A&O SHEARMAN

Restructuring across borders
Norway

CORPORATE RESTRUCTURING AND INSOLVENCY PROCEDURES | APRIL 2024

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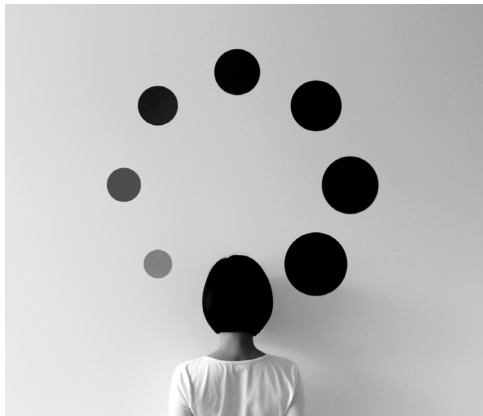

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Reconstruction

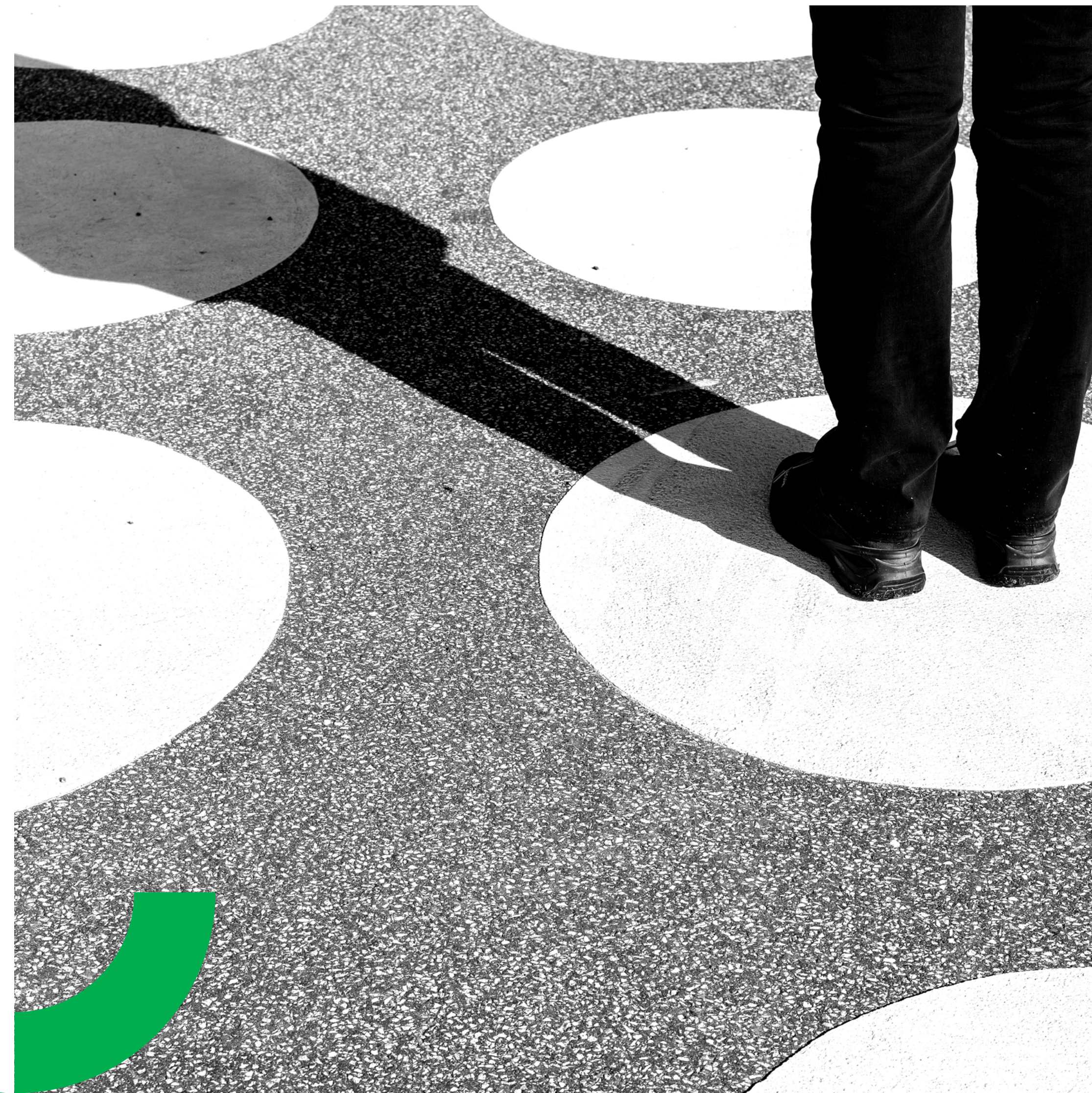
Introduction

In Norway there are in principle two in-court procedures; (1) outright bankruptcy which in reality is a liquidation of the company, and (2) a reconstruction either with a voluntary plan that requires unanimity, or a cram-down which requires the support of at least 50% of the creditors. Oftentimes, however, restructurings are handled out-of-court and include a consensual restructuring agreement with the key financial creditors.

Reconstruction proceedings may be opened by the court if the debtor "is in or in the foreseeable future will be in serious financial difficulties", and is an alternative for companies with sufficient means to fund such a proceeding while the company's business operations continue in parallel. This in contrast to bankruptcy proceedings, which should be opened if (i) a company's debt is higher than the value of its assets, (ii) there are no funds to cover ongoing obligations as they fall due for payment, and (iii) the situation is not considered to be temporary.

As for jurisprudence, Norway is party to several multilateral conventions which regulate, among other things, cross-border bankruptcy proceedings. An example is The Nordic Bankruptcy Convention. Norway is however not a part of the European Union (the "EU"), and is hence not directly bound by EU regulations.

A voluntary liquidation process of a private limited company is available and regulated by the Companies Act. A voluntary liquidation process requires, among other things, that all the company's creditors are being fully covered. We will hence not comment on this any further in the following.



Reconstruction

1.1 GENERAL OUTLINE AND CONDITIONS FOR OPENING RECONSTRUCTION PROCEEDINGS

The Reconstruction Act came into force on 11 May 2020 and was originally intended as a temporary act providing for remedial action for financial difficulties due to the COVID-19 pandemic. The act is currently in force until 1 July 2025. A proposal for a permanent reconstruction act has been circulated for public consideration but is not expected to be passed until late 2024 at the earliest.

The Reconstruction Act provides for two types of procedures: (i) voluntary debt settlement and (ii) compulsory composition. The conditions for opening are the same for both types of procedures.

If a debtor files for reconstruction, negotiations may be opened if the debtor "*is in or in the foreseeable future will be in serious financial difficulties*".

When determining whether the debtor meets the conditions of the Reconstruction Act, the court will assess this from the debtor's perspective. Hence, a debtor filing for reconstruction is presumed to be, or in the foreseeable future will be, in serious financial difficulties.

A creditor can also file for reconstruction proceedings. Contrary to when the debtor is filing, the creditor must demonstrate that the debtor is illiquid. It should be noted that the opening of reconstruction proceedings in any event is subject to the consent of the debtor.

1.2 THE RECONSTRUCTION BODIES

After the opening of reconstruction proceedings, the court shall immediately appoint a reconstructor and a creditors' committee, who together constitute the reconstruction committee. The reconstruction committee shall assist the debtor during the proceedings while also safeguarding the creditors' common interests.

Throughout the reconstruction process, the company and its board of directors will retain control over its operations and financial circumstances, albeit under the supervision of the reconstruction board. This implies, among other things, that the reconstruction committee shall be granted full access to the company's financial affairs and incidental operations, and the company is obliged to comply with any directives issued by the reconstruction committee in this context.

Further, the company (its board of directors) are responsible for making a proposal for reconstruction plan. However, the reconstruction board shall assist the company's board of directors with the compilation.

The reconstructor must be a lawyer with experience from insolvency proceedings.

1.3 DURATION OF THE RECONSTRUCTION NEGOTIATIONS

Reconstruction proceedings initially have a maximum duration of six months from the opening date. However, the court has the discretionary authority to prolong the negotiations following an application from the reconstruction committee. During ongoing reconstruction proceedings, there is an "automatic stay" protecting the debtor from bankruptcy and debt enforcement. However, the "automatic stay" protection is not applicable to creditors whose security is subject to the Norwegian Financial Collateral Act (Nw: "lov om finansiell sikkerhetsstillelse"). These creditors (including, for example, banks and financial institutions lending on a secured basis) may collect their security independently of the reconstruction process.

If the debt is not reconstructed by the deadline, and the proceedings are not prolonged, the court will discontinue the negotiations by declaring bankruptcy unless the debtor is able to demonstrate being solvent.

1.4 THE RECONSTRUCTION

One of the main intentions of the Reconstruction Act is to increase flexibility compared to the former legislation on judicial debt negotiations, which did not work as intended. The content of a debt composition under the Reconstruction Act may vary, and can for instance consist of a payment extension, debt reduction and liquidation of the debtor's assets. A newcomer in the Reconstruction Act is that debt may be converted to equity (with some limitations). However, this requires approval by the shareholders with a simple majority.

While a voluntary reconstruction plan must be unanimously accepted by all the creditors affected by the proposed plan, a compulsory composition under the Reconstruction Act may be implemented when accepted by creditors representing at least 50% of the total quantum of unsecured debt with voting rights. Furthermore, there is no requirement of a minimum dividend pay-out. This implicates that only unsecured creditors are eligible to vote. Creditors whose debt is fully secured are not affected by the reconstruction plan and are hence not eligible to vote.

The Reconstruction Act does not contain provisions providing for "classing" of claims.

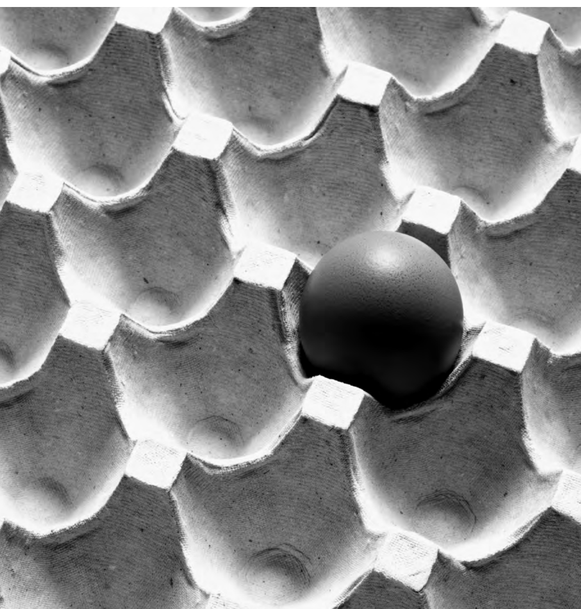
Furthermore, the Reconstruction Act allows the debtor, subject to approval by the reconstruction committee, to finance operating costs during the proceedings. Such debt may be secured by a priority lien on certain defined assets of the debtor (so-called "super priority" pledges). Such debt can also be secured by a statutory lien on the debtor's already pledged assets, taking priority over other secured debt for an amount of up to 5% of each asset's value, and up to a maximum amount (currently NOK 870,100) on each asset registered in an asset register.

The courts have the authority to both overturn the reconstruction committee's approval to finance the reconstruction proceedings by loans with super priority liens, and deny confirmation of the reconstruction proposal.

Bankruptcy

2.1 FRAMEWORK

Norwegian insolvency legislation is mainly found in two statues; the Act relating to Bankruptcy of 1984 (the "Bankruptcy Act") (Nw: konkursloven) and the Creditors' Recovery Act (Nw: dekningsloven).



2.2 OPENING OF BANKRUPTCY PROCEEDINGS

If a company is insolvent and this is not of a transient nature, bankruptcy proceedings shall be opened by the court. Insolvency means that the debt is higher than the value of the assets, there are no funds to cover ongoing obligations as they fall due for payment, and this situation is not considered to be temporary.

If a company is deemed permanently and irrevocably insolvent, the board of directors is generally required to petition for bankruptcy. There are nuances in this regard, including, among other things, if (i) creditors affected by the continued operations are informed about the situation and do not object, or (ii) the board of directors has a clear, reasonable and feasible plan to overcome the financial difficulties, bankruptcy may not be required. It is also important to note that the board of directors has a certain degree of discretion in its business judgement on how to navigate in the zone of insolvency.

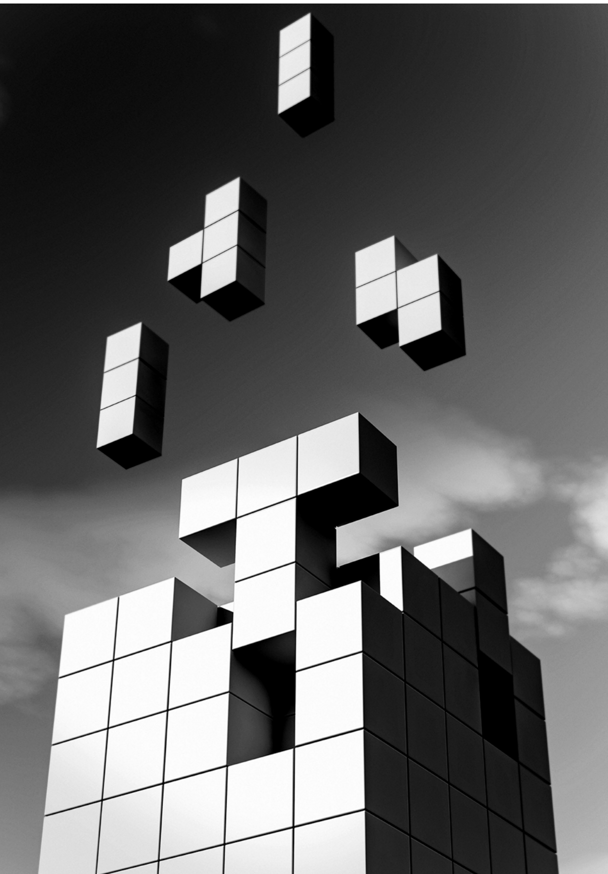
Failure to petition for bankruptcy may result in both civil and criminal liability for the board of directors and senior management.

Any unsecured creditor who has an overdue claim against the company may also petition for the debtor's bankruptcy. A creditor with security for their claim cannot petition for bankruptcy, unless the claim surpasses the security, and will rather have to legally enforce their claim.

2.3 DURING BANKRUPTCY PROCEEDINGS

The bankruptcy estate is established as a separate legal entity. The estate seizes "any asset belonging to the debtor at the time of seizure, which can be sold, leased or otherwise converted into money", which also include the debtors' assets with liens. The debtor hence loses control of its assets, and the board of directors becomes inoperative and is in most cases no longer authorised to act on behalf of the debtor.

Unless the bankruptcy estate sells all or part of the business operations to new owners, or the court or the bankruptcy trustee decides to (temporarily) continue some or all of the business operations, the debtor's business operations will be discontinued. The debtor's contracts will normally be terminated, however, the bankruptcy estate may decide, yet limited to the general provisions on the rights and obligations given in the Creditors' Recovery Act, to become a party to one or more contracts. As a general rule, these provisions apply to all types of contracts. However, a bankruptcy estate automatically assumes the position of the debtor company in two types of contracts, namely employment contracts and tenancy agreements, unless the bankruptcy trustee, within three and four weeks of the opening of the bankruptcy proceedings, respectively, decides and expressly states to each contractual party that the estate will not do so.



2.4 REALISATION OF ASSETS

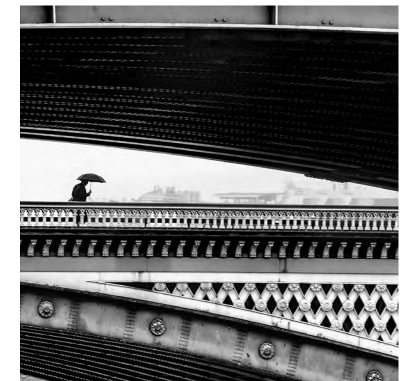
The bankruptcy estate aims to realise all the debtor's assets in a way that will provide the largest income for the estate/the highest dividend to the creditors. "Assets" include all cash, bank deposits, real property, inventory, vehicles, operating assets, account receivable, IPRs, etc.

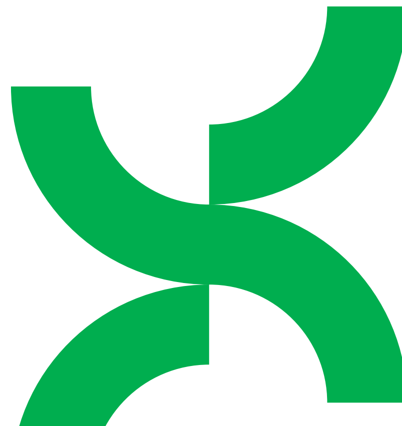
If assets cannot be realised, and/or are worth less than or equal to the encumbrances attached to them, the bankruptcy trustee may decide to abandon the assets. Regular abandonment implies that the estate's seizure of the asset is lifted, and the legal possession of the abandoned asset is reverted to the debtor company. Another option for how the trustee can handle overly encumbered assets is to transfer the title to the asset to the pledgee. In this scenario, the pledgee is given full rights of disposal as owner and may freely decide how to handle the asset.

2.5 CLAW-BACK OF CERTAIN TRANSACTIONS

The Creditors' Recovery Act contains claw-back provisions designed to allow the setting aside of certain pre-bankruptcy (or reconstruction) transactions, based on the fundamental principle that all creditors should be treated equally. Apart from obvious exceptions, such as for secured and preferential creditors, Norwegian insolvency law is strict in its enforcement of this equality principle and a number of rules make way for invalidating transactions not compatible with that principle.

These rules aim to protect creditors and, when applicable, empower the reconstructor or bankruptcy trustee to set aside or reverse said transactions. Potentially the estate might pursue personal liability claims against those officers and directors who took part in decisions and transactions to the detriment of the company and/or their creditors prior to the reconstruction or bankruptcy proceedings.





2.6 CLAIMS

2.6.1 Types of claims

There are five main types of claims: secured, preferential, ordinary, subordinated and claims incurred during reconstruction or bankruptcy proceedings.

Secured creditors can recover their claims out of the proceeds of the sale of the assets in which they have security, and the sale may be conducted by the bankruptcy estate. Alternatively, the bankruptcy trustee may "abandon" assets by lifting the estate's seizure cf. section 2.4 above.

Preferential claims consist of certain pension and salary-related claims due for a period of up to three months before the cut off date, as well as claims for income tax, VAT and certain other government claims due for a period of up to six months before the cut-off date.

Subordinated claims are claims for interest incurred after the cut off date, penalty tax and fines, gifts promised but not fulfilled, etc. (section 9-7 of the Creditors' Recovery Act). Such claims are subordinate to those of the ordinary creditors.

All claims other than those described above are ordinary claims.

2.6.2 Secured creditors

Secured creditors' claims are not technically ranked with a priority, however they are preferential to the extent that such claims will be settled from the realisation of the assets in which they are secured. Any remaining claim amount will be treated as an unsecured, ordinary claim, which may be registered as a dividend claim in the estate.

The secured creditors' enforcement will be subject to a stay or freeze for six months from the date on which a petition for the opening of bankruptcy proceedings was filed. However, the secured party may obtain consent from the bankruptcy trustee or reconstructor to enforce their rights during the stay. For creditors whose security is subject to the Norwegian Financial Collateral Act (Nw: "lov om finansiell sikkerhetsstillelse), the protection against enforcement for six months prior to the bankruptcy opening, is not applicable, cf. item 2.3 above.

The bankruptcy estate has various alternatives with regards to handling assets which are fully secured;

- sell the pledged asset, with full or part coverage to the security holder. The latter usually occurs if it is beneficial for the bankruptcy estate to sell the pledged asset together with other unencumbered assets with a view to achieving a higher sales price, or if the sale forms part of a transfer of all or parts of the business operations. The pledge will then follow the asset through the sale.
- abandon the pledged asset to the debtor, which gives the lienholder a possibility to legally enforce their claim.
- transfer the pledged asset to the pledgee. A transfer of this nature requires the consent of the pledgee.

Regardless of how secured assets are handled, the bankruptcy estate has a statutory lien of up to 5% of each asset's value, limited to a maximum amount (currently NOK 893,900). The statutory lien has precedence over all other pledges registered in each of the debtor's assets. The lien can only be claimed and used by the bankruptcy estate to cover necessary costs of the bankruptcy proceedings.

2.7 CLOSING OF THE BANKRUPTCY PROCEEDINGS

A limited company shall be dissolved and de-registered from the Norwegian Register of Business Enterprises upon closing of the bankruptcy proceedings. The practical effect of a limited liability company bankruptcy is that any uncovered debt will be extinguished when the company ceases to exist. A debtor only remains liable for remaining debt in the case of a personal bankruptcy, and partners in a general partnership are liable for the remaining debt in the case of bankruptcy in such a company.

Restructuring

INTRODUCTION

Until Norway introduced the Reconstruction Act, almost all large restructurings were done out of court. This is still the case now that the new reconstruction rules have come into effect, but we see more combinations of a consensual deal and a filing.

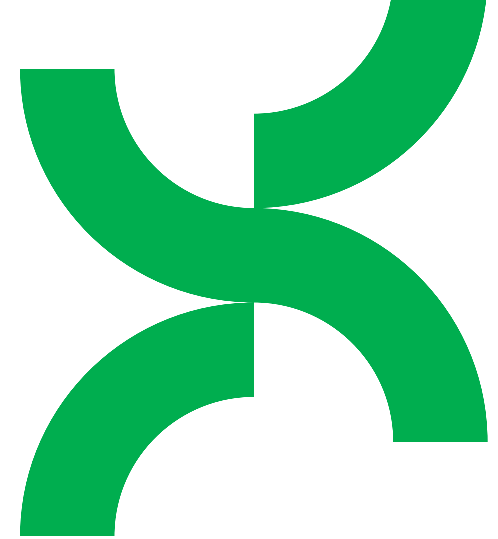
Two key reasons for the continued out-of-court focus is that secured creditors cannot involuntarily be bound by a reconstruction plan subject to the Reconstruction Act, and that issuance of new shares, both for cash and by conversion of debt to equity, requires the affirmative vote of the shareholders at a shareholders' meeting. Hence, two important stakeholder groups need to be involved outside the scope of the Reconstruction Act regime.

Given the above, a detailed analysis should be done from the get-go on what process is best suited to implement the necessary changes in the capital structure to ensure a viable company emerges from the process. All the involved stakeholders will be mindful of the potential major losses they will suffer if the company goes into liquidation. This fact often has a calming effect on the various stakeholder groups to achieve a consensual restructuring.

Based on the above, and given that the Reconstruction Act still offers limited flexibility and available plan structures, we expect that large companies will continue wanting to carry out restructurings out-of-court and only dealing with key finance providers and not the creditor group at large.

The various international procedures, such as Chapter 11 and Scheme of Arrangements (and similar) around the world, have been and will continue being considered as additional tools.

Key contacts



If you require advice on any of the matters raised in this document, please contact any of our partners or your usual contact at A&O Shearman, or email **rab@aoshearman.com**.

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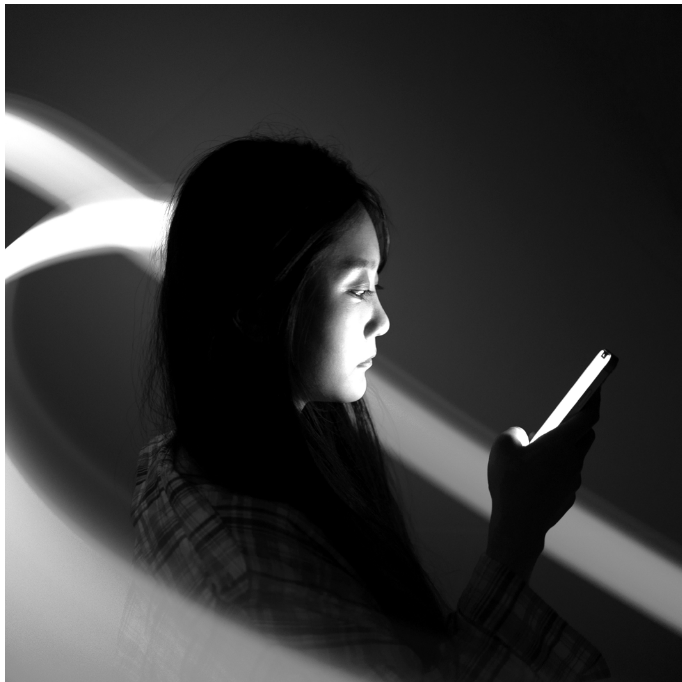
Further information

Developed by A&O Shearman's market-leading Restructuring group, "**Restructuring Across Borders**" is an easy-to-use website that provides information and guidance on all key practical aspects of restructuring and insolvency in Europe, Asia, the Middle East and the U.S.

To access this resource, please **click here**.



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