

Spain

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SECURITY AND PRIORITIES

1. What are the most common forms of security granted in relation to immovable and movable property? Are any specific formalities required for their creation and perfection (that is, made valid and enforceable)?

Immovable property

The most common types of security for immovable property are:

- **Mortgage (*hipoteca inmobiliaria*).** Under a mortgage, legal title to the property passes from the debtor to the creditor but possession does not. Legal title passes back to the debtor once the debt is repaid. A mortgage must be registered with the Land Register where the property is registered. If the debtor defaults on repayment of the debt, the creditor can enforce its rights through summary proceedings. During enforcement, the creditor can ask the court to administer the assets.
- **Pledge (*antichresis*).** Under a pledge, the debtor assigns revenue from the property to the creditor as security for debt. If the debtor defaults, the creditor can take possession of the pledged property to recover the debt (unless the contract expressly excludes this). The creditor can also ask the court for the property to be sold to recover the debt.

Movable property

The most common types of security for movable property are:

- **Chattel mortgage (*hipoteca mobiliaria*).** This is a mortgage over chattels. The mortgage must be registered with the Chattel Mortgage and Non-Possessory Pledge Registry (*Registro de Hipoteca mobiliaria y Prenda sin desplazamiento*).
- **Possessory pledge (*prenda posesoria*).** Under this pledge, the pledged asset is placed under the creditor's control. If the debtor defaults, the creditor can begin enforcement proceedings to sell the asset and recover the debt from the proceeds.
- **Non-possessory pledge (*prenda sin desplazamiento*).** With this pledge, the pledged asset remains in the debtor's possession and the creditor's interest is protected through registration of the right at the appropriate registry. There are certain specific obligations and restrictions imposed on the debtor related to the preservation, movement and disposal of the asset.

Formalities

Mortgages and non-possessory pledges must be granted by public deed and registered with the registry where the affected assets are registered. Registration creates a security right. If registration does not occur, the creditor has no right against any third party that acquires the relevant secured asset.

2. Where do creditors and shareholders rank on the insolvency of a company?

Creditors are ranked in the following categories (*Articles 89 to 92, Insolvency Act 22/2003 (Ley Concursal) (Insolvency Act)*):

- **Preferential creditors (*créditos privilegiados*).** These creditors are divided into two subcategories:
 - **Creditors with special privileges (*créditos con privilegio especial*).** This subcategory includes:
 - construction or repair creditors (*créditos refaccionarios*). For example, employees may be able to recover wages owed to them by the sale of assets they have manufactured which are owned by the debtor (employer) or are in the debtor's possession;
 - creditors with rights in property (limited to the secured amount);
 - creditors under financial lease agreements or sale and purchase agreements where the debtor repays the debt in instalments;
 - creditors with interests in book-entry securities;
 - creditors to whom property has been transferred.
 - **Creditors with general privileges (*créditos con privilegio general*).** This subcategory includes:
 - employees owed wages who do not have special privileges;
 - employees with indemnities arising from the termination of employment contracts, workplace accidents and professional illnesses, as well as debts owed for breaches of occupational health and safety obligations (if accrued before the declaration of insolvency);
 - employees owed amounts relating to tax and social security withholdings;
 - contractors and authors of intellectual property works who have assigned exploitation rights in their work in return for payment, if accrued in the six months before declaration of insolvency;
 - employees with up to 50% of the amounts owing on tax and social security claims as well as any other public debts, if they do not enjoy any other preferential treatment;
 - claims for non-contractual civil liability;

- creditors with up to 25% of the debt owed who petitioned for the insolvency of the debtor, provided the relevant debt owed is not subordinated.
- **Ordinary creditors (*créditos ordinarios*).** Creditors with debts that cannot be classed as privileged or subordinated (see *below*) are ordinary debts.
- **Subordinated creditors (*créditos subordinados*).** Creditors with debts which are considered subordinated debts are those:
 - reported late or inappropriately (that is, where there is a failure to report them within the statutory period);
 - treated as subordinated as a result of a contractual agreement, such as participative or subordinated loans;
 - relating to an interest of any kind, except those arising from rights in property, up to the limit stated in the guarantee;
 - owed to shareholders holding at least 5% (for companies listed on a recognised stock exchange) or 10% (for unlisted companies) of the company's share capital, or by any person related to the creditor (as defined in Article 93 of the Insolvency Act);
 - relating to any claim made in bad faith.

Although not covered by the Insolvency Act, there are other privileged debts, including:

- **Legal tacit mortgages (*hipoteca legal tácita*).** These relate to real estate taxes payable on immovable property for the previous financial year.
- **Super privileges granted to employees.** The last 30 days' wages owed to employees have priority over any other debt owed, including those relating to mortgages or any other creditors with rights in property.

3. Are there any mechanisms used by trade creditors to secure unpaid debts?

In addition to security rights in property (see *Question 1*), trade creditors can use credit rights (*garantías de crédito*) to secure unpaid debts. The most common credit rights are:

- **Bail (*fianza*).** A third-party guarantor (*fiador*) undertakes to pay or perform on the debtor's behalf, if the debtor is unable to do so. Joint and several guarantees (*fianza solidaria*) are common. These allow the creditor to enforce its credit right against the debtor or the guarantor, or against both at the same time.
- **Credit risk insurance (*seguro de caución*).** Under a credit risk insurance contract, the insurer pays the creditor if the debtor (who is the policyholder) defaults. If this occurs, the insurance company ranks the creditor's position in front of the debtor.
- **Lien (*derecho de retención*).** This mechanism allows the creditor to retain possession and control of property until the debtor repays its debt. It differs from a pledge because the creditor does not have the right to sell the property on default, but is entitled to hold the property until the debt is repaid.
- **Penalty clause (*cláusula penal*).** A penalty clause is frequently included in a contract. If the debtor defaults, a fixed sum must usually be paid as liquidated damages. These clauses can be declared void by the Insolvency Court.

4. Are there any procedures (other than the formal rescue or insolvency procedures described in *Question 6*) that can be invoked by creditors to recover their debt?

Provided insolvency proceedings have not begun, any creditor can bring the following civil actions against the debtor:

- **Ordinary proceedings.** These are used to obtain an order to make the debtor comply with a particular ruling or to seize the debtor's assets for an amount sufficient to let the creditor recover the debt owed and claim for damages. Court resolutions can be enforced immediately.
- **Monetary process (*proceso monitorio*).** These are brief proceedings that allow the creditor to recover amounts up to a maximum of EUR30,000 (about US\$43,100) (EUR150,000 (about US\$215,500) from May 2010), provided the debt is stated in a document.
- **Special proceedings for bills of exchange (*juicio cambiario*).** This is an action used to recover debts that are covered by bills of exchange, cheques or promissory notes.
- **Special proceedings to execute unpaid pledges and mortgages (*procedimiento de ejecución sobre bienes hipotecados o pignorados*).** This is a procedure used to enforce mortgages or pledges over assets. It can be started even if the debtor is involved in insolvency proceedings, but receivers may ask for a stay of a year if the affected property is used to carry on the activity of the company.

STATE SUPPORT

5. Please give brief details of the availability of state support for distressed businesses (if any).

Apart from agreements between distressed companies and the state, the Insolvency Act does not provide any specific mechanism of state support.

RESCUE AND INSOLVENCY PROCEDURES

6. Please briefly describe rescue and insolvency procedures available in your jurisdiction. In each case, please state:

- The objective of the procedure and, where relevant, prospects for recovery.
- How it is initiated, when, by whom and the companies it can be applied to.
- Substantive tests that apply (where relevant).
- How long it takes.
- The consents and approvals required.
- The effect on the company, shareholders and creditors.
- How the procedure is formally concluded.

Insolvency proceedings (*concurso*)

This is the only procedure that affects both individuals and legal entities.

- **Objective.** The aims of the proceedings depend on whether the debtor is being rescued or liquidated (bankruptcy):
 - **Rescue (*convenio*).** The objective is to restructure the debt to allow the debtor to continue operating. The debtor makes an arrangement with creditors to reduce its debt over a certain period of time, up to the limitations set by the Insolvency Act (a debt reduction of not more than 50% and/or a stay of proceedings of not more than five years);
 - **Liquidation (*liquidación*).** The objective is to sell the assets of the debtor company to repay as much of the debt owed to the creditors as possible.
- **How, when, by whom and to which companies.** The procedure begins with filing an insolvency petition with the Commercial Court (*Juzgado de lo Mercantil*) of the capital of the province in which the debtor has its centre of main interest (COMI). For legal entities, COMI is the place where the entity's registered office is located. Insolvency applies to both individuals and to legal entities. The Insolvency Act also has provisions covering the insolvency of groups of companies. Public bodies cannot be declared bankrupt. There are also special provisions for insurance companies or banks that become insolvent.

If insolvency proceedings are voluntary (*concurso voluntario*), the directors or liquidators must file the insolvency petition. If they are compulsory (*concurso necesario*), the insolvency petition can be filed by:

- a creditor, provided the company is deemed to be currently insolvent (*see below, Substantive tests*);
- shareholders who are personally liable for the company's debts, provided the company is currently, rather than imminently, insolvent (*see below, Substantive tests*).

An insolvency petition must be filed in writing and accompanied by certain documents (which may vary depending on who the petitioner is and if the insolvency is imminent or current).

A company must apply for insolvency within two months of the date on which it becomes aware, or should have become aware, that it is insolvent. The Insolvency Act sets out a series of situations in which the company is deemed to have knowledge of insolvency.

There is no time limit in which a creditor or shareholders must file an insolvency petition, provided the objective grounds for insolvency are met (*see below, Substantive tests*).

The declaration of insolvency must be published in the *Oficial State Gazette (Boletín Oficial del Estado)*. It must also be registered with the Registry for Insolvency Proceedings (*Registro de Procedimientos de Insolvencia*).

- **Substantive tests.** An insolvency petition can be filed if a company is unable to pay its debts as they become due (current insolvency) or if it foresees that this will happen in the near future (imminent insolvency).

If a company files an insolvency petition, it must provide evidence of its debts and its current or imminent insolvency.

If a creditor files an insolvency petition, it must be based on one of the following grounds:

- the company has failed to pay debts when they became due;

- the creditor cannot exercise its security rights because the company's assets have been seized;
- the company has disposed of or liquidated assets to put them beyond creditors' reach;
- the company has defaulted on one of the following in the three months before the insolvency petition is filed:
 - tax liabilities;
 - social security contributions;
 - salaries and indemnities related to employees.

- **How long.** It is difficult to estimate how long insolvency proceedings will take, but 12 to 20 months is usual, depending on the complexity of the case. A shorter procedure (*procedimiento abreviado*) is available to companies authorised to file short form annual accounts, and with debts below EUR10 million (about US\$14.4 million). If this procedure is used, the statutory time limits set out in the Insolvency Act are reduced by one-half.

- **Consents and approvals.** If the debtor has requested liquidation, an arrangement with its ordinary creditors must be reached and approved by the creditors at a creditors' meeting as well as by the court. The agreement can also be reached in writing (without holding a creditors' meeting).

The debtor or its creditors can make an arrangement proposal. If made by the company and liquidation is not required, the proposal can be put forward before the end of the period in which the creditors must submit proof of their claims (*convenio anticipado*). This proposal may provide for termination of the proceedings by fast track. If the anticipated arrangement is not put forward by the debtor, the debtor or the creditors can propose a suitable expiration period for contesting the inventory of assets and list of creditors. Privileged creditors are not affected by an arrangement and the debtor must reach separate agreements with each of these. They can also join the arrangement but if they do, they lose their preferential status and are subject to the proposed debt repayment structure. Creditors with subordinated debts or debts acquired after insolvency is filed cannot vote on the arrangement.

An arrangement is approved if at least one-half the ordinary creditors representing more than one-half of the total debt vote in its favour. However, if the total value of debts owed to ordinary creditors voting in favour of the arrangement is greater than the total value of debts owed to ordinary creditors voting against the arrangement, it can be approved if either:

- the agreement provides for ordinary debts to be repaid in full within three years;
- the agreement provides for ordinary debts to be repaid immediately with a write-off of less than 20%.

The agreement approved by creditors must be confirmed by the court if both:

- statutory requirements are met;
- no creditor objects to the arrangement or, if an objection is made, it is rejected by the court.

No consents or approvals are required if a company is to be liquidated. The company can request liquidation itself or it

starts automatically if no agreement is proposed in the due term, or is rejected.

■ **Effect.** Insolvency proceedings have the following effects:

- in a voluntary insolvency, directors remain in their positions and the company continues managing its assets, subject to the supervision of the receivers (*administradores concursales*), unless the court forces it to be treated in the same way as a compulsory insolvency (see below);
- in a compulsory insolvency, receivers take over the administration of the company's assets, unless the court orders it to be treated in the same way as a voluntary insolvency, and therefore the directors remain in their positions (see above);
- unless the company asks for liquidation, its business does not usually cease on insolvency (see Question 9). If the receivers are merely supervising, they determine the activities and transactions that can continue to be managed by the company in the ordinary course of business. If the receivers take over the management of the business, they must take the necessary steps to ensure that its commercial activities continue;
- during insolvency proceedings, shareholders continue to function as usual, but receivers can attend and have the right to be heard at their meetings. The same applies for the board of directors' meetings;
- once a company has been declared insolvent, a list of creditors is prepared and creditors are ranked according to the priority of their debts (see Question 2);
- debts of ordinary creditors and subordinated creditors are not paid until the agreement is approved and ordinary and privileged creditors are fully repaid, or until the company is wound up;
- any proceedings (see Question 4) that a creditor may wish to bring against the insolvent company that could affect its assets must be dealt with by the insolvency judge;
- once an insolvency order has been made, no arbitration proceedings can be started;
- if court and arbitration proceedings have already begun, they continue until the judgment or award becomes final and binding;
- no individual judicial or extra-judicial enforcement actions can be brought against the company's assets, and actions that have already begun are stayed from the date of the declaration of insolvency. However, there is an exception for creditors with a security interest in property over assets of the company that are used in its commercial activities. These creditors can bring enforcement proceedings from the date on which the composition agreement is approved or after one year of the insolvency order if the liquidation has not begun;
- the company's debts cannot be set off against monies owed to it;
- no interest accrues, other than interest on debts that have a legal guarantee;

- the limitation period for actions relating to debts that pre-date the insolvency is postponed during insolvency proceedings;
- contracts with mutual obligations that have not yet been performed remain in force, although the creditor can terminate them if the company defaults;
- clauses allowing a contract to be terminated if an insolvency is declared are void;
- during the liquidation, the company cannot administer or dispose of its assets;
- creditors must submit proof of their claims within one month of the court's decision to start insolvency proceedings.

■ **Conclusion.** Insolvency proceedings end if:

- the court declares that the conditions of the debtor's arrangement with the creditor have been fully met;
- the Court of Appeal (*Audiencia Provincial*) revokes the insolvency declaration;
- actions for breach of the agreement have been declared lapsed or rejected by the court.

In addition, insolvency proceedings end regardless of the stage they have reached (provided the receivers have prepared their report and the relevant parties have attended court), if:

- all recognised debts are repaid or the creditors are satisfied in full by other means;
- it is proved that the company has no assets to repay its debts and no party is liable for this lack of assets;
- once the list of creditors has been drawn up, all creditors agree to write off the company's debts and the court accepts this decision.

Out-of-court restructuring (*refinanciación*)

In March 2009, insolvency was reformed to include out-of-court refinancing proceedings.

- **Objective.** Out-of court refinancing proceedings allow the debtor to reach an agreement with the majority of its creditors to increase the available credit or to modify its obligations to avoid insolvency court proceedings.
- **How, when, by whom and to which companies.** These proceedings are started exclusively by the debtor. The debtor must obtain the agreement of a minimum number of creditors which represents at least 60% of the total due.
- **Substantive tests.** The out-of-court restructuring proceeding is exclusively filed by the debtor. The restructuring agreement must be approved by a creditor's majority representing 60% of the total due (see above, *How, when, by whom and to which companies*).
- **How long.** Not applicable.
- **Consents and approvals.** The restructuring agreement must include a viability plan and, if the debtor wants it to remain out of reach of eventual avoidance actions, it must be countersigned by an independent expert and granted in a public deed. The restructuring agreement must be approved by a

creditor's majority representing 60% of the total due (see above, *How, when, by whom and to which companies*).

- **Effect.** The restructuring agreement provides for modification of the debtor's total available credit or the debtor's obligations, and when it is approved by the required majority, it affects all the creditors. This allows the company to avoid insolvency court proceedings provided the debtor observes the agreement's provisions.
- **Conclusion.** The restructuring agreement allows the debtor to avoid insolvency court proceedings (provided the debtor observes the agreement's provisions). However, if the debtor does not achieve this agreement, there is no other solution than the insolvency petition (see above, *Insolvency proceedings (concurso)*).

7. What type of stakeholder has the most significant role in the outcome of the restructuring?

In a voluntary insolvency, directors have the most significant role because they remain in their positions and the company continues to manage its assets. However, they need the receiver's authorisation for any act related to their economic activity. The receivers can grant prior and general authorisation for certain acts to expedite the continuation of the debtor's managerial activity.

In compulsory insolvencies, the receiver's role is more significant because they take over the administration of the company's assets. In these types of insolvencies, the receivers must adopt all necessary measures related to the continuation of the professional debtor's activity.

In either case, the receiver's role is essential because restructuring operations cannot be approved without their consent. In any case, restructuring proceedings require the debtor's collaboration, who must appear in court every time he is summoned by the receivers or the judge.

LIABILITY AND TRANSACTIONS

8. Are there any circumstances in which a director, parent company (domestic or foreign) or other party can be held liable for the debts of an insolvent company?

Directors' liability is very strict and this is reflected in insolvency proceedings. When directors have not run the company properly, or they have not filed for insolvency within the term set by law, they risk being declared liable for the company's debts.

Liability may also arise if a company's insolvency was caused or aggravated by its directors' or liquidators' recklessness or gross negligence. This liability affects not only the appointed directors but also the de facto directors. This can have a serious effect when a group of companies becomes insolvent.

If the court finds that directors have acted in bad faith, it can disqualify them from managing companies for two to 15 years. It can also require liable parties (or anyone who committed the same offence in the two years before the declaration of insolvency) to

repay creditors all or part of any debt that is not recovered from the insolvent estate.

If shareholders and the company are liable for the company's debts before insolvency (for example, when shareholders' liability is not limited, such as in the case of collective companies (*sociedades colectivas*)), receivers or creditors can bring an action against the shareholders. They can also bring an action for the payment of unpaid capital.

If there are not enough assets in the insolvent estate to repay all debts and liability has been declared (or is likely to be declared), a seizure of assets can be ordered against:

- Directors, liquidators or anyone performing the same functions as directors or liquidators in the two years before the insolvency order is made, if it is probable that they were responsible for causing the insolvency.
- Shareholders who were liable for the company and its debts before the insolvency.

9. Can transactions that are effected by a company that subsequently becomes insolvent be set aside?

Generally, insolvency does not affect the validity and effectiveness of any existing contracts. However, receivers and creditors can bring an action for reintegration (*acciones de reintegración*) to restore the company's property and rights where they were disposed of, to the damage of the remaining creditors' interests. This is done by setting aside acts that have been detrimental to the estate and which the company has carried out in the two years before the declaration of the date of insolvency, even if there was no fraudulent purpose.

Receivers can also ask the court to cancel agreements that may be detrimental to the company, taking into consideration any indemnity for damages payable to the other contracting party.

Acts performed in the company's ordinary course of business on standard conditions cannot be set aside.

10. Please set out any conditions in which a company can continue to carry on business during insolvency or rescue proceedings. In particular:

- Who has the authority to supervise or carry on the company's business?
- What restrictions apply?

See *Question 6, Insolvency proceedings (concurso): Effect*.

The receiver must supervise the company's ordinary business and its use of funds. However, the company can enter into any transactions necessary to continue business, without the receiver's prior approval.

At the receiver's request and in exceptional cases, the court can order some or all the company's offices to be closed down and its commercial activities to be suspended or stopped.

INTERNATIONAL CASES

11. Please state whether:

- Courts in your jurisdiction recognise insolvency and rescue procedures in other jurisdictions.
- Courts co-operate where there are concurrent proceedings in other jurisdictions.
- There are any international treaties relating to insolvency to which your jurisdiction is a signatory.
- There are any special procedures that apply to foreign creditors.

- **Recognition.** Regulation (EC) No. 1346/2000 on insolvency proceedings (Insolvency Regulation) is applicable in Spain. Spain is also party to the United Nations Commission on International Trade Law (UNCITRAL) Model Law on Cross-Border Insolvency 1997 and the Insolvency Act incorporates this.

According to Article 17 of the Insolvency Regulation, the declaration of insolvency must, without further formalities, produce the same effects in any other member state that would apply under the law of the state where the proceedings began. This means that court decisions in one member state concerning the opening, conduct and closure of insolvency proceedings must be immediately and automatically recognised by all other member states.

However, the Insolvency Act requires foreign judgments to comply with certain formalities (under the *exequatur* procedure) before they can be recognised (*Article 220*), including that the:

- insolvency has been declared by a foreign court;
- foreign court's decision is final and binding;
- decision is adopted by the court where the debtor's COMI is located;
- decision is not illegal under Spanish law.

Generally, Spanish courts are required to apply reciprocity when recognising foreign insolvency decisions.

- **Concurrent proceedings.** If there are concurrent proceedings relating to the same group of companies, receivers in Spanish insolvency proceedings must co-operate with receivers in the foreign proceedings.
- **International treaties.** No bilateral treaties apply.
- **Procedures for foreign creditors.** The following procedures apply in relation to foreign creditors:

- receivers must notify foreign creditors of the insolvency;
- the court, on its own initiative or at the request of the receivers or of any interested party, can order decisions made during insolvency proceedings to be published in a foreign jurisdiction (in recognition of the fact that certain laws, provisions and acts in Spain must be published in the *Official Gazette*, the official state journal);
- foreign creditors must submit proof of their debts to the receivers in Spanish;
- foreign creditors can submit proof of their debts in Spanish proceedings, regardless of whether they have also submitted proof of them in a foreign procedure. If there is a reciprocal arrangement between Spain and the foreign jurisdiction, foreign creditors can submit proof of fiscal and social security debts. These rank as ordinary debts in Spain (*see Question 2*);
- if insolvency proceedings have begun in Spain and a creditor is fully or partially paid with assets located in a foreign jurisdiction, the creditor must repay the money to the company's estate;
- if a creditor is partially paid during foreign proceedings, the creditor cannot demand any other payment in the Spanish proceedings until other creditors of the same rank have been proportionally paid; and
- in the Spanish proceedings, foreign receivers (*see above, Concurrent proceedings*) can submit proof of debts that have been recognised during the foreign procedure (to the extent that this is allowed under foreign law). Foreign receivers can also participate in Spanish proceedings on behalf of creditors for whom they have submitted proof of debts.

PROPOSED REFORMS

12. Please summarise any proposals for reform and state whether they are likely to come into force and, if so, when.

During 2010, a general reform of the Insolvency Act is expected to be submitted to Parliament, but the details are still unknown.

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