Mediation in pre-insolvency proceedings

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Abstract: The Insolvency Procedure Act introduced the Out-of-court Settlement as a mechanism to restructure insolvency and to avoid the start of an Insolvency Procedure. Its success depends on the action of a mediator who has to prepare a Settlement Plan for credits, together with a "Feasibility Plan" and a "Continuation Plan" of the professional or business activities of the debtor, including a "Negotiation Proposal" of the debtor's loans and credits. Should the Plan be approved – it requires the favourable vote of the creditors of at least 60% of the liabilities, and 75% if the Plan consists in having the debtor transfer his assets as a payment for his debts–it must be converted into a public deed and published by the BOE (Spain Official Gazette) and registered at the Insolvency Procedure Registry.

Keywords: Mediation, Out-of-court Settlement, Pre-insolvency Proceedings, Insolvency Procedure, Insolvency Administrators.

Act 14/2013, on Entrepreneurship, introduced the Out-of-court Settlement as in the Insolvency Procedure Act as a new mechanism to reinforce how pre-insolvency situations are dealt with. The success of this mechanism depends on the intervention of the so-called "insolvency" mediator. The professional activity of this mediator is well governed by an administrative authorisation, which is the resolution issued by the Head of the Mediators Registry and the Mediators Institutions of the Ministry of Justice whereby it is incorporated to Section Two of this Registry as it is considered that the requirements have been fulfilled as stipulated by the Mediation Act, its Rules and Regulations, as well as the Insolvency Act [Act 5/2012 on Mediation, Arts. 27; 233.1, Insolvency Act Arts. 11.1 and 2,and Arts. 18 and 19 of the Rules and Regulations of Mediation].

Moreover, the actual possibility of practicing this profession relies on two more administrative acts: the incorporation of mediators who are registered at the official roster of mediators, and its communication by the Head of the Registry to the BOE (Spanish Official Gazette) for publication on its website. This way of regulating access to practice for insolvency mediators poses some serious doubts concerning how this is in accordance with what is stipulated in Arts. 9 and 10.2 of Directive 2006/123/CE of December 12, on services in the domestic market. Once his/her incorporation is made public, the mediator can be appointed to practice as an insolvency mediator.

The Act established what debtors can request an Out-of-the-court Settlement. These are: an entrepreneur, natural person, that either faces an insolvency situation, under Art. 2 of the Insolvency Act, or foresees non-compliance with his/her obligations on a regular basis. The request can be done if liabilities do not exceed five million Euros, which should be demonstrated by providing the corresponding Balance Sheet with the Request Form. Also, "a legal person, be it a venture capital enterprise or not" (therefore, sole owner or civil companies, associations and foundations) that faces an insolvency situation.

Moreover, the following requirement must exist: the requesting debtor shows before a Notary or the Commercial Registrar that in the event the insolvency procedure is started, it should not have a "special complexity" nature given that any of the following circumstances occur: 1. The list produced by the debtor includes at least fifty creditors. 2. The initial estimate of the liabilities does not exceed five million euros. 3.The valuation of goods and rights does not reach five million euros" (Art. 190 Insolvency Act); the requesting debtor proves also to have liquid assets enough to service the expenses derived from the Settlement, and that his equity and foreseeable income allow him to "likely successfully" achieve the payment agreement.

The procedure to negotiate and further perfect the Payment Settlement is initiated at the request of the debtor requiring to file the case in order to reach this kind of agreement, and the appointment of an "insolvency mediator" (Arts. 231.1. and 232. 1 of the Insolvency Act).The request is submitted to a Notary's address. However, if the debtor is an entrepreneur or a legal person that must be registered at the Commercial Registry, the request is submitted to the Commercial Registrar corresponding to the address of the debtor.

Moreover, the debtor must indicate in the form or request used to file the case, the money and the liquid assets in his possession, his goods and rights, and the forecast regular income. This list should be accompanied by a list of creditors including the amounts and the due dates for the credits, and the creditors holding secured or public loans. In addition, a list of contracts in force should be added and another list containing forecast monthly expenses. Lastly, when the debtor is obliged to keep accountability books, the request must include the annual accounts of the previous three years.

Following, the Notary or the Commercial Registrar must appoint as "insolvency"mediator the corresponding natural or legal person, according to the order of the official "insolvency" mediators' lists that is published in the corresponding section of the BOE (Spain Official Gazette) website, which is prepared by the Registry of Mediators and Mediation Institutions of the Ministry of Justice.

A specificity envisaged by Art. 233.1 of the Insolvency Act is the probability that a legal person becomes an insolvency mediator. In this case, the mediation is conducted by the mediators appointed by it.

The mediator appointed by a Notary or the Commercial Registrar needs to verify the existence and the amount of debts within ten days after accepting the position. Within the two following months, he/she has to summon the debtor and the creditors that might be affected by the agreement. The summoning must be conducted through the Notary and the meeting should be held at the debtor's domicile. In the summon, the following items have to be included: a) that the goal of the meeting is to reach a payment settlement, b) the amount owed to each creditor, and c) the date when the loans were agreed and when they are due, and the guarantees established.

The holders of loans secured by a pledge, mortgage or antichresis might expressly communicate to the mediator, within one month of the summon reception, their will to act in the agreement. Silence is interpreted as exercising their right to restrain from participating at the out-of-the-court agreement.

Filing a case does not prevent debtors to continue their activity (Art. 235.1 Insolvency Act). However, their capacity to act is restricted. On the other hand, while negotiations of the agreement are in progress, the debtor cannot be declared insolvent, unless the circumstances under Art. 5bis of the Insolvency Act (Art, 235.6 Insolvency Act) occur.

After the publication of the mediation case file start, and for a maximum period of three months after publication, the creditors affected by the out-of-the-court agreement are not able to start or continue any execution on the debtor's equity, as the negation of said agreement is under way. Moreover, during the same period creditors must restrain from conducting any act to improve the situation they face concerning the debtor. Creditors whose loan is secured by a security right are excluded from the previous rule.

One of the legal effects of the annotation of the out-of-the-court agreement negotiation file at public registries where the debtor's goods are registered is the closing of these registries for foreclosures or further seizures with retroactive effect to the presentation of the request to appoint an insolvency mediator.

Seizures or confiscations agreed during processes at the request of public right creditors of the debtors are excluded from the previous rule, as well as those started by creditors with collateralised guarantees that had to restrain from participating in the out-of-the-court agreement.

Insolvencymediators, at least twenty calendar days before the meeting, have to submit the to the creditors, with the previous consent of the debtor, a payment Plan of the amount due to the date of the request.If arrears or a waiting period is considered, this could not be longer than three years, and if a haircut is proposed, it could not be of more than 25% of the total amount due. The Plan should be accompanied by a "Feasibility Plan" containing a proposal to meet all the new obligations, and an amount is also included as food for the debtor and his family, and a "continuation plan" of his professional or business activity. Likewise, a "negotiation proposal" must be done dealing with the conditions of the debtor's credits and loans. Creditors can present alternative or modification proposals to the agreement proposal, and can express their total or partial approval or rejection of the proposal. Then, the mediator submits the payment plan and final feasibility plan approved by the debtor to the creditor. When the creditors who represent most of the liabilities that would be affected by the agreement decide to stop negotiations, the mediator has to "immediately" request a consecutive insolvency procedure.

At the meeting between the creditors and the mediator and the debtor, all alternative or modification of the Plan proposals will be dealt with as well as the reasons to oppose to it. However, when some of the creditor accepts the Plan within 10 days before the meeting, and if the creditor does not attend the meeting, the payment conditions accepted by this creditor cannot be altered.

Likewise, during the meeting, the approval of the Plan is addressed. For this to occur, the favourable vote of the creditors holding at least 15% of the liabilities is required when the Plan does not consist in transferring the goods of the debtor to service his debts.

If the Plan is approvedit must be notarised in a Public Deed. When the file has been started before the Commercial Registrar, a copy of the Deed containing the Settlement has to be presented, containing also the approval of the Plan, for the Registrar to close the file.

The closing of the case file is communicated by the Notary or by the Registrar to the Court that would have processed it, and also, to the Registries of Public Goods so that they can proceed to cancel all the annotations they might have done.

The Out-of-the-court Agreementis then published at the BOE (Spain Official Gazette) as well as at the Insolvency Public Registry.