

## **ESG-concerns in the Restructuring of Financially Distressed Companies**

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## Overview

- **I.** Context
- **II.** Problem definition
- **III.** Transfer of business within a (Belgian) judicial reorganisation procedure
- **IV.** Transfer of business within bankruptcy proceedings
- **V.** Preliminary conclusions

## I. ESG concerns in corporate restructurings - **CONTEXT**

- **Insolvency law** traditionally **creditor** centered (wealth maximisation)
- Nuances for:
  - Employees (still creditors)
  - Fresh start (personal insolvency)
  - Some jurisdictions (state interest)
- **Company law** traditionally oriented towards wealth maximisation for **shareholders**

## I. ESG concerns in corporate restructurings - **CONTEXT**

- In **company law** (last decade): shift away from ~~shareholder primacy~~
- Introduction of **ESG** (Environmental, Social, Governance) concerns in the policy goals of corporate lawmakers
  - Cf. CSR and corporate purpose debates
  - ESG: understood broadly, encompassing all UN sustainable development goals
  - Bolstered by certain jurisprudence by national courts (e.g. Dutch Shell Case) and actions by national legislators (e.g. French devoir de vigilance)
- Milestone: **EC** proposal for a **directive** introducing a **corporate sustainability due diligence obligation** (COM/2022/71 final)

## I. ESG concerns in corporate restructurings - **CONTEXT**

- **EU corporate sustainability due diligence obligation**

- Applies to large companies active in the EU

- Own operations, subsidiaries and entire value chains

- Entails:

- identify actual or potential adverse human rights and environmental impacts
- prevent or mitigate potential impacts
- bring to an end or minimise actual impacts
- establish and maintain a complaints procedure
- publicly communicate on due diligence

- Enforcement: fines for the company + directors' liability

## Overall question

- Will EU insolvency law undergo the same evolution as EU company law?
  - EU company law: shift away from shareholder primacy towards a more diversified corporate purpose, incl. ESG concerns
  - Similar tendency within (emerging) EU insolvency law?
    - *Shift away from strict creditor primacy towards a more diversified purpose of insolvency law?*

## II. Problem definition

- **Multiple possible encounters between ESG and insolvency law**
  - Bankruptcy trustee confronted with contracts or assets creating ESG concerns
  - ESG responsibility of board members of companies nearing insolvency
  - ESG due diligence after out-of-court transfer of an insolvent business
  - **→ Here: ESG concerns within the process of judicial control over restructurings of (nearly) insolvent companies ←**
    - Particularly transfer of business activities in going concern under court supervision

## II. Problem definition

- **Why** focus on transfer of business activities in going concern under court supervision?
  - (Most) valuable reorganisation tool
  - Multiple procedural options in many jurisdictions
  - Debated in a Belgian setting (Belgian law used as an example)
  - Multiple conflicting interests
  - Impacted by 2019 EU Directive on restructuring and insolvency (not yet transposed into Belgian law)



## II. Problem definition

- Transfer of (nearly) insolvent business in going concern – **multiple options** according to **Belgian insolvency law**
  - Within a formal/judicial reorganisation procedure
    - A. As part of a regular reorganisation plan (to be voted by the creditors – “creditors’ democracy”)
    - B. As part of a specific transfer of business procedure (to be decided by the court)
  - Outside a judicial reorganisation procedure
    - C. During a bankruptcy procedure
    - D. (Out-of-court restructuring)

## III. Transfer of business within a (Belgian) judicial reorganisation procedure

- **A) As part of a regular reorganisation plan (XX.75 CEL)**
  - Condition: business continuity of remaining entity (>< B)
  - To be negotiated during the period of temporary stay of enforcement actions
  - To be voted by the creditors (“creditors’ democracy”)
  - To be confirmed (“**approval**”) by the commercial court (XX.79 CEL) – BUT limited grounds for **denial**
    - non-respect of a rule of procedure (broadly understood)
      - ESG? Rights of employees
    - Breach of public order

## Existing case law:

- Discrimination of certain creditors
  - Fraud
  - (Abuse of the procedure)

## Quid ESG?

- No doubt if transfer >< formal legal rule of public order
- Uncertain if ESG-concerns qualify as “public order” (connection with mandatory law needed)

- non-respect of procedure (broadly understood)
  - ESG? Rights of employees
- **Breach of public order**

## III. Transfer of business

- **A) As part of a standard reorganisation plan**
  - **EU Directive (art. 10)**
    - 2. Member States shall ensure that the conditions under which a restructuring plan can be confirmed by a judicial or administrative authority [...] include at least the following:
      - (a) the restructuring plan has been adopted in accordance with Article 9;
      - (b) creditors with sufficient commonality of interest in the same class are treated equally, and in a manner proportionate to their claim;
      - (c) notification of the restructuring plan has been given in accordance with national law to all affected parties;
      - (d) where there are dissenting creditors, the restructuring plan satisfies the best-interest-of-creditors test;
      - (e) where applicable, any new financing is necessary to implement the restructuring plan and does not unfairly prejudice the interests of creditors.

## III. Transfer of business

- **A) As part of a standard reorganisation plan**
  - **EU Directive (art. 10)**
    - 3. Member States shall ensure that judicial or administrative authorities are able to refuse to confirm a restructuring plan where that plan would not have a reasonable prospect of preventing the insolvency of the debtor or ensuring the viability of the business.
    - + Article 13 (Workers) 1. Members States shall ensure that individual and collective workers' rights, under Union and national labour law [...] are not affected by the preventive restructuring framework

### III. Transfer of business

- **A) As part of a standard reorganisation plan**
  - **EU Directive**
    - No reference to ESG-concerns
    - Even not in preamble → creditor primacy (nuance for employees)
    - **Missed chance?** *E.g. art. 8 “content of restructuring plans”*
      - *“h) a statement of reasons which explains why the restructuring plan has a reasonable prospect of preventing the insolvency of the debtor and ensuring the viability of the business, including the necessary pre-conditions for the success of the plan. [...]”*
    - Future Belgian implementation: even less room for ESG-concerns in court approval? To avoid!

## III. Transfer of business within a (Belgian) judicial reorganisation procedure

- A) As part of a standard reorganisation plan
- **B) As part of a specific transfer of business procedure (XX.84 CEL)**
  - Formal reorganisation procedure (not a bankruptcy procedure, although some characteristics thereof; EU Directive not applicable)
  - Goal: transfer of business in going concern + winding up of remaining “shell company”
  - Transfer organized by **insolvency practitioner**
    - Collects bids from potential buyers; can define conditions
  - Final decision to sell must be taken by the **commercial court**
  - Uncertainty caused by ECJ case C-509/17 (**Plessers**)

## III. Transfer of business

- **B)** As part of a specific transfer of business procedure
  - Final decision by the **commercial court**: Grounds? - Limited guidance in the law:
    - *“As a matter of priority, the insolvency practitioner looks at the continuity of all or part of the company's activities, taking into account the rights of the creditors.”* (art. XX.87, §1 CEL)
    - *“If there are several comparable offers, the court will give preference to the offer that guarantees the preservation of employment through a social agreement.”* (art. XX.89, §1 CEL)
    - Comparable offers → workers' rights are decisive
    - What if offers are not comparable?
      - Commercial Court Ghent 28/01/2021 (E5-mode)
        - » The amount of the bid is not decisive, the continuity of business prevails
    - Can courts use ESG-criteria when selecting the preferred bid?



## III. Transfer of business

- **B)** As part of a specific transfer of business procedure
  - Final decision by the **commercial court**: Grounds? - Limited guidance in the law
    - How can courts use ESG-criteria when selecting the preferred bid?
      - Workers' rights
      - Through the concept of “public order” (*cf. supra*)
      - Through the concept of “business continuity”
        - » → “viability of the business” as central future concept?
      - How to cope with conflicting ESG-concerns?

## IV. Transfer of business within a **bankruptcy** proceeding

- Transfer in going concern during a **bankruptcy proceeding**
  - Bankruptcy trustee or every other interested party can ask the commercial court to temporarily continue the business of the bankrupt company (art. XX.140 CEL)
  - Transfer of business in going concern as part of the liquidation of the company (art. XX.166, §3 CEL)
    - Agreement between bankruptcy trustee and the buyer
    - To be approved by the commercial court
      - No guidance on criteria for approval
        - » Procedural flaw
        - » Public order (→ ESG)

## V. Preliminary Conclusions

- **Creditor primacy** is still the leading concept within EU insolvency law
  - No parallel developments as within EU company law (yet)
    - Key 2019 **EU directive** on restructuring and insolvency completely ignores ESG-concerns
    - Nuance for rights of **employees** (dual status) and bankruptcy of individuals
    - Awareness required as to important differences between company and insolvency law
- On the national level (**Belgium**), ESG-concerns can be usefully introduced during the process of judicial approval of transfer of business within insolvency procedures, particularly through concepts of
  - Public order
  - Business continuity
  - In the future: business viability