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An economic analysis of Dutch, US and German law

Jonkers, A.L.

Publication date

2020

Document Version

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Citation for published version (APA):

Jonkers, A. L. (2020). *Insider guarantees in corporate finance: An economic analysis of Dutch, US and German law*. [Thesis, fully internal, Universiteit van Amsterdam].

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INSIDER GUARANTEES IN CORPORATE FINANCE

An economic analysis of Dutch, US and German law

A.L. Jonkers

Insider guarantees in corporate finance

An economic analysis of Dutch, US and German law

ACADEMISCH PROEFSCHRIFT

ter verkrijging van de graad van doctor aan de Universiteit van Amsterdam op gezag van
de Rector Magnificus

prof. dr. ir. K.I.J. Maex

ten overstaan van een door het College voor Promoties ingestelde commissie, in het
openbaar te verdedigen in de Aula der Universiteit

op vrijdag 17 januari 2020, te 13.00 uur door Aart Lambertus Jonkers
geboren te Kampen

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Insider guarantees in corporate finance

An economic analysis of Dutch, US and German law

Summary - Insider guarantees play a crucial role in both the structuring of lending transactions of small and medium enterprises (SMEs), in which situation a private person who is shareholder or director of the enterprise often guarantees business debts towards a professional creditor such as the main bank, and in the structuring of large corporate groups, in which group companies often guarantee each other's debts towards a major lender. The dynamics involved in both situations are however underexposed in legal literature. This thesis aims to fundamentally impact the debate on guarantees in corporate finance. Distributional concerns in relation to weak guarantors have to some extent been brought forward in the literature, whereas the efficiency of the guarantee relationship in corporate finance has often been assumed, which may also have held back addressing distributional concerns. This book thoroughly reviews both the efficient functions and the opportunistic uses of the guarantee relationship towards both insiders and outsiders of the relationship from an economic perspective and compares Dutch, German and US law with reference to the economics involved.

The economic analysis of the guarantee relationship in corporate finance firstly shows it can indeed lead to efficiency gains. Those gains can however usually not be ascribed to the relatively uncontroversial functions of specialization in risk bearing, specialization in monitoring or signaling credit quality. The guarantee relationship in corporate finance instead often leads to efficiency gains by influencing the behavior of guarantor and debtor, more specifically reducing moral hazard created by limited liability towards the lender. This function deserves close scrutiny as changing the behavior of debtor and guarantor is likely to have effect on outsiders to the guarantee relationship.

The guarantee relationship is prone to opportunistic use towards both insiders and outsiders of the relationship. The analysis of opportunism towards insiders shows that such opportunistic use can be distributionally suspect, even in the context of corporate finance. Opportunistic use towards insiders can also lead to various inefficiencies, including overly cautious business decisions and high bankruptcy costs in case the guarantee is triggered. US law offers little protection against such opportunistic use. Dutch and German law do have some instruments to protect weak guarantors, but these instruments usually do not apply when a business owner guarantees corporate debts. The efficiency analysis has shown that such protection is warranted and probably would do little harm to the core efficient function of guarantees as guarding against moral hazard.

This book really breaks new ground in the analysis of opportunistic use of the guarantee towards outsiders of the relationship. Two main types of such opportunistic use are distinguished: (1) opaque priority structures and (2) covert insider dealing. When guarantees are used in setting up an opaque priority structure, the opportunistic behavior essentially occurs on the moment that the guarantee is issued. With a combination of incorporating and piercing the shield that incorporation creates with a guarantee, the guaranteed creditor can opportunistically profit from this often opaque structure in relation to other creditors of the debtor and guarantor. German, Dutch and US law regulate this behavior to a limited extent and need substantial improvement, which can be effected without threatening the core efficient function of the guarantee relationship in corporate finance.

Covert insider dealing through guarantees in turn comprises opportunistic behavior that occurs after the guarantee is concluded, but which is incentivized by the guarantee. The most obvious example is a shareholder or director who influences or represents the company in making payments on debts guaranteed by him or her or by a group company, at a time when the business is already beyond savior. German and US law regulate such behavior to some extent but both could do with some improvement, which can again be implemented without substantially threatening the core efficient functions of the guarantee relationship. Dutch law hardly regulates this type of behavior and needs substantial improvement.

Garanties van insiders in ondernemingsfinanciering

Een economische analyse van Amerikaans, Duits en Nederlands recht.

Samenvatting - Garanties van insiders spelen een sleutelrol in zowel de structurering van MKB-financiering, waarin de natuurlijke persoon die de aandelen houdt of bestuurder is van de te financieren onderneming vaak garant staat voor de schulden van de onderneming, als in de structurering van de financiering van grote groepen van vennootschappen, waarin de groepsvennootschappen veelal elkaars schulden garanderen richting de grootste schuldeiser. De dynamiek hierbij krijgt echter onvoldoende aandacht in de juridische literatuur. De vraag of de rechtvaardigheid gebiedt dat zwakke partijen die garant staan (meer) beschermd worden is wel uitgebreid aan bod gekomen, terwijl tegelijk de efficiëntie van het gebruik van garanties in ondernemingsfinanciering veelal aangenomen wordt. Dit proefschrift onderzoekt zowel de efficiënte functies van garanties, als de mogelijkheden tot opportunistisch gebruik van garanties richting zowel insiders als buitenstaanders van de garantie. Amerikaans, Duits en Nederlands recht worden vervolgens vergeleken tegen het licht van de economische dynamiek.

De economische analyse van garanties in ondernemingsfinanciering laat zien dat garanties inderdaad tot efficiëntievoordelen kunnen leiden, maar dit kan veelal niet worden toegeschreven aan minder controversiële functies, zoals specialisatie in het dragen van risico, specialisatie in monitoren van de debiteur en signaleren van kredietwaardigheid. Integendeel, de efficiëntievoordelen worden voornamelijk behaald door de belangen van de garant in lijn te brengen met die van de crediteur en aldus het gedrag van de garant en indirect de debiteur te beïnvloeden. Deze functie dient nauwgezet onderzocht te worden, aangezien het veranderen van het gedrag van garant en debiteur invloed zal hebben op buitenstaanders die niet voor de garantie gekozen hebben.

De garantierelatie is vatbaar voor opportunistisch gebruik ten opzichte van zowel insiders als buitenstaanders van de relatie. De analyse van opportunisme jegens insiders laat zien dat dergelijk opportunistisch gebruik verdacht kan zijn, zelfs in de context van ondernemingsfinanciering. Verschillende inefficiënties worden beschreven, waaronder te voorzichtige zakelijke beslissingen en hoge faillissementskosten in het geval de garantie ingeroepen wordt. Het Amerikaanse recht biedt te weinig bescherming tegen dergelijk opportunistisch gebruik. Nederlands en Duits recht hebben enkele instrumenten om zwakke garanten te beschermen, maar deze zijn meestal niet van toepassing wanneer een aandeelhouder ondernemingsschulden garandeert. De efficiëntie-analyse laat echter zien dat dergelijke bescherming noodzakelijk is en weinig in de weg zou staan aan de belangrijkste efficiënte functies.

Dit proefschrift is met name vernieuwend in de analyse van opportunistisch gebruik van garanties ten opzichte van buitenstaanders ten aanzien van de garantie. Twee categorieën van dergelijk opportunistisch gebruik worden onderscheiden: (1) ondoorzichtige prioriteitsstructuren en (2) verborgen voordelen voor insiders. Wanneer garanties worden gebruikt bij het opzetten van een ondoorzichtige prioriteitsstructuur, doet het opportunistische gedrag zich reeds voor op het moment dat de garantie wordt afgegeven. Met een combinatie van het incorporeren met beperkte aansprakelijkheid en het doorboren van het schild dat incorporatie creëert met een garantie, kan de gegarandeerde crediteur opportunistisch profiteren van deze vaak ondoorzichtige structuur ten opzichte van andere crediteuren van de debiteur en de garant. Duits, Nederlands en Amerikaans recht reguleren dit gedrag slechts in beperkte mate en moeten aanzienlijk worden verbeterd, hetgeen kan worden bereikt zonder de belangrijkste efficiënte functie te bedreigen.

De categorie van verborgen voordelen voor insiders omvat opportunistisch gedrag dat optreedt nadat de garantie is gesloten, maar dat door de garantie wordt gestimuleerd. Het meest voor de hand liggende voorbeeld is een aandeelhouder of bestuurder die het bedrijf beïnvloedt of vertegenwoordigt bij het doen van betalingen op door hem of haar of door een groepsmaatschappij gegarandeerde schulden, op een moment dat het bedrijf al bijna of geheel verloren is. Duits en Amerikaans recht reguleren dergelijk gedrag tot op zekere hoogte, maar kunnen verder verbeterd worden, welke verbeteringen geïmplementeerd kunnen worden zonder de wezenlijke efficiënte functies van de garantierelatie substantieel te bedreigen. Nederlandse recht reguleert dergelijk gedrag niet of nauwelijks en moet aanzienlijk worden verbeterd.

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Acknowledgements

I sincerely thank the Faculty of Law of the University of Amsterdam and specifically the Centre for the Study of European Contract Law for the opportunity to conduct this research. I particularly would like to thank prof. R.J. de Weijs and prof. A.F. Salomons for their excellent supervision of this project, which made me enjoy working on it throughout. The other colleagues at the Department of Private Law were also great. Special mention goes out to those I shared my office with, first and foremost Beatrijs van Schilfgaarde but also Anna van Duin, Olga Falgueres de Alamo and Irina Domurath. I feel very honored that the members of the PhD committee, prof. M. Brinkmann, prof. H.J. de Kluiver, prof. C.E. du Perron, dr. J. Roest, prof. R. Squire and prof. J. Vananroye have taken the time to read my manuscript. I would also like to thank my parents for their great care and of course my amazing wife Mary Gatacre and my children Edward, Elisabeth and Joseph.