

# StaRUG: The New German Restructuring Law



# Basic Concept of StaRUG Restructuring

- Entered into force on 1 January 2021
- Pre-insolvency proceeding based on likelihood of insolvency = defined as „imminent inability to pay“ (*drohende Zahlungsunfähigkeit*)
- Aims at a restructuring plan allowing for a cram down of minority creditors
  - „Restructuring moderation“ as a different, special add-on feature of StaRUG
- Public or non-public procedure
- New feature of German law: formerly no cram-down of creditors in out-of-court situation possible unless contractually agreed on
- „Third way“ in addition to a full-fledged insolvency proceeding and a debtor-in-possession insolvency proceeding
  - Restructuring plan resembles insolvency plan but more flexible



# Basic Concept of StaRUG Restructuring

- Tool box approach: choice of different „instruments“
  - Plan confirmation/sanctioning
  - Preliminary check of prerequisites (early examination)
  - In-court voting procedure
  - Stay of enforcement and execution („stabilisation“)
  - Not included: Termination of contracts/leases
- 24 restructuring courts (as compared to roughly 190 insolvency courts)
- Restructuring of *a debtor* (but: joint jurisdiction and intra-group security rights may be included in the plan)



# The Plan Procedure

- Court jurisdiction: COMI principle ( § 35 StaRUG)
  - Requires COMI shifting of foreign companies
  - But facilitates international recognition even for non-public StaRUG procedures
  - Still possible to cut liabilities of foreign intra-group guarantor company
- Restructuring procedure starts with a formal notice by debtor (only) to the restructuring court – no formal application necessary



# The Plan Procedure

- Documentation required: restructuring concept with comparative analysis of company value with and without the plan; financial blueprint, stage of negotiations
- Notice leads to *lis pendens* of the „restructuring case“
- Before the pendency of the case: ordinary rules of corporate governance and corporate law apply (no shift of fiduciary duties towards creditors – hot topic in German literature)
  - § 2 of the first governmental draft has not been enacted
- However, obligation to take counter-measures if the viability of the company is threatened ( § 1)



# The Plan Procedure

- Major effects of pendency:
  - Suspension of duty to file
  - But: duty to inform court if debtor becomes unable to pay or if over-indebtedness arises (liability risk for directors!)
  - Possible termination of the restructuring case *ex officio* (thus lifting the suspension of duty to file)
  - Loophole: Court may refrain from termination if success of plan is likely
  - Further duties of company and directors to honour the interests of the general body of creditors
  - Over-indebtedness/Balance sheet insolvency
    - 12 months forecast leaving more room for StaRUG
    - requires a prognosis but possible to take the success of the restructuring into account
    - Unresolved: whether required to actually file the StaRUG notice within six weeks if positive prognosis relies on cram down



## The Plan Procedure

- Debtor may administer the voting procedure himself
- Offers flexibility
- Proposal of plan offered for acceptance within (at least) 14 days
- Advance of only 14 days for voting in creditors' meeting
- Optional: Meeting without voting
- Electronic communication and voting possible
- Documentation of process required
  - any remaining doubts as to the proper process and the allocation of voting rights may endanger sanctioning
- Court-run voting procedure possible if requested



## The Plan Contents

- All creditors or group of creditors covered except for employees/workers' claims, victim of intentional torts, state fines
- Secured creditors
- Intra-group security right holders (but adequate compensation required)
- Interference with shareholder rights possible
  - Solving shareholder conflicts with StaRUG? (see also AG Dresden)
- Plan may allow for hair-cut, prolongation of claims, adjustment of covenants
- May allow for new finance, but no duty to advance fresh money





# The Plan Contents: Adjustment of complex financial contracts and syndicated loans possible

- No general termination of contracts
- But plan may allow for adjustments of conditions of claims and security rights deriving from multilateral contracts between the debtor and several creditors or from bonds and similar instruments
  - In particular: Covenants
- Includes adjustments of ICA (if debtor is party to that agreement)



# The Plan Contents: Adjustment of complex financial contracts and syndicated loans possible

- Majorities: 75% of affected creditor rights in each class
  - Composition of classes crucial
- No head count
- Cross class cram down possible under absolute priority rule
- But relative priority sufficient in particular situations



# Involvement of Practitioner („Restrukturierungsbeauftragter“)

- Appointment by court is either mandatory or happens on a voluntarily basis
- Certain rights of debtor and group of creditors to propose the IP
- Rather cheap....(general rule: up to 350€/hour)



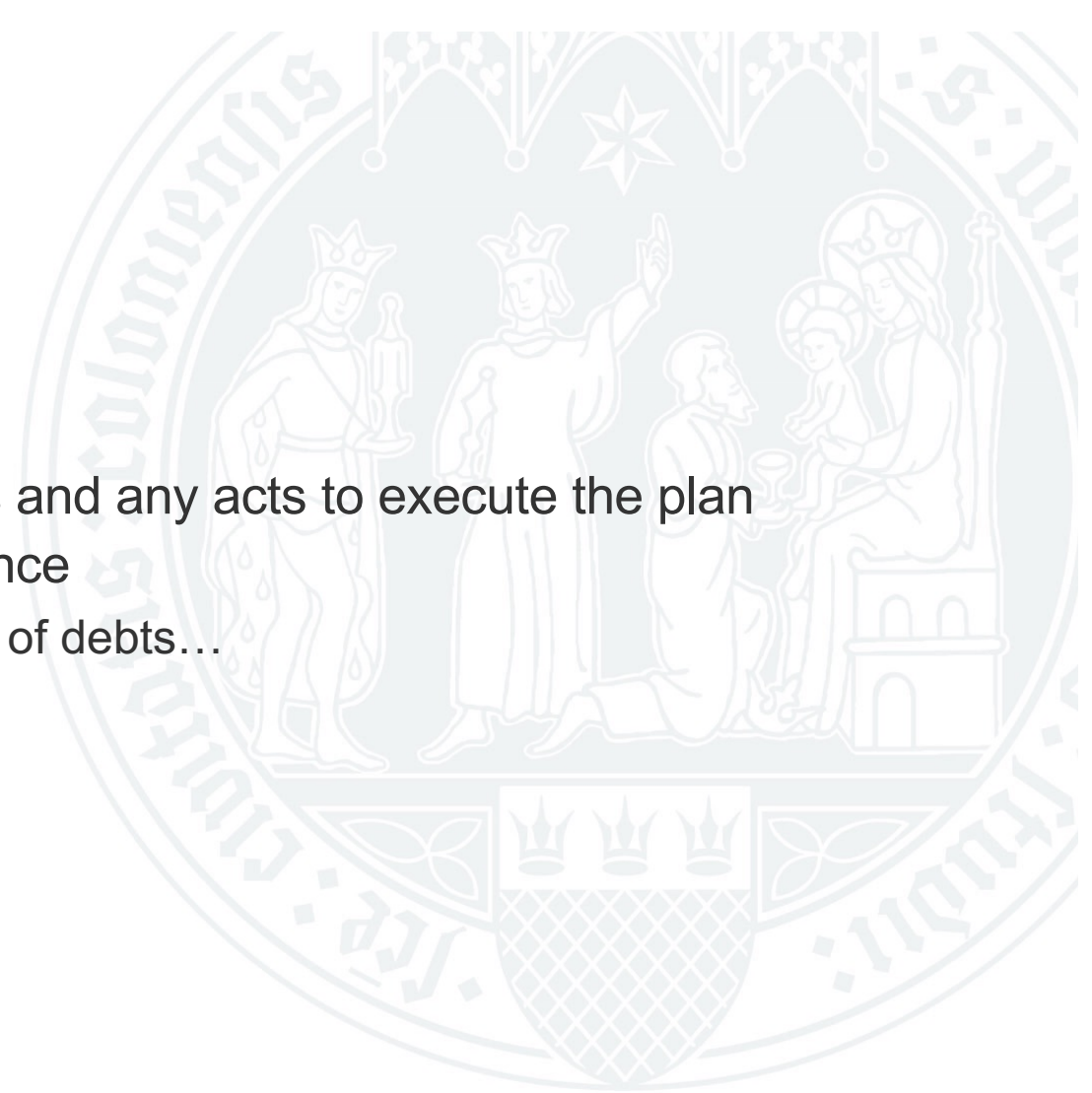
## „Moratorium“/stabilisation order

- Stay of execution
- And/or Stay of enforcement of rights to movable assets
- Grants debtor right to use movables
- No right for debtor to sell movables (unless consent by creditor)
- Duration: up to three months, but may be prolonged up to eight months after first court order subject to certain criteria
- Ban on ipso facto clauses, but clauses not specifically related to StaRUG case remain valid and effective
- Stay on rights of termination if counter-performance is indispensable for debtor, however, no stay if termination is based on grounds other than StaRUG (such as MAC)
- No duty to advance fresh money without security



## Safe Harbour provisions

- No fresh money privilege
- No super-priority
- Protection of plan and its effects and any acts to execute the plan content from transaction avoidance
  - Does not cover later repayment of debts...



# First experiences with the new law

- Three published court decisions
- Approx. 15 cases since January 2021 (including one high profile case covering debt bonds)
- No public announcements possible before July 2022
- International recognition unresolved (annex A, EIR)
- StaRUG as a game changer in out of court negotiations



# First experiences with the new law

- Court decisions: Closer look at imminent inability to pay and creation of creditor classes
- Rather generous approach with respect to the amendment of covenants
  - Not required for amendments to be strictly necessary; usefulness for the purpose of the envisaged restructuring is sufficient
- What is the next best scenario for the best interest of creditors test?
  - AG Cologne versus AG Hamburg (liquidation scenario)
- Cross class cram down (AG Dresden)
- No termination of pendency despite inability to pay
- No published stabilisation orders yet
- Some players start to amend financial documentation (e.g. imposing of information duties on the debtor)



## Position of debtor vs creditors

- Debtor is in the driver's seat: no application rights for individual creditors
- But: debtor dependant on fresh money to finance restructuring plan procedure
- Sanctioning: immediate appeal by creditors (within 2 weeks)
- Court may dismiss the appeal instantaneously if detriment caused by delay outweigh disadvantages for the appellant and no manifest statutory violation
- Creditor may claim damages caused by execution of the plan, but outside of plan procedure
- Rights of hold out-creditors subject to cram down; unclear, whether stabilisation order helps much





# Interrelationship with insolvency proceeding

- Debtor-in-possession insolvency proceeding („*Eigenverwaltung*“) allows for more, but is slightly less flexible
- Termination of contracts possible within insolvency proceeding
- Employees' compensation („*Insolvenzgeld*“) in insolvency proceeding only
- Similarities between Insolvency plan and Restructuring plan
- Insolvency proceeding including DIP after failed StaRUG still possible, but DIP depending on safeguarding creditors' interests
- Generally no second StaRUG attempt after first failure (ex officio termination of case)
- Same court may be competent for insolvency proceeding ( § 3 para. 2 InsO) (optional)
- Restructuring IP may become trustee subject to approval by creditor committee



## General assessment

- For restructuring purposes, StaRUG is worth a try
- Some uncertainties remain
- Particularly fitted for the needs of financial restructurings and larger companies
- DIP Insolvency proceeding as a further alternative
  
- Q&A?



Thanks for your attention.

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