

Lex Covid - A brief overview of insolvency-related measures

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The outbreak of COVID-19 and the measures adopted to prevent the spread of the infection are already having a negative impact on many companies and entrepreneurs. Many are now facing liquidity issues and a sharp drop in demand for their goods and services, and some have been forced to close down their business.

On April 9, 2020, the Chamber of Deputies of the Parliament of the Czech Republic adopted statutory changes in the regulation of insolvency proceedings, to provide relief for distressed businesses and provide protection for entrepreneurs and companies in financial difficulties caused by the outbreak of COVID-19 and the government measures taken to limit its spread. The proposed statutory changes also include a general restriction on creditors' insolvency petitions that will affect creditor-driven insolvency resolutions of those debtors who became insolvent prior to the outbreak.

The proposed changes will have to be countersigned by the President. Lex Covid should enter into force by mid-April 2020.

Proposed Measures

The key measures introduced by Lex Covid include the introduction of an extraordinary moratorium, suspension of debtor's obligation to file for insolvency, suspension of creditors' rights to file for insolvency, suspension of debt enforcement and protection for companies undergoing reorganization proceedings through optional suspension of fulfillment of the reorganization. In addition, it introduces certain measures in the personal bankruptcy proceedings plan as well as limitations to service of process and limit of appurtenances accrued between 12 March and 30 June 2020.

Extraordinary moratorium

All companies, negatively influenced by the governmental measures taken in connection to the COVID-19 pandemic, will have a right to apply for a special moratorium until August 31, 2020. A debtor can file the application prior to commencement of its insolvency proceedings or within 15 days of a creditor's insolvency petition.

Unlike ordinary moratorium, the special moratorium will not have to be supported by a majority of creditors and the court will grant it to a debtor which:

- Was not insolvent as of March 12, 2020;
- Is facing problems as a direct consequence of the governmental measures taken in connection to the COVID-19 pandemic; and
- Has not paid extraordinary profit shares or other payments to its owners since January 12, 2020.

The special moratorium can last for up to 3 months and can be prolonged by 3 months, if the majority of creditors agrees.

The special moratorium will provide the debtor with similar rights and duties as a regular insolvency moratorium and the case will be made public in the insolvency register.

The debtor can prioritize payments of debts originating within the moratorium period over older debts and can make use of debtor-in-possession financing.

Suspension of the obligation to file for insolvency

The statutory obligation to file for insolvency on behalf of the insolvent debtor will be suspended until 6 months after the end of emergency measures, but no later than on December 31, 2020.

This intended suspension, however, does not apply generally. Only companies which had not been insolvent before the measures were introduced, and the insolvency of which is a direct consequence of those measures, can apply for this suspension. All other companies and their directors still have the obligation to file for insolvency, otherwise they expose themselves to the risks of liability for damages to the creditors.

Suspension of rights of creditors to file for insolvency

No insolvency petitions filed by creditors until August 31, 2020 will be taken into account. There is no exception to this rule and no connection to the government measures or the pandemic situation has to be established.

Measures related to personal bankruptcy proceedings

In all personal bankruptcy proceedings, including those initiated before May 31, 2019, the court shall not terminate the proceedings even if the debtor is not able to meet a substantial part of the payment calendar, if the inability to do so is caused by the governmental measures.

All debtors in personal bankruptcy proceedings can have their debts terminated even if they do not pay off 30% of their debts, if their failure to do so is linked to the governmental measures taken in connection to COVID-19.

Optional suspension of fulfilment of the reorganization plan

Debtors in reorganization proceedings, that had their reorganization plan approved as of March 12, 2020, can ask the court for a suspension of fulfilment of the reorganization plan. The fulfilment of the plan can be suspended until 6 months after the end of emergency measures, but no later than December 31, 2020. The court will decide after considering representations from the insolvency trustee and the creditor's committee.

During the suspension, the reorganization proceedings cannot be turned into a bankruptcy liquidation. The debtor, however, still has to fulfil its obligations other than those arising under the reorganization plan.

Suspension of hardening periods

Hardening periods to challenge debtors' legal acts detrimental to its creditors are postponed up to 6 months after the end of emergency measures, but will continue no later than from December 31.

Relief from the effects of time limit expiration

Any party to insolvency proceedings, that missed a time limit in insolvency proceedings due to a circumstance related to the COVID-19 pandemic, can ask the court for a relief from the effects of the time limit expiration. Such a request must be filed within 7 days after the limitation is removed, but no sooner than 7 days after the emergency status is lifted.

Limited service

During the period ending 12 months after the end of governmental measures taken in connection with the COVID-19 pandemic, court decisions will not be served to persons who have the right to appeal. Creditors must therefore monitor the insolvency register more carefully.

Limitation of appurtenances

If a debtor fails to pay a monetary payable due between 12 March and 30 June 2020, the overall amount of all secondary claims (default interest, contractual penalties etc.) must not exceed the statutory default interest rate. This limit will have to be taken into account when calculating amounts of claims.

Our comments

The proposed measures are supposed to help the economy and protect subjects negatively influenced by the pandemic and related governmental measures. Most of those measures are therefore limited to these subjects and the proposed reliefs are contingent on direct negative causes of the pandemic and related governmental measures.

However, this is not the case of the suspension of rights of creditors to file for insolvency. This suspension applies regardless of whether the insolvency of their debtors is related to the pandemic, and therefore appears to be rather disproportional and inefficient. The ministry offers all dishonest debtors a free pass until August 31, 2020. Limiting the suspension only to debtors directly influenced by the pandemic that had not been insolvent up to March 12, 2020 would be a preferable and more proportional solution.

If you have any additional inquiries, please do not hesitate to contact us.

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