A&O SHEARMAN

Restructuring across borders
Finland

CORPORATE INSOLVENCY PROCEEDINGS | FEBRUARY 2024

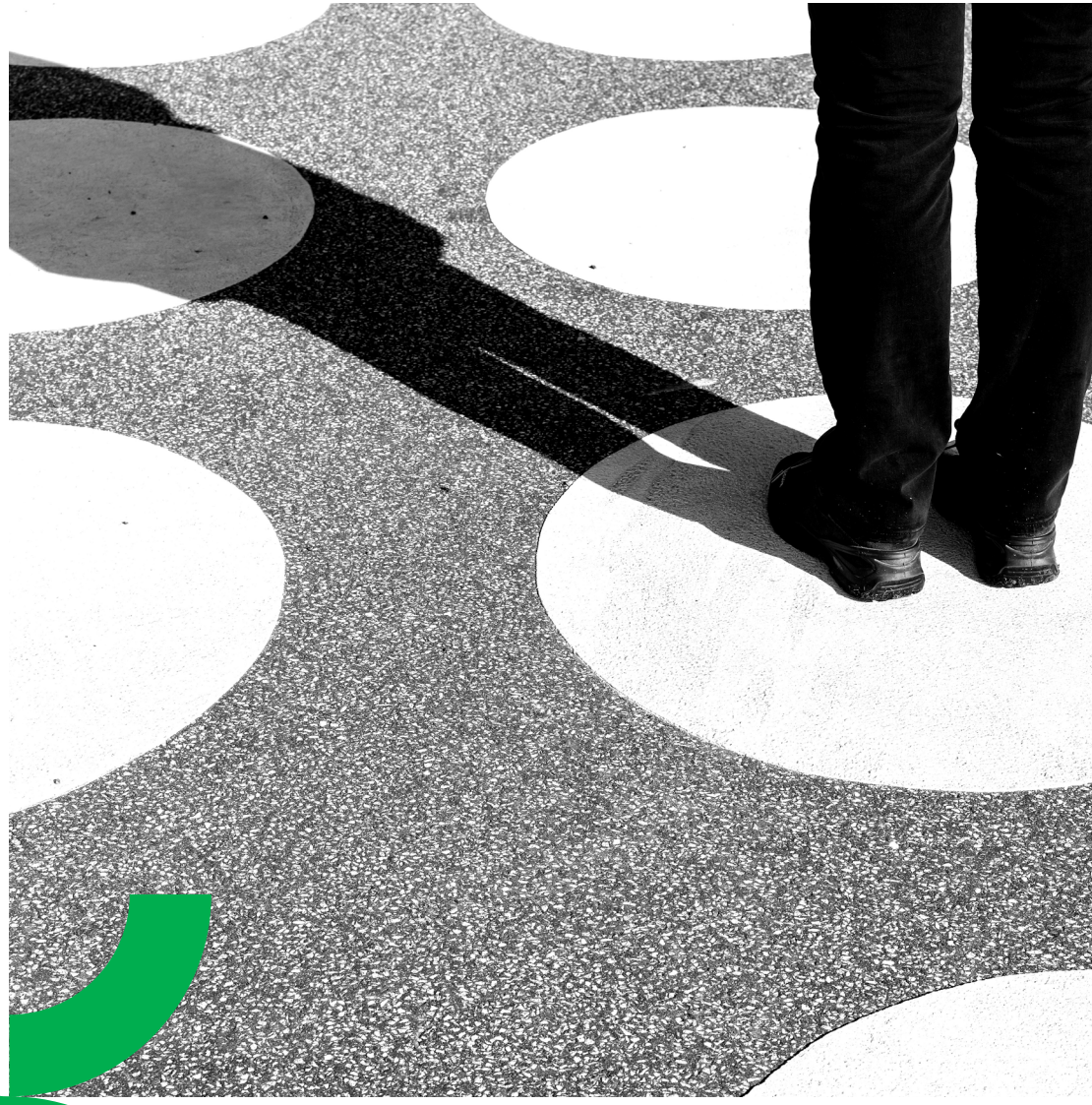
Contents

Introduction

There are three possible types of liquidation, restructuring and insolvency proceedings under Finnish law: (i) liquidation, (ii) company restructuring (which comprises early and regular restructuring proceedings), and (iii) bankruptcy. The availability and choice of proceedings is dependent on the circumstances of each individual company and the intention of the proceedings.

The following presentation gives a brief overview of the aforementioned restructuring and insolvency proceedings and briefly discusses also group level insolvency proceedings, out-of-court debt arrangements as well as recovery of assets ("clawback").

This presentation is of a general nature and does not purport to be exhaustive, and it does not cover legal issues beyond those expressly provided. This presentation is confined solely to matters relating to the laws of Finland as of the date of this presentation. This presentation is not an equivalent of a Finnish law legal opinion and does not constitute legal advice.



Liquidation

The purpose of liquidation proceedings is to ascertain the company's financial position, to convert the requisite amount of assets into cash, to repay the company's debts, and to return the surplus to the shareholders or other parties as provided in the company's Articles of Association. The liquidation does not involve court proceedings.

The starting point in liquidation is the assumption that the company's assets exceed its liabilities. Liquidation cannot be successfully carried out if the company is over-indebted or insolvent. The decision to start liquidation proceedings can be made in the General Meeting of the company. The liquidation is carried out by one or several liquidator(s) (selvitysmies) appointed by the General Meeting. The liquidator acts in lieu of the board of directors and the managing director and reports to the company's shareholders.

There is no moratorium with respect to the commencement of liquidation proceedings. The liquidator applies for a public summons to the company's creditors after the proceedings have commenced. Once the due date of the public summons to the company's creditors has passed and all of the company's known debts have been repaid, the liquidator shall distribute the company's assets to the shareholders or other parties as provided in the company's Articles of Association.

The liquidator manages the affairs of the company during the liquidation. Their task is to convert into cash enough of the assets of the company so that the liquidation can proceed, as well as repay the debts of the company. The business operations of the company may be continued only to a degree called for by an appropriate liquidation process. Placing a company in liquidation has no effect on the validity of a company's contracts.

The company's liquidation leads to its dissolution or, if the company's assets are not sufficient to cover all of its liabilities, the company's bankruptcy.

Company restructuring proceedings

Restructuring proceedings may be initiated in a company that is in risk of becoming insolvent or is insolvent, but its insolvency can be remedied by means of a restructuring. In formal proceedings, the applicable law is the Finnish Restructuring of Enterprises Act (laki yrityksen saneerauksesta, hereafter the "Restructuring Act").

After the implementation of the so-called EU Insolvency Directive, there have been two alternative, parallel proceedings: early company restructuring (varhainen saneerausmenettely) and regular company restructuring (perusmuotoinen saneerausmenettely). The former is intended to be a more easily attainable, expedited option when a debtor is facing insolvency but has not yet become insolvent. The latter is applicable when the debtor is insolvent, but the insolvency is remediable.

While there are differences between these two proceedings, the underlying principle remains the same. The purpose of both early and regular company restructuring proceedings is to investigate whether it is possible for the business or a part thereof to continue and, if so, to rehabilitate the company's viable business, to ensure its continued viability, and to arrange its debts. The means of restructuring are materially the same in early and regular proceedings.

There are fewer prerequisites and barriers for initiation and continuation of early restructuring proceedings than for the regular restructuring. The main prerequisite for initiating early restructuring proceedings is that the company in question is facing a risk of insolvency. Hence insolvent debtors are limited in choice to regular restructuring proceedings (or bankruptcy). If circumstances change during the early restructuring proceedings the court may, on application, decide to transfer from early to regular proceedings.

Only the debtor may apply for early restructuring proceedings. Regular restructuring proceedings can be initiated upon application of the debtor company or its creditor(s). If there are no barriers to initiate restructuring proceedings, the court approves the application and appoints a restructuring administrator.

Upon the commencement of the restructuring proceedings, or a separate court decision, a moratorium enters into force. The moratorium consists of interdictions protecting the prerequisites of restructuring and include, among other things, interdictions of repayment, debt collection and enforcement measures. In regular restructuring proceedings interdictions remain in force until the end of the restructuring proceedings, whereas in early restructuring proceedings the interdictions may remain in force for a maximum of 12 months, which also creates a practical time limit for the early proceedings.

After the commencement of the proceedings, the debtor retains its authority to dispose of its property and to decide on its activities, insofar as not otherwise provided in the Restructuring Act. However, after the commencement of the proceedings the debtor cannot perform certain legal acts without the consent of the administrator.

As a main rule, contracts entered into by the debtor company remain in force, but there are some exceptions, which allow the debtor to terminate disadvantageous contracts, for example. Also, so-called insolvency clauses, i.e. contracts, agreements and terms by which the parties have agreed upon the effects of insolvency or aim to avoid or circumvent the effects of insolvency proceedings, are not effective in restructuring.

A restructuring may include liquidating the debtor's assets partly – or in rare cases even entirely (restructuring by liquidation). In addition, consignment stock arrangements, retention of title and other similar arrangements may become under scrutiny to assess their validity in restructuring.

Company restructuring proceedings (cont.)

In restructuring proceedings, the debtor's debts are divided into restructuring debt and new debt. Restructuring debt is based on the time preceding the date when the restructuring application was filed. The moratorium, more specifically the interdiction of repayment, prevents the repayment of restructuring debts, and they can be subjected to debt arrangements. Debts arising on the application date and thereafter are normal debt and need to be treated as such, i.e. repaid as they become due.

Apart from some exceptions prescribed in the Finnish Restructuring Act, restructuring creditors will receive repayment on their restructuring receivables in accordance with a restructuring programme. Restructuring receivables are subject to various debt arrangements, which include changing the payment schedule or order of payment or reducing the balance or obligation to pay interest of restructuring debt. As a starting point, creditors with normal, unsecured restructuring receivables shall be treated equally and are entitled to equal repayment in relation to the amount of their receivables.

Secured creditors are in a special position in restructuring: they cannot enforce their security but they are entitled to full payment in the restructuring programme up to the value of the security (the rest is unsecured debt and subject to cuts). Also, lowest-priority restructuring debt cannot receive payment unless all the other restructuring debts of higher priority are repaid in full. Exceptions to these rules may be made only with the injured party's (or parties') consent.

The draft restructuring programme will be drawn up by the restructuring administrator and the court will affirm it upon the approval of all of the creditors or with the acceptance of the majority in each of the groups of creditors. Even if the majority does not exist in one or several groups of creditors, the restructuring programme may nonetheless be approved at the request of the administrator, or the debtor, subject to the conditions specified in the Restructuring Act (cross-class cramdown).

The restructuring proceedings end with the court affirmation of the restructuring programme, after which the implementation of the restructuring programme begins.

Bankruptcy

If a debtor fails to pay its debts when due and the incapacity of paying said debts is not temporary, the debtor is considered insolvent for bankruptcy purposes. Under certain conditions a bankruptcy application may then be filed with a court by the debtor or a creditor. If the application is approved, the court orders the bankruptcy (konkurssi) to commence. The applicable law in Finnish bankruptcy proceedings is the Bankruptcy Act (konkurssilaki).

The purpose of bankruptcy proceedings is to dissolve the company by selling all of its assets and distributing any possible surplus to the company's creditors. Bankruptcy is an insolvency proceeding covering all of the debtor's liabilities, where the debtor's assets are used to pay the claims in the bankruptcy.

In order to achieve the purpose of bankruptcy, the debtor's assets become subject to the creditors' authority at the beginning of the bankruptcy. The creditors are represented by an estate administrator (pesänhoitaja) appointed by the court. The estate administrator consults with and reports to the creditors' meeting (velkojainkokous). The right to exercise the creditors' authority belongs to the bankruptcy creditors. The creditors exercise their authority in the creditors' meeting and makes decisions on a vote per euro principle. The creditors may also establish a creditors' committee, an advisory body that assists the estate administrator and supervises his or her activities.

In practice, the estate administrator consults with concerned (major) creditors or the creditors' committee (if one is appointed by the court) on all important matters and submits them for a final decision by the creditors' meeting.

All of the bankrupt company's assets belong to the bankruptcy estate, and the right to dispose of said assets is transferred to the estate administrator(s) appointed by a court. The bankruptcy estate may (exceptionally) continue with the company's business operations but as a starting point the debtor's assets will be sold as soon as reasonably possible.

In order to be entitled to a disbursement, a creditor must lodge a claim in a bankruptcy in writing (a letter of lodgement), by delivering it to the estate administrator no later than on the lodgement date set forth by the estate administrator. However, there are certain specific exceptions in the Bankruptcy Act, pursuant to which a claim may be taken into account without being lodged. Retroactive lodgement is also possible, usually against a charge. A lodgement is required also in the realisation of security and set-off of receivables.

During the proceedings, the estate administrator drafts a disbursement list, and, if it meets the requirements set out in law, the court affirms the list. As a starting point, unsecured creditors have an equal right to receive payment from the net funds of the bankruptcy estate in the proportion of the amount of their claims (on a pro rata basis).

However, secured creditors have precedence over unsecured creditors to receive their claims and may use their so-called separatist rights to realise their security. Lowest-priority claims may receive payment only if claims of higher priority receive full payment.

As a main rule, the disbursement of funds takes place after all of the debtor company's assets have been realised and the debtor company's affairs have been settled. The assets of the bankruptcy estate are disposed of in the most advantageous manner in order to maximise the aggregate net proceeds, including through auctions, advertising, and direct solicitation of potential buyers. However, secured creditors may exercise a so-called separatist right to liquidate their collateral despite the bankruptcy proceedings in accordance with the provisions of the Bankruptcy Act and the limitations set therein.

The starting point is that the debtor company's contracts are not binding towards the bankruptcy estate. The bankruptcy estate has a right to choose whether to accede to or to terminate a contract entered into by the debtor, with some exceptions. Also, so-called insolvency clauses, i.e. contracts, agreements and terms by which the parties have agreed upon the effects of insolvency or aim to avoid or circumvent the effects of insolvency proceedings, are not effective in bankruptcy. The bankruptcy estate may also continue the debtor's court processes at its discretion, if this is deemed profitable.

Group insolvency proceedings

There is no legislation regarding group insolvency proceedings in Finland. Bankruptcy and restructuring proceedings are applicable on individual companies alone. However, in practice there have been proceedings involving groups of companies.

In bankruptcies, the debtor's group structure can be considered less relevant because the proceedings usually end with the dissolution of the companies. Each company has its own assets and debts, which also means resolving intra-group debts and receivables.

Taking into account the interests and necessities of a group may be relevant in group restructuring. The basic premise is that the restructuring applications, proceedings and programmes are considered individually, i.e. on a per company basis. However, restructuring programmes may include group-level instructions and harmonization of programmes.

In group bankruptcies or restructurings, the same person may act as the bankruptcy estate administrator or restructuring administrator of all group companies. If case of conflicts of interests between the group companies, resolving questions may then need to be outsourced to other insolvency practicioners.

Out-of-court debt arrangements and pre-pack proceedings

Out-of-court debt arrangements mean any voluntary restructuring of debts made outside formal insolvency proceedings. Pre-pack proceedings include an arrangement involving the sale of all or a part of the debtor's business which is effected shortly after the formal proceedings start in the form of a pre-planned restructuring programme.

The purpose of out-of-court arrangements is to minimize the negative effects of insolvency proceedings in the company's (or group's) business. Some of the downsides 9 are that out-of-court debt arrangements and pre-pack proceedings usually involve only select creditors and arrangements can be made only on a voluntary basis. Often success cannot be guaranteed beforehand, and informing creditors of difficulties may agitate their behaviour or look for formal options. Also, out-of-court arrangements require time but do not get the benefit of a moratorium by virtue of law. In pre-pack proceedings there is no moratorium for the duration of the pre-pack negotiations and arrangements preceding the formal proceedings.

Out-of-court restructuring and pre-pack proceedings are relatively common in practice even though, as of the time of writing, there is no legislation regarding pre-pack proceedings in Finland. This may change with a future EU insolvency directive.

Recovery of assets ("clawback")

Under Finnish law, recovery ("clawback", takaisinsaanti) is governed mainly by the Act on the Recovery of Assets to a Bankruptcy Estate (laki takaisinsaannista konkurssipesään, hereafter the "Recovery Act").

The Recovery Act regulates the recovery of legal actions or actions that are fraudulent or preferential or otherwise detrimental to the creditor collective made by the debtor within a certain time before bankruptcy, restructuring proceedings or distress. The Recovery Act has been formulated based on bankruptcy proceedings but is applied mutatis mutandis to restructuring proceedings and distress.

The grounds of recovery apply to a wide range of transactions that are to the detriment of creditors and comprise both subjective (requiring mala fide) and objective (irrespective of fide) grounds.

The most important grounds for recovery are gifts and agreements with the characteristics of a gift, the payment of debts (by unusual means, prematurely or in a considerable amount in relation to the assets of the estate) and the recovery of pledges and other securities as well as setoffs. Furthermore, the general grounds of recovery allow the recovery of a wide range of inappropriate legal acts (including transactions and transfers of assets, contracts and even passiveness) which were made by an insolvent debtor or which led to the insolvency of the debtor. Any recovered acts must be detrimental to the creditors: a legal act causing no damage to creditors cannot be recovered.

Legal acts between so-called close parties (i.e. parties within the debtor's sphere of interest) are subject to an increased risk of recovery, due to e.g. different preconditions of recovery, longer recovery times and/or a lighter burden of proof for the claimant.

Key contacts

If you require advice on any of the matters raised in this document, please contact any of our partners or your usual contact at A&O Shearman, or email **rab@aoshearman.com**

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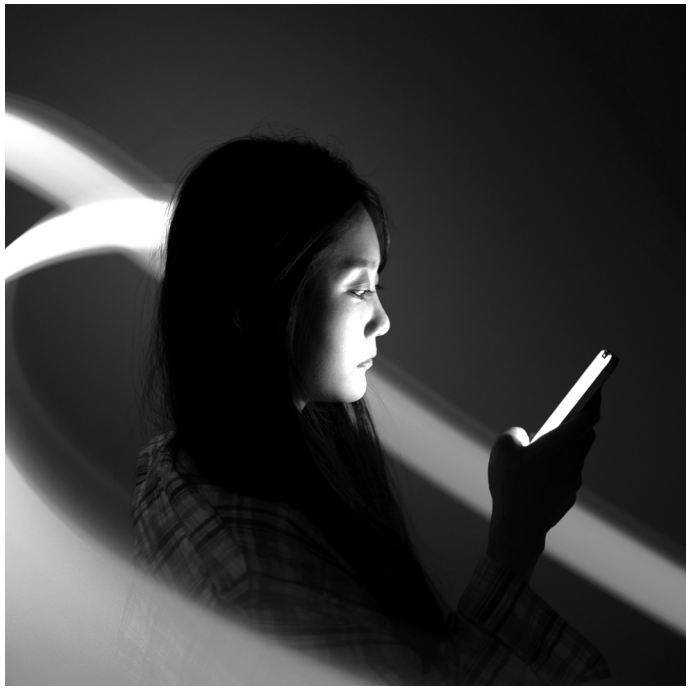
Further information

Developed by A&O Shearman's market-leading Restructuring group, "**Restructuring Across Borders**" is an easy-to-use website that provides information and guidance on all key practical aspects of restructuring and insolvency in Europe, Asia, the Middle East and the U.S.

To access this resource, please **click here**.



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