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Subject:	Proposal for a Directive of the European Parliament and of the Council harmonising certain aspects of insolvency law - Comments from Malta on Titles I-VI of the Commission proposal

Delegations will find in annex the comments from Malta on Titles I-VI of the Proposal for a Directive of the European Parliament and of the Council harmonising certain aspects of insolvency law.

ANNEX

MALTA - Comments on Titles I – VI of the Proposal for a Directive harmonising certain aspects of insolvency law (hereinafter referred to as the "Proposal") (ST 15896/23)

General Comments

Malta still holds a general scrutiny reservation on the entire proposal since national internal consultations are ongoing; and as such, the following comments are being made without prejudice to Malta's final position.

Title I (General Provisions)

Malta notes that **Article 1(2)(h)** of Directive (EU) 2019/1023 (the "Insolvency Directive") excludes from the scope of the directive all natural persons who are not entrepreneurs. Article 1(4) of the Insolvency Directive then gives the option to Member States to extend the application of debt discharge procedures to insolvent natural persons who are not entrepreneurs. On the other hand, with regards to debt discharge procedures, Article 1(2)(h) of this Proposal extends the applicability of the Proposal to natural persons who are not entrepreneurs but who are founders, owners or members of unlimited liability microenterprise debtors and who are personally liable for the debts of the debtor.

We would therefore like to question whether the extension of this provision beyond the scope of the Insolvency Directive is intentional and indeed lawful, especially since Article 56 of the Proposal makes it mandatory (not optional) on Member States to adopt the procedures of Title III of the Insolvency Directive for non-entrepreneurs (founders, owners or members of micro-enterprises).

Our suggestion is to delete the wording "and, with regard to debt discharge procedures, those founders, owners or members of unlimited liability microenterprise debtors who are personally liable for the debts of the debtor" from Article 1(2)(h), which should read "**natural persons who are not entrepreneurs**."

Article 2(f) - With regards to the definition of "legal act", Malta believes that the Proposal gives a very narrow definition and should also include acts *capable of producing a legal effect*.

Article 2(j) – In view of our comments regarding Title VI, Malta proposes the removal of the definition of "microenterprise".

Article 2(k) – In view of our comments regarding Title VI, Malta proposes the removal of the definition of "unlimited liability microenterprise".

Article 2(m) – In view of our comments regarding Title VI, Malta proposes the removal of the definition of "full discharge of debt".

Article 2(n) – Malta proposes the deletion of the definition of "repayment plan" since this terminology is not used anywhere else in the Proposal.

Title II (Avoidance Actions)

Malta currently has no equivalent legislation to **Article 6** (particularly paragraphs 1 and 2), however we believe that these provisions would be beneficial to the insolvency proceedings.

The closest our law comes to these provisions is in the fraudulent preference provisions in Article 303 of the Companies Act, whereby any act which dispossesses the property or rights of the company made in the period of six months prior to the dissolution of the Company, shall be deemed as fraudulent preference against its creditors if it is made gratuitously or at an undervalue or if preference to any creditor is given. A person who benefits from such disposition is personally liable in terms of the Companies Act.

However, Malta believes that the timeframe of three months (referred to in Article 6) prior to the submission of the request for the opening of insolvency proceedings may be too short. At Maltese law, fraudulent preferences can be deemed if the act is done within six months before the dissolution of the company. Considering that in Malta, the deemed date of dissolution can precede the date of the winding up application, we believe that a period of three months from the date of opening of insolvency proceedings, as proposed by Article 6(1) is unnecessarily short and might be detrimental to creditors. We understand that this period is intended to be a minimum period, (in view of minimum harmonisation), but suggest that this is made more explicit in the text in order to be clear that Member States may impose a lengthier period.

Regarding the presumption in **Article 6(2)** (which presumption can be found also in other Articles) that a creditor who is closely related to the debtor is presumed to have had knowledge of the substantive insolvency of the debtor, we understand from recital 12 that such presumption could be rebutted. However, this point does not seem to emerge from the operative part of the text. Article 303 of the Maltese Companies Act allows the opportunity for the person in whose favour the preferential act is made, to prove that he did not know and did not have reason to believe that the company was likely to be dissolved by reason of insolvency. Thus, Malta suggests that the point made in recital 12 (that such presumptions are rebuttable) should be included in the operative part of the text. Likewise, with reference to Article 8(1), Malta suggests the inclusion of the possibility of rebuttal of the presumption of knowledge of the debtor's intent to cause a detriment to the general body of creditors.

Malta supports the general intention of **Article 8**, given that it is qualified by the pre-requisite that the third party must have had knowledge of the debtor's intention to cause a detriment to the general body of creditors. Malta's only concern relates to the proviso to **Article 8(1)**, where there is a presumption of knowledge (of the debtor's intention to cause detriment) by a third party if such third party is closely related to the debtor. Given that this article refers to legal acts perfected within a period of four years prior to the opening of insolvency proceedings, this presumption is very strict and may have a wide scope of application.

With regards to **Articles 6, 7 and 8**, Malta believes that the wording *"submission of the request for the opening of insolvency proceedings"* is misleading, since it is our understanding that the winding up application automatically entails the opening of insolvency proceedings. Malta suggests that this wording is substituted with the words *"opening of insolvency proceedings"*.

Title III (Tracing Assets Belonging to the Insolvency Estate)

Article 14 - Malta has a centralised bank account registry pursuant to Article 32a of Directive (EU) 2015/849, now the 5th AML Directive, which is currently administered by the Financial Intelligence Analysis Unit (FIAU).

The directive proposes that a designated court is given direct and immediate access and search powers to this information, and **Article 14(4)** provides that "access and searches shall be considered to be direct and immediate where the national authorities operating the central bank account registries transmit the bank account information expeditiously by an automated mechanism to the designated courts, provided that no intermediary institution is able to interfere with the requested data or the information to be provided." Malta believes that this new role of the court runs contrary to the underlying tenets of national law. In Malta, courts have a strict adjudicatory role, as opposed to an investigative function in the civil sphere. Therefore, if the competent court is required to obtain direct access and carry out searches in the centralised bank account registry itself, we believe that the court will be acting outside the remit of its functions and consequently such a search may be inadmissible in proceedings.

We believe that the implementation of Chapter 1 of Title III should not be problematic for Malta, if an automated system is put in place thereby enabling the FIAU (or some other designated administrative authority) to transmit the relevant information to the designated court in a timely manner and adequate logs are kept each time an access and search has been performed.

Malta would prefer more flexibility in Article 14 and for it to be amended so as to include the possibility of the information being presented to the court, on demand, by other authorities who currently have access to the centralised bank account registry.

Title IV (Pre-Pack Proceedings)

Malta currently has no equivalent legislation and has serious doubts as to whether including pre-packs as one of the alternative options would in the end be beneficial. The closest our law comes to these provisions is with regards to the provisions of the Pre-Insolvency Act (Chapter 631 of the Laws of Malta) and the preventive restructuring procedures contemplated therein; and the company recovery procedure regulated by Article 329B of the Companies Act (Chapter 386 of the Laws of Malta), where our legislation provides tools how the financial and economic situation of the company can be improved in the interests of its creditors, employees and of the company itself as a viable going concern.

The pre-pack proceedings of Title IV, regulate a scenario where the debtor's business or part thereof is sold as a going concern under a contract that is negotiated confidentially prior to the commencement of an insolvency proceeding under the supervision of a monitor appointed by a court and followed by a brief insolvency proceeding, in which the pre-negotiated sale is formally authorised and executed and there is no national legislation equivalent to these proceedings. However, at a national level, "restructuring" in terms of the Pre-Insolvency Act includes the sale of a business as a going concern.

Malta is concerned with the confidentiality element required in the preparation phase and whether this can be accommodated within the Maltese legal framework, considering that these proceedings will be held in court. Open court proceedings are the standard mode of procedure and proceedings are only conducted behind closed doors in exceptional circumstances.

Article 27 – With regards to the assignment of executory contracts, Malta reserves its position given discussions are still ongoing locally in relation to the definition of executory contracts in general. However, the automatic assignment of executory contracts contemplated in Article 27 may conflict with the generic laws regulating contracts in Malta, particularly with Article 961 (1) of the Civil Code, which expressly states that "A contract is synallagmatic or bilateral when the contracting parties bind themselves mutually the one towards the other." In the scenario of Article 27, where the assignment can take place even without the consent of the debtor's counterparty, we believe that the requirement at Maltese law that the parties are binding themselves "mutually the one towards the other" would essentially be missing.

Title V (Directors' Duty to Request the Opening of Insolvency Proceedings and Civil Liability)

With regards to Title V, no equivalent provision obliging directors to submit a request for the opening of insolvency proceedings with the court is currently present in Maltese law. In terms of the Maltese Companies Act, where the directors become aware that the company is unable to pay its debts or is imminently likely to become unable to pay its debts, they shall convene a General Meeting of the company by means of a notice to that effect for a date not later than forty days from the date of the notice (which notice must be issued not later than thirty days from when the fact became known to them) for the purpose of reviewing the company's position and to determine the next steps that should be taken. Such steps would usually involve either the dissolution of the company or some form of restructuring.

Additionally, Maltese law provides that where a company has been dissolved and is insolvent and it appears that a director of the company knew, or ought to have known prior to the dissolution of the company that there was no reasonable prospect that the company would avoid being dissolved due to its insolvency, such director may be held liable to make a payment towards the company's assets at the discretion of the court. Under Maltese law, directors may also incur liability when proper accounting records are not kept by the insolvent company or when fraudulent trading results.

Thus, it would be our preference to have Article 36 (and consequently Article 37) worded in a more flexible manner to cater for our legal framework where creditors themselves can file for insolvency proceedings. It is Malta's position that creditors should have access to the appropriate information so that they are given the option to file for insolvency proceedings when they deem fit.

Title VI (Winding-up of Insolvent Microenterprises)

With regards to Title VI, Malta proposes the deletion of this title and the corresponding references to "*simplified winding up proceedings"*. Considering the small size of the Maltese economy, and given that many Maltese companies involved in insolvency proceedings or which are in the likelihood of insolvency possibly fall within the definition of a microenterprise within the meaning of the Annex to Commission Recommendation 2003/361/EC, this matter would need to be given specific attention as it may result in a situation where the simplified procedure would not be an exception to the rule but a widely used alternative. Maltese insolvency law does not consider the size of the company undergoing dissolution and winding up proceedings when it comes to the applicability of the provisions regulating the proceedings, and we believe that this approach should be retained.

While understanding the intention of Title VI to provide the smallest enterprises with less costly insolvency proceedings, Malta believes that there is not much added value in the proposed procedure for simplified winding up proceedings since it might lead to negative ramifications. A simplified procedure for microenterprises lacks many of the safeguards of this proposed directive, mainly in relation to the protection of the rights of creditors and the insolvency estate in general. Also, the fact that the insolvency practitioner is only required in certain instances and if certain conditions are fulfilled (Article 39) is concerning, in the sense that, the insolvency practitioner's function is an important one especially because they work closely with the debtor in supporting the liquidation process and protecting the liquidation estate to achieve a better outcome for creditors.

Malta believes that Titles V and VI cannot be regarded as a tool of minimum harmonisation and may lead to a disruption in the established basic principles.