

Composition outside insolvency proceedings

The Dutch Scheme

The Dutch Scheme is coming

Corona-crisis expedites legislative process

- Bill pending in Parliament since 5 July 2019
- By letter of 27 March 2020 the government designated the Bill as an urgent bill, requesting parliament to handle the bill with priority with a view to entry into force on 1 July 2020.
- First legislation that implements the recently adopted EU Restructuring Directive (EU 2019/1023)
- Inspired by UK Scheme and US Chapter 11
 - Combines best of both to create a fast and flexible restructuring procedure



Key features

Fast and (cost) effective restructuring instrument to preserve going concern value

- Debtor in possession
- Majority of votes binds class
- Court can cram down dissenting classes
- Low on formalities → minimal court involvement
- Quick → procedure can be finalized within 3 - 5 weeks
- Flexible
 - Maximum freedom as to plan contents
 - Can extend to all creditors (including secured) and equity holders
 - Court can take bespoke measures
- Choice between public and confidential process
 - Public procedure covered by Insolvency Regulation → jurisdiction based on COMI
 - Confidential procedure → jurisdiction based on connection with The Netherlands, which can extend to non-Dutch (group) companies
- Enhancement of deal certainty
 - 'snooze-you-lose' loss of standing to raise objections against court confirmation
 - Ability for court to render intermediate decisions
 - Confirmation by court not subject to appeal
- Measures to maintain going concern
 - Possibility to request stay (individual or general)
 - Right to require performance under key contracts notwithstanding pre-existing default
 - *Ipso facto* and change of control provisions are set aside by operation of law
 - Protection of security for DIP financing
- Specialized judges
 - One specialised team
 - 11 judges and 11 legal assistants



Access to the procedure / authority to offer plan

- Access requirement → Expected insolvency
 - "*debtor can reasonably be expected to become insolvent*"
 - Can be 12 months in advance e.g. if loan matures without prospect on refinancing
- Authority to offer plan by either (i) debtor or (ii) court appointed restructuring expert
- Offer by the debtor
 - One shot only → not eligible if it has offered composition plan during past three years that has failed
- Offer by court appointed restructuring expert
 - If court appoints expert, expert is authorized to offer plan
 - Debtor has authority to request expert to (also) submit its own plan for voting
 - Expert decides which plan is submitted to court for confirmation
 - Authority to request appointment: each individual creditor, each shareholder and the works council
 - Request can also be filed during negotiations on plan (to be) proposed by debtor
 - Court will honour request if access requirement (expected insolvency) is met, unless it is clear that interests of joint creditors are not served by the appointment. Examples set out in explanatory notes:
 - negotiations on a plan proposed by debtor are in advanced stage
 - filing of a request with purpose to create 'nuisance value'



Contents of the plan

Freedom of contract + right to amend or terminate onerous contracts

- Plan can be limited to certain classes (e.g. only secured creditors and shareholders)
- Possibility to issue ordinary and/or preferred equity
 - Against new funds and/or conversion of debt
 - Court confirmation order constitutes corporate action
- Amend or terminate onerous contracts
 - Statutory possibility to unilaterally propose amendment or termination of contracts
 - If counterparty does not accept proposal, right to terminate
 - Subject to adoption and confirmation of composition plan
 - Notice period for termination max. 3 months
 - Counterparty will have claim for damages resulting from early termination
 - Can be restructured under the composition plan
 - Not applicable to employment contracts → separate legal regime



Contents of the plan – group restructuring

Plan can extend to Dutch and non-Dutch group companies

- Starting point – plan no effect on claims / remedies against third-party debtors / security providers
 - Third party that pays debt to creditor will acquire the rights such creditor will receive under the plan, but only if and to the extent the creditor would otherwise receive a total consideration with a value in excess of its claim
- Exception – The plan can extend to rights and claims on group companies of the debtor – four requirements:
 - 1) The rights and claims on the group companies go to take recourse for a claim of the debtor
 - 2) The relevant group companies themselves meet the 'expected insolvency test'
 - 3) The relevant group companies agree to be included or the plan is offered by a court appointed expert
 - 4) The Dutch courts would have jurisdiction if the relevant group company would offer a plan itself
 - See below
- Test for court confirmation
 - The creditors will under the plan receive at least the same consideration for their claims against the relevant group companies as if the relevant group company would have offered a plan itself



Jurisdiction of the Dutch courts / recognition

Maximum flexibility based on choice between disclosed or confidential procedure

- Public procedure
 - Will be placed on Annex A of the EU Insolvency Regulation
 - Automatic recognition in EU as per the Insolvency Regulation
 - Jurisdiction limited to debtors and group companies with COMI in the Netherlands
- Confidential procedure
 - Outside of EU Insolvency Regulation
 - Jurisdiction of Dutch courts if (i) debtor or affected party are domiciled in the Netherlands or (ii) if there is a sufficient connection with the Dutch jurisdiction → very broad; examples:
 - Debtor has establishment or substantial assets in NL
 - Substantial part of the debts that are affected by the plan are governed by Dutch law or provide for choice of forum for Dutch courts
 - Substantial part of the group to which debtor belongs consists of companies domiciled in NL
 - Debtor is liable for debts of other debtor in respect of which Dutch courts have jurisdiction
 - Recognition outside NL on the basis of local rules of private international law
 - E.g. recognition as foreign insolvency proceeding under Chapter 15 or UNCITRAL Model law



Voting, required majority and class formation

Voting per class

- Creditors and shareholders whose rights are affected by the plan are entitled to vote
 - No exclusion of equity holders / related parties
 - If legal and beneficial title is split, the holders of beneficial title are entitled to vote
- Required majority (per class):
 - $\geq 2/3$ of claims that have voted (as regards creditors) or voting rights that were exercised (as regards shareholders) → **no** head-count
 - non-voting creditors / shareholders are **not** taken into account
- Class formation
 - Parties should be included in different classes if either:
 - they have a different rank or different rights in the event of liquidation in bankruptcy; or
 - they receive different rights under the proposed plan
 - Creditors with same rank / rights in bankruptcy can therefore be in different classes and be offered different consideration under the plan
 - Subject to consent other classes or successful cross-class cram-down (see below)



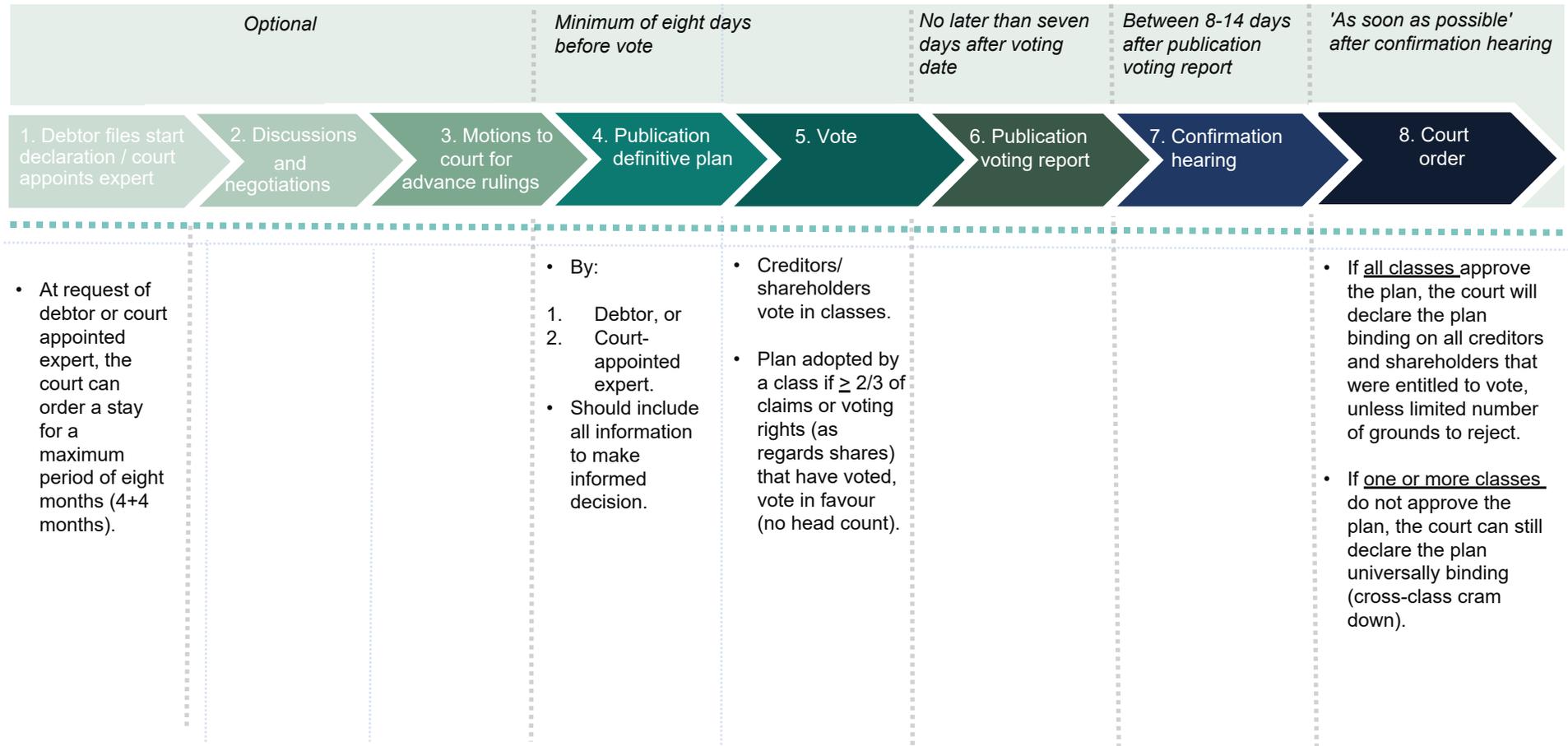
Process - steps

Formal process can be finalised in 3 – 5 weeks

1. Filing of start declaration with court by debtor **or** appointment by court of restructuring expert
2. Discussions and negotiations on plan
3. Option to request court decision in advance on (inter alia):
 - Satisfaction of disclosure requirements
 - Admission to voting of individual creditors / shareholders (amount of debt / number of voting rights)
 - Constitution of classes and voting procedure
 - Possible grounds to refuse court confirmation to cram-down consenting classes
4. Publication of definitive plan – min 8 days before voting date
5. Vote
6. Publication of voting report – within 7 days
7. Confirmation hearing – minimum 8 days, maximum of 14 days after voting report
8. Court order - 'As soon as possible' after confirmation hearing
 - **Not** subject to appeal



Process - steps



Additional procedural rules for SME's

As per EU Restructuring Directive

- If Debtor is SME and plan is offered by court-appointed expert, the following requires debtor approval:
 - Submission of Plan for voting
 - Submission of Plan for court confirmation that involves cross-class cram-down
- If (Board of) debtor refuses approval, expert can lodge proceeding with court:
 - Board should substantiate reasons to withhold approval
 - If court determines that reasons are not valid, court can render decision that replaces approval
 - Interference / pressure by shareholder is **no** valid reason
- SME defined in accordance with EU Directive 2013/34/EC as enterprise (= debtor + its group companies):
 - < 250 employees; and
 - either:
 - annual turnover \leq EUR 50 million; or
 - balance sheet total \leq EUR 43 million



Plan Confirmation

- By District Court
- Cross-class cram down possible
- Court will confirm
 - If adopted by at least one class of creditors (not equity)
 - If relevant consenting class is 'in the money' (i.e. expected to receive distribution in a bankruptcy)
 - Unless there is a ground for refusal
- Grounds for refusal – distinction between
 - Grounds investigated by court *ex officio*
 - Grounds investigated only if invoked by dissenting creditor / shareholder → distinction:
 - dissenting creditor / shareholder of consenting class
 - dissenting creditor / shareholder of dissenting class (cross-class cram down)



Grounds investigated *ex officio*

Can be invoked by **any** creditor/shareholder that has voted against

- Debtor not eligible to offer composition (i.e. no expected insolvency)
- Each of the following, in each case unless this cannot reasonably have affected outcome of voting
 - insufficient disclosure of information
 - no proper constitution of classes
 - no proper voting procedures
 - a creditor or shareholder has not been admitted to voting or for incorrect amount / number of shares
- Insufficient safeguards for performance under the plan
 - This regards performance of the plan as such, not performance under instruments issued thereunder
- In the event debtor attracts new financing for performance under the plan, the interests of the joint creditors are adversely affected thereby
- Plan has been adopted by unfair means (e.g. fraud, prejudicial treatment of individual creditors / shareholders)
- Other important reasons
 - discretion of court



Ground investigated if invoked by dissenting member consenting class

Investigated only if invoked by creditor / shareholder that has voted against

- **'Best of creditors interests test'** – worded as follows:

*Court **can** reject confirmation on the request of a dissenting creditor / shareholder if it summarily appears that such creditor under the plan is worse off than it would be in case of a liquidation in bankruptcy*

- Best of creditors interests test is based on comparison of:
 - expected distribution in event of liquidation in bankruptcy; and
 - **value** of consideration receivable under the plan (i.e. including value of shares / debt instruments)
- Wording "can" provides court discretion to reject plan on this ground or not
 - Justified by circumstance that majority of the class has voted in favour
 - Members of dissenting class protected by additional grounds to reject cross-class cram down



Grounds to reject cross-class cram-down

Investigated only **if** invoked by member of dissenting class that has voted against

- 'Absolute priority rule'
 - Breached in case of unfair distribution of reorganisation value realized by the Plan
 - Basis → plan should distribute in accordance with rank (statutory and contractual)
 - Exception is permitted if justified by (i) reasonable ground and (ii) interest of relevant opposing creditor / shareholder is not prejudiced thereby → Examples:
 - Payment of (certain) trade creditors in full to preserve going concern value
 - Equity stake for entrepreneur in exchange for continued commitment to support business
- 'Cash option' - for creditors of non-consenting class
 - Creditors of non-consenting class should be offered option under the Plan to choose distribution in cash equal to amount they could expect to receive in the event of a liquidation in bankruptcy
 - Rationale: no justification to force non-consenting class to continue to finance debtor
 - Particularly relevant for secured creditors → expected recovery on secured assets in bankruptcy
 - TBD whether cash option is choice of individual creditor or majority decision of class



Who can object to confirmation? – Limitations to standing

Limitations to standing prevent nuisance value and increase deal certainty

- Only creditors and shareholders that have voted against have standing in confirmation proceedings
- 'Snooze-you-lose' → failure to protest results in loss of authority to invoke relevant ground for rejection
 - A creditor / shareholder that fails to protest on the basis of a possible ground for rejection within a reasonable time after it discovers or should reasonably have discovered the relevant circumstances, loses the right to oppose Plan on this ground
 - Rationale: timely protest opens possibility to find solution or request court for intermediate decision
- Therefore - loss of standing for creditors and shareholders that:
 - did not vote or voted in favour
 - did not raise objection at early stage



Supporting measures – Court ordered stay

Court can order stay as required to continue going concern

- Authority to request vested in:
 - Debtor that has filed a start declaration or undertakes to submit plan within two months
 - Court-appointed restructuring expert
- Duration: maximum of 4 months initially with possibility to extend to max of eight months in total
- Stay can be general (applicable to all creditors) or limited to certain creditors (e.g. secured creditors)
- Legal effect of court ordered stay:
 - 1) No recourse on assets or possession of assets, other than with court approval
 - 2) Court can lift attachments → on request and if necessary to continue business operations
 - 3) Suspension of court proceedings to start formal insolvency proceeding (bankruptcy / moratorium)
 - 4) Default under agreement prior to stay, does not give right to terminate or suspend performance
 - 5) Continued authority of debtor to use, consume and dispose of encumbered assets
- Conditions:
 - Items 4 and 5 subject to adequate protection of affected creditors
 - Court can impose further conditions (e.g. timing to submit plan, reporting, appointment of observer)



Supporting measures – Overrule of *ipso facto* provisions / DIP financing

Ipsa facto provisions set aside / court authorisation protects security for DIP Financing

- Statutory provision that sets aside *ipso facto* contractual provisions
 - If triggered by Plan proceedings or related events
 - Also sets aside change of control provision triggered by debt-to-equity swap
- Possibility to request court authorisation for specific legal acts
 - Authority of debtor and court appointed restructuring expert
 - Effect: excludes avoidance of relevant act on account of fraudulent preference
- Test to be applied by court to grant authorisation:
 - Relevant legal act is necessary to continue going concern until plan confirmation
 - Interests of the joint creditors are served by legal act
 - No individual creditor is materially prejudiced as a result
- Most likely use → security for DIP Financing
 - Not limited thereto → can also be used for other legal acts
 - No (US style) super priority DIP financing



Bespoke measures

Court has discretion to take far reaching bespoke measures

- At request of debtor or at court's own motion
- If court ordered stay → At request of individual creditor / third party that is affected
- Wide authority
 - Can deviate from or set aside statutory provisions
 - Purpose: protection of interests of creditors / shareholders
- Examples:
 - Voting record date
 - Period within which Plan should be submitted for voting
 - Reporting requirements
 - Appointment of observer (with statutory information rights) if there is no court-appointed expert



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