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STUDENT PAPER

Crises, Creditors and Cramdowns: An evaluation of the protection of minority creditors under the WHOA in light of Directive (EU) 2019/1023

Hidde Volberda*

Covid-19 has severe economic consequences, leading to an increasing amount of businesses facing overwhelming debts. Since the financial crisis of 2008 the European Union has taken on a more rescue-oriented approach towards bankruptcy, resulting in Directive (EU) 2019/1023. This Directive creates a framework for pre-insolvency restructuring, thereby avoiding unnecessary bankruptcies. Accordingly, pre-insolvency restructuring is a valuable instrument in mitigating the negative economic effects of Covid-19. The Netherlands has recently adopted the Act on the Confirmation of Private Plans (WHOA), National Legislation on pre-insolvency restructuring. In order to balance the rights of secured and unsecured creditors the 20%-rule was adopted. This rule guarantees small-scale Small-to-Midsized (SME)-creditors the right to satisfaction of 20% of their claims in restructuring proceedings. In this paper, I evaluate whether the 20%-rule is in accordance with the Directive. I argue that the 20%-rule is in line with the Directive, but that the overly restrictive system of judicial review under the WHOA hampers its application in practice. Therefore, the Dutch legislator should allow for more room for judicial interpretation on the suitability of the application of the 20%-rule. This more nuanced approach better aligns the 20%-rule with the European Restructuring Directive.

Keywords: Restructuring Directive; WHOA; SMEs; insolvency; corporate rescue; Covid-19

1. Introduction

1.1. Covid-19 and the need for rescue-oriented bankruptcy law

1.1.1. The economic fallout of the Covid-19 pandemic

The Covid-19 pandemic has greatly affected daily life in Europe. The intense lockdown measures, taken by governments all across Europe to combat the spread of the Covid-19 virus, have had severe economic consequences.[1] With many businesses forced to close down temporarily or to operate on a far more limited scale, business revenue has dwindled since the start of the crisis in March 2020.[2] During the first year of the pandemic, the amount of corporate insolvencies did not increase due to governmental support for struggling businesses.[3] However, corporate insolvencies are expected to rise by 26% in 2021, with governments slowly

* Master student, Legal Research Master UU, NL; email: h.w.volberda@students.uu.nl.
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[1] Stephen Madaus and F. Javier Arias, 'Emergency COVID-19 Legislation in the Area of Insolvency and Restructuring Law' (2020) 17 European Company and Financial Law Review 318, 320. DOI: 10.1515/ecfr-2020-0018.

[2] Madaus and Arias (n 1) 320.

[3] Astradius Economic Research, '2021: A turn of the tide in Insolvencies' (March 2021), 4 <https://group.atradius.com/publications/economic-research/2021-a-turn-of-the-tide-in-insolvencies.html> accessed 6 September 2021.

phasing out their financial support measures.[4] Some authors even speak of a *bankruptcy epidemic,* on top of the Covid-19 pandemic.[5]

1.1.2. The role and use of corporate restructuring in times of crisis

In this harsh economic climate, adequate proceedings for pre-insolvency restructuring can be a structural response to mitigate the long-term negative effects of the Covid-19 crisis.[6] Restructuring proceedings enable a business that struggles financially to restructure before bankruptcy has become inevitable. This is economically beneficial, as the going-concern value of a financially distressed company is often higher than its liquidation value.[7] The liquidation value of a company is the value of a company when all of its assets are liquidated and sold in bankruptcy proceedings.[8] The going-concern value is the value of a company when it can be either preserved and restructured or sold with its current business structure.[9] Restructuring agreements can be used to preserve viable businesses, retaining their going concern value and avoiding bankruptcy liquidation. This, in turn, leads to the prevention of job and value loss.[10] Hence, effective restructuring proceedings can enhance the economic resilience of the European Union during the aftermath of the Covid-19 pandemic.[11]

1.1.3. Bankruptcy reforms in Europe and the Netherlands

The process of reforming European bankruptcy law was instigated by another crisis. After the financial crisis of 2008, there was a need for a more effective system of pre-insolvency restructuring in the European Union.[12] To attain this goal, the European Commission adopted Directive (EU) 2019/1023 (the Directive).[13] This need was similarly felt by the Dutch government, that started reforming its pre-insolvency legislation in 2012.[14] The economic fallout caused by the Covid-19 pandemic has made the need for a rescue-oriented system of pre-insolvency restructuring even more pressing.[15]

After a great number of insolvency practitioners and scholars urged the Dutch Parliament to adopt the Act on the Confirmation of Private Plans (*Wet Homologatie Onderhands Akkoord, WHOA*),[16] the Dutch House of Representatives adopted the law on 26 May 2020.[17] Subsequently, the Dutch First Chamber of Parliament adopted the law on 6 October 2020.[18] On the day of its adaptation, Sander Dekker, the Dutch minister for Legal Protection, emphasised that the WHOA could prove useful in preventing insolvencies of businesses that have struggled due to the Covid-crisis.[19] Initially, there was some uncertainty on whether the WHOA

[4] Astradius Economic Research (n 3), 1–4.

[5] Madaus and Arias (n 1) 321.

[6] Maaike van der Zee and Benjamin Gideonse. 'Het belang van klassenindeling onder de WHOA' (2021) 29 Onderneming en Financiering 34, 34.

[7] Gerard McCormack, 'Corporate Restructuring Law – A Second Chance for Europe?' (2017) 42 European Law Review 532, 542.

[8] Daoning Zhang 'Preventive Restructuring Frameworks: A Possible Solution for Financially Distressed Multinational Corporate Groups' (2019) 20 European Business Organization Law Review 285, 286. DOI: 10.1007/s40804-018-0125-3.290.

[9] Zhang (n 8) 289.

[10] Vanessa Finch, *Corporate Insolvency Law: Perspectives and Principles* (Cambridge University Press 2002), 246. DOI: 10.1017/CBO9781139164283.

[11] See: Garrido and others, 'Restructuring and Insolvency in Europe: Policy Options in the Implementation of the EU Directive' IMF Working Papers 21/152, 5. <https://www.imf.org/en/Publications/WP/Issues/2021/05/27/Restructuring-and-Insolvency-in-Europe-Policy-Options-in-the-Implementation-of-the-EU-50235> accessed 6 September 2021.

[12] Commission Staff Working Document Impact Assessment Accompanying the document Commission Recommendation on a new approach to business failure and insolvency (SWD/2014/62/final) 184; Kamerstukken II 2018–2019, 35249, no. 3 (Explanatory Memorandum to the WHOA), 1–4.

[13] Council Directive (EU) 2019/1023 of 20 June 2019 on restructuring and insolvency [2019] OJ L172/18. In subsequent footnotes referred to as: Directive (EU) 2019/1023.

[14] Explanatory Memorandum to the WHOA (n 13) 3.

[15] Anne Mennens and Jessie Pool 'Flattening the insolvency curve. Het voorkomen van onnodige coronafaillissementen door wijziging van insolventierecht?' [2020] (22) Tijdschrift voor Insolventierecht 135, 146.

[16] Ruud Hermans 'Insolventiejuristen Roepen Politiek op tot Onmiddellijke Invoering WHOA' (*NJB Blog*, 18 March 2020) <https://www.njb.nl/blogs/insolventiejuristen-roepen-politiek-op-tot-onmiddellijke-invoering-whoa/> accessed 27 August 2021.

[17] Maarten van Poll, 'Kamer neemt Wet aan die Faillissementen moet Helpen Voorkomen' Financieel Dagblad (26 May 2020).

[18] 'Wet Homologatie Onderhands Akkoord 35249' (*Eerste Kamer*) <https://www.eerstekamer.nl/wetsvoorstel/35249_wet_homologatie_onderhands> accessed 6 September 2021.

[19] Rijksoverheid, 'Nieuwe wet helpt faillissementen te voorkomen' (*Rijksoverheid.nl 6 October 2020*) <https://www.rijksoverheid.nl/actueel/nieuws/2020/10/06/nieuwe-wet-helpt-faillissementen-te-voorkomen> accessed 6 September 2021.

would be the official transposition of the Directive in the Netherlands.[20] However, in the legislative proposal submitted for the implementation of the Restructuring Directive in the Netherlands, it is proposed that the WHOA will function as the transposition of the Restructuring Directive.[21] Thus, if this law is adopted, the system of restructuring as laid down in the WHOA should be consistent with the Directive and all measures laid down therein should be implemented in the Netherlands.

1.2. Protection of SME-creditors in restructuring proceedings

While the WHOA is aimed at strengthening the Dutch economy, concerns have been raised regarding the protection of minority unsecured creditors under this new system.[22] Some fear that the newly adopted law favours big corporations at the expense of small businesses.[23] The stark contrast between the interests of secured creditors and shareholders on the one side, and small unsecured creditors on the other side, is a broader societal issue, transcending the borders of the Netherlands. Therefore, the Dutch legislator adopted the 20%-rule, an amendment intending to enhance the position of Small and Midsized Enterprises (SMEs) in restructuring proceedings.[24] The 20%-rule provides small-scale SMEs, in their capacity as creditors (hereinafter: 'SME-creditors') with the right to a reimbursement of 20% of their claims in case a court imposes a restructuring agreement on the class of creditors they belong to (this situation is referred to as a cross-class cramdown).[25] Small-scale SMEs are businesses with a maximum of 50 employees or a total yearly revenue of at most 12 million euros.[26] The 20%-rule only affects small-scale companies, thus excluding midsized enterprises. Throughout this article, the term 'small-scale SME-creditors' will be used to refer to SMEs as creditors in restructuring or insolvency proceedings. For the sake of clarity, it must be emphasised that, in this context, 'small-scale' refers to the size of these companies, not (to the size) of their claims in restructuring or insolvency proceedings. Especially amidst the Covid-crisis, it is relevant to assess whether the Dutch WHOA and the Restructuring Directive offer adequate protection to small-scale SME-creditors, as this type of enterprises are the most vulnerable in times of crisis.[27]

This article will analyse and compare national legislation and Union law. The Directive provides the relevant benchmarks to assess whether the 20%-rule is compatible with the European framework for pre-insolvency restructuring. On the basis of this analysis I will then address whether changes to the 20%-rule are necessary in order to fit the European Restructuring Directive.

This leads to the following research question: *does the WHOA's 20%-rule fit the system of pre-insolvency restructuring as laid down in Directive (EU) 2019/1023 and are adjustments to the 20%- rule necessary?*

To answer this question, I will first give a brief overview of the legislative history and aims of the Directive. Following this, I will describe the system of pre-insolvency restructuring that it lays down, paying special attention to the cross-class cramdown. Subsequently, I will address the system of pre-insolvency restructuring as implemented by the WHOA, focussing on the provisions intended to protect minority creditors. Thereafter, I will turn to the evaluative part of this paper. In this evaluation, I will specifically assess whether the 20%-rule meets the conditions necessary to justify a derogation from the rules on a cross-class cramdown, as laid down in Article 11 of the Directive. I argue that the 20%-rule does, in fact, fit the system of pre-insolvency restructuring as laid down by the Directive, but that its application can prove to be problematic in practice. This problem can be overcome by adjusting the current system for judicial review of the applicability of the 20%-rule.

[20] Kamerstukken II 2017-2018, 35249 no. 18; Explanatory Memorandum to the WHOA (n 12) 4. See also: MR Schreurs, 'Implementatie van de Herstructureringsrichtlijn: Wellicht Beter in de Surseance dan in de WHOA?' [2019] (33) Tijdschrift voor Insolventierecht 244.

[21] Ontwerp Memorie van Toelichting Wetsvoorstel Implementatiewet Richtlijn Herstructurering en Insolventie, 2. The document can be found at< https://www.internetconsultatie.nl/herstructurering> accessed 6 September 2021.

[22] Wiepke Bartstra, Aart Jonkers and Rolef de Weijs, 'Nieuwe Wet in Faillissementsrecht Benadeelt Vooral Kleine Ondernemingen' *Financieel Dagblad* 14 January 2020.

[23] Tom Jan Meus, 'Hoe een advocatenlobby in coronatijd de Kamer letterlijk de wet voorschreef' *Nieuw Rotterdamse Courant* (12 June 2020).

[24] Dutch Bankruptcy Act (DBA), art 384(4)(a).

[25] Kamerstukken II 2019-2020, 35 249 no. 25.

[26] On the basis of art 374(2) DBA and art 3:95a and 3:96 Dutch Civil Code (DCC).

[27] Kamerstukken II 2019-2020, 32637 no. 430 7–8.

2. Directive (EU) 2019/1023

2.1. The influence of the financial crisis on European insolvency law

Historically, the European approach to insolvency law was harsh and inflexible, stemming from long-held cultural beliefs, associating bankruptcy with failure.[28] This resulted in equally harsh insolvency legislation, focussing on liquidation rather than corporate restructuring.[29] However, the European approach to insolvency law has shifted towards a more rescue-oriented approach since the start of the millennium.[30] This process accelerated in 2014 when the European Commission noted that the Union was facing 'the biggest crisis in its history.'[31] The harsh and inflexible insolvency regimes of the Member States were a major reason for the slow economic recovery.[32] As such, the Union was in need of more flexible insolvency regimes aimed at restructuring instead of liquidation.[33] To this end the Commission proposed the Recommendation on a New Approach to Business Failure and Insolvency.[34]

In 2016 the European Commission found that the Member States' efforts to implement the recommended measures were rather lacklustre.[35] Thus, the Commission decided to turn the recommendation into binding legislation and proposed Directive (EU) 2019/1023. This Directive is a minimum harmonisation tool.[36] The system of pre-insolvency restructuring as laid down by the Directive is modelled upon, and for a large part resembles, the successful American Chapter 11 procedure.[37]

The aim of the Directive is most clearly stated in its first recital. The Directive aims to harmonise the insolvency and restructuring laws of the Member States, in order to remove the obstacles to the functioning of the internal market and the exercise of fundamental freedoms, that arise because of the divergence of laws on this matter. Furthermore, effective restructuring proceedings contribute to the prevention of both unnecessary insolvencies and job loss.[38]

2.2. Pre-insolvency restructuring under the Directive

2.2.1. Key features of the restructuring agreement

The basic idea for pre-insolvency restructuring is the negotiation of a restructuring plan between a debtor and his creditors and shareholders. The debtor presents a plan to restructure his business or his assets, in order to continue his activities and avoid liquidation.[39] Restructuring plans can contain a wide array of measures, as their content is not predefined by the Directive.[40]

In principle, the restructuring plan should be agreed upon unanimously by the affected parties. However, under certain conditions it is possible that the plan gets confirmed by a court and becomes binding even for dissenting parties.[41] Lastly, during the negotiations on the restructuring plan creditors cannot enforce their individual actions against the debtor.[42] This is referred to as the period of the stay.[43]

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[28] Nathalie Martin, 'The Role Of Culture and History In Developing Bankruptcy and Restructuring Law: The Perils Of Legal Transplantation' (2005) 28 Boston College International & Comparative Law Review 1, 51.

[29] Martin (n 28) 51.

[30] Gerard McCormack, Andrew Keay and Sarah Brown, *European Insolvency Law: Reform and Harmonization* (Edward Elgar Publishing 2017), 230. DOI: 10.4337/9781786433312.

[31] SWD(2014)/62/final (n 12) 2.

[32] SWD(2014)/62/final (n 12) 2.

[33] SWD(2014)/62/final (n 12) 2.

[34] Commission Recommendation 2014/135/EU of 12 March 2014 on a new approach to business failure and insolvency [2014] OJ L74/65.

[35] Proposal for a Directive Of The European Parliament And Of The Council on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures and amending Directive 2012/30/EU (COM/2016/SWD/723/final) 8.

[36] Nicolaes Tollenaar, 'The European Commission's Proposal for a Directive on Preventive Restructuring Proceedings' (2017) 30 Insolvency Intelligence 65, 66.

[37] McCormack, Keay and Brown (n 30) 227.

[38] Directive (EU) 2019/1023, 2nd recital.

[39] Horst Eidenmüller, 'Contracting for a European Insolvency Regime' (2017) 18 European Business Organization Law Review 273, 279. DOI: 10.1007/s40804-017-0067-1.

[40] ibid.

[41] Tollenaar, 'The European Commission's Proposal' (n 36) 66.

[42] Bob Wessels, On the genesis of the Proposal for a Restructuring Directive (2017) 1 Nederlands Tijdschrift voor Handelsrecht 13, 16.

[43] Irit Mevorach and Adrian Walters, 'The Characterization of Pre-insolvency Proceedings in Private International Law', (2020) European Business and Organization Law Review 1, 2. DOI: 10.1007/s40804-020-00176-x.

2.2.2. Voting and classes

Affected parties have the possibility to vote on the restructuring plan. This occurs in classes of creditors.[44] Class division is based on the commonality of interest and claims of those grouped in the class and the level of seniority of their claims.[45] It is required that affected parties are divided into a least two classes, namely that of secured and that of unsecured creditors.[46] Furthermore, Article 9(4) last clause provides that Member States must take measures to ensure that the interest of vulnerable parties is protected in the class formation. In each class, a majority is reached when the majority of the amount of value in that class votes in favour of the restructuring plan.[47] It is possible that minority creditors *within a class* get bound to a restructuring plan by a majority vote. However, this is only possible if certain conditions are met.

2.2.3. Conditions for confirmation

In order for a restructuring plan to be confirmed by a judicial authority, it should first of all meet the procedural requirements laid down in Article 9 of the Directive.[48] These relate to the voting procedures and class formation, as discussed in the previous section. Furthermore, the restructuring plan should meet two substantive requirements.

The first requirement is the feasibility test, laid down in Article 10(3) of the Directive. This article holds that judicial authorities shall not approve restructuring plans that do not reasonably contribute to the avoidance of insolvency and continuation of the business of the debtor.[49]

The second requirement is the creditors' best interest test, laid down in Article 10(2)(d) and Article 2(6) of the Directive. In order for this test to be fulfilled, none of the dissenting creditors should be worse off in the situation in which the restructuring plan is adopted, than in the situation of liquidation of the assets of the debtor.[50] To establish whether this test has been fulfilled, two factors need to be taken into account. First, the alternative scenario that determines the amount of payoff the dissenting creditor would get.[51] Second, the amount of payoff the dissenting creditor would get in this scenario.[52] Thus, the creditors' best interest test protects creditors from losing value that they would otherwise receive through liquidation of the company.[53]

2.3. The cross-class cramdown

2.3.1. General outline of the cross-class cramdown

The Directive deviates from the earlier Recommendation in one very important aspect, namely by obliging Member States to implement cross-class cramdown proceedings in their national system for pre-insolvency restructuring.[54] In case of a cross-class cramdown a court confirms a restructuring plan, which binds an entire dissenting class of creditors to the restructuring plan, instead of the dissenting creditors within a class.[55] A cross-class cramdown is possible in two scenarios. The first scenario is that in which the majority of voting classes votes in favour of the plan, on the condition that one of these classes is a class of secured creditors or is senior to the ordinary unsecured creditor class.[56] The second scenario is that in which at least one class of the affected parties votes in favour of the restructuring plan, provided that this class would receive payment under the normal ranking of priority under applicable national law.[57]

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[44] Directive (EU) 2019/1023, art 9(4).

[45] McCormack (n 7) 551.

[46] Directive (EU) 2019/1023, art 9(4).

[47] Directive (EU) 2019/1023, art 6.

[48] Directive (EU) 2019/102, art 10(2)(a).

[49] McCormack (n 8) 553.

[50] Directive (EU) 2019/1023, art 2(6).

[51] Stephan Madaus, 'Is the Relative Priority Rule right for your Jurisdiction: a Simple Guide to the Relative Priority Rule' (18 January 2020) WP, 2 <https://stephanmadaus.de/2020/01/20/a-simple-guide-to-the-relative-priority-rule/> accessed 6 September 2021.

[52] ibid.

[53] ibid 3.

[54] McCormack (n 7) 549.

[55] Alex Krohn, 'Rethinking Priority: The Dawn of the Relative Priority Rule and a New 'Best Interest of Creditors' Test in the European Union' (20 June 2020) WP, 2. DOI: 10.2139/ssrn.3554349 accessed 6 September 2021.

[56] Directive (EU) 2019/1023, art 11(1)(b)(i).

[57] Directive (EU) 2019/1023, art (11)(1)(b)(ii).

A cross-class cramdown might seem like a far-reaching infringement on the autonomy of the dissenting parties involved.[58] However, the possibility for a cross-class cramdown comes with several advantages. Without it, dissenting parties can adopt a holdout position, by blocking an otherwise reasonable restructuring plan. The possibility of a cross-class cramdown, however, forces creditors to cooperate and thus prevents parties from adopting a hold-out position.[59] In order to compensate for the infringement on contractual autonomy, the cross-class cramdown has to satisfy certain requirements.

First of all, a plan should meet all the requirements that apply to regular restructuring plans.[60] Thus, the procedural requirements of Article 9 should be satisfied together with the feasibility test and the creditors' best interest test. Furthermore, in order for the court to issue a cross-class cramdown it is necessary to determine how the value realised through the restructuring plan (reorganisation value) should be distributed amongst the stakeholders.[61] To reach a fair distribution Member States can implement either an absolute or a relative priority rule.[62] In this article I will mostly sidestep the widespread academic debate on whether absolute priority or relative priority is preferable, as the Dutch legislator has already implemented a form of conditional absolute priority in the WHOA.[63] Member States are allowed to introduce provisions that deviate from the procedure for a cross-class cramdown as laid down in Article 11 of the Directive, if these provisions meet two cumulative requirements.[64] I will return to this in Chapter 4.

3. The WHOA

3.1. Restructuring through the WHOA: core principles

3.1.1. The reorganisation agreement

The Netherlands is in the process of implementing Directive (EU) 2019/1023 in its national legislation and aims to do so through the WHOA.[65] The WHOA adds several articles to the Dutch Bankruptcy Act (DBA), thereby introducing the possibility for a court-confirmed pre-insolvency restructuring agreement, outside of bankruptcy or moratorium, in the Dutch legal order.[66] The core mechanism of restructuring under the WHOA is an agreement between the debtor and the parties involved, which can be confirmed by the court. There are no substantive requirements on the content of the restructuring plan, however employee rights may not be affected by it.[67] The plan does need to satisfy several procedural requirements, laid down in Article 375 of the DBA.[68]

3.1.2. Voting on the agreement

The affected parties can vote on the agreement, and to this object they are divided into different classes.[69] Class division is determined on the basis of a commonality of interest of the creditors in the class, as is prescribed by the Directive.[70] In order to bind dissenting parties, the agreement needs to be confirmed by the court, which is only possible if the requirements laid down in Article 384 DBA are satisfied.[71]

3.1.3. Confirmation by the court in case of a cramdown

If not all creditors within a class vote in favour of a restructuring plan, the court can confirm the agreement and make it binding for the dissenting creditors within that class.[72] Confirmation of an agreement is not

[58] Stephan Madaus, 'Leaving the Shadows of US Bankruptcy Law: A Proposal to Divide the Realms of Insolvency and Restructuring Law' (2018) 19 European Business and Organization Law Review 615, 637. DOI: 10.1007/s40804-018-0113-7.

[59] Krohn (n 55) 3.

[60] Directive (EU) 2019/1023, art (11)(1)(a).

[61] Madaus, 'Is the Relative Priority Rule right for your Jurisdiction' (n 51) 4.

[62] Directive (EU) 2019/1023, art 11(2), art 11(1)(c).

[63] Anne Mennens, *Het Dwangakkoord buiten surseance en faillissement, O&R 118* (Kluwer: 2020), 734.

[64] Directive (EU) 2019/1023, art 11(2) last clause.

[65] Ontwerp Memorie van Toelichting Wetsvoorstel Implementatiewet Richtlijn Herstructurering en Insolventie (n 21).

[66] Mennens (n 63) 1–2.

[67] Explanatory Memorandum to the WHOA (n 12), 9.

[68] Nicolaes Tollenaar, 'Het Wetsvoorstel Homologatie Onderhands Akkoord onder de Loep Genomen' [2019] (32) Tijdschrift voor Insolventierecht 217, 227.

[69] Géza Orbán, 'De indeling van schuldeisers en aandeelhouders in verschillende klassen onder de WHOA: een Engelsrechtelijk perspectief' [2018] (36) Tijdschrift voor Insolventierecht 225, 225.

[70] DBA, art 374.

[71] Robert van Galen, 'Het Wetsvoorstel Homologatie Onderhands Akkoord' [2020] (39) Ondernemingsrecht 193, 202.

[72] DBA, art 383(1) and art 384(1).

always possible, as the court must refuse confirmation on the following grounds. First of all, the Court has to check whether one of the general grounds for refusal, as laid down in Article 384(2), is present.[73] In this regard it is most important that the Court checks that (1) all affected parties have been notified of the proposal of the agreement and have had the possibility to vote on it; (2) the agreement contains all the information required by Article 375 DBA and (3) the classification of creditors has occurred in line with the requirements of Article 374 DBA.[74] Secondly, under Article 384(2)(i) DBA the court has the discretion to refuse confirmation of the agreement, if there are any other reasons that justify this. This compensates for the lack of a mandatory feasibility test, as it exist in the Directive.[75] Thirdly, under Article 384(3)(a) DBA courts *can* refuse the confirmation of an agreement if a dissenting party invokes that under this agreement it is worse off than it would have been in case of a liquidation in bankruptcy proceedings.[76] Thus, the judge has the discretionary power to refuse an agreement on the ground that the creditors' best interest test is not satisfied.[77]

3.2. The cross-class cramdown

Under certain conditions it is possible that a debtor requests a court to confirm a restructuring agreement, even if not all classes of affected parties have voted in favour of the agreement.[78] Confirmation can be requested as long as at least one class of creditors has voted in favour of the agreement.[79] In line with the Directive it is necessary that this single class voting in favour of the agreement expects repayment in bankruptcy.[80]

In order for an agreement to be confirmed, the court will first of all assess whether one of the grounds for refusal applicable to regular cramdowns, as mentioned in Paragraph 3.1.3, is present. Besides this, the WHOA lays down several additional requirements that need to be satisfied for the court to confirm an agreement that is binding on dissenting classes of creditors. These are the: the WHOA priority rule (WHOA-PR); the 20% rule for small-scale SME-creditors; the right to cash for non-secured creditors and the right to other forms of reimbursement for secured creditors.[81] I will limit my discussion to the WHOA-PR and the 20%-rule, as the interplay between these two rules is most relevant in the context of this article.

3.3. Protection of dissenting creditors under the WHOA

3.3.1. The WHOA priority rule

The Netherlands has implemented a conditional absolute priority rule in the form of the earlier mentioned WHOA-PR.[82] The main rule is that a restructuring agreement cannot deviate from the regular priority ranking, as is applicable in case of a liquidation, to the detriment of a dissenting party.[83] However, derogations from this rule are possible if there is a reasonable ground to deviate from the regular priority ranking and if the interest of the dissenting class of creditors, to whom this deviation is disadvantageous, is not impaired by it.[84]

This formulation leads to several questions relating to the interpretation of the terms used in the WHOA-PR. First of all, it is necessary to delineate what deviations from the regular priority ranking should be considered disadvantageous to the dissenting parties. Consider the situation of class skipping. This is the situation in which a class of secured creditors decides to give some of the value it would normally receive to the class of shareholders, thereby skipping the class of unsecured creditors.[85] Is this disadvantageous to the class of unsecured creditors? Tollenaar argus that it is not, as the class of unsecured creditors has no claim to the transferred money. As a result the class does not receive less than it would in case of liquidation, and thus

[73] Van Galen (n 71) 202 .

[74] Explanatory Memorandum to the WHOA (n 12) 68.

[75] Tollenaar, 'Het Wetsvoorstel Homologatie Onderhands Akkoord onder de Loep Genomen' (n 68) 234

[76] Explanatory Memorandum to the WHOA (n 12) 69.

[77] Tollenaar, 'Het Wetsvoorstel Homologatie Onderhands Akkoord onder de Loep Genomen' (n 68) 235.

[78] DBA, art 383(1).

[79] DBA, art 383(1).

[80] Explanatory Memorandum to the WHOA (n 12) 3.

[81] DBA, art 384(4).

[82] DBA, art 384(4)(b).

[83] Wiepke Bartstra, Rolef de Weijs and Aart Jonkers, 'WHOA-Priority Rule en WHOA-initiatiefrechten: Gaten in schuldeiserbescherming bij reorganisaties' [2020] (15) Tijdschrift voor Insolventierecht 96, 101.

[84] Mennens (n 63) 729.

[85] Bartstra, de Weijs and Jonkers, 'WHOA-Priority Rule en WHOA-initiatiefrechten' (n 83) 101

class skipping is not disadvantageous to that class.[86] Bartstra and others, on the contrary, argue that the class of unsecured creditors is ranked higher than the class of shareholders, and as a result of this they are more entitled to the value being transferred.[87] Therefore, they contend that the deviation in the abovementioned situation is, in fact, disadvantageous to the unsecured creditors.[88] Unfortunately, the Dutch legislator has not offered any guidance on what it considers a disadvantageous deviation from the regular priority ranking.[89]

Similar problems arise with the interpretation of other key terms in the WHOA-PR. It is unclear what should be considered a *reasonable ground* for a deviation from the regular priority ranking under the WHOA. Several authors argue that that a deviation should be considered reasonable if this deviation is necessary to successfully reorganise.[90] But whether this is the case has not been confirmed by the Dutch legislator. Lastly, it is not explained in what situations a deviation from the regular priority ranking does not impair the interest of a higher ranked class of creditors.[91] Mennens reasonably argues that a deviation from the regular priority ranking will necessarily impair the interest of higher ranked creditors. If this is in fact what the Dutch legislator intended, in many cases it would not be possible to fulfil the non-impairment condition.

3.3.2. The 20%-rule

A recent addition to the instruments to protect dissenting creditors under the WHOA is the 20%-rule for small-scale SMEs, laid down in Article 384(4)(a) DBA. In short, this rule holds that small SME-creditors can request a judge not to confirm a restructuring agreement, if under that agreement the value assigned to the class of small SME-creditors is less than 20% of the total amount of their claims.[92] These creditors will be classified as a separate class of creditors.[93] Derogation from the 20%-rule is possible only if there is a compelling reason that justifies a payment of less than 20%.[94] In the next chapter I will assess whether the 20%-rule fits the system of pre-insolvency restructuring of Directive (EU) 2019/1023.

4. The 20%-rule in the light of the restructuring Directive

4.1. The 20%-rule is a derogation from article 11(1) Directive

The 20%-rule is a derogation from the standard proceeding for a cross-class cramdown as laid down in article 11(1) of the Directive. The reason for this is that the 20%-rule violates the absolute priority rule. The Dutch legislator has opted to implement a conditional form of the absolute priority rule, on the ground of article 11(2) first clause of the Directive. In other words, any rule that violates the absolute priority rule is a derogation from Article 11 and should subsequently satisfy the conditions for such a derogation, as laid down in Article 11(2) second clause of the Directive. Below, I will illustrate with an example that the 20%-rule violates the absolute priority rule.

Consider the following scenario. A financially distressed debtor has debts totalling 145. The business is worth 90 in liquidation proceedings and 100 in restructuring proceedings. The bank, as a secured creditor, has a claim of 95. The small-SME-creditors have claims totalling a value of 50. A restructuring agreement is reached in which the value is distributed according to the normal rules of priority. Thus, the bank receives 95 and the unsecured SME-creditors receive the remaining 5. The 5 that the small SME-creditors receive is less than the 10 they are entitled to under the 20% rule. Therefore, they request the court to refuse the confirmation of the agreement. The only way to reach an agreement in which the SME-creditors receive the 10 they are entitled to under the 20% rule, would be to transfer the value of 5 from the bank to the SMEs. But this leads to a violation of the absolute priority rule, as the bank receives less than it's entitled to on the basis of the regular ranking of priority.[95]

The example above is illustrative for most cases in which the 20%-rule is meant to be applied. The 20%-rule is only useful in those cases in which the class of SME-creditors is not already entitled to receive 20%

[86] See in this sense: Tollenaar, 'Het Wetsvoorstel Homologatie Onderhands Akkoord onder de Loep Genomen' (n 68) 235–236.

[87] Bartstra, de Weijs and Jonkers, 'WHOA-Priority Rule en WHOA-initiatiefrechten' (n 83) 101.

[88] Bartstra, de Weijs and Jonkers, 'WHOA-Priority Rule en WHOA-initiatiefrechten' (n 83) 101.

[89] Bartstra, de Weijs and Jonkers, 'WHOA-Priority Rule en WHOA-initiatiefrechten' (n 83) 101; Explanatory Memorandum to the WHOA (n 13) 69.

[90] Mennens (n 63) 481; Sophie Moulen Janssen *De positie van aandeelhouders bij preventieve herstructureringen* (Wolters Kluwer 2020) 116.

[91] Mennens (n 63) 481.

[92] DBA, art 384(4)(a).

[93] Frank Verstijlen, 'Whoa: Omkering van Waarden' [2020] (1718) Nederlands Juristenblad 1943, 1944.

[94] DBA, art 384(4)(a).

[95] Verstijlen (n 93) 1946.

of the total value of their claims under the restructuring agreement. If the class of SME-creditors is already entitled to receive 20% of their claims, the 20%-rule is superfluous.[96] In that scenario, the class of small SME-creditors can invoke both the creditor best interest rule and the absolute priority rule to receive the value they are entitled to. In cases in which the SME-creditors are not already entitled to 20% of the value of their claims, the only way to grant the class of SME-creditors 20% of value is by taking away this value from another class and giving it to the class of SME-creditors. This is not necessarily contrary to the creditor best interest principle. If enough value is realised through the agreement, the other classes might still receive a similar or higher amount than they would receive in liquidation proceedings. However, such a transfer is a violation of the absolute priority rule. In order to give the class of SME-creditors more than they are entitled to on the basis of the priority ranking, another class of creditors will have to receive less than it is entitled to on the basis of that ranking. As such, in any case in which the 20%-rule can be effectively invoked by the class of SME-creditors the absolute priority rule is necessarily violated in order to satisfy the claim of the class of SME-creditors.

Therefore, the 20%-rule is a derogation from the provisions on cross-class cramdowns as laid down in Article 11 of the Directive. In order for such a derogation to be justified, the provision introduced by the Member State should be necessary in order to achieve the goals of the restructuring plan and the restructuring plan should not unfairly prejudice the claims or interest of other affected parties.[97] In the following subsections I will evaluate whether the 20%-rule meets these requirements.

4.2. Does the WHOA satisfy the requirement of an unfair prejudice test

4.2.1. Definition of the unfair prejudice test

If Member States wish to derogate from the rules of Article 11, they must introduce an unfair prejudice test in their national pre-insolvency proceedings, in order to comply with the Directive.[98] Unfortunately, the Directive does not define what such a test entails in relation to a cross-class cramdown. Nonetheless, it gives some guidance as to the meaning of the term in relation to the stay of enforcement of actions. In such cases, a judge has to assess whether the stay preserves value overall and whether one or more of the creditors act in bad faith by requesting the stay.[99] Furthermore, Recital 37 states that a situation is unfairly prejudicing if, for example, one class of creditors is substantially worse off due to the stay of enforcement of actions, or in case one class of creditors is treated less favourably than another class of creditors of a similar rank.[100] The definition of 'unfair prejudice' has not been given in relation to the cross-class cramdown specifically. But, the definitions above can by analogy be assumed to apply to the situation of a cross-class cramdown, since it is implausible that the term 'unfair prejudice' would have a widely different meaning throughout the Restructuring Directive.

4.2.2. Does the WHOA implement an unfair prejudice test

Under the Dutch WHOA, the interplay between the WHOA-PR and the 20%-rule enables the judge to review how the value realised through an agreement is distributed amongst the stakeholders.[101] This review is not mandatory, but must be requested by one of the affected parties.[102] The term 'unfair prejudice' is not used in the WHOA, but the judge has the power to review and possibly refuse the confirmation of an agreement in case of an infringement of party rights. [103]

The strict standards for derogating from the absolute priority rule set by the Dutch WHOA, however, lead to quite restricted possibilities for judicial reviews. Under the WHOA a deviation from the normal priority ranking to the detriment of a higher ranked creditor is only possible when two cumulative requirements have been met: 1) there must be a reasonable ground for this deviation; and 2) the interest of the affected

[96] Verstijlen (n 93) 1946.

[97] Directive (EU) 2019/1023, art 11 last clause.

[98] Directive (EU) 2019/1023, art 11 last clause; JCOERE Consortium, 'Report 1: Identifying substantive and procedural rules in preventive restructuring frameworks including the Preventive Restructuring Directive which may be incompatible with judicial co-operation obligations' (University College Cork 2019), 130–131 available at <https://www.ucc.ie/en/jcoere/research/report1/> accessed 27 August 2021.

[99] Directive (EU) 2019/1023, recital 36.

[100] Directive (EU) 2019/1023, recital 37.

[101] Explanatory Memorandum to the WHOA (n 13) 69.

[102] DBA, art 384(4).

[103] In the explanatory memorandum to the WHOA the term fair is used in the context of art 384 sub 4. However, this is not the case for the final legislative document.

creditors must not be impaired.[104] It can be argued that satisfying the 20% rule is a reasonable ground to deviate from the normal order of priority ranking.[105] However, the Dutch legislator has failed to specify whether this is indeed the case.[106] Nevertheless, if the 20%-rule is understood to be a reasonable ground to deviate from the WHOA-PR the first condition could be satisfied.

Satisfying the second condition, however, will not be possible in many cases. It was already argued above that in order to satisfy the 20%-rule, value needs to be transferred from a higher ranked class to the class of SME-creditors. Such a transfer of value is a deviation from the standard priority ranking. As mentioned, according to the WHOA, this deviation may not impair the interest of any dissenting party. The Dutch legislator has not given any specific considerations as to when the interest of a dissenting party is impaired.[107] Article 54 of the Restructuring Directive, contrastingly, gives a definition. It holds that impairment of a party's interest means that there is a reduction of the value of its claims.[108] In the exemplary scenario in 4.1, there is a reduction in value of the claims of the bank. To satisfy the 20%-rule, a value of 5 must be transferred from the bank to the small SME-creditors. This is an impairment of the bank's interest and, therefore, the second condition for a deviation from the WHOA-PR cannot be satisfied. Thus, the judge is held to refuse confirmation of the agreement.[109]

This shows that the possibilities for judicial review under the WHOA are quite restricted, as the court is bound to refuse any agreement that infringes the rights of higher-ranked dissenting parties. This is possibly unintentional, as the Dutch legislator could have meant to exclude the 20%-rule from this provision.[110] However, since the Dutch legislator has not done so the 20%-rule conflicts with the non-infringement condition of the WHOA-PR. Therefore, the court is bound to refuse confirmation, on the ground that it cannot approve deviations from the standard priority ranking that impair the right or interest of higher ranked creditors.[111] This leads to a stalemate. On the one hand, secured creditors can invoke the WHOA-PR in order to prevent the confirmation of an agreement in which value is transferred from their class to the class of small-scale SME-creditors on the basis of the 20%-rule. On the other hand, small-scale SME-creditors can invoke the 20%-rule and request the judge to refuse confirmation of an agreement in which they do not receive 20% of their claims, to which they are entitled under the 20%-rule.

In conclusion the current possibilities for judicial review under the WHOA are more restrictive than required by the Directive. The Directive grants the court room for interpretation by adopting the term *unfair* in the test itself, and *substantially* in its explanations as to what constitutes unfair prejudice.[112] The non-impairment requirement of the WHOA-PR, however, lacks these open norms and, as such, binds the judge to refuse any agreement impairing the rights of higher-ranked creditors. From a compliance point of view, being overly restrictive is not problematic because the Directive is a form of minimum harmonisation. Therefore, the requirement of an unfair prejudice test is satisfied by the WHOA. Now, it must be assessed whether the 20%-rule is necessary to achieve the goals of the restructuring plan.

4.3. Is the 20%-rule necessary to achieve the goals of the restructuring plan

Two separate questions can be derived from the necessity requirement that is laid down by Article 11 of the Directive. The first question is whether the national provision is necessary in light of the restructuring plan and the aim of restructuring proceedings in general. The second question is less straightforward, namely whether the national provision can be expected to effectively contribute to achieving this aim. Answering this question is necessary to assess whether the provision introduced by the Member State can contribute to the attainment of the goal of the restructuring plan in practice.

4.3.1. Necessity

Legal provisions are by their very nature phrased in general terms and thus never tailored to one specific restructuring plan. Therefore, it should not only be assessed whether the 20%-rule is expected to contribute

[104] Van Galen (n 71) 205.

[105] Verstijlen (n 93) 1946.

[106] Verstijlen (n 93) 1946.

[107] Bartstra, de Weijs and Jonkers, 'WHOA-Priority Rule en WHOA-initiatiefrechten' (n 83) 101.

[108] Directive (EU) 2019/1023, recital 54.

[109] DBA, art 384(1) and (4)(b).

[110] Verstijlen (n 93) 1943.

[111] DBA, art 384(4)(a).

[112] Directive (EU) 2019/1023, art 11(2) last clause and recital 37.

to the goals of one individual restructuring plan (as a strict reading of Article 11 would suggest), but also whether the 20%-rule is expected to contribute to the broader policy goals pursued by the introduction of a system of pre-insolvency restructuring. In order to conduct this evaluation, I will draw upon the policy goals as formulated in the Directive.

In this regard, it can be observed that the Directive has the underlying objective of strengthening the position of SMEs in insolvency and pre-insolvency proceedings.[113] In its 17th Recital the Directive states that SMEs in particular should benefit from the system of pre-insolvency restructuring.[114] The Directive introduces several provisions that benefit SME-debtors, such as the debtor in possession norm and tools to have early access to restructuring proceedings.[115] Yet, the Directive also aims to enhance the position of SMEs as creditors, given that it mentions higher recovery rates for SME-creditors under the new restructuring system as a specific advantage to this group of creditors.[116] Furthermore, the aim of the Directive is to prevent both job and value loss within the Union.[117] In 2018, Micro to Small-sized companies, to which the 20%-rule is beneficial, provide 38.4% of all value and 49.8% of all employment in the Union. Furthermore, relative to their size SMEs are less resilient to losses and thus run a greater risk of insolvency due to such losses.[118] Considering this, strengthening the position of such companies in case of pre-insolvency restructuring, effectively contributes to reducing value and job loss in the EU.

Lastly, Recital 56 of the Directive explicitly mentions the possibility for Member States to deviate from the absolute priority rule. This possibility exists in order to satisfy the claims of suppliers that meet two requirements: the suppliers should be essential and their claims should be affected by the stay.[119] On the one hand the Dutch 20%-rule is broader, as the rule is not limited to essential suppliers, nor is it limited to claims affected by the stay. On the other hand, the Dutch 20%-rule is narrower, as it only affects small-scale SME-creditors as opposed to Recital 56, which also includes Midsized creditors. Nevertheless, the 20%-rule is a provision that in its outset and aim is very similar to one of the exemplary provisions laid down in Recital 56. The 20%-rule aims to safeguard the interests of more junior and often small-scale creditors that play an important role in realizing the reorganisation surplus vis a vis more senior creditors. This reasoning corresponds to the ratio for the justification of a deviation from the absolute priority rule, that is laid down in Recital 56. As the 20%-rule fits the Directive's objective of strengthening the position of SMEs and is similar to one of the exemplary justifications for deviating from the absolute priority rule, the 20%-rule can be deemed necessary in light of the overarching goal of the restructuring directive.

4.3.2. Achieving the goals of the restructuring plan – forum shopping on the national level

In Paragraph 4.2., I signalled a dogmatic problem for the 20%-rule. The rule conflicts with the WHOA-PR, leading to the necessary refusal of confirmation of the agreement by the court. This will hamper the efficacy of the rule in practice. This problem is not insurmountable, as the Dutch legislator could opt to give the 20%-rule priority over the WHOA-PR through an amendment to the WHOA. Yet too large of an infringement on the rights of secured creditors could lead to the problem of forum shopping. This is the situation in which parties have a clear strategic interest in using one proceeding over the other.[120] Forum shopping could occur both on the national and on the European level, as a result of the 20%-rule.

On the national level the 20%-rule might incentivise forum shopping, as it creates a dichotomy between the rights of creditors in case of bankruptcy proceedings and their rights in restructuring proceedings.[121] This leads to a situation in which SME-creditors and secured creditors will have clear interests in using restructuring and liquidation proceedings respectively. Restructuring proceedings are more beneficial to small SME-creditors, who can use the 20%-rule in their favour. Secured creditors, on the other hand, will prefer liquidation proceedings, as they have a very strong position in these proceedings. In sum, both parties will have a separate interest in using either one of the proceedings, even if this is not the most effective

[113] Mevorach and Walters (n 43) 2–3, fn. 6.

[114] Directive (EU) 2019/1023, recital 17.

[115] Jonathan McCarthy, 'A Class Apart: The Relevance of the EU Preventive Restructuring Directive for Small and Medium Enterprises' 2020 European Business and Organization Law Review (published online 22 June 2020) 4–6 DOI: 1007/s40804-020-00192-x.

[116] COM/2016/SWD/723/final (n 35) 19.

[117] COM/2016/SWD/723/final (n 35) 5.

[118] Directive (EU) 2019/1023, recital 17.

[119] Directive (EU) 2019/1023, recital 56.

[120] Jochem Hummelen, *Distress Dynamics: an Efficiency Assessment of Dutch Bankruptcy Law* (RUG 2015) 54.

[121] Verstijlen (n 93) 1945.

use of the common pool of assets.[122] There might be situations in which secured creditors will nevertheless prefer restructuring proceedings, as the gains realised through these proceedings compensate for the fact that they have to transfer some value to the class of SME-creditors. In these cases an equilibrium is reached and the 20%-rule might work as intended. However, another problem is introduced by the 20%-rule. This is the fact that both secured creditors and small-scale SME-creditors now have an individual interest in using bankruptcy and restructuring proceedings respectively. As a result of this both classes of creditors are no longer motivated to use that proceeding that generates the highest value for the creditors as a group, but will strategically use that proceeding that is most beneficial for their respective class.[123] As mentioned above there might be situations in which the interests of both types of creditors overlap. If this is not the case, however, the dichotomy between the rights of both classes under the different proceedings invites strategic use of those proceedings for individual gains. This makes it less likely that the remaining assets of a financially struggling debtor are used in the most efficient way.[124]

In the worst-case scenario, secured creditors could try to avoid restructuring proceedings altogether due to their weakened position in that regime. This would severely diminish the effectiveness of such proceedings in practice. This issue was discussed in the parliamentary debate on an earlier version on the 20%-rule.[125] One of the drafters of the 20%-rule argued that it would be cynical to think that banks would rather turn to bankruptcy proceedings than to suffer financial damage through restructuring proceedings.[126] In my opinion, avoidance of restructuring proceedings by secured creditors is a serious risk, given that there is a substantial discrepancy between the secured creditor's position in liquidation and restructuring. In the end, the secured creditor might have negotiated a loan agreement, in which it has (at least partly) adjusted the costs of its loan for its strong position in liquidation.[127] Therefore, the Dutch legislator should be cautious when implementing rules deteriorating the rights of secured creditors in restructuring proceedings. If an infringement of these rights is considered too rigorous, it could have the contrary effect of shying secured creditors away from restructuring proceedings. This could, in turn, result in a less used and therefore less effective system of pre-insolvency restructuring, contrary to the aims of both the WHOA and the Directive.

4.3.3. Achieving the goals of the restructuring plan – forum shopping on the European level

Absent a unified European approach on the protection of SME-creditors, the 20%-rule is likely to also incentivise forum shopping on the European level. Large corporations that operate in multiple jurisdictions will be motivated by their secured creditors not to restructure through the WHOA, because these secured creditors are aware that their position is weaker under Dutch Law. It is unlikely that the provisions against forum shopping laid down in the Recast European Insolvency Regulation (EIR Recast) can prevent such forum shopping.[128]

Under the regime of the EIR Recast, main insolvency proceedings can be opened in the state in which a company has its 'Centre of Main Interests' (COMI).[129] Forum shopping in cross-border insolvencies occurs if a company relocates its COMI to another jurisdiction, to benefit from the more favourable insolvency or restructuring legislation of that jurisdiction.[130] Such a COMI-shift can be achieved by either moving a company's registered office to another country, or by moving a company's head office to another country while leaving behind the registered office.[131] The EIR Recast is designed to prevent forum shopping, which is clearly reflected in Recitals 5 and 29 of the Regulation.[132] The Regulation is extended to apply to restructuring

[122] Thomas Jackson 'Of Liquidation, Continuation, and Delay: An Analysis of Bankruptcy Policy and Nonbankruptcy Rules' (1986) 60 American Bankruptcy Law Journal 399, 403–404.

[123] ibid.

[124] ibid.

[125] Kamerstukken II 2019–2020, 33225, 35249 no. 20 p 27–28

[126] ibid.

[127] Nicolaes Tollenaar 'Amandementen op de WHOA een tikkeltje onbesuisd' [2020] (23) Tijdschrift voor Insolventierecht 153, 156-157.

[128] Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (recast) [2015] OJ L141/19.

[129] Gerard McCormack, 'Something Old, Something New: Recasting the European Insolvency Regulation' (2016) 79 Mod L Rev 121, 123. DOI: 10.1111/1468-2230.12169.

[130] Peter Mankowski, 'The European World of Insolvency Tourism: Renewed, But Still Brave?' (2017) 64 The Netherlands International Law Review 95, 97. DOI: 10.1007/s40802-017-0080-7.

[131] Wolf-Georg Ringe, 'Insolvency Forum Shopping, Revisited' in V Lazić S Stuij (eds), *Recasting the Insolvency Regulation. Short Studies in Private International Law* (T.M.C. Asser Press 2020), 10. DOI: 10.1007/978-94-6265-363-4_1.

[132] Horst Eidenmüller, 'The Rise and Fall of Regulatory Competition in Corporate Insolvency Law in the European Union' (2019) 20 European Business Organization Law Review 547, 548. DOI: 10.1007/s40804-019-00160-0.

proceedings as well, on the basis it 10th Recital. In order for a restructuring proceeding to fall within the scope of the EIR, the proceeding should meet the conditions laid down in Article 1 of the EIR and should be listed in Annex A to the Regulation.[133] However, it is doubtful whether the EIR can effectively prevent forum shopping, especially in regard to restructuring proceedings.

One of the main instruments to combat forum shopping is the introduction of a suspension period in Article 3(1) of the Recast EIR.[134] On the ground of this article the COMI of a company will be presumed to be in the country where said company has its registered office. However, this presumption will be rebutted in case the registered office of a company shifted within three months prior to the request to open insolvency proceedings. The court then has to establish whether or not the company's COMI is actually located within its jurisdiction.[135] Two main problems can be identified with this approach. First of all, Ringe points out that the suspension period only applies in cases in which a company's registered office is moved.[136] However, a common forum shopping strategy is to move a company's head office instead of its registered office. Second, the relocation of a company's registered office just before filing for insolvency does not lead to an automatic rejection of the opening of insolvency or restructuring proceedings.[137] The court merely has to establish whether the COMI of the company is really located in its jurisdiction.[138] Both Ringe and Eidenmüller conclude that as a result of this COMI-shifts and forum shopping will still be possible under the Recast EIR.[139] Therefore, it is unlikely that forum shopping is effectively curbed by the EIR recast. If no Union-wide measures are taken to enhance the position of SME-creditors, the 20%-rule could lead to avoidance of the WHOA in cross-border restructurings.

4.4. Concluding remarks

Overall, I conclude that the 20%-rule is in accordance with the restructuring Directive, as it fits the requirements laid down in the Directive. The Netherlands has introduced an prejudice test, albeit that this test is more restrictive than necessary. This can be problematic when applying the 20%-rule in practice. Furthermore, the 20%-rule can be deemed to contribute to the overall goal of restructuring proceedings. Therefore, the 20%-rule meets the requirements for a derogation from Article 11 of the Directive. However, the 20%-rule creates incentives for forum shopping and the overly restrictive system of judicial review can hamper its effectiveness in practice. In the last section I will illustrate how a more nuance form and application of the 20%-rule can overcome this problem.

5. Further aligning the 20%-rule with the Restructuring Directive

5.1. Ensuring minimum protection

As has become apparent from the last section, the introduction of the 20%-rule in the Netherlands could be to the disadvantage of larger creditors that do not enjoy the protection of this rule. This unfavourable treatment of larger creditors in the Netherlands shows some resemblance to the situation of reverse discrimination. This is the situation in which a Member State treats its own citizens less favourably than those who can rely on Union Law.[140] However, as long as the minimum level of protection laid down in the Directive is guaranteed no reverse discrimination takes place. In that scenario those larger creditors whose debtor restructures through the WHOA are not treated *less* favourably than is prescribed by Union Law.[141] Larger creditors restructuring through the WHOA might face a less favourable regime than is in place in other Member States, but this is a logical effect and intended consequence of the fact that the Restructuring Directive is only minimum harmonisation.[142] However, the Dutch legislator and judiciary should be cautious that the 20%-rule does not undermine the minimum level of protection laid down in the Directive.

[133] Regulation (EU) 2015/848, art 1(1).

[134] Ringe (n 131) 10.

[135] Ringe (n 131) 9–10.

[136] Ringe (n 131) 10.

[137] Ringe (n 131) 9.

[138] Eidenmuller (n 132) 558.

[139] Ringe (n 131) 10; Eidenmuller (n 132) 558.

[140] Dominik Hanf, 'Reverse Discrimination' in Eu Law: Constitutional Aberration, Constitutional Necessity, or Judicial Choice' (2011) 18 Maastricht Journal of European and Comparative Law 29, 30. DOI: 10.1177/1023263X1101800103; Johanna Croon-Gestefeld, Reconceptualising European Equality Law: A Comparative Institutional Analysis (Hart Publishing 2017), 120. Chapter DOI: 10.5040/9781509909674.ch-005

[141] ibid.

[142] Tollenaar 'The European Commission's Proposal for a Directive' (n 36) 66.

5.2. Introducing a substantial infringement test

In order to better align the WHOA with the Directive and to ensure that the minimum level of protection for creditors laid down therein is guaranteed, the Dutch legislator should adjust the current system of judicial review of the WHOA-PR. Currently, judges have some possibility to review whether a deviation from the WHOA-PR in favour of the 20%-rule is justified. However, the hard non-infringement condition of the WHOA-PR entails that any agreement which harms the interest of a higher ranked creditor should be refused confirmation by the judge. The Dutch legislator could solve this issue by introducing more open norms in the non-infringement condition, as are used in the Directive.[143] It could adopt the terminology used in the directive and make it so that only a substantial infringement on the rights of higher ranked creditors necessitates the refusal of confirmation of an agreement by the court.[144] This gives the judiciary more room to assess whether a deviation from the normal ranking of priority is reasonable or whether it constitutes to great an infringement of the rights of higher ranked creditors.

Stalemates can be prevented in this way as well. Judges will now no longer be bound to refuse confirmation of otherwise reasonable agreements, if there is merely a non-substantial infringement of the rights of higher ranked creditors. The court has the possibility to weigh and balance the interests of several parties, and to rule accordingly. Thus, by adjusting the infringement-condition to a substantial condition the Dutch legislator gives judges a tool to resolve conflicts arising from the interplay between the WHOA-PR and the 20%-rule. Moreover, after this change the requirement for an unfair prejudice test as laid down Article 11 last clause of the Directive will undoubtedly be satisfied.

5.3. Carefully applying the 20%-rule

Lastly, even after these changes, the Dutch judiciary should be careful when applying the 20%-rule and be aware of the constraints of Union Law. In assessing whether to accept an appeal to the 20%-rule, judges should acknowledge that the rules of priority are the cornerstone of restructuring proceedings and that deviations from these rules are the exception. This means a nuanced approach to the application of the 20%-rule is necessary, entailing that the 20%-rule cannot always trump the WHOA-PR. Such a priority for the 20%-rule could be inferred from the fact that a reasonable ground is needed in order to deviate from the WHOA-PR, whereas a compelling reason is required in order to not apply the 20%-rule.[145] However, the wording of Article 11 of the Directive clearly reflects that following the rules of priority is the default, with only limited options for deviations. This should be observed by judges applying the 20%-rule as well. Thus, a cautious approach to applying the 20%-rule should be taken, which ensures that the minimum level of protection for larger creditors is guaranteed.

This should also prevent creditors who restructure through the WHOA from being treated less favourably than they should be under Union law. While some larger enterprises might still prefer to opt for restructuring proceedings in other Member States, that are possibly more beneficial for large creditors, the problem of reverse discrimination does not occur. This will reduce incentives for forum shopping on the European level. Also, a nuanced approach to the application of the 20%-rule should reduce the strategic incentive to evade restructuring proceedings in favour of insolvency proceedings on the national level. Stalemates are no longer to be expected and parties to the agreement will be ensured that their rights will not be unreasonably infringed upon.

6. Conclusion

In this article I focussed on the protection of SME-creditors in pre-insolvency proceedings. An effective system of corporate rescue can help to mitigate the negative effects of the Covid-crisis, and adequate protection of SME-creditors is crucial to this end. Accordingly, I assessed whether the WHOA's 20%-rule, intended to protect SME-creditors in the event of a cross-class cramdown, is in accordance with Directive (EU) 2019/1023. In the first two sections I described the system of pre-insolvency restructuring as adopted by the Directive and implemented in the Netherlands through the WHOA. This descriptive framework allowed me to assess whether the 20%-rule meets the requirements to deviate from the standard rules for a cross-class cramdown, as laid down in the Directive. This resulted in a twofold evaluation, namely whether 1) the Netherlands has adequately implemented an unfair prejudice test and 2) whether the 20%-rule is necessary to attain the goals of the restructuring plan. I argued that the 20%-rule meets these requirements, but that

[143] Directive (EU) 2019/1023, recital 37.

[144] ibid.

[145] DBA, article 384 sub 4 a and b.

the 20%-rule is often incompatible with the WHOA-PR due to an overly strict system of judicial review. In overcoming this problem the Dutch legislator should be cautious, as a too strict protection of SME-creditors could lead to forum shopping both on the national and European level.

I then argued that it would be wise if the Dutch legislator adjusted the current system of judicial review by introducing more open norms, in order to better align the 20%-rule with the Directive. This can be done by changing the non-infringement test of Article 384 sub 4 b to a substantial infringement test. In this way courts have the possibility for a more nuanced review of the justification of a deviation to the WHOA-PR. When conducting this review judges then should be aware that the rules of priority are default, and thus be careful in having the 20%-rule trumping the rules of priority. In the end, if these changes are made the 20%-rule can be a tool to enhance the protection of SME-creditors, fitting within the European restructuring framework.

Competing Interests

The author has no competing interests to declare.

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