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Bankruptcy, Insolvency & Rehabilitation Proceedings in Israel

ILN RESTRUCTURING & INSOLVENCY GROUP



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KEY FACTS OF BANKRUPTCY, INSOLVENCY & REHABILITATION PROCEEDINGS UNDER ISRAELI LAW

The Israeli parliament (Knesset) passed a new statute regarding insolvency law, which is named: The Insolvency and Rehabilitation Law-2018, (the "**Law**"). The Law was enacted on March 5, 2018, and it will come into force on September 15, 2019. The Law offers a comprehensive reform and provides Israel with modern insolvency legislation dealing with both corporate and individual insolvency.

The Law has three primary objectives:

1. to promote the debtor's economic rehabilitation;
2. to maximize debt repayment to creditors and to divide the debtor's pool of assets in a more equitable manner between the secured and unsecured creditors;
3. to increase the certainty and stability by streamlining processes and reducing the bureaucratic burden.

The key principles of the Law are as follows:

1. A clear and simple definition of insolvency

An entity shall be deemed insolvent if it cannot actively pay its debts. According to the Law, a creditor is entitled to file an application for a court order to open insolvency proceedings only when a debt has not been paid to a said creditor on time. According to this, creditors may not file applications preemptively.

2. Reducing the bureaucratic burden and streamlining the process

The jurisdiction to conduct insolvency proceedings in relation to corporations is the district court. However, a significant share of the proceedings being conducted will be decided by administrative authorities and thus will not require court rulings. The Law empowers the

administrative aspects of insolvency proceedings to the Official Receiver or, under its new name, the "Administrator in Charge of Insolvency Proceedings and Economic Rehabilitation."

3. Uniformity in the opening of proceedings

The Law establishes a uniform and orderly procedure for opening proceedings against a corporation facing insolvency. The Law prescribes that the court shall decide whether a corporation is insolvent and, only subsequently, determine the most appropriate procedure for handling that corporation on the basis of data submitted to the court.

4. Creditors' debt repayment order and distribution of funds

According to the Law, some of the debt repayments will be carved out from the sums owed to the strong secured creditors (i.e. banks and tax authorities). They will then be distributed among the general unsecured creditors holding no collateral whatsoever. In the majority of cases, these general creditors (usually suppliers, customers, and employees) receive only a tiny portion, if any, of the debtor's pool of assets. Within this context, the Law prescribes, inter alia, that 25% of the assets pledged under a floating lien (to differentiate from a specific lien on a specific asset) be carved out in favor of the debtor's general unsecured creditors. It further determines that the volume of assets used to repay the holder of the floating lien be reduced. The Law also reduces the preferential right given to the tax authorities when dividing up the debtor's assets.



5. *Minimizing damages*

The Law imposes an obligation on the board of directors of the debtor corporation to take all reasonable measures to minimize the extent of the insolvency during the period prior to the opening of insolvency proceedings.

Proceedings for corporations

A creditor or a debtor wishing to initiate insolvency proceedings must file a standard application to obtain a commencement of insolvency proceedings order. The court will determine whether to channel the corporate entity into a course of rehabilitation or winding up. This decision depends on the economic status of the entity and is independent of the manner in which the application has been drafted.

Upon issue of the order by the court for the initiation of insolvency proceedings, an automatic stay of proceedings will apply. The court may choose to operate the corporate entity in order to view to its economic rehabilitation. In such a case, stay of proceedings will apply against the secured creditors, subject to adequate protection in order to safeguard the value of their security.

Simultaneously with the issue of the order, the court will appoint a trustee to be entrusted with full control of the company's assets.

The Law creates a new mechanism entitled protective negotiations, which is a temporary provision to be in effect for four years. This mechanism allows a public company to initiate out-of-court protective negotiations with its creditors while allowing it to remain active and without appointment of a trustee. During the period of the protective negotiations, a complete stay of proceedings shall not apply but the creditors may not file an application for an

initiation of insolvency proceedings order against the corporation and may not call for the immediate repayment of debt.

Proceedings for individuals

Under the new Law, a substantial part of the administration of insolvency proceedings relative to individuals passes from the court to administrative authorities.

Insolvency proceedings below NIS150,000 will be administered entirely by the Enforcement and Collection Authority. Insolvency proceedings above NIS150,000 will be conducted before the official receiver (the Insolvency Commissioner) and, if relevant, before the court with respect to further, more specific matters.

At the end of this audit a payment plan is established, at the end of which the debtor will receive a discharge. The default scenario is a payment period of three years. The court reserves the right to increase or decrease the period depending upon the circumstances of the case.

If the debtor has no proven financial ability to pay the creditors, he may be granted an immediate discharge.

Order of Repayment

Under Israeli law, generally speaking the order of repayment in insolvency proceedings is as follows:

1. Creditors secured by a fixed charge
2. Expenses of insolvency proceedings
3. Preferred creditors
4. Creditors with a floating charge
5. Ordinary creditors
6. Deferred creditors and shareholders



Directors' and CEO's liabilities

The Law allows the court to impose liability on a director or general manager that knew, or ought to have known, that the corporate entity was insolvent and did not take reasonable steps to reduce potential impact.

However, the Law creates a presumption that a director or general manager took reasonable steps to reduce the extent of the insolvency, if

measures were taken to evaluate the economic position of the corporation and acted to ensure that the corporation take one of the following measures:

1. Receipt of assistance from a corporate rehabilitation specialist
2. Negotiations for debt settlement
3. Commencement of insolvency proceedings