Is there still a future for rental guarantees (Parts II and III)?

In April 2011 we published a client briefing in relation to Part I of this series (Hoge Raad (*Dutch Supreme Court*) 14 January 2011 – Aukema qq vs Uni-Invest BV). In that case the question was raised whether the landlord was entitled to claim contractual damages in case of an early termination of the rental agreement in question by the liquidator (*curator*) in the bankruptcy of the tenant on the basis of section 39 of the Dutch Bankruptcy Act ("DBA"). It was held that such a claim for damages was not allowed as this would be contrary to the purpose (*strekking*) of section 39 DBA.

Recently two cases were published (Hoge Raad (*Dutch Supreme Court*) 15 November 2013 – Romania Beheer BV ("Part II") and Hoge Raad (*Dutch Supreme Court*) 22 November 2013 – Transeuropean Properties IV NL Autodrome BV ("TEP") vs Mr J.C.M. Silvius/Mr P.J. van Steen qq ("Part III")) in which the Dutch Supreme Court further developed (and complicated) its theory set out in Part I of this series. Part II deals with the consequences of the termination of a rental agreement by the liquidator on the scope of the obligations of the guarantor of the tenants obligations under such agreement. In Part III the Dutch Supreme Court decides that its theory just referred to also applies in situations where the rental agreement forms part of a financial sale and lease back transaction.

Please click here for the text of our April 2011 client briefing.

Part II of this series concerns the following:

1. Three subsidiaries of Romania Beheer entered into a rental agreement as tenants with the plaintiff as landlord.
2. Romania Beheer co-signed the rental agreement as guarantor (in this case by way of surety (*borgstelling*)) of the obligations of the tenants pursuant to the rental agreement.
3. The tenants were declared bankrupt on 20 January 2009 and the liquidator in the bankruptcy of the tenants terminated the rental agreement on 21 January 2009 with observance of the statutory notice period (in this case three months) on the basis of section 39 DBA.
4. The landlord turned to Romania Beheer and filed a claim under its guarantee (as set out in the rental agreement) of all sums due by the tenants pursuant to the rental agreement, as a consequence of the early termination thereof.
5. Romania Beheer "replied" by paying the sums due by the tenants until the end of the notice period set out in 3. above, but refused to pay anything in excess thereof with the argument, basically, that the guarantee only covered the obligations of the tenants under the rental agreement, which in the circumstances of the case (especially the termination of such agreement by the liquidator on the basis of section 39 DBA) were limited to the rentals falling due until the end of the notice period.
6. The landlord disagreed and the parties went to court. The cantonal court, in first instance, found in favour of the landlord. The court of appeal, however, found in favour of Romania Beheer, but the Dutch Supreme Court decided in favour of the landlord.

It is interesting to devote some attention to the considerations of the Dutch Supreme Court, especially

since these seem to go to the roots of the "rental guarantee practice" in the Netherlands.

First of all the Dutch Supreme Court said that its judgment in the Aukema qq/Uni-Invest case (Part I of this series) should be understood in such a way that a contractual indemnity in the rental agreement in favour of the landlord, payable in case of an early termination of such agreement by the liquidator on the basis of section 39 DBA, does not have any effect against the bankrupt estate (*boedel*). Furthermore, according to the Dutch Supreme Court, although the contractual indemnity and the validity thereof in relation to the tenants themselves (as distinguished from their bankruptcy estates) were not affected by a termination of the rental agreement on the basis of section 39 DBA, the ensuing claim could not be filed for verification in the bankruptcy of the tenants.

Consequently, again according to the Dutch Supreme Court, where a third party has guaranteed payment of such claim, neither the bankruptcy of the tenants nor the termination of the relevant rental agreement on the basis of section 39 DBA, will result in a change of the obligations under such guarantee, unless the guarantee stipulates otherwise. As a result, the guarantor has to pay the full amount of the contractual indemnification payable pursuant to the rental agreement to the landlord.

Finally, the Dutch Supreme Court mentioned that any possible recourse claim (*regresvordering*) of the guarantor against the bankrupt tenants, insofar as it relates to the non-verifiable "part" of the landlord's claim against the tenants, cannot be exercised against the bankruptcy estate of the tenants.

Thus the hot potato seems to rest squarely in the lap of the guarantor (if any).

Part III of this series involves a financial sale and leaseback

The simplified facts of the case are as follows:

- The owners of certain properties which were rented out to Autodrome Holding entered into a sale and leaseback transaction with a third party.
- TEP was incorporated for the purpose of acquiring title to the properties just referred to from the said owners and of renting the same out to Autodrome Holding.
- The sale and leaseback transactions were effected on 9 February 2008; the rental agreements were made between TEP as landlord and Autodrome Holding as tenant for an initial duration of ten years.
- ABN AMRO Bank issued an irrevocable, unconditional and independent bank guarantee on the request of Autodrome Holding, covering its obligations under the rental agreement; the maximum amount of the bank guarantee was equal to the aggregate of the rental instalments for a 12 month period plus VAT in respect thereof.
- Autodrome Holding B.V. was declared bankrupt on 23 April 2009 and the liquidators in the bankruptcy terminated the rental agreement on the basis of section 39 DBA on 29 April 2009 with effect from 31 July 2009.
- TEP turned to ABN AMRO and claimed (and obtained) payment of the maximum amount due under the bank guarantee. Subsequently ABN AMRO turned to Autodrome Holding and reclaimed the amount paid under the bank guarantee from Autodrome Holding under the indemnity given by the latter to the bank. The claim was paid by set off (*verrekening*) against the credit balance maintained by Autodrome Holding on its bank account with the bank. All these payments were effected on or around 14 May 2009.
- The liquidators claimed payment by TEP of the amount received by it under the bank guarantee to the extent that such amount exceeded the rent due until 31 July 2009 (being the date by reference to which the rental agreement was terminated by the liquidators). The liquidators based their claim on unjust enrichment (*ongerechtvaardigde verrijking*) by TEP (it had received substantially more than it was entitled to on the basis of section 39 DBA) while the bankruptcy estate was impoverished by the same amount as a consequence of the set-off applied by ABN AMRO referred to above.
- TEP refused to repay and the parties ended up in court.

TEP lost in all instances.

TEP argued both before the court of appeal and before the Dutch Supreme Court that the sale and leaseback transaction, of which the rental agreement between it and Autodrome Holding formed an integral part, should be distinguished from a rental agreement as referred to in section 39 DBA. TEP supported its reasoning with the following arguments:

- The nature of a financial sale and leaseback transaction which is used first and foremost to obtain new financing for the original owners (freeing up capital

which was tied up in the properties) is essentially different from the nature of a typical rental agreement.

- The balance between the mutual rights and obligations of the parties involved in the transaction would be disturbed if the doctrine developed in the Aukema qq/ Uni-Invest case would be applied to the present one.
- The creditworthiness of the tenant (enhanced, obviously, by the bank guarantee issued by ABN AMRO) was of essential importance to the new owner/landlord of the properties in entering into the (financial) sale and leaseback transaction; by collecting the rental income the owner/landlord earned the moneys required for him to repay the loan granted to him (for the purpose of paying the purchase price of the properties to the original owners).

In its judgment, the Dutch Supreme Court did not enter into the merits of the arguments put forward on behalf TEP. It merely repeated its doctrine developed in the Aukema qq/Uni-Invest case and signalled that that doctrine also applied to the rental agreement in the matter at hand and that this was not changed by the fact that the rental agreement formed part of a sale and leaseback transaction nor by the fact that such a transaction was specifically used to obtain new financing.

The conclusion from this case seems to be that the Aukema qq/Uni-Invest doctrine also applies to the "leaseback" leg (rental agreement) of a sale and leaseback transaction even if such a transaction is used as a means for the original owner/seller to obtain financing.

Overall conclusions

The doctrine developed in the Aukema qq/Uni-Invest case seems to have firmly taken root (Part I of this series).

The doctrine also applies to guarantors (*borgen*) of the obligations of tenants, who, although they are bound to the terms of their guarantees (*borgstellingen*), cannot file their recourse claims (*regresvorderingen*) against such tenants in the bankruptcy of such tenants (Part II of this series), to the extent that such claims exceed the non-verifiable "part" of the landlord's contractual claim for indemnification because of early termination of the relevant rental agreement.

The doctrine also applies to rental agreements forming part of financial sale-and-lease-back transactions (Part III of this series).

Observations

The foregoing gives rise to the following observations from our part.

In the Aukema qq/Uni-Invest case, the Dutch Supreme Court decided that the doctrine developed in that case should be distinguished from its decision of 13 May 2005 in the BaBy XL case (JOR 2005/222, m.nt. Van Andel). In that case the landlord terminated the rental agreement and claimed damages from the tenant on the basis of what was agreed to in the rental agreement. However, the Dutch Supreme Court denied the claim put forward by the liquidators in the bankruptcy of BaBy XL that such termination and claim of damages were in violation, inter alia, of section 39 DBA.

Therefore, as long as the landlord terminates the rental agreement before the liquidator, this termination and the ensuing claim for damages based on what has been agreed in those respects in the rental agreement will be valid and effective, including in the bankruptcy of the tenant.

So far banks issued a bank guarantee in respect of the obligations of the tenant(s), have remained outside the firing line of liquidators, although bank guarantees played a prominent role both in the Aukema qq/Uni-Invest case and in the TEP/Autodrome case. In light of the decision in the second case (Romania Beheer), we fear that it will just be a matter of time before liquidators will wake up to this possibility, with potentially disastrous consequences for the guaranteeing banks' recourse claims (*regresvorderingen*) against the tenant(s) and the value of the security obtained by such banks from the relevant tenant(s) in respect of such claims.

We believe that the conclusions set out in the last two bullet points of our April 2011 client briefing (page 2) are even more compelling following the Dutch Supreme Court's decisions in the two most recent cases discussed in this client briefing. Please click here for the text of those bullet points.

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