

Appointment of an Examiner in insolvent companies

A recent amendment to the Cypriot Companies Law, Cap. 113 has introduced a new procedure in the Cypriot Legal System, which provides for the appointment of an Examiner in companies which are, or are likely to be, unable to pay their debts, but for which there is a reasonable prospect of their survival, and of the whole or any part of their business as a going concern. This procedure is based on the respective provisions of the Irish Companies Act. Even though, the rationale and hopes behind this amendment was largely to provide help and a “breathing space”¹ to these companies in order to survive, with the ultimate goal of the legislation being the rescue of jobs, viable businesses and supporting the economy, the very first examples of the practical application of this procedure in Cyprus, indicated the head-on collision of the Irish “hope” with the Cypriot reality.

Many of the problems of this procedure have already been identified by its application in Ireland. However, the problems of the Cypriot procedure are multiplied mainly due to the fact that the Irish Law was practically transposed into the respective Cyprus Companies Law, without taking into account the ‘realities’ of the Cypriot System of Administration of Justice, as well as the addition of provisions by the Cypriot Legislator, without prior consideration regarding their practical implementation.

Once an Application to appoint an Examiner is filed (along with the report of the independent expert) the company for which the application is being filed, is placed under the protection of the Court. Heavy restrictions are imposed to the rights of the Company’s creditors with the commencement of the protection period. For example, the creditors cannot apply for the Liquidation of the Company, they may not seek for the appointment of a receiver or take any steps regarding the enforcement of judgements against the Company. In addition, the company cannot pay existing debts without the Court’s prior leave. In view of the serious impact that the filing of the

¹ *Re Gallium Ltd, trading as First Equity Group* [2009] 2 ILRM 11.

application has on both the creditors and the company, the legislator has set very tight and strict time-frame for the completion of the Examinership process.

The entire process, according to the relevant provisions of the law, should be completed within four months from the date of filing of the application. This period may be extended by two months following a request by an appointed Examiner in order to complete his final report. During the four-month period, the following actions must take place:

1. Notification of all interested parties within 3 days from the filing of the application.
2. Submission of an objection by the interested parties that wish to be heard and object.
3. The hearing of the application for the appointment of the examiner.
4. The ruling of the Court deciding whether the Examiner should be appointed or the application be dismissed.
5. If an Examiner is appointed, he should call for meetings with the various classes of creditors and members of the company in order to negotiate and draft the Scheme of Arrangement.
6. If the Scheme of Arrangement is approved by the Creditors, the Examiner should prepare the relevant report and present it before the Court for its approval.

The first Application/ Petition (hereinafter “**the Application**”) for the appointment of an Examiner which has been filed to the Cypriot Courts, has revealed many problems regarding the application of this procedure in Cyprus.

To begin with, the application was filed late June and the Court’s Registrar fixed the case for hearing in September. Subsequently, a procedure that is supposed to be completed within four months, had already been delayed by two months.

The Cypriot Legislator considered it appropriate to include a provision which obliges the applicant to notify all interested parties regarding the filing of the application, within 3 days from the date of its filing. Failure to comply with this

obligation constitutes a criminal offence which is punishable with a fine of up to €5.000.

Needless to say that the above strict deadlines were not met and the Court decided not to extend the provided 3-day deadline, and not to allow the publication of the above application for the purpose of informing the interested parties. The above application was eventually discontinued, due to the fact that almost three and a half months out of the four had passed without the commencement of the Application's hearing.

Following the withdrawal of the aforementioned application, another application was filed for the appointment of an Examiner, where the extension of the 3-day notice period was once again requested. The Court rejected this request on the grounds that the time-frame provided cannot be extended. As a result, the second application was also withdrawn, and a new one was filed. The third application is currently pending before the District Court of Nicosia and therefore no comments shall be made at this stage.

The aforementioned circumstances are just the tip of the iceberg regarding all the potential problems that may arise in the context of this new procedure. There is a statutory obligation that the application for the Appointment of an Examiner has to be accompanied by an Independent Expert's report. This report is one of the main factors to be considered by the Court when exercising its discretion on the Appointment of an Examiner, with particular view to the prospects of survival of the company and its business as a going concern. The role of this report is therefore of high importance.

The risk on this point, is that the independent expert may prepare his report with the view of serving the interests of the Applicant who appoints him, rather than acting objectively and independently, in order to serve the interests of Justice. Specific Best-Practice Directives have been enacted in Ireland for the Independent Experts, in order to disincentivize biased behaviors. In Cyprus the existing legal framework does not provide a safety mechanism and additional regulation is required, both for the Independent Experts and the procedure as a whole.

In addition to the above indicative problems, it is worth noting that the majority of temporary licenses granted to insolvency practitioners have expired. Due to the fact that having an active Insolvency Practitioner's license is a prerequisite in order to be appointed as an Examiner, relevant legislative measures are expected to be taken by the House of Representatives in order to resolve this issue.

In the light of the above, the first signs indicate that Examinership may not serve the purpose for which it was voted, while the risk remains that it may be used as a tool for abuse rather than rescue.