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Reform of the Insolvency Law 2010

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Due to the effects of the recent economic crisis, the need arose to make it easier for insolvent companies to continue their business through a restructuring. Up until now there has been the Bankruptcy Act (*Konkursordnung* – KO) alongside with the Composition Act (*Ausgleichsordnung* - AO) in Austria.

The Reform of the Insolvency Law 2010 (*Insolvenzrechtsänderungsgesetz* 2010 - IRÄG 2010) has brought a uniform Insolvency Act (*Insolvenzordnung* – IO). The Composition Act that governed composition proceedings aiming at a settlement between the insolvent debtor and its creditors was repealed.

The compulsory settlement (*Zwangsausgleich*) that made such a settlement also possible in the course of a bankruptcy proceeding will disappear. Instead new restructuring proceedings are implemented into the IO. The amendment entered into force on July 1 2010.

Besides that, one will have to get used to numerous new terms: the trustee (*Masseverwalter*) is now called the insolvency administrator (*Insolvenzverwalter*), the creditors of a bankrupt estate (*Konkursgläubiger*) will be called the creditors of an insolvent estate (*Insolvenzgläubiger*), and so forth.

New restructuring instruments

The composition proceedings under the old Composition Act enabled the restructuring of the company by self-administration of the debtor. However, the debtor had to provide for a minimum quota of 40% payable within the next two years. Therefore, composition proceedings under the Composition Act had fallen in a sleeping beauty slumber.

In 2009 there had been only 39 judicial compositions overall – as opposed to several thousand bankruptcy proceedings. Hence, in general insolvent companies were restructured by way of compulsory settlement (minimum quota required being 20% payable within two years). This had the disadvantage that no self-administration was possible, which was a hindrance to restructuring. The IO now provides the following new restructuring instruments.

Self-administration by the debtor

A diligently elaborated restructuring plan has to be filed together with the application to open insolvency proceedings. The minimum quota is 30% payable within two years. The debtor keeps the self-administration only being supervised by a restructuring administrator appointed by the court.

Administrator appointed by court

If the Debtor is not able to provide the minimum quota of 30% (but of 20%) payable within the two years time, he is still allowed to file a restructuring plan together with the opening application. In this case the court appoints an insolvency administrator and the restructuring proceedings will be processed without self-administration of the debtor.

Settlement in bankruptcy proceedings (formerly the compulsory settlement)

The debtor will still be able to attain the restructuring of the company in the course of bankruptcy proceedings and even upon the application of a creditor by offering the creditors a restructuring plan. For this purpose the debtor also has to pay at least 20% of the debts within two years and the creditors have to approve the restructuring plan in the restructuring hearing by simple majority.

Restrictions on the termination of contracts

A further important alteration introduced by the IRÄG 2010 is the restriction of the creditors' rights to terminate contracts with the debtor when insolvency proceedings are opened. Up until now many of the creditors exercised this right. However, in particular the termination of lease contracts, energy supply and telephone contracts may hinder the restructuring of the company considerably.

The IRÄG 2010 shall facilitate the continuation of insolvent companies and their restructuring. If the termination of a contract may harm the continuation of the company, henceforth the creditor may only terminate the contract within six months after the opening of the insolvency proceedings upon good cause shown. The deterioration of the debtor's financial situation and the non-fulfilment of a claim that became due before the opening of the insolvency proceedings are not to be considered as a good cause.

These restrictions do not apply on the termination of employment contracts, on the entitlement to the disbursement of a credit (which is important for banks) and when the termination of the contract is essential for the avoidance of severe personal or economical detriments of the contractual partner. Such a severe personal or economic detriment will be given in any case where the creditor is also threatened with insolvency. This leaves scope for interpretation that does not add to legal certainty.

Restrictions on eviction executions

On continuation of the company an eviction execution due to outstanding arrears of rent of the time before the opening of the insolvency proceedings is inadmissible, if the administrator makes a corresponding application.

Advance of costs by majority shareholders

A total of 864 company insolvencies were opened in the first quarter of 2010. In 740 cases the courts rejected the opening due to lack of assets. In order to reduce the number of such rejections, majority shareholders that hold more than 50% of the company are in the future obliged to provide an advance of costs.

Conclusion

The IRÄG 2010 causes significant changes with regard to the restructuring of insolvent companies. The legislator had given preferential consideration to the interests of the debtors. This leads to a deterioration of the creditors' position. The adoption of the new restructuring instruments in practice remains to be seen.

Please note that the information provided above only summarises the main aspects of the issues addressed and is not complete, nor is it necessarily up to date. It cannot replace advice on individual cases.