

The Dutch Pre-Pack: An Alternative on the Rise?

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Introduction

1 Pre-pack practice has been a “hot issue” in both the United Kingdom and in the Netherlands for the last couple of years. In the UK, pre-pack practice has been heavily criticised. In 2014, Teresa Graham published a Report in which she reviewed pre-pack practice.¹ Graham set out six recommendations for improving the practice, especially with regard to the so called ‘connected party sales’. Furthermore, the Joint Insolvency Committee launched a consultation on a revised draft of Statements of Insolvency Practice number 16 in 2015. In January 2016 the House of Commons published a briefing paper discussing the current position of the pre-pack.² With the revision of the Dutch Insolvency Act, the Dutch have introduced a legislative framework for their pre-pack practice in the *Wet Continuïteit Ondernemingen I*.³ The Dutch pre-pack is derived from English practice, but different on many levels. In recent case law, the Dutch court referred preliminary questions to the European Court of Justice (the “ECJ”) about the applicability of the Acquired Rights Directive (the “ARD”).⁴ In this article, pre-pack practice in both the UK and the Netherlands will be discussed. The focus will be on the role of the creditors and the protection of employee rights. It will be assessed whether the Dutch proposed pre-pack regime can be an alternative to the English pre-pack in international restructurings.

Corporate rescue regimes in the UK and the Netherlands

2 First, it is necessary to briefly introduce the concept of corporate rescue and the regimes in the UK and the Netherlands. One could say that the best possible outcome for a company in case of a corporate rescue procedure is ‘to overcome its difficulties and be restored to financial health, with the survival of the company as an entity and no changes in ownership’.⁵ A distinction must be made between corporate rescue

¹ T. Graham, ‘Graham Review into Pre-pack Administration June 2014’, Report to the Honorable Vince Cable MP.

² L. Conway, House of Commons Briefing Paper January 2016.

³ *Kamerstukken II* 2014/15, 34 218, 2.

⁴ 2001/23/EC of 12 March 2001; Rb. Midden-Nederland, 24 February 2016, ECLI:NL:RBME:2016:954.

⁵ R. Parry, *Corporate Rescue* (2008, Sweet and Maxwell, London), at 2.

and business rescue. Rescuing a company in its purest form would leave the corporate entity intact with the same operations and the same people in charge. Business rescue, or 'corporate recycling' as it is called by Frisby,⁶ involves the sale of the business or part of the business to a third party. Therefore, after the business sale, the business is transferred to new owners and the corporate entity is left behind as an 'empty shell'. This empty shell will then be liquidated.

3 In many cases it might be feasible to sell the business or to sell the company's assets on a piecemeal basis before liquidating the company. The proceeds can then be used to pay off the creditors.⁷ In other cases, the business might not be worth rescuing; for example when the business model is out-dated or the competition too strong. In these cases it might be better to liquidate the company and to not aim for the rescue of the company or its business. In order to determine what route is most desirable, the insolvency practitioner must be able to decide what the best decision under certain circumstances will be. Therefore, it can be argued that a well-designed corporate rescue system should offer flexibility to the insolvency practitioner and give the opportunity to come to the best possible solution for the debtor and the creditors as a whole on the basis of these circumstances.⁸ Most corporate rescue laws operate on the assumption that the value of the company will be higher if the company itself or its business is preserved as a going concern instead of focussing solely on the liquidation of the company.⁹ It has been acknowledged that corporate rescue is a necessary alternative to liquidation in each insolvency system.¹⁰ The insolvency practitioner must be able to achieve the best possible outcome for the creditors as a whole within minimum time and with minimum expense.

The United Kingdom

4 Corporate rescue in the UK is mainly facilitated by the use of the administration procedure.¹¹ However, although the focus of the administration procedure is on rescuing the company as a going concern, the administrator is not obliged to rescue the company at all costs. In practice, an administration procedure with the continuation of the company as a result is quite rare.¹² In fact, the term 'corporate rescue' might be misleading since many cases labelled as successful corporate rescues actually involve the liquidation of the company and the sale of the business. If the administrator finds that, under the specific circumstances of a case, the rescue of a company as a going concern is not an option, he may look for alternative solutions. In such a case the administrator can shift his focus to saving the business or liquidating the company instead of trying to rescue the company as a going

⁶ S. Frisby, "In Search of a Rescue Regime: The Enterprise Act 2002" (2004) 67(2) *M.L.R.* 247, at 249.

⁷ Parry, above note 5, at vii.

⁸ *Ibid.*

⁹ K. Gromek Broc and R. Parry (eds), *Corporate Rescue: An Overview of Recent Developments* (2006, Kluwer Law International, Alphen aan den Rijn), at 2.

¹⁰ *Ibid.*

¹¹ V. Finch, "Corporate Rescue: who is interested?" (2012) *J.B.L.* 190, at 193.

¹² Parry, above note 5, at 15.

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concern.¹³ Rescuing the company as a going concern is intended to mean ‘the company and as much of its business as possible’.¹⁴ It can be argued that this essentially gives primacy to saving the business of the company if this will lead to better results for the creditors as a whole.¹⁵

5 Several studies have indicated that the costs of the administration procedure have risen since the Enterprise Act 2002 (“EA 2002”) was introduced. However, so have the realisations of the procedures; in addition, administrations are completed more quickly.¹⁶ The number of administrations has risen, allegedly because of the possibility of an out of court appointment and the possibility of a focus on business rescue.¹⁷ These changes in the administration procedure have led, amongst other reasons, to a significant rise of the pre-pack.¹⁸

The Netherlands

6 The Dutch “*faillissements*” (hereafter: liquidation) procedure aims at the winding up of the company. However, in practice the liquidation procedure is also used as the most important instrument for the reorganisation and continuation of businesses in financial difficulties.¹⁹ A big advantage of this procedure can be found in the rules governing employment contracts. Since the liquidation procedure is aimed at the winding up of the company, the ARD excludes the automatic transfer of employment contracts upon the transfer of the business.²⁰

7 Though at first sight the Dutch Insolvency Act (“DIA”) does not seem very rescue-orientated, the liquidation procedure can be used quite effectively for restructuring purposes. The liquidation procedure gives two possible routes for the continuation of the business or company. First, there is an option for liquidation compositions. The liquidation composition must be offered to all ordinary creditors who can adopt the proposal by a simple majority that together represents at least half of the debts.²¹ The proposal often consists of an offer to partially pay the debts after which the total amount of these debts will be discharged.²² A major advantage of this procedure is the court approval and the binding of a dissenting minority of ordinary creditors.

¹³ IA 1986 Sch B1, para. 3(3)(b).

¹⁴ Paragraph 647 of the Explanatory Notes to the Enterprise Act 2002.

¹⁵ V. Finch, *Corporate Insolvency Law: Perspectives and principles* (2009, Cambridge University Press, Cambridge), at 383.

¹⁶ R. Goode, *Principles of corporate insolvency law* (2011, Sweet and Maxwell, London), at 473.

¹⁷ Finch, above note 15, at 393-394.

¹⁸ G.M. Weisgard and M. Griffiths, *Company Voluntary Arrangements and Administrations* (2013, Jordan Publishing Limited), at 299.

¹⁹ N.E.D. Faber and others (eds), *Commencement of Insolvency Proceedings* (2012, Oxford University Press, Oxford), at 427.

²⁰ Article 5 (1) ARD; Article 7:666 section 1 Dutch Civil Code (hereafter : ‘DCC’).

²¹ Articles 138 and 145 DIA; an exception can be made under the conditions mentioned in Article 146 DIA.

²² Groenewegen and Van Buren-Dee, *Tekst & Commentaar Insolventierecht* (2014, Kluwer, Deventer), art. 138 DIA, aant. 4.

After the court approval the liquidation procedure comes to an end without liquidating the company (article 161 DIA). Therefore, the liquidation composition gives the possibility to restructure the debts within the same legal entity.²³ However, these liquidation procedures are used very rarely in practice. The fact that the composition only works against the unsecured creditors is a major drawback.²⁴

8 This second route involves the asset transaction in liquidation, also known as ‘restarts’. The Dutch pre-pack is derived from these restarts. As part of a restart the assets of a company are sold followed by the liquidation of the corporate entity as an “empty shell”.²⁵ Big advantages of this asset sale by the trustee are the speed of the procedure and the private element of the sale.²⁶ In contrast to the composition plan, the asset sale does not require public voting within a creditor meeting. The consent of the supervisory judge is required just as the permission of some of the secured creditors to sell the encumbered assets which are secured by their security rights.²⁷ Most restarts of business are based upon these asset transactions followed by liquidation.

The pre-pack

9 In a nutshell, the pre-pack involves the sale of a business, which is pre-arranged before the formal insolvency of the company. Immediately after the formal opening of the insolvency procedure, the business sale is executed. The lack of transparency of the process is an often criticised aspect of the pre-pack in both the UK and the Netherlands. More particularly; the concerns in the UK are focussed on the ‘connected party sales’, possible conflict of interest of an insolvency practitioner and the lack of involvement of the unsecured creditors.²⁸ In the Netherlands the main concern has been the applicability of the ARD.

10 The pre-packaged business sale in the UK can be described as ‘the pre-arranged sale of all or part of the company’s business before the company enters formal insolvency proceedings, with the sale executed at or soon after the formal appointment of the administrator’.²⁹ The administrator, also referred to as the putative or prospective administrator,³⁰ will be introduced to the company’s directors and business before formally appointed. If a buyer is found, the sale is negotiated and at a pre-arranged time the administrator is formally appointed out of court to

²³ J.A.A. Adriaanse, *Restructuring in the shadow of the law: Informal reorganisation in the Netherlands* (2005, Kluwer, Deventer), at 16.

²⁴ *Ibid.*

²⁵ *Ibid.*

²⁶ L. Kortmann, “Improved pre-packs: going Dutch”, (2012) *Corporate Rescue and Insolvency* 225, at 225.

²⁷ *Ibid.*, at 226.

²⁸ Conway, above note 2, at 3.

²⁹ Graham, above note 1, at 14.

³⁰ J. Armour, ‘The Rise of the ‘pre-pack: Corporate restructuring in the UK and proposals for reform’, in: R.P. Austin and F.J.G. Aoun (eds), *Restructuring Companies in Troubled Times: Director and Creditor Perspectives* (2012, Ross Parsons Centre, Sydney); Goode, above note 16, at 413.

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immediately execute the sale of the business.³¹ This way the business can be transferred fast and there is no influence of the chaos that might emerge in case of a formal administration procedure. Therefore, business can continue ‘as usual’ with new or the same management in charge.³² Pre-packs are commonly used for the restructuring of businesses that highly depend on their intellectual property or businesses in the service industry whose goodwill and value will evaporate at the slightest hint of insolvency.³³ Furthermore, businesses that heavily depend on the skills and knowhow of their employees can suffer marginally if these employees decide to leave due to the formal insolvency proceedings.³⁴ The English pre-pack procedure has proven to be a very successful restructuring mechanism, not only on domestic, but also on international level. Big insolvent enterprises shifted their centre of main interest to the UK in order to use the advanced insolvency procedures.³⁵ It seems that, even though one acknowledges the problems surrounding the pre-pack, the merits of the procedure are generally outweighing these forms of criticism. The forum shopping of big enterprises towards the UK is a source of ‘inward investment’ and, according to Graham, should be perceived as a positive advantage to the economy.³⁶

11 With the proposed Dutch pre-pack a debtor who approaches insolvency, but is not yet insolvent,³⁷ can request the court to appoint an intended trustee. This intended trustee is the insolvency practitioner who is likely to be appointed as trustee in case of a liquidation procedure.³⁸ With this request, the debtor has to prove that the appointment of the intended trustee will have “added value”. Added value is present in at least two cases: when the debtor can show that the preparation by an intended trustee can limit the damage for the stakeholders in the case of a potential liquidation procedure, or when he can show that the preparation in secrecy can increase the value and job preservation to such an extent that this preservation outweighs the fact that the preparation is conducted in secrecy and lacks certain aspects of transparency.³⁹ If the court considers this added value present, an intended trustee can be appointed for a maximum of two weeks.⁴⁰ Furthermore, the court can make the appointment of the intended trustee subject to certain conditions, such as the involvement of the representatives of the employees or the unions.⁴¹

³¹ Armour, above note 30, at 16.

³² M. Hyde and I. White, “Pre-packed administrations: unwrapped” (2009) *Law and Financial Markets Review* 134, at 134.

³³ M. Ellis, “The Thin Line in the Sand: Pre-packs and Phoenixes” (2006) *Recovery (spring)*, at 3.

³⁴ Parry, above note 5, at 16.

³⁵ For example Hellas Telecommunications, which resulted in the UK’s biggest pre-pack administration.

³⁶ Graham, above note 1 at 7.

³⁷ Proposed article 363 sub 1 DIA; The debtor may not yet be insolvent since he has to be able to pay the salary of the intended trustee as well as the debts that fall due in short term.

³⁸ Proposed article 363 sub 1 first sentence DIA.

³⁹ Proposed article 363 sub 1 third sentence DIA.

⁴⁰ Proposed article 363 sub 3 DIA. For the extension of the period the debtor has to prove once again that the appointment will have added value. Before the extension of the period, the court will hear the intended trustee and the intended supervisory judge.

⁴¹ Proposed article 363 sub 4 DIA; *Kamerstukken II* 2014/15, 34 218, 3, at 14 (MvT).

The unsecured creditors

12 In most of the pre-packed administrations the unsecured creditors are ‘out of the money’ and receive very little, if anything at all, from the distribution of the empty corporate shell.⁴² The statutory priority for distribution in insolvency places the unsecured creditors almost at the bottom of the line in both the UK and the Netherlands. Since a return out of an ordinary administration procedure is rare for the unsecured creditors, the fact that the unsecured creditors receive very little out of the proceedings is not the main problem. The questions whether there is adequate legal protection to ensure that the pre-pack truly obtained the highest possible price and whether the practitioner paid enough attention to the rights and interest of the unsecured creditors, are the main concerns.⁴³

13 When unsecured creditors believe that their interest is not adequately protected, they can file for a breach of duty of the administrator to act in the interest of the creditors as a whole.⁴⁴ However, in practice this translates into additional costs which essentially means that the unsecured creditors will not file for such a breach. Moreover, it is very difficult to establish a breach of duty since the commercial judgements of the administrators are rarely challenged by the courts.⁴⁵ It seems that the unsecured creditors have to deal with the fact that they will not get much, if anything at all, out of the insolvency. However, the SIP 16 statements and the involvement of an administrator should at least provide the unsecured creditors with the necessary information after the business has been sold.

14 In the Netherlands the intended trustee and the intended supervisory judge are involved in the process to watch over the debtor and make sure the interests of the unsecured creditors and employees are not neglected.⁴⁶ Since most of the creditors are not involved in the preparation process, the responsibility on the intended trustee and intended supervisory judge is even bigger than would be the case in an ‘ordinary’ liquidation procedure.⁴⁷ They have to make sure that the interest of all parties are taken into account because the unsecured creditors and employees are not involved in the process. Except for the interest of the creditors as a whole, the intended trustee should keep in mind the ‘interest of the society as a whole’, such as the preservation of jobs, knowledge and the productivity.⁴⁸

⁴² ‘Out of the money’ meaning that after the expenses and return to the preferential and secured creditors, there will be no return for the unsecured creditors.

⁴³ Armour, above note 30, at 19.

⁴⁴ IA 1986, Sch. B1, para. 3(2).

⁴⁵ Weisgard and Griffiths, above note 18.

⁴⁶ *Kamerstukken II* 2014/15, 34 218, 3, at 7 (MvT).

⁴⁷ *Ibid.*

⁴⁸ *Ibid.*, at 18.

The secured creditors

15 Neither the Graham Report nor the Dutch proposed legislation assess the role that will be played by the secured creditors in a pre-pack.⁴⁹ It has been argued that it is the degree of certainty and control for the secured creditors in a pre-pack that makes the procedure so attractive and successful.⁵⁰

16 Administrative receivership was abandoned after the introduction of the EA 2002 with the idea that there was too much power in the hands of the floating charge holder.⁵¹ However, it has been argued that the pre-pack has in fact replaced this administrative receivership and maybe provided the secured creditors with even more power than they used to have under the pre-Enterprise regime.⁵² One could say that, as long as the banks do not suffer too much from the insolvency of the company, they are quite keen on keeping the lending in place for the NewCo.⁵³ It stands out that most of the critical literature is focused on the lack of transparency or the role of the unsecured creditors and it seems that the role played by the secured creditors is relatively untouched.

17 The EA 2002 provides for the general enforcement of the floating charge to be carried out through the administration procedure.⁵⁴ The out of court appointment by the QFCH has proven to be the chief means by which a floating charge holder will enforce its debt.⁵⁵ However, before the floating charge can be a 'qualified floating charge', the floating charge itself as well as the holder of the floating charge has to meet certain conditions.⁵⁶ One of these conditions is the requirement that the floating charges holders' security interest must relate to the whole, or substantially the whole, of the company's property.⁵⁷ If the floating charge holder does not meet the requirements, the only other opportunity is the court appointment of the administrator.⁵⁸ Without the use of an administrator, there is no option for the floating charge holder to enforce their security right.⁵⁹

18 The consent of the bank is most likely required to appoint an administrator out of court.⁶⁰ Therefore, it has been argued that most pre-packs are enforced and

⁴⁹ 'Secured creditors' and 'banks' will be used exchangeable from here on.

⁵⁰ S. Harris, "The Decision to Pre-Pack" (2004) *Recovery (Winter)* 26, at 27.

⁵¹ Parry, above note 5, at 10.

⁵² P. Walton, "Pre-packaged administrations – trick or treat?" (2006) 19(8) *Insolvency Intelligence* 113, at 116.

⁵³ W.E. Moojen, "Banken ook bij pre-pack bepalend voor uitkomst" *FD* 18 September 2014.

⁵⁴ Finch, above note 15, at 381.

⁵⁵ Parry, above note 5, at 44.

⁵⁶ IA 1986, Sch. B1, para. 14 (2) and (3).

⁵⁷ IA 1986, Sch. B1, para. 14 (3).

⁵⁸ Parry, above note 5, at 45.

⁵⁹ Finch, above note 15, at 44.

⁶⁰ C. Mallon and S.Y. Waisman (eds), *The Law and practice of restructuring in the UK and US* (2011, Oxford University Press, Oxford), at 232.

empowered by the banks as a tool to maximise their own returns on security rights.⁶¹ It might be hard to convince an outsider that the English administrator is not biased when he is appointed out of court by, or at the prompting of, a secured creditor. Especially when the business is sold to the management and the secured creditors are not harmed and actively involved in this process, this might create a perception of a ‘willy-nilly’ deal between the bank and the debtor.⁶²

19 Such an out of court appointment is not possible in the Netherlands. This could indicate that there might be less influence of the secured creditors on the insolvency practitioner. Moreover, the Dutch proposed pre-pack cannot be started by another party than the debtor himself.⁶³ However, this does not necessarily mean that the banks will not have influence in the process. The banks in the Netherlands who have security rights on the assets of the debtor will have a position as a ‘*separatist*’ in liquidation procedures.⁶⁴ This essentially means that, at any moment of default, either during or outside liquidation, the pledgees and mortgagees may exercise their rights as if there was no liquidation procedure.⁶⁵ They may exercise these foreclosure rights without having to obtain a court approved enforcement order. This provides the secured creditor with a very strong bargaining position, since the debtor and trustee will always have the threat of the secured creditor taking recourse at the assets when the debtor is in default. The secured creditor thereby has the possibility to block the going concern sale of the business.⁶⁶ Moreover, post-petition financing shall only be provided by these banks if they are optimistic about the continuation of the business. Therefore, it can be argued that there is in fact little power in the hands of the debtor or the trustee on its own.⁶⁷ It should be noted that the banks are within the group that have expressed their support in the development of the Dutch pre-pack.⁶⁸

20 It has been stated that the reason that banks have so much influence is that the Dutch as well as the English businesses are often over-collateralised.⁶⁹ The process of over-collateralisation essentially entails the posting of more collateral than is needed to obtain or secure financing. Therefore, the banks will have security on (almost) everything owned by the debtor and when the insolvency of a debtor occurs, it is the secured creditor who obtains almost everything and very little, if any, is left for the unsecured creditors. Banks often prefer to provide the NewCo with credit when this offers perspective that their full loan will be repaid in the future. With the intensive care departments of banks, permanent control is kept on the loans and

⁶¹ N.W.A. Tollenaar, “Faillissementsrecht van Nederland: geef ons de pre-pack!” (2011) 23 *TvI* 130, at 138.

⁶² S. Davies, “Pre-pack – he who pays the piper calls the tune” (2006) *Recovery (summer)* 16, at 17.

⁶³ It is of course possible that banks will exercise pressure on the debtor to start a procedure.

⁶⁴ Article 57 DIA.

⁶⁵ Articles 3:248; 3:268 DCC and Article 57 DIA.

⁶⁶ J.M. Hummelen, “Het verkoopproces in een pre-packaged activatransactie” (2015) 2 *TvI*, at 14.

⁶⁷ J.H.S.G.K. Timmermans, ‘De curator en het boedelkrediet’ in: J.G. Princen and A. van der Schee (eds), *De ondernemende curator* (2011, Kluwer, Deventer) at 68.

⁶⁸ M.H.F. van Vught, “De Nederlandse pre-pack: time-out, please!” (2014) 1 *F.I.P.* 26, at 26.

⁶⁹ Moojen, above note 53.

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finance of the debtors. It can be questioned what the consequences of these high stakes and over-collateralisation are for the influence of the banks in the pre-pack.

21 An essential part of the pre-pack in both jurisdictions is the continuation of finance after the liquidation or administration procedure has started. It seems that, as long as the banks receive (almost) all their outstanding credit out of the business sale, they are willing to continue financing in the NewCo.⁷⁰ Without this new credit from either the secured creditor or a new investor, the NewCo will be doomed to fail. It has been argued that, because the banks are willing to continue the financing as long as their debts are fulfilled, the purchaser will be able to buy the assets at 'rock-bottom' value and nothing will be left for the unsecured creditors, nor for the equity.⁷¹ As long as a purchaser is found and the secured creditor is satisfied, it is likely that insolvency practitioner will agree with the sale.⁷²

22 If one compares the position of the separatist in the Netherlands with the QFCH in the UK, it can be argued that the Dutch secured creditors have a more powerful position. The Dutch secured creditors may simply ignore the liquidation procedure and enforce their foreclosure right without using the court or a formal insolvency procedure.⁷³ However, there is the possibility of a moratorium for the maximum period of 4 months ordered by the supervisory judge.⁷⁴ In this period the secured creditors will not be allowed to take recourse to the assets of the debtor without the approval of the supervisory judge. In neither of the jurisdictions the pre-pack can be executed without the release of the banks. In the UK, the enforcement of the floating charge has to go through an administration procedure, giving the banks a major degree of leverage in both jurisdictions. One could say that the banks in the UK have a major influence on the pre-pack since an out of court administrator is often appointed at the prompting of the banks. However, the banks want to avoid being directly associated with a failed company. Therefore, it will most likely be the company or directors that appoint the administrator, but at the prompting of the banks. In the Netherlands on the other hand, the banks have a very strong position and a lot of influence in the process as separatist. However, the court, intended supervisory judge and intended trustee are involved in the procedure to provide the necessary checks and balances. However, in general, the blessing of the banks is required in both jurisdictions since the secured creditors have to release their assets for the sale. Therefore, a pre-pack seems to be impossible in the UK as well as the Netherlands without the blessing of the secured creditors.

23 It has been argued that the fact that under the proposed Dutch legislation it is the debtor, and no one else who can request for the appointment of an intended trustee,

⁷⁰ Mallon and Waisman, above note 60, at 237-238.

⁷¹ Moojen, above note 53.

⁷² *Ibid.*

⁷³ Article 57 DIA.

⁷⁴ Article 63a DIA.

can be seen as an advantage over the English procedure.⁷⁵ Where the English out of court appointed administrator might create the perception of a bias towards the secured creditors or management, the Dutch intended trustee is court appointed and subject to control of the intended supervisory judge. This difference in manner of appointment and the degree of court control can create the perception that the Dutch intended trustee is less biased. However, the secured creditor will always be at the table together with the debtor, purchaser and insolvency practitioner.⁷⁶ Neither in the UK nor in the Netherlands the position of the secured creditor is subject to much discussion at the moment. The QFCH in the UK has an important role to play through the out of court appointment of the administrator and the post-petition financing of the debtor. The Dutch secured creditors will always be involved at a certain stage of the process since they have the possibility to take recourse on the assets at any moment of default. Without the consent of the banks, there is no way the debtor will be able to sell the assets, let alone the business in a pre-pack. The first and foremost reason being that in both jurisdictions the secured creditor has to provide a release in respect of the assets being sold.⁷⁷ In combination with the over-collateralisation, this means that the bank will have to provide a release on (almost) all assets of the debtor. Therefore, the banks will always be involved in the process.

24 It seems that it is in fact ‘he who pays the piper that calls the tune’.⁷⁸ The pre-pack provides the banks with an assured return and a high level of influence in the procedure.⁷⁹ It can be argued that the whole process is controlled by the banks and absolutely nothing will happen without the consent of the secured creditors.⁸⁰

Employee protection and the ARD

25 Insolvency and labour law often appear to be opposites. Labour law requires formal procedures, stakeholder influence and court involvement. Insolvency law on the other hand thrives on a quick and silent approach and freedom for the insolvency practitioner to determine what is best for the company.⁸¹ One of the main justifications for the pre-pack in the UK is the fact that it often saves jobs. A large number of the SIP 16 statements cite the preservation of jobs as one of the primary reasons to pre-pack.⁸² Furthermore, Graham found that in most cases (almost) all jobs are preserved after the use of a pre-pack.⁸³ However, the prospect of

⁷⁵ P.J. Frölich, “Redding en sanering: monomaan of modern paradigma? Over de pre-pack en dergelijke” (2015) *AA* 192, at 197.

⁷⁶ Hummelen, above note 66, at 14.

⁷⁷ Mallon and Waisman, above note 60, at 232.

⁷⁸ Davies, above note 62.

⁷⁹ A. Kastrinou, “An analysis of the pre-pack technique and recent developments in the area” (2008) *Company Lawyer* 259, at 262.

⁸⁰ Walton, above note 52, at 121.

⁸¹ R.M. Beltzer, “Continuïteit van ondernemingen en pre-pack – hoe het idee een Europese richtlijn mist” (2015) 23 *O&F* 32, at 35.

⁸² Graham, above note 1, at 24.

⁸³ *Ibid.*; Though the jobs are saved, the contracts and other arrangements might have been adapted.

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administration or liquidation is rarely well perceived by the employees.⁸⁴ It might therefore be reassuring for the English employees that the pre-packs do not constitute insolvency proceedings within the meaning of the ARD,⁸⁵ meaning that the ARD, implemented in the UK by the Transfer of Undertakings (Protection of Employment) Regulations (“TUPE”), applies to pre-packs. TUPE does not apply to proceedings that are aimed at the liquidation of the company. An important question therefore was whether the pre-pack is one of these procedures that is aimed at the liquidation of the company. The court held in the case of *OTG Ltd v Barke*⁸⁶ that, just as an ordinary administration procedure, pre-packs are not aimed at the liquidation of the company.⁸⁷ This means that pre-packs are not excluded from the application of TUPE. Furthermore, the court held that any dismissal made for the principal or sole reason of the transfer will automatically be unfair.⁸⁸ Employment contracts therefore continue to function as long as they are not terminated within 14 days of entering administration by the insolvency practitioner for economic, technical or organisational (ETO) reasons.⁸⁹ The position of the ARD and employees in the UK seems quite straightforward and the employees are fairly well protected.

26 The Dutch, on the other hand, have a different view with regard to the applicability of the ARD on their procedure. Although the best practice rules of Insolad⁹⁰ and the explanatory memorandum also point out the possible preservation of jobs as a big justification for the pre-pack,⁹¹ the applicability of the ARD was subject to a lot of discussion in the period of drafting the Dutch legislation. The Dutch Minister made it clear that, in his view, the ARD provisions do not apply to the pre-pack.⁹² Since it only becomes apparent what will happen to the undertaking *after* the company entered the liquidation procedure in a pre-pack procedure, the articles 7:662-7:666 DCC implementing the ARD do not apply to the proposed pre-pack procedure.⁹³

27 It can be argued that this makes it rather easy to get rid of personnel using a pre-pack procedure.⁹⁴ There already is very little protection for the employees in liquidation and they would not be protected by the ARD during the pre-pack. As one would suspect, the Unions did not agree to this practice and, following the restart of

⁸⁴ Hyde and White, above note 32, at 135.

⁸⁵ *OTG Ltd v Barke* [2011] B.C.C. 608.

⁸⁶ *OTG Ltd v Barke* [2011] B.C.C. 608. See also: *Oakland v Wellswood (Yorkshire) Ltd.* [2010] B.C.C. 263; *Key2law (Surrey) LLP v De’Antiquis (Secretary of State for Business, Innovation and Skills Intervening)* [2011] B.C.C. 375; *Pressure Coolers Ltd v Molloy* [2011] B.C.C. 894.

⁸⁷ *OTG Ltd v Barke* [2011] B.C.C. 608 [17].

⁸⁸ *Ibid.*, [31 (1) (b)].

⁸⁹ *Powdrill v. Watson* [1995] B.C.C. 319.

⁹⁰ Insolad is an association of Dutch insolvency lawyers.

⁹¹ *Kamerstukken II* 2014/15, 34 218, 3, at 27-30 (MvT).

⁹² *Kamerstukken II* 2014/15, 34 218, 3, at 34-37 (MvT).

⁹³ *Ibid.*

⁹⁴ M.R. van Zanten, “De beoogd curator, uitgegroeid van fly on the wall tot spin in het web” (2015) 35 *TvI* 2015 226, at 235-236; R.J. Van der Ham, “Liever failliet dan doorgaan met slecht personeel: over het risico van misbruik van de pre-pack” (2014) 5 *ArbeidsRecht* 15, at 18.

Dutch company Heiploeg, went to court.⁹⁵ In the decision by the sub-district court it was held that the employees were indeed not protected by the articles 7:662-7:666 DCC.⁹⁶ The sub-district court held that the ARD was not applicable in this procedure and followed the path set out by the legislator.⁹⁷ Furthermore, the sub-district court refused to interpret the Dutch articles more in the light of the ARD. It argued that the ECJ was clear about the criteria for the Dutch liquidation, restart and suspension of payments procedures in *Abels*.⁹⁸ Therefore, the sub-district court held that, only if the liquidation procedure in the pre-pack does not meet the criteria set in *Abels*, there will be reason to refer preliminary questions to the ECJ.⁹⁹

28 This uncertainty with regard to the applicability of the ARD led to the unions starting more cases. In the recent case of *Estro*¹⁰⁰ this has resulted in preliminary questions to the ECJ. In the pre-pack of Estro, around a thousand people lost their jobs, with 1600 employees keeping their jobs. The unions went to court, arguing that these kind of pre-packs are not aimed at the liquidation of the company but are in fact solely focussed on the ‘restart’ aspect of the liquidation procedure and that therefore the ARD should apply to the pre-pack. The Newco, called ‘Smallsteps’, referred to the case of *Heiploeg* and *Abels* and considers the matter an ‘acte clair’ or ‘acte éclairé’ since the ECJ systematically held that the ARD does not apply in a case of Dutch liquidation.¹⁰¹ The court decided to refer preliminary questions to the ECJ essentially as follows:

1. Is the Dutch liquidation procedure, preceded by a court-controlled pre-pack, which is explicitly focussed on the continuation of (parts of) the undertaking, compatible with the goal of the ARD and is the article 7:666 sub 1 sub a still compatible?
2. Does the ARD apply to cases where a court appointed intended trustee will prepare the sale of the business which will be sold immediately after the start of the liquidation procedure?
3. Does it make any difference whether the primary goal of the intended trustee in the pre-pack is the continuation of the business or the maximisation of the proceedings? And how should this matter be viewed if both the continuation and the maximisation of the proceedings are aimed for?
4. Is the date of the transfer of the undertaking the date of consensus between both parties *before* the liquidation procedure has started or is this the moment when the undertaking truly passes to the buyer?

⁹⁵ <http://www.fnv.nl/over-fnv/pers/persberichten/persarchief/2014/juli/868755-vakbonden_dagen_garnalenverwerker_heiplaag/> last accessed 22 March 2016.

⁹⁶ These articles implement the ARD in Dutch legislation.

⁹⁷ Rb. Overijssel, 28 July 2015, ECLI:NL:RBOVE:2015:3589, r.o. 4.4 and 4.5; *Kamerstukken II* 2014/15, 34 218, 3, at 34-37 (MvT).

⁹⁸ ECJ 7 February 1985/900C-135/83 (*Abels*).

⁹⁹ Rb. Overijssel, 28 July 2015, ECLI:NL:RBOVE:2015:3589, r.o. 4.5.5.

¹⁰⁰ Rb. Midden-Nederland, 24 February 2016, ECLI:NL:RBME:2016:954.

¹⁰¹ Rb. Midden-Nederland, 24 February 2016, ECLI:NL:RBME:2016:954, r.o. 5.4.

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29 One can wonder why these questions were raised in the first place. The pre-pack uses the liquidation procedure to achieve the restart, which is obviously aimed at the liquidation of the company and therefore not subject to the application of the Directive. The proposed procedure is in fact no more than an adapted version of the already existing restart procedure where the ARD is not applicable.¹⁰² What is the difference between the pre-pack and the ‘ordinary restart’ that requires the ARD to be applicable to the pre-pack? It has been argued that, though the ARD is quite clear on the subject of its applicability, the European case law is not and this might cause some friction.¹⁰³ The question has been raised whether, in order to determine the applicability of the ARD, one should look solely at the formal goal of a procedure or if one should take into account the more material conditions of a procedure as well.¹⁰⁴

30 In the case of *Dethier/Dassy*¹⁰⁵, later confirmed in the case of *Europièces/Sanders*,¹⁰⁶ the ECJ held that:

“It follows from that case-law that, in deciding whether the Directive applies to the transfer of an undertaking subject to an administrative or judicial procedure, the determining factor to be taken into consideration is the purpose of the procedure in question (*D’Urso and Others*,¹⁰⁷ paragraph 26, and *Spano and Others*¹⁰⁸, paragraph 24). However, as the Advocate General has stated in points 31, 41 and 45 of his Opinion, *account should also be taken of the form of the procedure in question, in particular in so far as it means that the undertaking continues or ceases trading, and also of the Directive’s objectives.*”¹⁰⁹

31 If one looks at this paragraph, it could be argued that the ARD in fact does apply to the Dutch pre-pack procedure, contrary to the statement made in the explanatory memorandum and ruled in *Heiploeg*. In that case, one should not look at the formal goal of the liquidation procedure but more at the material goal of the procedure, what is happening in fact?¹¹⁰ The liquidation procedure is then used as a ‘gateway’ to the restart through a pre-pack. In that case the liquidation procedure is primarily used to rescue the business instead of liquidation of the company. It has been argued that it is not unlikely that this will be the outcome of questions referred to the ECJ.¹¹¹ If

¹⁰² L.G. Verburg, “De doorstart in faillissement en het debiet van ‘662’” (2014) 8 *F.I.P.* 26, at 27-28.

¹⁰³ Beltzer, above note 81, at 36.

¹⁰⁴ Van Zanten, above note 94, at 236.

¹⁰⁵ ECJ 12 March 1998, C-319/94, ECLI:EU:C:1998:99, (*Dethier Équipement/Dassy and Sovam*).

¹⁰⁶ ECJ 12 November 1998, C-399/96, ECLI:EU:C:1998:532, (*Europièces/Sanders*).

¹⁰⁷ ECJ 25 July 1991, C-362/89, ECLI:EU:C:1991:326, (*D’Urso and others*).

¹⁰⁸ ECJ EG 7 December 1995, C-472/93, ECLI:EU:C:1995:421, (*Spano/Fiat*).

¹⁰⁹ ECJ 12 March 1998, C-319/94, ECLI:EU:C:1998:99, (*Dethier Équipement/Dassy and Sovam*) [25]; emphasis added.

¹¹⁰ R.M. Beltzer, “Overgang van onderneming en faillissement: over een blinde vlek bij curatoren of wishful thinking onder arbeidsrechtjuristen” (2014) 8 *F.I.P.* 21, at 22-23.

¹¹¹ Beltzer, above note 81, at 39.

one exclusively looks at the formal goal of the liquidation procedure in a pre-pack, one does not see that the procedure does not serve a liquidation purpose *in these particular cases*. Quite the opposite actually happens, namely, the liquidation procedure is used to facilitate a restart through a pre-pack and therefore is not aimed at the liquidation of the business.¹¹² The purpose of the ARD is to protect employees in the event of a transfer of undertaking, in particular to ensure that their rights are safeguarded.¹¹³ The Dutch proposed pre-pack procedure is, at least for now, not subject to the ARD and thereby a procedure with a relatively low level of protection for the employees is created, against the goals of the ARD.

32 It has been argued that, because the English pre-pack is subject to TUPE and the Dutch pre-pack is derived from English practice, the Dutch pre-pack should also be subject to the ARD.¹¹⁴ However, one should be wary in ‘copy pasting’ legislation from other jurisdictions and thereby simply coping with the decisions made in the other jurisdiction.¹¹⁵ It is not as simple as it seems and the labour laws in both jurisdictions are very different.¹¹⁶ One could argue that the fact that the Dutch redundancy laws are less flexible than the UK redundancy laws can justify the non-applicability of the ARD in the Netherlands. It has been argued that the applicability of TUPE in the UK will have far less influence on the results of a pre-pack than the applicability of article 7:662 BW would have on the results of the Dutch pre-pack.¹¹⁷

33 Verburg argues, by referring to *OTG/Barke*¹¹⁸ that the English system is very different from the Dutch pre-pack and that therefore the Dutch should not copy the applicability of TUPE in the UK.¹¹⁹ A decision has to be made in the Netherlands whether the procedure is aimed at liquidation *or* at the continuation of the business.¹²⁰ In the English administration procedure this distinction only becomes apparent when the administrator declares what statutory objects he is following.¹²¹ Since this intention only becomes apparent when the proposals are filed, the Court has chosen an ‘absolute’ rather than a ‘fact based’ approach in order to increase the legal certainty and ensure the easy approach of the procedure.¹²² It was held in *OTG/Barke* that the line between the procedures aimed at liquidation and at

¹¹² *Ibid.*, at 40.

¹¹³ *OTG Ltd v Barke* [2011] B.C.C. 608 [21.5].

¹¹⁴ P. Huffman and I. Zaal, “De toepasselijkheid van de Richtlijn overgang van onderneming bij insolvente ondernemingen” (2014) 98 *TAP* 167, at 172.

¹¹⁵ Verburg, above note 102, at 30.

¹¹⁶ *Ibid.*

¹¹⁷ *Ibid.*

¹¹⁸ *OTG Ltd v Barke* [2011] B.C.C. 608.

¹¹⁹ Verburg, above note 102, at 30

¹²⁰ *Ibid.*

¹²¹ *OTG Ltd v Barke* [2011] B.C.C. 608 [21.3].

¹²² *OTG Ltd v Barke* [2011] B.C.C. 608.

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continuation in the UK is a less clear line than the difference between liquidation and suspension of payments in the Netherlands.¹²³

34 The UK court chose the ‘absolute’ approach because it is too comprehensive to determine every case ‘fact based’.¹²⁴ One could argue that such an absolute approach should be applied in the Netherlands as well and that therefore the ARD should not apply to any case of liquidation. However, when one looks at the Dutch liquidation procedure, the ‘fact based’ result will be different from the formal goal of the liquidation procedure in many cases, especially pre-packs. Looking at the Dutch practice and the possibilities for a trustee, most of the time the liquidation procedure is the only possibility, within the insolvency laws, to truly achieve corporate rescue. The suspension of payment procedure has proved not to be a successful restructuring mechanism. This does not mean that every time the liquidation procedure is used, it is used to restart the company. It is however not uncommon that the liquidation of the company (the corporate shell) is the result, but the procedure was in fact aimed at the rescue of the business and not the liquidation of the company.

35 The big difference with regard to the position of employees between the UK and the Dutch procedure is the non-applicability of the ARD in the Netherlands. The UK has opted for the ‘absolute approach’ in *OTG/Barke* and the reason behind this is easy to grasp. The purpose of administration is generally not the liquidation of the company but rather the continuation of the business.¹²⁵ By using the absolute approach the legal certainty of the procedure will increase. Furthermore, a clear line will avoid the risk of difficult and unpredictable disputes about the administrator's intentions which would be undesirable for employment protection rights to depend upon.¹²⁶ As stated by the Employment Appeals Tribunal in *OTG/Barke*, ‘a bright-line rule has clear advantages.’¹²⁷ The Dutch have also opted for such a ‘bright line rule’, by not applying the ARD in any case of liquidation. However, one can question if this is a correct reading of the ARD. The Dutch procedure can draw a clear line between the pre-pack and liquidation procedure. As discussed before, the intended trustee is *formally* appointed, often to look at the possibilities of a restart through a pre-pack. It can be hard to justify to the employees and unions that, though the formally appointed intended trustee is looking at these possibilities and the procedure is developed to promote the corporate rescue culture, the procedure is aimed at the liquidation of the company rather than the continuation. The Dutch proposed pre-pack is a formal procedure and is easily distinguished from the ‘ordinary’ liquidation procedure which in fact is aimed at the liquidation of the company. Therefore, the absolute approach that every liquidation procedure in the

¹²³ The court hereby refers to the Abels-case, where the Dutch suspension of payments structure was held to be aimed at the continuation but the Dutch liquidation procedure was not. *OTG Ltd v Barke* [2011] B.C.C. 608 [8.4].

¹²⁴ *OTG Ltd v Barke* [2011] B.C.C. 608.

¹²⁵ C. Wynn-Evans, “TUPE, Administration and the Rescue Culture: *OTG Limited v Barke & Others* and Consolidated Appeals”, (2011) 4 *Industrial Law Journal* 451, at 455.

¹²⁶ *Ibid.*, at 456.

¹²⁷ *OTG Ltd v Barke* [2011] B.C.C. 608. [22].

Netherlands is aimed at the liquidation of the company and never at the continuation of the business might be too oversimplifying.

36 To sum up, the English and Dutch pre-pack differ marginally with regard to employment protection. It is not crystal clear that the ARD is not applicable as it is stated by the Dutch legislator or by the drafters of the proposal.¹²⁸ Hopefully the preliminary questions that were referred to the ECJ in the *Estro* case will provide clarity on the matter. What the consequences will be if the ARD is applicable to the Dutch pre-pack is unclear. One should also keep in mind the differences in redundancy laws in both jurisdictions. The UK has quite flexible redundancy laws and the pre-pack can function with the applicability of the TUPE. A pre-pack in the Netherlands on the other hand, will most likely fail if the ARD provisions will apply.

Conclusion

37 The economic crisis has prompted the move towards a more debtor friendly oriented insolvency regime in the European Union. The concept of rescue itself is being revisited¹²⁹ and business rescue is ranked at the top of the European insolvency law related agenda. The European Commission published a recommendation on a new approach to business failure and insolvency ‘to encourage Member States to put in place a framework that enables the efficient restructuring of viable enterprises in financial difficulty’ and to ‘give honest entrepreneurs a second chance’.¹³⁰ The Dutch have followed this route set out by the European Union and are moving their insolvency regime from the traditional ‘pay what you owe’ towards ‘business rescue’ by introducing the pre-pack in their insolvency regime.¹³¹ With this pre-pack, the Dutch are introducing a procedure that is already heavily criticised in the country of origin.

38 A pre-pack procedure in the UK cannot be completed without the involvement of the secured creditors, often banks or other financial institutions. The debtor needs the secured creditor to provide a release on the encumbered assets or else they cannot be sold. The creditors on the other hand need the administration procedure to take recourse on their secured assets. Therefore, the secured creditors are always involved in the process. A ‘pre-pack pool’ with independent experts as recommended in the

¹²⁸ A.M. Wolfram-van Doorn and E. Schmieman, “De Wet Continuïteit Ondernemingen I: een stevige eerste steen voor de nieuwe organisatiepijler” (2015) 34 *TvI* 220.

¹²⁹ P.J. Omar, “Upstreaming rescue: pre-insolvency proceedings and the European Insolvency Regulation” (2014) 25(1) *I.C.C.L.R.* 19, at 20.

¹³⁰ All the EU member states were invited to implement the principles of the recommendation. In the evaluation of this recommendation of the 30 September 2015 the Member States were asked to communicate to the Commission, on a yearly basis, data concerning the insolvency procedures. This evaluation can be found on <http://ec.europa.eu/justice/civil/files/evaluation_recommendation_final.pdf> last accessed: 22 March 2016.

¹³¹ Frölich, above note 75, at 193.

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Graham Report, might provide extra checks and balances to the process, this pool became operational on 2 November 2015.¹³²

39 The Dutch pre-pack essentially is an adapted version of the asset transaction in liquidation, also known as a ‘restart’. In the practice of an ordinary restart, the debtor will prepare the sale of the business, together with his own advisors, before filing for “faillissement”. In the proposed pre-pack, the debtor has the opportunity to formally involve an intended trustee and an intended supervisory judge in the process of preparing the business sale.¹³³ Since the intended trustee and intended supervisory judge are involved early in the preparation, they will not be confronted with a prepared asset transaction at the moment of the formal appointment as trustee and supervisory judge in liquidation.

40 The Dutch intended trustee is court appointed and therefore it can be argued that his independence is guaranteed.¹³⁴ The appearance of a biased trustee might therefore not, or at least to a lesser degree than in the UK, be part of the Dutch procedure. However, the Dutch secured creditors do have a powerful position in the pre-pack because of their position as *separatist*. The secured creditors in the Netherlands can take recourse to their encumbered assets as if there is no liquidation procedure. To protect the intended trustee and the debtor from the powerful secured creditors, the Dutch intended trustees are appointed by the court and the secured creditors do not have influence on the appointment itself or on the person who is going to be assigned as intended trustee. The intended trustee is supervised by the intended supervisory judge from the moment of appointment and his appointment can be made subject to certain conditions.

41 The ARD provisions will, at least until decided otherwise by the ECJ, not apply to the pre-pack in the Netherlands. One could argue that the whole Dutch procedure will be at stake if the ARD does apply to the pre-pack. Furthermore, the court has recently decided that the Dutch pre-pack indeed is not subject to the ARD.¹³⁵ However, this might change after the ECJ answers the preliminary questions referred to in the case of *Estro*. The Dutch court-controlled pre-pack offers a form of security to the public and the unsecured creditors that cannot be offered in the UK. However, the involvement of a court will provide extra costs and might cost more time to complete. The UK procedure on the other hand, can be swift, quick and out of court which is an advantage in a pre-pack situation. On the other hand, it might be easier to get rid of the employees under the proposed Dutch legislation. If the ARD provisions indeed do not apply to the Dutch proposed procedure, this might lead to an easier way to dispose expensive or unnecessary employees in the Netherlands.

¹³² Conway, above note 2, at 3.

¹³³ *Kamerstukken II* 2014/15, 34 218, 3, at 7 (MvT).

¹³⁴ Frölich, above note 75, at 197.

¹³⁵ Rb. Overijssel, 28 July 2015, ECLI:NL:RBOVE:2015:3589, *JAR* 2015/220, m.nt. J. van der Pijl.

42 It can be argued that the Dutch participate in, or started, a ‘race to the bottom’ with the introduction of the pre-pack. The position of the secured creditors as separatist is crucial in the proposed procedure. Without their support, the pre-pack is doomed to fail. Next to this crucial influence of the banks, the provisions of the ARD, for now, do not apply to the Dutch pre-pack. These two elements create a procedure that might be very attractive for restructuring an enterprise. Whether or not the Dutch restructuring practice will turn out to form an equally big economic advantage as in the UK, remains to be seen. However, the improvements made to the domestic procedures might at least cause the Dutch companies to no longer “forum-shop” in the UK.

43 The stigma of insolvency still exists and both jurisdictions are heavily fault based. However, both the English and the Dutch practice are taking steps towards a more second chance orientated procedure. One should keep in mind that not all failing companies are the result of bad management, and that a pre-pack can offer unfortunate companies and directors the opportunity to start again. However, one should be wary that the pre-pack is not some panacea that can be used to cure all financial ills of a troubled company.¹³⁶

44 Whether the international restructuring practice will use the Dutch regime instead of the English pre-pack remains to be seen. However, the Dutch might have created a procedure that can compete with the UK practice. The procedure is attractive for the secured creditors and the procedure is, for now, not subject to the ARD provisions. On the other hand, the UK pre-pack has proven to be an effective procedure in the past. The Graham Report has provided an overview of the criticised elements and reforms to improve the procedure are occurring. One should be wary that the added value that the pre-pack can offer to a rescue regime, is not getting flooded by the criticism in the media and academic literature. It is necessary to continue providing safeguards to avoid the abuse of the procedure, and then time will tell how the international restructuring business will respond. The developments in the Dutch corporate rescue legislation however, are absolutely worth keeping a close eye on.

¹³⁶ N.W.A. Tollenaar, “Van pre-pack naar stille bewindvoering: een nuttige rechtsfiguur in de maak” (2013) 6 *F.I.P.* 202, at 203.