

LME Transactions Unveiled: insights from the Netherlands, Luxembourg, Belgium and Switzerland

1. Introduction

Liability Management Exercises (LMEs) are strategic actions taken by a company, together with a (group of) financier(s) to manage debt obligations. The primary goals of LMEs are to attract new liquidity, reduce the overall debt burden, extend maturities, and improve financial stability. The core of LMEs is that the company enters into a transaction with one (group of) financier(s), which transaction is in principle permitted under the existing financing documents and can be implemented without an in-court (restructuring) process.

It took a while for LMEs to gain a foothold in Europe. This is generally attributed to the different legal and cultural environments in Europe compared to the US, with normally relatively higher thresholds in ICAs. Europe has traditionally offered relatively light-touch and, compared to the US, less expensive restructuring processes, which would in principle reduce the need for LMEs. That being said, LMEs seem to be gradually gaining ground in Europe as well, driven in part by the growing presence of US funds in the European debt markets. In this article we provide different insights on the emerging European LME market from a Dutch, Luxembourg, Belgian and Swiss law perspective.

2. Different LME transactions

The most well-known types of LMEs are the following transactions:

- 1 **Open Market Purchases:** Repurchase of a modest amount of debt discretely.
- 2 **Tender Offers:** Companies offer to buy back medium-to-large amounts of debt at a specified price within a short time period
- 3 **Exchange Offers:** Creditors exchange existing debt for new debt with different covenant terms and, potentially, new (higher) security rights.
- 4 **Consent Solicitation Offers:** Alter existing covenant terms to suit changing needs with existing debt outstanding.
- 5 **Drop-down Financings:** Transferring assets to subsidiaries to raise additional liquidity, whereby security rights are created over those assets.
- 6 **Up-tiering:** Inserting priority tranches of debt or restructuring existing debt.
- 7 **Double-dip Transactions:** New financing provided to a non-obligor, which on-lends the financing to the parent company, which intercompany claim is secured in favour of the financier; the financier benefits from two security packages (from the non-obligor and the parent company).

3. Legal considerations

LMEs offer key advantages such as improved liquidity, extended debt maturities and potential cost savings. However, they can carry reputational considerations, for instance LMEs can influence how credit rating agencies view the company. In addition, there have been instances where non-participating financiers pursued legal actions believing the LME unfairly impacted their position. In that light, a careful assessment of fiduciary duties and potential risks is essential, especially given the difference in legal regimes across Europe.

While in the US much of the LME risk is centered around the terms and interpretation of the ICA, in Europe much of the emphasis is on fiduciary duties and insolvency filing requirements, which is described in this article. When dealing with public debt, it is furthermore important to consider capital markets regulatory considerations, like inside information, disclosure obligations and closed periods.

Directors' Duties

When the company faces financial distress, the following considerations should be taken into account by directors with regard to their duties.



Under **Dutch law**, if a company enters into a state of financial distress, its management should attach more importance to the interests of the creditors with a view to ensure the availability of recourse of their claims. There is no strict duty for the management to file for bankruptcy, however, the board should be careful in continuing the business of the company after it has become evident (or should have become evident) that the company had entered into a state of insolvency and should refrain from entering into new contracts when the director reasonably foresees that the company is unable to fulfil the obligations thereunder.



Under **Luxembourg law**, there is no real shift of director duties in case of financial distress – the board members of a Luxembourg company continue to owe their duties to the company and must act in the interest of the company. Naturally, if the financial situation deteriorates and the company becomes exposed to potential creditor claims, the board will need to assess those risks and factor all relevant circumstances into its decision-making.

Bankruptcy filing obligations arise where the company is in payment default and has lost its creditworthiness. Once these conditions are met, the board must file for bankruptcy within one month.



Under **Belgian law**, once a company enters into a state of financial distress – particular when insolvency becomes imminent, directors must increasingly take into account the interests of the company's creditors to carefully consider their equal treatment.

Bankruptcy filing obligations are triggered when the company is in persistent cessation of payment and has lost its creditworthiness. The board has 30 days to file for bankruptcy, once both conditions are met.



Under **Swiss law**, in a state of financial distress, directors must take timely measures to preserve liquidity and avoid over-indebtedness. While fiduciary duties do not formally shift, directors must appropriately take into account the interests of creditors and ensure equal treatment, especially when insolvency becomes imminent.

Bankruptcy filing obligations are triggered if the liabilities are no longer covered by the assets and there is no realistic prospect of a timely restructuring.

Creditor Consent

LMEs often require the consent of a significant portion of creditors. In Europe, obtaining this consent can be challenging due to fewer restructuring tools, less process flexibility, more transparency requirements, and varying legal frameworks across jurisdictions. In terms of European court led processes, much has been achieved in the last few years with the evolution of debtor in possession restructuring processes, which for some jurisdictions have been proven to be quite efficient.



Under **Dutch law**, the WHOA can be used to cram-down creditors. In addition, a Dutch share pledge enforcement is a proven restructuring mechanism, which can be completed with the required consents under the ICA.



Under **Luxembourg law**, the new restructuring framework can be used to cram-down creditors. However, given the novelty of these tools, their practical application is still evolving and certain aspects remain unclear. On the contrary, the very well court tested and very much used Luxembourg collateral law permits the use of a very fast, flexible and cost-efficient Luxembourg share pledge enforcement as an efficient restructuring mechanism, which can be completed with the required consents / distressed disposals under the ICA.



Under **Belgian law**, via a homologated restructuring plan, a company in distress can apply a (cross-class) cram-down to impose certain measures on dissenting creditors. Depending on ICA provisions, a secured creditor can also impose certain LMEs via enforcement of a share pledge (including via exercising the voting rights only) which is possible without prior notification or court approval.



Under **Swiss law**, there is no formal pre-insolvency restructuring regime with cram-down mechanisms, however, the court-approved moratorium allows for a restructuring plan that can bind dissenting creditors if approved by the required majorities. In addition, out-of-court restructurings are possible and often rely on ICAs to coordinate creditor actions.

Coercive Elements

Some LMEs may include coercive elements, such as “uptiering” or changing collateral value. See below per jurisdiction (i) how contracts (ICA’s) should be interpreted, and (ii) claw-back requirements.

	Interpretation of contracts to determine whether the LME is permitted	Requirements for nullification on the basis of fraudulent conveyance (cumulative)
The Netherlands 	The prevailing case law stipulates that other circumstances should be taken into account by interpreting (financing) agreements and the interpretation should not be based solely on the literal text. Instead, Dutch courts must consider the intentions and reasonable expectations of the parties involved, taking into account all relevant circumstances	<ol style="list-style-type: none"> 1. Non-participating financiers are prejudiced by the LME; and 2. The company and the participating financier to the LME had knowledge of such prejudice
Luxembourg 	When interpreting an agreement, courts shall consider the common intention of the contracting parties acting in good faith, instead of the literal meaning of the terms employed	<ol style="list-style-type: none"> 1. The transaction must have impoverished the creditor (creditor recoveries are diminished) 2. The transaction must have been performed with the intention to defraud creditors; and 3. The company must be insolvent at the time the claim is brought
Belgium 	Interpretation according to the common intention of the parties even if this differs from the literal meaning of the words. In particular if the agreement or relevant provisions are challenged and/or leave room for certain different interpretation	<ol style="list-style-type: none"> 1. Non-participating financiers are prejudiced by the LME; and 2. There was bad faith on the part of the insolvent company and the lender (i.e. knowingly taking action against the interests of the other creditors typically requiring proof that the transaction was abnormal and parties involved should have known about the abnormal nature and its prejudice to other creditors.
Switzerland 	Contractual and statutory rights of the non-participating creditors cannot be amended without their consent	<ol style="list-style-type: none"> 1. The non-participating financiers are prejudiced; and 2. The company and the participating financier were aware or should have been aware of the resulting prejudice

Tax Treatment

The tax treatment of LMEs can vary significantly across European jurisdictions. Companies must carefully consider the tax implications of debt buybacks, exchanges, and other restructuring activities to avoid adverse tax consequences.



The structure and type of the LME primarily determine the **Dutch** tax consequences. LMEs that reduce a company's debt – such as waivers or discounted buybacks – may trigger taxable waiver income at the level of the debtor. A debt waiver profit exemption may apply, subject to conditions. If applicable, such profits are generally exempt, although the debtor's in-year and carry-forward losses are reduced accordingly. Where LMEs involve intra-group transactions or related parties, the arm's-length principle must be observed, and interest deduction limitation rules should be considered. The Dutch conditional interest withholding tax (levied at 25.8%) may apply to payments to affiliated entities in low-tax jurisdictions or abusive structures, unless exemptions or treaty relief are available. Transactions such as back-to-back financing, creditor substitutions, and tender or exchange offers may require robust transfer pricing documentation to support deductibility and avoid potential recharacterization. VAT consequences are typically limited, though asset transfers or restructuring services may attract VAT depending on the nature of the services and structure.



The tax implications of an LME at borrower / issuer level in **Luxembourg** depend on the type of measure that will be put in place. Generally speaking, however, the following attention points should be on the radar of the parties to the arrangement. An LME that will lead to a reduction of the outstanding indebtedness of a Luxembourg borrower / issuer may give rise to an extraordinary income, which will be taxable at a rate of 23.87%. This extraordinary income can be offset by way of existing carried forward tax losses, to the extent available. Whilst Luxembourg generally does not levy withholding tax on arm's length interest payments, there are specific categories of interest that may give rise to withholding tax. A restructuring or a change to the terms and conditions of the loan / bonds should therefore be carefully reviewed, in order to ensure that the conditions for these categories to apply are not met. It is, moreover, important to ensure that transactions between related parties take place on at arm's length terms. If that is not the case, the Luxembourg tax authorities can requalify the transaction into a hidden dividend distribution (subject to 15% withholding tax, unless an exemption is available) or an informal capital contribution, or can proceed to a taxable upward profit adjustment. Additionally, it should be ensured that receivables on the balance sheet of a Luxembourg company always remain financed on a back-to-back basis, with a view to ensuring that the company does not incur adverse Luxembourg corporate income and net wealth tax consequences. Finally, whilst it is rare that transactions are subject to mandatory registration in Luxembourg, it is recommended to always keep an eye on this tax as well, as it may give rise to unpleasant surprises if triggered.



Under **Belgian law**, an LME resulting in a reduction of a Belgian company's overall indebtedness (e.g., through a debt waiver or a buyback at a discount) can trigger taxable income for the company. Furthermore, transferring assets to related entities during an LME must occur at market value and may incur registration duties. When structuring back-to-back financing arrangements, important transfer pricing considerations arise, requiring adherence to the arm's-length principle, and the beneficial ownership of the interest payments is rigorously scrutinized by Belgian tax authorities to ensure that any withholding tax exemptions or reduced rates are legitimately claimed by the ultimate recipient, not merely an intermediary. In addition, where new creditors are introduced, Belgium generally levies a 30% interest withholding tax, though various domestic and treaty exemptions may apply depending a.o. on the status and location of the creditor, necessitating thorough analysis to assess the eligibility thereto.



The **Swiss** tax implications of an LME depend significantly on the specific structure and type of the transaction. At the level of the Swiss company, LME transactions should in principle be reviewed from both a corporate income tax perspective (the applicable rate varies depending on the Swiss company's domicile) and an issuance stamp duty perspective (amounting to 1% of the value), which may be triggered (unless an exemption applies) depending on the applicable circumstances and the transaction as well as its implementation, particularly in scenarios involving debt waivers, debt-to-equity swaps, or drop-down financing arrangements. It should also be noted that if an LME transaction, particularly when a foreign beneficiary is involved, is not properly implemented, adverse Swiss dividend withholding tax consequences of up to 35% may arise. This Swiss withholding tax may be partially or fully reduced or reclaimed under an applicable double tax treaty between Switzerland and the foreign recipient's jurisdiction. In cases involving a change of creditor, it is crucial to analyse the Swiss non-bank lender rules to mitigate the risk of triggering additional Swiss withholding tax of up to 35% on interest payments. Additionally, LME transactions should be reviewed from a transfer pricing perspective, especially where related parties are involved. This includes arrangements such as back-to-back financing, creditor changes, tender offers, or exchange offers, where adherence to arm's length principles, or alternatively, to the safe harbour interest rates as annually published and updated by the Swiss Federal Tax Administration, is essential.

3. LME led governance changes

In certain instances, special committees are installed with the relevant companies to oversee the implementation of the LME as a matter of due process, or in order to manage conflicts of interests. In this respect, it is relevant to underline that in **all our four home jurisdictions**, directors' duties generally apply equally to all members of the board, as they share a "collective responsibility". While the board may delegate specific tasks by granting a power of attorney to a strategic or special committee to act on behalf of the company, the board (acting as a collective body) remains accountable for the overall management of the company. As a result, in all our four home jurisdictions, strategic or special committees remain under the overall supervision of the board of directors or, depending on the circumstances, serve only in an advisory capacity. Finally, it is relevant to underline that in all our four home jurisdictions, the concept of 'shadow directorship' or 'de facto directorship' applies, pursuant to which individuals or bodies who exercise actual decision-making power should comply with the directors' duties, even if they have not been formally appointed as directors.

4. Final remarks

While the US market is much more advanced as concerns the use of LMEs, these tools are increasingly being deployed in Europe. For companies in the Netherlands, Luxembourg, Belgium, and Switzerland, LMEs can be a powerful tool - not just to manage liabilities, but to reshape financial strategy. As each European jurisdiction has its own insolvency test and considerations around board of director liability, navigating the complexities of LMEs in Europe requires a thorough understanding of the legal and financial landscapes. With careful planning and legal insight, Dutch, Luxembourg, Belgian and Swiss companies (and their directors) can effectively manage their risks and liabilities and turn to LMEs for unlocking opportunities to build momentum for long-term stability and preserve value.

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