

Restructuring in Germany, France and The Netherlands

Christine Borries - Hogan Lovells

Jean Baron - CBF Associes

Krijn Hoogenboezem- RESOR



Topics

- Overview insolvency proceedings
- Key aspects per jurisdiction / most commonly used process
- European development: Pre-insolvency proceedings



Overview insolvency proceedings



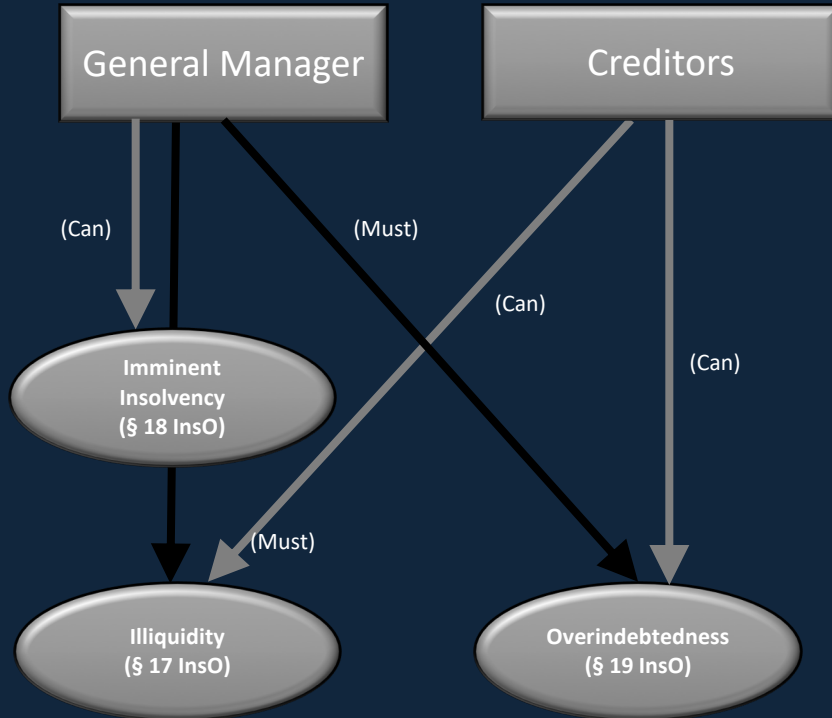
Overview



- German law generally provides for unitary insolvency proceedings, the outcome of which may be liquidation or reorganisation. The main purpose of the proceedings is to satisfy the creditors' claims in the best way possible.
- A special tool to reorganise a company is the insolvency plan (*Insolvenzplan*) – as the case may be – as debtor-in-possession proceedings
- Insolvency proceedings are supervised by the court and are subject to several creditor protection rules
- The debtor acts through an insolvency administrator (IA) or through the management which is supervised by a trustee (*Sachwalter*)
- Since 01/2021 a reorganization under the new German Scheme (*StaRUG*) has become an additional option



Obligation to file for Insolvency, § 15a InsO



Neutral rule concerning the legal form:

- Legal Persons
- Associations without legal personality
- Even B.V., Ltd., etc. as long as COMI in Germany

Criminal liability due to deliberate/negligent infringements:

- Deferred, defective or delayed application
- Fine or arrest up to 3 years
- Employment ban up to 5 years

Illiquidity, § 17 InsO

The debtor is illiquid if he is
unable to meet his due and payable payment obligations.

(§ 17 Abs.2 S.1 InsO)

(Case law: at least 90 % within three weeks)



Overindebtedness, § 19 InsO

The debtor is overindebted if the debtor's assets no longer cover his payment obligations, unless the ability of the company to continue as a going concern within the next twelve (four)* months is predominantly likely under the circumstances.
(§ 19 Abs. 2 Satz 1 InsO)

→ Two-fold Test:

1. Going Concern Forecast
2. If negative: Insolvency-based valuation of liquidation value (e.g. including hidden reserves and charges)

*The reduction of the forecast period is valid until 31.12.2023 and is intended to mitigate the economic impact of the Ukraine crisis. The forecast period of 12 months is decisive again since 01.09.2023.

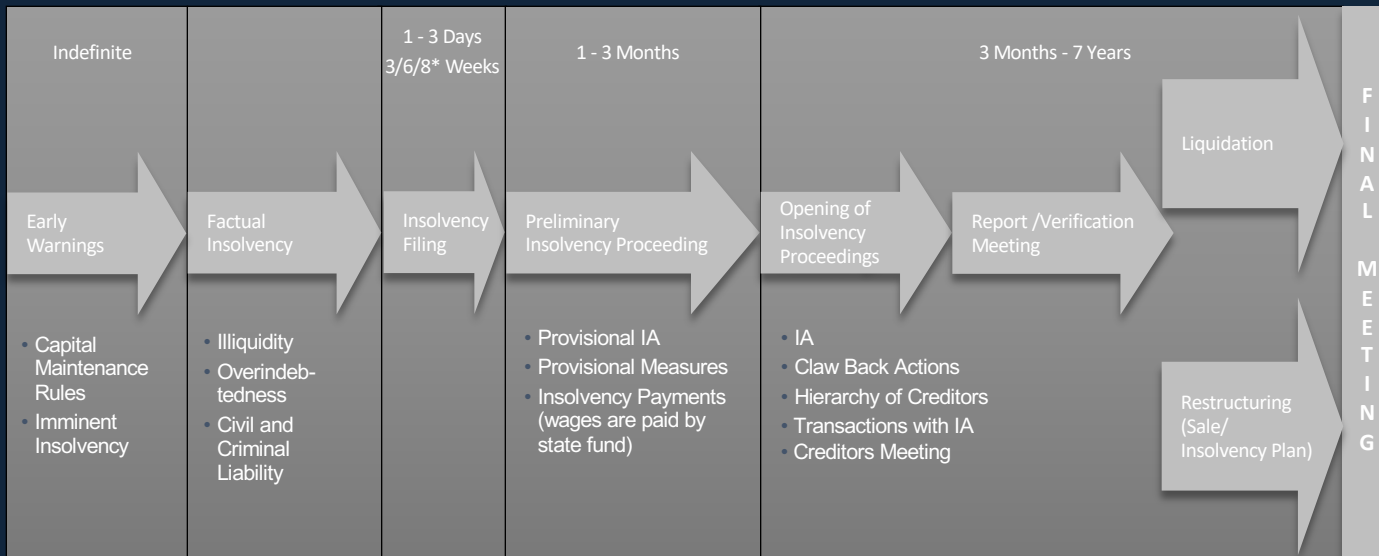


Impending Illiquidity, § 18 InsO

The debtor is impending illiquid if he is likely to be unable to meet his existing obligations to pay at the date of their maturity. In general, a forecast period of 24 months is to be taken as a basis.
(§ 18 Abs. 2 InsO)



Course of Insolvency Proceedings

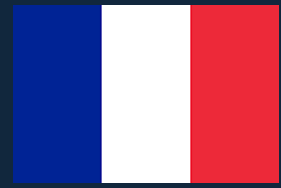


*The extended insolvency filing period of 8 weeks is valid until 31.12.2023 and will be max. 6 weeks from then on.

General Legal Consequences of opened insolvency proceedings

- Stay on individual actions and enforcement measures initiated by creditors against the insolvent company.
- IA is charged with the administration of the debtor's assets and business. The management of the insolvent company is no longer in charge of the company affairs.
- Executory contracts generally remain in place but mutual obligations are suspended during the proceedings. The IA can decide to enter into the contract or to finally refuse fulfilment. Depending on his choice, the creditor's respective claim is either preferential or a mere insolvency claim.
- The administrator can challenge certain transactions entered into prior to the opening of insolvency proceedings which constitute an unfair preference and have an adverse effect on insolvency creditors as a whole ("claw back right").





FRENCH LAW PROVIDES A DUAL SYSTEM :

- Pre-insolvency proceedings (Mandat ad hoc & Conciliation)
- Judicial proceedings (Sauvegarde, Redressement & Liquidation)

PARTICULARITY :

- Judges elected among traders
- 2 different independent professionals
 - ✓ *Administrateur Judiciaire (restructuring)*
 - ✓ *Mandataire Judiciaire (liquidation)*



Proposal for a directive of the European Parliament and the Council harmonising certain aspects of insolvency law, 7 déc. 2022

TRANSPOSITION OF THE « RESTRUCTURING AND INSOLVENCY » DIRECTIVE INTO FRENCH LAW
Ordonnance n°2021-1193 of 15 September 2021

2022

2021

2014

2010

CONCILIATION, « PREPACK » & FAST TRACK SAFEGUARD PROCEDURE
Ordonnance n°2014-326 of 12 March

2005

FAST TRACK FINANCIAL SAFEGUARD (*)
Law 2010-1249 of 22 October 2010
➢ Financial Cram-down
(*) Merged in 2021 with FAST TRACK SAGEGUARD

BUSINESS SAFEGUARD ACT
Law 2005-845 of 26 July 2005)

1985

REORGANIZATION & LIQUIDATION PROCEEDINGS
Law 85-98 of 25 January 1985
➢ Formal restructuring

1984

AMICABLE SETTLEMENT
Law 84-148 of 1 March 1984
➢ Lightly Court supervised

Dutch Insolvency law



Two insolvency proceedings :

- Liquidation proceedings - Bankruptcy (*faillissement*)
- Reorganisation proceedings – Suspension of payments (*surséance van betaling*)



Suspension of Payments (reorganisation)

- Temporary liquidity issues: foresee that cannot continue to pay debts when they fall due
- Only debtor can file
- Debtor partially in possession – jointly with administrator
- Not very successful (But: Steinhoff)



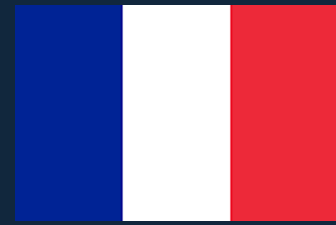
Bankruptcy

- Non-temporary liquidity issues: has ceased to pay debts as they fall due
- Creditors and debtor can file
- Debtor divested of powers – trustee in control



Most commonly used process





- Very small firms : 60% end up directly in Judicial Liquidation
- Small/medium/large caps :
 - ✓ *Pre-insolvency (average 60 to 70% success) or safeguard where business is not totally in illiquidity or in order to prepare a formal restructuring plan (sale plan or reorganization plan),*
 - ✓ *Direct restructuring plans with Reorganisation proceedings when wagers are unpaid (AGS intervention).*





Bankruptcy: most commonly used to restructure

- Expedited business / asset sale (in bankruptcy)
- UK style pre-pack (similar steps and timeline)
- Employees (applicability TUPE a risk in pre-pack sale of business - CJEU)
- Sale "free and clear" requires consent of secured lenders



Asset / Business Sale



- The IA ordinarily tries to use the 3 month period during which state funded wages are paid, to sell the business or parts of it to an investor
- Thus, the sale of operations is often pre-arranged prior to the opening of main insolvency proceedings and only becomes effective upon such proceedings being formally opened
- In general, the sale of assets is free and clear of any liability on the part of the buyer, provided that the insolvency proceedings have actually been opened. This can be facilitated by carving out the profitable parts of the operations into an SPV, while retaining liabilities, redundant employees and nonprofitable parts of the business in an entity to be liquidated ("*smart way of cherry picking*")




Reorganisation process (in insolvency)





Flawed reorganisation system in formal insolvency proceedings for reorganisation

- Negative stigma
 - Does not bind secured or preferential creditors
 - No cram down of shareholders
 - No / limited ability to reduce workforce
- 

Protective Shield Proceedings



- Preparatory procedure for a reorganization of the insolvent legal entity through an insolvency plan in combination with self-administration (*Eigenverwaltung*)
- No independent reorganisation procedure, but the establishment of special rules during the preliminary insolvency proceedings
- Essential characteristics:
 - Deadline for setting up the insolvency plan
 - Determination of the provisional trustee (*vorläufiger Sachwalter*)
 - Establishment of estate liabilities possible
 - Protective court orders against enforcement measures possible



Self Administration (*Eigenverwaltung*)

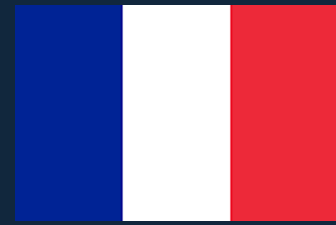
- In case of self-administration, debtors can manage and dispose of the insolvency assets themselves under the supervision of a (preliminary) trustee (*Sachwalter*)
- As of 1 January 2021 the requirements to be eligible for self-administration have increased.
- Required is a self-administration plan, which must include:
 - financial plan for a period of six months with a well-founded presentation of the sources of financing that are to ensure the continuation of ordinary business operations and the coverage of the costs of the proceedings during this period.
 - concept for the conduct of the insolvency proceedings, containing a presentation of the nature, extent and causes of the crisis, setting out the objective of self-administration and describing measures to achieve the objective.
 - description of the status of negotiations with creditors, persons involved in the debtor and third parties on the measures envisaged must be prepared.
 - debtor must present the arrangements it has made to fulfil its obligations under insolvency law.
 - a reasoned description of any additional or reduced costs that are likely to be incurred in the course of self-administration compared to regular proceedings.



Insolvency Plan

- The insolvency plan can be submitted either by the debtor or by the insolvency administrator only within pending insolvency proceedings
- The content of an insolvency plan can be freely arranged and include all provisions that could be agreed upon in an individual contract (e.g.: waivers and deferrals of claims or restrictions of security rights)
- The insolvency plan can also stipulate corporate structural measures such as reduction/increase of share capital, debt-to-equity swaps or contributions in kind. The plan must describe the proposed measures for reorganising the debtor and how the plan affects the rights of creditors and/or shareholders





- Reorganization throughout a formal proceeding but usually prepared in pre-restructuring
- Affected parties
- Cramdown possible within classes of "affected parties" (voting rule : 2/3 majority of participants)
- Cramdown of shareholders mainly in sale plans
- Led by debtor and JA with ability for creditors to propose an alternative plan (little appetite for lenders led plan in French banks)



EFFECTS OF THE STAY ON CASHFLOW

Opening →

- Liabilities frozen
- Loan instalments frozen
- No automatic termination of workers contracts:
 - ✓ Wage Guarantees Insurance (AGS) intervention for up to 3 months salary
 - ✓ Possibility of dismissals
- Termination of contracts

18 months maximum

Procedure →

Reorganization plan
(*Plan de continuation*)

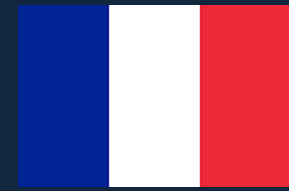
Sale plan
(*plan de cession*)



Pre-insolvency proceedings



FRANCE PRE-INSOLVENCY SYSTEM (1)



- 2 Confidential proceedings, Court-lightly supervised :
 - ✓ *Mandat ad hoc*
 - ✓ *Conciliation* } driven by JA (Judicial Administrator)
- Debtor initiates before default, JA pilots discussions with stakeholders
- Independance of JA thanks to decision of the President of the Court
- Subordination clauses and absolute priority rule respected
- Exit: contractual agreement, protocols
- Settlement recorded or homologated by Court (unfair



FRANCE PRE-INSOLVENCY SYSTEM (2)

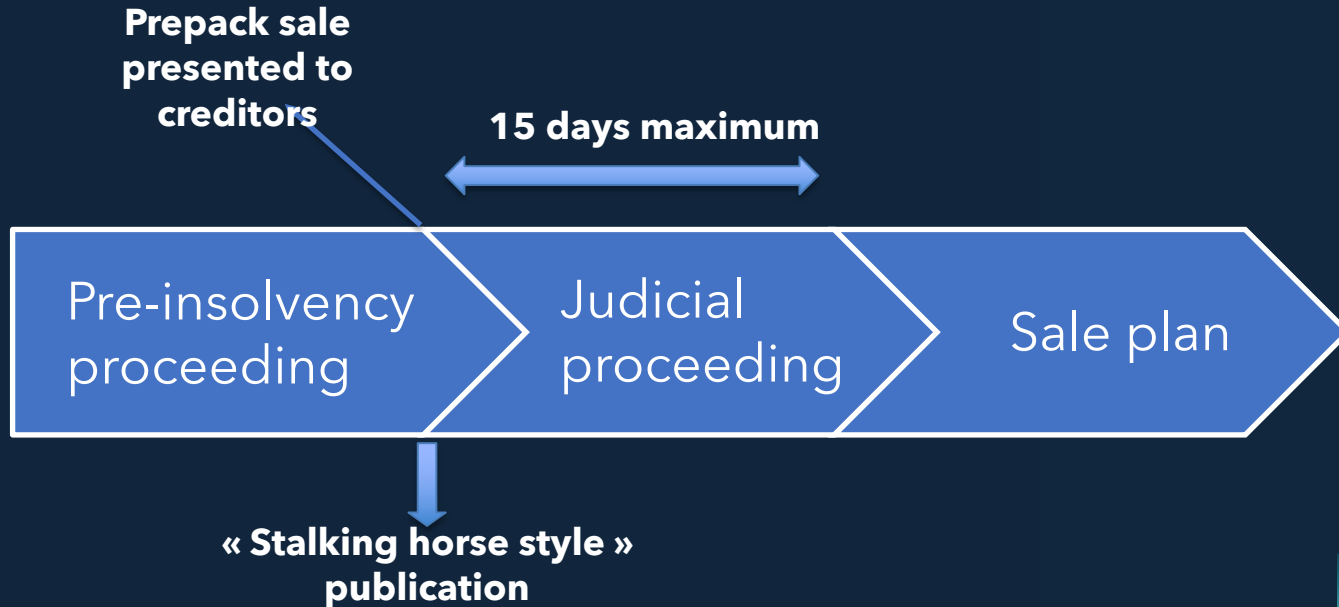
- No voting rules. In practice, the settlement is adopted if there is unanimous agreement
- New Money privilege
 - ✓ *No automatic suspension of proceedings against debtor or stay (only 24 months moratorium can be imposed on a dissenting creditor by the President of the Court)*
 - ✓ *No automatic stay (before Directive) in amicable settlement. If stay and majority rules are necessary → Fast-track safeguard*



Safeguard & Fast-track safeguard



Pre-pack Sale



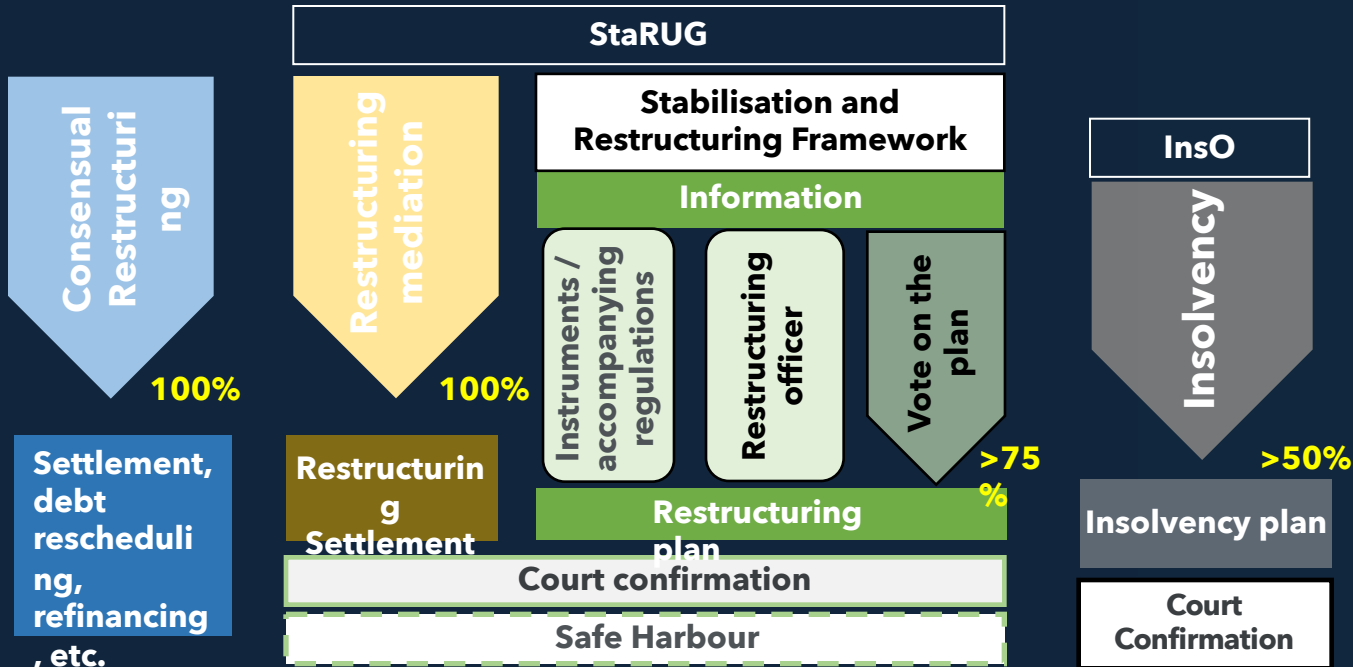
The German Scheme ("StaRUG")



- On January 1 the "Act on the Stabilization and Restructuring Framework for Enterprises" came into force.
- Implementation of the EU Restructuring Directive
- It enables non-insolvency reorganization for threatened insolvent companies
- The StaRUG creates a legal framework that is intended to enable sustainable and "insolvency-repellent restructuring". In this respect, the procedure under the StaRUG precedes the insolvency proceedings in terms of time and can therefore also be described as preventive restructuring or reorganisation.
- The new procedure has the advantage that it is not yet tainted with the stigma of insolvency.
- The core of the measures provided for in the StaRUG is the restructuring plan. The restructuring plan offers almost the same possibilities as an insolvency plan.
- The objective of every restructuring plan must be the elimination of insolvency or the threat of insolvency and, on the other hand, the guarantee of the company's ability to continue as a going concern. Therefore, it is precisely the avoidance of insolvency and the ability to continue as a going concern that must be concretely presented in the restructuring plan.



Overview of the new restructuring procedure under StaRUG



Overview - StaRUG

What can be regulated in the restructuring plan?



- Drafting of restructuring claims
- Separation entitlements
- Contractual covenants, also in other agreements
- Interference in company rights up to expropriation
- Fresh Money
- Interference with third-party collateral within the group



- Employee claims / pensions
- Tortious claims
- Interference in legal relationships for the future
- No intervention und no termination of ongoing contractual relationships



Pre-insolvency proceedings: WVOA: Dutch Scheme, available since 2021



- Plan proceedings when likelihood of insolvency
- Good parts of Ch11 and UK schemes
- Implementation of EU Directive
- EIR optional (!)



WHOA (vs StaRUG, UK Scheme, CH 11)

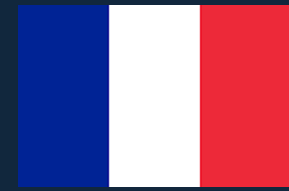
- 67% per class, no head count
- Binds secured, preferred creditors and shareholders
- Cross class cram down if one in the money class votes in favour (using absolute priority rule)
- Can also restructure group guarantees
- Ability to terminate long term contracts



WHOA (vs StaRUG, UK Scheme, CH 11)

- Limited court involvement - no court entry test
- Very fast - can be completed in 6 weeks
- Restructuring expert, if appointed, has power to offer plan (semi-exclusive)
- Going Dutch = Cheap
- Very successful start since 2021, larger cases coming through since 2023
- Parallel WHOA and Scheme proceedings for cross border restructuring





European Directive implementation in France: Classes of affected parties



CLASS OF AFFECTED PARTIES (1)

EUROPEAN DIRECTIVE n° 2019/1023 OF JUNE 20, 2019

- Harmonize the insolvency laws of the Member States,
- establish the classes of creditors (“affected parties”)

IN FRANCE, ORDER n°2021-1193 OF SEPTEMBER 15, 2021

- The transposition of the 2019 directive

And also :

- Security rights
- Conciliation and accelerated safeguard



CLASS OF AFFECTED PARTIES (2)

PURPOSES :

- Better consideration of the economic interests of creditors
- Overcome any blocking situation detrimental to the debtor
- Flexibility for the debtor and the judicial administrator on the establishment of classes



CLASS OF AFFECTED PARTIES (3)


DOMAIN

- Classes of affected parts:
 - ✓ *new committees in which the debtors' plans will be negotiated*
 - ✓ *creditors together, taking into account the rank of their debt and their potential payment in a liquidation context.*
- Mandatory Affected Party Classes:
 - ✓ *in Fast-track Safeguard procedure*
 - ✓ *in Safeguard procedure or Insolvency proceeding (>250 employees & turnover > €20 million or turnover > €40 millions)*
- Classes of Affected Parties with Voluntary use:



CLASS OF AFFECTED PARTIES (4)

CONSTITUTION OF CLASSES

- To be a class member:
 - ✓ *be a creditor whose rights are affected by the plan*
 - ✓ *be an equity holder*
 - Central role of the Judicial Administrator:
 - ✓ *in classes' distribution and the calculation's methods of the votes*
 - ✓ *in the constitution of the classes : "community of economic interest"*
 - ✓ *at least two classes: unsecured creditors and creditors holding security right*
- 

CLASS OF AFFECTED PARTIES (5)

VOTE

- Free requests to creditors in terms of **deadlines and discounts**
- Proposed plan submitted to classes of affected parties
 - ✓ *each class - two-thirds majority of the votes*
 - ✓ *equal treatment between creditors*
 - ✓ *Best interest of creditors' test: situation assessed in an alternative liquidation scenario*
- Possibility of imposing the plan on recalcitrant class members



CLASS OF AFFECTED PARTIES (6)

VOTE

- **"Cross class cram down"** enforcement mechanism: Ability to impose the plan on classes of affected parties who rejected it:
 - ✓ *best interest of creditors' test*
 - ✓ **"absolute priority rule"**: *the debt held by the dissenting class must be totally disinterested, before any class of lower rank*
- Plan adopted:
 - ✓ *either by a majority of classes of affected parties, with at least one class of creditors holding security rights*
 - ✓ *either by at least one class of "in-the-money" affected parties*



CLASS OF AFFECTED PARTIES (7)

RISKS :

- Criteria retained by the judicial administrator in the constitution of classes and the distribution of votes
- Criteria examined by the Tribunal
 - ✓ for the protection of affected parties in a class
 - ✓ for the protection of classes of dissidents affected parties in the event of cross-class enforcement.

