The Netherlands

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Draft Bill on debt restructuring plans for businesses in financial problems

On 5 September 2017 a draft Bill introducing a new instrument to the Dutch Bankruptcy Act, ie a binding debt restructuring plan for creditors and shareholders of businesses in financial problems (in Dutch: *Wet homologatie onderhands akkoord ter voorkoming van faillissement*), was submitted by the Ministry of Security and Justice for public consultation. The Bill will enable a business that is facing financial problems to enter into a debt restructuring plan with some of its creditors and shareholders and, subject to certain requirements and safeguards, have this plan approved by the court and declared binding on all creditors and shareholders, including dissenting creditors and shareholders. The rationale underlying the Bill is to avoid the situation where a business which is still economically viable but which has too many debts becomes insolvent because a small number of creditors or shareholders refuses to consent to a debt restructuring plan. The public consultation closed on 1 December 2017. Several interested parties have provided their input to the Ministry. This input may be taken into consideration in the preparation of the Bill that will eventually be submitted to the Dutch Parliament.

SUBMISSION OF A DEBT RESTRUCTURING PLAN

The draft Bill enables a business – either in the form of a company or of a private individual acting in a profession or trade – that runs the risk of becoming insolvent as a result of an overload of debt to propose a debt restructuring plan to all or some of its creditors and shareholders. The initiative to submit the plan may also be taken by a creditor. A creditor may ask the debtor to propose a restructuring plan. If the debtor refuses to do so, the creditor is entitled to request the court to appoint an expert to propose a plan. The draft Bill is not applicable to banks or insurers that are facing financial problems. It is a tool typically aimed at the rescue of ordinary commercial or industrial enterprises that are not subject to specific rules concerning insolvency, intervention or regulatory supervision.

The restructuring plan may impact on the rights of such creditors and shareholders. The plan can provide for a moratorium of payments or a partial release of the debtor from certain payment obligations. It can also provide for a write-down of certain liabilities or a conversion from debt into equity (cf the "bail-in" for banks as part of a resolution procedure). Another possible feature is an amendment of the terms of onerous contracts or of the debtor's articles of association. It is also possible that recourse rights of sureties and co-debtors vis-à-vis the debtor will be affected. The same goes for the rights of creditors vis-à-vis sureties and co-debtors of the debtor.

VOTING AND CREDITOR APPROVAL

Only those creditors and shareholders whose rights are affected by the plan are entitled to vote on the plan. In addition, the draft Bill provides for the creation of different classes of creditors and shareholders for voting purposes. Creditors and shareholders whose rights are more or less similar will form part of the same class. Creditors and shareholders that would have a different ranking in bankruptcy will always be in different classes.

A restructuring plan is adopted once it is approved by all classes. A plan is approved by a particular class of creditors if the creditors in the class that voted in favour of the plan represent at least two-thirds of the total amount of claims held by the voting creditors in that class. Similarly, a plan is approved by a class of shareholders if the shareholders in the class that voted in favour of the plan represent at least two-thirds of the total amount of the issued capital held by the voting shareholders in that class.

COURT APPROVAL AND SAFEGUARDS

If the plan is approved by at least one class, the debtor may request the court to approve the plan. If all classes have approved the plan, the court must declare the plan generally binding unless a ground for refusal applies. Grounds for refusal are, for instance, that compliance by the debtor with its obligations under the plan is not sufficiently safeguarded or that a creditor or shareholder would receive significantly less under the plan than it would receive if the debtor would be wound up under normal insolvency proceedings. If one or more classes have voted against the plan, the court can nevertheless declare the plan generally binding. However, the court will refuse to do so if, under the plan, creditors or shareholders of a particular class will not be repaid in full while at the same time a lower ranking class will be entitled to some form of compensation. This will also be the case if creditors or shareholders of a particular class will not be repaid in full while at the same time creditors or shareholders of a higher ranking class will receive more than 100% of their claims or the nominal value of the shares. The court will also refuse to approve the plan if creditors or shareholders of a particular class will receive less than another class of creditors or shareholders with the same ranking or if creditors will be denied a payment in cash for the amount that they may reasonably expect to receive if the debtor would be wound up under normal insolvency proceedings.

Court approval entails that the plan will become binding on all creditors and shareholders, including those creditors and shareholders (of the same class or a different class) who voted against the plan.

In addition to the safeguards for creditors and shareholders that are embodied in the voting thresholds and the obligation for a court to withhold its approval if one of the many grounds for refusal occurs, the court may take any measures it deems fit to safeguard adequately

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the interests of the creditors and shareholders. With a view to the possibility that the debtor ends up in insolvency proceedings after all, the draft Bill contains a provision that protects lenders that prior to these insolvency proceedings have provided a loan to the debtor and obtained a right of pledge or mortgage on assets of the debtor to secure the repayment of such loan against an action by the insolvency trustee based on fraudulent conveyance. If it was the intention that this loan would be used for payments that were necessary to ensure the continuity of the debtor's business within the framework of the restructuring plan, the draft Bill contains a rebuttable presumption that the vesting of these pledges and mortgage rights has not been fraudulent.

STAY AND FREEZE

At the debtor's request, the court can stay a petition for its insolvency for a period of up to four months or until a restructuring plan has been approved by the court. The court can also order a freeze and determine that any powers of third parties to take recourse against assets belonging to the debtor's estate cannot be exercised during a period of up to four months to be determined by the court, except with the authorisation of the court. Cash and securities provided as collateral pursuant to a security financial collateral arrangement are exempted from the freeze. Although, taken literally, this exemption only pertains to security financial collateral arrangements governed by Dutch law, a Dutch court will, in our opinion, act analogously with respect to securities and cash provided as collateral under a foreign security financial collateral arrangement.

In the case of a traditional right of pledge, it is uncertain whether the freeze applies to securities deposited with a custodian or cash held in a bank account. The relevant provision in the draft Bill refers to a provision in the Bankruptcy Act dealing with a freeze in a suspension of payments procedure. The views expressed in legislative history on the scope of this provision have been contradictory as to the question of whether this provision applies to intangible assets. If the provision is merely aimed at freezing the rights of creditors in connection with movable and/or real property belonging to the estate, this would lead to the conclusion that the freeze is not applicable to financial collateral, except to the extent that this consists of bearer securities. If, however, the provision is applicable to securities or rights with respect thereto or cash, it would merely delay the exercise of the right of the pledgee to take recourse against the collateral (and thus expose the pledgee to the risk of the securities declining in value).

MUTUAL CONTRACTS AND CONTRACTUAL COUNTERPARTY RIGHTS

A debtor may propose that the terms of mutual agreements that it has with its counterparties be amended. If a counterparty rejects such a proposal, the debtor has the right to terminate the agreement, subject to a maximum notice period of three months. The counterparty of the debtor is entitled to damages resulting from the amendment or the termination. The amount of these damages may be reduced or modified as part of the restructuring plan.

The draft Bill contains a provision restricting the exercise of contractual counterparty rights. The mere proposing of a debt restructuring plan, and events directly linked thereto, shall not, per se, make it possible for a counterparty to exercise any termination, suspension or modification rights. This entails that *ipso facto* clauses pursuant to which creditors are entitled to terminate, suspend or amend a contract on the occurrence of the proposing of a debt restructuring plan will be without effect.

PROS AND CONS

The draft Bill introduces an important instrument to restructure businesses which are facing financial problems but which are still economically viable. That is certainly a pro.

The draft Bill does not contain explicit provisions to safeguard contractual netting and close-out rights contained in master agreements for financial transactions such as the ISDA Master Agreement for derivatives transactions. These rights could be affected as part of a restructuring plan, even if the counterparty were to vote against the restructuring plan. That is definitely a con. Although the court should not approve the debt restructuring plan if as a result the counterparty would receive significantly less than it would receive if the debtor were to be wound up under normal insolvency proceedings, it would in our view be advisable that it be made clear in the draft Bill that netting and close-out rights of creditors under such master agreements may not be affected in such a way that a counterparty would be worse off than in an insolvency situation or that an explicit safeguard for netting and close-out rights be included. With such a provision it may be possible to avoid concerns with financial counterparties that need to rely on netting and collateral enforceability for regulatory capital purposes.

The draft Bill also restricts the exercise of contractual netting and close-out rights under such master agreements. It provides that the mere proposing of a debt restructuring plan and events directly linked thereto, shall not, per se, make it possible for a counterparty to exercise any termination, suspension or modification rights. The proposing of a debt restructuring plan is likely to be covered by the definition of an event of default in such a master agreement. However, it is also likely that netting and close-out rights qualify as termination rights and are thus caught by this provision. The prohibition is drafted in such a way that it suggests that such rights *can* be exercised if the debtor has ceased to perform any substantive obligations under the contract, including payment and delivery obligations and provision of collateral, but that is not clear from the draft Bill nor from the explanatory memorandum thereto. That is also definitely a con.

A pro is that cash and securities provided as collateral pursuant to a security financial collateral arrangement are exempt from the freeze. A con is that this exemption may not extend to master agreements for financial transactions pursuant to which the providing of collateral is not inherent. ■