# Mediation and companies in distress

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Companies in distress need early and timely intervention to increase the chances of having a successful turnaround. Mediation and a court's confidential appointment of a specialised mediator can be helpful and even be key to this process. A mediator can resolve disputes, contribute towards devising the right measures to turn around the company and can possibly prepare for the opening of formal reorganisation proceedings that will be opened in an early stage of the distressed company, thereby increasing its chances of success in turning things around.

## Introduction

The court's appointment of a mediator to provide companies in distress with the assistance required for their survival is a measure that has existed for a long time.

As, from the first signs of difficulty, only prompt intervention enables companies in distress to turn themselves around, practitioners have seen the need to provide companies in distress with external and neutral third-party assistance even before insolvency proceedings begin.

A company experiencing only slight difficulties often sees them intensify within a matter of months or even a few weeks. Essential decisions for that company's survival must therefore be taken quickly, when the company and its stakeholders are going through a critical time. External support is often considered to be a rational and pragmatic option, and this is when mediation can play a crucial role.

Mediation has proved itself to be an alternative method for dispute resolution and is very successful in many sectors. This method of dispute resolution is increasingly being used in the business sector to resolve conflicts, especially conflicts between directors or shareholders. Mediation responds to the need to

avoid judicial proceedings and to embark on a more pragmatic and multidisciplinary approach to tackling the problem. It focuses on the importance of 'non-legal' issues. In this light, a mediator for a company in distress positions itself as an intermediary inside the tripartite relationship consisting of the debtor, the court and third parties, such as creditors.

The appointment of a mediator therefore responds to the need to offer economic players a flexible and informal method to support the debtor during its reorganisation in order to find a discreet and efficient solution to its conflicts and difficulties.

## How mediation for distressed companies compares with standard mediation

Although the function of a mediator in the context of a company in distress is inspired by the role of a mediator under ordinary law, the two roles are not identical.

The mediator's role in the context of a company experiencing financial difficulties is generally considered to be close to the role of a mediator under ordinary law in that the mediator acts as an intermediary between the debtor and third parties with whom the debtor is encountering problems – such as economic, strategic, logistical or other problems. Intervention by a mediator in a company in distress takes place on a strictly voluntary basis, similar to how a mediator intervenes under ordinary law.

However, the mediator appointed to assist a company in distress plays a more active role than a mediator under ordinary law. Essentially, the former is expected to intervene in the disputes encountered by the debtor and advise the debtor in its decision-making. It can act as an intermediary between the debtor and its creditors, encourage the debtor to question its corporate strategy, and suggest alternatives that it considers appropriate. In this way, the mediator acts as an adviser or assistant to the debtor, thereby intervening intensively in the problems being faced.

## Opportunities for mediation for companies in distress

### *Disputes inside the company*

The mediator is not restricted to dealing only with creditors. Although creditors are the mediator's main interlocutors, its task goes well beyond this: the mediator's interlocutors can also be the company's directors or managers, and shareholders or partners.

The mediator can therefore help the debtor solve conflicts and disputes between its directors (or managers), shareholders (or partners) or between the company's directors (or managers) and the shareholders (or partners) that are susceptible to obstructing the company's operations. In this regard, we are mainly referring to:

- potential breaches of the usual obligations that are incumbent on the directors of a company in distress;
- the obstructions caused by two groups of directors or managers in which no clear majority can be obtained;
- recurring problems with convening a general meeting or preparing financial statements;
- disputes between groups;
- situations in which a director or manager can be held liable under civil or criminal law;
- disputes over the paying up of share capital by partners or shareholders;
- disputes concerning a lack of liquidity, for example, the need for additional bank loans or for shareholders to make further personal investment in the company;
- procedures to withdraw or exclude shareholders;
- blocking a general meeting or the impossibility to obtain a clear majority; and
- disagreements over the appointment or resignation of directors or managers.

The mediator can also help the debtor solve disputes between the management and workers or union representatives in the company, especially in the following types of disputes:

- protecting jobs inside the company;
- negotiating the transfer of certain employment contracts under different conditions; and
- negotiating an effort by the company's workers to help the company continue to function.

### *Disputes outside the company*

In the context of a company in distress, the mediator will be asked to deal with a limited number of the company's external stakeholders (eg, creditors, suppliers, banks and commissioners), with a view to reorganising the company and safeguarding its activities. The mediator's usual tasks in relation to this are:

- negotiating deadlines for payment of debts to the company's creditors and suppliers;
- negotiating a possible reduction in late-payment interest and indemnities being demanded by the creditors;
- help with the company's cash flow, for example, by negotiating loans with banks or seeking alternative sources of financing;
- encouraging renewed contacts with certain creditors;
- starting the process of negotiating an amicable settlement with certain creditors; and
- approaching potential investors in or buyers of the company (the mediator can be a financier with a private equity or investment fund network).

### *Opposing interests without a recognised dispute*

There are certain situations in which a mediator can assist to resolve that do not create real conflicts or disputes in the strict sense of the word but cause functional tensions between the different players in the company and third parties. For example, when a financial backer realises that its debtor is unable to respect repayment deadlines and is obliged to take measures without entering into a personal dispute.

### *Anticipating risks of obstruction*

If the debtor foresees a risk that matters will worsen to the point where it will have to apply for reorganisation, a mediator can be appointed in anticipation to prepare creditors and obtain their cooperation as soon as possible. This would minimise the number of uncooperative creditors without alarming them or confronting them with the fait accompli of the start of the formal reorganisation procedure.

### *Other collateral losses*

In some companies, especially family-held ones, events outside the company's administration and operations can have an unfavourable impact on management, throwing the company into problems. Such a situation is even more likely in a poor economic climate. The company's players must therefore make vital decisions in difficult times. In these circumstances, the mediator can help the debtor to organise and protect the company's future.

The following are examples of such situations:

- a single director's incapacity for medical reasons;
- an event in which confidentiality is essential for the company's survival (a complex trial or the conviction of the delegate responsible for the company's day-to-day management or its main shareholder); or
- specific events in family-held companies, such as succession, joint ownership, family disputes or divorce.

## The mediator's trump cards for a company in distress

Involving a mediator outside or before the opening of the reorganisation procedures maximises the chances of success of the company's turnaround because the mediator holds a number of trump cards.

### *Confidentiality*

The bad publicity surrounding a formal insolvency procedure is viewed negatively by the business world and often hastens the demise of a company in distress. It can also result in creditors refusing to deal with the company and suppliers withholding goods while awaiting payment. Furthermore, there are specific clauses in contracts stating that such events will result in the termination of the contract or, at the very least, the deterioration of commercial dealings. The appointment of a mediator, however, can be confidential and in such cases, not publicised. Confidentiality can be the result of appropriate national legislation as is the case in Belgium, or from a court's order, or even from a separate agreement between the mediator and the debtor if need be. The confidentiality surrounding the mediator's work therefore provides a valuable and indisputable advantage compared to other practitioners who could be appointed. In addition, the confidentiality attached to the mediator's role is twofold, applying to both its appointment and its work.

This enables the mediator to retain the confidence of third parties, who are familiar with confidentiality obligations, without alarming them and therefore allowing the company's business activity to continue.

### *Neutrality and impartiality*

Another important aspect to the mediator's role is that the mediator holds a neutral position. Since it is appointed by a judge, the mediator's position as a person of trust is reinforced.

However, the impartiality required of mediators for companies in distress is not as strict as that which is required for mediators under ordinary law or for other insolvency practitioners, and one can even talk about a 'nuanced' impartiality. The mediator's task involves advising the debtor and giving an opinion on strategies or behaviour. This means the mediator is inevitably more heavily involved in the relationship with the debtor.

The mediator therefore offers more guarantees concerning the accuracy of company data, which, during negotiations, it discloses to the court and to third parties because this ensures it does not compromise the mediator's independence or reputation.

### *Authority*

In the same vein as the previous point, one can consider the court's intervention in the appointment process offers a non-negligible benefit from the point of view of analysing the subsequent risks of the management's acts that are being contested on the basis of the mediator's suggestions and propositions. The management benefits from an additional lever in terms of the legality of the operations performed.

The liability of a company in distress's directors can be reduced by the assistance of a specialised mediator because any restructuring measures are implemented in consultation and cooperation with a court-appointed neutral expert. It will therefore be more difficult for third parties to prove that the managing director has not acted in a careful and prudent manner.

The moral authority that the mediator enjoys from its professional knowledge and court appointment can also lead the partners involved in negotiations to make greater concessions.

#### *Existing management maintains control*

The mediator does not take over the management or control of the company. It analyses and negotiates, suggesting avenues for solutions, but does not have the debtor's decision-making power.

The mediator's appointment and performance do not upset the existing management structure, and this differentiates the mediator from an administrator under ordinary law. Management retains the freedom to make company-related decisions, whereas an administrator possesses actual authority, defined by the court and sometimes demarcated, that the management cannot contest.

The mediator therefore supplements the company's existing structure, which is not modified. The mediator does not threaten existing management, who will be relieved to take action rapidly based on the mediator's enlightened advice.

#### *Adaptability and flexibility of the procedure*

The appointment of a mediator has genuine benefits in terms of adaptability and flexibility. The appointment is made within the scope of an agreement between the court and the company in distress on the request of the company itself, possibly after a suggestion by the court or by the insolvency court. The purpose of the appointment is to create the conditions for turning the company around or for stabilising it in a less conflictual context.

The mediator is not obliged to report to the court about its task. This flexibility of the mediator's mandate starkly contrasts with the formal nature of the judicial reorganisation.

The mediator's confidential work procedure provides the debtor with a period for negotiating, during which the debtor can choose which of its less uncooperative interlocutors it wishes to obtain an agreement or transfer with. The subsequent formal period of reorganisation can therefore be substantially shortened or can even become a formality, permitting the pre-established agreement to be officialised, or providing a means exerting pressure on stubborn creditors for them to endorse the agreement made with the initial creditors.

## Profile of the mediator

Subject to specific provisions in the applicable national law, the choice of who should be appointed as a mediator depends on the actual circumstances of the distress. Should the reasons of the distress essentially be financial or economic, then the appointment of an auditor might be the appropriate choice. Should the distress be caused by legal issues and disputes, a legal expert might be more appropriate. Ideally, the mediator will be chosen among the mediators complying with their national legislations and accredited by official state bodies because of their education and training in principled negotiation.

However, this is not always the case. In Belgium, for instance, should a court decide to appoint a mediator in the course of litigation, the court is legally obliged to appoint a mediator who is accredited with the federal state authority. Such a requirement does not apply in the case of 'company mediation' in the framework of insolvency, and the court may freely chose a mediator.

## The company mediator under Belgian law

Belgian insolvency legislation expressly provides for the appointment of a mediator to assist a company in distress. The mediator is known as 'a company mediator', or *médiateur d'entreprise* in French and *ondernemingsbemiddelaar* in Dutch. Belgium is one of the very few countries to stipulate this specifically in its insolvency law.

The company mediator is appointed on the sole initiative of the debtor. The company assesses the expediency for, and the potential contribution from, appointing the mediator having regard to the circumstances, economic climate and the company's specific needs. Since the appointment of the mediator is, in essence, a voluntary appointment, imposing such an appointment would be contrary to the philosophy of mediation.

The president of the court or the specific chamber for companies in distress specifies the extent and duration of the company mediator's task by issuing an order. The court's power is limited because the order must observe the limits and scope of the debtor's application. No appointment or mediation task can be imposed on the debtor without its agreement, but the court or the specific chamber for companies in distress can suggest an appropriate task for a specific problem.

Company mediation is voluntary. Consequently, under Belgian law, the company mediator's task ends when either the debtor or the mediator decides on it. The mediator's task can also be prolonged after the reorganisation procedure starts, if the debtor and the mediator so desire.

## Conclusion

The appointment of a mediator to help turnaround a company in distress is a powerful but regrettably little-known tool, especially in Europe.

There is all the more reason to have a mediator in large companies where there are complex problems that often have international dimensions. Nevertheless, as a tool, its cost can also be limited making it suitable for small companies too.

A prudent intervention by a specialist upstream of the debtor's difficulties is regarded as an effective and pragmatic solution in response to the different players' current problems. The skills and qualities inherent in the mediator's role make this an ideal solution for quickly obtaining an agreement with creditors or preparing to transfer the business activities to be saved.

The mediator enables a full and detailed analysis of the company's difficulties. The flexibility of its status and of the procedure enables the company to customise the mediator's role in accordance with its needs and objectives.

Finally, an awareness campaign must be carried out at management level of companies in distress to draw their attention to the benefits of this tool.

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