Restructuring Cross Border Groups: Key Considerations Around Foreign Tax and Finance Driven SPVs

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June 2020

INSOL SPECIAL REPORT

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Acknowledgement

INSOL International is very pleased to publish a Special Report titled "Restructuring Cross-border Groups: Key Considerations Around Foreign Tax and Finance-driven SPVs" by Professor Reinout Vriesendorp, Ferdinand Hengst and Wies van Kesteren of De Brauw Blackstone Westbroek, with contributions from Professor Irene Lynch Fannon of University College Cork, Michel Nickels and Benoit Nerriec of Elvinger Hoss Prussen.

The use of foreign or offshore special purpose vehicles ("SPVs") is increasingly more commonplace amongst multinational groups for the purposes of holding foreign assets or to obtain financing for the group's operations. Many of these SPVs are incorporated in jurisdictions such as The Netherlands, Ireland and Luxembourg due to the favourable tax regimes that are available in such countries. While operating as a going concern, the group as a whole may not pay much attention to the SPVs but in a situation of financial distress, the SPVs can play an important role in any restructuring or insolvency procedure because the groups financiers may be direct creditors of the SPVs.

This report provides an overview of the key considerations involved in restructuring cross-border groups where the group has foreign SPVs incorporated in The Netherlands, Ireland and Luxembourg. The report also focuses on the relevant fiduciary duties of the board of directors of the SPVs; the possibility of SPVs disrupting a cross-border group restructuring and the implications on upstream and downstream guarantees between related companies.

INSOL International sincerely thanks Professor Reinout Vriesendorp, Ferdinand Hengst, Wies van Kesteren, Professor Irene Lynch Fannon, Michel Nickels and Benoit Nerriec for carrying out extensive research and writing this excellent special report.

June 2020

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Restructuring Cross-border Groups: Key Considerations Around Foreign Tax and Finance-driven SPVs*

1. Introduction

1.1 Concern with special purpose vehicles

Fuelled by ever-increasing globalisation and international trade, the use of foreign or "off-shore" special purpose vehicles ("SPVs") by internationally operating groups has continued to grow in recent years. SPVs are frequently deployed as intermediate holding companies for foreign assets or activities, and for group financing. Often, one of the main reasons why SPVs are incorporated in a jurisdiction other than the home jurisdiction of the TopCo or the group as a whole is for tax purposes.

The use of SPVs involves drawing alien laws into the group but this is not a major concern for a group in a going-concern situation and, therefore, typically not on the radar of the board. However, in a restructuring environment, SPVs have been shown to play a disproportionately important role, not least because most restructurings are implemented at the level of the holding company or issuer of debt instruments – precisely the role often assigned to SPVs. In this report, we intend to raise awareness of this issue among insolvency specialists and board members and provide a starting point for thinking about specific complications when restructuring a group that includes such SPVs.

1.2 The Netherlands, the Republic of Ireland and Luxembourg

The Netherlands, the Republic of Ireland and Luxembourg are among the jurisdictions most frequently used for incorporation of this type of SPV. In contrast to other typical off-shore jurisdictions (e.g. British Virgin Islands, Guernsey, Cayman Islands and Bermuda), two of these (the Netherlands and Luxembourg) operate a civil rather than common law system (as in the Republic of Ireland). Thus, these three jurisdictions provide a good combination for examining the typical consequences in a comparative civil and common law context.

In the Netherlands and Luxembourg, any legal entity can constitute an SPV in accordance with general corporate law provisions. In Ireland, however, SPVs are established with reference to section 110 of the Taxes Consolidation Act 1997(as amended) which deals with the taxation regime for SPVs operating in Ireland. In recent years, the Central Bank of Ireland has added restrictions regarding certain types of SPV, in particular those dealing with assets based on real property.

1.2.1 The Netherlands

By International Monetary Fund standards, the Netherlands is the world's largest recipient and the biggest provider of foreign direct investments ("FDIs"), ahead of the United States ("US") and China.[1] Over the period 2013–2015, the Netherlands represented 33% of the aggregate FDI outflow from the European Union ("EU") to non-EU countries, second only to Luxembourg (40%).[2] Recent figures show that 80% of the FDI inflow in the Netherlands is channelled into SPVs with limited physical presence or employment in the Netherlands.[3]

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* The views expressed in this report are the views of the authors and not of INSOL International, London.

[1] International Monetary Fund Data (Coordinated Direct Investment Survey, 12 December 2018); reference year 2017.

[2] Eurostat, Foreign Direct Investment Statistics (April 2017).

[3] Organization for Economic Co-operation and Development, *FDI in Figures* (April 2016).

One of the main drivers is that the Netherlands has concluded a large number of tax treaties providing, in many cases, reduced or zero withholding tax on dividends, interests and royalties. Moreover, the Netherlands itself does not have a withholding tax in place as regards interest and royalty payments (at least until 2021[4]), while the levying of dividend withholding tax is restricted by tax treaties and EU law. In addition to the tax treaty network, one of the benefits of the Netherlands is its broad participation-exemption which fully exempts dividends and capital gains arising from qualifying subsidiaries from corporate income tax. Third, many taxpayers have arrangements to clear in advance the tax treatment of structuring or contemplated transactions with the Dutch tax authorities by means of a binding agreement – an Advance Tax Ruling. In addition to the beneficial tax regime for cross-border groups, a key attraction for debt-issuers to use a Netherlands-based SPV is that the Netherlands provides financial creditors with a very reliable and predictable entry point for enforcement of security and, in the summer of 2019, moved to become the front-runner in modernised restructuring schemes on the European continent.

1.2.2 Republic of Ireland

The Republic of Ireland also benefits from a broad range of tax treaties. This has contributed to the success of its strategy to foster FDI by pursuing a consistent policy since the 1980s regarding the attraction of multinationals. Next to an extensive network of international tax treaties, this strategy has partly relied on corporate tax structures, including a relatively low corporate tax rate of 12.5% generally applicable to all corporates. Furthermore, key elements of the strategy include the availability of a young, English-speaking and well-educated indigenous workforce and a shared common law tradition, particularly relevant to US multinationals. In line with the growing importance of the key characteristics of the regulatory framework to the growth of the funds industry,[5] the Irish strategy has also been supported by pro-business responsive regulation.

1.2.3 Luxembourg

Also catching the eye of international tax-structuring experts, Luxembourg has for years topped the rankings as the most popular jurisdiction for the incorporation of holding companies. In addition, the “double-Luxco“ structure has been developed in order to mitigate the risk for secured creditors, resulting in a hostile centre of main interests (“COMI”) relocation to France of acquisition structures initially set-up in Luxembourg for the acquisition of French assets.[6] The main feature of the “double-Luxco” is to avoid the application of French restructuring procedures, which suspend the enforcement of securities. Such structures may also be used for the purposes of creditor protection, where the assets are located in other EU Member States.

1.3 Subject of this report

The restructuring toolkit in most European jurisdictions has in recent years been subject to review and changes, with more focus on restructuring of debts and out-of-court solutions than on the traditional liquidation bankruptcy. This is fuelled by increased restructuring activity in Europe, by the European Directive on restructuring

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[4] The Dutch government has announced its intention to introduce a withholding tax on intra-group interest and royalty payments made to low-tax jurisdictions (such as listed jurisdictions with a statutory rate below 9%) or EU blacklisted jurisdictions and in abusive situations.

[5] According to www.irishfunds.ie, 880 fund managers from 50 different countries have assets administered in Ireland. Over 40% of global hedge funds’ assets are administered in Ireland. The Irish Stock Exchange is a market leader in the listing of debt securities (www.ise.ie).

[6] This structure has its origins in the famous French *Coeur Défense* case.

and insolvency,[7] and the adoption of the United Nations Commission on International Trade Law ("UNCITRAL") Model Law on Enterprise Group Insolvency.[8] For instance, Spain, France and Germany have each designed and implemented informal (out-of-court) restructuring procedures, while the United Kingdom ("UK") has greatly increased the use of its long-existing restructuring scheme of arrangement, and, in addition, has also announced a general reform of its debt-restructuring regime. Furthermore, the Republic of Ireland has a UK-type scheme of arrangement process, arising from its shared common and company law heritage with England and Wales. It also has a modern restructuring process modelled on the US Chapter 11, which was introduced in 1990. In some jurisdictions, including in the US and the Netherlands, important case law on the role of SPVs was made in autumn 2018, and national legislative initiatives are being developed. These plans will likely precede the implementation of the European initiatives and may even achieve more.

This report focuses on the specific issues relating to the involvement of SPVs in restructuring matters under existing legislation, specifically when those SPVs are located in the Netherlands, Ireland or Luxembourg, as the key European jurisdictions in this regard. We will explain the concepts largely by reference to the Netherlands and then compare them with the situation in Ireland and Luxembourg. We will also describe how recent developments and anticipated new legislation will affect typical considerations. The report is intended as a reference guide for insolvency specialists advising international groups on such restructurings. Please note that comparisons to jurisdictions other than the Dutch, Irish and Luxembourg contexts have not been vetted by experts from those other jurisdictions and are for illustrative purposes only.

In our research, we took the approach of interpreting restructuring processes during the last decade (post-Lehman Brothers era) that involved SPVs in international groups, which we believe has allowed us to combine both legal and practical considerations. The report reflects the situation as at 1 June 2020.[9]

2. Typical considerations

2.1 Case study

For the purpose of analysing the various considerations applicable to the restructuring of SPVs, it is beneficial to use a case study that includes a number of common elements. However, as no two international groups are structured and financed in the same way, it is not possible to build an exemplary case study which covers all situations.

In our case study, TopCo is the parent, located in the main (home) jurisdiction of the wider group; HoldCo is an intermediate holding company located in an undefined jurisdiction; FinCo is a financing SPV with its seat in the Netherlands, Ireland or Luxembourg; and the OpCos are operational subsidiaries located in a variety of jurisdictions (see diagram below).

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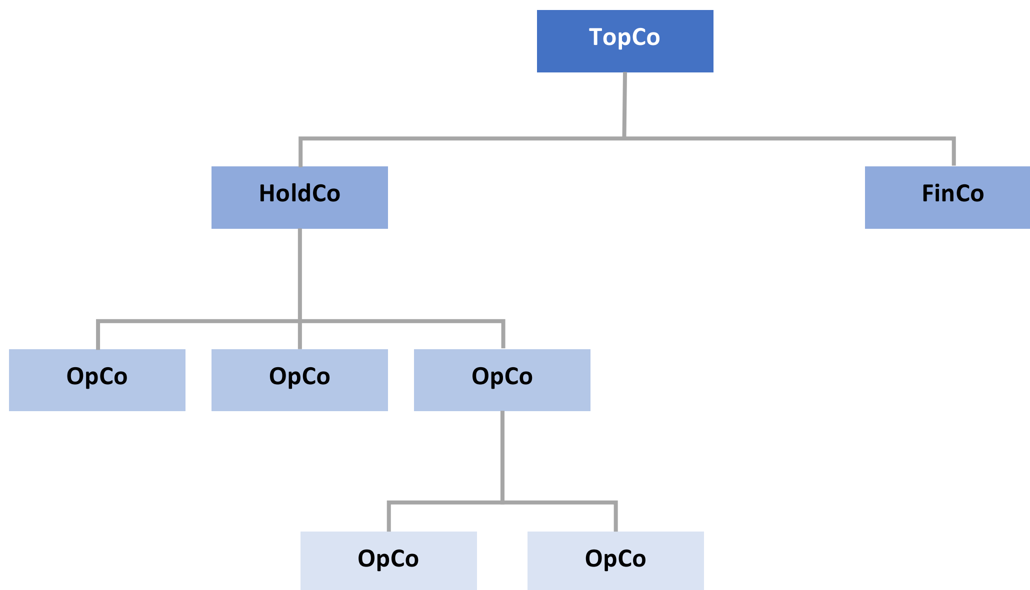
[7] Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks, on discharge of debt and disqualifications, and on measures to increase the efficiency of procedures concerning restructuring, insolvency and discharge of debt, and amending Directive (EU) 2017/1132, EU 26.6.2019, L 172/18.

[8] UNCITRAL Model Law on Enterprise Group Insolvency and its Guide to Enactment, available at: https://undocs.org/en/A/CN.9/WG.V/WP.165, adopted on 15 July 2019, https://undocs.org/en/A/74/17; see also Part 3 (Treatment of enterprise groups in insolvency) of UNCITRAL Legislative Guide on Insolvency Law, available at: https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/uncitral/en/leg-guide-insol-part3-ebook-e.pdf.

[9] This report does not deal with any specific laws and regulations that were introduced as a response to the Covid-19 crisis. The report has also not dealt with specific issues that have arisen due to this crisis.



We identify four key considerations that need to be taken into account in the case of restructuring an international group of companies as outlined above. These are:

i) fiduciary duties for the board of FinCo;

ii) disruption of a global restructuring by action at FinCo level;

iii) the key role of upstream and downstream guarantees; and

iv) recognition of restructuring results.

Many other considerations play a role, but from our research it appears that these four considerations were embedded in the majority of restructurings over the past few years. In this section, we will briefly introduce each of the considerations. In the following sections, we will discuss the legal frameworks in the Netherlands, Ireland and Luxembourg for each consideration indicated.

2.2 Key concerns for the board: fiduciary duties

The boards of directors of foreign subsidiaries will have to consider their fiduciary duties under the applicable (foreign) law, which may substantially deviate from what they are familiar with. This is particularly important for directors who have been appointed (sometimes without extensive consideration) in the foreign subsidiary, simply by virtue of their position elsewhere in the group, so they will need to get comfortable with the duties and potential risks before entering into any restructuring transaction.

Across the EU, director fiduciary duties are to a large extent comparable and based on the same legal principles. The devil is, however, in the detail. To protect the individual directors in choppy waters, it is important for the directors to thoroughly understand any sensitivities and deviations that are outside of their experience, such as fatal filing deadlines and the subsidiary's ability to continue as a going concern.

2.3 Disruption at FinCo level

In a going concern situation, directors of FinCo need not be overly cautious in aligning with the needs of the parent and the wider group. Creditors, too, typically look at the group as a whole and do not focus particularly on the SPV that issued the debt instruments. However, in distress situations, both directors and creditors may become concerned about their position under the laws of the various jurisdictions and may change their behaviour accordingly. In insolvency, and sometimes even at an earlier stage, the board is under an obligation primarily to consider the position of that company and their principal duty is towards creditors, not towards the parent-shareholder. Conversely, FinCo's creditors will try to protect their own interests, which may not be aligned with the approach taken by creditors of the parent or the wider group.

Accordingly, in stormy weather, the foreign FinCo may become a forum for disruption and, therefore, assessing the independent position of the board and creditors of the FinCo should be part of any restructuring.

2.4 Key role of upstream and downstream guarantees

Where financing of a group is attracted by FinCo, TopCo (downstream) or OpCos (upstream) typically provide guarantees. As such, financiers have direct recourse against the entities which hold the group's assets and on the parent. These guarantees may take one of the following forms: individual guarantees on the debt, typically provided in the context of a specific contract; a more widely applicable guarantee, such as a parent company guarantee given to a creditor or group of creditors; or a blanket guarantee for consolidation purposes, such as the specific Dutch guarantee under section 2:403 of the Dutch Civil Code.

While creditors and management outside the restructuring space typically assume that TopCo's creditors are better positioned than creditors of the subsidiaries, the reverse is true in a restructuring. An OpCo creditor has direct recourse against the assets and the cash-generating ability of that OpCo, provided that such an OpCo is healthy. A FinCo typically has direct claims on those OpCos by virtue of its intra-group on-lending claims and can pay its debt out of the proceeds. A TopCo, or pure-play intermediate holding company, on the other hand is, as shareholder, dependent on distributions from its subsidiaries – by default, subordinated to creditors – for it to be able to pay its own debts, unless it also has intra-group financing claims.

Creditors with guarantees securing the principal claim against FinCo have the benefit of "double-dipping": namely, they have recourse against the assets of both the borrower and the guarantor, or, if effectively there is only one pool of assets, they may have two claims into that pool. The treatment of double-dipping varies substantially between jurisdictions, but it may result in a very favourable position for the creditor holding the guarantee.

2.5 Recognition of restructuring results in foreign jurisdictions

The reality is that the management, advisors and main creditors in TopCo's jurisdiction or the group's home jurisdiction will be focussed on restructuring processes in their own jurisdiction, and justifiably so. However, it is important to consider whether the result achieved realises the desired effect in relation to foreign group companies as well.

A haircut agreed in a scheme of arrangement under English law, or a share issue as part of a debt for equity swap ordered in US Chapter 11, may often not be effective

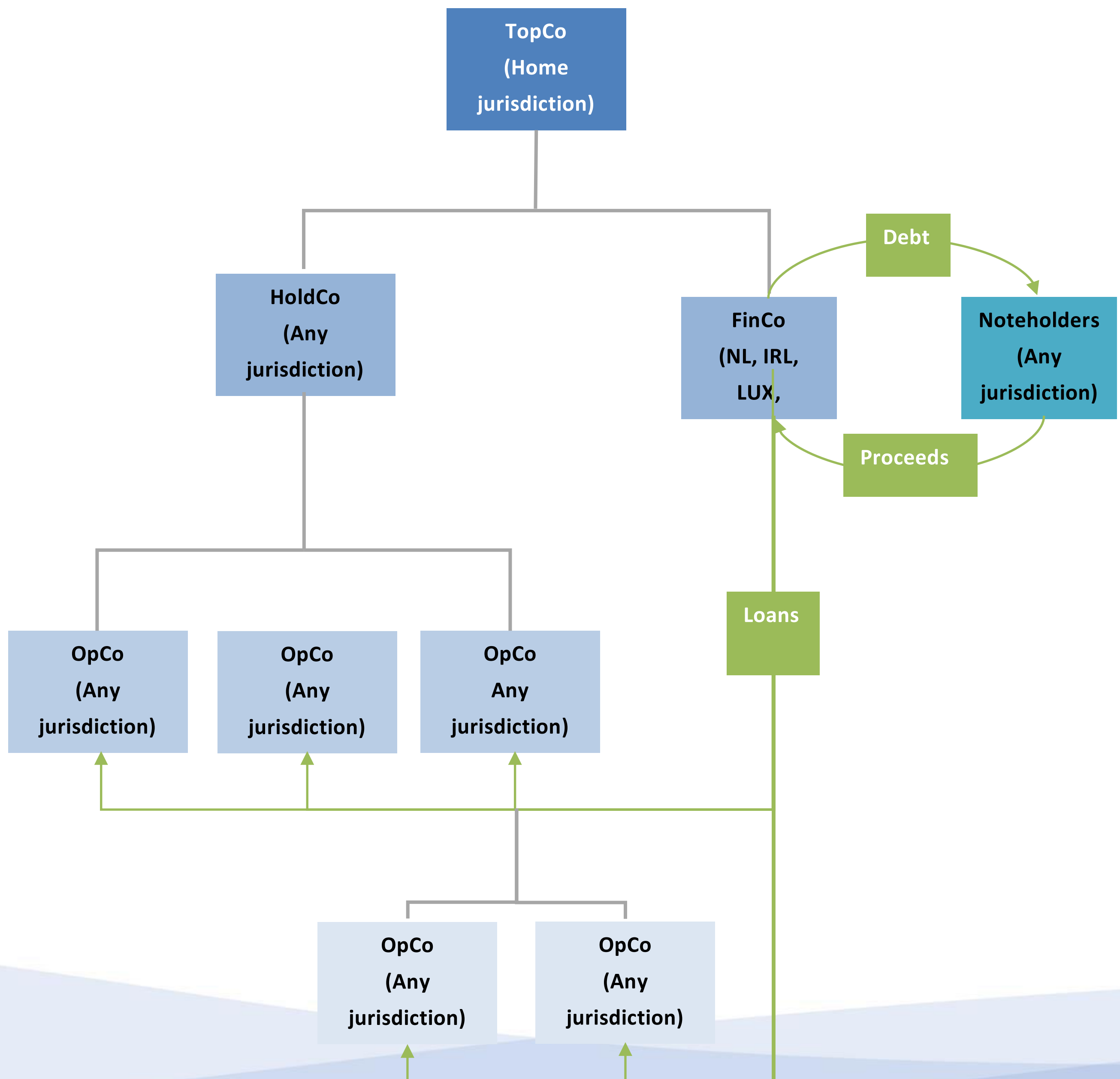
when it concerns a debtor outside England or the US, bar further court proceedings in the foreign jurisdiction. The steps required in the foreign jurisdiction to achieve the same result may impact on the certainty of the deal and its timing and needs to be carefully reviewed, preferably well in advance. The options for recognition of (foreign) restructuring plans under Dutch, Irish and Luxembourg law are discussed below in section 6 of this report.

3. Fiduciary duties

3.1 Introduction

To give further content to the board's fiduciary duties, please consider the following addition to the case study provided above.

The case study assumes that FinCo's sole purpose is to raise financing for the group. FinCo issues notes and on-lends the proceeds of those notes into the group. FinCo's stakeholders are TopCo, as shareholder, and the noteholders, as FinCo's creditors (see below).



3.2 The Netherlands

Under Dutch law, the management board is responsible for the day-to-day management of the company. The management board owes its duties to, and therefore must consider the interests of, the company and all of its stakeholders. Primarily, the board needs to consider the general interest of all stakeholders in preserving a going concern. Subsequently, the board needs to take into account the specific interests of the different groups of stakeholders, such as shareholders, creditors and employees.

FinCo's board does not owe any special duties to any of FinCo's individual stakeholders. The interests of the stakeholders ought to be considered on a group level, as well as on FinCo level. Provided that FinCo's continuity is not at stake, its corporate interest will be defined by the interests of the wider group because it has no other activity than to finance the group.

However, when FinCo's continuity is at stake and depending mostly on the recourse position of FinCo on the assets of the group, the board will need to consider that the interests of FinCo and its creditors may no longer be aligned with the interests of the group or parts of the group. Under Dutch law, the board is obliged to give priority to FinCo's corporate interest at the risk of being blamed for mismanagement.

Furthermore, the board's focus will have to shift from realising shareholder value to ensuring that payment obligations are met. The shift is a sliding scale depending on the level of distress. On the brink of insolvency, the interest of the noteholders to receive payment of their due and payable claims becomes most prevalent and will outweigh the shareholder interest.

Unlike some jurisdictions, Dutch law does not require the board to file for insolvency (bankruptcy or suspension of payments) if the company's continuity becomes unlikely or, even, if insolvency becomes inevitable. The flexibility for the board to time a filing for insolvency is a notable advantage of Dutch law. This does not affect the fact that the board may, at some point, have no other choice than to file for insolvency to protect themselves. Entering into new obligations when FinCo can no longer reasonably be expected to continue paying its obligations, but also not convening a meeting of shareholders when the net assets are forecasted to drop below half the company's paid-in capital, may put directors at risk of being personally liable.

A specific concern is that certain pre-bankruptcy transactions can be challenged pursuant to Dutch preference law, which is more restrictive than, for example, US bankruptcy law. Under Dutch law, any pre-bankruptcy transaction is exposed to claw-back if: (i) there was no specific legal obligation to perform the transaction; (ii) creditors are prejudiced as a result of the transaction; and, if so, (iii) the management board knew or ought to have known that there was a reasonable chance of such prejudice (i.e. of bankruptcy of FinCo). If a transaction is successfully challenged, it can be nullified, causing the effects of the legal act to be reversed or undone by operation of law to the extent possible. It can also be a ground for directors' liability.

Currently, entering into what in other jurisdictions may be considered secured debtor in-possession financing in court-approved super senior loans also risks being challenged under Dutch preference law. A Bill introducing court confirmation of an extrajudicial restructuring plan ("CERP") will change that.[10] Under the Bill, security

[10] Enactment is envisaged in the summer of 2020. A booklet explaining the highlights of the Bill along with an unofficial English translation of the Bill and its explanatory memorandum can be found on De Brauw's website: https://www.debrauw.com/CERP.

provided in exchange for funds relating to a restructuring will be deemed not to have prejudiced creditors if certain formalities are met.

Another fiduciary duty for directors of a Dutch SPV relates to accounting and publication of its annual accounts with the Dutch Trade Register. Managing directors may be personally liable towards the company, the estate or third parties (e.g. creditors, shareholders) if they have manifestly improperly managed the company and such failure is severely reproachable. A director's conduct is manifestly improper if, given the circumstances, no adequate director would have acted in the same way. Although the Dutch Supreme Court has consistently ruled that this is a high bar for liability, manifestly improper management is deemed to exist if the company has not complied with its accounting obligation or the requirements to disclose its annual accounts. Furthermore, this manifestly improper management is assumed to have been an important cause for the company's bankruptcy. If awarded, the consequences can be severe: if the company goes bankrupt, managing directors can be personally liable for the entire shortfall in the insolvent estate.

The board's fiduciary duties under Dutch law both in and outside insolvency proceedings play an important role in the restructuring of an international group with Dutch entities. These duties may trigger individuals on the board of a Dutch SPV to take matters into their own hands, thus causing a threat to the group's restructuring plans as discussed in section 4.

3.3 Ireland

Under Irish law, the directors' duties range from what are described as "fiduciary duties" to what are described as "common law duties". The former is based on the idea that a director is similar to a trustee. Accordingly, fiduciary duties derive from equity; they are fiduciary in nature. In contrast, the common law duties focus primarily on the level of skill and care required from a director. This legal analysis, which distinguishes between equity and common law, is shared with the legal framework in England and Wales.

In any event, duties derived from case law derived from English and Irish common law principles are now codified in legislation and are stated to be owed to the company "*and the company alone*".[11] The directors of an Irish FinCo will therefore owe their duties to that FinCo. The legislation envisages that, in the exercise of their duties, directors shall take into account the interests of employees in addition to those of individual shareholders under s. 224 of the Companies Act 2014. In the case of FinCo, this would include the interests of TopCo. Nevertheless, the directors' duties are owed to the company. The received opinion is that, as with Dutch law, there is no specific enforceable obligation owed to stakeholders, including employees and, more importantly in the context of this report, particularly to individual shareholders such as TopCo.[12] Therefore, the directors of FinCo in Ireland would have a broad discretion to consider the interests of FinCo as a going concern, and those interests would also reflect the interests of TopCo and the group. The references in legislation to other stakeholders seem to be intended to have the same effect as "other stakeholder statutes" in the US: they appear to be designed to give more discretion to directors rather than less.

[11] Companies Act 2014, section 228. For a further but concise description, see Irene Lynch Fannon and Karole Cuddihy, 'Corporations and partnership law: Ireland' in *International Encyclopaedia of Laws* (Kluwer 2016).

[12] This issue has been the subject of a comprehensive review of Irish company law by the Company Law Review Group, which published a report in 2017 on this matter: Company Law Review Group, *Report on the Protection of Employees and Unsecured Creditors* (2017), available at: https://dbei.gov.ie/en/Publications/CLRG-Report-on-the-Protection-of-Employees-and-Unsecured-Creditors.html.

Where the company moves from being a healthy going concern to an entity where continuity is at stake, there is a shift in emphasis. The obligation to consider the interests of creditors when continuity is at stake is part of Irish case law. This case law has been developed with reference to case law from other common law jurisdictions, including New Zealand, Australia, and England and Wales. According to this case law, a director's duty to consider the interests of creditors arises at the point where the company becomes unable to pay its debts or is near insolvency. The extent of these duties is, however, unclear as they have not been codified and can only be derived from case law.

In this sense, the situation described in relation to directors' duties in the Netherlands is broadly similar in Ireland. Unfortunately, however, the Irish position is not as clear as the statements regarding the Netherlands would suggest for the latter jurisdiction. So, for example as described in section 3.2. when FinCo's continuity appears to be at stake, different considerations apply to the emphasis on the group's interest. Directors of an Irish FinCo would have to be advised that they must continue to pay attention to FinCo's interest, but that their decision-making at that point must demonstrate some consideration of the interests of the creditors, in our example the noteholders. The extent of this obligation relies *inter alia* on the following statement from a decision of the Irish Supreme Court in relation to payments made on behalf of a number of group companies to the Revenue authorities where the court referred to other common law decisions and stated:[13]

> "*At the time the payments were made, the four companies were under the management of their directors pending imminent liquidation. Because of the insolvency of the companies the shareholders no longer had any interest. The only parties with an interest were the creditors. The payments could not have been lawful because they were made in total disregard of their interests.*"

A recent report from the Company Law Review Group in 2017 has stated that this legal ought to be codified.[14]

In addition to the codified duties, directors have to operate within a more modern legislative framework which creates specific penalties of restriction and disqualification for directors of insolvent companies. Case law indicates that the court may consider a number of issues within the legislative framework. These issues require compliance with domestic legislation, compliance with duties generally and, finally, that the directors have considered creditors' interests once the company reaches a point of insolvency. Once a company becomes insolvent, the liquidator is bound to apply for a restriction order which has a semi-automatic quality (but not necessarily disqualification orders) unless relieved from doing so in relation to a certain director by the regulatory authorities (the Office of Director of Corporate Enforcement[15]). Once the application is made by the liquidator, directors are obliged to positively demonstrate to the court that they have acted honestly and responsibly in relation to the insolvent company. Where this is not proved to the satisfaction of the court, the director will be subject to a restriction order which prevents him / her from being involved in the management of other companies unless these companies comply with certain conditions. These conditions focus primarily on capitalisation requirements. Directors also face the possibility of the even more stringent penalty of disqualification. This can be applied on the basis of a number of enumerated

[13] *Re Frederick Inns Ltd (in liquidation)* [1994] 1 ILRM 387.

[14] See Company Law Review Group, *Report on the Protection of Employees and Unsecured Creditors* (2017), available at: https://dbei.gov.ie/en/Publications/CLRG-Report-on-the-Protection-of-Employees-and-Unsecured-Creditors.html.

[15] See s 818, 842 Companies Act 2014, See further www.odce.ie.

grounds, the most common of which is the finding that the director is "unfit to be involved in the management of a company".

The abovementioned provisions are regularly and consistently applied in the case of a company's insolvency. In addition, there are other provisions relating to fraudulent and reckless trading which, although often used unsuccessfully, have an impact on decision-making. These latter stipulations are the legislative provisions that will shape the decision-making of directors of an Irish FinCo where continuity is at stake. Therefore, as described in section 3.2, Irish law differs from the description of Dutch law insofar as, under Irish law, there is an actual obligation to consider whether one should continue to trade or alternatively file for bankruptcy. The obligation is not couched in terms of a positive obligation to file for bankruptcy, but the reckless trading provision does impose liability on individuals who continue to trade where there is no reasonable prospect of the creditor being paid, or where it would be reasonable to decide that to continue trading would cause loss to creditors and therefore it is reasonable to expect directors to file for bankruptcy.

Similar to the Dutch system are the transactional avoidance provisions which may address particular last-minute transactions. Of particular interest in this context is a provision in Irish law which allows transactions to be set aside if the effect of the disposal is to perpetrate a fraud on the company, its creditors or members. The court may find "merely … that the company, its creditors or members [are] deprived of something to which it is, or to which they are, lawfully entitled".[16]

Because of the abovementioned obligations and legislative standards, in a distressed situation, the board's focus will have to shift from realising shareholder value – in this case for TopCo – to ensuring that creditors' interests – in this case the noteholders – are brought to the fore. The interplay between these obligations will depend on the apparent solvency of the company and the likelihood that the company is or will become unable to pay its debts.

3.4 Luxembourg

Under Luxembourg law, the board of directors is in charge of the management of the company. Its powers are determined either by law, the articles of incorporation of the company or the provisions of a shareholder agreement, if any. Its powers and competences are generally defined as those which are not specifically reserved by law or the articles of incorporation of the company to the general meeting.

The board of directors shall at all times ensure that its decisions are compliant with the company's interest and they need to submit any of its decisions to a corporate interest test. The question as to whether the relevant facts are sufficient to conclude that there is adequate corporate benefit or interest turns on commercial considerations such as the nature of the transaction in question, the status (current and on-going) of the relevant company, and prevailing market and economic considerations. Such matters must be weighed by the directors: i.e. would a director acting reasonably conclude that the relevant transaction appears to be in the corporate interest of the company, balancing the relevant considerations? Furthering the company's corporate interest implies making decisions aimed at supporting the continuity and prosperity of the company. It is therefore absolutely justified to forego a short-term profit, or to accept a loss in the short term, in view of the long-term sustainability of the company.

[16] Murphy J in *Re Chatelain Thudichum (in liquidation) Ltd v Conway* [2010] [R529].

Decisions taken within a group are based on concerns that, by nature, cannot be compared to those of isolated companies. The existence of a group may thus justify a transaction with a group company that would be considered as irregular outside the context of a group. The intragroup solidarity may result, in certain circumstances, in the impoverishment of the company for the benefit of collective welfare. However, this may not cause a gross imbalance at the expense of the company, i.e. the individual interest of the company cannot be sacrificed in the interest of the group; it may only be tempered.

In the absence of any legal provisions under Luxembourg law, taken in the context of a group, it appears that three conditions have to be met in order for a decision not to be declared void because of the lack of corporate interest. First, the group may not structurally impair a group company in the name of common welfare. A temporary sacrifice is accepted insofar as the survival of the company is not at stake and the transaction is not entirely in contradiction with the company's corporate interest. Second, the company making a temporary sacrifice must afterwards make a reasonable profit from this sacrifice; its belonging to the group must bring certain benefits. In other words: when taking into account the interests of the group, the directors of the subsidiary are actually not sacrificing the interest of the company but working in pursuit of its long-term benefits. Third, the sacrifices of a group company must serve the interests of the whole group and not just the parent company's interest. The existence of a legitimate group interest is subject to certain conditions:

i) the existence of a structured group;

ii) the existence of an overall group policy;

iii) the transactions entered into by the company are given due consideration and provide for a balance of the rights and obligations (including the considerations paid in the context of such transactions) of the group companies that are party to such transactions; and

iv) the transactions entered into by the company neither exceed its assets nor put it at a serious risk of becoming insolvent.

Apart from the interests that it must serve, the board of directors has certain duties in relation to corporate housekeeping, which include, for example, the obligation to submit the annual accounts of the company to the shareholders for approval no later than six months after the end of the financial year and to publish the approved annual accounts in accordance with the applicable legal provisions. The violation of such obligations may not only result in personal criminal and civil liability of the board members but may also entail a judicial liquidation of the company.

In addition, the board of directors has specific duties if the company is facing financial difficulties. Under Luxembourg insolvency law,[17] if the legal conditions for the opening of bankruptcy proceedings have been met, the board of directors has the obligation to file for bankruptcy within one month. Failing to do so may result in criminal and civil liability of the board members. Although, in practice, public prosecutors only prosecute cases where the non-filing for bankruptcy resulted in an increase of the losses of the insolvent company, this provision has a serious impact on the decision-making process at board level.

[17] Luxembourg insolvency law is based on Belgian insolvency law, with the main difference that Luxembourg insolvency law has so far not been reformed, whereas Belgium insolvency law has been subject to certain important modifications. The currently pending Luxembourg draft Bill will be discussed below.

Finally, Luxembourg insolvency law contains provisions that affect the behaviour of board members in insolvency scenarios in a similar way as in the Netherlands. For instance, as under Dutch law, certain types of transactions are at risk of avoidance if they occur during the so called "suspect period". This timeframe is determined by the court opening the insolvency proceedings and usually corresponds with a six-month period prior to the insolvency. In Luxembourg, such transactions may result in liability of the directors that approved the transactions, as it does in the Netherlands. Another stipulation that impacts the board of directors is its obligation not to favour certain creditors to the detriment of the insolvent estate and to fully cooperate with the insolvency receiver as soon as insolvency proceedings have been opened.
As a consequence of the above obligations of board members of a Luxembourg company, specifically in the context of financial distress or a pre-insolvency scenario, it is necessary to keep in mind that board members may encounter personal civil and criminal liability under Luxembourg law when restructuring an international group including a Luxembourg SPV.

4. Disruption at FinCo level

4.1 Introduction

As discussed in section 2.3, FinCo's jurisdiction may become a forum simply because either or both of its board and its creditors may use the toolkit additionally available under local laws to protect their interests, including their interests in the restructuring of TopCo, or perhaps to gain a position they would not have as a creditor of (only) the parent company.

To prevent and control any disruptions stemming from FinCo, it is important for an insolvency specialist or board dealing with a group of companies in distress to consider at an early stage the disruption that can come from a foreign FinCo. It may be wise to address the concerns of FinCo's board as soon as FinCo, or the group, starts experiencing distress. FinCo's directors will be more likely to consider the interests of the wider group restructuring if they feel that the board of TopCo is concerned with their position and personal interests, rather than prioritising their own position, possibly to the detriment of the group restructuring.

The same applies to the noteholders: if TopCo involves FinCo's noteholders in the group restructuring in the same way as it does its direct creditors – if the noteholders are not already creditors of the TopCo through a guarantee – the noteholders may feel more comfortable in following the other group financiers in a group restructuring, instead of enforcing local recourse, instigating liability claims aimed at the board, or even filing for bankruptcy of FinCo, thus posing a threat to the group and its restructuring.

The decision of the US Bankruptcy Court Southern District of New York of 4 December 2017 (*Re Oi Brasil Holdings Coöperatief UA*, Case No 17-11888 (SHL), 16-11794 (SHL) and 16-11791 (SHL)) proves that the threat of disturbance of a group restructuring by rogue creditors is not a theoretical one and that they are willing to use and invest in proceedings in FinCo's jurisdiction to increase their leverage over TopCo.

A hedge fund held notes issued by a Dutch financing SPV, similar to FinCo in our case study. Once the group became distressed, the hedge fund increased its investment as it believed the notes to be undervalued in the initial restructuring negotiations. It subsequently filed a petition for the SPV's bankruptcy in the Netherlands, to which the SPV responded by filing for suspension of payments. The hedge fund pressed both the other noteholders and the administrator to have the

suspension of payments converted into a bankruptcy. According to the New York court, one of the main reasons for the hedge fund's actions was to force the parent company to negotiate with the SPV's bondholders, including the hedge fund itself.

4.2 The Netherlands

Under Dutch law, the trustee appointed in the FinCo bankruptcy and the administrator appointed in suspension of payments will have strong regard towards both FinCo's standalone interests and those of its creditor body. Most recently, it was confirmed in Dutch case law that FinCo's individual corporate interest and the interest of its individual creditor body ultimately take priority over the interest of the wider group and the group creditors.[18] This means that, in case of FinCo's insolvency, a new entrant appears on stage and FinCo will pursue its own course.

The appointment of an administrator or trustee has four main consequences. First, it leads to diminished control of TopCo or the local board over FinCo and its assets. For instance, the trustee – and administrator less so – could make FinCo withdraw its credit lines to the OpCos and even reclaim the money it had lent to them. Second, the opening of insolvency proceeding will cause value destruction due to its public nature. Third, the administrator or trustee can furthermore order a "cooling-off" period or moratorium of up to two months, disrupting timelines elsewhere. And, finally, the fees and expenses of the administrator or trustee are paid for by the debtor.

To prevent insolvency proceedings and their possible negative implications for the group restructuring, it is important for an insolvency specialist or board dealing with a distressed group to keep an eye on FinCo's board and noteholders from the very start of the financial problems. This can prevent them from acting on their own, including going as far as filing for insolvency themselves.

The imminent introduction of CERP may prove to be of great value in this regard. Under CERP, the Dutch court can declare the extrajudicial restructuring plan, introduced by the legislative proposal, binding on all creditors, while the debtor stays in possession.

Another benefit of CERP is that claims from FinCo's noteholders under a guarantee provided by the (non-Dutch) TopCo can be made part of the restructuring plan. That way a double-dip can be prevented. This is described in more detail at the end of section 5.2.

4.3 Ireland

In Ireland, there are a number of insolvency proceedings available either to FinCo's creditors or to other stakeholders. The most traditional of these – an official liquidation – can be initiated by any creditor of FinCo's which has not been paid to a specified amount. This type of proceeding is not available to other stakeholders. FinCo's directors could initiate a voluntary liquidation if they are aware that a company is unable to pay its debts. Furthermore, they may also be motivated by a concern regarding personal liability or personal penalties imposed under Irish law as described above. Voluntary liquidations can be controlled by the company and the shareholders as a "members voluntary liquidation" or may be converted into a "creditors voluntary liquidation" if the company is insolvent. There are no provisions in Irish law which specifically require directors to file for insolvency.

[18] Thereby creating a hold-out position for the joint financiers of FinCo against the wider financier group at TopCo or group level. See Dutch Supreme Court 7 July 2017 *Re PTIF/Citicorp*.

In addition to insolvency procedures, Irish law provides for two kinds of restructuring procedure. They are both debtor in possession ("DIP") processes. The first is the Examinership process described below. The second is also a DIP process: a scheme of arrangement under similar legislative provisions as the English scheme of arrangement. This has been part of Irish company law since 1963 and derives from English company law which applied in Ireland prior to independence.

An Examinership can be initiated by the company, a director, a creditor (including employees) or a member holding at least one-tenth of the paid-up capital. It might therefore be possible for TopCo or an OpCo to initiate the Examinership in response to any pre-emptory moves or threatened moves towards liquidation by FinCo's creditors. Alternatively, the Examinership may be initiated by stakeholders in FinCo as a defensive mechanism. Once an examiner is appointed by the court, the court will also order a stay. This stay will initially last 70 days and can be extended by further applications to the court. During the stay, the examiner can seek to rescue or restructure the company in consultation with creditors and shareholders. The examiner will also seek additional finance. The relevant legislative framework includes a number of significantly disruptive elements in this context, including the examiner's access to certain charged assets to support borrowing and financing during the restructuring period and the examiner's ability to arrive at a restructuring plan through the use of cram-down (both intra and cross class cram down) provisions. The operation of all of these provisions are subject to court approval. It is important to realise that in some cases the outcome of the Examinership process can be quite different from what might have been intended by the initiator of the process, depending on further sources of funding and the agreements reached with shareholders and / or noteholders. There have been a number of cases illustrating this in recent years.[19]

The second type of restructuring process available is the Irish equivalent of the English scheme of arrangement. Interestingly, its provisions are not often utilised by insolvency specialists in Ireland as they generally regard the Examinership to be far superior.

Finally, under Irish law, receiverships are available as a remedy to secured noteholders. The right to appoint a receiver "to enter into possession and take control of property of the company"[20] in accordance with the terms of the loan documents is recognised as a right available to secured lenders in many common law countries including Ireland, Australia and New Zealand. This is a right based on contract, but it is governed by some legislative provisions. The right of a secured lender to appoint a receiver to realise the assets has been curtailed significantly in English law under the Enterprise Act 2002, but, if anything, it has been strengthened in Irish law due to its recognition under the Companies Act 2014. This Act contains an explicit statement of the receiver's powers and duties.

Examinership as a DIP process is often used as a countermove against a receivership. In the scenario described in this report, the DIP process could be used by TopCo in its role as a member or shareholder of FinCo to prevent an early move by a secured noteholder of FinCo. TopCo, in its capacity as a shareholder of FinCo, could apply to have an examiner appointed or could cause FinCo to apply to have an examiner appointed. In a DIP process, the control remains with the company rather than the lender. If TopCo, as a majority or sole shareholder, has applied to appoint an examiner, it can control the restructuring through that examiner. At the very least,

[19] For further detail on the history of this process, its development and utilisation, see Irene Lynch Fannon and Gerard Nicholas Murphy, *Corporate Insolvency and Rescue* (2nd edn, Bloomsbury 2012) and Lynch Fannon and Cuddihy (n 10 above) for a brief summary of the process.
[20] Companies Act 2014, section 437(3)(a).

the original senior lender will not have the right to appoint a receiver under Irish law and will have to cooperate on the rescue of FinCo.

As follows from the above, a number of potential disruptive influences can be identified:

i) An Examinership can commence once the company is "insolvent or likely to be insolvent" and there is a reasonable prospect of rescuing the company. The examiner will seek ways to restructure the company, including changing the rights of the noteholders or classes of them. Changes can also be made to the interests of shareholders such as TopCo. The availability of cram-down provisions in the legislation is critical to evaluating the effect of potential disruption. However, the court must finally approve the restructuring plan and may assess it in light of the overarching criteria of whether the restructuring plan is "unfairly prejudicial" to participants. These criteria specified in the legislation has been interpreted by the Irish courts in a number of cases.

ii) The English-style scheme of arrangement has not been utilised very frequently in Ireland to achieve a restructuring despite the legislative framework being present. However, although there have been one or two significant cases in recent times, the practice of the English courts regarding facilitating restructuring might not be replicated in Ireland even if there was an active line of jurisprudence in this area.

iii) Of potentially more significance in terms of disruption is the possibility of the appointment of a receiver to FinCo by one creditor having the right to do so. As the receiver can take over the management of FinCo with a view to securing payment of the particular creditor, this could have significant disruptive effects. Note that an Examinership can be initiated within a three-day period from the date of the appointment of a receiver and has been used in this way as a defence. The difficulty, however, is that a creditor with the right to appoint a receiver may be in a position to move quickly to the detriment of other noteholders, and certainly to the detriment of TopCo and similar stakeholders.

4.4 Luxembourg

On a preliminary note, it is important to briefly present the bankruptcy provisions currently existing under Luxembourg law. In this respect, it should be noted that Luxembourg insolvency law is based on Belgian law which goes back to the 19th century. To date, it has not gone through any important legislative reform. Although courts and administrators have established a particular practice in this area, they are still limited by the existing legal provisions. The main disadvantage is that, from a practical point of view, no real alternative exists to an insolvency proceeding. In other words, the existing legal collective restructuring mechanisms and suspensive measures, which should allow for avoiding insolvency proceedings, are almost never used and, in the very rare cases they are applied, do not result in a positive outcome.[21] This situation is often very frustrating for all parties involved: court, creditors and the insolvent company.

In response to this situation, the Luxembourg government proposed a Bill at the beginning of 2013.[22] The proposal has two main objectives: (i) the modernisation of Luxembourg insolvency law; and (ii) the introduction of mechanisms which will

[21] The proceedings referenced here are: (i) the *gestion contrôlée* (controlled management); (ii) the *concordat préventif de faillite* (composition with creditors); and (iii) the *sursis de paiement* (suspension of payments).
[22] Bill of Law No 6539.

effectively allow companies whose continuity is at stake to avoid the opening of a bankruptcy proceeding, e.g. collective arrangements with creditors.

However, as of today, the discussions in Parliament regarding this Bill are still ongoing, and it is difficult to assess when and if the proposal will come into force. In addition, thereto, it is at this stage not yet clear how exactly these mechanisms will function.

That being said, if a Luxembourg company finds itself in a situation where it is not in a position to pay its outstanding debts and does not obtain any funding either from third parties or related parties (such as a shareholder loan), the only outcome is a bankruptcy proceeding. This is due to the fact that, as described in section 3.4 Luxembourg law contains an obligation for directors to file for bankruptcy if the legal conditions for the opening of such proceedings have been met.

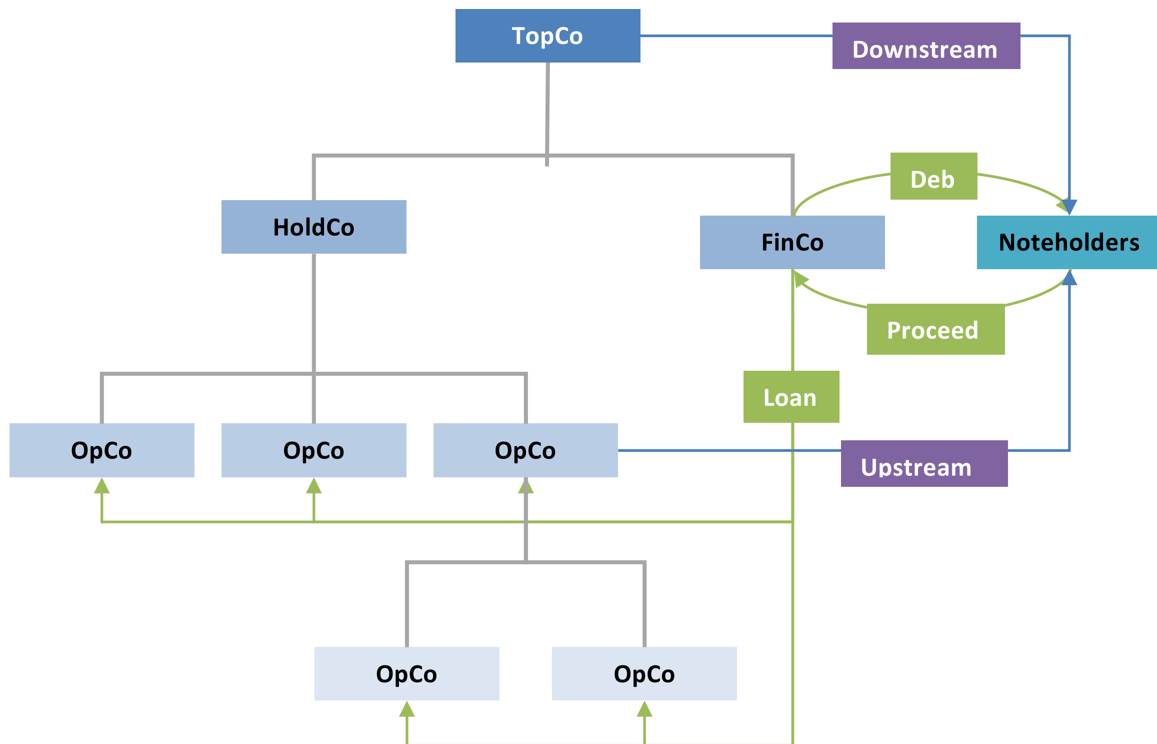
As a consequence, it is very difficult to prevent disruption because the directors are forced to act once the legal conditions of bankruptcy have been met. In this regard, however, one should note that the Luxembourg bankruptcy conditions are not based on a "negative equity test" under which the company would be considered bankrupt if its debts exceed its assets. Instead, a Luxembourg company is considered "bankrupt" as long as there is at least one substantial creditor whose claim is due and payable and which the company is not able to pay out of its existing assets or those received on the basis of third-party or shareholder funding, regardless of the company's debts exceeding its assets. As a consequence, in order to mitigate the disruption risk, directors will in general try to negotiate standstill agreements with creditors as soon as possible as this may prevent creditors from formally claiming payment and thereby triggering the one-month period for the bankruptcy filing as explained in section 3.4.

The opening of a bankruptcy proceeding will result in the appointment of a bankruptcy trustee, who is in charge of the realisation of the assets of the company and payment of the creditors' claims in accordance with their respective rank. In practice, the bankruptcy trustee has certain flexibility and may, for example, enter into settlement agreements and transactions on behalf of the insolvent estate, subject to court-approval. In this regard, if the bankruptcy trustee takes into account the impact of FinCo's insolvency on other group companies, and specifically on the OpCo's, he or she may take action to ensure, to some extent, business continuity, limiting the decrease of value and the social impact at the level of the OpCos. In addition, thereto, it is important to stress the fact that in the case of bankruptcy of companies which are part of an international group of companies, the courts usually appoint bankruptcy trustees who have extensive experience in the handling of bankruptcy scenarios for this type of company. These experienced bankruptcy trustees understand complex group structures and, in discussions with all involved parties (creditors, management, court, etc.), may achieve solutions that mitigate the consequences of the opening of FinCo's insolvency proceedings.

5. Upstream / downstream guarantees for obligations of FinCo

5.1 Introduction

In our case study, we assume a common guarantee structure, see below.



5.2 The Netherlands

For a group restructuring to succeed, any restructuring proposal will likely need to reflect the relative positions of the creditors under applicable law. (See also the *INSOL Statement of Principles for a Global Approach to Multi-creditor Workouts*.) In situations involving a FinCo, the difficulty is that creditors of FinCo may be looking at a very different outcome than creditors of TopCo, even if they were intended to be *pari passu*. The credit position of FinCo may be much worse than that of TopCo if all proceeds were on-lent by FinCo to TopCo and subordinated entities, but it may be much better if the proceeds were loaned forward directly into the (more creditworthy) OpCos. See our example below.

The FinCo-creditors will likely take the position that they should be treated as creditors of the group rather than only of FinCo ("substantive consolidation") or, if that would give them a better recovery position, as creditors with a preferred position exactly because they are creditors of FinCo. Under current Dutch law, there is no legal basis for substantive consolidation although there are examples of restructuring agreements where creditor groups have tried to achieve the same consensually through turn-over and equalisation agreements.

This restructuring hurdle, created by not issuing all debt by the same legal entity and under the same applicable law, is supplemented by what has become known as "double dipping" by creditors. Double-dipping often occurs when a noteholder, whose claim is restructured at FinCo level, seeks recourse against TopCo's assets based on the guarantee provided by TopCo for FinCo's debt. Relative to other group or TopCo creditors, who may view their position as *pari passu* to those of FinCo, as long as the FinCo creditor has not been fully paid, the FinCo creditor does not only have a potentially better claim on FinCo, but can effectively make two claims against the group's assets: one via FinCo and one directly towards the guarantors. Therefore, it is useful to restructure both the debt and the guarantee at the same time and, preferably, in the same restructuring plan.

Double-dipping in relation to SPVs is a top priority in (cross-border) restructuring matters in the Netherlands. The aforementioned decision of the US Bankruptcy Court of 4 December 2017 (*Re Oi Brasil Holdings Coöperatief UA*: paragraph 4.1) illustrates how far a bondholder was willing to go for double-dipping. In its decision, the court spent considerable time commenting on a hedge fund's investment strategy aimed at making a profit through double-dipping.

The fund held notes issued by a Dutch SPV and guaranteed by the group's parent, which itself (together with other group companies, including the Dutch SPV) was being restructured in Brazil. The hedge fund's strategy was to advocate strict corporate separateness of the SPV and its parent, separation of proceedings and enforcement of intercompany claims, which would give the fund two paths for recovery (a double dip). This strategy was at risk when the group sought substantive consolidation of the group's debtors and elimination of intercompany claims in the Brazilian insolvency proceedings and subsequently filed for recognition of the Brazilian insolvency proceedings as main proceedings under US Chapter 15. That prompted the fund to try and prevent the group's plan from succeeding. It motivated the administrator of the Dutch SPV to move out of suspension of payments into a (for restructuring purposes, unhelpful) bankruptcy, went through several rounds of litigations, and as trustee – unsuccessfully (prevented by the US Bankruptcy Court) – tried to disrupt the Chapter 15 recognition proceedings on that basis, with, of course, detrimental effects for the wider group and its creditors.

Even though the Dutch trustee and the hedge fund were not entirely successful in the US Bankruptcy Court, it does show that a noteholder can attach such importance to double-dipping that it is willing to set up a comprehensive and costly strategy to preserve the possibility of double-dipping. That may, as in this case, come at great cost for both the debtor and the other creditors as it will draw on the timelines, even when unsuccessful.

Claims governed by Dutch law can be addressed in a number of ways regardless of whether they are principal claims or guarantee claims. An extrajudicial option is consensual restructuring pursuant to the terms of the debt document or pursuant to a consecutive agreement. Save for general legal principles, such as public order and public morality, parties are free to conclude any contract. This enables parties to restructure a guarantee along with the secured claim in any way they can agree on.

A non-cooperative creditor is an obvious obstacle in a consensual restructuring. Under current legislation, a non-consenting creditor can only be legally forced into a restructuring plan if his or her perseverance to receive full payment, resulting in a refusal of the restructuring plan, constitutes an abuse of power. This does not often occur.

Pending legislation – the aforementioned CERP – will increase the possibility of extrajudicial restructuring considerably. After the implementation of CERP, the legal framework will allow a debtor to propose a restructuring plan to its creditors. Once the plan is approved by at least one class of affected creditors, the debtor can request the court to declare the plan binding on all creditors. A very welcome feature of CERP is the option to include guarantees issued by other group companies in the restructuring plan of the Dutch entity, provided that certain conditions are met. Furthermore, CERP allows for the amendment or termination of contracts that are onerous for the debtor.

Under CERP, the FinCo-restructuring can include the guarantee provided by TopCo to FinCo's noteholders. This is a very effective measure to prevent the noteholders from interfering with the group restructuring by double-dipping. Also, the indenture or other documentation providing for the guarantee, irrespective of its governing law and

majority vote requirements, can be amended. That removes a future risk of double-dipping and thereby making the group and its financing future-proof.

Another route to a court-approved restructuring plan is through a suspension of payments. These proceedings are not particularly suitable for the restructuring of guarantees issued by third parties, but they can nevertheless be very helpful in a group restructuring. If used well, in particular the ability to request the court to order so-called *specific measures helpful for the restructuring,* they allow for the Dutch restructuring efforts to be aligned with the other proceedings in the home jurisdiction of TopCo and the OpCos.

A suspension of payments proceeding in respect of a Dutch FinCo can offer support to cross-border restructurings. The following examples are taken from recent case law and include:

i) tailoring the timetable of the Dutch proceedings to the foreign proceedings;[23]

ii) applying technical aspects of the foreign proceedings to the Dutch proceedings, i.e. voting procedures, position of registered holders versus beneficial creditors, and contractual provisions;[24]

iii) approval by the Dutch court of a non-European Insolvency Regulation ("EIR") restructuring agreement, making it binding on all creditors and providing it with automatic recognition under the European Insolvency Regulation Recast ("EIR Recast") for the Dutch SPV;[25] and

iv) changing an indenture, governed by US federal law, with smaller majorities than contractually intended.[26]

Note: as long as the English courts adhere to the so-called Gibbs rule, an amendment by a non-English instrument of English law governing obligations remains difficult to achieve and may need proper consent if the debtor has assets in England.[27]

On the flip side, pending the introduction of CERP, the current suspension of payments has as the main drawbacks that: (i) it affects only the unsecured creditors and provides no tools to also bind secured creditors; and (ii) it is a public proceeding, which may lead to negative publicity and it becoming a self-fulfilling prophecy.

5.3 Ireland

The extent of the ability of a noteholder, whose main agreement is with FinCo, to double dip into the assets of TopCo as guarantor depends on a number of issues under Irish law.

i) First are the terms of the guarantee agreement. Where an insolvency process is initiated in another jurisdiction than the Irish jurisdiction, the noteholder will

[23] *UPC* (Dutch Supreme Court 26 August 2013, ECLI:NL:HR:2003:AI0369), *Isolux* (District Court of Amsterdam 21 September 2016, unpublished), *PTIF/Oi* (Dutch Supreme Court 7 July 2017, ECLI:NL:HR:2017:1280).

[24] *UPC* (n 21); *Plaza Centers* (District Court of Amsterdam 9 May 2014, published on www.plazacenters.com); *Isolux* (n 21) and *PTIF/Oi* (n 21).

[25] *UPC* (n 21); *Plaza Centers* (n 22); *Isolux* (n 21); and *PTIF/Oi* (n 21)).

[26] Deviating from US Court of Appeals for the Second Circuit of 17 January 2017 (*Marblegate Asset Management LLC v Education Management Finance Corp*, Case No 15-2124-cv(L)).

[27] The Gibbs Rule is a general proposition that a debt instrument governed by English law cannot be discharged or compromised in a foreign insolvency proceeding. The rule is derived from *Anthony Gibbs Sons v La Societe Industrielle et Commerciale des Metaux* (1890) 25 QBD 399.

be paid in accordance with the formal legal framework pertaining in that jurisdiction. The first question will be whether the agreement between the noteholder and FinCo is governed by Irish law and, if so, if the jurisdiction where the insolvency process is initiated recognises the guarantee, which effectively allows for double-dipping. In this way, the noteholder's ability to double-dip against a guarantor (TopCo) is entirely dependent on the terms of the guarantee agreement and the jurisdictional rules surrounding TopCo.

ii) Second is the nature of the insolvency proceeding which emerges. If FinCo becomes subject to the abovementioned Examinership, the noteholder may withhold consent to the restructuring. However, the Examinership process and final compromise may proceed without the noteholder's consent if there is an agreement from other creditors. This is due to the aforementioned cross class cram-down provisions. This means that, unlike the current position in Dutch law as described in section 5.2, a creditor cannot persevere in the attempt to achieve full payment as the Examinership provides for a cram-down in a judicially monitored setting.[28] However, although it is possible, whether the Examinership would succeed in the context of imposing a cram-down on a secured noteholder is ultimately a matter for the court when it finally approves the compromise. It is also possible that the noteholder agrees to the restructuring plan and accepts a haircut, which may or may not be cognisant of double-dipping possibilities. In this latter scenario, the terms of the guarantee will normally address the compromising of the debt. So, where FinCo's noteholder obtains a guarantee from TopCo, the terms of the guarantee may provide that the guarantee alters once a debt is compromised in a formal restructuring process. Alternatively, the terms of the guarantee may provide complete cover or insurance even where a compromise is reached under a restructuring process. This would allow the noteholder of FinCo to accept a compromise in Ireland but allow recourse in TopCo's home jurisdiction under the guarantee. However, alteration of the guarantee is also possible under the Examinership compromise. These are but two possible scenarios which might be addressed in a guarantee agreement, for instance providing that the guarantee relates only to the frontline debt and, in the case of a compromise, relates only to the amount of the compromised debt.

Of unexpected and untested relevance are some additional provisions of the Irish Companies Act 2014. These provisions allow for "pooling" or "contribution" orders between companies in insolvency proceedings and "related" companies. If the related companies are incorporated outside the jurisdiction of the insolvent company, the effect of any order will depend on the jurisdictional reach of the provisions. As the provisions have been untested to date, little is known about their effect. The provisions are based on similar ones in New Zealand,[29] as described in a recent Company Law Review Group Report.[30] Under these provisions, the court is provided with a number of criteria to establish whether there is a sufficient managerial and financial connection between companies in a group. Where these criteria are satisfied, the court can potentially order a contribution from one company to another to satisfy creditors of the first company. There are no reported cases on these provisions and their operation in Ireland.

[28] The Dutch CERP proposal may change this as it will provide for restructuring plans various tools including cram-down provisions similar to the Irish legal framework.
[29] *Re Lewis Holdings Ltd v Steel & Tube Holdings Ltd* [2015] NZCCLR 5.
[30] See Company Law Review Group (n 11 above).

5.4 Luxembourg

The guarantee structure, described in section 5.1, contemplates both upstream and downstream guarantees, although the latter are more frequent in practice.

In relation to upstream guarantees, it has to be noted that noteholders of FinCo willing to enforce such guarantees could face some difficulties under Luxembourg law in the event that the upstream guarantee does not, among other things, meet the corporate interest test for the OpCo providing the guarantee. This test can either be applied on a standalone basis or at a group level. The test will pass on a standalone basis if the OpCo has a direct benefit in granting the upstream guarantee because of, for example, a guarantee fee received as consideration. At group level, Luxembourg law relies on criteria set out by a French court precedent. In order to fulfil this test at the group level and thus permit noteholders to enforce the guarantee given by the OpCo, the conditions listed in section 3.4 have to be satisfied, namely: existence of a structured group; existence of an overall group policy; appropriate consideration given; and that the obligations by the OpCo either do not exceed its assets or put it at risk of becoming insolvent. The potential consequences of the absence of corporate interest in providing upstream guarantees is discussed in legal doctrine. While some authors express the view that a lack of corporate interest could only give rise to liability of the directors of the relevant company (OpCo), others consider as a consequence that the relevant obligations would be null and void if the contractual counterparty (FinCo) knew or should have known, in light of the circumstances, of the absence of corporate benefit for the OpCo.

The analysis is different with respect to downstream guarantees. In the event of FinCo being unable to repay its debt to the noteholders, the noteholders can effectively make two claims against the group's assets. One claim may be made as part of the insolvency proceedings opened against FinCo whereby the noteholders will declare their claims to the bankruptcy trustee for the principal amount and any other outstanding amount due to them. In addition thereto, the noteholders will have a strong interest in enforcing the guarantee granted by TopCo, if their claim is not, or not fully, covered by the assets of the bankruptcy estate or an enforceable security right.[31] The claim against TopCo is the second claim the noteholders can pursue, provided the conditions of enforcement of the guarantee are satisfied (for example, because of an event of default under the notes). That being said, it is important to stress that the noteholders will not be entitled to recover their claims twice and thus obtain an amount that exceeds their principal claim, as well as any other amounts due (such as interest or enforcement costs). The noteholders may bring the two claims at the same time – subject to the fulfilment of the enforcement conditions under the guarantee – but, once they have recovered the full amount due to them either from the insolvency estate or from TopCo through the guarantee, their claim based on the notes is considered fully paid and is extinguished.

In Luxembourg, most of the restructuring proceedings take the form of a bankruptcy proceeding.[32] Even though a consensual restructuring is possible, it is uncommon. If a consensual restructuring is contemplated and there is a non-cooperative creditor, this creditor cannot be forced to accept the restructuring plan. However, as discussed in section 4.4, a new Bill is currently being discussed in Luxembourg, which should, among others measures, introduce more effective restructuring mechanisms.

[31] The beneficiaries of securities granted pursuant to the Luxembourg Law of 5 August 2005 on financial collateral arrangements are treated differently from other secured creditors, i.e. with an enforcement procedure which is more favourable. However, collateral securities are not discussed in this report and references to secured creditors are thus meant to include only beneficiaries of personal guarantees.

[32] The use of another type of proceeding is extremely rare (see section 4.4).

6. Recognition

6.1 The Netherlands

According to Dutch private international law, foreign insolvency proceedings are not recognised in the Netherlands (according to the principle of territoriality). For example, a general seizure of assets pursuant to foreign insolvency proceedings does not affect the debtor's assets located in the Netherlands. Creditors (domestic and foreign alike) remain able to seize assets in the Netherlands. Foreign insolvency proceedings opened in an EU Member State (with the exception of Denmark) are, however, automatically recognised under the EIR Recast. Insolvency proceedings opened in the Netherlands are deemed to cover all assets of the insolvent entity regardless of their location (the principle of universality).[33]

As other jurisdictions generally apply the same principles as the Netherlands, a somewhat ambivalent approach is required for cross-border group restructurings. First, they require an entity-by-entity approach. Second, in case an entity has assets in multiple jurisdictions, it can be beneficial to file for insolvency proceedings in some or all of those jurisdictions in order to cover all the assets.

Under current legislation, the most effective option for a group restructuring is a suspension of payments, since it provides for an option to have a restructuring plan approved by a court, making it binding on all unsecured creditors. On top of that, under the EIR Recast, suspension of payments proceedings opened in the Netherlands are automatically recognised as insolvency proceedings across the EU and may lead to an EU-wide stay. This enables FinCo to restructure its full EU debt through only one insolvency procedure, rather than insolvency proceedings in multiple jurisdictions. Furthermore, there are examples of the court-approved suspension of payment restructuring plan, as the result of foreign main insolvency proceedings, being recognised in the US under Chapter 15 of the US Bankruptcy Code or its predecessor, Article 304.[34] After US recognition, an automatic stay goes into effect with regard to FinCo's assets in the US.

Another option for FinCo is to simultaneously file for a suspension of payments in the Netherlands and Chapter 11 in the US. The Chapter 11 filing will lead to an automatic stay on all the FinCo's assets, regardless of which jurisdiction these assets are located. Because of the US contempt of court legislation, this worldwide stay is likely to sort out practical (if not legal) effects in most jurisdictions.

As mentioned in section 5.2, the pending legislative proposal for CERP will make restructuring of debt at FinCo and group level even more effective. CERP will allow for a cram-down class constitution and will allow guarantees to be included in the restructuring plan, which can be declared binding by the court as soon as at least one class of creditor has approved the plan. With CERP in its public variant being added to Annex A of the EIR Recast, a restructuring plan in accordance with CERP will be automatically recognised throughout the EU.[35]

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[33] The different inbound (territoriality) and outbound (universality) approach under Dutch law caused confusion when, in a recent judgment, the District Court of Noord-Holland, the Netherlands, declared the Indian airline Jet Airways (India) Ltd. bankrupt, assuming jurisdiction because of its Dutch representative office (ECLI:NL:RBNHO:2019:5425 Rechtbank Noord-Holland, 21-05-2019, C/15/288017 / FT RK 19/540). The Dutch trustee, working under order of the Dutch court and abiding by Dutch bankruptcy law, had to take the view that his mandate extended to all assets and liabilities of the company, even though he was refused access to the premises and records of Jet Airways, which did not recognise his standing (although a cooperation protocol was written up in a later stage and approved by the Indian and Dutch courts).

[34] See *UPC* and *Isolux* (n 21).

[35] While the imminent introduction of CERP is a major development that impacts much of what is written here, it goes beyond the scope of this report to elaborate. We refer to the detailed introduction to CERP, in INSOL

6.2 Ireland

The general rules described above apply in Ireland as well. At this point, it is important to bear in mind that there are two restructuring processes available under Irish law. The first is an Examinership, which is covered by the EIR Recast.

This is currently included in Annex A of the EIR which means that, at the end of the restructuring process, the final compromise or settlement, (which is also called a scheme) is approved by a court order. Because the Examinership is a listed process, the order of court will be automatically recognised throughout the EU. This is obviously advantageous. At the same time, however, because the Examinership process is listed in the EIR, the initial question of jurisdiction will be determined by the COMI question, and therefore it is rarely the case that non-Irish companies have availed themselves of Examinership as a restructuring process because this strategy would be reliant on a successful COMI shift. Similarly, the EIR Recast will provide for the recognition of Member State insolvency processes in Ireland where these are listed. The second restructuring process is essentially the same as the English scheme of arrangement and is not covered by the EIR Recast.[36]

Where the EIR Recast does not apply, Irish law provides for the recognition of foreign insolvency procedures in the following two ways. Please note that no distinction is made regarding the domicile of the creditors affected by the foreign insolvency in question.

i) Under section 1417 of the Companies Act 2014, the Minister for Jobs, Enterprise and Innovation can give an order that makes liquidation orders issued by a court in a particular jurisdiction, where the EIR Recast does not apply, enforceable and recognised in Ireland. Currently, no countries have been recognised by ministerial order for the purposes of section 1417. The UK was recognised under a previous version of this provision until this was no longer necessary following the enactment of the first EIR 1346/2000.

ii) According to common law rules of private international law, Irish courts have an inherent power to make an order in aid of insolvency proceedings in other jurisdictions recognised.[37] The position of non-EU Member States and Denmark are governed by these common law principles.

There is some discussion at present of introducing a model law based on the UNCITRAL model law in relation to recognition of non-EU insolvency processes.

6.3 Luxembourg

As Luxembourg is party to the EIR Recast, the advantage of automatic recognition of insolvency proceedings opened in Luxembourg applies in the same way as described for the Netherlands in section 6.1.

Insolvency proceedings that are not governed by the EIR Recast are governed by Luxembourg's private international law principles. These rules ensue from Luxembourg case law and are based on the principle of universality, as opposed to the principle of territoriality that is applied in other countries. As a result, any foreign

World Q3 2019, available at: https://lxpfk4cwk12voofpqrz5sbwj-wpengine.netdna-ssl.com/wp-content/uploads/2017/06/INSOL-WTQ-2019-SRK.pdf.

[36] See further Irene Lynch Fannon, 'Insolvency and rescue' in Thomas B. Courtney, Lyndon Mac Cann, Irene Lynch Fannon, William Johnston, Daibhi O'Leary and Nessa Cahill (eds), *Bloomsbury Professional's Guide to the Companies Act 2014* (Bloomsbury 2015). Leary *Mount Capital Fund Ltd* [2012] 2 IR 486.

decision may immediately be enforced, without any exequatur measures, regarding the divestiture of the management and, in general, the legal capacity of the insolvent company, i.e. the recognition of the authority of the insolvency receiver. The execution of any enforcement measures in Luxembourg against the assets of the debtor will, however, require that the relevant foreign decision goes through an exequatur process, including, amongst others, a verification that the decision complies with Luxembourg public order standards.

7. Conclusions

Each year internationally oriented companies increase the use of foreign-domiciled SPVs. While as a going concern, the applicability of foreign laws and practices to those SPVs is hardly noted by management and advisors to the company, they become very important in restructuring: not only in implementation, but perhaps even more importantly in the run-up to a restructuring and while optionality between restructuring options still exists.

In this report, we have tried to illustrate a number of considerations typically arising when SPVs in the Netherlands, Luxembourg and Ireland are present in the to-be restructured group. We identified four key considerations which played a significant role in many recent cross-border restructurings:

i) deviating fiduciary duties for the board of FinCo and the understandable lack of focus thereon, with potential risks of director liability;

ii) the risk that board duties and creditor recourse positions at FinCo level have a disproportionate likelihood of disrupting a global restructuring;

iii) the key role of upstream and downstream guarantees and the ability or inability to pick them up as part of the main restructuring plan; and

iv) recognition of restructuring results.

In describing these considerations, we sought to achieve a balance between an introduction to the relevant topics on the one hand, and sufficient detail to serve as a first point of reference in practice on the other. This report is by no means comprehensive, and many more considerations will play a role, but, in an effort to improve the quality and chance of success of restructuring plans, we hope to have contributed to awareness and an earlier consideration of the potential pitfalls.

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