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Global Restructuring & Insolvency Guide

Austria

Overview and Introduction

On 1 July 2010, the Austrian Bankruptcy Reform Act (the "**IRÄG 2010**") entered into force. With this reform, the insolvency regime in Austria was considerably changed. Up to that point, the Austrian Insolvency Law was divided into two separate regimes: bankruptcy and reorganisation. Accordingly, commercial entities and private individuals were either subject to the Bankruptcy Act (*Konkursordnung*) or to the Settlement and Reconciliation Act (*Ausgleichsordnung*). This dual system has now been replaced by a unitary system: the insolvency proceedings (*Insolvenzverfahren*) under the Insolvency Proceedings Act (*Insolvenzordnung*).

The aim of this Guide is to give an overview of the insolvency regime and to highlight the significant changes to bankruptcy and reorganisation proceedings brought in by the IRÄG 2010.

Applicable Legislation

Insolvency Act

The insolvency regime in Austria is primarily governed by the Insolvency Proceedings Act (the "**Insolvency Act**" or "**IA**"), which provides the legislative framework for bankruptcies and reorganisations of commercial (legal) entities and private individuals. With respect to legal entities, both limited and unlimited partnerships, companies and − according to the Austrian Supreme Court − even municipalities are subject to insolvency proceedings.

Business Reorganisation Act

Besides the Insolvency Act, the Business Reorganisation Act of 1997 (*UnternehmensReorganisationsgesetz*; the "**Business Reorganisation Act**") governs the reorganisation of businesses. Since it is applicable only to certain cases of reorganisation and, in particular, since it lacks to a very large extent any practical relevance, this act is not covered in this Guide.

Insolvency Act

Background

As mentioned above, on 1 July 2010 the IRÄG 2010 entered into force. Its main purposes are to simplify the legislative framework as such, to facilitate the initiation of insolvency proceedings, to accelerate decisions on the opening of insolvency proceedings and to reduce the number of cases in which insolvency proceedings cannot be opened in the absence of sufficient funds. Furthermore, the uniform structure of one single type of insolvency proceeding − instead of (as existed previously) a dual structure of bankruptcy and restructuring − makes it possible to achieve different aims in one single proceeding (see below for further details).

Meaning of the Term "Insolvency"

Under both the former Bankruptcy Act and the currently effective IA, the opening of insolvency proceedings requires either the "illiquidity" (section 66 of the IA) or the "over-indebtedness" (section 67 of the IA) of the debtor. While section 66 is applicable to any debtor, under section 67 insolvency proceedings in cases of over-indebtedness can only be initiated for legal entities, estates or registered partnerships without a personally liable partner. For initiating proceedings for restructuring,[1] it is also

[1] See "Restructuring Proceedings and Restructuring Plan" below.

sufficient if the illiquidity of the debtor is not already existent but is impending (section 167(2) of the IA).

The IA does not provide for a definition for the terms "illiquidity" or "over-indebtedness". The terms have been substantiated by case law as follows:

> *"A person is deemed illiquid when this person due to a lack of available funds is not able to pay its due and payable debts and the debtor will not be in the position to gain sufficient funds shortly."*
>
> *"A company is deemed over-indebted if payable and non-payable receivables together exceed all assets of the debtor and the prospect for the company's going concern is negative."*

Under these preconditions, insolvency proceedings may be initiated at the request of either the debtor[2] or the creditor.[3]

Corporate Insolvency

Whilst the following overview is predominantly related to corporate insolvency, the specific regulations for private insolvency are also outlined below.

Debtor's Petition

Upon voluntary petition of the debtor to the insolvency court, the insolvency proceedings have to be immediately opened. In cases of illiquidity or over-indebtedness, the debtor is obliged to apply for the opening of insolvency proceedings without culpable delay, but in any event not later than 60 days after the occurrence of the debtor's illiquidity and/or over-indebtedness within the meaning of the IA. If the debtor, and/or the management of the debtor where the debtor is a corporation, ignores this obligation, they will become personally liable to the creditors for all damages arising as a consequence of the delayed application to the insolvency court. If the corporation is without management (for example, due to revocation, withdrawal or death of its members), the obligation to apply for the opening of insolvency proceedings passes on to the corporation's majority shareholders (i.e. shareholders with a stake of more than 50% in the corporation).[4]

Creditor's Petition

Creditors are also entitled to apply for the opening of insolvency proceedings. The creditor is required to provide *prima facie* evidence that, firstly, he has a claim against the debtor and, secondly, that the debtor is illiquid. The claims of the particular creditor applying for the opening of insolvency proceedings need not be payable at the time of the application.

Opening of the Insolvency Proceedings

The insolvency court has to assess whether the conditions for the opening of the proceedings are fulfilled. Also, in cases where the application has been withdrawn by the creditor, the insolvency court will continue with this assessment as the withdrawal alone does not suffice to rebut the debtor's illiquidity. The debtor has the right to comment on the creditor's application for the initiation of insolvency proceedings. The insolvency court is obliged to open the insolvency proceedings if it comes to the conclusion that the debtor is in fact either illiquid or over-indebted. Upon its decision to commence insolvency proceedings, the insolvency court will publish its decision in the publicly accessible insolvency public register (*Insolvenzdatei*), available at www.edikte.justiz.gv.at. Where a company is subject to insolvency proceedings, the competent commercial court will also be notified and an entry made in the company's register.

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2 See section 69 of the IA.

3 See section 70 of the IA.

4 See section 69, para 3a of the IA (applicable as of 1 July 2013).

In cases where the assets of the debtor are insufficient to cover the costs of the insolvency proceedings, the insolvency court may reject the opening of insolvency proceedings. This decision also has to be published in the online insolvency register (*Insolvenzdatei*: www.edikte.justiz.gv.at).

Insolvency Proceedings

The insolvency proceedings can be opened as either restructuring proceedings (*Sanierungsverfahren*)[5] or bankruptcy proceedings (*Konkursverfahren*).[6] When restructuring proceedings are opened and there is no prospect of success for the reorganisation of the debtor, the proceedings will be continued as bankruptcy proceedings.[7]

Restructuring Proceedings and Restructuring Plan

There are two main differences between bankruptcy proceedings and restructuring proceedings. First, restructuring proceedings are not foreseen for the insolvency of natural persons who are not operating a business ("**private insolvency**"). Furthermore, in bankruptcy cases, the insolvency court deprives the debtor completely of its legal powers to act on its own behalf, appointing an insolvency administrator to act on behalf of the insolvency estate.[8] Restructuring proceedings, however, may be opened either as restructuring proceedings with no self-administration or as self-administered restructuring proceedings. In case of restructuring proceedings with no self-administration, an insolvency administrator will be appointed, too. In case of self-administered restructuring proceedings, however, the debtor will not be completely deprived of its powers, but will be able to self-administrate the proceedings under the supervision of a restructuring administrator.

In order to open the insolvency proceedings as restructuring proceedings, the debtor has to − prior to the opening of the proceedings − elaborate a restructuring plan. The main purpose of this plan is to find a compromise between the debtor and the creditors, in particular on the quota that will be eventually distributed to the creditors within a given period. In this respect, the quota at which the debts must be settled in restructuring proceedings with no self-administration has to amount to at least 20% and has to be paid within a period of two years. By contrast, in case of self-administered restructuring proceedings, the settlement to be achieved within the two-year period has to amount to at least 30%.[9] If no restructuring plan is presented prior to the opening of the insolvency proceedings, the proceedings will be opened as bankruptcy proceedings.

The restructuring plan has to be accepted by the creditors. In this respect, two voting requirements have to be fulfilled. Firstly, the restructuring plan has to be accepted by the majority of the creditors present at the court hearing. Secondly, of those creditors present at such court hearing, the accepting ones have to represent the majority of the notified claims. If the creditors reject the restructuring plan within 90 days of the opening of the proceedings, the insolvency court is obliged to revoke the self-administration and appoint the insolvency administrator to act on behalf of the insolvency estate.

Bankruptcy Proceedings

If bankruptcy proceedings have been initiated, the insolvency court in any event appoints an insolvency administrator.[10] As of this appointment, every legal action concerning the insolvency estate must be executed only by the insolvency administrator, and the debtor is prohibited from disposing of its assets. The responsibilities of the insolvency administrator are as follows:

- To clarify the financial situation of the debtor as well any guarantees given by third persons in favour of the debtor;

5 See section 167 of the IA.

6 See section 180 of the IA.

7 See section 167, paras 2 and 3 of the IA.

8 See section 80 of the IA.

9 See sections 140, 141, 167 and 169 of the IA.

10 See section 80 of the IA.

- To assess immediately after his appointment whether the business of the debtor can be continued or reopened (if already closed);
- To assess whether reorganisation is in the interest of the creditors and if a reorganisation plan is likely to be implemented; and
- To appraise the insolvency estate and administrate any outstanding legal actions.

Please note that in the course of bankruptcy proceedings, it is also possible to apply for the conclusion of a restructuring plan.[11] As for restructuring proceedings with no self-administration, the quota offered has to amount to at least 20% and the repayment period must not be longer than two years. In cases of natural persons other than entrepreneurs, the repayment period must not exceed five years.[12] The acceptance of the restructuring plan will not, however, lead to a renaming of the bankruptcy proceedings as restructuring proceedings; the insolvency proceedings will be continued as bankruptcy proceedings. If no restructuring plan is accepted within one year after the opening of the insolvency proceedings, the insolvency court has to order the closure of the debtor's business in order to protect the creditors' interests. The insolvency administrator may apply for an extension of this deadline for another year; however, in total, the insolvency court may not grant an extension period longer than two years.[13]

Contractual Relationships

In general, contracts entered into by the debtor remain unaffected by the opening of insolvency proceedings. However, the insolvency administrator has the option to either fulfil the debtor's obligations under the contract or withdraw from the contract within a time period set out by the insolvency court.

Furthermore, special provisions for rent agreements, employment contracts and contracts with a fixed deadline for the performance of the agreed obligations have to be observed.

It has to be noted that an agreement according to which a party has the right to withdraw from a contract or according to which the contract will be dissolved due to the initiation of insolvency proceedings against the other party is invalid under Austrian Insolvency Law (section 25b of the IA). The counterparty will remain bound by the terms of the relevant contract. Furthermore, within six months of the opening of the insolvency proceedings, contracts that are considered necessary for the continuation of the debtor's business can be terminated by the creditor only due to a material cause (section 25a of the IA). In this respect, neither the deterioration of the economic situation of the debtor nor the failure of the debtor to settle claims that became due prior to the opening of insolvency proceedings is deemed to constitute a material cause. However, the restrictions on the termination rights of the creditor pursuant to section 25 of the IA will not apply if the termination of the contract is indispensable for the avoidance of severe personal or economic disadvantages for the creditor.

Clawback and Recovery Mechanisms (Antecedent Transactions)

The basic principle of the insolvency regime is to ensure the equal treatment of all creditors. The aim of the legal regulations on clawbacks and recovery mechanisms is to remedy disadvantages suffered by the creditors due to the debtor's transfer of assets to third parties before the insolvency proceedings have been opened. Legal acts that intend to discriminate against certain or all of the creditors may be appealed by the insolvency administrator[14] and annulled by the insolvency court.

A transaction may be avoided *inter alia* under the following circumstances.

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11 See section 140 of the IA.

12 See section 141 of the IA.

13 See section 115, para 4 of the IA.

14 See section 37 of the IA.

Intentional Discrimination of Creditors

Under section 28(1) and (2) of the IA, the insolvency administrator is entitled to avoid transactions by the debtor if such transactions were entered into by the debtor with the intent (*Absicht*) to harm its creditors, provided that the other party was aware or at least negligently unaware of this intent. If the other party was aware of the debtor's intent, transactions entered into within the last 10 years prior to the opening of insolvency proceedings may be avoided; if the other party was negligently unaware of such intent, transactions entered into within the last two years prior to the opening of insolvency proceedings may be avoided. Furthermore, according to section 28(4) of the IA, the insolvency administrator is entitled to avoid purchase, swap and distribution agreements that were entered into by the debtor in the year prior to the opening of insolvency proceedings if the other party was aware of or must have been aware of a creditor-harming dissipation of funds.

Transactions for No Consideration

Under section 29(1) of the IA, the insolvency administrator is entitled to avoid transactions for no consideration entered into by the debtor if such transactions were entered into in the two years prior to the opening of insolvency proceedings.

Transactions Favourable for One Creditor

Under section 30(1) of the IA, the insolvency administrator is entitled to avoid transactions made after the insolvency of the debtor, or after the application for the opening of insolvency proceedings, or 60 days prior to the insolvency of the debtor or the application for the opening of insolvency proceedings, provided that such transactions gave, or made possible, to an insolvency creditor security or satisfaction to which such creditor had no right or no right to claim in such manner or at such time. An avoidance under section 30(1) of the IA further requires that the transaction to be avoided was entered into in the year prior to the opening of the insolvency proceedings.

Knowledge of the Insolvency

Under section 31(2) of the IA, the insolvency administrator is entitled to avoid transactions made after the debtor has become insolvent or after an application for the opening of insolvency proceedings has been filed with the competent court, provided that (i) the transaction gave, or made possible, to an insolvency creditor security or satisfaction or (ii) the transaction was entered into by the debtor with another person to the direct detriment of the creditors. Furthermore, both cases require that the other party to the transaction was, or reasonably should have been, aware of the fact that the debtor was insolvent or that an application for the opening of insolvency proceedings had been filed.

Under section 31(3) of the IA, the insolvency administrator is entitled to avoid transactions made after the debtor has become insolvent or after an application for the opening of insolvency proceedings has been filed with the competent court, provided that (i) the transaction was entered into by the debtor with another person to the detriment of the creditors, (ii) the other person was, or reasonably should have been, aware of the fact that the debtor was insolvent or that an application for the opening of insolvency proceedings had been filed, and (iii) the detriment to the insolvency estate was objectively foreseeable. In this respect, the law stipulates that the detriment was objectively foreseeable if, for instance, it was obvious at the time that the presented restructuring plan was inadequate.

An avoidance under section 31 of the IA further requires that the transaction to be avoided was entered into within the last six months prior to the opening of the insolvency proceedings.

Distribution

The IA provides for a certain settlement order depending on the legal basis of the individual creditor's claim. It distinguishes between four different kinds of claims, listed below in order of priority.

Claims based upon *In Rem* Rights

Creditors holding *in rem* rights such as mortgages, liens, reservation of title, or even claims based on security assignments, may claim for the exclusion of these assets. They take priority over the unsecured claims in the settlement process. The remaining assets are distributed among the creditors.

Preferential Claims

Preferential claims are listed exhaustively in section 46 of the IA. Such claims are, for instance: the administrative costs of the insolvency proceedings; claims of employees of the debtor for salary; claims of the debtor's social insurance; and all claims substantiated by acts of the insolvency administrator during the operation of the debtor's business. Preferential claims have to arise during the insolvency proceedings and serve the continuation of the debtor's business, which is the main justification for their preferential treatment. Preferential claims have to be settled by the insolvency administrator out of the funds available first (i.e. prior to any lower ranking claims) and in full, unless the insolvency estate lacks sufficient funds. In that case, a specific order of priority in relation to preferential claims applies.

Claims Provable in Insolvency Proceedings

All claims of creditors which were in existence at the time of the opening of the insolvency proceedings fall under this category. Such claims will be settled only after assets serving as security for other creditors have been excluded from the insolvency estate and preferential claims have been settled. All of these claims are treated equally and settled *pro rata* (*Konkursquote*) in proportion to the aggregate amount of all claims notified to the insolvency court and accepted by the insolvency administrator in the insolvency proceedings.

Lower-ranking and Excluded Claims

Lower-ranking claims are shareholder claims that are treated as equity of the debtor within the meaning of the Equity Substitution Act (*Eigenkapitalersatzgesetz*). If the shareholder has granted a loan to the debtor, and the debtor is in financial crisis, this loan is deemed as equity of this company (*Eigenkapitalersatz*). A financial crisis exists if the company is over-indebted or unable to pay its debts, or the debt-to-equity ratio is below 8% and the notional debt repayment period is more than 15 years. These claims will be satisfied only after all the other claims above have been settled. In contrast, excluded claims are excluded entirely from the settlement.

Termination of the Insolvency

Insolvency proceedings are generally terminated after various hearings, in particular: the examination hearing (*Prüfungstagsatzung*), at which claims of the creditors are acknowledged or rejected; the reporting hearing (*Berichtstagsatzung*), at which a decision is made on further proceedings; and the distribution hearing (*Schlussverteilung*), at which the remaining assets of the debtor are distributed among the creditors.

Private Insolvency[15]

Since 1995, both companies and individuals have been able to request the opening of insolvency proceedings. The IA provides specific provisions on insolvency proceedings for natural persons (including entrepreneurs and non-entrepreneurs). These specific provisions on private insolvency proceedings are outlined below.

Opening of Private Insolvency Proceedings

In contrast to the insolvency proceedings for companies, the insolvency court is not entitled to reject the opening of private insolvency proceedings where the assets of the debtor are not sufficient to cover the costs of the proceedings. In such cases, the debtor must:

- Provide a list of assets confirming that the list covers all assets and obligations;
- Provide for an adequate payment plan;[16]
- Confirm that his assets will cover the costs of the insolvency proceedings; and

[15] See section 181 ff of the IA.

[16] See "Payment Plan" below.

- If the debtor is not an entrepreneur, substantiate that an out-of-court settlement has failed or would have failed.

Debt Settlement Procedures

Under the IA, private insolvency proceedings for individuals other than entrepreneurs are given the special name "debt settlement procedures" (*Schuldenregulierungsverfahren*). In debt settlement procedures, the debtor is generally entitled to manage its assets on his own behalf (*Eigenverwaltung*). Only if the insolvency court comes to the conclusion that the debtor is not in a position to manage his assets, or the financial circumstances are unclear, or the debtor does not provide a detailed list of assets, may the court appoint an insolvency administrator.

Payment Plan

The debtor may request the acceptance of a payment plan not only at the opening of private insolvency proceedings[17] but also during the insolvency proceedings.[18] This plan is comparable to a restructuring plan; however, the court hearing on its acceptance may only take place after the realization of the debtor's disposable assets. The aim of the plan is to find a compromise between the insolvent debtor and the majority of his creditors so that the creditors agree on a certain quota. The quota has to be paid within five years, or within seven years in specific cases.

Proceedings of Absorption and Discharge of Residual Debt

If the disposable assets of the debtor have been realized and the payment plan has not been accepted, the insolvency court may start absorption proceedings (*Abschöpfungsverfahren mit Restschuldbefreiung*) on request of the debtor.[19] The debtor must assign a sizable amount of his income to a trustee for seven years. The trustee is then obliged to settle the creditor's claims in the given order.[20] During these proceedings the debtor's income is reduced to a minimum living wage. If the debtor is unemployed, he has to accept any reasonable employment opportunity. If the debtor can satisfy either at least 50% of the claims within a period of three years, or at least 10% of the claims within the whole period of seven years, the insolvency court may release the debtor and discharge the remaining debts. If the debtor is unable to meet these requirements, the court may – depending on the settlement actually achieved – do any of the following: (i) discharge the remaining debts, nonetheless; (ii) adjourn its final decision for a period of three years and determine the extent to which the outstanding debts have to be settled by the debtor during this period; (iii) prolong the repayment period for a term not exceeding three years; or (iv) not grant residual debt discharge. In the last case, all unsettled debt, including late interest, becomes directly collectable by the creditors.

Conclusion and Additional Observations

The latest major amendment to the Austrian insolvency laws took place in 2010. The goal of the IRÄG 2010 was to simplify insolvency proceedings and, beyond that, to facilitate the going concern of companies as well as their restructuring. Furthermore, the new regulations focus on the concept of self-administration.

According to several statistical sources, private insolvencies were constantly increasing in Austria until 2011, whilst company insolvencies were on the decrease. In 2012, however, the development slightly shifted, leading to the number of private insolvencies decreasing, while the number of company insolvencies increased. In 2013, both, the number of private insolvencies as well as the number of company insolvencies decreased, by approximately 5 and 10%, respectively. However, due to the insolvency of a major Austrian construction company, the total amount of company debt increased by about 100%. This amount, in absolute figures, represents a peak in Austrian insolvency history so far. In 2015, the number of company insolvencies continued to decrease by approximately 5%, while the number of private insolvencies (after having decreased in 2014 by approximately 7%), increased by approximately 5%.

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17 See "Opening of Private Insolvency Proceedings" above.

18 See section 193 of the IA.

19 See section 199 of the IA.

20 See "Distribution" above.

Finally, it is worth noting that since Austria is a member state of the EU, the European Regulation on Insolvency Proceedings (*EU-Insolvenzverordnung*) is applicable and must be taken into consideration in cases of cross-border insolvency proceedings.

Austria

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