



European Economic and Social Committee

INT/391
**Overcoming the stigma of
business failure**

Brussels, 29 May 2008

OPINION

of the

European Economic and Social Committee

on the

Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions – Overcoming the stigma of business failure – for a second chance policy – Implementing the Lisbon Partnership for

Growth and Jobs

COM(2007) 584 final

On 5 October 2007 the European Commission decided to consult the European Economic and Social Committee, under Article 262 of the Treaty establishing the European Community, on the

Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions – Overcoming the stigma of business failure – for a second chance policy – Implementing the Lisbon Partnership for Growth and Jobs
COM(2007) 584 final.

The Section for the Single Market, Production and Consumption, which was responsible for preparing the Committee's work on the subject, adopted its opinion on 6 May 2008. The rapporteur was Mr Morgan.

At its 445th plenary session, held on 28 and 29 May 2008 (meeting of 29 May), the European Economic and Social Committee adopted the following opinion by 70 votes with 3 abstentions.

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1. Conclusions and Recommendations

- 1.1 Since 2001 the Commission has been addressing the negative effects of business failure. In particular, it has flagged the need to improve bankruptcy procedures. Given its limited competence in this area, the Commission has concentrated on collecting data on the legal and social consequences of business failure, facilitating the identification and dissemination of good practices and to working on early warning tools as a means of reducing the stigma of failure.
- 1.2 The EESC endorses the emphasis placed by the Commission on the need to overcome the stigma of business failure. Good national framework conditions for entrepreneurship are crucial to the full exploitation of the EU's entrepreneurial potential and to the creation of dynamic companies. The societal appreciation of successful entrepreneurship, vital to this end, should go hand in hand with a policy of promoting a second chance for entrepreneurs who have failed.
- 1.3 The Commission is right to assert that business creation, business success and business failure are each inherent in the market economy. It correctly highlights that as part of the general lack of societal appreciation and understanding of entrepreneurship, events such as business distress or business failure are neither sufficiently understood as a normal economic

development nor seen as an opportunity for a fresh start. The EU must change its mind set. The more the stigma of failure attaches to a former bankrupt, the more at risk any new venture may be, and this risk attaches itself to all the stakeholders in the enterprise.

- 1.4 The US laws seek to balance the interests of debtors, creditors and society as a whole. It is the Opinion of the EESC that Member State laws should be drafted to achieve the same balance. Insolvency and the non payment of debts can create enormous difficulties for creditors and drive them in their turn into insolvency. Stripping the debt out of a company to give it a chance to restart can be most unfair on creditors. Insolvency laws need to strike the right balance.
- 1.5 From the point of view of society in general, keeping all or part of the enterprise in business may be the best solution. If the company is potentially viable, then all the stakeholders will benefit furthermore, if an insolvent company can be rescued by the insolvency practitioners, then employees will continue to be employed. If a bankrupt entrepreneur goes back into business, then he creates new employment. Employment in any of these ways clearly serves society at large.
- 1.6 There are many ways in which an enterprise can fail, even with the best intentioned entrepreneur. In the start up phase, it may not be possible to establish a viable enterprise. Beyond the start, a flawed business model may still mean that the company has no future. On the other hand, potentially viable companies can fail because of mistakes made by the entrepreneurs as well as for reasons right out of their control. Such companies can and should be saved by receivers with most of the jobs protected.
- 1.7 It is important to distinguish between the company and its directors. Directors may go bankrupt while a receiver is rescuing the company and its employees. When a company fails, the entrepreneurs may well be bankrupted because of the bank guarantees which they have given, even though their personal conduct was not fraudulent. It is these non-fraudulent entrepreneurs with which the Commission is concerned. When they have created a good business and then have the misfortune to fail through inexperience or bad luck, they deserve a second chance; the economy needs their skills. Others, who fail through incompetence and a lack of vision probably have little to offer the economy, even if they can find financial backers. Not all bankrupt entrepreneurs deserve a second chance.
- 1.8 The Commission's initiative has helped trigger reform across the EU. Many Member States have already drawn some inspiration from the good practices and policy conclusions collected at the European level. Around one third of Member States have put forward plans to reform their national insolvency legislation. Even so, almost half of the EU countries still need to take the first steps in this direction. While the Commission has limited competency in this policy domain, the EESC urges it to use every means at its disposal to energise Member State finance ministers to act. In the opinion of the EESC, Member State progress is generally unsatisfactory.

- 1.9 The EESC fully endorses all the points made in the Communication in respect of insolvency law, subject of course to the detail of the laws ultimately put in place. These involve the formal recognition of non-fraudulent bankruptcies, early discharge from debts and reduction of legal restrictions, disqualifications and prohibitions with accelerated proceedings. The medium term target should be that proceedings take no more than twelve months.
- 1.10 The EESC believes that it is imperative that all Member States complete the revision of their insolvency laws with the least possible delay. In addition to changes in the law, it is vitally important that bankruptcies be handled expeditiously by the courts. The process needs to be well organised. These changes are the centre piece of the Second Chance programme.
- 1.11 Active support to businesses at risk is the second message contained in the Communication. It is not part of the Second Chance programme per se. Instead it is a programme designed to avoid bankruptcy and to preserve businesses and jobs. In section 4.0 a number of examples are given of business failures which could have been avoided. In this respect the thrust of the Communication is to head off avoidable failures through early warning, the provision of temporary funding and the services of advisors.
- 1.12 This programme is not very practical for the generality of SMEs since there are few mechanisms for the pro-active identification of businesses at risk amongst the tens of thousands of SMEs in each Member State. Even so, Member States are encouraged to make the most of such possibilities as do exist, e.g. the French use of the VAT authorities to provide an early warning of possible company cash flow problems. The Commission says that support measures should focus on bankruptcy prevention, expert advice and timely intervention. The problem arises when directors do not realise that their business is at risk. Member State governments will need to work with the Accountancy profession and SME support organisation to develop such pro-active measures as are appropriate to their own SME culture.
- 1.13 It is clear that the most important recommendation in the Communication relates to the reform of Insolvency Law. This is the key measure without which the Second Chance programme will not get off the ground.
- 1.14 Some of the softer recommendations in the Communication can be implemented without changes to insolvency law. When the law has been changed, the other soft measures proposed by the Commission can be undertaken. Without changes in the Insolvency Law, the main point of the Commission's Communication will be missed.
- 1.15 The EESC believes that each Member State should respond to this Communication by including its proposals within its National plan for the Lisbon Strategy (guideline #15 applies).

2. **Introduction**

- 2.1 Since 2001 the Commission has been addressing the negative effects of business failure. In particular, it has flagged the need to improve bankruptcy procedures. Given its limited competence in this area the Commission has concentrated on collecting data on the legal and social consequences of business failure, facilitating the identification and dissemination of good practices and to working on early warning tools as a means of reducing the stigma of failure.
- 2.2 This has helped trigger reform across the EU. Many Member States have already drawn some inspiration from the good practices and policy conclusions collected at the European level. Around one third of Member States have put forward plans to reform their national insolvency legislation. However, almost half of the EU countries still need to take the first steps in this direction. Even though the Commission has limited competency in this policy domain, the EESC urges it to use every means at its disposal to energise Member State finance ministers to act. In the opinion of the EESC, Member State progress is generally unsatisfactory.

TABLE A: CURRENT SITUATION IN MEMBER STATES

Y	Measures exist	(Y)	Measures planned/available partially	N	No measures exist
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	Information/ education	Overall strategy	Publicity when non-fraudulent Court decision	Reduced restrictions, etc	Better legal treatment for honest bankrupts	Short discharge period and/or debt relief	Streamlined proceedings	Stimulate support	Foster links	Discussion within financial sector	Total Y+(Y)
Belgium	N	N	(Y)	(Y)	Y	(Y)	N	N	N	N	4
Bulgaria	N	N	N	N	N	N	N	N	N	N	0
Czech Republic	N	N	N	N	N	N	(Y)	N	N	N	1
Denmark	N	N	N	Y	(Y)	Y	(Y)	N	N	N	4
Germany	(Y)	N	N	Y	Y	(Y)	N	N	N	N	4
Estonia	N	N	N	N	N	(Y)	(Y)	N	N	N	2
Ireland	N	N	N	N	N	Y	Y	N	N	N	2
Greece	N	N	N	Y	(Y)	(Y)	Y	N	N	N	4
Spain	N	N	N	N	Y	Y	Y	N	N	N	3
France	N	N	N	N	(Y)	N	Y	N	(Y)	N	3
Italy	N	N	N	Y	Y	(Y)	(Y)	N	N	N	4
Cyprus	N	N	(Y)	(Y)	N	(Y)	(Y)	N	N	N	4
Latvia	N	N	N	N	N	N	(Y)	N	N	N	1
Lithuania	N	N	N	Y	(Y)	Y	(Y)	N	N	N	4
Luxembourg	N	N	N	N	N	N	N	Y	N	N	1
Hungary	N	N	N	N	N	N	N	N	N	N	0
Malta	N	N	N	(Y)	(Y)	N	N	N	N	N	2
Netherlands	(Y)	N	N	N	(Y)	(Y)	N	N	N	(Y)	4
Austria	N	(Y)	N	(Y)	(Y)	(Y)	Y	(Y)	(Y)	N	7
Poland	N	N	N	N	(Y)	(Y)	Y	N	N	N	3
Portugal	N	N	N	N	N	N	N	N	N	N	0
Romania	N	N	N	(Y)	(Y)	N	Y	N	N	N	3
Slovenia	N	N	N	N	N	(Y)	N	N	N	N	1
Slovakia	N	N	N	N	N	N	N	N	N	N	0
Finland	N	N	N	Y	N	(Y)	Y	Y	N	N	4
Sweden	N	N	N	N	Y	(Y)	Y	N	N	N	3
United Kingdom	N	N	Y	Y	Y	Y	Y	N	N	N	5
Total Y+(Y)	2	1	3	12	15	17	17	3	2	1	
United States	N	N	N	Y	(Y)	Y	Y	N	N	N	4

- 2.3 Table A is taken from the Communication. Columns 4 to 6 relate to reform of insolvency laws. It is very obvious that the Member States are very active in respect of legislation while at the same time it also shows that very few countries have put revised laws into effect. If the totals under the columns related to legislation in effect, then they would not be 12 – 15 – 17 – 17 but rather 6 – 6 – 5 – 10. This is a poor result from 27 Member States. Slow action or inaction is undoubtedly damaging entrepreneurial activity in Member States because until the necessary changes are made, the possibility of failure is an important barrier to enterprise.
- 2.4 Another feature of the table is that the six columns which surround the columns related to legislation are more or less blank. This is somewhat surprising because even though the insolvency legislation has not been changed in most Member States, the other softer measures could nevertheless be undertaken.
- 2.5 In order to provide a comparator, the EESC has asked the Commission to provide data for the USA equivalent to that given in the table for the EU States. The following is the explanation of the US entry on the chart:
- Reduced restrictions –Y- In the US none of the more common restrictions found in the EU (e.g. preventing a bankrupt from becoming a director of a company, preventing a bankrupt from being a trustee, and establishing some sort of credit limit for a bankrupt) apply. In fact, section 525 of the US Bankruptcy Code provides that individuals may not be discriminated against solely on the ground that they are or have been the subject of bankruptcy proceedings.
 - Better legal treatment –(Y)- Like other EU countries, no discharge is granted in case of misconduct, fraudulent behaviour, etc. No other extra "better treatment" exists.
 - Short discharge –Y- There is no specified period during which the bankrupt retains the status of bankrupt before being discharged.
 - Streamlined proceedings –Y- The most common form of bankruptcy procedure used by individuals is the Chapter 7 relating to liquidation or bankruptcy. Generally the process takes 3-4 months to finalise. As a safeguard against multiple filings, Chapter 7 cannot be used by any individual who has already used it in the previous 6 years.
- 2.6 The US Code exhibits a completely different mind set from that which pertains in most, if not all, Member States. The legal standpoint of most Member States at the moment shows how far this issue is just not understood. The time being taken to change insolvency laws reveals that, in the vernacular, the EU just does not "get it". A change of mind set will accelerate the introduction of new laws. Equally, without such a change the softer measures will never get off the ground.
- 2.7 In the 19th Century the stigma of business failure was such that it drove failed entrepreneurs to suicide. While there are fewer suicides in the 21st Century, the social stigma remains. EU citizens need to see entrepreneurs as doing something very worth while, even when they fail. Some failure is inevitable. A little less than three quarters (73.0%) of the 931 435 enterprises

that were born in 1998 within the business economies of Spain, Finland, Italy, Luxembourg, Sweden and the United Kingdom survived two years. Slightly less than half (49.1%) of the same cohort of enterprises survived five years through to 2003.

- 2.8 The Commission is right to assert that business creation, business success and business failure are each inherent in the market economy. It correctly highlights that as part of the general lack of societal appreciation and understanding of entrepreneurship, events such as business distress or business failure are neither sufficiently understood as a normal economic development nor seen as an opportunity for a fresh start. The EU must change its mind set. The more the stigma of failure attaches to a former bankrupt, the more at risk any new venture may be, and this risk attaches itself to all the stakeholders in the enterprise.
- 2.9 The US laws seek to balance the interests of debtors, creditors and society as a whole. It is the Opinion of the EESC that Member State laws should be drafted to achieve the same balance. As is described in Section 4 below, insolvency and the non payment of debts can create enormous difficulties for creditors and drive them in their turn into insolvency. Stripping the debt out of a company to give it a chance to restart can be most unfair on creditors. Insolvency laws need to strike the right balance.
- 2.10 From the point of view of society in general, keeping all or part of the enterprise in business may be the best solution. If the company is potentially viable, then all the stakeholders will benefit.
- 2.11 Employees' interests are served in a number of ways. In the event of an insolvency, Member States have implemented the Insolvency Directive which provides for payments to the work force. If an insolvent company can be rescued by the insolvency practitioners, then employees will continue to be employed. If a bankrupt entrepreneur goes back into business, then he creates new employment. Employment in any of these ways clearly serves society at large.

3. Gist of the Communication from the Commission

3.1 Public image, education and the media

3.1.1 The first step to tackle the negative effects of business failure is to publicly discuss it. In the EU the general public often perceives bankruptcy as a criminal affair, no matter the cause. The media have a positive role to play in tackling this misperception. The lessons to be learnt are as follows:

- (a) The benefits of a fresh start should be put forward in information campaigns and education programmes, showing that making several attempts goes hand in hand with a normal learning process, research and discovery.

- (b) The media can play a role in disassociating bankruptcy and fraud and disseminating the benefits of renewed entrepreneurship, thus improving the image of business restarters amongst the public at large and highlighting the value of their experience.
- (c) Further discussing the issue with all relevant actors should help uncover the many facets of stigma surrounding business failure.

3.2 The role of insolvency law

3.2.1 Making a fresh start after bankruptcy can be challenging from a legal standpoint. In many countries bankruptcy law treats everyone in the same way irrespective of whether the bankrupt was fraudulent or irresponsible or whether the failure was through no obvious fault of the owner or the manager, i.e. honest and above board.

3.2.2 Numerous rules impose restrictions, prohibitions and disqualifications on bankrupts solely on the basis of the existence of bankruptcy proceedings. This automaticity of approach takes no account of the risks that are an everyday fact of business life and implies a belief that a bankrupt is someone in whom society can have no trust or confidence. A radical shift in the rationale of insolvency laws is needed in the EU. The main points are as follows:

- (a) It is vital to create the right framework which, while protecting all parties' interests appropriately, recognises the possibility for an entrepreneur to fail and start again. Bankruptcy law should include a clear distinction between non-fraudulent and fraudulent bankrupts.
- (b) Entrepreneurs who go bankrupt through no fault of their own should be entitled to receive a formal court decision declaring them non-fraudulent and excusable. The decision should be publicly accessible.
- (c) An early discharge from remaining debts subject to certain criteria should be provided for in insolvency law.
- (d) Legal restrictions, disqualifications or prohibitions should be reduced.
- (e) Legal proceedings should be made simpler and faster, thus maximising the value of the assets in a bankruptcy estate prior to the reallocation of the assets. Typically, proceedings should last a maximum of one year.

3.3 Active support to businesses at risk

3.3.1 The stigma of business failure is one reason why many SMEs in financial trouble conceal their problems until it is too late. Timely action is crucial to avoid bankruptcy and a rescue is in many cases, preferable to liquidation. The main lessons are:

- (a) The number of insolvencies cannot be reduced to zero, but early support for viable enterprises will keep insolvencies to a minimum. Support measures should focus on bankruptcy prevention, expert advice and timely intervention.

- (b) Attention needs to be paid to the accessibility of support, as businesses at risk cannot afford expensive advice.
- (c) The networking opportunities provided by the EU and European business organisations should be fully exploited.
- (d) Insolvency laws should provide an option to restructure and rescue rather than focus solely on liquidation.

3.4 Active support to entrepreneurs restarting after failure

3.4.1 The main constraints that entrepreneurs face when setting up a second venture – resources, skills and psychological support – are not sufficiently addressed by public support. In general, fresh starts are deterred because of the lack of resources to set up a new business, notably of financial means. The lessons to be learnt are that:

- (a) Relevant authorities should devote sufficient financial means to fresh starts by removing barriers to public finance schemes for start-ups.
- (b) Banks and financial institutions should reconsider their very cautious attitude towards restarters, often based on negative credit ratings. The Commission plans to put this issue on the agenda of the Round Table of Bankers and SMEs.
- (c) EU countries should ensure that the names of non-fraudulent bankrupts do not appear on lists restricting access to loans in the banking sector.
- (d) Those responsible for public procurement should be aware that public procurement directives do not allow for former non-fraudulent bankrupts to be disadvantaged.
- (e) Adequate psychological and technical support and specific training and coaching should be available for restarters.
- (f) Relevant authorities should fuel links between potential restarters and customers, business partners and investors so that the needs of the restarters may be supported.

3.5 In conclusion, good national framework conditions for entrepreneurship are crucial to the full exploitation of the EU's entrepreneurial potential and to the creation of dynamic companies. The societal appreciation of successful entrepreneurship, vital to this end, should go hand in hand with a policy of promoting a second chance for entrepreneurs who have failed.

4. General Remarks

4.1 The EESC endorses the emphasis placed by the Commission on the need to overcome the stigma of business failure. The Commission is correct to assert that business creation, business success and business failure are each inherent in the market economy. It correctly highlights that as part of the general lack of societal appreciation and understanding of entrepreneurship, events such as business distress or business failure are neither sufficiently understood as a normal economic development nor seen as an opportunity for a fresh start.

- 4.2 Even so, the EESC is of the opinion that while much of the guidance embodied in the Communication is indispensable, parts of it do not seem very credible. The Committee's reservations are highlighted at various points in sections 4 and 5 of the Opinion.
- 4.3 The purpose and goal of entrepreneurial activity is to create a business which is both profitable and scaleable. Entrepreneurs innovate to satisfy customer needs which are either not being satisfied, or not being satisfied in the most efficient way.
- 4.4 An entrepreneur may identify a trading opportunity. For example, a London entrepreneur saw the opportunity for an import/export business between the UK and India, meeting needs in both countries. It filled a gap in the market. Other entrepreneurs fill gaps in the market by, for example, opening restaurants or hairdressing salons in communities that are not well provided for.
- 4.5 Amazon is a prime example of meeting needs in a more efficient way. Bookshops survive for those who have the time and inclination to browse. Amazon meets the needs of a different sector of the book-buying public.
- 4.6 Some entrepreneurs start a business to exploit advances in science and technology. Such businesses are often spin-outs from universities, research institutes or science based companies. Four London University professors have founded a company to provide image analysis services using proprietary software to improve the ways in which the therapeutic effect of drugs under development can be measured. Software IP is at the heart of this business. One of the professors has been appointed MD and he is in the process of finding out whether or not he is an entrepreneur.
- 4.7 In order to succeed, the entrepreneur needs three things above all else. First, he or she must have the necessary knowledge and experience to correctly assess the market opportunity and the know-how to make a reality of the business proposition, whether it is a new restaurant, an on-line travel service or a breakthrough in the application of science. The first step in any enterprise is to prove the proposition – "make it real". It means developing a product or service to the point where there are customers willing to pay the price which is necessary for the business to make profits and pay its way. Many would-be entrepreneurs fail at this point. Some can learn from their mistakes and start again. Others will never learn.
- 4.8 The second requirement is funding. Some start-up enterprises are sufficiently attractive to venture capitalists from the beginning. Most venture capitalists will not get involved until the entrepreneur has made the proposition "real". We do now have the risk capital scheme proposed by the EIB but, again, its capacity will be limited. Funding usually becomes available in tranches or rounds. If first phase funding produces good results, follow on funding is much easier to achieve.

- 4.9 More often than not, funding for the start up phase comes from family and friends. Bank loans are available, but the banks need security. If the business has no assets, banks take the assets of entrepreneurs as security. For the entrepreneur, family and friends, the crunch comes when they give personal guarantees. These guarantees will usually carry on beyond the start up phase because private companies will generally have to rely on the support of banks until the company goes public. If the bank calls in its guarantees, the entrepreneur may lose his or her home. In these circumstances tax and social security obligations can make the situation even worse.
- 4.10 In the Committee Opinions on "Tax incentives for R&D"¹ we have encouraged Member States to give tax relief to private individuals who invest in start up companies. Clearly such tax incentives could make it easier for entrepreneurs to capitalise new businesses.
- 4.11 Beyond the start up phase, the entrepreneur depends on the third indispensable component of success, a viable business model. This is the key to scaling up the business. The model depends on a set of ratios which encapsulate the elements of the business. Sales less product costs give a gross margin which, after the deduction of expenses, leaves a profit before tax sufficient to service and pay down bank loans. When a business model is dysfunctional, or when the management does not have the skill or experience to manage sales etc. to make it work, then those who have provided the bank guarantees are liable to be bankrupted. Clearly such a bankruptcy is a learning experience. If the entrepreneur has learnt the imperatives of the business model, there may be scope to restart.
- 4.12 Previously successful business models are always threatened by change in staff, customers, markets, technologies and competitors. After successfully founding a business, the entrepreneurs will be continually tested by change, particularly in businesses involved with technology. Entrepreneurs who fail the test of change may learn from the experience. Others, particularly second or third generation owners, may not.
- 4.13 In making the business model work, the role of the entrepreneur and his team is paramount. In particular, financial management skills are indispensable. A good business can be too successful and overtrade so that it gets to the point where it cannot pay its bills. In this case it may be put into administration by its creditors. Such businesses may offer every possibility of a successful restart.
- 4.14 Another financial trap can arise when a major customer defaults and fails to pay his bills, leaving the entrepreneur unable to pay his bills and the bank ready to foreclose. According to Commission statistics, one in four insolvencies is caused by late payment. In such a case, a restart may also be viable. The vulnerability of small and young companies is well recognised by both Member State governments and the Commission. The issue is addressed by the Late Payment Directive and will be covered again in the upcoming Small Companies Act.

¹ OJ C 10, 15/01/2008.

- 4.15 Some companies fail through no fault of their own for reasons that could not have been anticipated such as the fall out from the 9/11 event or the impact of extreme weather conditions. Even so, with foresight, insurance could have softened the blow. Therefore organisations which support small businesses are encouraged to introduce entrepreneurs to the benefits which prudential instruments can provide.
- 4.16 In summary, there are many ways in which an enterprise can fail, even with the best intentioned entrepreneur. In the start up phase, it may not be possible to establish a viable enterprise. Beyond the start, a flawed business model may still mean that the company has no future. On the other hand, potentially viable companies can fail because of mistakes made by the entrepreneurs as well as for reasons right out of their control. Such companies can and should be saved by receivers with most of the jobs protected.
- 4.17 It is important to distinguish between the company and its directors. Directors may go bankrupt while a receiver is rescuing the company and its employees. When a company fails the entrepreneurs may well be bankrupted because of the bank guarantees which they have given, even though their personal conduct was not fraudulent. It is these non-fraudulent entrepreneurs with which the Commission is concerned. Others, who fail through incompetence and a lack of vision probably have little to offer the economy, even if they can find financial backers. Not all bankrupt entrepreneurs deserve a second chance.

5. **Specific Comments**

5.1 Public Image, Education and the Media

5.1.1 Clearly the most powerful message which Member State governments can give to the general public will follow from the changes to insolvency law. When the law clearly encourages a second chance for entrepreneurs, this will be reflected in media messages.

5.1.2 Governments can also work with organisations and institutions which work closely with entrepreneurial businesses. The most clearly involved institution is the accountancy profession, while representative organisations for SMEs and sole traders can also play a part.

5.1.3 The Communication mentions the idea of an award programme for successful restarters. If the organisations mentioned above would adopt such schemes, favourable media comment might follow.

5.2 The role of insolvency law

5.2.1 The EESC fully endorses all the points made in the Communication in respect of insolvency law, subject of course to the detail of the laws ultimately put in place. These points are detailed in section 3.2 above and involve the formal recognition of non-fraudulent

bankruptcies, early discharge from debts and reduction of legal restrictions, disqualifications and prohibitions with accelerated proceedings. The medium term target should be that proceedings take no more than twelve months.

5.2.2 The EESC believes that it is imperative that all Member States complete the revision of their insolvency laws with the least possible delay. In addition to changes in the law, it is vitally important that bankruptcies be handled expeditiously by the courts. The process needs to be well organised. These changes are the centre piece of the Second Chance programme.

5.3 Active Support to Businesses at Risk

5.3.1 This is the second message contained in the Communication. It is not part of the Restart programme per se. Instead it is a programme designed to avoid bankruptcy and to preserve businesses and jobs. In this respect the thrust of the Communication is to head off avoidable failures through early warning, the provision of temporary funding and the services of advisors.

5.3.2 The only problem is that this programme is not very practical for the generality of SMEs since there are few mechanisms for the pro-active identification of businesses at risk amongst the tens of thousands of SMEs in each Member State. Even so, Member States are encouraged to make the most of such possibilities as do exist, e.g. the French use of the VAT authorities to provide an early warning of possible company cash flow problems. The Commission says that support measures should focus on bankruptcy prevention, expert advice and timely intervention. The problem arises when directors do not realise that their business is at risk. Member State governments will need to work with the Accountancy profession and SME support organisation to develop such pro-active measures as are appropriate to their SME culture.

5.3.3 The EESC does not underestimate the difficulties involved in providing such support. Government intervention to reverse market forces has the potential to be counter-productive and undermine market disciplines.

5.3.4 In public limited companies there is the double obligation that accounts are filed in a timely fashion and that the accountants and management certify that the company is a going concern, i.e. that it can pay its debts. The enforcement of such disciplines on all companies, especially the early filing of accounts, would improve the system of early warning alerts.

5.3.5 To the extent possible, the EESC welcomes this focus on businesses at risk since it offers the prospect of job preservation and continuity of employment.

- 5.4 Active Support to Entrepreneurs Restarting after Failure
- 5.4.1 Whereas between twelve and seventeen Member States have either changed or are changing their insolvency law, there is virtually no observed Member State activity in respect of this group of Commission recommendations.
- 5.4.2 The reason for this low level of activity is that, once again, a number of the proposal can be seen as running contrary to market forces. This is particularly true of the proposals that banks should be less than cautious and that relevant authorities should create support networks for restarting entrepreneurs.
- 5.4.3 It should be possible for the proposals which fall within the competence of Member State governments – public finance schemes, access to loans by non-fraudulent bankrupts and public procurement – to be implemented without too many problems even before the insolvency laws are changed.
- 5.4.4 It should also be possible for those who offer training to entrepreneurs to offer training to restarters as the demand emerges.
- 5.5 Other Commission Proposals
- 5.5.1 The EESC is pleased to endorse the new Commission website "for a second chance policy at <http://ec.europa.eu/sme2chance>. It will be of particular help to organisations involved in supporting Member State 2nd chance policy initiatives.
- 5.5.2 In its 2009 SME Spring event the Commission will feature fresh start and other second chance issues. The EESC would expect that this initiative will give added impetus to the "soft" elements of the Second Chance programme.

Brussels, 29 May 2008.

The President
of the
European Economic and Social Committee

The Secretary-General
of the
European Economic and Social Committee

Dimitris Dimitriadis

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