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Conditional creditors within the financial liabilities of Spanish schemes of arrangement

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An unresolved question - and one that generates disparate opinions - is addressed in this paper concerning whether and how conditional or litigating creditors should be acknowledged in terms of quorum and voting under the Fourth Additional Provision of the Insolvency Act.

In the publication *Actualidad Jurídica Uría Menéndez*, issue no. 49 (2018), the lawyer A. Alonso Hernández addresses the thorny problem, until now unresolved (despite the 'Abengoa' II Order of 5 June 2015), of whether contingent (financial) claims form part of the financial liabilities that may be affected by a court's approval ('homologation') of a refinancing arrangement under the Fourth Additional Provision of the Insolvency Act. The author proposes extending the effects of the arrangement to contingent creditors. He also proposes the application by analogy of Article 87(3) of the Insolvency Act to the extent that this allows for the creation of 'provisions' that ensure relief for these creditors once the contingency has been eliminated. He also postulates that, as other affected creditors, contingent creditors should have the procedural standing to file an objection to an homologation.

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I subscribe to these proposals with respect to conditional creditors, but, for the reasons explained below, not in the case of other contingent creditors.

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The real problem lies in determining whether to compute these liabilities for the purposes of quorum and voting on their full value (they are not present, but prospective, claims) or without own value. The above author disagrees with Azofra – and concurs with Yáñez and Villoria – by proposing that these claims be computed without own value and offering a series of

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reasons – not least the dogmatism regarding the treatment of conditions precedent – that bar an existing claim during the pendency stage from being considered conditional in spite of the interim protection granted to conditional creditors by Article 1121 of the Civil Code. Alonso Hernández goes on to suggest that the treatment that these creditors deserve is the same as that provided in the old Code of Commerce to creditors with claims pending litigation and, by analogy, with claims subject to a condition precedent; namely, the granting of the procedural rights to which I have referred and the right for the terms of the arrangement and the viability plan to have a reserve cushion envisaged for application to contingent claims.

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However, I believe that the most serious part of the problem remains to be resolved.

It seems to me that the promoter of a scheme of arrangement cannot leave contingent or conditioned (financial) creditors, as a class, out of the perimeter. Not because the proposal would be vexatious to this excluded class, which it would not be, but because it would harm the position of dissenters within the class included in the perimeter. The implications are evident: claims of the excluded class would not be subject to the haircut under the Fourth Additional Provision, but could be enforced without hindrance and, if insolvency proceedings should be opened, they would have to sustain only one haircut, while dissenters of the non-excluded class would sustain the forgiveness of debt both within pre-insolvency and insolvency proceedings.

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I believe that, in spite of the uniform treatment provided by Article 87(3) of the Insolvency Act, conditional claims should be distinguished from litigated claims. A claim subject to a condition precedent is *naturally headed towards full realization,* even if the condition is ultimately not fulfilled, which would be a *failure* of contract. But a litigated claim is not headed from the outset to a predetermined end. Not even its final crystallization produces retroactive effects. For want of space I cannot address the more complex case of a claim against guarantors and a guarantor's claim for contribution, referring below only to claims subject to a condition precedent before ending with litigated claims. Other problematic contingent claims will not be dealt with either.

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Let us imagine that Alonso Hernández is right (that is, claims subject to a condition precedent compute without own value) and that the condition is fulfilled before the application for homologation (para. 5) or the homologation itself (para. 6) under the Fourth Additional Provision of the Insolvency Act. It is very difficult for either the proposer or the court to have instruments to include the confirmed claim before the court decision is rendered, especially if the value of the confirmed claim is of such a kind that it is sufficient to, if computed, alter the outcome of the collective vote already produced. However, this confirmed creditor - it seems - could contest the homologation under para. 7, because, hypothetically, the confirmed claim is decisive for altering the outcome of the vote.

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Suppose, on the other hand, that the confirmed conditional claim is not of a value sufficient to alter the content of the arrangement. The creditor will have been left without exercising his or her right to vote and will not be able to (effectively) contest the homologation, according to the rule known as the arrangement's 'resilience test', even if he or she is in time to contest. Does this make sense? It does not if we force an analogical argument based on Article 204(3)(c) of the Companies Act.

(7) Only a vote unduly cast would be irrelevant for the purposes of para. 7 of the Fourth Additional Provision of the Insolvency Act, not a vote that has been passed over, which is confirmed by Article 87(1) of the Insolvency Act for claims subject to a condition subsequent. It is practically a constitutional safeguard. If any holder of a marginal share could be deprived of his vote without further ado, it would almost not be necessary to convene meetings of shareholders or meetings for the approval of refinancing arrangements.

Imagine now a confirmed conditional claim when it is no longer possible to contest the court decision. It is evident that there is no longer any procedural step or stage in which this confirmation can be taken into consideration in any of the senses relative to the vote or by analogy of Article 87(1) of the Insolvency Act ("the actions and decisions in which an act, acceptance or vote of a conditional creditor were decisive may be voided at the request of a party"), because we will have been left with no playing field in which to fight this match. Suppose, moreover, that it is a creditor

(8) with a claim capable of altering the global computation of votes. In spite of being a creditor that would pass the 'resilience test', nothing can be done, because the court decision is res judicata and there is no alternative avenue to judicially contest the refinancing, at least as long as the debtor does not breach the arrangement. Note that the problem is the vote, not the practical effect of the arrangement (e.g., forgiveness of debt, debt-equity swap, etc.), since this effect can always be realised for and against the consolidated creditor as long as the execution of the refinancing arrangement is alive.

These considerations force me to prefer an interpretation contrary to that of the author who has given rise to these comments. Even despite appearing aberrant in light of the theory of conditions - which it is not, because we simply reclassify this condition as subsequent and notprecedent - it is true that a person could be thus allowed to vote - moreover with decisive effects - who might turn out to have no claim, thereby artificially inflating the quorum and majorities required to agree the arrangement. But what difference does it make? Under the Fourth Additional

(9) Provision there is no claim verification stage. Included are claims that can be simulated, claims subject to a condition subsequent, claims subject to a longstop date, prima facie *contra legem* claims, confessed claims, claims that will be satisfied by set-off, and so on. This 'rubbish' included amongst the financial liabilities cannot be substantially altered by the addition of conditional claims. The contrary view encourages the debtor and the insider creditors (once again, the example of 'Abengoa') to arbitrarily manipulate the list in order to expel from the computation so-called contingent claims, but which are not, such as the claims against the guarantor, with or without the benefits of excussion.

(10) With the proposal I advocate, constitutional rights of participation that cannot be stolen from creditors are safeguarded, especially (but not only) if they have the density of vote to break the resilience of a scheme of arrangement. Indeed, a person without entitlement might vote. But in this case it would matter not if the arrangement would nonetheless not be affected by the detraction of that vote. And if the subtraction of the vote from the (ultimately not consolidated) claim was decisive for the precise calculation, it would be a matter of finally opting for one of two evils: either to accept an arrangement that would not have garnered the required votes if the false creditor had not voted, or to accept an arrangement that would not have been agreed if the true creditor had been able to vote. The second option has a constitutional component, the first one does not.

(11) The option I support has lower transaction costs because it exempts from finding out whether, for the time being, a certain claim is not contingent. And it is no small gain. Let us not forget that one way or another all claims subject to reciprocity ('functional' synallagma) are relatively 'conditional' in the sense of Article 1124 of the Civil Code: the creditor 'lodges' his claim, but it turns out that the 'condition' on which the enforceability of this claim depends (perhaps), which is the creditor's fulfilment of his own obligation, has not yet been fulfilled. Will we therefore remove all synallagmatic creditors from the share and vote calculation of the financial liabilities?

(12) I now turn briefly to litigating claim holders when what is litigated is the very existence of the claim. I believe that two types of situation should be distinguished. When it is the (alleged) debtor who seeks an adjudication of nonexistence (cancellation) of the claim, and the creditor objects, the claim must be included as a simple condition, because the status quo prior to litigation is the existence and not prima facie cancellation of the claim. When it is the would-be creditor who claims the existence of a claim or demands its payment and the debtor objects to it, the opposite occurs, and the status quo is that of prima facie non-existence of a claim that has to be included in the computation: if the outcome of the lawsuit is favourable to the creditor, it will be a prospective claim not affected by the homologation. I know that the division is not all-encompassing and that there are uncertain procedural cases, but essentially it is a matter of preventing a claim from being included or taken off the list by strategic procedural action by the alleged debtor or the alleged creditor.

(13) To conclude. Why this digression if we can limit ourselves to applying to the scheme of arrangement the rules of a composition with creditors and adhere, whether we like it or not, to the provisions of Article 87(3) of the Insolvency Act? I think there are intuitive reasons: (1) because outside insolvency proceedings there is no room for claims against the debtor to unfold independently, but there is in pre-insolvency proceedings; (2) because either the insolvency proceedings are non-suited and the problem disappears, or the arrangement is complied with and the problem for the contingent creditors disappears; (3) because the insolvency proceedings continue until the debtor company is wound up and liquidated, so there is no point in worrying about the realization of contingencies of the claims beyond this moment, but this is not the case in pre-insolvency proceedings.