A&O SHEARMAN

Restructuring across borders
Iceland

CORPORATE RESTRUCTURING AND INSOLVENCY PROCEDURES | MARCH 2025

Contents

Introduction

This factsheet contains general information concerning the legal framework in Iceland which applies to restructuring companies and insolvency.

The principal restructuring and insolvency regimes for companies under the Icelandic Bankruptcy Act no. 21/1991 ("Bankruptcy Act") are:

- Moratorium (*greiðslustöðvun*)
- Composition (*nauðasamningar*)
- Bankruptcy (*gjaldþrot*)

Moratorium

A company that cannot pay its debts when they fall due can apply for a suspension of payments or "moratorium" with a relevant District Court, which will then issue a court order provided that there is some possibility that the company can reorganise its finances with the help of a special assistant, i.e. an attorney or a certified public accountant hired by the company for that purpose. The goal of a moratorium is twofold: (1) to overcome the company's financial difficulties so that it can fulfil its obligations, and/or (2) help the company enter bankruptcy earlier so that assets are then available to creditors to a greater extent. In this way, the interests of both the company and the creditors are taken care of.

During the moratorium period the company is not allowed to dispose of assets and rights or incur liabilities, unless with the consent of the special assistant and where there is legal authorisation for the disposal under the Bankruptcy Act, e.g. authorisation to fulfil certain obligations if it is necessary to prevent significant damage to the company. Moreover, during this period the company's creditors cannot take advantage of remedies due to the company's non-compliance, e.g. creditors cannot initiate enforcement actions against the company. However, the moratorium does not prevent creditors' claims from accumulating interest or fines being imposed due to the company's non-compliance.

An application of moratorium is only available to the company itself and therefore creditors can never directly induce a moratorium. If the criteria are met, a district judge shall grant a moratorium for three weeks initially. After the initial three week period the company can apply for an extension for up to three months and then apply for a second extension also for up to three months. The maximum period for a moratorium of a company is however six months and three weeks.

As soon as a moratorium has been granted, the company's special assistant shall convene a creditors' meeting no later than three days before the initial moratorium period expires. At this meeting, the assistant shall provide detailed information on the assets and liabilities of the company and present his opinion on how the company's finances can be restructured as well as informing the creditors whether an application for an extension of the moratorium will be filed. The assistant will furthermore seek the opinion of the creditors regarding his plans; however, no registration of creditors' claims is required concerning as part of a moratorium.

Composition

Under the Bankruptcy Act, composition with creditors is an agreement on the settlement or cancellation of debts concluded between a debtor and a certain majority of his creditors, which is subsequently confirmed in court. A composition agreement is also binding upon the debtor's other creditors, regardless of their will, if a certain majority of creditors in number and value confirm the agreement. The purpose of a composition is to try to bring about a reorganisation of the finances of the debtor. A composition agreement may provide for total cancellation of debts, proportional cancellation of debts, deferred dates of payment, changes in form of payment or a combination of the latter three.

Composition is only available to the debtor. He must file a petition with a relevant District Court which includes a written declaration of at least 1/4 of the voting creditors (as determined from the enumeration of liabilities in the petition, both by number and value) that they recommend composition based on the debtor's proposal. Such a proposal must among other things specify, to what extent the debtor offers payment of the composition claims. After the District Court has received such a petition it shall without undue delay issue a court order stating whether a license to seek composition with creditors is granted and if so, it shall also appoint an administrator to carry out the preparations for composition.

The composition administrator shall, immediately following his appointment, inspect the debtor's financial situation and take any measures necessary for commencing control and supervision of the debtor's finances with full cooperation of the debtor. The composition administrator shall then issue a recall in the Legal Gazette for all known creditors to register their claims with the administrator within four weeks of the notice. In addition, all known creditors shall receive a special notification thereof.

Composition (cont.)

A creditors' meeting to vote on a debtor's composition proposal shall be held within four weeks 'of' the expiry of the four-week recall period. A composition proposal shall be deemed approved if supported by the same proportion of votes as the proportion of composition claims to be cancelled according to the proposal, provided this reaches 60% at a minimum, by a number of voting creditors as well as value. If neither proportional nor total cancellation is proposed, a composition proposal shall be deemed approved if supported by at least 60% of all voting creditors by number as well as value. Should the proposal, for example, provide for the cancellation of 70% of claims, it would therefore need the support of 70% of all voting creditors by number and value.

If the composition procedure has ended with approval of the debtor's proposal, the debtor shall submit a written petition for confirmation of the composition agreement to Court within one week after this conclusion was announced at a creditors' meeting. If the Court agrees to the composition, it shall be binding upon the creditors and their successors and assignees.

A composition agreement has the same effect as a court settlement between the debtor and its creditors on the claims stated on the creditors' list by the compositions administrator, insofar as these were not challenged by the debtor. However, a composition agreement does not affect the right of a creditor to obtain satisfaction through a security which a third party may have provided for performance or to claim payment in full from a guarantor. Lastly, not all claims would be affected by a composition. Claims that would be considered priority claims under bankruptcy proceedings are not affected by a composition agreement. Accordingly, claims are secured upon the debtor's assets, to the extent the value of the relevant asset covers the claim, and the security interests are not affected by the composition.

Bankruptcy

Bankruptcy is when an insolvent debtor is deprived of his assets and other financial rights by a Court order, which goes to another legal entity, the debtor's estate, which is governed by a court-appointed liquidator. Bankruptcy is a joint enforcement measure of all creditors in their interest with the aim of bringing the estate assets to a financial value and that the proceeds will be used to pay the claims of the debtor's creditors.

There are essentially two tests applied in determining whether the condition for placing a company into bankruptcy are met, (a) a test in determining whether the debtor has sufficient cash available to satisfy his debts when they become due (cash flow test) and (b) a test in determining whether a debtor has sufficient assets to cover outstanding debt (balance sheet test).

A debtor may file for bankruptcy if he is unable to honour his debts to his creditors in full when they become due, provided it is not deemed likely that his payment difficulties will be over within a short period of time. However, a debtor who is obliged to keep accounts, e.g. a limited liability company, has the duty of filing a petition for bankruptcy if either of the above-mentioned scenarios has occurred. Therefore, under the Bankruptcy Act and Public Limited Liability Companies Acts the board of a company can incur liability towards the creditors of a company if it fails to file for bankruptcy when the conditions are fulfilled.

A creditor can also petition for a debtor's bankruptcy in certain circumstances, e.g. if unsuccessful or only partially successful attachment or debt enforcement proceedings have taken place against the debtor, provided the debtor does not establish that he is nevertheless capable of honouring his financial obligations in full when they become due, or will become capable of doing so within a short period of time.

During the bankruptcy, the liquidator has custody of the estate and is solely responsible for managing its interests and being responsible for its obligations. He appears on behalf of the estate in court and makes contracts and other legal documents in its name. All claims against an estate automatically fall due upon the announcement of the District Court judge's decision that the debtor's estate shall be declared bankrupt, regardless of what may have been previously agreed upon or determined in another way.

The estate's liquidator shall issue and publish a notice to creditors announcing the bankruptcy, the notice which shall be published in the Legal Gazette. The notice shall include a call upon any creditor and others, who maintain that they have a claim against the estate, to declare their claims to the liquidator by sending or delivering their statements of claim digitally, electronically or on paper within the period determined for that purpose in the notice (generally two months, can be longer in exceptional circumstances).

The general principle under Icelandic bankruptcy law is that if a claim against an estate is not stated to the liquidator before the time provided for in the notice to creditors expires, it is cancelled with respect to the estate. Moreover, the status and priority of claims submitted by creditors in bankruptcy proceedings differs depending on the type of the claim e.g. claims which are secured by collateral or other security interest in the estate's assets are prioritised over general claims.

The Bankruptcy Act contains provisions enabling the liquidator to seek clawback by having measures undertaken by the debtor rescinded. Such measures include gifts, transactions at an undervalue, salary 'payments'", repayment of debt, creation of security over unsecured debt, and any other improper measures.

European insolvency regulation

The European Insolvency Regulation has not been implemented into Icelandic law as Iceland is a member of the European Economic Area, not the European Union, and the European Insolvency Regulation is not included in the EEA agreement.

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**.

This factsheet has been prepared with the assistance of BBA//Fjeldco. Any queries under Icelandic law may be addressed to the key contacts from BBA//Fjeldco listed below:

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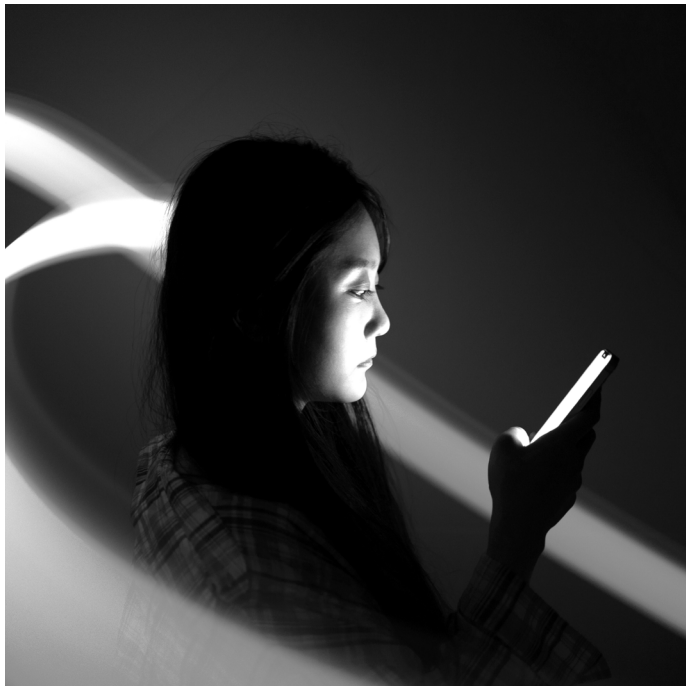
Further information

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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