

The way forward where value breaks in the junior debt – a ruling from the Dutch courts

Background

The Schoeller Arca Systems group ("SAS") had entered into financing arrangements comprised of a EUR 142,000,000 senior facility and a EUR 180,000,000 bridge facility. The payment obligations under both facilities were secured by, amongst other security, a right of pledge over the shares in the holding company of the group, a Dutch company ("Dutch Holdco"). Pursuant to an English law intercreditor agreement, the bridge facility was subordinated to the senior facility.

In order to avoid insolvency proceedings, it was necessary to deleverage the SAS group. A restructuring plan was prepared which involved the enforcement of the share pledge over the Dutch Holdco, and the sale of the SAS group to a bidco established by the existing owners of SAS ("Bidco"). The plan contemplated enforcement by private sale with Dutch court approval, thereby avoiding the need for a public auction process. The purchase price consisted of a continuation of the senior facilities and a cash payment to the bridge lenders (representing a partial recovery for the bridge lenders). Following the enforcement the SAS group members would be released from their guarantee and security obligations in respect of the bridge facility, through the security trustee exercising the powers granted to it under the Intercreditor Agreement, pursuant to a direction from the majority senior lenders.

During the court proceedings, one of the two remaining bridge lenders (the "Opposing Bridge Lender") objected to the proposed private sale. In addition, an alternative bidder (the "Alternative Bidder") submitted an alternative offer to the court for approval by way of private sale.

On 23 September the Dutch court gave its approval in respect of the private sale, to Bidco, of the shares in the Dutch Holdco. In doing so it concluded that "in circumstances where no unconditional and better offer is made than the offer of purchaser (i.e. Bidco), and the pledgee and pledgor are in agreement with the offer of purchaser, it cannot be determined that the proceeds for which the shares are being sold do not represent the maximum possible proceeds."

Key issues before the Dutch court

The following key issues were considered by the Dutch court:

Public auction or private sale

The Opposing Bridge Lender argued that enforcement should take place by public auction instead of by private sale as that would result in a higher purchase price and therefore more proceeds being available to the bridge lenders. In its interim judgment the Dutch court ruled that upon receipt of a request for approval of a private sale, the court shall "determine whether in case of a private sale a better offer is expected than in a public auction, all in the interest of the debtor (i.e. the pledgor) and the various creditors who are entitled to take recourse against the various proceeds of the sale". Furthermore the court ruled that "it can be assumed that a private sale will result in a higher purchase price than a sale by public auction, taking into account the structure and complexity of the SAS group and the requirements of further financing thereof."

Key Issues

Public auction or private sale?

Timing of enforcement

Credibility of alternative offers

Rights of junior creditors

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Timing of enforcement

It was undisputed in the court proceedings that SAS was in default of its payment obligations for which the security had been granted, and that therefore the pledgee had the right of summary execution. The Opposing Lender questioned how immediate the financial difficulties were and argued that there was sufficient time to arrange a public auction or to consider alternative bids in a private sale. In this respect the court ruled that "The right of summary execution is not disputed. This means that the debate about the cash flow of the company is not relevant for the question whether the exercise of the right of summary execution is necessary in the short term. It is at the discretion of the pledgee to determine the timing of enforcement, which it has done by filing the request for approval."

The alternative offer – was it realistic?

After receipt of an alternative offer from the Alternative Bidder the court issued an interim judgment and held a second hearing for the purposes of determining the "reality" of the alternative offer. In its judgment the court stated that it should be determined whether the alternative offer was an "unconditional" and "better" offer. In this case the court concluded that it was not an unconditional offer as it was still subject to final investment committee approval. Furthermore, it was not a better offer as one of the senior lenders and one of the bridge lenders had confirmed that they would not agree to the proposed terms of the alternative offer. The court added in its conclusion that "the extensive opportunity that was given in the proceedings to submit a better offer had not resulted in an unconditional and better offer" and that it was the task of the Opposing Bridge Lender to "promote an alternative better offer for as long as it opposed the enforcement sale to Bidco."

Rights of junior creditors

The Opposing Bridge Lender argued that as a result of the enforcement, the bridge lenders would be left with a claim against an "empty" company (the pledgor) as all its assets had been sold to Bidco. The court ruled in its interim judgment that "the starting point is that bridge lenders, when entering into the transaction, agreed to a subordinated/second ranking pledge."

Comment

This decision is clearly of significant importance to the Dutch restructuring market. As Ilse van Gasteren, senior associate in our Restructuring Group in Amsterdam observes: "It is the first time that the Dutch court has approved a "Dutch pre-pack" by way of an enforcement sale of a Dutch holding company, which is pre-agreed between a buyer, the company and the senior lenders, while the junior lenders oppose the proposed sale."

This decision of the Dutch court is also instructive for the many European cross-border restructurings currently underway.

The acknowledgment that the structure and complexity of the group made it unsuitable for sale by public auction is helpful, and significant, particularly in jurisdictions where pre-pack solutions are not available and it is imperative to avoid the detrimental impact of public auctions such as the termination of contracts, the withdrawal of supplier lines and the loss of employees.

The suggested values in this case clearly showed value breaking in the junior facility, although at significantly different points depending on which suggested value was taken. Key to the court ruling however was what was actually deliverable at that time and in those circumstances. Geeta Khehar, Finance partner and a member of our Restructuring Group, notes that: "This demonstrates the practical and commercial approach the courts are willing to take in complex restructuring situations. An unconditional offer which provides support for the relevant group has clearly been preferred to a higher offer with some conditionality."

Mark Hyde, partner in our Restructuring Group, comments: "This is another very important judgment for restructuring professionals following the recent English High Court judgment in (IMO) Car Wash which established how out of the money creditors fall to be dealt with under an English law Scheme of Arrangement. Now we have a clear example of a court tackling head on, the not uncommon issue as to how to implement a restructuring where value clearly breaks in the junior debt."

Clifford Chance London and Clifford Chance Amsterdam advised the senior lenders on this restructuring. A more detailed analysis from a Dutch law perspective is available on request.

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