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ASR/Achmea aftermath: Dutch Supreme Court reconfirms validity of security surplus arrangements in highly anticipated ruling

In this client briefing we explain the importance of this ruling for the Dutch finance and restructuring practice and summarize the various legal elements and related issues of security surplus arrangements (*overwaarde-arrangementen*) which are frequently applied by financiers in the Netherlands.

The validity and enforceability of security surplus arrangements (*overwaarde-arrangementen*) in bankruptcy has been a hot topic in the Dutch finance and restructuring practice. Recently, several trustees in bankruptcy (*faillissementscuratoren*) have tried to contest the validity of such arrangements. Although the validity of the security surplus arrangements in case of bankruptcy of the security provider was upheld in several district court rulings in the Netherlands, the discussion about this topic continued, especially after the ASR/Achmea ruling. To obtain certainty about the validity of security surplus arrangements the Dutch Supreme Court (*Hoge Raad*) was requested to issue a preliminary ruling (*prejudiciële vraag*) in respect of the enforceability and validity of the security surplus arrangement in the bankruptcy of the security provider. The preliminary ruling by the Supreme Court was given on Friday 16 October 2015. The Supreme Court ruled that security surplus arrangements are valid and enforceable in case of bankruptcy of the security provider, provided that the security provider is or becomes a party to the arrangement.[i]

The Dutch Supreme Court ruled on 16 October 2015 that:

- security surplus arrangements (*overwaarde-arrangementen*) are (still) valid and enforceable
- the security provider must be a party to the security surplus arrangement
- parties to an agreement can stipulate the moment of contractual recourse claims coming into existence (thereby allowing those claims to be pledged immediately)

What exactly is a security surplus arrangement under Dutch law?

An ordinary security surplus arrangement under Dutch law will involve two or more financiers that (i) provide bilateral financing (each a "**Loan**") to a common obligor (the "**Obligor**") and (ii) wish to have a mutual right of recourse to any surplus security proceeds which one financier receives as a result of enforcing its security over the assets of such Obligor (in the event that the other financier's security is insufficient to discharge the Loan it advanced to the Obligor).

The mechanics of a security surplus arrangement are typically as follows. Each financier will guarantee the payment of the Loan granted by the other financier to the Obligor by making use of a suretyship (*borgtocht*). The suretyship gives a financier the right to claim payment of the Loan from the other financier(s) in the event that the Obligor does not discharge its Loan in full. The arrangement is usually structured in such a way that cross-defaults trigger acceleration of the Loans granted by the financiers, as a result of which the security created in favour of each financier becomes enforceable. A financier

does not incur any liability under the suretyship with respect to the Loan granted by another financier beyond the net value of the proceeds of the security it holds (the "net" value is determined by deducting all amounts which the Obligor owes to the financier under its Loan from the gross security proceeds). Accordingly, the financiers' right to claim payment from another financier under the suretyship is limited to the net proceeds of the security which such other financier holds.

The most important aspect of a security surplus arrangement is that the recourse right (*regresrecht*) which the enforcing financier will have vis-à-vis the Obligor (after paying the other financier under the suretyship) is treated as a secured claim under the security it holds. In this way, any payment made under the suretyship will result in a secured recourse claim which may then be repaid from the proceeds of enforcement of the security granted by the Obligor.

Uncertainty caused by Supreme Court ruling in ASR/Achmea (2012)

The validity and enforceability of security surplus arrangements as described above was already explicitly approved by the Supreme Court in its ruling dated 9 July 2004 (Bannenberg q.q./NMB Heller).[ii] Therefore, from this ruling onwards there had been little debate in Dutch legal literature and practice as to the enforceability and validity of a security surplus arrangement. This situation changed, however, in 2012 due to a Supreme Court ruling dated 6 April 2012 (ASR/Achmea), whereby it was decided that recourse claims – contrary to prevailing views in Dutch legal literature at that time – are future claims and only come into existence after the debtor or surety has paid its obligations vis-à-vis the creditor.[iii] This ruling by the Supreme Court raised the question if the once approved security surplus arrangements are still valid and enforceable in case the enforcing financier pays the creditor under the suretyship (ie the other financier) after the Obligor was declared bankrupt.

A request for preliminary ruling from the Dutch Supreme Court

Although the majority opinion in Dutch legal literature was that security surplus arrangements would still be valid in case the financier acting as surety pays the other financier in its capacity as creditor after the Obligor has been declared bankrupt, several trustees in bankruptcy tried to contest the validity and enforceability of the security surplus arrangements. Up and until now these attempts by trustees have been unsuccessful, and two district court rulings made clear that the Supreme Court ruling in ASR/Achmea had in their view not altered the effectiveness of security surplus arrangements in the bankruptcy of the Obligor.[iv]

Another district court then asked the Supreme Court for a preliminary ruling.[v] The Supreme Court was asked to answer the following main question: can a recourse claim that arises after the bankruptcy of the Obligor still be used to take recourse against the proceeds of enforcement of the security rights which were granted by the bankrupt Obligor? A related question that the Supreme Court has been asked to answer is whether the Obligor will have to be a party to the security surplus arrangement in order for it to be valid and enforceable in the Obligor's bankruptcy. The answer to both questions was highly anticipated.

By answering the questions it was asked in connection with the preliminary ruling the Supreme Court has upheld its earlier ruling of Bannenberg/NMB Heller and has made clear that security surplus arrangements still lead to valid and enforceable recourse claims of the enforcing financier vis-à-vis the Obligor, even if those recourse claims arise after the Obligor's bankruptcy. While having the Obligor co-sign the arrangement was in each case considered to be the prudent way to act for a financier, we now know that the security provider being a party to the arrangement is also crucial for the validity and enforceability of a security surplus arrangement. The actual act of becoming a party to the arrangement (preferably by co-signing the arrangement) can still be performed by the Obligor after the financiers have entered into the contract of suretyship. It will depend on the interpretation of all facts and circumstances whether or not the Obligor has become a party to the security surplus arrangement. Making use of an irrevocable power of attorney granted to each financier to act as attorney (*vertegenwoordiger*) of the Obligor should also suffice in this respect (provided it is not used just prior to the bankruptcy of the Obligor).

A bonus ruling relevant for the Dutch finance and restructuring practice

Finally, the Supreme Court also mitigated the practical consequences of its ASR Achmea ruling of 2012 in this preliminary ruling. The Supreme Court stated that parties can stipulate that a contractual recourse claims will come into existence from the moment of the entering into by all parties of the security surplus arrangement. This means that alongside of the statutory recourse claim which only

comes into existence after the debtor or surety has paid its obligations vis-à-vis the creditor, there is also room for a contractual recourse claim that already exists. This ruling is relevant not only in the context of security surplus arrangements, but also in other financing transactions whereby recourse rights are pledged and/or subordinated. Making use of the option of the already existing contractual right of recourse will allow for the valid creation of a right of pledge which – contrary to what is the case when pledging statutory recourse rights – cannot be frustrated by a subsequent bankruptcy of the pledgor.

[i] Supreme Court 16 October, ECLI:NL:HR:2015:3023 (De Lage Landen/Van Logtestijn q.q.).

[ii] Supreme Court 9 July 2004, NJ 2004, 618 (Bannenberg q.q./NMB Heller)

[iii] Supreme Court 6 April 2012, JOR 2014/172 (ASR/Achmea).

[iv] District court Amsterdam 27 August 2014, JOR 2014/318 (ING Commercial Finance/Ingwersen q.q.) and District court Amsterdam 17 September 2014, JOR 2015/23 (Jongepier q.q./Rabobank & De Lage Landen).

[v] District court Middle Netherlands 8 October 2014, JOR 2015/24 (De Lage Landen/Van Logtestijn q.q.).

Contacts

Guido Bergervoet
+31 20 711 9534
guido.bergervoet@cliffordchance.com

Ilse van Gasteren
+31 20 711 9272
ilse.vangasteren@cliffordchance.com

Jelle Hofland
+31 20 711 9256
jelle.hofland@cliffordchance.com

Erwin Bos
+31 20 711 9220
erwin.bos@cliffordchance.com

Mirjam van der Kaay
+31 20 711 9372
mirjam.vanderkaay@cliffordchance.com

Evert Verwey
+31 20 711 9681
evert.verwey@cliffordchance.com