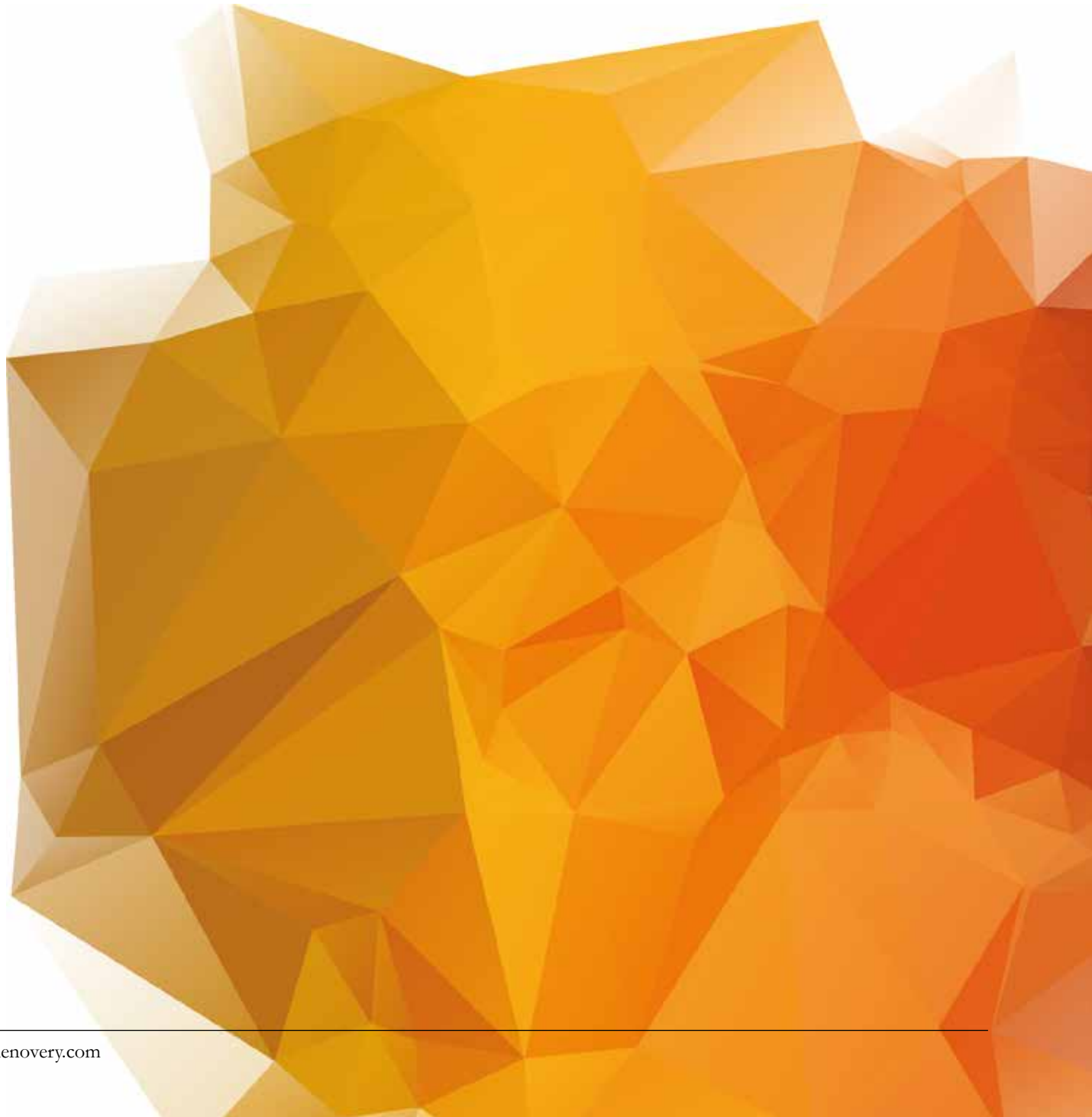
ALLEN & OVERY

WHOA report

Wet homologatie onderhands akkoord "The Dutch Scheme" | 2019



New opportunities:
The dutch scheme

The available options to successfully restructure financially distressed, but viable, businesses in the Netherlands are about to improve substantially. Currently, outside formal insolvency proceedings a (financial) restructuring of a business is only possible on a consensual basis with the support of all parties to the restructuring, meaning that every minor hold out creditor, or even equity holders, could frustrate the process. Moreover, Dutch insolvency proceedings such as the suspension of payments proceedings (surséance van betaling) have proven ineffective to restructure distressed companies with secured debt. Therefore, currently restructuring of financially distressed companies is often dealt with through bankruptcy, which approach has its own downsides and is often detrimental to the value of the company and to its stakeholders. This, however, is about to change.

The Dutch government is in the process of introducing an Act on the confirmation of private restructuring plans (the Wet homologatie onderhands akkoord (WHOA)) to restructure a debtor's (financial) obligations outside bankruptcy. Inspired by the United States Chapter 11 procedure and the English Scheme of Arrangement and with considerable attention to European bankruptcy law developments, including the recently adopted Preventive Restructuring Framework Directive, the WHOA builds upon the most favourable provisions and developments in global restructuring law and will likely be of interest to many global restructuring professionals.

In this Alert we provide an overview of the main features of the WHOA.

Quick read:

The highlights of the WHOA

The WHOA introduces the possibility to offer a restructuring plan to prevent the debtor going insolvent or to accommodate a controlled liquidation and distribution of the (insolvent) debtor's assets to its creditors. A restructuring plan under the WHOA can not only be proposed by a debtor but, interestingly, it can also be initiated by the creditors and shareholders of a debtor and its work counsel (if established).

They may request the competent court to appoint a 'restructuring expert' if the debtor is in a position where it is reasonably likely that it will not be able to continue paying his liabilities. The court-appointed specialist will then prepare a restructuring plan on behalf of the debtor. The debtor itself may also apply for the appointment of a restructuring expert, eg if the debtor deems itself incapable of preparing a restructuring plan.

The WHOA provides for a wide range of options to restructure a debtor's financial obligations. These include, for example, deferring or partially releasing payment obligations, amending the terms of debt instruments or offering debt for equity swaps. Under the WHOA the debtor could also amend the terms of onerous contracts, for example lease or long-term supply agreements.

A restructuring plan can apply to all creditors and shareholders of a company, or it can be limited to a certain category of creditors, eg secured creditors. Except for the rights of employees, the restructuring plan may lead to an amendment of the rights of any creditor or shareholder, including preferential and secured creditors, guarantors and co-debtors. As a result, the WHOA provides proper options for group restructurings.

Once approved and confirmed by the relevant percentage of creditors and the court, the restructuring plan will be binding on all creditors and shareholders involved in the restructuring plan. Subject to certain safeguards, creditors and shareholders who have voted against the restructuring plan can be (cross-class) crammed down and thus also become bound by the restructuring plan.

To enhance the prospects of a successful restructuring the WHOA provides for a temporary moratorium, safe harbours for DIP financing and the option for the debtor to seek guidance or a decision from the court concerning certain procedural matters at an early stage. Restructurings under the WHOA are swift and informal procedures, with limited court involvement only to the extent requested during the process and for the approval of the plan.

The WHOA can provide for restructurings that stretch beyond Dutch borders. One of the most interesting features of the WHOA is that it will provide debtors with an option, at the beginning of the process, to choose whether or not the restructuring plan will fall under the scope of the European Insolvency Regulation or to remain purely domestic in scope, but possibly subject to recognition in other jurisdictions on the basis of their own private international laws.

In the next sections, we will discuss the most interesting features of the WHOA in more detail.

How does it work?

SCOPE AND WHO CAN INITIATE

The WHOA will apply to legal entities and natural persons practising an independent profession or exercising a business. Banks and insurance companies are excluded as these entities are covered by specific legislation. Debtors whose restructuring plans have been voted down or have been rejected by the court within three years prior to the initiation of a restructuring plan under the WHOA are excluded as well.

A restructuring plan can be proposed by a debtor who is in a position where it is reasonably likely that it will not be able to continue paying his liabilities.

Upon commencement of the preparations of a restructuring plan the debtor must submit a written declaration at the registry of the competent court. The declaration can be viewed by the creditors and shareholders of the debtor that are entitled to vote on the restructuring plan.

Alternatively, a restructuring plan could also be initiated by the creditors, shareholders and works council (if established) of a debtor by requesting the court to appoint a restructuring expert to prepare a restructuring plan on the debtor's behalf.

For the initiation of a restructuring under the WHOA, the debtor does not need prior approval from its shareholders, regardless any provisions to the contrary in its articles of association or agreements between the shareholders.

COURT-APPOINTED RESTRUCTURING EXPERT

Creditors, shareholders and the works council (if established) may request the court to appoint a 'restructuring expert' if it is reasonably likely that the debtor will not be able to continue paying his liabilities. The court-appointed expert will prepare a restructuring plan on the debtor's behalf. The court will only appoint a restructuring expert if this is in the interest of the joint creditors of the debtor. Moreover, the debtor and the requesting creditor or shareholder will be given the opportunity to express their views on the request that a restructuring plan be prepared on behalf of the debtor. The debtor itself may also apply for the appointment of a restructuring expert, eg if the debtor deems itself incapable of preparing a restructuring plan. After the appointment of a restructuring expert, the debtor has an obligation to provide the expert with all the documents and information required to fulfil its task. The fees and expenses of the restructuring expert are payable by the debtor.

CLASSES OF CREDITORS AND SHAREHOLDERS

A debtor has the option to divide creditors and shareholders that are subject to the restructuring plan into separate classes. Notwithstanding this discretion, creditors and shareholders who have dissimilar, incomparable rights in a debtor's bankruptcy or that would obtain dissimilar, incomparable rights under the restructuring plan (eg secured creditors vs. unsecured creditors and senior vs subordinated creditors) must be placed in separate classes. Insofar as this requirement is met, the class formation is very flexible and largely left up to the debtor. Nevertheless, if a class of creditors or shareholders is subdivided into one or more separate classes, they may only be treated differently if there is a proper and reasonable justification for this distinction.

WHO IS ENTITLED TO VOTE

The debtor must provide its final restructuring proposal to its creditors and shareholders at least eight days prior to a vote. Only creditors and shareholders whose rights are amended or varied are entitled to vote on the restructuring plan. If depositary receipts of shares have been issued, the debtor or restructuring expert may invite the holders of these receipts to vote instead of the shareholder. The same applies in case of shares that have been encumbered with a right of use or enjoyment. In cases where the economic interest of a claim rests with a third party (eg bonds/notes), the debtor or restructuring expert may then invite the bond holders to vote instead of the bond trustee.

VOTING PROCESS

The voting will take place in the different classes, either in a physical meeting or through electronic means of communication. Under the WHOA, there is no "majority in number" threshold (also known as headcount test). The majorities required for a particular class to consent to the proposed restructuring plan are a two-thirds majority in value of the outstanding capital (for a class of shareholders) and a two thirds majority in value of outstanding claims (for a class of creditors). The WHOA provides for an option to (cross-class) cram down dissenting creditors, See page 6.

THE RESTRUCTURING PLAN

a restructuring plan is set out in the form of a contract between the debtor and the relevant creditors and shareholders. The debtor is to a large extent free to determine the content and form of the restructuring plan. A restructuring plan could include for example:

– the amendment, deferral or hair-cut of current or future (payment) obligations;

– an amendment of future recourse rights (such as guarantees or indemnities), provided that those future recourse rights relate to or arise out of or in connection with claims that are varied or amended under the proposed restructuring plan;

– a debt-for-equity swap, in which case rules relating to the adoption of shareholders' resolutions or minutes, whether by law, contract or found in the articles of association of the company, are not applicable to the adoption of the restructuring plan; or

– an amendment of the terms of contracts (eg lower lease instalments, new financing terms, financial covenants).The debtor or the restructuring expert may propose an amendment to the contract. If such proposal is not accepted by the counter-party, the contract may be terminated taking into account a notice period effective as of the confirmation of the restructuring plan by the court (a three month notice period will be deemed acceptable). The restructuring plan may propose to amend or vary any liabilities or claims for damages arising from such termination.

The restructuring plan must contain all information required by the creditors and shareholders to form an educated view of the restructuring plan, including information about: (i) class formation and its basis; (ii) financial consequences of the plan for each class; (iii) expected value of assets and activities of the debtor; (iv) expected proceeds in case of liquidation; (v) applied valuation methods; and (vi) voting procedures.

WHO CAN BE INCLUDED

The debtor is in principle free to include or exclude certain groups of creditors, such as trade creditors or even individual creditors. Equity holders can also be included in a restructuring plan. Notwithstanding this discretion to include or exclude, every creditor or shareholder whose rights will be affected by the restructuring plan must be included in the restructuring plan to be effective against that creditor or shareholder. In addition, creditors or shareholders may not be excluded if it would result in unfair treatment without a proper justification of some creditors or shareholders vis-à-vis other creditors or shareholders. Creditors and shareholders who are not included in the restructuring plan will retain their rights, without any amendments or variations. Rights of employees cannot be amended on the basis of the WHOA.

The WHOA also introduces the option, in contrast to the current situation, to include secured creditors in a restructuring plan. The secured position of such creditors is protected with (inter alia) an Absolute Priority Rule.

COURT CONFIRMATION

If at least one class of creditors has voted in favour of the restructuring plan, the debtor or restructuring expert can request the court to confirm the restructuring plan. The court will then schedule a hearing date within eight to fourteen days after submission of the final restructuring plan by the debtor. Creditors and shareholders who voted against the restructuring plan could use this period to request to the court to dismiss the restructuring plan on the grounds provided in the WHOA. After the hearing, the court will provide its decision as soon as possible. In principle, the court must reject the restructuring plan, if:

(i) the debtor is not in a position where it is reasonably likely that it will not be able to continue paying his liabilities;

(ii) the procedural requirements have not been met;

(iii) a creditor or shareholder should have been admitted to the vote for a different amount, unless this would not affect the result of voting;

(iv) performance of the restructuring plan is not sufficiently guaranteed;

(v) the debtor requires new financing for the restructuring which is detrimental to the joint creditors;

(vi) the restructuring plan is the result of fraud or undue preference of certain creditors or shareholders (irrespective of whether this could be attributed to the debtor);

(vii) the fees and expenses of the restructuring expert or other court-appointed persons are not paid; or

(viii) there are other compelling reasons against the confirmation of the restructuring plan.

SAFEGUARDS

The WHOA provides for certain provisions aimed at protecting opposing creditors or shareholders that are part of a class that voted against the restructuring plan or were wrongly denied a voting opportunity. These rules should prevent such creditors or shareholders from being unfairly prejudiced under the proposed plan. A court can dismiss a restructuring plan, for example, if opposing creditors or shareholders are worse off under the restructuring plan than they would have been in a liquidation scenario of the debtor, if the statutory order of priority is disregarded under the restructuring plan without justifiable business reasons or if the debtor does not receive a minimum amount of cash equal to the amount of cash it would have received in the debtor's bankruptcy. The court can only dismiss a restructuring plan for these reasons upon request of the opposing creditors or shareholders. Provided that none of the aforementioned rejection grounds apply, the court will confirm the restructuring plan. In doing so the court will have the power to cram down dissenting creditors and shareholders who voted against the restructuring plan, provided that lower ranking creditors can never cram down higher ranking creditors.

The Dutch legislator has opted for an Absolute Priority Rule in the WHOA providing the basic protection that shareholders or lower ranked creditors could not hold on to any value if higher ranking creditors are not paid in full. Under the Preventive Restructuring Framework Directive it is also possible to opt for a Relative Priority Rule stipulating that dissenting voting classes of affected creditors should be treated at least as favourably as any other class of the same rank and more favourably than any junior class. This means that shareholders or junior creditors in that case could retain some value, as long as higher ranking creditors are treated more favourably. The WHOA does not contain such a Relative Priority Rule.

After confirmation by the court, the restructuring plan will be binding on the debtor and all creditors and shareholders whose rights are amended by the restructuring plan. There is no possibility to appeal the confirmation of a restructuring plan.

TAX

The WHOA does not provide for specific Dutch tax rules and, therefore, the general Dutch tax rules apply. This means that for Dutch corporate income tax purposes a debtor will have to recognise taxable income if under a restructuring plan debts of the debtor are written off or waived. Although a debt waiver in principle constitutes a taxable release of the debt, the debtor could apply for an exemption (*kwijtscheldingswinstvrijstelling*), provided that certain conditions are met, and which exemption is restricted to amounts exceeding the amount of available tax losses, if any, that are available to the debtor. As a result, a debt waiver typically results in a forfeiture of tax losses but not in an actual amount of corporate income tax actualiteit becoming payable. In addition, for a Dutch creditor whose claims are (partly) waived under a restructuring plan, such waiver will generally result in a tax deductible loss for Dutch corporate income tax purposes although anti-abuse provisions may apply, which are particularly relevant if the debt restructuring involves related parties of the debtor.

In case of a debt-for-equity swap under a restructuring plan, this should generally not result in the debtor having to recognise a taxable gain. If, however, a Dutch creditor has already recognised a tax loss in relation to the debtor, then certain anti-abuse provisions may prevent the Dutch creditor from realising tax exempt income on its newly obtained shareholding in the debtor pursuant to the Dutch participation exemption regime.

Opportunities:
Certainty and flexibility

DEAL CERTAINTY

– **First**, the debtor or restructuring expert drafting the restructuring plan can ask the court for preliminary judgments on several points, eg information provided under the restructuring plan including the applied valuation (methods), the class formation or the voting rights and procedures.

– **Second**, subject to certain requirements the court can issue special orders on the basis of which emergency funding can be provided or other legal acts can be performed to enable the debtor to continue its business. Such funding or legal acts are exempted from annulment on the basis of fraudulent conveyance (Actio Pauliana). No special priority applies to emergency funding provided in this context.

– **Third**, General stay: once the debtor has proposed a restructuring plan and submitted the written declaration at the court registry, all bankruptcy applications for the involved debtor are stayed for a maximum of four months (and if so requested the court could further extend the stay to a maximum of eight months) provided such stay is in the interest of the debtor's creditors. In addition, the debtor may under certain circumstances request a full and temporary stay on enforcement preventing in principle any creditor from foreclosing upon the assets of the debtor.

– **Fourth**, Ipso facto clauses are temporarily not enforceable to prevent these from interfering with the (preparation of a) restructuring plan.

– **Fifth**, the confirmation of a restructuring plan and other important decisions of the court cannot be appealed.

(CROSS-CLASS) CRAM DOWN

Provided that the voting requirements and certain other requirements are met, the WHOA provides for horizontal cram down and vertical cram down (cross-class cram down, never cram-up). A restructuring plan could therefore be implemented without the consent of the entire group of creditors. This prevents single or small groups of holdout creditors from delaying or blocking a restructuring plan.

In light of the option to cram down dissenting creditors or shareholders, the WHOA provides for appropriate protection for creditors or shareholders that may be disproportionately disadvantaged without their consent.

FLEXIBILITY

Plans under the WHOA are in essence free in form and content. The intention of the legislator is to minimise the involvement of the court and leave a large amount of freedom to the parties involved. Apart from some essential safeguards, the WHOA provides for a flexible and customisable procedure. Furthermore, the court has the power to issue tailored rulings during the process aimed at safeguarding the interests of shareholders and/or creditors.

GROUP RESTRUCTURING

The WHOA contains specific provisions for group restructuring making it possible, amongst other things, to restructure (future) rights of recourse, suretyships, third party guarantees and claims on co-debtors.
A restructuring plan could also amend creditors' rights against group companies of the debtor if, amongst other things, these group companies would be likely to go insolvent if they are not included in the restructuring plan and if these group companies have agreed to the proposed restructuring plan. These provisions for group restructurings will prove to be a favourable development, especially in light of the many Dutch finance companies that are part of larger, worldwide operating groups.

INTERNATIONAL RESTRUCTURING

Debtors may choose whether or not the restructuring plan will fall under the scope of the European Insolvency Regulation.

– If the debtor applies for the restructuring plan to fall under the scope of the European Insolvency Regulation, the final restructuring plan will benefit from automatic recognition in courts of all the EU member states (except for Denmark).
However, in accordance with the terms of the European Insolvency Regulation, the proceeding will have to be publicly announced and only debtors with their centre of main interest (COMI) in the Netherlands will be eligible to choose this option.

– Alternatively, the debtor could apply for the proceeding to remain purely domestic in scope. The proceeding will then still be a court process, but will progress in private, with the parties not benefiting from automatic recognition under the European Insolvency Regulation. Instead, for such recognition the parties will have to rely on private domestic law principles of other jurisdictions. In this situation the COMI of the debtor does not need to be in the Netherlands, although the debtor should either have its registered office or place of residence in the Netherlands or, if not, there must be 'sufficient connection' with the Netherlands on other grounds.

Allen & Overy

As a firm with an internationally recognised practice in corporate, banking and litigation, Allen & Overy is closely monitoring the major developments in Dutch and European restructuring law. Due to our renowned expertise and the significant network of Allen & Overy offices across Europe, we are pre-eminently suited to advise clients about the consequences and possibilities of the WHOA in Dutch and European matters.

Since the WHOA introduces a whole new system of restructuring possibilities, there is still a lot of uncertainty about the exact effects and details of restructuring procedures under the Act. With extensive experience in large restructuring and insolvency matters and a well-established litigation practice for the Dutch courts, English schemes in front of English courts and Chapter 11 in front of New York Courts. Allen & Overy can help clients to fully benefit from these new opportunities under Dutch law.

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