



# **INTERNATIONAL INSOLVENCY INSTITUTE**

## **Tenth Annual International Insolvency Conference**

Rome, Italy

### **SALES OF BUSINESSES IN INTERNATIONAL CASES: CLEAR OR NOT-SO-CLEAR TITLE?**

#### *Sales of Businesses in Insolvency in Germany*

*By*

*Annerose Tashiro*

Schultze & Braun

Achern

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# **INTERNATIONAL INSOLVENCY INSTITUTE**

## **10th Anniversary Conference**

### **Panel on International Sales of Businesses**

#### **GERMANY**

#### **Dr. Annerose Tashiro, Schultze & Braun, Achern**

#### **1. The parties in control of the sales' process and their obligations and responsibilities**

In most of the cases in Germany, the insolvency court appoints, upon the commencement of the proceedings, an insolvency administrator who will step into the shoes of the insolvent company, who will be administering the assets and the business of the debtor and who will also realize the assets of the company in order to maximize the estate for all creditors. With his appointment order, he is the only responsible person for any and all decisions he will be taking in that respect. He can seek either to rescue the business and/or the company if it suits the case or he can just dispose of a whole or a significant part of the business or he can also sell single items of the assets through either auction or sale. We will be concentrating here on the sale of the whole business or a substantive part of the business as a going-concern.

Upon the commencement of the insolvency proceedings the case is overlooked by a clerk (Rechtspfleger) at the insolvency court who will be receiving regular reports from the administrator and can and will also request the administrator to submit certain statements on the status of the administration and/or certain matters. The insolvency judge has typically no further role or control of the case. Typically, the insolvency administrator will have upon appointment by the clerk a creditors' committee of a hand full people who will be supporting the administrator and who will give there insight and view regarding certain questions. The creditors' committee is to some extent a representative body of the creditors' meeting or the creditors' assembly as such. The committee is typically elected in order to facilitate the process and "day-to-day work" between the administrator

and the creditors. The members of the creditors' committee shall support and supervise the administration and shall be having an insight of the case, the documentation and also the money transfers and funds of the case.

However, unless the insolvency code stipulates under certain circumstances the prerequisite to obtain creditors' committee approval, the creditors' committee's approval is usually not required by law to administer the case and sell assets. However, typically, especially when it comes to the sale of substantive assets, the administrator will seek to get the creditors' committee approval in order to minimize and manage his liability issues.

Finally the creditors' meeting has the possibility to decide on the future of the insolvent debtor in a so called report meeting upon a report by the administrator about the financial status of the company and whether there are any outlooks to maintain the enterprise in parts or in whole and which affects this would have for the creditors. The creditors' meeting which typically convenes about 2 to 3 months after the commencement can decide whether to stop the business of the debtor and wind-down the company or whether it shall be continued as a going-concern.

## **2. The forms of sales procedures available**

In Germany, the Insolvency Code (Insolvenzordnung) does not provide any specific procedures for the sales process as such. As mentioned above the only formal prerequisite here would be the consent of the creditors' meeting to continue the business as a going concern and not to shut down the company.

The Insolvency Code provides only three sections (see below under no 5) under which a sale requires the approval of the creditors' committee or the creditors' meeting, but it also clearly states in section 164 that a breach of such requirement does not affect the validity of any legal transactions the insolvency administrator enters into. Finally such breach could only affect the liability of the insolvency administrators.

Apart from that the form of the sales' procedure is entirely in the discretion of the insolvency administrator upon his judgment and assessment of the company the industry sector, the products or any other circumstances that would have any influence on the question how to structure such process.

Depending on the volume and size of the case, the administrator's experience the availability and access to knowledge within the company, the administrator might

gain external assistance from M&A advisors or investment bankers to help him to structure the sales process.

However, there is no formality which involves the court, no documents have to be filed with the court and the sales process however structured does not need to be checked or even approved by the court. The court clerk and the judge will learn formally and officially about the sale through the administrator's regular reportings. This does not mean that the administrator might not in certain special circumstances discuss various options with the clerk or the judge "off the record".

Also creditors will not necessarily be formally informed about the sales process or hiring an M&A advisor or the like.

### **3. Canvassing the market/identifying prospective purchasers**

As mentioned above depending on the circumstances the identification of potential buyers can defer from case to case and the insolvency administrator might decide from case to case which would be the best way to pursue in order to maximize the outcome of the sales process. In prominent and public cases interested potential buyers will present themselves in any event and find their ways to the investment bankers/M&A advisors. In rather non-public or non-prominent cases the administrator would address and identify potential buyers through an assessment of the market in cooperation with the management of the debtor who typically know the market or he will engage M&A advisors who will use their resources and channels to the market and advertise potential sales opportunities.

### **4. The offering for sale/bid process**

In Germany usually insolvency administrators do not only try to find the highest purchase price. Typically insolvency administrators prefer that the prospective buyer submits a concept for the company that is laying out the future shape of the business, how many employees will be taken over, what the business plan for the new company shall look like and whether the overall outlook is convincing and presents a sustainable prospect for the business. Usually workers' council or unions have a say in deciding on the buyer when it comes down to different concepts and structures.

Therefore auctions are not seen so often in Germany for the sale of the whole or a substantial part of the business, as the supporting concept is of high importance and a higher price might not be often the best solution at all.

Often insolvency administrators start with indicative offers or indications and move then forward to negotiate with two or three potential buyers.

Experience shows that in many cases of insolvent companies, the quality and quantity of documentation is very poor, often facts coming from the debtor's accounting are not reliable and many questions from the bidders remain unanswered. Administrators will not take over any sort of liability for the documentation and the data base or data room is often unsatisfactory. Considering that all decisions made by the administrator fall into his personal responsibility and no court approval or creditors' committee approval would entirely release him, the risk is always and completely with the buyer. No administrator would undersign any form of representations and warranties – his liability would be entirely excluded to the legally possible extent. Buyers must take this risk into their consideration and calculation of the purchase price. Buyers' requests for certainty and clarification will typically be answered with "impossible, you must take this into account when calculating the bid". Commercial, legal and to some extent financial due diligence is therefore a significant tool for bidders.

Furthermore, from experience one can say that insolvency administrators do not tend to agree on exclusivity so often and are trying to keep the bidding process and negotiations as broad and open as possible which can be often frustrating for bidders who are seeking certainty and assurance.

## **5. Requirements of Court/creditors' approval and the position of unsuccessful bidders**

As described above, there is no requirement for court approval under German law for the sale of the whole or a substantial part of the debtor's business.

The necessity to seek creditors' committee's or creditors' meeting's approval has been addressed above already. The cases in which the Code provides for the necessity of creditors' committee's or creditors meeting's approval are (1) the sale of the company or the business as a whole, (2) the sale of the company of the business to an insider if he has a share in the new buying company of at least 20 % or if the buyer is a substantial non-subordinated insolvency creditor whose claim totals at least 20 % of all claims and (3) finally: a sale of the business requires the approval of the creditors' meeting upon petition of the debtor or a creditor in the event a sale to another different buyer would be more favorable to the insolvency estate. However, the petitioner must provide evidence or proof to the court that will result in such conclusion. The court would then order the requirement of the creditors' meeting's approval.

Likewise, especially a non-successful bidder might file a petition with the insolvency court to request creditors' meeting's approval and seek through that process to demonstrate that his bid would be higher and gain votes from the creditors or make them voting against the challenged bid. However, the Insolvency Code does not determine the purchase price as the threshold; it rather specifies and differentiates bids and potential bidders as being more or less in favor of the estate. This will take into account the number of employees taken-over, as dismissed ones will have severance payments claims and/or damage claims. It would also take into consideration the volume and scope of the business taken over, its affect to contractual relationships as well as the timing. A bid being advantageous to the estate and by that to the all creditors is not just the comparison of two numbers.

However, as mentioned above, the legal transaction/the sale is - even in case of violating the requirements of creditors' committee's or creditors' meeting's approval - still valid.

Therefore practically, the only remaining ankle for anyhow unsatisfied creditors or unsuccessful bidders would be to challenge the liability of the insolvency administrator. With this, he must then prove that the insolvency administrator damaged the estate, either with gross negligence or willfulness. It should be clear that this is fairly difficult to achieve.