Dutch procedure to bind non-consenting creditors to restructuring plans one step closer

September 14, 2017

A draft bill on court confirmation of extrajudicial restructuring plans to prevent bankruptcy was published for public consultation on 5 September 2017. Interested parties may give feedback until 1 December 2017.

The draft bill is a revision of a previous draft bill (the Continuity of Companies Act II or WCO II) and incorporates consultation input from a number of observers, including De Brauw. The revised draft bill still contains substantial elements of a proposal published by De Brauw partners Ruud Hermans and Reinout Vriesendorp in 2013. Their proposal was, in turn, inspired by the UK scheme of arrangement and the US Chapter 11 proceedings.

The revised draft bill introduces a brief statutory procedure to bind creditors (including preferential and secured creditors) and shareholders to a restructuring plan. That plan amends or restricts their rights – if necessary by way of a cross-class cram-down – with the approval of the Dutch courts. No formal insolvency proceedings (that is, bankruptcy or suspension of payments) need to be brought and no trustee or administrator needs to be appointed. The debtor stays in full control during the entire process.

Compared to the previous WCO II proposal and following suggestions made by observers including De Brauw, the revised draft bill contains, in our view, substantial improvements to the class constitution test and to the limited grounds for cross-class cram-down. It introduces an absolute priority rule and certain additional features that practitioners have asked for. Those features include the possibility to amend or terminate onerous contracts and a temporary stay on collection and enforcement actions. We still see room for further enhancement and will therefore prepare consultation feedback once more. We invite you to share with us any thoughts you have, so that we can incorporate this in our submission.

Why has this instrument been introduced?

The revised draft bill aims to assist the rescue of operationally viable enterprises which are at risk of becoming insolvent due to a debt overload, where rescue may be jeopardised or even blocked by a small number of creditors or shareholders. It presupposes an amicable solution, but could also serve as a last resort for business rescue. With this new instrument, the Dutch government is in step with similar developments elsewhere in Europe. It is in fact likely that the new instrument will precede adoption of the proposed EU Directive on preventive restructuring frameworks.

Who can offer a restructuring plan for court confirmation and when?

The starting point is that the debtor offers a restructuring plan to all or some of his creditors and shareholders. Not all debtors have this right; only legal entities and individuals who practise an independent profession or carry on a business are eligible to offer a plan. In addition, if a debtor is heading for insolvency and refuses to offer a plan despite a creditor's request to do so, that creditor can ask the court to appoint an expert who may offer a plan on the debtor's behalf. An expert can also be appointed at a creditor's request if the debtor's plan has not been accepted by any voting class.

Under the revised draft, a debtor may only offer a plan if he anticipates that he will be not be able to continue paying his due and payable debts.

What are the contents of the plan, and who will be affected by it?

The debtor is free to determine the plan's content and structure, as he is best placed to assess how to obtain support from his creditors and shareholders. The plan can amend creditors' and shareholders' rights. For example, it can defer or partially release payment obligations, amend the terms of debt instruments (such as those included in an indenture, even if governed by foreign laws), exchange different types of debt instruments, swap debt for equity, or amend the debtor's articles of association. A plan may be limited to one category of creditor or shareholder. In addition, the confirmation of the plan may also affect the claim of creditors towards sureties, third-party security providers or co-debtors.

Support for the plan and the confirmation process

Stay

Like the previous draft bill, this revised draft bill does not provide for a generic automatic stay of insolvency proceedings. However, at the debtor's request, the court can stay insolvency proceedings and also – a welcome addition – collection and enforcement actions. In both cases, the stay can be granted for a maximum period of four months.

Class constitution and other preliminary disputes

Until the plan is submitted for voting, interested parties can approach the court to settle disputes on various issues, such as alleged inadequacy of the information provided by the debtor, admission of certain creditors or shareholders to voting, class constitution, voting procedures, etc. The court's decision is final and not subject to appeal. This should result in an expedited treatment of the voting and confirmation process.

Termination of onerous contracts

A welcome new feature of the revised draft bill is that a debtor can also propose to his counterparty to amend the terms of onerous contracts, for example lease or long-term supply agreements. If the counterparty does not accept the proposal, the debtor may terminate the contract, subject to a maximum three-month notice period. The compensation the counterparty is entitled to as a result of the amendment or termination can subsequently be limited under the plan.

Ipso facto clauses without effect

Ipse facto clauses, which would, for example, give creditors the

right to amend, suspend or terminate contracts in connection with the plan, remain without effect.

Tailor-made measures

In addition, the court may order any measures it deems necessary to adequately protect the interests of the creditors and shareholders.

New money security
New money providers are protected through a refutable presumption that pledges and mortgages are not voidable on the basis of fraudulent conveyance if they have been provided by the debtor for new money intended to ensure the debtor's going concern while the plan is being negotiated.

Class constitution and voting

The plan does not have to be offered to all creditors and shareholders. Logically, voting is limited to those creditors and shareholders whose rights are affected by the plan. Classes are constituted if creditors and shareholders whose interests or rights (prior to or as a result of the plan) differ to the extent that their positions cannot be deemed similar. These creditors and shareholders will be placed in separate classes for voting purposes. Creditors and shareholders who would rank differently in the debtor's bankruptcy are in any event placed in separate classes.

A plan is adopted when all classes have approved it. For a class of creditors to approve the plan, creditors in that class representing at least two thirds of the total value of the claims held by those who voted in that class must vote in favour of the plan. The same applies to shareholders, provided that the shareholders represent at least two thirds of the total value of the issued capital held by those who voted in that specific class.

Plan confirmation and cram-down

After approval of the plan by at least one class, the debtor may request court confirmation of the plan. If approved by all classes, the court must declare the plan binding on all creditors and shareholders ("universally binding"), including on those who voted against it, unless specific circumstances apply. For example, the court will not confirm a plan if a creditor or shareholder receives less under the plan than he would receive in bankruptcy (the "best interest of creditors test"), or if fulfilment of the debtor's obligations under the plan is not sufficiently guaranteed.

If one or more classes of creditors or shareholders vote against the plan, the court can still declare the plan universally binding despite this rejection. This leads to a cross-class cram-down. However, creditors and shareholders who voted against the plan can request the court to deny confirmation on the basis of one of the following grounds. Denial is possible if, under the plan:

- creditors or shareholders are not repaid in full, while a lower-ranking class receives or retains rights (the "absolute priority rule"), unless those rights constitute arm's length consideration for the provision of a new loan or new capital;
- creditors or shareholders are not repaid in full, while a higher-ranking class receives more than 100% of their claims or the nominal value of the shares (the "not more than 100%-rule");
- creditors or shareholders receive less than another class of equally ranked creditors or shareholders, or creditors' or shareholders' rights are modified while other creditors or shareholders with an equal or lower rank remain outside the plan, in both cases without reasonable ground (the "no unfair discrimination-test"); or
- creditors do not have the right to opt for a cash payment equal to what they could reasonably expect to receive on liquidation of the debtor's assets in bankruptcy.

Under the revised draft bill, the grounds for refusal of the cram-down have shifted from principle-based to rule-based. This is a welcome move, as the latter provides more clarity and, hence, deal certainty.

Effects of a plan confirmation

If the court confirms the plan, all creditors and shareholders who were eligible to vote are bound by its terms. Consequently, their rights against the debtor are amended in accordance with the plan. If the implementation of the plan requires a resolution by the general meeting, the declaration of the court replaces that resolution. This provides a solution if shareholders resist an intended restructuring on unfair or unreasonable grounds, as they will be unable to block the implementation of the plan by refusing to adopt the necessary resolutions.

Restructuring of groups

The bill facilitates the restructuring of a group of companies through one single plan. The plan can amend or cancel not only the creditors' principal claims on the debtor, but also any future recourse claims made by sureties, third-party security providers and co-debtors. If a surety, third-party security provider or co-debtor faced insolvency as a result of the amendment or cancellation of a recourse claim, the plan could also amend or cancel the rights of creditors towards that surety, third-party security provider or co-debtor. For example, a group financed through bonds issued by its finance company and guaranteed by the parent and other group companies will have the opportunity to restructure effectively if the plan amends the rights of the bondholders not only against the finance company but also against the parent and other group companies.

Relatively quick process

The process could be relatively quick due to:

- the short timelines between the offer of, the voting on, and the confirmation of the plan,
- the newly-introduced procedure to settle class constitution and other preliminary disputes at an early stage,
- the court's decision on preliminary disputes and on the confirmation of the plan being final and not subject to appeal, and
- the maximum four-month stay of insolvency proceedings and collection and enforcement actions speeding up the process.

What impact will this legislation have, if enacted?

As a debtor, the revised bill will provide a quick and easy way to restructure your debts without being limited by opposing creditors or shareholders. As a creditor, you will need to be aware that your claims on and contract with a debtor can be amended against your will. As a shareholder, the revised draft bill provides additional tools for the benefit of your investment, but you could face dilution of your stake if new capital is provided under a plan.

Submitting feedback on the draft bill

The revised draft bill went into public consultation on 5 September 2017. Interested parties may submit feedback until 1 December 2017. Although we believe that the revised draft bill contains substantial improvements, we still see room for further enhancement and will therefore prepare consultation feedback once more. We invite you to share with us any thoughts you have, so that we can incorporate this in our submission.

Useful sources

Dedicated De Brauw website (with an unofficial English translation of the bill and the explanatory memorandum)
Public consultation (in Dutch)