# New toolbox, new questions

Professor Dr Dominik Skauradszun and Walter Nijnens, LL.M., outline their first interpretations of the brand new Directive on Preventive Restructuring Frameworks

**The brand new Directive on Preventive Restructuring Frameworks (EU No 2019/1023 of 20 June 2019) presents a promising toolbox for restructuring debtor companies, containing features such as a very early starting point, the debtor-in-possession-approach, a flexible stay, the restructuring plan's adoption out-of-court and the cross-class cram-down.**

However, all that glitters is not gold. Therefore, this overview points out challenges regarding two tools that have not yet been sufficiently reviewed in the legal literature. The first is about the restriction of equity holders' rights, the second about the stay. Furthermore, the paper demonstrates the problems arising from the question of international jurisdiction over the new frameworks.

## The stay as a mere paper tiger?

At least from the starting point, the purpose and mechanism of a stay is clear. This tool can support the negotiations for a restructuring plan in a preventive restructuring framework. It goes without saying that the numerous flexibility clauses just regarding the stay may create a quite different level playing field. This is why it is recommendable to use the flexibility clause in Article 7(3) Directive so that a granted stay must end if illiquidity occurs. This is caused by the widely accepted principle that the debtor's estate needs to be protected then and, therefore, payments shall be prohibited after illiquidity occurs. It would not be logical if a debtor, on the one hand, is protected by a stay and, on the other hand, can dispose of the estate although illiquidity occurred. Moreover, if the stay does not end, creditors will not be able to request the opening of insolvency proceedings (Article 7(2) Directive).[1]

Furthermore, the stay has not only effects on enforcement proceedings, but also on several important contracts.[2] It also blocks all termination rights and rights to withhold performance by virtue of a contractual clause (Article 7(5) Directive). Having said that, the stay with its termination blocker could turn out to be a mere paper tiger.[3]

At this point, the prospective Brexit could play a special role: contractual partners with a strong market power and in-depth knowledge about non-performing contracts could force the debtor to enter into contracts with choice-of-law clauses and prorogation clauses both in favour of non-EU law and non-EU courts. If a contract is governed by the law of a non-EU state and if the parties agreed on a non-EU court in the event of a dispute, it is highly likely that this contractual party can enforce its rights before a non-EU court. Since the contract is governed by non-EU law, the non-EU court does not have to respect the granted stay and, therefore, will not have to allow the termination blocker.[4] Post-Brexit, this could apply to English law and London courts.

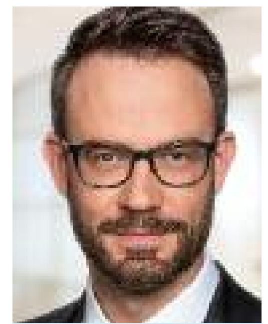
The analogous situation in banking recovery and resolution law based on the Single Resolution Mechanism Regulation[5] has shown that this concern is not a theoretical one. In 2018, both the European and national resolution authorities realised that choice-of-law clauses and prorogations in favour of non-EU law and non-EU courts give rise to many problems since non-EU courts most likely will not respect a termination blocker based on European law.[6]

## Equity holder rights: misty Article 12 Directive

Restructurings under the Directive can be divided into three phases:

(1) Preparation, negotiation and drafting of the restructuring plan;
(2) Adoption and confirmation; and finally
(3) The plan's implementation.

In all three phases, conflicts between directors and equity holders are possible. These conflicts are foreseeable and



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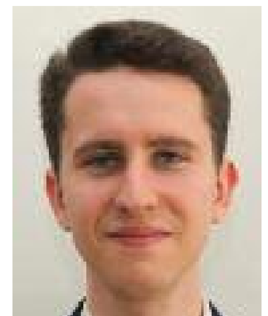

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hardly surprising since restructuring measures based on the Directive cover all kinds of corporate measures and these measures mostly affect equity holders heavily. This applies to capital decreases and increases, and especially debt-to-equity-swaps (cf Article 2(1)(1) and Recital 96).[7]

The only Article which explicitly covers equity holder rights is Article 12. Due to the vague wording, which starts with an *exception* without stating the *basic principles*, the provision needs to be interpreted. We have presented this interpretation in several comprehensive reviews[8] and found the following results.

If equity holders are included as affected parties in the adoption process of the restructuring plan (Articles 9-11 Directive), they do not have the powers usually provided to them by corporate law in the second and third phase. The European legislator saw corporate law as a counterpart to restructuring law (cf Recital 96) and, therefore, imagined that the danger caused by equity holder rights could be best handled with a *closed and final system*. This system only contains the adoption (Article 9), the plan's confirmation (Article 10), and the potential cross-class cram-down (Article 11).

Corporate instructions by the shareholders' meeting for the purpose of a non-adoption, a non-confirmation or a non-implementation may be lawful outside the preventive restructuring frameworks. However, these corporate measures are ineffective in the adoption and implementation phase of the restructuring plan in case equity holders were not excluded from Articles 9 to 11.[9]

## Directors caught between two stools

As Article 12 Directive does not mention the preparatory phase and Chapter 3 restructuring plans only regulate the second and third phase, it does not conflict with the Directive if equity holders exercise their

influence in the preparatory phase. At this point, however, directors' obligations need to be examined as well. Hence, the balance between restructuring law and corporate law will be established by means of another Article, namely Article 19(a) of the Directive.[10] This provision stipulates that Member States need to ensure that the directors have due regard to the interests of creditors, equity holders, and other stakeholders. At least three things can be stated: first, Article 19(a) Directive does not establish the priority of creditors. It could be said that, as a result of this provision, directors are caught between two (or three) stools. Second, an instruction prohibiting directors from using the preventive restructuring frameworks, although such a framework could rescue the company, cannot be lawful.[11] Third, the preventive restructuring frameworks are not designed for strategically replacing equity holders. The difficulty is to assess all shades between these extremes.

Whilst the second and third phase are regulated by the (strict) closed system established by Article 12 Directive and the extremes relating to Article 19(a) Directive are clear, all cases between the extremes in phase 1 need to be examined. This will take some time.

## International jurisdiction: a less technical, but strategic topic

Nowadays, most restructurings have cross-border aspects. The success of the stay and the restructuring plan, therefore, depends on whether the court judgments will be recognised and be enforceable in other Member States. The three key themes are "international jurisdiction", "recognition" and "enforcement". Surprisingly, the Directive does not regulate even one of these major features. Consequently, we reviewed two relevant EU Regulations, Brussels I[12] and the European Insolvency Regulation (EIR)[13], and can state the following:

Brussels I applies to preventive restructuring frameworks, as they are civil and commercial matters (Article 1(1) Brussels I) and do not fall under the insolvency exception of Article 1(2)(b) Brussels I as long as they are not within the scope

of the EIR.[14] As the frameworks are concerned with companies which are not yet insolvent, but only have a likelihood of insolvency, there is little room to view them as falling under bankruptcy or winding-up. The frameworks are not even analogous to insolvency proceedings since

(1) they shall prevent insolvency of the debtor,
(2) because of the contractual elements of the restructuring plan; and
(3) the out-of-court preparation and adoption.[15]

Consequently, recognition (Article 36(1) Brussels I) and enforcement (Article 39 Brussels I) of judgments under the Brussels I framework are both possible. The confirmation decision by judicial authorities, unlike those of administrative authorities, are judgments as defined by the Regulation (Article 2(a) Brussels I).

Unfortunately, jurisdiction under Brussels I is quite problematic. Article 24(1) Brussels I provides for exclusive jurisdiction for the forum rei sitae with regard to rights in rem in immovable property. The court of the Member State in which an employee is domiciled has jurisdiction over cases brought by an employer concerning individual contracts of employment (Article 22(1) Brussels I). The general rule (Article 4(1) Brussels I) entails a forum rei-provision. Brussels I is ill-equipped regarding jurisdiction for restructuring frameworks, as there is no real defendant. Therefore, it is best to view all affected parties as individual defendants. Their claims can then be concentrated at the court for the place where one of them is domiciled (Article 8(1) Brussels I). However, this will lead to forum shopping. As the possibility of concentration of claims does not exist for claims based on Articles 22(1) and 24(1) Brussels I, the result can be that more than one preventive restructuring framework is required.[16]

The EIR framework regarding jurisdiction (Article 3), recognition (Article 19(1)) and enforcement (Articles 19(1) and 32(1)) could apply if Member States decide to add their preventive restructuring frameworks to Annex A.[17] The frameworks will likely meet the conditions imposed by Article 1 EIR (public, collective proceedings, purpose etc.). Recognition and enforcement under the EIR would be possible too. Regarding jurisdiction, the COMI-principle would apply to the opening of (main) restructuring proceedings.

## Conclusion

Although many questions remain unanswered, the Dutch have already presented their implementation of the Directive.[19] Dutch practitioners call it "a world leading restructuring tool".[20] Time will tell whether a more in-depth discussion of the unresolved questions would have been beneficial for both Dutch and foreign parties. Many other Member States, in any case, will have to make an effort not to miss the boat in this forward-looking restructuring culture. ■

**Footnotes:**

1 D. Skauradszun and W. Nijnens, 'The Toolbox for Cross-Border Restructurings Post-Brexit – Why, What & Where? ' [2019] NIBLeJ.
2 G. Kayser, 'Eingriffe des Richtlinienvorschlags der Europäischen Union in das deutsche Vertrags-, Insolvenz- und Gesellschaftsrecht' [2017] ZIP 1393, 1397 ("Massive impact").
3 D. Skauradszun, 'Ein Umsetzungskonzept für den präventiven Restrukturierungsrahmen' [2019] KTS 161, 175.
4 Skauradszun/Nijnens (n 1).
5 Regulation (EU) No 806/2014 of the European Parliament and of the Council of 15 July 2014.
6 Cf the consultation by the German Financial Supervisory Authority (BaFin) regarding section 60a of the German Sanierungs- und Abwicklungsgesetz ('Vertragliche Anerkennung der vorübergehenden Aussetzung von Beendigungsrechten'), BaFin Konsultation 11/2018, 1. See also Skauradszun (n 3) 176.
7 Ch. H. Seibt and A. Treuenfeld, 'Gesellschafts- und kapitalmarktrechtliche Aspekte der EU-Restrukturierungsrichtlinie' [2019] Der Betrieb 1190, 1196; F. Grell and U. Klockenbrink, 'Auswirkungen der Richtlinie über präventive Restrukturie-rungsrahmen auf Fremdkapitalgeber: Ausgewählte Themen von Cram Down bis Lender Liability' [2019] Der Betrieb 1489; D. Skauradszun, 'Anteilsinhaberrechte im präventiven Restrukturierungsrahmen' [2019] NZG 761, 762.
8 Skauradszun (n 7); Skauradszun/Nijnens (n 1); Skauradszun (n 3).
9 Skauradszun (n 7); Skauradszun/Nijnens (n 1). Cf Article 370(5) in the proposed Dutch Act on the Confirmation of Private Plans (WHOA, *Wet Homologatie Onderhands Akkoord*).
10 Skauradszun (n 7); Skauradszun/Nijnens (n 1).
11 Seibt/Treuenfeld (n 7) 1198; Skauradszun (n 7); Skauradszun/Nijnens (n 1).
12 Regulation (EU) No 1215/2012 of the European Parliament and of the Council of 12 December 2012.
13 Regulation (EU) No 2015/848 of the European Parliament and of the Council of 20 May 2015.
14 In depth D. Skauradszun, in B. Kübler, H. Prütting and R. Bork (eds), InsO (80th edn, RWS 2019) Art 32 EIR para 11; D. Skauradszun and W. Nijnens, 'Brussels Ia or EIR Recast? The Allocation of Preventive Restructuring Frameworks' [2019] ICR 193; Skauradszun/Nijnens (n 1).
15 Skauradszun/Nijnens (n 14); D. Skauradszun, 'Die Restrukturierungsrichtlinie und das "verschwitzte" internationale Zivilverfahrensrecht' [2019] ZIP 1501.
16 For a more elaborate discussion see Skauradszun (n 14); Skauradszun/Nijnens (n 1).
17 The Netherlands plan to ask the European Commission to initiate proceedings to add the *openbare akkoordprocedure buiten faillissement* (public pre-insolvency plan procedure) to Annex A EIR. See Kamerstukken II 2018/19, 35 249, nr. 3, 6.
18 Skauradszun (n 14); Skauradszun/Nijnens (n 1).
19 The preparation of the "Dutch scheme", however, started many years ago.
20 RESOR, press release dated 10 July 2019.

**MANY MEMBER STATES WILL HAVE TO MAKE AN EFFORT NOT TO MISS THE BOAT IN THIS FORWARD-LOOKING RESTRUCTURING CULTURE**