

Summary of *Evaluatie Garantstellingsregeling curatoren 1999-2005* (evaluation of the Trustees Guarantee Rules 1999-2005) by R.D. Vriesendorp, F.M.J. Verstijlen, G. van Dijck and D.F. Kopalit (Boom Juridische uitgevers, The Hague 2006).

1. Introduction

The Trustees Guarantee Rules (*Garantstellingsregeling curatoren*; hereafter: ‘TGR’) came into effect on 26 April 1993 and tries to remedy or at least reduce funding problems for trustees when making a claim on the basis of wrongful trading or transaction avoidance rules. A first evaluation of this instrument took place in 1998/1999 (R.D. Vriesendorp, F.M.J. Verstijlen, C.W.M. Slegers, *De Garantstellingsregeling curatoren*, Tilburg, 1999). The recommendations at that time did not result in an adjustment of the TGR. Because the number of bankruptcy filings has substantially increased over the last few years and because the nature of bankruptcy fraud seems to have become more complex, the need was felt to evaluate the functioning of the TGR for the period 1999-2005.

2. Scope of the evaluation and research questions

Chapter 1 deals with the goals of the evaluation: on the one hand an update of the previous evaluation of the (old) TGR in 1998/1999 for the period 1999-2005 and on the other hand the development of elements for a possible – partially or completely – revised instrument. In this respect five research questions were formulated:

- What is (are) the purpose(s) of the TGR?
- How does the TGR function in practice?
- How is the TGR assessed by the persons involved in the instrument?
- What are the bottlenecks of the TGR?
- How should a new instrument be drafted?

3. Purpose of the TGR

The purpose of the TGR is described in chapter 2. The instrument enables a bankruptcy trustee (*curator*) who is confronted with an empty estate, to institute legal actions on the basis of director’s liability (art. 138 or 248 Book 2 Dutch Civil Code), fraudulent conveyance or transactional avoidance (*faillissementspauliana*; art. 42 et seq. Bankruptcy Act) or to investigate such possibilities. Such trustee can obtain a (current-account) credit facility with the Kas Bank N.V. The Dutch government, through the Ministry of Justice, provides Kas Bank N.V. with a guarantee for the deficit. The purpose of the TGR is to stimulate bankruptcy trustees (in their task as liquidator of bankrupt estates for the benefit of the creditors) to fight the abuse of legal entities. This purpose did not change per January 1, 2005, although the TGR was changed at that time, mainly to keep the costs under control.

4. Functioning of the TGR

The functioning of the TGR is dealt with in the chapters 3-7, successively factual information concerning the application (ch. 3), the decision-making (ch. 4), the progress and control (ch. 5), the handling (ch. 6) and the results (ch. 7). In this respect interviews were held with the persons involved at the Ministry of Justice, review of the files at the Ministry of Justice took place and questionnaires were sent to bankruptcy trustees (both members and non-members of the Dutch insolvency practitioners association ‘Insolad’) and to all bankruptcy judges (*rechters-commissarissen*).

5. Assessment of the TGR

The results of the completed questionnaires from bankruptcy trustees and bankruptcy judges provided us with information regarding the assessment of the TGR by these parties involved. Compared to the previous evaluation in 1998/1999 the instrument was less appreciated with respect to most topics (except for the contacts between trustees and judges). On a scale of 1-10 the assessment shows the following picture:

<i>Topic</i>	<i>Period</i>	<i>TGR 1993-1998 (1999)</i>	<i>TGR 1999-2004 (2006)</i>	<i>TGR 2005 (2006)</i>
duration of application		6,3	4,6	5,4
contacts with Ministry of Justice		6,7	5,3	5,3
contacts with bankruptcy judge		7,7	8,2	7,4
contacts with bank		7,1	6,1	6,0
duration of handling		6,4	4,9	-
manner of handling		6,5	5,0	-
overall assessment		6,7	4,8	4,5

6. Bottlenecks

In this study we identify in chapter 9 the following bottlenecks with regard to the TGR.

1. The purpose of the TGR is to provide the bankruptcy trustee with an empty estate with the means to institute legal actions on the basis of director's liability, fraudulent conveyance/transactional avoidance or to investigate the possibilities thereto and thus to fight against fraud and abuse of legal entities. In practice, however, the Ministry of Justice seems to emphasize on protecting the interests of the unsecured creditors, in a sense that they obtain a substantial greater portion from the estate as distribution on their unpaid claims against the bankrupt debtor. This goal is hardly reached; the contribution to the fight against fraud is insignificant.
2. The majority of the persons involved (bankruptcy trustees and judges) claimed to be unsatisfied with the (strict application of the) recovery criterion as requirement for a positive decision, especially when quick and adequate action by the trustee is required at the beginning of the bankruptcy. Trustees have to demonstrate that there will be sufficient recourse in the event of a favourable judgement. The additional requirement by the Ministry of Justice that the amount of the favourable judgement should be at least four times the amount requested as guarantee, does not improve the chances for a successful application either.
3. Comparing the number of TGR-applications in the period 1999-2005 with the total number of bankruptcy filings in the same period, seems to indicate a decreasing interest in comparison with the previous period (1993-1998). The relative number of applications has decreased substantially, which is regretted by the joint bankruptcy judges.
4. The employees of the Ministry of Justice are dissatisfied with the communication between them and the bankruptcy judges: they hardly give reasons for their recommendations and the contacts with the bankruptcy judges are difficult. The other way round is the same. Also, the contacts between bankruptcy trustees and the Ministry of Justice are not always smooth.

5. Pursuant to art. 4 par. 2 TGR 2005 the guarantee is not continued if the trustee does not report periodically in time. A similar sanction exists if the trustee does not renew the guarantee in time. Furthermore, it is unclear to what extent the ultimate costs must be borne by the trustee *pro se*. This opacity does not result in an attractive instrument, but may, on the contrary deter trustees.
6. The activities by the trustee required for a successful application require a substantial amount of time, especially where he must demonstrate that recourse will be possible. Because these activities by definition must be performed before the guarantee can be awarded by the Ministry of Justice, the costs involved will not be reimbursed. Consequently, these costs will remain for the account of the estate, which in case of an empty estate will result that such costs will be for the account of the trustee *pro se*.
7. Apart from the activities of the trustee in connection with the guarantee, he must perform numerous other activities in the bankruptcy which also require reimbursement. In this respect, it is not realistic to require that any income for the estate should be allocated to diminish the outstanding balance of the credit facility with the bank in order to decrease the exposure of the Ministry of Justice under the guarantee. In case of a so-called bankruptcy of the estate (*boedelfaillissement*) the trustee is under the legal obligation to satisfy the debts of the estate in accordance with statutory priority rules; in this respect the claim of the Ministry of Justice has no specific priority.
8. Although the TGR only imposes costs on the Ministry of Justice, a successful guarantee will result in an increase of the bankrupt estate from which unpaid creditors could receive a higher distribution on their claims than without the guarantee. For society as a whole, the guarantee is positive if it resulted in a fight against abuse of legal entities. However, there is hardly any insight into the proceeds of the TGR because the Ministry of Justice restricts the registration thereof solely to what trustees voluntarily report. Consequently, it remains unclear whether or not the TGR is successful or profitable.
9. The credit facility covered by the guarantee is granted by the Kas Bank N.V. in cooperation with the Ministry of Justice. Compared with the situation previously evaluated, this arrangement appears to be an improvement for the Ministry of Justice and a part of the trustees. A substantial part of the trustees, however, insist upon the abolition of the intervention of a financial institution between the Ministry of Justice and the trustee. It is considered more efficient and effective if the trustees organise the credit facility themselves and obtain a direct guarantee from the Ministry of Justice.

7. Recommendations

Chapter 10 contains the following concrete recommendations that could remove the bottlenecks mentioned here above.

1. The requirement of sufficient recourse should be handled with flexibility in the beginning of a bankruptcy, when the application is aimed at a guarantee for the costs involved with the investigation in the possibilities for recourse. In this phase, a bankruptcy trustee must normally act vigorously in order to safeguard (potential) assets, while it is not always clear at that time whether or not the recourse requirement is met.
2. Communication between the Ministry of Justice and the persons directly involved (bankruptcy trustees and judges) must improve, just as the image of the Ministry in practice. In this respect the Ministry of Justice must inform the parties involved what they may and can expect and demand from the government. In addition we recommend to bring the employees of the Ministry of Justice who are involved in carrying out the TGR, in contact with the bankruptcy practice.

3. The number of administrative actions with respect to the application, the periodical reporting and the renewals of the guarantees should be reduced. A guarantee should be granted for an indefinite period of time in order to prevent that a trustee must renew the guarantee each year. Separate periodical reporting requirements can be substituted with submission of the periodic public reports by the trustee pursuant to art. 73a Bankruptcy Act. If necessary, the Ministry of Justice can always ask for further information.
4. The sanction that a guarantee will not be continued in case of non-reporting or non-renewal by the trustee is likely not to occur anymore if the previous recommendation is implemented. For the few remaining situations in which the Ministry of Justice wishes to impose a sanction, such sanction must be clarified. First of all, it must be clear that any termination of a guarantee does not affect costs made prior thereto but only future costs. This means that the balance due of the credit facility will be covered by the guarantee under the obligation of a winding-up of the guarantee as soon as possible. Further, the impression arising from art. 4 par. 3 and 5 par. 3 TGR that a bankruptcy trustee will be personally liable for the settlement of the deficit must be taken away. To the extent the behaviour of the trustee falls within the scope as set by the Supreme Court, such sanction is superfluous, while otherwise it is unclear on which legal grounds such personal liability can be based. We recommend to abolish those provisions.
5. Because the current expectations of the Ministry of Justice with respect to the task and activities of the bankruptcy judge do not correspond with daily practice, such expectations should be restricted.
6. It is recommended that the guarantee also covers the costs of legal proceedings incurred before awarding the guarantee and the costs involved in the preparation of the application under the TGR, provided that the trustee has sufficiently accounted for the need for such costs.
7. The requirement that any asset of the estate must be used to cover the costs of legal actions and proceedings as meant in the TGR and to reduce the outstanding balance of the credit facility under the TGR, should be restricted to any asset or income derived from such actions and proceedings and to the extent such income exceeds the costs of the trustee in connection therewith. Moreover, the Ministry of Justice should have the possibility to secure the unsecured recourse claim, resulting from any payment under the guarantee.
8. The proceeds of the legal actions and proceedings under the TGR must be better administered. In this respect, trustees applying under the TGR should always be obliged to inform the Ministry of Justice about the proceeds, if any, of their actions.
9. Improvement of the coordination of any actions by the bankruptcy trustee, tax collector and the public prosecutor in the context of the scope of the TGR is recommended. In this respect, it may be useful to create one – if practical, only virtual – governmental focal point.
10. Finally, we recommend to have the transactional avoidance claim pursuant to art. 47 Bankruptcy Act and the claim for tortious prejudicing creditors' interests (the so-called Peeters/Gatzen-claim) also covered by the TGR.

8. Fundamental reconsideration?

The last chapter (ch. 11) deals with the question whether or not the TGR should be completely and fundamentally revised. The instrument seems broadly applicable in theory, but appears to have a very limited scope in practice. Two sorts of reconsideration are possible.

In the first place, it is sensible to (fundamentally) reconsider the scope of the instrument. Theoretically, one could restrict the instrument only to the protection of the rights of recourse of the creditors and thus validating the current practice. Such restriction implies that the TGR will

serve primarily as an instrument to enlarge the distribution to the unsecured creditors. However, as demonstrated in this research, that goal was hardly ever reached in practice. Consequently, the TGR does not provide any effective means in the fight against *criminal* condemnable behaviour with legal entities. Another option is to focus the instrument on the fight against *civil* reprehensible behaviour (apparent improper governance by directors and transactional avoidance). In this view, the instrument does not focus on the enlargement of the distribution to the unsecured creditors, but primarily on the general interest in the fight against such civil reprehensible behaviour. It is expected that the instrument of the TGR on such basis will have a broader scope and can be used in more cases and more effectively. Another view is to limit the instrument of the TGR to reprehensible behaviour which is also condemnable from a criminal law point of view. Such scope of the TGR requires an increase of the capacity and the expertise of the public prosecution, if necessary strengthened with a mandatory notification by the bankruptcy trustee of any offences, provided that the trustee will be adequately reimbursed and a duty to investigate will be imposed upon the public prosecutor.

In the second place, one could wonder whether or not the Ministry of Justice should execute the TGR for any of the purposes described above. It appears as if the emphasis of the TGR has shifted to the requirement that it must be almost certain that the bankruptcy trustee will have recourse on the wrongful acting director or perpetrator, instead of operating as a contribution in the fight against bankruptcy fraud. Possibly, one could leave this issue to the private market or perhaps privatisation of the funding of these legal actions and proceedings is an even better solution. Recently, a market for claims connected with bankruptcies developed. In this respect it is advisable to change the law and to make the trustee's claim pursuant to art. 138/248 Book 2 Dutch Civil Code transferable. Less far-reaching in the direction of market working or privatisation is the introduction of a so-called 'success fee' or 'commitment fee' in order to cover the operating costs of the TGR.