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German scheme under the StaRUG (draft bill)

Germany uses the implementation of the EU directive to make a bold move: As from January 2021, German companies too can successfully carry out their restructurings with cram-down decisions, moratorium and other instruments outside insolvency.

In addition to the amendment of the German Insolvency Code (*Insolvenzordnung*), which incorporates in particular the experiences gained from the insolvency law reform in 2012 (ESUG), the German Act on the Further Development of Restructuring and Insolvency Law (*Gesetz zur Fortentwicklung des Sanierungs- und Insolvenzrechts*) contains in particular the long-awaited German Act on the Stabilisation and Restructuring Framework for Companies (*Gesetz über den Stabilisierungs- und Restrukturierungsrahmen für Unternehmen*; **StaRUG**). The StaRUG could boost the restructuring landscape in Germany and, finally, provide Germany with an internationally competitive cram-down instrument (scheme) outside insolvency. Now, the hurdles of the legislative process need to be cleared, so that, as provided for by the draft bill, the new law can take effect already on 1 January 2021.

The StaRUG creates a framework for restructuring outside insolvency which enables companies to take restructuring measures on the basis of a restructuring plan accepted by the majority of the creditors. With this, the StaRUG closes the gap between a consensual out-of-restructuring and an in-court-restructuring within insolvency by way of self-administration and insolvency plan or transfer of assets. In the past, it became evident time and again that a consensual restructuring is not always possible due to the requirement of achieving a consent of 100% (ruthless creditors, capital market investors). Insolvency, too, remains the second best solution due to the associated stigmatisation and major legal implications of the proceedings as a whole.

Overview of the key points:

Early availability

The restructuring framework is already available upon imminent illiquidity, i.e. if the debtor is not expected to be in a position to meet its future payment obligations when due. In this context, a prognosis period of 24 months will generally apply in future. This means that companies in danger

of running into financial difficulties in 2021 or 2022, e.g. due to foreseeable covenant breach or lack of a refinancing solution, should take a look at this instrument already today.

Management must protect the creditors' interests

Upon occurrence of the imminent illiquidity, the management must protect the creditors' interests (as well). Depending on the quality of the crisis, this may trigger different obligations to act and results in internal liability or, depending on *lis pendens* of the restructuring issue, in liability *vis-à-vis* the creditors. This is a new area of directors' liability risk requiring careful legal guidance.

Proceedings led by the debtor and modular proceedings

The debtor is the driving force of the restructuring framework and choses from a modular system the relevant elements in order to successfully implement the restructuring concept. The proceedings are not opened by the court, the latter is merely notified of a restructuring project, appoints a restructuring officer, if necessary (see below), and is involved in specific instances for certain instruments of the restructuring framework, such as in particular (i) the confirmation of the restructuring plan accepted by the majority, (ii) the initial review of certain questions regarding the restructuring plan, (iii) the moratorium (stabilisation order), or (iv) the termination of mutual agreements.

Restructuring plan with cross-group cram-down

The concept of the restructuring plan, i.e. the heart of the restructuring framework, is based on the insolvency plan. The restructuring plan can provide for claims, claims for separate satisfaction and intra-group third-party collateral and, which is important and correct since it does not involve proceedings as a whole, it can be narrowed down to certain claims so that for instance operative creditors (such as suppliers) need not be included in the restructuring. Voting takes place in groups with a group-related majority of 75% of the voting rights (volume) within the group. If the necessary majority is not reached, consent can be replaced by a cross-group majority under certain circumstances.

Stabilisation order (moratorium)

On application by the debtor, the restructuring court can also issue a stabilisation order in addition to the confirmation of a restructuring plan. By way of such moratorium, enforcement measures against the debtor are prohibited for 3 or 4 months (stay of enforcement (*Vollstreckungssperre*)) and security created over movable assets may not be realised (stay of realisation (*Verwertungssperre*). Moreover, a creditor cannot refuse to fulfil its contractual obligations simply due to to the fact that obligations of the debtor are outstanding on the date the order is issued.

Termination

On application by the debtor, the restructuring court can, in addition to the confirmation of a restructuring plan, also terminate mutual agreements that were not fully performed by any party if the debtor's contracting partner is not willing to agree to an amendment or a termination of the agreement required for the realisation of the restructuring project. As a result of the decision, the agreement (e.g. a lease agreement) will be terminated after three months; the resulting damage claims of the contracting partner (e.g. a lessor) can become a separate group under the restructuring plan.

Restructuring nominee

For moderation during the restructuring project, but also to protect the interests of all creditors jointly, a restructuring nominee (*Restrukturierungsbeauftragter*) may be appointed by the court on application by the debtor and must be appointed by the court in certain cases of increased degrees of intervention (e.g. cross-group cram-down, stabilisation order or termination of agreement). The restructuring nominee provides information to the court, moderates the proceedings and the court may provide for certain examination and approval rights for the restructuring nominee. Under certain circumstances, the court must appoint the restructuring nominee proposed by the debtor. If this proposal is not binding for the court, the

creditors may propose a restructuring nominee under certain circumstances. In such cases where the appointment is restricted, the court may appoint a special restructuring nominee.

Financing / safe harbour

The requirements of the courts prescribed in their rulings on restructuring loans (*Sanierungskredite*) also apply to financings during the preparation and implementation of a restructuring project, i.e. a restructuring opinion must also be prepared within the restructuring framework, if necessary. However, the provisions and the enforcement measures of a final and non-appealable restructuring plan are excluded from an appeal in a consequential insolvency (safe harbour). This also includes loan commitments required in order to finance the restructuring on the basis of the plan, including extension, deferral and assumption of joint and several liability. For the avoidance of doubt, it is noted that no risk of avoidance or liability arises solely from being aware of the restructuring framework. No use is being made of the possibility provided for in the EU directive to handle a new financing with priority in the event of a consequential insolvency.

Dual approach of international recognition

On application by the debtor, public announcements will be made as regards the restructuring issue. In this case, this is a procedure within the meaning of Annex A to the EU Insolvency Regulation (*Europäische Insolvenzverordnung*; **EUInsVO**) with the corresponding requirements for commencement (COMI) and legal consequences for the international recognition pursuant to EUInsVO. If the debtor takes the choice not to file such application prior to the first decision in the restructuring issue, the restructuring will be a non-public issue and the jurisdiction of the restructuring court and the recognition of the court decision follows from Brussels I or general international private, insolvency or civil procedure law.

In brief

The draft bill of the restructuring framework has the quality, in the event of its implementation, to (finally) furnish Germany with an efficient and practicable restructuring instrument outside insolvency and to change the restructuring landscape.

Key strengths:

- Early availability: The restructuring framework is already available upon imminent illiquidity (i.e. no more than 24 months prior to illiquidity).

- Modular proceedings led by the debtor: In light of the restructuring concept to be negotiated with the stakeholders, the debtor decides which plan will be submitted to the creditors for voting and which modules of the restructuring framework are required by it (cram-down plan, initial review, moratorium, termination of agreements, new financing as part of the plan) and confirmed by the court, if necessary.

- Dual PIL approach: The debtor decides whether or not the proceedings are deemed to be insolvency proceedings within the meaning of EUInsVO.

- Plan only for relevant legal relationships: The restructuring plan can only apply to certain legal relationships or creditors and thus allows for tailored solutions.

- (Broad) cram-down mechanism: Minorities blocking the vote can be outvoted both within a group with a majority of 75% and by a cross-class cram down. The principle of priority is modified („relaxed“priority rule).

NOTE: Should the ambitious timetable be implemented and StaRUG take effect on 1 January 2021, the rough **roadmap for companies in difficulties** is set up as well. Now at the latest, in the last three months of suspension of over-indebtedness as reason to file for insolvency, it is important to start working on a restructuring concept in order to be able to make a positive going-concern prognosis for avoiding over-indebtedness then required again and to make use of the restructuring framework from January 2021 onwards.

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