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Global Restructuring & Insolvency Guide

Sweden

Overview and Introduction

The Swedish insolvency system mainly consists of two separate regimes: the bankruptcy rules and the company reorganisation rules. The former are applicable to both private individuals and legal persons while the latter, as indicated by the name, are merely applicable to undertakings, i.e. businesses.

Applicable Legislation

The legislation governing bankruptcy proceedings is the Bankruptcy Act (Sw: *Konkurslagen*). The legislation governing company reorganisation proceedings is the Company Reorganisation Act (Sw: *Lag om företagsrekonstruktion*).

Bankruptcy

Under Swedish bankruptcy proceedings, creditors can collectively and compulsorily take the total assets of a debtor for payment of their claims. During bankruptcy, the assets of the bankruptcy estate are taken into the possession of an administrator on behalf of the creditors.

Bankruptcy proceedings may be initiated on the debtor's own application or on the application of a creditor. The debtor shall, if proven to be insolvent following the petition, be declared bankrupt. A debtor is considered to be insolvent if it cannot pay its debts when due and this incapacity is not merely temporary.

Commencement of Bankruptcy Proceedings

The petition for bankruptcy is submitted, in writing, to the district court with jurisdiction over the debtor in actions regarding general payment obligations, i.e. in general, the district court where the debtor is domiciled. The applicant shall state and prove the circumstances whereby the court is competent, if these are not known.

If the petition is made by the debtor, the petition documents should preferably enclose a schedule, signed by the debtor, of the assets and debts of the estate, and the name and postal address of every creditor together with accounts and other documents that concern the estate. However, the debtor's assertion that it is insolvent is normally accepted, with or without providing any detail.

If the petition is made by a creditor, the creditor should in the petition provide information about its claim and the circumstances upon which it bases the claim. The creditor should also enclose the original or copies of those documents to which it wishes to refer.

As mentioned above, a debtor can only be declared bankrupt if shown to be insolvent. If the petition for bankruptcy is made by the debtor, insolvency is normally assumed and not independently tested. The Bankruptcy Act states that information from the debtor that it is insolvent shall be accepted unless there is special reason not to do so. Such special reasons can, according to the preparatory work to the Act, be that there is a difference of opinion among the representatives of a legal person regarding the question of whether the company is insolvent or not.

If the bankruptcy petition is made by the creditor, the court will make an evaluation of the debtor's financial position in order to decide if the debtor is insolvent.

The Bankruptcy Decision

In the event that a debtor's bankruptcy petition is lodged, the court will immediately determine the petition. However, under some circumstances, the bankruptcy application of the debtor is determined at a hearing, e.g. if there are special reasons not to accept the information regarding the insolvency of the debtor.

If a creditor's bankruptcy petition is disputed by the debtor, the court lists a hearing for determination of the petition, to be held within two weeks of the petition being submitted to the court. If prior to the hearing the debtor consents to the bankruptcy petition of a creditor, the court will immediately consider the petition.

When a decision on bankruptcy is made, the district court will decide the date for a meeting at which the debtor confirms the estate inventory under oath (a "meeting for the administration of oaths"). The court will also appoint an administrator, commonly a specialist lawyer, and summon the debtor, administrator, supervisory authority[1] and creditor who presented the bankruptcy petition to the meeting for the administration of oaths. Furthermore, a public notice of the bankruptcy decision – through which other creditors are summoned to the meeting for the administration of oaths – is published immediately.

The Assets of the Bankruptcy Estate

When the bankruptcy decision has been made, the debtor may not control property belonging to the bankruptcy estate. Nor is the debtor permitted to enter into obligations which could be claimed in the bankruptcy. The bankrupt's assets are thus taken possession of, administered and disposed of by the administrator.

The bankruptcy estate – a separate legal entity formed for the purpose of winding up the bankrupt person or entity and governed by the administrator – includes all property belonging to the debtor when the bankruptcy decision was made or that accrues to him during the bankruptcy and may be attached. The bankruptcy estate also includes property that can be brought into the estate by recovery.

Recovery means that property or payment which the debtor has distributed or made to someone else is restored or repaid to the bankruptcy estate. Such recovery may, under the Bankruptcy Act, take place in certain cases. For instance, a gift is to be annulled if it has been completed up to six months before the day upon which the petition to declare the debtor bankrupt was filed with the district court ("the day of grace"), and payment of wages, fees or pension, made up to six months before the day of grace and which obviously exceeded what could be regarded as reasonable having regard to the work performed, the profitability of the operation and circumstances in general, is to be annulled. The same goes for payment of debt to specific creditors to the detriment of other creditors or the sale or distribution of any asset below market price. As a rule of thumb, any legal action by the bankrupt company six months prior to the bankruptcy decision to the detriment of the creditors as a whole, is recoverable to the estate. If the beneficiary is related to the bankrupt entity or person, this period can be as long as five years prior to the bankruptcy.

The Administrator

The administrator's general obligation is to have regard to the common rights and best interests of creditors and to execute all measures that promote an advantageous and expeditious winding-up of the estate.

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[1] The Enforcement Authority (Sw: *Kronofogdemyndigheten*) acts as the supervisory authority. The supervisory authority insures that the administration of the estate is pursued appropriately, in accordance with the Swedish Bankruptcy Act and other statues. The Enforcement Authority is a Swedish governmental body that also handles debt collection, default summonses and debt restructuring.

The administrator shall initially, as soon as possible, prepare an estate inventory, in which the assets of the estate are listed at carefully estimated values. The estate inventory also contains the name and postal address of every creditor. The debtor provides prospective additional information and/or makes prospective comments on the estate inventory, and subsequently under oath confirms the estate inventory at the meeting for the administration of oaths.

Moreover, the administrator prepares, as soon as possible, a written report on the condition of the estate and the reasons for the insolvency of the debtor, as far as these can be established, and, if possible, states the point in time at which the insolvency may be assumed to have occurred. The report also contains, *inter alia*, a review of assets and debts of various kinds and information about whether there is any circumstance giving rise to a right of recovery to the bankruptcy estate. Further, the administrator is charged with the task of assessing whether the business's books and records have been diligently kept and if any criminal acts have been committed.

The administrator's duties also include selling the property of the estate and taking measures to collect outstanding claims. If the debtor conducted a business operation, the administrator may, if it is lawfully possible, continue with the operation on behalf of the bankruptcy estate to the extent that it is purposeful. This also applies if the administrator, after the business operation has been discontinued, wishes to resume the activity, all in order to be able to achieve the highest possible purchase price for the assets, e.g. by divesting a "going concern".

The Debtor's Obligations

A debtor has many obligations, some of them quite extensive, during bankruptcy proceedings. Below are some examples.

The debtor has a duty to provide information and to attend certain meetings during the bankruptcy. The debtor must, for instance, submit to the court, the supervisory authority, the administrator and examiners such information as they request which is of significance to the bankruptcy investigation, and is obliged to attend inventory meetings, settlement meetings and meetings to consider proposals for composition.

Moreover, the debtor may not, following the issue of the bankruptcy decision and before he has sworn an estate inventory oath – which is something a debtor is required to do at the oath administration meeting – travel abroad without the consent of the court. If later during the bankruptcy there is reason to fear that the debtor will avoid his obligations as prescribed by the Bankruptcy Act by leaving the country, he may be prohibited from travelling abroad. If the debtor changes his place of residence he must advise the administrator of where he is staying.

The Creditors' Claims in Bankruptcy

Creditors either have priority claims or non-priority claims. Creditors' rights of priority in the event of bankruptcy are governed by the Swedish Rights of Priority Act (Sw: *Förmånsrättslagen*).

There are two general types of priority claims: specific and general priority claims. Generally, a specific right of priority has precedence over a general right of priority and all priority claims have priority over non-priority claims, i.e. non-priority claims will not be paid at all until the priority claims have been settled.

A specific right of priority is attached to, *inter alia*:

- Maritime liens and aircraft liens;
- Pledges and rights to retain possession of personal property as security for a debt ("possessory liens");
- Security interests based upon mortgages granted in ships, or ship buildings or aircraft and reserve parts for aircraft;
- Certain claims of policyholders and other parties entitled to indemnification from an insurer; and

- Mortgages in real property.

A general right of priority is attached to, *inter alia*:

- Creditors' costs incurred in having the debtor placed into bankruptcy;
- Employees' claims for wages or other compensation arising from the employment; and
- Entitlements to holiday pay and holiday remuneration which have accrued prior to the filing of the petition for bankruptcy.

One of the fundamental principles of Swedish bankruptcy proceedings is that all kinds of claims are admitted, provided that they are considered enforceable in Sweden. The fact that the claim is brought by a creditor who is not in any way personally connected with Sweden, or that the claim has arisen from a transaction or event that took place in a foreign jurisdiction, are irrelevant in this respect. Accordingly, all foreign creditors are welcome to participate on the same footing as those creditors who are Swedish nationals and residents and whose claims have originated in Sweden.

Non-priority claims rarely receive payment from the bankruptcy estate. However, if non-priority claims may be assumed to obtain a distribution in the bankruptcy the court will decide that a lodging of proofs procedure shall take place in the bankruptcy. If it is decided that such a procedure is to take place, the court gives a public notice of the decision and all creditors with claims are then generally required to lodge proof in order to receive payment for their claims. The proof of claim document states the amount of the claim, if possible, and the basis of the claim. If a priority right is claimed, the creditor must also state the basis for this.

Writing-off of Bankruptcy

Bankruptcy proceedings can be ended through distribution; through agreement between the debtor and the creditors according to which they reach a settlement; or through the writing-off of the bankruptcy.

The court decides to write-off the bankruptcy if, *inter alia*, the court, after hearing the administrator, finds that the assets of the bankruptcy estate are not sufficient for payment of bankruptcy expenses incurred and expected and other debts that the estate has incurred. The bankruptcy may, however, not be written off before an estate inventory has been confirmed under oath and the administrator has prepared his written report on the condition of the estate and the reasons for the insolvency. Subsequent to the write-off of the bankruptcy, a bankrupt legal entity is struck from the commercial register and ceases to exist. A bankrupt individual, however, survives and so do the claims against him, subject to general statutes of limitation.

Distribution and Completion

If the bankruptcy is not written off, the money in the estate, to the extent that the funds are not utilised for payment of the bankruptcy expenses and other debts that the estate has incurred, are to be distributed to the creditors. When there is to be distribution, the administrator prepares a proposal for distribution, in which he takes all claims and priorities into account.

The distribution proposal shall be kept available at the court and the supervisory authority for those persons who wish to review the documents. A person wishing to raise an objection to the distribution proposal shall do so at the court not later than the date decided by the court. When the period for raising an objection has expired, the court shall determine the distribution in the bankruptcy in accordance with the distribution proposal, unless by raising an objection or by other means, it is indicated that an error or inadequacy exists which affects someone's rights.

When the decision to confirm the distribution and the decision to decide the administrator's fees have gained legal force, the administrator must, as soon as possible, send the funds allocated to the creditors.

A bankruptcy is considered complete when the district court has confirmed distribution. If funds become available for distribution after the distribution proposal has been prepared, the administrator shall, through post-distribution payments, distribute them to the creditors.

Company Reorganisation

The Company Reorganisation Act provides an alternative insolvency procedure, which, as opposed to bankruptcy proceedings, does not entail that the owners and management lose control over the company and/or its assets. A business which has difficulty fulfilling payment obligations may, pursuant to the Company Reorganisation Act and following an order by a court, commence specific company reorganisation proceedings in order to reorganise its business.

Through a company reorganisation, an administrator appointed by the court shall investigate whether the business which the debtor is operating is capable of continuing, in whole or in part, and if so, the manner in which such can take place and whether there exists a possibility for the debtor to reach a financial agreement with its creditors (a “composition”).

Commencement of Company Reorganisation

An application for a company reorganisation may be submitted by the debtor or by a creditor. However, a creditor’s application will only be granted where the debtor consents thereto.

The application is submitted in writing to the district court with jurisdiction over the debtor in actions regarding general payment obligations, i.e. in general the district court where the debtor is domiciled.

An application by a debtor must contain a brief account of the debtor’s finances and the reasons for the payment difficulties, a schedule of creditors, a statement regarding the manner in which the debtor believes the business should be operated and how an agreement can be reached with the creditors, as well as a nomination of an administrator. An application by a creditor must contain information regarding the creditor’s claim against the debtor, information regarding the debtor’s difficulties in fulfilling payment obligations and a nomination of an administrator.

Two conditions must be fulfilled to obtain an order for a company reorganisation. First, the debtor must be deemed to be unable to make payment of its debts as they become due or it is likely that such inability will exist within a short time. In other words, there must be a lack of liquidity or a risk of future lack of liquidity. Furthermore, there must be reasonable cause to assume that the purpose of a company reorganisation can be achieved. In this regard, the court does not carry out any detailed assessment: rather, the aim is to prevent abuse where the conditions for a successful company reorganisation do not exist. The assessment is thus of a more general and formal nature.

Where an application is accepted for consideration, the court shall immediately adjudicate the matter. Upon the approval of an application, the court appoints an administrator.

The Administrator

The administrator must enjoy the confidence of the creditors and meet exacting qualification requirements. The legislature imposes upon the administrator a great deal of responsibility and independence. The administrator conducts the work alongside the debtor but has sole discretion on a number of issues. In the absence of consent by the administrator, the debtor may, for example, not pay debts which arose prior to the order regarding company reorganisation, provide security for such debts, or incur new obligations.

The Company Reorganisation Act states that the debtor must comply with the administrator’s instructions regarding the manner in which the business is to be conducted. In practice, however, the administrator’s work will be focused on the measures aimed at implementing the reorganisation, primarily negotiations with creditors, and certain structural issues. The administrator’s directions normally do not cover the day-to-day business since the administrator rarely holds any specific industry experience. The company’s management thus normally continues to attend to the day-to-day management of the company’s business, albeit under the supervision of the administrator.

Suspension of Payments

The debtor normally suspends its payments prior to, or in connection with, the filing of an application for a company reorganisation order. The principal reason for the decision to suspend payments prior to the application is to stop the flow of funds from the company; however, this also acts as a means of countering pressure from creditors. Payment to specific creditors might be deemed to constitute a sanctionable preference with respect to such creditors, which can thus be avoided through a suspension of payments.

Through the court's company reorganisation order, the debtor is in practice precluded from paying debts which arose before the order was issued, irrespective of whether such debts are prioritised or non-prioritised. This follows from the fact that the debtor needs the administrator's consent in order to pay such debts, along with the fact that the administrator may consent to such a payment only where special cause exists. Such special cause could, according to the preparatory works to the Company Reorganisation Act, for instance, be if non-payment endangers the completion of the company reorganisation procedure.

After the suspension of payments has been implemented, deliveries of goods and services are paid for in cash. "Cash" means, in practice, that no new indebtedness may arise to, for example, trade creditors. The intention is thereby to prevent the debtor from increasing its debt burden.

Protection during Administration

As a consequence of the court's decision to start the company reorganisation, the debtor obtains protection from an array of threats as long as the procedure subsists. The debtor thereby obtains breathing space in order to plan how to resolve the crisis. It may be said that the debtor benefits from a "protecting veil" during the reorganisation. Two of the most important consequences are that the debtor's contracts may not be terminated due to demonstrated or anticipated payment difficulties and that the debtor is protected against actions by the company's creditors since enforcement measures, including petition for bankruptcy, cannot be initiated against the debtor during the procedure.

Composition

A company reorganisation is often aimed at achieving a composition. The district court may, upon the debtor's written request, decide to initiate composition negotiations with the creditors. If the district court initiates such negotiations it must immediately arrange a meeting to which the debtor, administrator and all creditors shall be summoned to appear.

Composition negotiations only concern creditors with claims originating before the application for company reorganisation. Furthermore, creditors who can settle their claims through set-offs or who have claims subject to rights of priority may not participate in the composition negotiations. A creditor may participate even though its claim is not due or if it is conditioned.

The composition agreement gives equally entitled creditors the same rights and at least 25% of the amount of their respective claims. Agreed compositions are paid within one year unless agreed otherwise. The composition has to be seconded by a certain percentage of the creditors. For instance, a composition proposal which yields at least 50% of the amount of the claim is deemed to be accepted by the creditors where three-fifths of the creditors voting have accepted the proposal and their claims amount to three-fifths of the total amount of claims held by creditors entitled to vote. A settled composition binds all creditors, known or unknown, who had the right to participate in the composition negotiations.

Termination of Company Reorganisation

The court must order that the company reorganisation terminate, where, *inter alia*, such measures have been executed that the purpose of the company reorganisation may be deemed to have been achieved, or the administrator or a creditor so requests and the purpose of the company reorganisation cannot be deemed to be achieved.

It is assumed that the formal procedure will be concluded within three months and the court will, three months after the date of the order in respect of company reorganisation, order that the company

reorganisation terminates. Where special cause exists, the court may prolong the period of the reorganisation. However, a company reorganisation may not proceed for a period longer than a total of one year, in the absence of composition proceedings.

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