

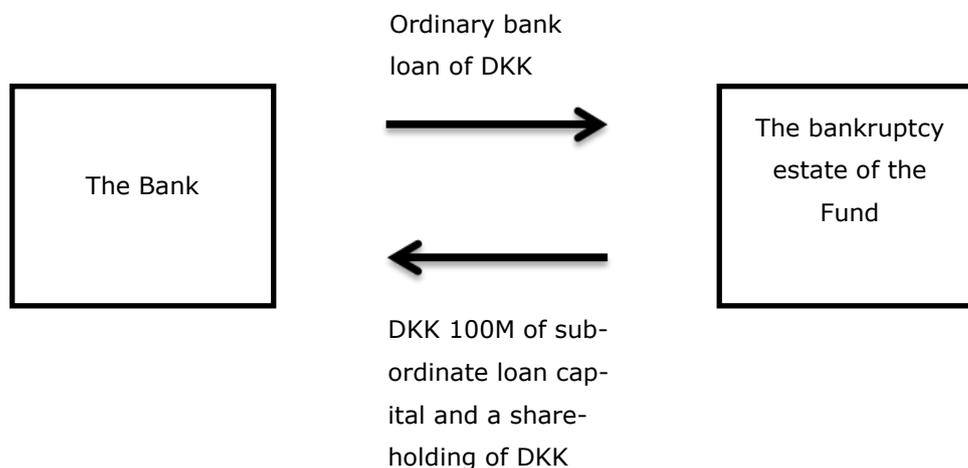
LEADING DECISION REGARDING SET-OFF AGAINST SUBORDINATE LOAN CAPITAL

31 January 2013, the Danish Supreme Court delivered its decision in a leading case regarding set-off against subordinate loan capital. According to the Danish Supreme Court, a bank was entitled to set-off its claims for repayment of two ordinary bank loans against the bankruptcy estate's claim against the bank for repayment of subordinate loan capital. The Danish Supreme Court upheld the High Court's decision and ruled that the general conditions for set-off against a bankruptcy estate were fulfilled.

The Case in brief

In 2008, Vestjysk Bank A/S (in the following referred to as the "Bank") granted two ordinary bank loans totalling DKK 140M to EBH-Fonden (in the following referred to as the "Fund"). The Fund invested a total amount of DKK 40M of the borrowed money in shares in the Bank and provided the Bank with a subordinate loan of DKK 100M. As the subordinate loan was to be included in the capital base of the Bank, it was a condition that the Danish Financial Supervisory Authority granted permission for early redemption, should early redemption be carried out on the borrower's initiative.

Should it not be possible to carry out the set-off, the Bank would only be able to make its claims against the bankruptcy estate, but would at the same time be obliged to repay the subordinate loan when it became due.



When the Fund was declared bankrupt in November 2009, the ordinary loans became due. After the date when the petition for a liquidation order was presented to the court and before the date of the liquidation order, the Bank was granted permission for early redemption of the subordinate loan by the Danish Financial Supervisory Authority, as the Bank wished to repay the subordinate loan by set-off. Subsequently, the Bank set its claim on the two ordinary bank loans off against the subordinate loan.

The Bankruptcy Estate of the Fund raised objections against the set-off and stated that set-off could not be carried out due to the nature of the subordinate loan.

The legal Background

The normal conditions for set-off against bankruptcy are i) reciprocity between the parties, ii) the claims may be equalised, iii) the counterclaim is a bankruptcy claim, iv) both the counterclaim and the main claim exist at the date when the petition for a liquidation order was presented to the court or are both established between the aforementioned date and the date of the liquidation order, and v) set-off is not impossible due to the nature of the claims.

The Decision

The Supreme Court upheld the High Court's decision, which allowed set-off, and referred to the grounds for the High Court's decision. Particularly, the High Court's grounds were the following:

- that the purpose of the provision of that time in the Danish Financial Business Act section 136¹ on the Danish Business Authority's granting of permission to redeem a subordinate loan before the agreed due date was to stabilise the capital base in a credit institution which has obtained a subordinate loan.
- that the fact that the bankruptcy estate's claim against the Bank was a subordinate loan did not imply that the Bank's set-off was precluded due to the nature of the claims,
- that it was without importance for the permission for set-off when the Danish Financial Supervisory Authority's permission was given.
- that there were no terms in the agreement or other circumstances which precluded set-off.

Furthermore, the High Court ruled that the set-off took effect from the date of the liquidation order, and therefore the bankruptcy estate was not entitled to interests from that date, which was the Supreme Court agreed, as the Supreme Court added that the permission from the Financial Supervisory Authority had been granted at the date of the liquidation order.

Our Assessment

The Supreme Court has established that the "nature" of a claim does not prevent a bank from using ordinary claims for set-off against subordinate loans.

¹now added to executive order 915 of 12 September 2012 on the calculation of capital base

If you have any questions or require additional information on the decision, please contact partner Christoffer Galbo (cga@mwblaw.dk) or junior associate Ted Rosenbaum (tro@mwblaw.dk)

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