments where it feels like you are in a classroom, with a lot of children throwing darts at the teacher. It is really shocking. I think what may help is to slightly increase the powers of these *mandataires ad hoc* or *conciliateur*. I don't know in which directions, maybe in their reporting to the Court, the behavior of creditors or shareholders who are not behaving fairly. If they could at least have a way to get some more grip on the process, it would definitely be very helpful in some instances.

Cedric Boghanim

Well, I would disagree. I think that, ultimately, the role has been described by Thomas Revial as a mediator, as someone who is unbiased. That's what the basis should be. I think what the *mandataire* could be doing more of, generally speaking, is being involved, in one form or another. In other words, make sure that they have a role in the process, from start to finish. Now, does it necessarily mean that we need to increase the role and the power of the mediator ? I think it would add complexity and therefore I would question it. But, generally speaking, and to answer the question, it is a useful role and it works. It provides and adds value, clearly, by mediating a process which, sometimes, can be extremely challenging. I would simply question the need to further change the position of the *mandataire* today.

Second roundtable

A Chapter 11 in Continental Europe ? Past reforms in Spain and Italy Assessment of the EU strategy on insolvency law

- Does the restructuring community still need more efficient insolvency laws in Continental Europe ?
- What can we learn from the last legal developments and the current trend in Italy and Spain ?
- Do France, Italy and Spain follow the same path ?

KEYNOTE SPEAKER

Michael Shotter, Head of EU Commission's Civil Justice Policy Unit in the European Commission's DG Justice & Consumers

Capital Markets Union : Investing in a modern insolvency and restructuring framework across the EU

Introduction by Sophie Vermeille

I am very happy to see that the European Union is now more and more focused on insolvency law. Until very recently, the EU Commission has been much more focused on the banking industry, especially with the introduction of the bail in tool, which is a very interesting concept for us because, as you may not be aware, the bail in introduced by the EU Commission now authorizes the cramdown of shareholders as well as creditors of banks. I was always wondering why do the EU institutions focus only on banks and why do they not do anything for corporates.

I am therefore very happy that things are now changing and delighted that Michael Shotter has agreed to tell us a bit more today about what will be happening in the future and share his views about the importance of this new focus for the EU Commission.

Thank you

Michael Shotter

Thank you very much, Sophie.

Ladies and Gentlemen.

As Sophie mentioned, my task, I think, is to give a bit of explanation about some of the developments in Brussels and also some of the emerging thinking, because there has been quite a lot going on.

First of all, let me start with the good news. After two and a half years of intense negotiations between co-legislators, the revised insolvency regulation has been adopted. It is now published and is in force. It will enter into application in June 2017.

The revised regulation has brought a number of useful novelties. It now also covers preventive insolvency proceedings with the aim of rescuing businesses, so its scope has been enlarged. It also covers a larger range of personal insolvency proceedings. But apart from the enlarged scope it also contains some useful clarifications on the jurisdiction rules where, if I can put it this way, it provides some useful tweaking of these rules, in particular, by clarifying, in the recitals, the definition or the application of the COMI (Center Of Main Interest) principle.

It has also established a system of inter connected insolvency registers across the European Union to increase transparency on pending insolvencies. This interconnection will kick in as of June 2019. These rules are pretty tangible and useful things. It also, for the first time, introduces some arrangements for coordinating group insolvency proceedings in the cross border context.

All in all, this new recast insolvency regulation, provides the Union with a more modern, up to date set of rules for covering cross border insolvency proceedings. That is very good news for all of us as it is a very important instrument, as has been seen over the last years. I think it will now be even more relevant.

This is not to say that we do not need to do more. Of course we need to do more. We need to do a lot more to improve the situation on the ground. That is why, given that the insolvency regulation has its focus on jurisdiction, applicable law and recognition issues, important as they are, we need, I think, to move a step further into the area of substantive insolvency law where certainly there is work to be done to resolve, I think, the issue of the patchwork of legal rules that we find across member states.

Now, I don't have to remind you that in the wake of the economic crisis, there has been a surge of non-performing loans in all member states, the number of bankruptcies has soared across the EU and although that trend has been stabilizing, the number of foreclosures is still higher than in pre-crisis times.

It should also be borne in mind that a significant number of these non-performing loans have not been cleared and are still weighing down on balance sheets and on the economy.

Now this burdens the economy, reducing the creditworthiness of businesses and the availability of loans, in particular to small and medium size enterprises. We should also keep in mind that entrepreneurs and consumers still suffer from the stigma of failure associated with bankruptcy for far too long, across the European Union. We should ask ourselves whether all this makes sense. Whether the current insolvency systems are the best approach to help entrepreneurs get back on their feet.

We should ask ourselves whether the current systems do what they should to help build a dynamic economy across the European Union. All this helps explain the Commission's interest, I think, in this subject, to come back to what Sophie said at the beginning, why we are coming to this subject now from the point of view of the companies.

It is because we need to think very carefully and seriously about modernizing the substantive legal framework for insolvency across the European Union as the next step following the recast of the insolvency regulation.

When we discuss and think about this, we obviously should look beyond Europe as well. I notice that this section of the discussions has a reference to Chapter 11, entitled "Should we have a Chapter 11 for continental Europe ?". This shows that this is being well taken on board by the organizers of today's discussion. The US is indeed an interesting point of reference. Bearing in mind also, let's not forget that, in the US, for many years, bankruptcy has been regulated through federal regulation, facilitating recovery and a second chance. Even though the US was, initially, I think, worse hit by the economic crisis, actually, what we have seen, is that it was more efficient than the European Union, in many respects, in reducing the number of non-performing loans.

For natural persons in the United States, the average discharge period, it should be borne in mind, is less than one year. Whilst in the European Union, many member states have a discharge period of between five and seven years. There is quite a lot of evidence showing that shorter discharge period allowed US households to recover more quickly from the crisis. Of course, let's not forget also that the United States is in the process of reviewing its own system as well and that the American Bankruptcy Institute has just come out with a report and various recommendations. I think it is right that we look whether we have sufficiently modern systems in place. Even the United States is doing that and I think one of the concerns in the United States is whether their Chapter 11 does enough for the mainstream, smaller cases rather than just the big and complicated cases. If they are thinking about reforming their system, it is right that we should be thinking about ours as well.

Indeed this is exactly what the Juncker Commission is in the process of doing. Smart and efficient insolvency rules are key to boosting investment, jobs and growth. This is a key priority for President Juncker's Commission. It was underlined in the President's State of the Union speech in September and we see that it is not just a matter that has caught the attention of one President. It has also caught the attention of five Presidents in the guise of the Five President's Report on completing Europe's economic and monetary union, published in the summer. This refers to the importance of addressing bottlenecks, such as insolvency, thereby contributing to the wider financial union and stabilization of the functioning of the economic and monetary union.

Given all the importance that is obviously attached at the high political level there has been some follow up in the autumn. Two recent developments since the Commission came back, after the summer. The Commission's work on insolvency is now reflected in two particular flagship initiatives.

The establishment of a Capital Markets Union, which was adopted in September, and also the initiative adopted last week to upgrade the single market in the form of the "single market strategy".

Let me elaborate a little bit on, first of all, the Capital Markets Union. Why is this relevant in the context of a Capital Markets Union ? Well, I think there is a good reason. It is because investors will look at their rights and their potential losses in the event of financial difficulties or the insolvency of the debtor. Twenty-eight different insolvency regimes in the European Union make this assessment difficult and costly. Insolvency law in general, and restructuring procedures in particular, are not only a matter to consider for a company winding up its activity. Insolvency rules are important throu-

ghout the lifetime of the business as they inform investment decisions upstream and therefore affect businesses access to funding. This represents a challenge, especially for SMEs. It is no surprise, then, that when the Commission carried out a consultation in the spring of last year, respondents to the Capital Market Union initial green paper, banks, central banks, investment institutions and businesses questioned during the Capital Market Union consultation, stressed the close links between insolvency law and improving investment conditions in Europe. This connection was underlined, not surprisingly. Whilst there are many ideas coming back to us as to where the focus should be many are underlining how complex this initiative undertaken by the Commission would inevitably be, the connection between the clarity for investment decisions and cross border investment actually being carried out was clear.

In terms of the single market strategy, the Commission underlined its interest in this issue of insolvency reform from a slightly different angle. Less from the investment angle and more from the perspective of the creation of an entrepreneurial culture. It underlined how the effects of bankruptcy can have a deterrent effect on entrepreneurial activity in this single market strategy. The fear of social stigma, the legal consequences and the inability to pay off debts is stronger in Europe than in other parts of the world. Bona fide entrepreneurs need to know that they will have a second chance as a way of helping start-ups and encouraging entrepreneurs to try new ideas.

In answer to both these challenges, the Commission announced in last autumn's initiatives, that, before the end of 2016, it intends to bring forward a legislative initiative on business insolvency, including early restructuring and second chance. This is intended to address the most important barriers to the free movement of capital, building on national regimes that work well.

In the meantime, the Commission will consult with stakeholders in the New Year and it intends to engage further with member states on this very important subject. But one thing that is clear, and this was underlined in both the CMU and the single market strategy, was that one particular field of focus for the Commission's ongoing work will be the follow up given to the Commission's recommendation on a new approach to business failure and insolvency which was adopted in March last year.

In that recommendation, we invited member states to set up a framework that allows viable, - and I underline viable – enterprises, in financial difficulties, to restructure early and efficiently, thereby avoiding all the disadvantages that can occur in liquidation. In several member states, the rules still steer viable enterprises in financial difficulty towards liquidation rather than restructuring. In particular, it is not possible to restructure a company at an early enough stage before formal insolvency proceedings are opened. However, studies have shown, that the earlier a company restructures, the higher the chance the restructuring will be successful, and the higher the returns will be to creditors. So, in other words, and I'm sure this is not surprising to you, here, today : time is of the essence.

Second, the evaluation we carried out of how the recommendation has been followed up has showed that whilst early restructuring does exist in a number of Member States, the procedures can be, nevertheless, inefficient and costly. The more expensive and lengthy the procedures are the fewer incentives companies have to restructure at an early enough stage when the business can still be rescued.

The recommendation deals with a number of points in this regard. For example it advocates flexible procedures with a strong out-of-court element, whilst recognizing that Court involvement is necessary at key stages to safeguard creditor rights and those of other interested parties liable to be affected by a restructuring plan.

The recommendation also advocates a debtor-in-possession approach. It foresees the possibility to request a temporary stay of enforcement actions with a number of conditions and guidelines on how that should be applied as well as the possibility of a "cramdown", providing that the restructuring plan has been confirmed by a Court. It also recommends steps to ensure that new financing can be made available without being declared void, voidable or unenforceable.

Finally, the last part or the recommendation also deals with this issue of second chance, the idea of giving an honest entrepreneur, who has gone insolvent or bankrupt, a second chance, by limiting discharge periods to a maximum of three years.

I don't want to imply going forward that we would only be interested in the follow up to the recommendation. We are also, at the present time, carrying out a comparative study, which I think provides some indications about other areas we are interested in. For example, the areas covered by this study are : directors liability and disqualifications in the event of an insolvency, the qualifications, status and powers surrounding the profession of insolvency practitioner, how this is dealt with in national legislation, the ranking of claims and the order of priorities. Another issue is that of avoidance and adjustment actions and finally, some more procedural matters relating to the opening of formal insolvency proceeding.

We have given ourselves quite a lot to look at. I don't dispute the fact that this is a complex area. There is a lot of national law involved. There is a lot of new national law involved, I think we see that and we shall hear more about that in a few moments. I am going to be very interested to hear what is being said. It is an area where, I think the Commission has a reason to be interested, as I have just explained.

Ladies and Gentlemen, I don't want to take up any more if your time, I think I have already probably exceeded your patience.

I have focused what I had to say on the Commission's perspective, as it is developing. I will leave the floor now to the other speakers who are going to tell us about Spain, Italy and France. I will be interested in what they have to say because we need a new approach across the European Union, an approach that focuses on the restructuring of companies instead of their liquidation, an approach that gives viable businesses in financial difficulties and the people they employ, a second chance. An approach that rescues viable business and helps them re-enter the productive economy. But above all, we need to be guided by, I think, the objectives that the Commission is pursuing. To place these reforms in the context of a reinvigorated single market, where national insolvency regimes operate in a coherent framework that opens the way to a true Capital Markets Union and to resumed growth and investment across the European Union.

Thank you very much.

Second panel

Panelists :

Julie Miecamp, Deputy Editor at Reorg-Research Inc. (Interviewer)

Adrian Thery, Partner, Garrigues, Madrid

Luca Ramella, Managing Director, Alix Partners, Milan

Francesco Faldi, Partner, Linklaters, Milan

Julie Miecamp

We are here today to discuss Spain and Italy which are known for their complicated insolvency law. I would like to start by asking Francesco and Adrian to take the lead and say what sort of insolvency tools are available in Spain and Italy. Just to give us a brief outline of the existing landscape.

Adrian Thery

In Spain, we have had a very different situation before the crisis and after the crisis. Before the crisis, the situation regarding insolvency instruments was quite binary. Out-of-Court or pre-insolvency instruments did not exist. We only had fully consensual deals. If we didn't have a consensus, you had no deal and you had to enter insolvency. The formal insolvency proceedings, called *concurso*, are pretty much like the Chapter 11 with a lot of limitations. The proceedings aim to reach at a reorganization plan and if no reorganization plan was achieved, the *concurso* would move to a forced liquidation of the company. In fact, 95 % of the *concursos* ended up in liquidation during the first part of the crisis. Reorganization plans were very difficult to achieve. Only very big corporations that were too big to fail managed to implement a reorganization plan. The liquidation of such large companies would have entailed so much loss of value for their stakeholders that they ultimately approved a reorganization plan. Otherwise for small companies you had business sales, ongoing concern sales where the company as such was liquidated but the business was maintained and sold during the liquidation of the company.

After the crisis and in line with the Euro recommendations, the government made several amendments to the Spanish insolvency law by Royal decree. Many pre-insolvency instruments were introduced in Spain. I will mention three of them.

We have the *moratorium*, which provides for a shield, a stay against enforcement from creditors, during four months. The *moratorium* also provides for a shield for directors who failed to apply for formal insolvency proceedings when the company was insolvent and may have faced wrongful liabilities.

Then we have an instrument that goes one step further, the so-called *formal refinancing agreement*. This is an out-of-Court refinancing agreement requiring no agreement from the Court. If you simply meet some majority requirements then the debtor and the creditor get two protections, basically. The first is global protection whereby the refinancing agreement cannot be declared void. Then there is a second protection providing an advantage from the perspective of DIP financing. The new money is granted a type of super priority ranking. If the company ends up in formal insolvency proceedings, half of the new money will be in a post-petition claim and the other half will be treated as a privileged claim.

The third pre-insolvency instrument is the so-called Spanish *scheme of arrangement*, a homologation proceeding, which, on top of the features available in the *formal refinancing agreement* may also bind dissenters and other creditors, through the majority principle, in order to impose a restructuring plan on them. The Spanish *scheme of arrangement*, which is very much used in practice nowadays, does not allow for a cramdown of the shareholders. Shareholders may not be compelled to sell their shares. They are not a class, so they are kept outside of the scope of the Spanish scheme of arrangement and this allows them to have an important holdout value.

This is basically the Spanish landscape. The main restructurings of listed companies in Spain, such as Pescanova or Martinsa, happened through reorganization plans approved with informal insolvency proceedings. But more and more, we use these pre-insolvency instruments and mainly the *scheme of arrangement* for companies who only have financial difficulties. They are being dealt with the Spanish *scheme of arrangement*. It is always difficult to find companies having only purely financial difficulties and things usually come together with operational problems. Those cannot be tackled through the Spanish scheme.

Julie Miecamp

In terms of landscape for Italy, do we have something that is similar, are we kind of moving towards having similar solutions across Europe here ?

Francesco Faldi

The question is : did Italy do its homework ? Basically, that is the question. Certainly the problems are really the same across Europe. In Italy we have the same problems, the same type of discussions. That is reassuring, in some way. The story is similar to Spain but just to give you a quick snapshot, our insolvency law was actually drafted in 1942. For decades, it remained unchanged. Then, before the crisis, in 2005 and 2006, we implemented a first reform. Since then, every year, or couple of years, we have changed something. Including during the last reform this year, between June and August, which is actually the thing we should check to see if we are really going in the right direction or not. The reforms from 2005 to this year were trying to help companies being rescued. We were trying to implement some of the Chapter 11 tools. Just to give you an idea, the Prime Minister asked his advisors, including us, to make some suggestions. We did an analysis of what were the key themes across Europe and the negative points in the Italian legislation. In a nutshell, we had almost the vast majority, if not all of the restructurings through purely consensual deals. Why ? Because our insolvency proceedings, the heavy one which we call "*fallimento*", bankruptcy, or "*concordato preventivo*", in particular, external administration, they used to be very lengthy and very disruptive. Concordato has changed, but the other two remain the same and the other two are with full dispossession. A Court appointed officer deals with the company and the restructuring so there is no way to use this tool like in the US by appointing the right *administrateur* and doing a sort of prepack administration. That is not possible in Italy using those insolvency proceedings. The *concordato preventivo* used to be rigid and lengthy but it is the sole one we had, allowing for the

cramdown of dissenting creditors, originally only unsecured creditors, but now we can also deal, with some limitations, with secured creditors. Therefore only consensual deals remained. Remember that Italy is a pretty severe regime in terms of civil and criminal liability of directors but also stakeholders. Therefore, the initial reforms were actually aimed at reducing those risks, reducing clawback risks, reducing liability risks, reducing criminal liability. How ? In which way ? Let me try to explain quickly. The concept of insolvency is not a pure liquidity test, nor an asset and liability test, it is more complex. Trying to make it simple, it is whether or not the company will be able, with its own forces, in the medium term scenario, to pay all its debts as they fall due. A medium term scenario leads you to the concept of a business plan. There is no way for a prudent manager to understand that, except by preparing a business plan. So the scenario is a three, five-year business plan. Whether the company will be able, in three, five years, to pay its debt. It is not just whether it will be able to pay the debt in one week or one month. And if a director is paying debt falling due now or in a month, while knowing that in a year or two, he will not be able to pay other debts, it is a preference and he can be liable for that. So it is a pretty heavy regime. We have, for pure consensual deals, procedures, which are not really procedures. It is just having a third party, an expert, or an expert plus the Court, rubber stamping your business plan, and saying that it is reasonable. It will rescue the company and therefore, there won't be any clawback and the management will be exempted from liabilities. This is the vast majority of restructurings in Italy.

Then, what are the problems ? Not having a real quick cramdown proceeding, the *concordato*. And not having a good environment for DIP financing. We had a number of rules implementing, trying to implement DIP financing but remember that in any case, in Italy, a DIP financing is senior to the unsecured but is junior to secured creditors. The Court cannot create super seniority, even though, in a minute, we can say that the market can open now.

What did we change in August ? We had an attempt to implement, I think successfully, an Italian *scheme of arrangement*. We took one of our purely consensual proceedings, which we call *Articolo 182 bis*, which is a debt restructuring agreement with an expert and the Court saying that it is able to rescue the Company, and we said that that can be implemented with a 75 % majority of banks or financial institutions and that the dissenting minority will be bound by the agreement. This relates only to banks and financial institutions as suppliers cannot be bound by the agreement. If you simply need their consent there is this important tool which will be recognized in Europe after 2017 because of the euro regulation. Then, we've made some changes to the *concordato*. In a nutshell, we tried to allow creditors to make counter proposals, to have a say in a *concordato* and we tried to make DIP financing a bit easier and we tried to avoid the sale of assets to related parties of the shareholders with no proper auction.

Julie Miecamp

Thank you. So in that context, what sort of practical difficulties have you encountered when you were doing restructuring deals in Italy ?

Luca Ramella

Well let me say that this morning, listening to our colleagues describing the French environment, I heard a lot of things that are the same in Italy : the lack of DIP financing, which is critical in restructuring, the length and time constraints of restructurings, the fact that assets are deteriorating during lengthy proceedings so that when you eventually reach a final agreement, you don't have the same assets so you have to prepare a new plan for a different company. As well as the fact that you have to pay a price to shareholders even if they are not in the money anymore. The concept of enterprise value is unknown in France. It is also the case in Italy. Things have recently changed, thanks to the last reform. Let me say, I want to be a bit mean by saying that this reform was made and drafted, for the benefit of the banks. For one bank, basically. One bank has "de facto" dictated the reform to (Prime Minister) Mr. Renzi. Simply because, in Italy, we cannot have a bad bank at the moment. If we had the possibility to create bad banks we would have had the possibility to clean up the balance sheet. But we cannot. Banks have been complaining a lot about this, and obtained, as partial relief, some kind of improvement in the insolvency law and some improvements in the ability to recover their claims by enforcing collaterals.

It happened, and I am pretty happy it did as I think our insolvency law was very creditor unfriendly before while it is now more creditor friendly. I think that it is now quite balanced. In a *concordato*, we can cram down shareholders and they are aware of that. You can negotiate pre-insolvency agreements with shareholders aware that you may cram them down to zero in an insolvency procedure. The second things is the fact that, in a pre-insolvency package you can cram down the financial lenders : it is something that I don't think will be often used but it is an effective threat that will make negotiations shorter, simply because small lenders know that if they don't agree, at a certain point, you cram them down with a 70 % majority. Same for alternative plans. As you know, in the US, you have the possibility to present alternative plans. But how many times did we see it happen ? Seldom. The mere threat that if your plan is outrageous and the haircut proposed to creditors is too high, you know that somebody else may show up with an alternative plan and you may be in trouble. The fact that the *concordato* exists, is helping to reach more acceptable reorganization plans.

Julie Miecamp

Do you mean that it actually increases negotiations between the creditors and the company as opposed to just allowing the company to do everything as we might have seen in other transactions ? I think maybe SEAT, Pagine Gialle ?

Francesco Faldi

Absolutely. It increases the negotiations between the creditors and the company because at the end of the day, two things now happen. Before the reform, you could file for a *concordato* and there was a possibility for the existing shareholders to make a proposal to the Court, which was the sole proposal, by simply saying we make a capital increase and the plan implies a capital increase. In a liquidation scenario like San Rafaele, there was an auction, which was different, but there was a way for the shareholder to fully control the process. Now if you are a creditor, with a certain percentage, more than 10 %, you can make your own proposal to the Court and basically you have two competitive proposals. Once again, I don't think this is going to happen very often, but the mere fact that it is possible is enough for the creditors to have a better deal.

Julie Miecamp

Before we move to see if there is something similar in Spain, do you want to explain the SEAT case ?

Francesco Faldi

In thirty seconds how SEAT went and how it could have gone if the new law was implemented. For more than a year, creditors didn't hear anything from the company. There was a negotiation between the company and the Judge on very technical things in relation to the proposal of the company, and no information at all. It was even impossible to sell the loan, for a reasonable price. Now, creditors, representing at least 10 % have the right to present a counter proposal and it is well designed so the Court appointed judicial commissioner has to allow the people to get information to be able to present a counter proposal. With confidentiality agreements, you could have access to documents and the proposal is then voted. If approved, there is an obligation for the company, the directors, and, to a certain extent, the shareholders, to comply with it. I mean, if the shareholders are not for example voting a share capital increase, reserved to creditors, the Court may appoint an officer who will vote in place of the shareholders. So that new tool is actually significantly changing things, in real life.

Julie Miecamp

Something similar has been introduced in France where the *mandataire* can actually decide to vote for shareholders, but at a very late stage, I would say when you are close to liquidation or *redressement judiciaire,* if I am not mistaken. I was curious to know how negotiations were going in Spain. Is there a lot of debate ? Is there a lot of opportunities for creditors to propose a real alternative to what managers might offer ? And if they can offer an alternative, is it respected or do they again have to be supported by shareholders at the last minute.

Adrian Thery

The problem in Spain right now with formal insolvency proceedings and also with the scheme of arrangement is that you need the equity to approve the plan. The Court may not dilute the equity without a shareholders' meeting. Even if a creditor led plan is approved by the creditors meeting, the equity can veto that plan and bring the company into liquidation, which is what happened with a listed company in Barcelona called *La Sede Barcelona*. A creditor led plan was aborted by the shareholders who rejected the capital increase. It also happened in the *Pescanova* case where creditors approved a reorganization plan with certain distributions of the equity post-restructuring. During a meeting held after the creditor's meeting, shareholders changed the equity allocation post-restructuring approved by the creditors. The judge simply could not impose the plan to shareholders. You mentioned before that in France a benchmark for the amount of new equity granted to out-of-the-money shareholders would be around ten to fifteen percent. In Spain it is closer to twenty per cent. This is what shareholders of Pescanova received as well as those of another recent case, *Cordere.* This is really a problem. It is useless to reach a pre-insolvency agreement providing for the cramdown of minority creditors if shareholders can remain unimpaired and block the reorganization plan.

Julie Miecamp

And that won't change with the new law, right ?

Adrian Thery

It is being considered, but the problem, I think, is that Italy and France might be the first ones to have a real cramdown of shareholders because I believe that, in fact, in the UK, the way to disenfranchise shareholders is through the combination of a scheme of arrangement plus a prepack. So, in the UK, you are effectively liquidating the old company, transferring the business to a Newco and combining that with a scheme of arrangement which is pretty inefficient because you can do that only with holding companies, as most are in the UK. But with continental companies which are complex industrial companies, that doesn't work. You really need that cramdown feature so the Court can cram down the shareholders and pass a plan without having to liquidate the company.

Julie Miecamp

So if we focus on what still needs to be done, it seems that it is the same theme across Europe, we need to find a way to cramdown shareholders. The question remains : How far along have we come in Spain or in Italy in terms of making these jurisdictions more attractive to companies, in order for them to restructure ? In Spain in particular, I am thinking about Spain because a lot of Spanish companies have gone to the UK, to implement restructuring deals. SEAT was probably the only Italian example that I can think of. France has had a couple of examples of companies going to different jurisdictions. Are we now getting into a place where Spain or France or Italy can retain perhaps more of their companies here ?

Adrian Thery

The UK scheme has been very attractive to Spanish companies when there was no Spanish scheme. Now that there is, there have been very few COMI shifts. You do not really need COMI shifts. It is simply a matter of applicable law. The problem is that, for a Spanish company to disenfranchise the equity in the UK, you need, as I said, to combine it with an administration. And an administration is a formal insolvency proceeding so you do need a COMI shift, effectively. It is not sufficient to have a connection through the finance documents and a submission to English law. For Spanish corporates, right now, we have a very, very successful tool for creditor holdouts, which is the Spanish scheme which is tantamount to that of the UK and has very limited possibilities of being challenged. I mean, it is really working nicely. But the equity is a pending issue in Spain. We have tried to resolve it through a threat to the directors and the equity. If they do not approve a reorganization plan proposed by the creditors, we would tell the directors or equity that they might be liable for damages to the company. But this has not been enough. You really need a judge to disable and to buy in shareholders into a creditor led reorganization plan. For that, valuation is of the essence. I really do not see how you can have disenfranchised creditors or even shareholders if there is no determination of the enterprise value. It is key, it is a matter that affects fundamental rights and that might also affect investments in European countries. If I were an investor and I could be disenfranchised with no valuation proposition that would be quite something.

Julie Miecamp

The problem is similar in France and it has to do with language in the law. I am surprised to see how vague it is in both

France and Spain. An "unreasonable shareholder" or a situation, in France, that would "threaten employment". These are the very criteria that you rely on as opposed to valuation. So, yes, again, I think it is a common theme in the three countries. Would you like to add something ?

Luca Ramella

Yes, well I think, the law as it is today, in Italy, is a very effective law, with some factual limitations. Let me clarify what I mean. When I filed for Chapter 11 bankruptcy proceedings in the US a few years ago and we were selecting the venue and deciding which Judge was better for our case, there was, anyway, on an average, a very good level of judges evaluating the case and it was a matter of timing, a matter of a better understanding of the business, but basically, we had to deal with super expert judges, which is not the case in Italy. Our judges in Italy are very different. We have judges with a very big and strong know how and they cooperate with the company to prepare an effective plan exactly in the same way as you do it in the US where sometimes you don't prepack, a Chapter 11. But instead you negotiate with the Judge in the due course of the procedure, you end up with something that is worthwhile. I had a couple of cases of restructuring where we had a very wise and expert Judge also in Italy and we had the opportunity to do well. But sometimes the Judge is a former public prosecutor who has just moved to the insolvency Court and you have to talk with him about a multi-billion company in a procedure he does not fully understand. And then they have to appoint a receiver or a commissary or an expert and they sometimes appoint friends or friends of friends or the administrator of the butcher who is down the road or something like that and then you end up with an expert coming in the company who doesn't have a clue about a multi billion company because the biggest thing he did was the accounting of a shop. So this is what has to change : not the law, but the experience and people knowing how to deal with that. And it's very different, as I said. For instance, we don't have insolvency for groups, but we had a case of a French company, filed in Italy, where we needed to have a group procedure. We sat with the Judge, we discussed the way to do it and we ended up with something, which was de facto a group insolvency, but this was an expert and wise Judge. One other thing that is factual and not about the law, is the Italian labor law. France is the last socialist European country where they take care about the labor more than the creditors. But in Italy it's very similar. We are dealing with situations where you cannot do anything in the restructuring because the labor issues are pretty big, we had some protections to the labor and the insolvency that are gone now. In the US when we filed for Chapter 11 in Dallas, we filed, in our first day motions, the DIP financing to reject some leases of our stores, as our client was a retailer, and finally to make employees redundant. We proposed to pay them a severance of two weeks and the Judge said : "Oh, Hold on ! Why ? What is that ?" And we answered : "sorry but we don't have a lot of money we can only pay two weeks" and he said "that's not what I mean, why do you pay two weeks ?" OK ? It is pretty different from France, you know. The law works. I don't think there are big issues in Italy now on how the law works. But the interpretation of the judges, the interpretation of the expert that will be appointed or of the receiver, this has to become appropriate and this is a long process. It was a long process in the US as well. It did not happen in one day. Chapter 11 has been reformed I think many times and judges get to learn the process better. We need that process in Italy too. I don't think we need any additional significant reform in our country.

Julie Miecamp

Do you want perhaps to add something on how there is sometimes a confusion in France, Spain or Italy, about preserving jobs and preserving the employees because the valuation, the concept of a valuation of the company is never taken on board. Is that something that you see as a difficulty in Spain ? Or is that getting better ?

Adrian Thery

I think that one thing that explains why southern European countries may be more debtor friendly in general is that the law confuse the protection of the business and of the workers with the protection of the company as a legal entity. That was a confusion that is no longer there. The laws are being adapted to protect businesses by either winding up companies or craming down the equity and giving creditors access to the new equity. I think everything is progressing in the right direction. I really think that in jurisdictions such as Spain or probably all over Europe, where there is no guidance and certainty about valuation, shareholder cramdowns is now a central issue. It should be addressed because, for instance in France, the *administrateur judiciaire* has no visibility on the Court's view on valuation. If I were an *administrateur judiciaire*, I would be a bit scared to come up with a valuation that has not been sanctioned by the Court because I would then be liable for it. In the absence of a Court sanctioned valuation, you need a process, a fair trial and effective remedies. This is difficult. There is a big tension between the important objective of cramming down or wiping out equity in certain situations of over indebtedness and the objective of facilitating pre insolvency, instruments with light Court involvement. In the end, to disenfranchise stakeholders, you need a process. Pre-insolvency does not provide it. That is why in Chapter 11 in the US invented the cramdown and provided a process. If Chapter 11 works well for insolvency and out of Court agreements it is because all the stakeholders can see exactly what would happen should the company files for Chapter 11. Therefore, to have pre-insolvency workouts, you do not really need pre-insolvency instruments, only a Chapter 11 that works well. Chapter 11 is indeed being revised in the US but it is only limited to tweaks to the regulations so as to keep a level playing field, not be too debtor or creditor friendly. They are not contemplating a holistic modification of Chapter 11. They are simply doing some tweaks.

Whereas in the UK, I think the scheme of arrangements is working in practice but it is not an insolvency tool. Therefore, there are some uncertainties as to the valuation. Hedge funds do not know where the fulcrum security is, *i.e.* which part of the debt to buy, in order to be able to implement loan to own transactions. The investors do not know the valuation of the company should it go bankrupt. The also do not know what the valuation would be in case of distress. I believe that valuation certainty is of the essence. Chapter 11 is achieving that better than the UK scheme of arrangement. Also I think that the shareholder cramdown is a matter that has to be tackled from a European perspective because, imagine there is a COMI shift of a Spanish corporation to France. It is difficult to me to see a French Judge doing an equity cramdown of a Spanish corporation with Spanish corporate rules. And this can only be tackled from a European perspective.

Francesco Faldi

With respect to Italy, we have made a lot of changes with the last government. For better or worse labor protections are no

longer similar to that of France. It is now much easier to make people redundant. In particular in the context of insolvency or quasi insolvency proceedings. If you sell a business in a *concordato* – my labor colleagues wouldn't say it in that way – you may even cherry-pick your people – as long as you use criteria which are not discriminating.

As for judges, unfortunately, they vary a lot. This is because, in London, in England, you really have the Corporation dealing with the judges, full stop. In Italy, that's not the case. If you go to Milan, usually you will have pretty good judges. If you go to Rome, it will vary. I had some very good experiences, some less good. In small towns, of course, it depends. It really depends on the Judge you find. It is difficult to address this issue because this causes political tensions and affects whether or not cases should be centralised. In terms of DIP financing, I think two words may be important. We have a DIP financing that is not super senior. The judge may not say that you will be super senior to a secured creditor. However it is now easier because in the past you needed an expert to say that DIP financing was actually improving the recovery of the unsecured creditors, which is no longer the case. The condition now is that the DIP financing must be urgent, needed for the business and there is no other alternative means. Italian lenders are considering transactions where there is a DIP lender asking for a super senior seniority. You can achieve the same result by having contractually agreed with the senior lender in an inter party agreement that you are super senior and by operation of law you will be senior to all the unsecured creditors. It is something that is workable, depending, of course, on the economics of the transaction but there is certainly an appetite over by lenders to explore these types of transactions.

Luca Ramella

One thing that I would like to note on DIP financing that is critical : In the US, our colleagues say : "First comes the DIP financing then comes the rest". If you don't have the DIP financing, you don't have a Chapter 11. In Italy, things are quite different. Have you seen the day sale outstanding in Italy ? How long are the payment terms ? Almost one hundred days ! That means that if you have the automatic stay, you don't pay your creditors and you collect the money. Just by slightly decreasing the level of your turnover you decrease the working capital, and generate a lot of cash. With this kind of payment terms you have an instrument, which is reducing the working capital and squeezing a lot of money in the short term. I have never seen a company filing and then saying "I don't have money", because for at least 100 days they can keep collecting money from past sales. Even if the activity of the company stops for one month, the company still collects money. It is critical, but not that critical with this shape of working capital. I think it is pretty peculiar in our country. And I think perhaps in France this helps a bit. Otherwise DIP financing would have been super critical and I think there would have been much more work from our legislators focused on DIP financing. Instead this working capital is a very good amortization.

Julie Miecamp

One last point. Across the board here, we have just said that there were limitations to DIP financing and attracting investors into the situations. All of you are practitioners who have gained experience internationally so how far do you think your respective countries might be from having a law that would make your job a little bit easier and allow for efficient and timely negotiations. How far along are we ?

Luca Ramella

If you Google Luca Ramella, the first thing that appears is Alix Partners. The second thing is that I recommend to my clients not to invest in Italy. Why ? My experience is that, so far, any kind of investment in a distressed entity without a pre-package with shareholders and creditors was impossible in our country. In addition these stories of good P&L and bad balance sheet are a fantastic dream that I haven't ever seen yet, and I have been doing this job for the last 35 years ! Maybe in the next 35 years I will find a good P&L and a bad balance sheet. Normally a bad balance sheet is because there is a bad P&L or one that is not that good ; so you have to fix the company first and in this environment in the last six to seven years it has been very, very difficult. Inflexible labor laws, a disastrous Italian economy, the European economy not very good too, unfavorable exchange rates for the Euro, cost of oil above 100. How can you fix a company ? Would you have called investors and said "come to Italy because there are great opportunities now" ? Things have now changed and I would say that with this kind of new law, particularly if you can pre package and reach an agreement with some of the main creditors, even without an agreement with the company, you can probably make some very good deals. Things have changed significantly. Not just because of the law which has been a dramatic improvement for creditors and investors but also because of the general environment. Not by chance, Prime Minsiter Renzi introduced the reform of the Italian labor law called the jobs act. Then he made the change of insolvency law and helped to fix the P&L, which, in our opinion, is the first thing you should do when you start thinking about an investment in a distressed environment, and then the rules of the insolvency and pre-insolvency agreements.

Adrian Thery

In Spain, we think that the traditional main player in insolvency proceedings which were typically the banks, have left their place in favor of hedge funds. We are seeing huge NPL (non-performing loans) transactions in Spain. Hedge funds are buying in NPLs and a lot of the bank's positions in secondary trades. Traditionally, the banks were more focused on collateral enforcement, whereas hedge funds in general are interested in taking some risk over the future of the company and therefore getting the equity. All the regulations are going toward that direction, i.e. to allow the company to be saved in certain moments so as to make it more attractive to hedge fund. For instance, before a couple of years, in Spain, any hedge fund that had acquired post petition a claim would lose its voting right, whereas now this feature of the law has been amended so the hedge funds don't lose the voting rights vis-à-vis the reorganization plan, even if they acquired the claims post petition. In general, we are seeing that trend. As for shareholders cramdown, banks are an important lobby in a big country. However, local banks might not love shareholder cramdowns, because banks are generally relationship banks and so they usually also lend to the top part of the structures, so they give loans not only to companies but also to shareholders. Therefore, they might see at first sight that shareholder cramdown is something that make them lose leverage to the benefit of hedge funds. However, if you take into account that banks are generally, right now in this particular moment, at least in Spain, not recovering and are there-

fore forced to sell their claims on the secondary markets, banks should realize that with a shareholder cramdown, they will be able to sell their claims at a much higher value than what they are able to do right now.

Julie Miecamp

OK, I am conscious of time so I wonder if there are any questions in the audience.

A participant

We are sponsor investors investing in Italy. We advise equity investors and lenders. If you are a lender, and you have the opportunity, you can try and implement a double Luxco structure, to have a double pledge on the two Luxcos, which is an effective way, as a lender, to enforce. Just for the people not aware of that, in Italy we've implemented the financial collateral directive slightly in a different way than Luxemburg so the shares of a listed company are within the scope of the financial collateral directive. As for the shares of a non-listed company, it's a bit of a question mark, but more or less there is no precedent or enforcement of them through the financial collateral directive and more or less the market thinks that they are not subject to that scope whilst that is the case in Luxemburg. The Italian deed of pledge, works in theory but in practice it is not effective because if the debtor challenges the enforcement the Judge can block it. It is not the case in Luxemburg, there may be some litigation for damages, but you cannot stop the enforcement process. That's the reason why really there is no Italian restructuring deal, which has been made using a pledge and enforcing it. On the contrary, in Luxemburg it is different, in England it is different, so yes I mean, as far as we are concerned that is a problem but only where you have that type of structure, which is often not the case in Italian transactions.

Sophie Vermeille

I think I am going to make just one comment because the question that you ask, is very important and I think, if you look at the situation in the US, they are the only ones who have managed really to answer it properly. Basically, if you give a collateral to a creditor in the US, there is this guarantee that they are not going to be worse off, during the Chapter 11 if they have been able to actually enforce the security interest. This is very important because you have the automatic stay, which protects the company, but also you have the collateral, which gives you really a right to, not to suffer any loss before the shareholder and the unsecured creditors. The issues that we have in France, is that as secured creditors are not well protected, we, as their lawyers, are forced to use other types of instruments, which are basically bankruptcy proof. This usually means a type of contractual arrangement, which entails transfer of ownership for instance. We have a new "*fiducie*", a kind of French trust which is very dangerous in the end for the company because if there is no longer any asset how can the company bounce back ? There is no contradiction with the idea that in order to save jobs, you need to save entrepreneurs and also preserve the rights of the creators if we adopt the US way. Otherwise there is still this contradiction between debtor and creditors.

Closing remarks

Insolvency law reform in Continental Europe : Can national leaders bring in sufficient reforms ?

- The triggers of national insolvency law reforms : past and future
- How key is a judicial reform in Continental Europe ?
- Can we expect a loss of sovereignty of Member States ?

Speakers :

Lorenzo Stanghellini, professor of business organization law at the Law School of the University of Florence

Sophie Vermeille, President of Droit & Croissance, Rules for Growth

Sophie Vermeille

By way of introduction, Professor Lorenzo, we both share an experience working with public authorities, trying to convince them to do some reforms. We have seen, with the second roundtable as well as the first roundtable that there were many common lessons to draw. We have seen many piecemeal reforms, in Spain, Italy and France over the last years.

Can you tell us, what were the drivers of the reform in Italy and why did we end up with so many reforms ?

Lorenzo Stanghellini

I have to say that I have no particular merit in being here apart from the fact that I have been involved in some of these reforms. Just to be transparent on this, I was in the commission appointed by the government in 2005 that basically modified radically the law that was up to then the 1942 law. Then, I was involved in some way with the reform of 2012 that basically boosted the *concordato preventivo* or restructuring procedure, to make it suitable for going concern reorganizations. Finally, I had *some* role - I'm not making it bigger than it is – by way of consultancy work for the Bank of Italy and the Ministry of Finance, in the 2015 insolvency reform.

I would say that the driver of the 2015 reform was totally different from the previous ones. The declared goal of the 2015 reform was mentioned a few minutes ago, it was to put some pressure on the banks. I would say, some movement on the stock of non-performing loans that is quite huge in Italy. More than 300 billion euros that is a heavy load on the balance sheets of banks and hampers the economy and the enterprises especially small and medium enterprises as Mr. Shotter mentioned a few minutes ago.

The goal of this reform was to empower creditors in two ways. First, to allow them to file competing plans as was mentioned a few minutes ago. Second, was to introduce a *scheme of arrangement* to give shareholders more leverage during negotiations.

Coming to your question, I would say that two factors contribute to these incremental and piecemeal reforms.

First of all, as far as Italy is concerned, the law, up to ten years ago, was, basically the same law it was in the 19th century. You can change the law, but you cannot change the culture with a magic wand. The product that you have is somewhat suboptimal. It's not something that you would design in a kind of soft, protected room, with experts. It's something that, to put it bluntly, is done through negotiations and mediations. So, what you do is a big leap, maybe a big leap forward, not the optimal.

Second, insolvency law is very sensitive to the context. Compare it with corporate law, that is quite easy to refine or even reform. In 2003, for instance, in Italy was enacted a comprehensive, good company reform, which basically went without big discussions, apart from academic discussions. When you try to touch insolvency law, it is a very difficult issue. You have to deal with judges, professionals, banks and even competitors. For instance, in 2013 a minor reform was driven by the Association of Entrepreneurs (Confindustria) that thought, right or wrong, that the *concordato preventivo* had gone too far. This meant that an entrepreneur who had survived through a *concordato preventivo* was bringing unfair competition to the others. The head of the Association announced it publicly and immediately there were rumors. And the law was changed to restrict the possibility of *concordato preventivo.* So, it is nice and interesting to discuss, but once you have to deal with, to work on reforms, you have to put the helmet on, a jacket, and start running, and it is very difficult. And this does not produce optimal results.

Sophie Vermeille

It's very interesting because I think we can draw some parallels with the situation in France. Until 2014 in France we had what we thought was a very debtor friendly regime, which was in fact a very shareholder friendly regime. And it really changed in the 2014 reform.

One of the reasons for this reform is that the Ministry of Finance realized at the time that the tradition among French managers was to stop paying social taxes just before filing for bankruptcy proceedings, (in order to build enough cash reserves to make it through the period of automatic stay, because they would anticipate that they would not have access to debt financing during this period), had a really major cost on the Treasury.

We used to have a very debtor friendly regime. The idea was to give the keys to the management, to the shareholders, because we thought that was the only way to save the business. Suddenly we began to realize that there is actually something really wrong with access to finance in France. That was the starting point. Later on, Droit & Croissance invited economists around the table, to discuss the lack of economic theory in French law.

When I listened to the previous panel what I noticed is this question about pre insolvency tools. And of course, in France, I think, we are the winner in terms of number of pre-insolvency tools and we have invented everything. I quite agree with what you said Adrian during your roundtable, I really think that the efficiency of the negotiations during the pre insolvency processes depends on your fallback positions. The fallback position is the formal insolvency proceedings. If you look at economic theory, it is game theory, so people negotiate because they are encouraged to do so, because they save cost. Until 2014 in France we thought that by threatening creditors we would end up with good results but this is in contradiction with economic theory. It is by encouraging the parties and especially the one who has the most interest in taking the issue and dealing with the issue upfront, i.e. the creditors, that you actually facilitate the restructuring of the company. Not by giving the keys to shareholders who, in effect have no interest in negotiating upfront because they are always going to hope that they can be made whole.

Just to give you an example, if you want to make a good reform, make sure that you have an economist but also practitioners because one cannot do without the other and they work together in order to design a new reform.

If you compare the situation with the US. Chapter 11 was enacted in 1978. Then they had a reform in 2005, which was small, but actually had quite a major impact. Now they are in the process of reforming Chapter 11 again but it is a very long process. It has now taken three years. They are doing that in a very professional way. You can watch the hearings on the web site. Whereas, in France, you have to draft new laws in five months ! This also explains the low quality of French laws. This is why I believe that the *Loi Macron* was a missed opportunity to introduce a real shareholder cramdown.

The lack of law and economics research is perhaps one of the main issue in European corporate law. It explains why we cannot anticipate economic crises and then wait for the crisis to force us to adopt reforms in a limited timeframe. This explains why it took us so much time to reach a good result.

The second point I thought would be interesting to discuss is the judiciary. It was briefly touched upon during the last roundtable. I think it is important not to forget that insolvency proceedings are also about judges. What are your views on this issue ? Because, to be honest when I went to London and spent some time with investors and I started to talk about Italy, the first thing they told me was that their concern was not necessarily Italian law, but the judiciary. Can you tell us a bit more ?

Lorenzo Stanghellini

I have to say that the perception is quite right overall. In a sense you have less possibilities to foresee what the outcome will be. First of all, I would like to point out a quite peculiar feature of insolvency law. In insolvency law - that's my opinion - there is no effective appeal, there is no effective recourse against wrong decisions by the Court, at least, when time is of the essence.

For instance when a debtor asks for an authorization to a new finance and for one reason or another the Judge says no, there is no point in getting this authorization. In the appeal phase, three months later, it is too late.

Just last Monday, I discouraged a client from filing an appeal against a decision against a crucial part of the plan because even if the decision was openly wrong, and there was no question about that, there was no point in obtaining the right decision three or even two months later. And, I advised my client to simply amend the plan.

It is not only judges who are important. They are terribly important because the first instance judge is the man who at

least when the survival of the business is in danger, is the one who has the key for making it live or die. This calls for either the specialization of bankruptcy Judges or perhaps some other kind of regulation for the role of the judge.

My experience is that, in Italy, there is a bankruptcy section for each tribunal, a total of 136. I heard that France had 134. This is not, I think, by chance, because, as you know, Italy has a structure of law and organization that is due to France's influence. So, you find good judges and not so good judges. I'm not talking about dishonest judges but simply not experienced enough. Moreover, and this is more important to note, even in large cities like Milan, you might find judges that don't like the law as it is.

I will take an example to clarify. One of the points of the 2012 reform was to introduce the so-called critical vendor doctrine. The possibility to pay in full and immediately the suppliers without which the business would go bust. This clearly runs against the *pari passu* principle. What did the Milan Court said - and that was quite unexpected – the Court said, oh, the *pari passu* principle cannot be derogated, so what we can allow is only a payment for the same percentage that the supplier will get in a plan once it is filed. This is tantamount to killing the law. And we are not talking about Florence or Palermo. We are talking about Milan. So this means that there is a strong need for specialization and probably more training in law and economics. In Italy judges can be public prosecutors one day and bankruptcy judges the other and maybe only graduated two years ago. They might lack total experience. I think this is a point where the EU might, if they wish, intervene. (Laughter)

Sophie Vermeille

I think there is a message for a recommendation. Because as we just said, again if you negotiate during the pre insolvency phase, if your fallback position is bad, because of the Judge, again it's going to be an issue, that's what you said. And in France we can also draw some parallels, we have actually 134 Courts, I just checked before the conference, but we are making some progress actually, because in the *Loi Macron,* there is a provision which will enter into force in March of 2016 and we will have more specialized Courts for big cases so there is this understanding but I think there will be nine Courts. When we look at the situation in the US, we see that actually, for the big cases, there are only two Courts. There is the Southern District of New York or Delaware. When General Motors filed for bankruptcy, even though General Motors is based in Michigan, they went to the Court in New York. So I think it is important to keep this in mind, and especially for the new Commission. Because it is really important. The Judge is really central.

In terms of expertise, we have, as you know, a very specific system, Lorenzo. The Commercial Court of first degree is made of non-professional judges who are elected by their peers. At least we can think that they have a good understanding of business culture and so on. We have to be honest and recognize that sometimes there is a lack of legal background for sophisticated cases and also for financial cases because you can imagine if you end up in a small Court, even if you have a businessman in front of you, it's going to be hard to talk to him about LBOs and so on.

And we have for the Court of Appeals and the Supreme Court, professional judges and I think we have the questions as you have mentioned. There is a kind of taboo in Europe around the competency of judges and their expertise. What do you expect from them ? When you look at the UK, where judges are basically former barristers. We may ask the question : is this the best solution because apparently there are a lot of cases, which are now moved to London. If I take the case of Germany I tend to see that German Law, the law by the book is quite great, but I still see so many cases, so many German cases going to the UK. So, maybe the answer lies in the quality of the Judiciary. And I think it is important to bear this in mind.

I think that to finish up we have to ask ourselves : Is there any chance that we could have a Chapter 11 in Europe ? Can we really expect the member states to agree to lose their sovereignty with respect to this issue ?

Lorenzo Stanghellini

This question goes much higher than me and Mr. Shotter explained to us that the path is already established and, even though the result is not guaranteed, there is political will to proceed in that direction. I think that there is evidence that the fact that insolvency regimes are so different in member states creates an uneven playing field that has an impact not only on the survival of distressed businesses, but also on the cost of credit because of the fact that creditors anticipate different recovery rates and price the credit accordingly.

So I will not go into the details as an observer from one side of the EU, but I would like to remind that the position of the European Parliament of November 2011 was quite strong, probably even stronger than the recommendation of 2014, in recommending the EU to take into serious consideration harmonization. Therefore, harmonization could take up speed after the 2014 recommendation and the European Insolvency Regulation recast of 2015.

I'd say that one important factor may be the Bank Recovery and Resolution Directive and the bail-in. At least for the Euro zone, in case of cross-border bail-ins, there is the entirely new challenge of applying different regimes for each member state. Once the Single Solution Board in Brussels decides that a cross-border group goes into resolution and applies the bail-in, it has to deal with different jurisdictions and to comply with the no creditor worse off requirement in each of them.

Sophie Vermeille

Can you explain what this means ?

Lorenzo Stanghellini

The "no creditor worse off" principle means that if a bank is subject to a bail-in or a *sauvetage intérieur*, and it is rescued by writing down shareholders and claims up to the point in which the bank has capital to survive, then there is a precise requirement in the directive that states that no affected party (shareholder or creditor) can be treated worse than if the Bank were liquidated.

This means that if for instance a French group with German subsidiaries is bailed-in, the creditors of the French entities have to be treated according to French priority ranking of creditors and the creditors of the German entities of the same group have to be treated differently because, for instance in Germany, creditor ranking is different. Ultimately, they are

all creditors of the same group. So this might be one of the drivers with a spillover effect for the harmonization regime, another way to describe insolvency regimes for banks, spillover effect from banks to ordinary businesses.

To put it short, there are two possible avenues to overcome this unlevel playing field. The first is regulatory competition. For instance, this is what happens when businesses move to another member state to achieve better re organization. But there is a COMI requirement that limits forum shopping, even non-abusive forum shopping.

There is another possible avenue, that is a kind of import of specific parts of the insolvency regime of other member states. I have no difficulty in admitting that the Italian amendment in 2015 was heavily inspired by the French technique of disempowering shareholders. That was considered more compatible with the former second directive on company law (now Directive 2012/30/EU, and specifically Art. 29) than the German approach that basically treats shareholders like a class. Maybe even the latter it is acceptable, but the French approach might be more clever, or at least, less directly *against* the directive.

The same is true for the UK scheme of arrangement, which was imported with some modifications in Italy. But I don't think this is enough. Harmonization is desirable and quite surprisingly to me, scholars from such an extraordinarily reputable UK institution like Oxford – the British are not known to favor harmonization -, have published a paper, calling strongly for harmonization. A paper by Kristin Van Zwieten and Horst Eidenmuller[1]. It is very well written and very well reasoned.

Having said that, and hoping that you will take the lead, there are two possible outcomes (I have to say that I am just speculating). Either an *a minima* harmonization, dealing, for instance, with avoidance rules, preference for new financing creditor ranking, along the line I was mentioning. Or, a higher degree of harmonization that, reasonably, could not be the entire spectrum of insolvency procedure but could be limited to a rescue procedure. And I would say rescue procedure not only in formal reorganization like internal reorganization that deals with the liability side of the balance sheet, as the recommendation seems to have envisaged, but also rescue via a business sale or a going concern sale that are quite important. This is an important and accurate point that is made in the Oxford paper I mentioned earlier.

If this happens, I recommend that two objectives are kept over the radar and don't slip into the cracks. First, is the role of the judiciary and the qualification of insolvency practitioners. I am not sure that we can go as far as to unify jurisdictional systems, but the EU institutions can recommend, or require, some form of specialization or qualification for insolvency practitioners. Second is corporate liability or what is usually known as "wrongful trading". That is an important part. Mr. Shotter, you mentioned a second chance for entrepreneurs. This is true for natural persons but when you deal with corporates, you deal with people who are not entrepreneurs. They don't need a second chance. They need to be aware of the consequence of a business failure for their own fate. So, if, like in Italy, there is a strong tendency to file a liability suit every time there is a bankruptcy, then you might have that even if you give a discharge to a natural person, you still have punitive attitude to entrepreneurship. Therefore I think corporate liability should take an important part in the proposed harmonization.

Sophie Vermeille

It's quite interesting to mention that in the US, there is one federal insolvency law and fifty corporate laws and we have spent so many years in Europe trying to design a European corporate law and we just forgot about the insolvency law. Maybe we should have figured out why in the US there is one federal insolvency whereas there are fifty corporate laws. I really think that in terms of harmonization it's much more important to harmonize insolvency law than corporate law.

Can we really achieve this goal ? It is going to be tough and we have to recognize this. I mean, I am French and we all know that the French are very proud of their law. We invented the Civil Code. Napoleon is French. And, as you can see this is a very emotional issue for the French.

I think we have to move forward. I think the issue is more : "Can we integrate the principles of economics in our law, to move forward and have a more efficient law ?", rather than, "Is it a battle between common law versus civil law ?" Because this issue is an old issue and we should forget it.

We have many challenges today. I think one of the points that is going to be an issue if you want to harmonize insolvency law is the fate of employees.

Can you imagine being appointed as a judge in a small Court to decide over the fate of the main company in your neighborhood ? What kind of decision are you going to reach, between rehabilitation and liquidation ? Of course you are going to be encouraged to vote for rehabilitation, even though it's not going to produce the best result. So it's not just a lack of business knowledge in this respect. Eighty per cent of companies emerging from a *redressement judiciaire*, go into liquidation within the next five years. That is eighty per cent ! And for the safeguard proceedings, that number is fifty per cent. The results are not great. We need to forget about saving the jobs in the short term and think about saving the jobs in the near future, in the long term.

That's the kind of issue we are facing in France today. If you want to really change our model, because, as you've said, Lorenzo, when it comes to reforming insolvency law, it is a very sensitive issue and we must take the culture into account.

1 http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2662213.