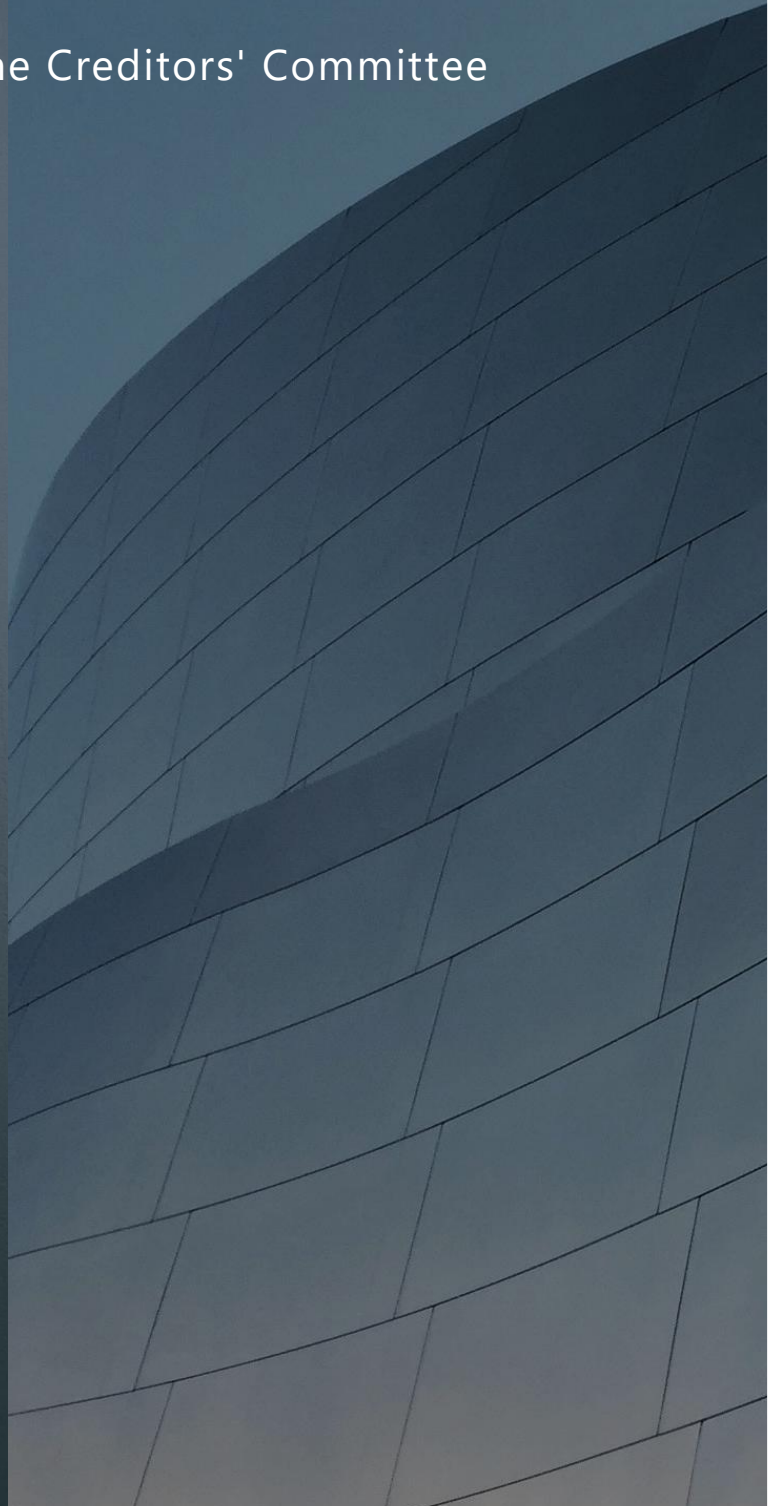


MAYER | BROWN

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GERMAN INSOLVENCY LAW

Rights and Duties of the Creditors' Committee



RIGHTS AND DUTIES OF THE CREDITORS' COMMITTEE

The principal body representing insolvency creditors is the creditors' assembly, through which creditors jointly exercise their rights vis-a-vis the insolvency debtor, the insolvency court and the insolvency administrator. Another important body that ensures creditor autonomy is the creditors' committee (*Gläubigerausschuss*), a representative body typically elected by the creditors' assembly. The creditors' committee's role is comparable to the monitoring bodies of a supervisory or advisory board under corporate law, and its primary functions include supervisory and supporting tasks vis-a-vis the insolvency administrator.

By appointing a creditors' committee, insolvency creditors can strengthen their influence over the insolvency proceedings. In most cases, creditors are only informed about the current status of the proceeding and decide on specific measures of the insolvency administrator in the initial reporting meeting, the claims verification meeting and the final meeting of the creditors' assembly. In contrast, the creditors' committee ensures that the creditor groups it represents are better and more regularly informed about the insolvency proceeding and the actions taken by the insolvency administrator. Furthermore, the creditors' committee provides creditors with a limited ability to influence certain decisions.

I. APPOINTMENT OF THE CREDITORS' COMMITTEE

Unlike the totality of creditors – which comes into existence automatically upon the opening of insolvency proceedings, with every creditor represented and only requiring an invitation to an assembly – the creditors' committee must be appointed separately. In this regard, the German

Insolvency Code distinguishes between several types of committees:

- The provisional committee as a compulsory committee pursuant to Sec. 22a para. 1 German Insolvency Code (*Insolvenzordnung*, “**InsO**”), which – except in very few cases – must be appointed if certain codified key figures regarding the debtor's balance sheet total, turnover and number of employees are met;
- The optional provisional committee pursuant to Sec. 22a para. 2 InsO, which can be appointed upon request of the debtor, a creditor or the preliminary insolvency administrator during preliminary insolvency proceedings;



- The interim committee pursuant to Sec. 67 para. 1 InsO, which is typically established in larger proceedings and can, in particular, be appointed, if the insolvency administrator must make material decisions regarding the insolvency estate before the first creditors' assembly takes place;
- The final creditors' committee pursuant to Sec. 68 InsO;
- The group creditors' committee pursuant to Sec. 269c para. 1 InsO, which the insolvency court may appoint in case of group insolvencies – where separate creditors' committees exist for various insolvent

group companies –at the request of one of these committees. Each (including provisional) creditors' committee of group companies of not merely minor importance provides one member to the group creditors' committee.

The appointment of the final creditors' committee is resolved by the creditors' assembly. If a preliminary and/or interim committee has already been appointed prior to the first creditors' assembly, the assembly decides whether it should be retained.



Upon request of a creditor with a right to separate satisfaction, a non-subordinated ordinary creditor or the insolvency administrator, the insolvency court may revoke the creditors' assembly's resolution to appoint or retain a creditors' committee, if the creditors' assembly's resolution disregards the common interests of the creditors.

II. COMPOSITION OF THE CREDITORS' COMMITTEE

When composing the creditors' committee, all relevant groups of creditors – such as creditors with a right to separate satisfaction, creditors with the highest claims, small claims creditors and employees – should be considered. The actual selection of the creditors' assembly or the insolvency court is subject to their best judgment; thus, they are free to determine the precise number of committee members, and the creditor groups represented. The insolvency administrator and the insolvency debtor are excluded from membership.

Representatives of the individual creditor groups do not necessarily have to be creditors themselves; external experts may also be appointed. To avoid a deadlock in decision-making, the committee should be composed of an odd number of members.

Once the creditors' assembly has approved or appointed a final creditors' committee and its specific composition, the appointment of individual members may only be revoked for cause. Moreover, a member of the creditors' committee cannot resign from office without cause. However, the creditors' assembly may appoint additional members at any time.

III. INDEPENDENCY OF THE CREDITORS' COMMITTEE

The creditors' committee is independent of any other body in the insolvency proceeding. Unlike the creditors' assembly, the creditors' committee is not subject to the supervision of the insolvency court. Accordingly, the insolvency court cannot revoke or correct resolutions of the creditors' committee or impose administrative sanctions on its members. The court also cannot demand to be informed about the results of committee meeting or request the minutes. In addition, the creditors' committee is independent vis-à-vis the creditors' assembly; the assembly has no right of direction over the committee and cannot resolve to revoke or amend its decisions.

On the other hand, the creditors' committee has no right to issue instructions to the insolvency administrator. Any misconduct discovered must be reported to the insolvency court to prompt intervention. The creditors' committee has no influence on general management except as explicitly provided by statutory law.

All rights and obligations of the committee pertain only to the internal relationship among the parties involved in the insolvency proceedings. The committee is not entitled to make binding declarations externally or establish any debts of the

insolvency estate (*Masseverbindlichkeiten*). Thus, despite its rights, the creditors' committee remains a supportive and monitoring body rather than an executive one. Any actions by the committee or its members – particularly regarding contract negotiations or the establishment of debts of the insolvency estate – are therefore excluded.

IV. REPRESENTATION OF INTERESTS

Although the creditors' committee is independent of the creditors' assembly, its members must act in the interest of all creditors. Each member, whether a creditor or a representative of a creditor or creditor group, must act independently, without taking instructions and pursuing special interests. Pursuing individual interests constitutes a breach of duty, as does favoring the interests of a specific creditor. Particularly problematic is the exploitation of an advantage based on advance information obtained through committee membership.

V. RIGHTS AND DUTIES OF THE CREDITORS' COMMITTEE

The principle of creditor autonomy, which is fundamental to insolvency proceeding, requires that the insolvency administrator be monitored and that creditors are involved in essential decisions. The legislator has provided a system that combines governmental supervision with creditor monitoring. The insolvency administrator is subject to judicial oversight by the insolvency court. Furthermore, Sec. 160 InsO, which requires the insolvency administrator to obtain consent of the creditors' committee for particularly important legal acts, demonstrates the legislator's intent to significantly strengthen creditor participation.

1. SUPPORT AND MONITORING

The core responsibility of the creditors' committee is to support and monitor the insolvency administrator. As part of its supervisory duty, the committee must inform itself about the state of the business operations, access books and records, and

monitor financial transactions and cash on hand. In large proceedings, third-party specialists may be engaged to fulfill these obligations.

The nature and extent of the committee's support and supervisory actions depend on the necessities and goals of the proceeding. For example, diligence standards are heightened if the debtor company is being continued by an insolvency administrator lacking relevant industry expertise. Unlike the insolvency court, the creditors' committee must not only monitor the lawfulness but also the appropriateness and economic efficiency of the administrator's actions.



2. SELECTION OF THE INSOLVENCY ADMINISTRATOR

One of the most important rights of the creditors' committee is participation in the appointment of the insolvency administrator. Pursuant to Sec. 56a InsO, the preliminary creditors' committee must be given the opportunity to determine requirements for the insolvency administrator, which the insolvency court must consider when making the appointment. The court may only deviate from an unanimous proposal of the provisional creditors' committee if the proposed person is unfit for the office.

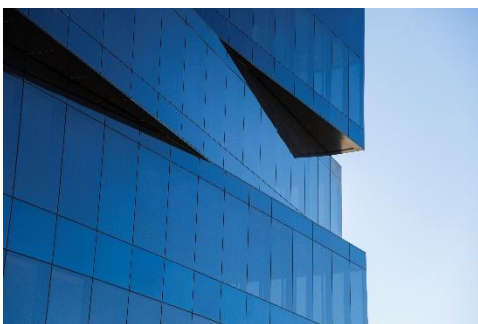
3. INFORMATION RIGHTS

To effectively exercise its support and control duties, the creditors' committee has information

and notification rights vis-à-vis the insolvency administrator, the insolvency trustee (Sachwalter) and the debtor. Under Sec. 261 para. 2 InsO, the insolvency administrator must inform the committee about the status and prospects for the successful fulfillment of an insolvency plan. The insolvency trustee must immediately notify the committee upon identifying circumstances that could be detrimental to creditors in a debtor-in-possession proceeding (Eigenverwaltung). The debtor is also obliged to provide information on all aspects relating to the proceedings (Sec. 97 para. 1 sentence 1 InsO). Additionally, under Sec. 258 para. 3 sentence 2 InsO, the committee must be notified in advance of the effective date of the closure of the insolvency proceeding.

4. MOTION RIGHTS

In line with its supporting and monitoring duties, the creditors' committee has the right to file certain motions. For example, under Sec. 59 para. 1 sentence 2 InsO, the committee may seek the dismissal of the insolvency administrator for material reasons. Under Sec. 75 para. 1 no. 2 InsO, the committee may apply to the insolvency court to convene a creditors' assembly.



5. APPROVAL AND RATIFICATION RESERVATIONS

The insolvency administrator is required to obtain the consent of the creditors' committee for certain measures. Under Sec. 160 InsO, measures of particular importance to the insolvency proceedings

require the committee's prior approval. Such measures include, for example, the sale of the debtor's company, business or all inventories; taking out a loan that would place a substantial burden on the insolvency estate; or deciding to conduct or settle a lawsuit involving a significant amount in dispute.

Additional approval requirements exist, for example, regarding distributions to the insolvency creditors (Sec. 187 para. 3 sentence 2 InsO), rejection of the insolvency plan (Sec. 231 para. 2 InsO), or continuation of disposition and distribution after suspension (Sec. 233 InsO). However, if the insolvency administrator fails to obtain required approval, the validity of the measure vis-a-vis third parties is not affected.

6. CO-DETERMINATION AND PARTICIPATION RIGHTS

The creditors' committee also has certain co-determination and participation rights, including those under Secs. 195, 187 para. 3 sentence 2 InsO regarding distribution of the insolvency estate, Sec. 149 para. 1 InsO relating to the investment of funds, and Sec. 218 para. 3 InsO concerning the preparation of insolvency plans by the administrator.

7. RIGHTS TO COMMENT AND TO BE HEARD

The committee has rights to comment and to be heard, for instance regarding the termination of insolvency proceedings (Sec. 214 para. 2 sentence 1 InsO).

VI. ORGANIZATION AND RESOLUTIONS OF THE CREDITORS' COMMITTEE

The creditors' committee is entitled to establish its own rules of procedure, which may be particularly advisable in large proceedings. Apart from the provisions in Sec. 72 InsO, the German Insolvency Code contains no specific rules regarding the

organization of the creditor's committee, such as the election of a chairperson and deputy, the convening of meetings, or the procedure for adopting resolutions.

Resolutions of the creditors' committee require a simple majority (Sec. 72 InsO). For a resolution to be valid, a majority of the committee members must be present.

Within the committee, the principle of equality applies; the amount of registered claims is irrelevant. A decision is passed if it receives the majority of the votes cast. In case of a tie, the motion is deemed rejected. Multiple voting rights, such as for the chairperson, are prohibited.

VII. LIABILITY

Under Sec. 71 InsO, members of the creditors' committee are liable to creditors with a right to separate satisfaction and to insolvency creditors for culpable breaches of statutory duties, but not to the debtor, preferential creditors (*Massegläubiger*), or creditors entitled to segregation (*aussonderungsberechtigte Gläubiger*). Liability particularly covers culpable breaches of supporting and supervisory duties. The standard of liability is that of a prudent and conscientious committee member, taking into account the member's personal ability and experience. However, a member cannot exculpate themselves by claiming a lack of necessary experience; accepting the office entails an obligation to inform oneself accordingly.

If several committee members breach their duties, they are jointly and severally liable. Typically, insurance coverage comparable to D&O insurance is obtained for committee members.

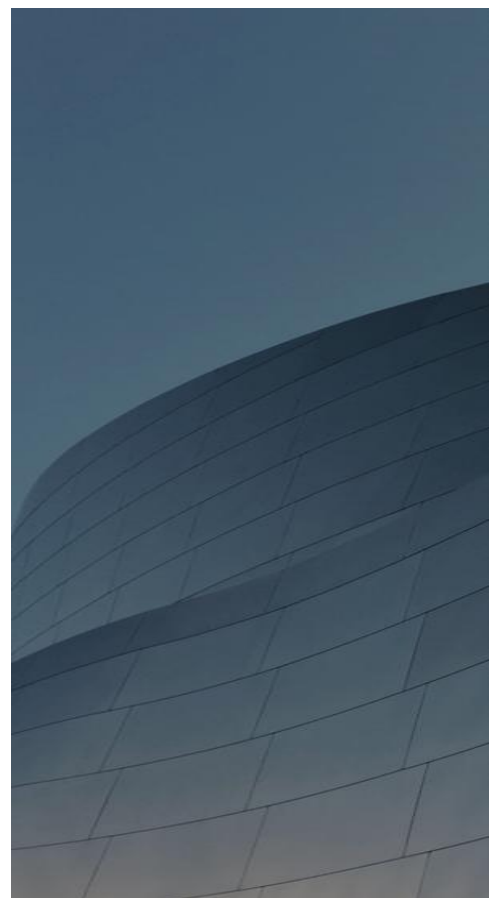
CONCLUSION

A creditors' committee can act much faster and more flexibly than the creditors' assembly. Its appointment is particularly advisable in larger proceedings, where a committee is mandatory, as well as in debtor-in-possession proceedings and in

insolvency proceedings where the debtor's business is (at least preliminarily) being continued.

Although committee members – despite representing specific creditor groups – are obliged to fulfill their duties independently and free from particular interests, the risk of conflicts of interests is inherent to the office and cannot be denied. Moreover, membership in the creditors' committee confers a considerable information advantage over other creditors, enabling members to gain a better understanding of the ongoing proceeding and, often, to influence the proceedings.

Given these circumstances, a membership in a creditors' committee also entails a significant liability risk. In most cases, however, this risk is significantly mitigated by obtaining insurance coverage comparable to D&O insurance. Ultimately, the benefits of committee membership should outweigh the potential disadvantages.



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