LEGISLATION WATCH / NETHERLANDS

A New Tool for Dutch Restructurings: The Ability to Bind Holdouts without a Formal Insolvency Proceeding

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Introduction

On September 5, 2017 the Dutch justice department published a draft bill which introduces a new debtor-in-possession restructuring tool. The draft bill allows a debtor to present a restructuring plan outside of formal bankruptcy proceedings, a process previously unavailable under Dutch insolvency law. Such a plan can (upon acceptance by a qualified majority of creditors and/or shareholders, as applicable) be confirmed by a court, thus making it binding upon creditors and shareholders. An earlier version of this bill was published in 2014, but was not ultimately passed into law.

Currently, Dutch law does not enable a debtor to implement a restructuring outside of formal insolvency proceedings, unless all creditors agree. Accordingly, holdout creditors generally cannot be forced to accept a restructuring, unless a restructuring plan is presented within formal insolvency proceedings. The draft bill seeks to provide a framework for presenting a restructuring plan whereby the debtor remains in possession and no formal insolvency proceedings are opened, as well as enable the debtor to proceed with a restructuring where not all creditors are in agreement.

Should the draft bill enter into force, debtors will be able to offer a restructuring plan that can, if supported by the requisite majority of creditors and/or shareholders, be confirmed by a court, making it binding on all secured and unsecured creditors as well as shareholders, regardless of whether these parties voted for or against the plan or abstained from voting. By introducing a cram-down mechanism, the draft bill aims to minimize the need for viable enterprises to enter into formal bankruptcy proceedings. Parts of the draft bill were inspired by Chapter 11 of the U.S. Bankruptcy Code and the UK scheme of arrangement, each of which provides a

Overview of Proposed New Dutch Restructuring Tool

The Restructuring Plan	Creditor Approval	Court Confirmation
— Restructuring Plan can be offered to some or all creditors	— Classes divided according to the interests and rights of various creditors and equity holders vis-à-vis the debtor	— Following class acceptance, court will confirm a plan unless the plan (i) provides creditors or shareholders with less than they would receive in a liquidation or (ii) is not feasible
— No specific content requirements, but must be accompanied by a valuation of the debtor's assets and a description of the valuation method	— Classes not impacted by the restructuring do not vote	— Court can also cram down on non-accepting classes if the plan complies with a absolute priority rule
— Wide discretion for the debtor to fashion a plan most beneficial to the debtor's specific needs	— Class acceptance occurs if a 2/3 supermajority of the claims voting in a class vote in favor of the plan	
	— If class acceptance occurs, holdout creditors in such class are bound	

"pre-packaged" procedure in which creditors agree on the terms of a restructuring outside of court and then such restructuring is brought to the court only after it has been approved by the requisite majorities.[1] This bill anticipates the coming into force of the draft directive of the European Commission on preventive restructuring frameworks as published on November 22, 2016.[2]

Offering a Restructuring Plan

Under the draft bill, a debtor entity[3] can offer a restructuring plan to all or some of its creditors and shareholders. This means that a plan may target specific parts of the capital structure. One or more creditors can also take the initiative and ask a debtor to propose a plan. Should the debtor refuse, each creditor may petition the court to appoint an expert who can then offer a plan on the debtor's behalf.[4]

Apart from certain formalities, e.g. the plan must be accompanied by a valuation of the debtor's assets and a description of the valuation methods, the draft bill does not set any requirements for the plan's contents as such. Instead, it grants the debtor substantial leeway in composing a plan. A plan can substantially amend the existing creditors' and shareholders' rights and, *inter alia*, result in the deferral or release of payment obligations, the amendment of the terms of debt instruments, or a debt for equity swap. A plan may also seek to restructure the claims of creditors with respect to guarantors, third-party security providers or co-debtors.

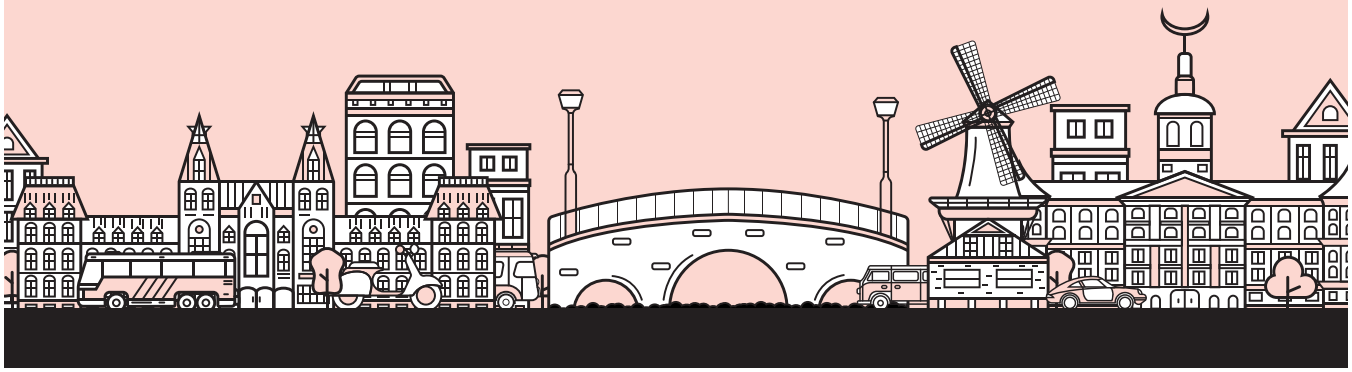
The draft bill also enables a debtor to amend the terms and conditions of long-term agreements, such as leasing contracts. The debtor may terminate the contract (subject to a maximum notice period of three months) when the counterparty refuses the debtor's amendment proposal. In addition, any compensation to which the counterparty would be entitled as a result of the amendment or termination of the contract can be limited as part of the plan.[5]

The offering of a plan and the corresponding negotiations will not automatically stay any enforcement actions by the creditors, including requests to open insolvency proceedings. At the debtor's request, however, the court can freeze individual enforcement actions, including any petition for bankruptcy. A court-granted stay has a maximum duration of four months.

Voting and Confirmation Process

A restructuring plan, before it can be confirmed by a court, needs to be accepted by at least one class of creditors and/or shareholders. A 2/3 supermajority of the claims voting in a class is required for acceptance. For the purposes of voting creditors and/or shareholders are subdivided into classes. Class composition is determined by looking at the interests and rights that certain groups of creditors and shareholders have in common. Creditors and shareholders that do not share the same bankruptcy priority[6] will always compose a separate class.[7]

Although a plan may effectuate a comprehensive debt restructuring across all classes, it may also be limited to a particular class. Subsequent voting is restricted to creditors and shareholders who are affected by the plan. Before the plan is submitted to a vote, interested parties can, if so inclined petition



the court to rule 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. Any court decision is final and not subject to appeal.[8] Once the court has ruled, or no petition has been filed, the plan will be submitted to a vote to all the creditors and/shareholders that would be affected by the plan.

Once at least one class accepts the plan with a 2/3 supermajority, the plan can be submitted to the court for confirmation. The court will refuse to confirm a plan under which creditors or shareholders would receive less than they would in formal bankruptcy proceedings (the "best interest of creditors test"), or if there is insufficient evidence that the plan is feasible.[9] The court can also set aside the non-acceptance of one or more classes and confirm the plan, but only if the plan's contents are in accordance with an absolute priority rule that is intended to be modeled on the absolute priority rule as enshrined in Chapter 11 of the U.S. bankruptcy Code. The current phrasing intends to clarify that a court should not confirm a plan if (1) a crammed down creditor, that voted against the plain is impaired and (2) the plan 'elevates' a lower ranking creditor/shareholder.

Once the court confirms the plan, it will bind all classes and their members including the creditors and shareholders who voted against the plan or abstained from voting. As a result, all their rights against the debtor will be amended in accordance with the plan. The draft bill also provides a mechanism for ensuring implementation even if the plan is not supported by shareholders: the court's order confirming the plan can replace a shareholders resolution which may be needed to implement it (this could be needed if, for example, during a shareholders meeting one or more shareholders refuse to vote in favor of implementing the plan).

Other Measures Envisioned by the Draft Bill

In addition to its powers to confirm or reject a composition plan, the court has general authority to order all measures it deems necessary to adequately protect the interests of the creditors and shareholders. This provision is similar to 11 U.S.C. § 105, under which U.S. bankruptcy courts can "issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title".

The draft bill also contains 'safe harbor' rules for security interests conveyed in exchange for 'fresh' funds that seek to facilitate the realization of the restructuring plan. In case the restructuring plan fails and the debtor enters into formal insolvency proceedings, these rules should protect the creation of the aforementioned security interest from being avoided by a bankruptcy trustee, should the debtor enter into formal insolvency proceedings after all.

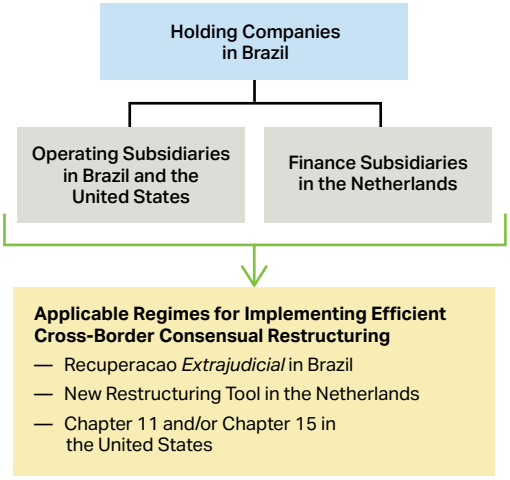
Conclusion

For distressed companies, the revised bill will provide a quick and effective way to restructure debts without the possibility of being blocked by a minority of opposing creditors or shareholders. Perhaps even more importantly for debtors, the process does not involve an administrator or bankruptcy trustee, thus allowing the debtor to remain in possession.

From an emerging markets perspective, the new legislation is particularly relevant because it could simplify the process for implementing complex cross-border consensual restructurings, particularly when paired with prepackaged options in other jurisdictions. For example, a Brazilian corporate group with finance subsidiaries in the Netherlands could concurrently make use of Brazil's recuperação extrajudicial process and the new legislation in the Netherlands (together with other proceedings as necessary, such as Chapter 11 or Chapter 15 in the United States) to implement a relatively quick consensual restructuring with minimal court involvement.

Potential Cross-Border Application of New Restructuring Tool

Structure of Hypothetical International Corporate Group



The comment period, during which interested parties could submit their views on the draft bill to the Dutch justice department, closed on December 1, 2017. The draft bill has been received favorably by the market and expectations are that a final draft could be submitted to Dutch parliament somewhere in the first six months of 2018. Barring any delays during the parliamentary process, the bill could be enacted by early 2019.

1. For the avoidance of doubt, however, there are significant differences between Chapter 11 and the UK scheme of arrangement, including with respect to pre-filing conduct, debtor eligibility, the scope of any applicable stay, the role of the court, the composition of classes, voting thresholds, the ability to bind holdouts in the same class and the ability to cram-down on non-consenting classes.
2. 2016/359 (COD), COM (2016) 723 final.
3. The explanatory memorandum to the draft bill notes that multiple related debtors' plans may, from an administrative perspective, be dealt with concurrently by the court.
4. The draft bill does not provide much guidance, but we expect that the court appointed expert will prepare and offer a plan in the same manner as the debtor would otherwise do.
5. Presumably, in most cases the nominal amount for compensation because of termination will be treated as a pre-bankruptcy unsecured claim, meaning that it may be subjected to the discount that the plan provides for.
6. Generally speaking – and subject to many exceptions – Dutch law allows for the following list of priorities: (1) claims that are secured by security rights *in rem*; (2) administrative costs for the estate (3) pre-bankruptcy claims that have preference as determined by law; (3) pre-bankruptcy unsecured claims; (4) pre-bankruptcy claims that are subordinated by contract; and (5) shareholder equity.
7. The draft bill gives limited guidance as to class composition. Creditors and other interested parties can turn to court to challenge the composition of classes. Presumably in due course case law will provide further guidance.
8. Court involvement is optional. If the plan can be completed consensually there is no need to involve the court.
9. As noted above, the draft bill stipulates that a proposed plan should be accompanied by a valuation report.

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