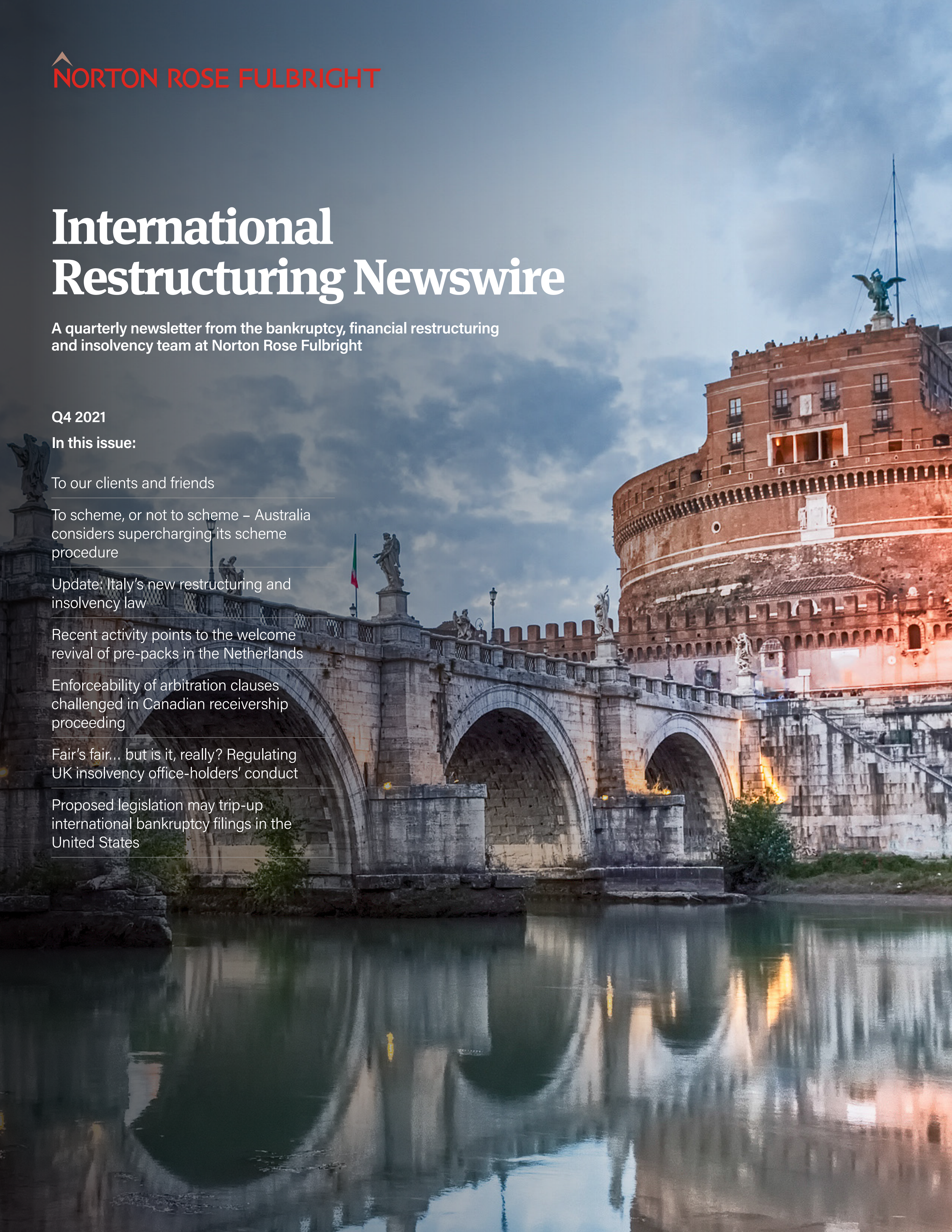
NORTON ROSE FULBRIGHT

International Restructuring Newswire

A quarterly newsletter from the bankruptcy, financial restructuring and insolvency team at Norton Rose Fulbright

Q4 2021

In this issue:



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International Restructuring Newswire

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To our clients and friends:

Welcome to the Q4 edition of the Norton Rose Fulbright *International Restructuring Newswire.*

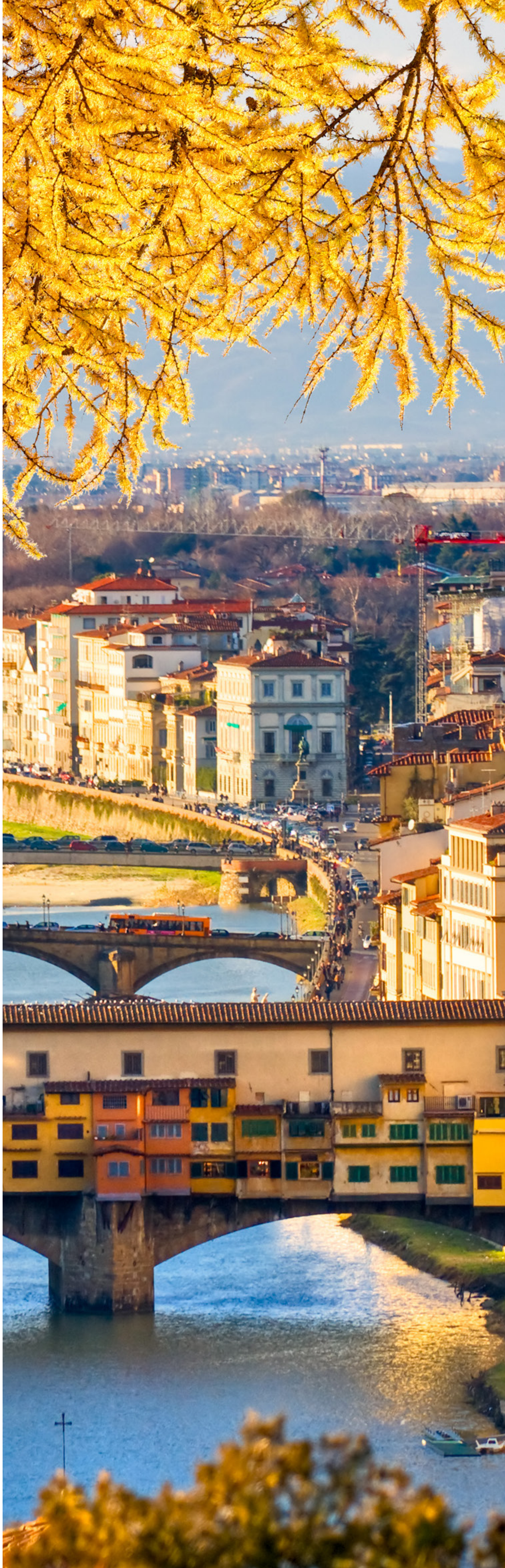
We enter the last quarter of the year with the realization that restructuring activity in 2021 has been well below expectations. In the US and elsewhere, new commercial bankruptcy filings have been at record lows. The lower number of filings is a consequence of the continued strength of the capital markets that has made it easy to access financing as well as government relief efforts have helped fend off, at least temporarily, severe financial distress. Lenders have maintained a flexible and accommodating approach with their borrowers. Instead of accelerating debt and foreclosing, lenders are offering more lenient terms and extending maturities, to avoid becoming owners of their borrowers. How long this period of relative quietude will last is anybody's guess. There is certainly enough noise in the markets to question the nascent financial recovery: accelerating inflation, disruption in the commercial real estate markets in China, gridlock in the US Congress over the budget, not to mention supply-chain woes. Financial markets, however, continue to see the bright side of nearly all developments.

While we all await an uptick in financial restructurings, please feel free to peruse this issue for an update in restructuring law changes in Italy, Australia, the Netherlands, Canada, and the UK. And to top it off, we offer an article on some disconcerting proposed legislation in the US that, if enacted, may impede global reorganizations.

On the bright side, we can all look forward to attending the just announced in-person INSOL conference in London next June. Our very own Scott Atkins, president of INSOL, will preside over the event. See you there.

All the best,

Howard Seife
Global Head
Bankruptcy, Financial Restructuring and Insolvency



In the news

Dr Omar Salah appointed Professor of Global Finance & Restructuring Law at Tilburg University

Dr Omar Salah, has been appointed Professor of Global Finance & Restructuring Law at Tilburg University in the Netherlands. Part of Tilburg Law School, the professorship commenced as of September 1, 2021, and will run alongside Omar's practice as partner in the firm's financial restructuring and insolvency group.

In this post, Omar will research international financing and restructuring of multinationals, including the question to what extent legislation in the field of restructuring and insolvency in other countries, such as the United States and the United Kingdom, provides inspiration for legal developments in the Netherlands. These international influences also form a starting point for his research into law reform programs in the field of restructuring insolvency law elsewhere in the world, for instance in Indonesia and the Caribbean. In addition, he will research to what extent developments in the international practice of finance have an impact on financing structures in the Netherlands.

In addition to conducting research, Omar will teach international legal practice in the area of property and insolvency law, including within Tilburg Law School's Global Law Bachelor's programme.

Natasha Toholka recognized by Women in Insolvency and Restructuring Victoria (WIRV)

Natasha Toholka was recognised as the '2021 Outstanding Female' by WIRV in August. Natasha was praised for her industry expertise, mentoring and significant contribution to gender diversity.

Omar Salah inducted into III NextGen Leadership Program

Omar Salah has been inducted into Class X of the NextGen Leadership Program of the International Insolvency Institute (III). The NextGen Leadership Program was established in 2012 and recognises the most prominent "rising stars" in the international insolvency area who are considered to represent 'the best of the future experts in international insolvency.'

International Corporate Rescue

Scott Atkins and Dr Kai Luck had their article, "The New World Bank Insolvency Principles: Informal Workouts and MSE Insolvency Processes as Key Pillars of Economic and Financial Stability," published in Volume 18, Issue 4 of the 2021 edition of International Corporate Rescue.

International Corporate Rescue

Scott Atkins and Dr Kai Luck had their article, "Outer Space – The New Frontier for Restructuring and Insolvency," published in Volume 18, Issue 5 of the 2021 edition of International Corporate Rescue.

Global Restructuring Review

Scott Atkins co-authored an article with Debra Grassgreen, president of the International Insolvency Institute, in the September 14 edition of the GRR – "The use of mediation to improve global restructuring outcomes in a post-pandemic world."

Oxford Business Law Blog

Scott Atkins had an article published on the Oxford Business Law Blog entitled "AI for Banks – Key Ethical and Security Risks."

Australian Restructuring Insolvency & Turnaround Association ('ARITA')

Jonathon Taylor and India Bennett authored an article "Case: The use of s 447A of the Corporations Act to facilitate a share transfer," published on ARITA's website.

International Women's Insolvency & Restructuring Confederation (IWIRC) Europe

July 6, 2021
Alison Goldthorp moderated the IWIRC panel on different European restructuring processes. Regina Rath and Sylwia Bea spoke about the new German insolvency process.

American Bankruptcy Institute Southeast Conference 2021

July 30, 2021
Jason Boland participated on an energy restructuring panel with a focus on the most recent wave of energy and oil & gas restructurings, discussing the latest trends and strategies nationally and regionally.

APKI Webinar

September 2, 2021
Scott Atkins participated in the Indonesian Receivers and Administrators Association's webinar which discussed the temporary insolvency measures introduced in Australia and other jurisdictions in response to COVID-19. The webinar featured a keynote address by the Minister of Law and Human Rights of the Republic of Indonesia.

Jindal Global Law School Insolvency Law Series, India

September 3, 2021
Omar Salah spoke at the inaugural event of Jindal Global Law School on their new Insolvency Law Working Paper Series. Jindal Global Law School is based in India and their new working papers series focus on international insolvency law. Omar was part of a distinguished panel discussing global restructuring and insolvency law from an Indian perspective, Singapore perspective and European perspective.

UNCITRAL Academy

September 8, 2021
Scott Atkins spoke on a panel at the inaugural United Nations Commission on International Trade Law (UNCITRAL) Academy, as part of Singapore Convention Week 2021. The panel discussed the potential uses of mediation in debt restructuring and insolvency.

Forum on Asian Insolvency Reform

September 13–14, 2021
Scott Atkins chaired an expert panel that explored the impact of COVID-19 on MSME sectors, the various reforms that have been introduced globally over the last 18 months in response to the pandemic, and the potential for further insolvency and non-insolvency measures to assist MSMEs in the post-pandemic recovery period.

World Development Report 2022

October 4, 2021
Scott Atkins was part of closed-door, invitation-only roundtable discussion hosted by the WDR. The focus was on Chapter 3 of the Report where the panel discussed the insolvency frameworks needed to help manage the rise in non-performing loans that is expected as government support measures are withdrawn.

Norton Rose Fulbright Restructuring in Europe Webinar

October 7, 2021
Sarah Coucher, Global FRI Strategic Initiative Director, hosted a European restructuring webinar on the impact of the withdrawal of temporary measures and the evolving landscape with our partners Alison Goldthorp (UK), Philippe Hameau (France), Regina Rath (Germany), Sylwia Maria Bea (Germany), Tiziana Del Prete (Italy), Omar Salah (the Netherlands) and senior associate Koen Durlinger (the Netherlands).

International Society of Transport Aircraft Trading (ISTAT)

October 12, 2021
David Rosenzweig spoke on an aviation restructuring panel for the ISTAT Learning Lab series. The panel included Alyssa Vazquez and Kenneth Gray, also from Norton Rose Fulbright. ISTAT is an international, not-for-profit organization dedicated to providing aviation professionals with forums for increased networking and educational opportunities and includes more than 5,000 members worldwide.

Singapore Insolvency Conference 2021

October 14, 2021
Scott Atkins spoke on a panel at the Singapore Insolvency Conference regarding the insolvency reforms and emergency measures adopted across Asia in response to the COVID-19 pandemic.

III Annual Conference 2021

October 18-20, 2021
Omar Salah will speak at the Annual Conference of the International Insolvency Institute. The Annual Conference is the premier international insolvency conference for practitioners, academics, and members of the judiciary. While this year will be different due to its hybrid nature, the quality of the programs will continue the highest quality of programming that III is known for.

INSOLAD, the Netherlands

November 12, 2021
Omar Salah will speak at the annual conference of INSOLAD. INSOLAD is the Dutch wing of INSOL Europe and the association for restructuring and insolvency professionals in the Netherlands.

INSOL Europe

November 25, 2021
Omar Salah will speak at the EECC Conference of INSOL Europe. The theme of the conference is "A Wake-up Call for Sleepy Companies?". INSOL Europe is the leading European organisation of professionals who specialise in insolvency, business reconstruction and recovery.

To scheme, or not to scheme – Australia considers supercharging its scheme procedure

Jonathon Turner, Alexander Proudford, Sophie Timms

In early August 2021, the Australian Government released a consultation paper considering potential reform to improve the scheme of arrangement (scheme) regime pursuant to Part 5.1 of the *Corporations Act* 2001 (Cth) (Corporations Act). The release of the consultation paper followed Australia's recent introduction of the small business restructuring process with a view to ensuring more companies can benefit from improvements to the insolvency regime.

A number of international jurisdictions, including Singapore and the United Kingdom, have recently reformed their scheme processes and as such provide a roadmap for potential options for Australian reform. This article looks at the recent reforms in both Singapore and the United Kingdom and discusses the potential options for reform in Australia that could make Australia a competitive restructuring venue for distressed enterprises.

What is a scheme?

While the scheme regime in Australia can be utilised in both a solvent and insolvent context, the focus of this article is in respect of the use of schemes to restructure companies that are facing significant financial difficulty.

Schemes create a binding contractual agreement between the company and its creditors containing terms that allow the company to restructure and meet its debt obligations. Unlike other forms of restructuring processes in Australia, schemes are primarily "debtor-in-possession" (**DIP**) processes where the company's existing management is not displaced in favour of a court-appointed officer (i.e. an administrator, receiver or liquidator).

Due to the strict threshold and procedural requirements of schemes, and the resulting costs to implement them, schemes have traditionally been reserved for large scale corporate restructurings (for example the restructuring of the Nine Network, Boart Longyear and Slater & Gordon Ltd), with only 17 creditors' schemes being approved in Australia since the 2008-09 Global Financial Crisis.

What does the consultation paper seek?

The consultation paper seeks feedback on a number of possible changes to the Australian scheme process, but most importantly:

- whether to introduce an automatic moratorium or stay to allow "a company and its creditors the breathing space to create a binding agreement to ensure that restructure of economically viable companies is not disrupted by a minority of creditors"; and
- whether to introduce a "cross-class cram down", which would enable a scheme to be approved by a company's creditors irrespective of opposition from one or more classes of creditors.

What lessons can be learned from other international jurisdictions?

Singapore

In early 2017, the Singaporean Government introduced sweeping changes to Singapore's insolvency and restructuring regime (**2017 Reforms**). Schemes featured prominently in the 2017 Reforms as Singapore sought to bolster its attractiveness as an international centre for debt restructuring, competing with the likes of the United Kingdom and the United States. Central to these reforms was the use, with modification, of certain provisions from the United States Bankruptcy Code. As such, the reforms resulted in a hybrid system. Two of the key reforms introduced include an expanded moratorium and the ability to achieve a cross-class cram down. Today, these reforms now sit in an omnibus statute, the *Insolvency, Restructuring and Dissolution Act 2018* (**IRDA**), with only minor modification.[1]

1 For details on Singapore's insolvency reforms see "Singapore's efforts to become an international hub for debt restructuring," in the January 2019 edition of

Moratorium

Prior to the 2017 Reforms, a company could only apply for a moratorium if it had already made a scheme proposal. Practically speaking, this required the scheme company to undertake substantial work as quickly as possible in order to stave off potential proceedings. This was regarded as counterproductive as what the company truly needed was time to properly consider and propose a scheme to its creditors.

Since the 2017 Reforms, companies are now provided with an automatic moratorium of 30 days upon the filing of the application. Further, the moratorium is engaged even if the company only intends to propose a scheme. Importantly, Singaporean courts are also now empowered to grant moratoriums to cover a "corporate group", including any subsidiary or parent company, in order to facilitate group-wide restructurings. The moratorium available for these group-wide restructurings can also be ordered to apply extraterritorially, so long as the scheme company is in Singapore.

Cross-class cram down

A cross-class cram down is a mechanism which prevents a minority non-consenting creditor in another class from blocking a company's restructuring plan. This was introduced by the 2017 Reforms as it is often difficult to achieve total cross-class consensus in a restructuring, which created an obstacle to the implementation of a scheme. In order to achieve a cross-class cram down, at least 75% in value and a majority in number of all creditors attending and voting (across both consenting and non-consenting classes) must vote in favour of the scheme, and the court must be satisfied that the scheme is "fair and equitable" to each dissenting class of creditors and does not "discriminate unfairly" between two or more classes of creditors. Interestingly, the 2017 Reforms also followed the traditional scheme threshold, requiring 75% in value of claims in a class to approve the scheme rather than the United States Bankruptcy Code threshold of 66 2/3%, when addressing the issue of whether each class is deemed to accept the terms on offer. The 2017 Reforms resulted in a practical difficulty whereby shareholders, as "junior claimants", could not retain their shares unless the unsecured creditors, as the more "senior claimants", were paid in full (which is similar to Chapter 11's "absolute priority rule"). The IRDA clarified this and now provides that in a cross-class cram down shareholders do not need to be divested of their shares before the cram down can be made. Hence, shareholders can retain their equity in a plan that crams down a class of creditors.

United Kingdom

In the United Kingdom, schemes are statutory procedures carried out pursuant to Part 26 of the *Companies Act 2006* (**Companies Act**). Analogous to both the Singaporean and Australian position, a scheme must be approved by 75% in value and the majority in number of each class of the company's members and creditors. In late June 2020, the *Corporate Insolvency and Governance Act 2020* (**CIGA**) came into force in the United Kingdom and introduced what has been termed the "super scheme", the restructuring plan. The new restructuring plan has already been utilised on a number of occasions since its introduction. Whilst the restructuring plan is primarily based on the existing scheme process, it benefits from cross-class cram-down provisions and the introduction of a standalone short-term moratorium mechanism that is intended to promote informal rescue.[2]

Moratorium

Prior to the introduction of the CIGA, a moratorium was not available as of right. Under the CIGA, an eligible company can now obtain a moratorium by filing an application to the court. Entities including financial institutions, insurance companies, those that have an outstanding winding-up petition and those that have entered into a moratorium in the previous 12 months, are not eligible for a moratorium without a further order of the court. Furthermore, in order to be granted the moratorium, the company must:

- supply a statement from the directors that the company is or is likely to become unable to pay its debts; and
- include confirmation by the monitor that the moratorium would likely result in the company's rescue.

If successful, the order allows for a moratorium of 20 days which can be extended by a further 20 business days on a subsequent application. The moratorium period can then be extended for a further period by support of creditors (12 months) or by order of the Court (indefinite). The moratorium regime provides for a modified DIP model in that during the period of moratorium, the company is supervised by a "monitor", a licensed insolvency practitioner, to provide oversight and safeguards for creditors.

Cross-class cram down

The United Kingdom's restructuring plan provides for two ways of imposing a plan on creditors without their consent. The first is if the court is satisfied that the creditors have

Norton Rose Fulbright's *International Restructuring Newswire*.

2 We previously covered CIGA in the Q4 2020 issue of *International Restructuring Newswire* – "Lighting up the CIGA!" In the Q2 2021 issue we followed up and wrote on the first UK cross class cram down under CIGA – "DeepOcean – The first UK cross-class cram-down case under the Corporate Insolvency and Governance Act 2020."

no "genuine economic interest" in the company. Whilst the court has wide discretion as to the assessment of what is classified as "economic interest", courts will likely have to make determinations on commercial issues and matters of valuation, which in turn will require the provision of expert evidence.

The second is if the court is satisfied that:

- if the scheme is approved, no members of the dissenting classes would be any worse off than they would be in the event of the "relevant alternative"; and
- at least one class of creditors or members, which would receive a payment or have a "genuine economic interest" in the company in the event of the relevant alternative, has approved the restructuring plan.

As the CIGA does not prescribe examples of alternatives, it will be interesting to see how the "relevant alternative" test is developed by the courts. This may be a decisive aspect of the cross-class cram down mechanism in the restructuring plan, as there is considerable flexibility for debtors, or dissenting creditors, to frame the relevant alternative using valuation evidence. As such, the courts have considerable discretion in developing the law in this area.

Australia

Before turning to considering the potential changes that may be implemented in the future, it is important to understand the current position in Australia.

In respect of the two issues expressly identified in the consultation paper we note that:

- Currently, where multiple classes of creditors are affected by a scheme, the requisite majority approval must be obtained from each class. This allows one dissenting class the ability to block the scheme and strongarm the company. The underlying rationale for the existing regime is to ensure that minority interests are adequately protected. However, this safeguard can be exploited by a dissenting class (e.g. by withholding approval of the scheme until the company provides more favourable conditions).
- Australian schemes are also not subject to an automatic moratorium on enforcement and proceedings prior to the commencement of the court process. Rather, there exists a discretionary power under section 411(16) of the Corporations Act which allows a court to stay actions by creditors upon application by the company. This existing provision is somewhat similar to the CIGA moratorium provision, in that it does not arise automatically. It also arises too late in the process to be of real benefit.

The current complexity and rigidity of the Australian scheme process is one of the reasons that it is such an underutilised restructuring process in Australia.

Our view on the consultation paper changes

With the consultation process now closed, we eagerly await confirmation that the Government will move forward with reforms to the scheme regime. While the scheme regime will remain of limited use to companies other than large distressed corporates, we consider that there is real utility to reform the regime to make it more closely aligned with other jurisdictions. In so doing, it is hoped that increased flexibility and the introduction of measures to counter issues that currently deter the use of the scheme regime, will provide for better outcomes for a range of stakeholders.

Moratorium

The proposed automatic moratorium in the consultation paper appears to contemplate something similar to what was introduced in Singapore. As mentioned above, the United Kingdom did not see the need to introduce an automatic moratorium as part of its recent reforms under the CIGA. Instead, a standalone provision has been created whereby companies must make a separate application to the court. This also provides benefit outside of the scheme context and promotes informal restructuring more generally.

Whilst there is already an existing power under section 411(16) of the Corporations Act for a court to stay actions by creditors, the introduction of an automatic stay or a standalone moratorium would give Australian companies beginning the scheme process some respite from proceedings and allow the company time to focus on restructuring its liabilities.

While there are obvious benefits of the introduction of an automatic moratorium in conjunction with scheme reform, we consider that a better and more flexible approach would be to adopt a standalone DIP moratorium regime akin to that adopted in the United Kingdom. This would support informal restructuring with appropriate supervision by the Court and a registered liquidator acting as monitor. It would also incorporate a structure for the payment of debt during the moratorium period thereby providing certainty for directors and creditors. Finally, we consider that it would be necessary for the moratorium to incorporate protection for directors from insolvent trading liability during this period.

Cross-class cram down
If properly implemented, a cross-class cram down mechanism would be a valuable addition to the Australian regime. Given that the Singaporean courts have provided greater clarity, primarily due to the 2017 Reforms taking place a number of years prior to the introduction of the CIGA, we are of the view that the "fair and equitable" test would also be appropriate for Australian scheme cross-class cram downs. In considering the content of "fair and equitable", courts focus on whether the dissenting creditor would receive, under the proposed scheme, an amount less than what such a creditor would receive if the proposed scheme was not approved. Furthermore, in order to be consistent with the existing threshold requirements, we believe that if a cross-class cram down mechanism is introduced, the traditional 75% requirement of creditor value approval will be incorporated (as in Singapore).

Additional potential amendments

While the consultation paper focuses on the moratorium and cross-class cram down issues, there is opportunity to consider other amendments that may enhance the utility of the scheme regime. We consider that reform in respect of the protection of employee entitlements and the provision of additional finance during any moratorium ought to be considered. In particular, in circumstances of severe financial distress, the provision of additional working capital may prove critical to the ultimate outcome for all creditors and the regime ought to appropriately incentivise this.

The waiting game

We look forward to further developments pending review of the submissions received during the consultation process and hope that Australia will, in the not too distant future, join other international jurisdictions in modernising the scheme process. Stay tuned.

Jonathon Turner is a partner, Alexander Proudford is an associate and Sophie Timms is a lawyer in our Sydney office. All are members of the firm's financial restructuring and insolvency group.

Update: Italy's New Restructuring and insolvency Law

Although full implementation is delayed, certain provisions of Italy's New Code of the Business Crisis and Insolvency are gradually entering into force

Tiziana Del Prete and Giuseppe Pastore

In our Q3 2021 issue of the *International Restructuring Newswire*, we provided an overview of the main features of Italy's New Code of the Business Crisis and Insolvency (the New Code). We noted that the unpredictability of the evolution of the Covid-19 pandemic caused the Italian Government to postpone for one year (from August 2020 to September 2021) the effective date of the New Code and the implementation of the New Code. The effective date of the New Code has been further postponed by the Italian Government.

In August 2021, the Italian Government passed Law Decree n. 118/2021 (**Law Decree 118/2021**), providing for the postponement until May 16, 2022 of the entry into force of the New Code and until December 31, 2023 for the hotly-debated new out-of-court early warning procedures. This prolonged delay of the implementation of the out-of-court early warning procedures is indicative of the fact that this feature of the New Code received a negative response from both the restructuring legal community and big business. We expect that the early warning procedures will continue to be the subject of debate and amendment.

What has become clear over the past summer to all market observers is that when it comes to the long-awaited reform of restructuring and insolvency laws in Italy, the Italian legislators have decided that gradual implementation is preferable to a one-shot overhaul of the relevant legal and regulatory framework.

In addition to providing the above-mentioned postponements, Law Decree 118/2021 adds a new and interesting feature to the New Code, a quasi-private settlement procedure, which is the focus of this brief article.

The new Settlement Procedure

Law Decree 118/2021 introduces a procedure to resolve distressed company situations, a quasi-private settlement option that is in line with EU Directive no. 1023/2019 (the **Settlement Procedure**). The Settlement Procedure option will become effective and a reality in November 2021. It is a break-through turning point in Italian restructuring and insolvency law because it provides, for the first time in history, a procedure for potential business crisis solutions that do not require major intervention by the courts.

The Settlement Procedure will be an option for any company that is in a distressed situation, but is able to continue conducting business. It is designed to allow a company to overcome temporary distress and resume active and healthy business activities.

Three essential aspects characterize the new Settlement Procedure.

First, it is an **out-of-court procedure**. The distressed company does not have to file any papers or requests with a court to initiate the process. Instead, starting from November 15, 2021, a company will be able to use a single national telematics platform (the **Platform**) to request the appointment of an independent expert (the **Expert**), a third party professional selected within five working days by an ad hoc committee organized by the relevant local Chamber of Commerce. The Expert will have the responsibility to examine the restructuring plan submitted by the company and facilitate the relationship, and eventual negotiations, between the company and its creditors.

Second, it is a **confidential procedure**. All interested parties to the distressed situation must keep confidential all the information relating to the company, as well as any actions taken or planned by the company. To protect confidentiality, except in certain cases identified below, the submission of a request by a company for an Expert via the Platform will not be disclosed to anyone.

Third, it is a **voluntary procedure**. It is activated only upon request of the distressed company. In addition, although a company's supervisory body has a duty to inform the company's management body when a distressed situation arises, so that the latter may seek recourse to any of the possible available procedures, the company is under no obligation ever to select or to start the Settlement Procedure.

The Expert

One of the most important features of the Settlement Procedure is the introduction of a new figure, the Expert, who will have a critical role in helping the distressed company find solutions that will enable it to emerge from distress and crisis.

Law Decree 118/2021 provides that all Chambers of Commerce across Italy will keep lists of persons who may be appointed as an Expert. These persons will have experience in corporate crisis and restructuring and may include accountants, lawyers and other types of business advisors and consultants. They must meet strict requirements relating to independence, professionalism, impartiality and confidentiality.

Once selected to assist a distressed company, the Expert will meet with the relevant managers of the company and evaluate whether a solid, concrete prospect for a corporate restructuring exists. The Expert has 180 days to gather the required information and reach a conclusion. This period may be extended, for example, upon request of all parties involved (including the Expert), or when the distressed company requires more time because simultaneously it has filed for certain protective or precautionary measures with a court and more time is needed to get the court's protective order.

At the conclusion of the evaluation period, whether 180 days or longer, the Expert may determine that a restructuring is reasonably foreseeable and a solid, concrete possibility. On the other hand, the Expert may determine that this is not the case (an example of a failed settlement), but no immediate consequences for the distressed company or for the creditors follow from this negative conclusion.

The role of the Expert is different from the role of a Judicial Commissioner. The latter is appointed by a bankruptcy court to collaborate with the court in the context of the classic Composition with Creditors' Procedure (the ***concordato preventivo***). The Judicial Commissioner advises the court on specific matters and prepares a report for the court that addresses the reasons for the crisis, the behavior of the distressed company during the procedure, and the details (and evaluation) of the restructuring plan and of the guarantees that the distressed company has offered to its creditors.

By comparison, the Expert is not appointed by the court and, at least in the first stage, operates entirely outside of the court. The Expert interacts with the distressed company and its creditors, facilitating negotiations and serving as a sort of guarantor for the fairness of the proposal that the distressed company presents to the creditors. A court may step in only after it is presented with a request to issue a protective or precautionary measure. At that point, but not before, the Expert will begin to interact with the court, which can ask the Expert for certain opinions or clarifications.

The role of the Expert is also different from the role of an independent professional (the ***attestatore***), who is appointed by a company to evaluate and confirm the truthfulness of financial and accounting statements and reports, as well as the feasibility of a proposed restructuring plan in the context of the classic Composition with Creditors' Procedure and Debt Restructuring Agreements (the ***accordi di ristrutturazione dei debiti***). As stated above, the Expert's work involves interacting with the distressed company and its creditors, whereas the *attestatore*'s work does not involve discussing anything with creditors or interfering in any way with the business activities carried out by the distressed company.

Court intervention

A court will get involved in the new Settlement Procedure only if and when the distressed company requests that a court grant protective or precautionary measures relating to the assets of the distressed company, such as freezing the enforcement actions of one or more creditors. To have recourse to these types of protective or precautionary measures, the distressed company must file a specific request with a court. Since this request must be registered at the Register of Companies (a public database), the confidentiality of the distressed company's situation is lost when the company takes this step.

Nevertheless, protective and precautionary measures are often necessary to enable the distressed company to conduct successful negotiations with its creditors.

Moreover, during the Settlement Procedure, the ordinary and extraordinary actions of the distressed company remains in the hands of management of the distressed company. For any extraordinary action, however, the distressed company must inform the Expert, who, if in disagreement with the action, must register a dissenting opinion at the Register of Companies. In this case, not only will the confidentiality of the distressed company's situation be lost, but the extraordinary action (and related consequences) will not be protected from a possible future claw-back action.

A court may also intervene to authorize certain financings, giving the creditors of these financings a super-senior priority over the other creditors in the event the distressed company is the subject of a bankruptcy procedure. And, a court may intervene to authorize the distressed company to transfer all or substantially all of its assets and business as a going concern, or certain of its assets and business, and exempt the buyer from having joint liability for the debts resulting from the accounting books of the seller/distressed company. This feature is in contrast to a basic principle of Italian law that provides that a buyer of a going concern is always jointly liable with the seller for the debts resulting from the accounting books of the seller. While the exemption from joint liability does not apply to the distressed company's obligations to employees, it still constitutes a significant change in Italian law and is an attractive aspect for buyers of and investors in a distressed company.

Overall, the acquisition of a going concern or assets from a distressed company that has initiated the Settlement Procedure may proceed with very limited involvement of the court, which must only determine that the offer is the best solution for the creditors.

The outcomes of the Settlement Procedure

Extra-judicial outcomes of the Settlement Procedure include:

1. An agreement between the distressed company and one or more creditors that ensures the continuity of the business for a period of no less than two years;
2. A moratorium agreement, according to which the creditors agree not to pursue any enforcement action for a certain period of time;
3. A more general agreement between the distressed company and the creditors and ratified by the Expert (any action executed in the context of such agreement will be protected by the claw-back action).

Judicial outcomes of the Settlement Procedure include:

1. Request for the homologation (i.e, court approval) of a debt restructuring arrangement pursuant to art. 182 bis of the Bankruptcy Act;
2. Request for the access to one of the other insolvency procedures regulated by the bankruptcy law.

The Simplified Composition with Creditors' Procedure

In the event that the Expert's final report indicates that the Settlement Procedure has failed (i.e., that the distressed company and the creditors have not reached an agreement), then Law Decree 118/2021 introduces the ability to start a Simplified Composition with Creditors Procedure (the **Simplified Procedure**). The Simplified Procedure entails the assignment of the assets of the distressed company to the creditors, a type of liquidation.

The Simplified Procedure is another significant novelty in the new Italian restructuring and insolvency legal and regulatory framework. No vote is required by the creditors for the Simplified Procedure to be initiated, but creditors have the right to file an opposition if they believe that the liquidation plan creates prejudice to their interests.

The court will authorize the Simplified Procedure to proceed after it verifies the regularity of the relevant proceedings, the respect of the priority of the creditors, and the feasibility of the liquidation plan. Even if one or more creditors oppose, the court may still approve the liquidation plan as long as it determines that no better solution is available for the creditors as compared to a bankruptcy liquidation plan.

In the Simplified Procedure, a Judicial Commissioner is not appointed; instead, the court appoints a collaborator, who has a limited advisory role and a liquidator, who will manage the liquidation of the assets of the distressed company. The liquidator may be a person indicated by the distressed company.

With the Simplified Procedure, the distressed company is not bound to guarantee a 20 percent return to the creditors, which is currently the requirement in the *concordato preventivo* procedure aimed at liquidating the assets (in fact, it should be remembered that the 20 percent return to the creditors is not applied in the *concordato preventivo* procedure aimed at preservation of going concern values). The court will determine only if the liquidation plan gives creditors a "sufficient return", no worse than what the creditors would get in a bankruptcy scenario.

It is important to note that the distressed company cannot start the Settlement Procedure if a *concordato preventivo* procedure is pending relating to the distressed company, or if another procedure is pending concerning the homologation of a debt of the distressed company.

Conclusions

The new Settlement Procedure is a significant development in Italy's restructuring and insolvency legal and regulatory regime that is geared to enabling distressed companies and their creditors to achieve a restructuring with little to light touch from the court system and formal bankruptcy officials. By making the effective date relatively soon (November 2021), the Italian legislator is sending numerous messages:

- Distressed companies need viable out-of-court options to reach settlements with creditors, continue to do business and avoid bankruptcy.
- Courts should intervene in distressed company situations only in specific cases and for certain tasks (for example, to order protective and precautionary measures that will help in negotiating a settlement between the distressed company and its creditors).
- Public prosecutors should remain completely absent from the distressed company scenario.
- Confidentiality, which is a key and attractive feature of the new Settlement Procedure option, can provide the platform to reach a consensual restructuring.
- Business and legal professionals can play an important role in helping distressed companies to avoid bankruptcy and maintain good relations with creditors and are encouraged to use their experience to propose innovative and creative solutions for all the parties involved.

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Recent activity points to the welcome revival of pre-packs in the Netherlands

Pre-packs were often used in the aftermath of the global financial crisis in the Netherlands, but their use came to an almost complete halt after a European Court of Justice decision in 2017. Recently, there have been two important developments which could revive the use of pre-packs in the Netherlands.

Prof. Omar Salah and Koen Durlinger

In the aftermath of the global financial crisis, the restructuring market witnessed an increase in the use of pre-packs in the Netherlands. Most Dutch courts took a pragmatic approach and facilitated pre-packs, even though prepacks lacked a statutory basis in the Dutch Bankruptcy Code ("DBC").[1] Back then, as the global financial crisis evolved and more enterprises suffered financial distress, debtors and their creditors searched for creative restructuring tools and solutions. The pre-pack was one of the tools applied in practice to liquidate part of the business while restructuring another part through bankruptcy proceedings.

As part of a recalibration of Dutch insolvency law in 2012, a codification of pre-packs in the DBC was considered as well as the codification of the 'Dutch scheme' (please refer to the Q1 2020, Q4 2020 and Q2 2021 issues of our *International Restructuring Newswire* for articles on the Dutch scheme). In 2015, a legislative proposal was drafted to codify pre-packs in the DBC: a draft bill for the Act on Continuity of Enterprises I (*Wet Continuïteit Ondernemingen I*; "**WCO I**"). However, the legislative process for WCO I was put on hold when litigation ensued in some pre-packs regarding matters relating to the European Directive on 'Transfer of Undertakings and Protection of Employees' ("**TUPE**") concerning the treatment of employment contracts.[2]

Some of the pre-packs had resulted in litigation on questions involving transfer of undertakings – being a business, business unit or a part thereof – and protection of employees. Pursuant to TUPE, in a transfer of an undertaking employees of a business are transferred to the purchaser of such business by operation of law without changes in the terms of their employment contracts. However, an exception applies in the event of bankruptcy: if the seller is in bankruptcy proceedings, the main rule that all employees are automatically transferred to the purchaser does not apply (the "**bankruptcy exception**"). Generally, the restructuring market assumed that the bankruptcy exception applied in pre-packs, given that as part of a pre-pack the seller formally enters bankruptcy proceedings.

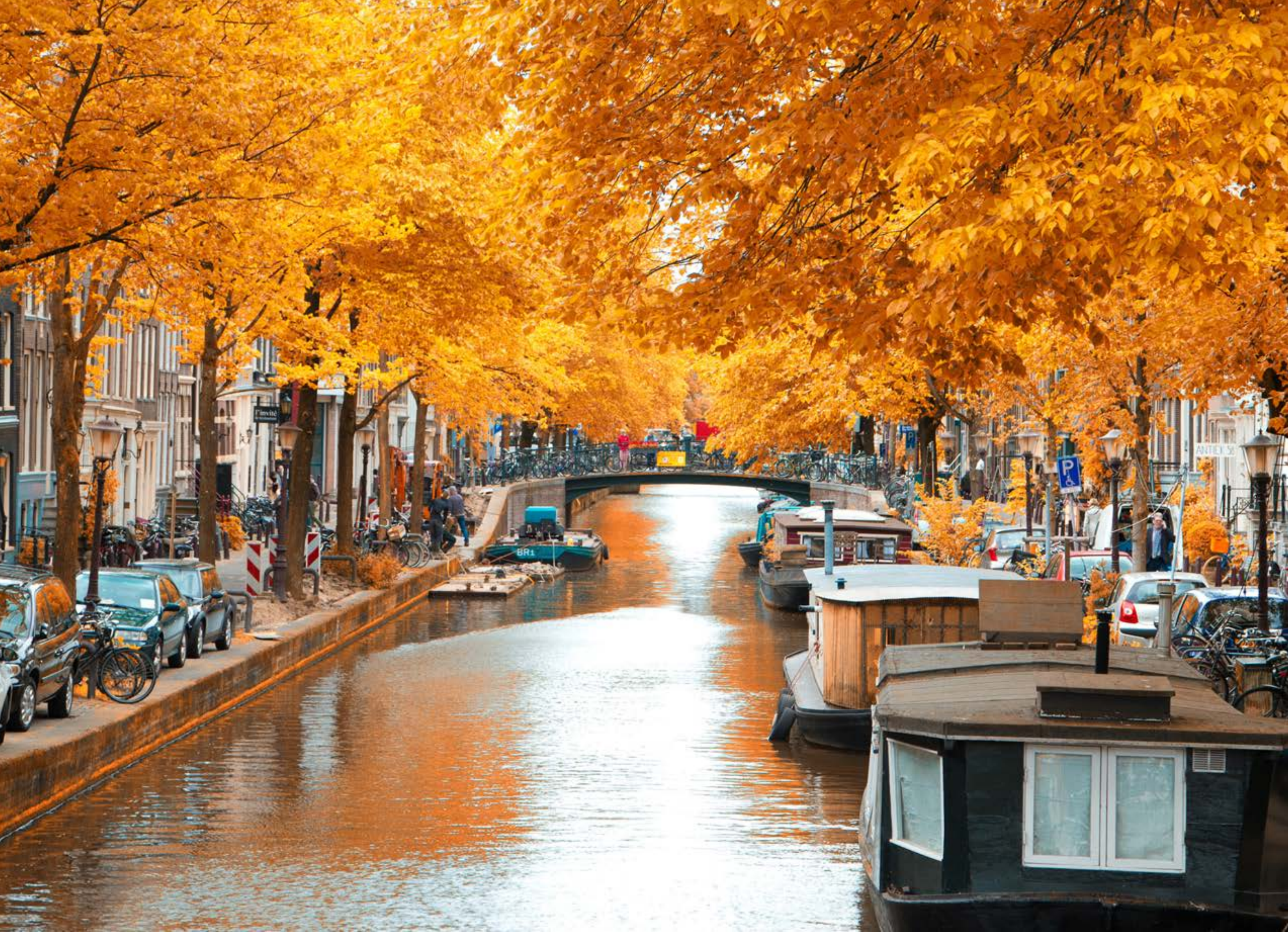
Nevertheless, in the *Estro* case the European Court of Justice ("**ECJ**") upset market expectations and ruled instead that the bankruptcy exception did not apply to the Dutch pre-pack of *Estro*.[3] This resulted in legal uncertainty and the Dutch market witnessed a decline in the use of pre-packs. Two recent developments may alter the pre-pack landscape: (i) in the *Heiploeg* case,[4] the Dutch Supreme Court in 2020 took a contrary position and ruled in an interlocutory decision that the bankruptcy exception does apply in the pre-pack of Heiploeg; and (ii) the Dutch government separately launched a public consultation to introduce WCO I for pre-packs with a limited scope focusing on enterprises with activities with "societal interests."

1 Not all District Courts of the Netherlands facilitated pre-packs. Only 8 of the 11 District Courts granted requests for a pre-pack, while the other 3 District Courts did not do so given that the pre-pack did not have a legal basis in the DBC (yet).

2 Council Directive 2001/23/EC of 12 March 2001 on the approximation of the laws of the Member States relating to the safeguarding of employees' rights in the event of transfers of undertakings, businesses or parts of undertakings or businesses.

3 European Court of Justice 22 June 2017, C-126/16, ECLI:EU:C:2017:489 (*Estro*).

4 Dutch Supreme Court 17 April 2020, ECLI:NL:HR:2020:753 (*Heiploeg*).



Background of pre-packs in the Netherlands

In the last decade, various debtors used pre-packs in the Netherlands to restructure their liabilities, including liabilities under employment contracts. A debtor in financial distress, that had a purchaser for the viable parts of its business, would request the court to ´appoint´ a prospective bankruptcy trustee and a prospective supervisory judge (formally, there was no appointment given that there was no legal basis for pre-packs in the DBC, but the courts would disclose to the debtor the names of the individuals that would be appointed as bankruptcy trustee and supervisory judge in a subsequent bankruptcy of the debtor). The prospective bankruptcy trustee would – under supervision of the prospective supervisory judge – monitor the preparation of the sale of the viable parts of the business of the debtor to a purchaser through an asset deal. Once all elements of the deal were agreed upon, the debtor would file for bankruptcy; upon the declaration of bankruptcy proceedings, the prospective bankruptcy trustee and the prospective supervisory judge were appointed as bankruptcy trustee and supervisory judge respectively; and the deal was signed and closed by the bankruptcy trustee with approval of the supervisory judge.

Pre-packs have proven to be a useful restructuring tool with various advantages in practice. By making use of a pre-pack, the (viable part of a) business of a debtor is sold as a going-concern. The proceeds of such sale are expected to exceed the proceeds of a piecemeal sale of the assets of the debtor in liquidation. This also safeguards business continuity and jobs, while at the same time it does allow the buyer to right size the workforce as part of the restructuring of the debtor. This latter point proved to be the topic of much debate as well as litigation in the Netherlands as a result of which the legislative process for WCO I was delayed – eventually leading to the judgment of the ECJ in the *Estro* case on 22 June 2017. In short, the ECJ ruled that in a pre-pack sale, the employees of a business transfer to the purchaser of such business by operation of law without changes to the terms of their employment contract.

Unfortunately, the *Estro* case limited the options to restructure employment liabilities while increasing legal uncertainty around pre-packs. Consequently, the use of pre-packs came to an almost complete halt in the Netherlands. However, two significant developments may lead to welcome revival of the use of pre-packs in the Netherlands.

The Dutch Supreme Court in the *Heiploeg* case

Heiploeg is one of Europe's largest processors of shrimp. In 2011, the financial position of Heiploeg deteriorated. As part of its financial restructuring, Heiploeg sold the viable part of its business in a pre-pack. The purchaser offered two-thirds of all employees an employment contract, while the employment contracts of the remaining one-third of the employees were terminated. However, litigation ensued on the question whether all employees were transferred by the operation of law to the purchaser of the business, despite the sale being conducted through a pre-pack.

Contrary to the ECJ ruling in *Estro*, the Dutch Supreme Court came to the (preliminary) conclusion that the bankruptcy exception applies because all three conditions for the bankruptcy exception in TUPE were met: (i) the seller was in bankruptcy proceedings; (ii) the bankruptcy proceedings were instituted with the purpose of liquidating assets of the seller; and (iii) the bankruptcy proceedings were under the supervision of a competent public authority. The latter two conditions were at tension with the judgment in the *Estro* case. On the second requirement, the Dutch Supreme Court found that the purpose of the pre-pack was to liquidate the assets of the bankrupt debtor given that the bankruptcy of Heiploeg was inevitable, the purchaser of the business was not affiliated with Heiploeg and the District Court had appointed a prospective bankruptcy trustee and prospective supervisory judge with the aim to achieve the highest possible return for the creditors of the (soon to be) bankrupt company. On the third requirement, the Dutch Supreme Court concluded that pre-packs involve actual supervision by a competent authority, because the prospective bankruptcy trustee has the opportunity to monitor the negotiation of the deal pre-bankruptcy and in the subsequent bankruptcy the pre-pack sale is actually signed and closed by the bankruptcy trustee with approval of the supervisory judge.

Given that the preliminary finding of the Dutch Supreme Court in the *Heiploeg* case may be at odds with the judgment of the ECJ in the *Estro* case, the Dutch Supreme Court referred to the ECJ with preliminary questions on whether – in the view of the ECJ – a Dutch pre-pack does not fulfil the requirements of the bankruptcy exception. In addition to finding that the bankruptcy exception applies in the *Heiploeg* case, the Dutch Supreme Court set out the purpose and process of Dutch bankruptcy proceedings as well as the pre-pack and asked the ECJ to consider each point while giving its preliminary ruling to the questions raised by the Dutch Supreme Court. As a subsequent step, the Advocate General of the ECJ will provide its conclusion, followed by decision by the ECJ. The Dutch market is awaiting the decision with much interest.

WCO I continued: Pre-packs for enterprises with activities with societal interests

As mentioned above, WCO I was put on hold when disputes arose on the bankruptcy exception under TUPE, initially to await the outcome of the ECJ's ruling in the *Estro* case. To address the legal uncertainly created by the ECJ ruling in the *Estro* case, the Dutch legislature launched a draft bill for the 'Act on Transfer of Undertaking in Bankruptcy' (*Wet overgang van onderneming in faillissement*; "**WOVO**") for public consultation in May 2019. The intent of this draft bill was to set up a new legal framework for transfer of undertakings in bankruptcy (irrespective of whether that is through a pre-pack or a 'regular' bankruptcy). However, the interlocutory decision of the Dutch Supreme Court in the *Heiploeg* case illustrated that a completely new legal framework may not be required. As a result, the legislative process for both WCO I and WOVO were put on hold again.

On 25 May 2021, the Dutch government published a legislative amendment to WCO I for public consultation. According to the explanatory memorandum to the legislative amendment, pre-packs were no longer used in practice due to legal uncertainty arising from the *Estro* case and WOVO was put on hold in response to the *Heiploeg* case. However, there had been cases where the use of a pre-pack would have been very desirable, not only from an economic perspective, but also from a societal point of view. In the explanatory memorandum, reference is made to bankruptcies of various hospitals in the Netherlands. The application of a pre-pack would have resulted in a controlled wind down in these cases.

In essence, the legislative amendment leads to two changes to WCO I: (i) it clarifies that the purpose of a pre-pack needs to be a controlled liquidation of the activities of the bankrupt debtor (replacing previous language which stated that the purpose was continuity of the debtors' business); and (ii) it limits the scope of WCO I to enterprises with activities that serve societal interests.

Although the first change may raise the impression that pre-packs can only be used to liquidate businesses and no longer for a restart through bankruptcy, the explanatory memorandum clearly states that that is not the case and that pre-packs can still be used for pre-pack sales. However, the main purpose of the pre-pack needs to be a controlled liquidation. As discussed above, the purpose of the bankruptcy proceeding is relevant in light of the requirements that need to be met for the bankruptcy exception under TUPE. Even though the explanatory memorandum comes with a caveat that the *Estro* case leaves legal uncertainty on the question whether all employees are automatically transferred in case of a pre-pack sale, we believe that this clarification language on the purpose of the bankruptcy proceedings mitigates this risk considerably.

The second change is not meant to limit the scope of WCO I permanently to enterprises with activities with societal interests only. The Dutch legislature clarified that it intends a phased approach whereby pre-packs are now introduced for enterprises with activities with societal interests and that later, i.e. after the ECJ has issued its preliminary ruling in the *Heiploeg* case, it will be made available for other debtors as well.

The Dutch legislature demonstrates a clear sense of urgency with this legislative amendment to WCO I. According to the legislature, it is paramount that enterprises with activities with societal interests be allowed to use pre-packs. With respect to the scope of 'societal interests', examples that are given in the explanatory memorandum include companies active in the healthcare, education, energy, waste processing, internet and telecom sectors. While an explicit reference to the Covid-19 pandemic is not included in the explanatory memorandum, one cannot ignore the impression that the pandemic also played an important role in the introduction of pre-packs on an expedited basis through a phased approach. This approach stresses the acknowledgement by the Dutch government that there is a need for pre-packs in practice. The public consultation was closed on 27 July 2021. As a next step, the government may publish a formal amended draft bill for WCO I, but whether that will happen remains to be seen. We welcome the phased approach of the government: making a first step to allow pre-packs for certain sectors is commendable, so long as a further codification for other debtors follows soon thereafter.

Conclusion

Clearly, the legal uncertainty arising from the *Estro* case has had an adverse effect on the use of pre-packs in the Netherlands. However, companies facing financial distress have been in need of a restructuring solution that addresses a controlled liquidation of part of the business while facilitating the continuation of another part thereof. While the Dutch scheme that entered into force on 1 January 2021 provides for an effective tool to restructuring debt outside of formal bankruptcy proceedings and suspension of payments, the ability to use the 'Dutch pre-pack' would be a very welcome addition to the restructuring toolkit in the Netherlands. Both the recent interlocutory decision by the Dutch Supreme Court in the *Heiploeg* case and a phased introduction of WCO I allowing pre-packs for enterprises with activities with societal interests offer hope for the revival of the pre-pack in the Netherlands.

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Enforceability of arbitration clauses challenged in Canadian receivership proceeding

Evan Cobb

Parties to commercial arrangements will often determine for efficiency, confidentiality or other reasons that any disputes will be determined by arbitration rather than through a traditional court process. Arbitration provisions are included in those contractual arrangements and, in the ordinary course, parties' agreements to arbitrate disputes are enforceable and complied with.

In Canada, provincial statutes generally preserve the parties' agreements to arbitrate. For example, the *Arbitration Act* of British Columbia provides that if a party to an arbitration agreement commences court proceedings notwithstanding an agreement to arbitrate the matter in dispute, the counterparty to the arbitration agreement may apply to court for an order staying such court proceeding. The court must then make an order staying such court proceedings unless it determines the arbitration agreement was void, inoperative or incapable of being performed.

Arbitration and insolvency

The protections of arbitration agreements in Canada are generally robust, but when one of the parties to a dispute that would otherwise be subject to arbitration is in an insolvency proceeding in Canada, the rules can change and one cannot assume that the parties' agreement to arbitrate disputes will proceed as expected.

If the insolvent party is the *target* of a claim that would otherwise be arbitrated, it is not surprising that the pursuit of such a claim through arbitration against the insolvent party is generally stayed and, further, that the claim normally is dealt with through a centralized claims process in the insolvency proceeding and not through arbitration. This is a sensible and efficient approach to dealing with all claims against an insolvent party in a single forum. A debtor should not be expected to expend extensive estate resources defending claims in various jurisdictions and in venues that may not have a complete understanding of the ongoing insolvency process and all of the interests involved. In Canada, this is often referred to as the 'single control model' in insolvency proceedings.

If the insolvent party, or its estate representative, is the party *asserting* the claim that would otherwise be arbitrated, the appropriate venue to resolve that claim is far less clear. On one hand, the insolvent party or its estate representative could advocate for the matter to be resolved through an expedited court process for speed and efficiency in the context of an insolvency proceeding that must be wrapped up quickly for the benefit of all stakeholders. On the other hand, the counterparty could argue that they would be unreasonably prejudiced if the arbitration agreement on which they relied, and their contractual right to defend a claim against them through an arbitration process, is not respected.

This second more complex scenario was recently considered in the Canadian context by the British Columbia Court of Appeal in *Petrowest Corporation v. Peace River Hydro Partners* (***Petrowest***).

The *Petrowest* decision

Petrowest Corporation was subject to receivership proceedings in British Columbia, Canada.

The "receiver" in such a proceeding is an insolvency practitioner, or firm of insolvency practitioners, appointed by the court on application of a secured creditor usually to undertake a court-supervised enforcement and realization process. Generally, the receiver's activities will involve monetizing the assets of the debtor for the benefit of all creditors, and distributing the realized value to creditors in accordance with their respective priorities. As part of its mandate, the receiver can pursue any claims that may be available to the debtor. The receiver is not bound by the executory contracts of the debtor, and may disclaim those contracts during the asset realization process, though the counterparty to such executory contract may challenge the disclaimer in court based upon, among other things, the equities as between the parties.

The receiver holds a unique position. As described by the British Columbia Court of Appeal, the assets of the debtor do not vest in the receiver and the receiver is not an agent of the debtor, rather the receiver acts "in fulfilment of its own court-authorized and fiduciary duties, owed to all stakeholders".

In the *Petrowest* case, the receiver pursued claims under several agreements to which Petrowest Corporation was a party. The agreements in question were principally subcontracts between Petrowest Corporation or its affiliates and Peace River Hydro Partners pursuant to which Petrowest Corporation and its affiliates would perform work related to a construction contract between Peace River Hydro Partners and BC Hydro, as project owner, relating to the construction of a hydroelectric plant.

The agreements that were the subject of the litigation included provisions requiring that claims by Petrowest Corporation against Peace River Hydro Partners be pursued through arbitration.

The receiver argued that it was not bound by the contractual requirements to arbitrate such disputes, because the receiver disclaimed the agreement to arbitrate, and that such disputes could instead be determined by the court. In Canada, a disclaimed agreement is effectively treated to be at an end.

The Court of Appeal put the issue simply as follows:

> The receiver has adopted the [subcontracts with Peace River Hydro Partners] and is suing on them…Can the receiver sue on the contracts and yet disclaim the arbitration clauses [contained in those same contracts]?

The Court of Appeal determined that a receiver cannot pick and choose among the terms of an agreement that it wishes to enforce and those that it wishes to disclaim. Otherwise, the receiver could fundamentally alter the commercial deal the parties agreed to by preserving favourable terms and disclaiming unfavourable terms. That cannot be an acceptable result as it unduly sacrifices the certainty that contracting parties require from their legally binding commercial arrangements.

Notwithstanding this determination, the Court of Appeal also determined that the receiver in the *Petrowest* case could still avoid the application of the arbitration clauses found in those contracts on which the receiver wished to sue.

One may ask how a receiver could seek to pursue a claim under Petrowest Corporation's contract while disclaiming the arbitration obligations that are found in that same contract. The court provided two reasons for this conclusion:

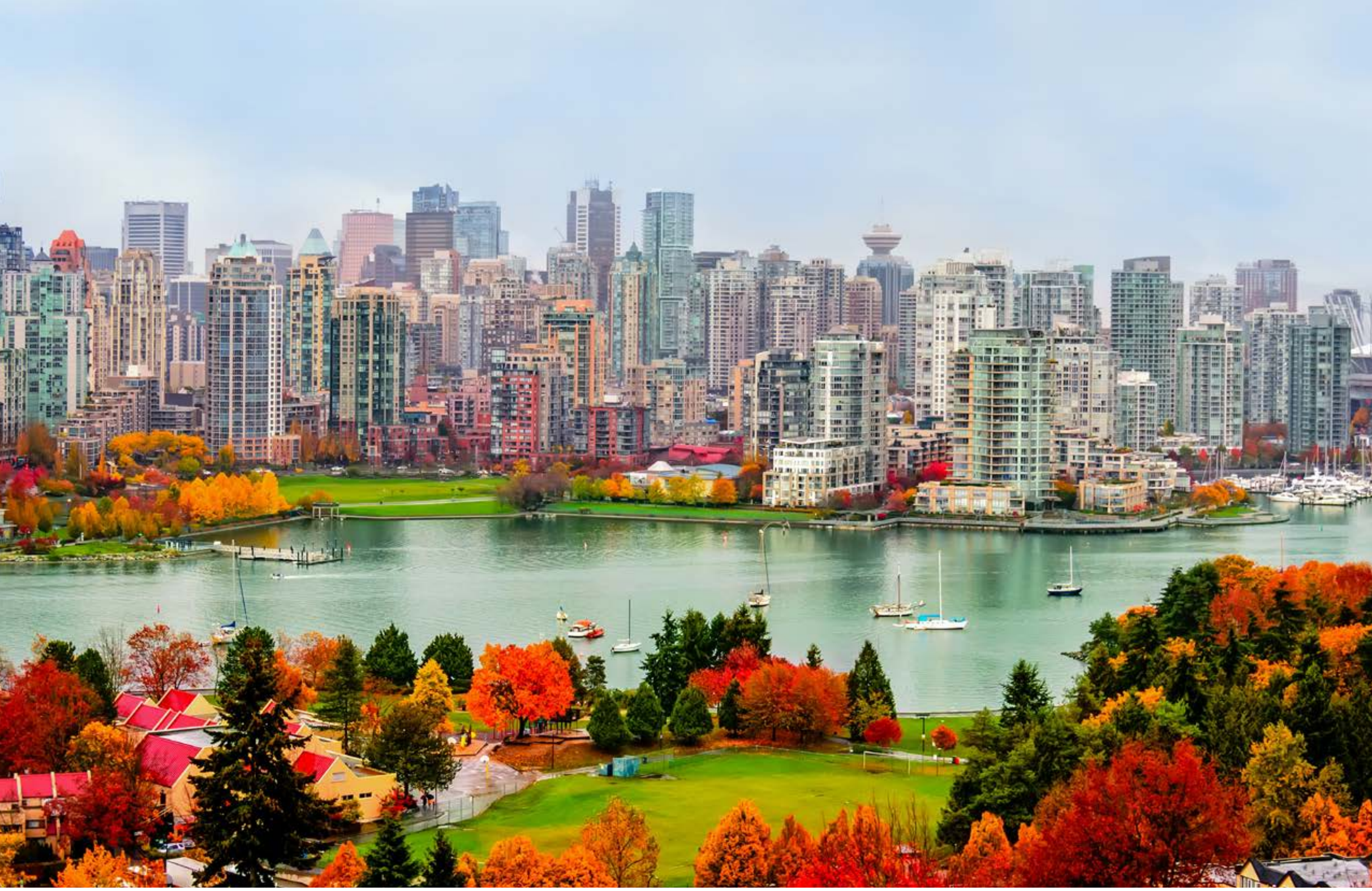
1. **The doctrine of separability**. The Court of Appeal explained that under this doctrine arbitration clauses are not simply a term of the contract in which they reside, but are instead an independent agreement. The court concluded that it is open to the receiver to disclaim the arbitration agreements notwithstanding that it has adopted the contracts containing those arbitration agreements for the purpose of suing on such contracts. This flows from the separability of the arbitration agreements. The disclaimer of the arbitration agreements leaves the receiver free to pursue these contractual claims through a court process.
2. **The position of the receiver**. The receiver is pursuing the claims in this case but the receiver is not a party to the arbitration agreements, which were agreements by Petrowest Corporation itself. As a result, the receiver is not bound by the arbitration agreements and is not compelled by applicable provincial arbitration statutes to proceed through the arbitration process.

The Court of Appeal's decision is not the end of the line, however. This matter will be considered further by the Supreme Court of Canada in the near future. Leave to appeal to the Supreme Court of Canada has been sought and granted.

Implications for commercial arbitration matters

The *Petrowest* decision will be relevant to parties to agreements with Canadian counterparties that contain arbitration clauses. Those parties may not be able to rely upon arbitration clauses when defending claims by the receiver of an insolvent Canadian counterparty.

The court in *Petrowest* notes that the analysis would be different in a debtor-in-possession restructuring scenario, where the debtor itself is pursuing contractual claims. However,



even in a debtor-in-possession restructuring, the debtor itself has the ability to disclaim agreements. When considering a disputed disclaimer in a debtor-in-possession context, the court is to review, among other things, whether the disclaimer would enhance the prospects of a viable compromise and whether the disclaimer would likely cause significant financial hardship to the counterparty. If these criteria are met, then a disclaimer of an arbitration agreement within a debtor-in-possession restructuring can also be feasible.

The following may be issues to be considered further following the *Petrowest* decision.

First, the scope of the doctrine of separability. The Court of Appeal explained that typically the doctrine is employed to preserve the effect of an arbitration agreement and the jurisdiction of the arbitrator even where a party impugns the validity of the contract in which it is found. It is not clear from the court's analysis if the doctrine necessarily must apply in all cases where a receiver is seeking to avoid the application of an arbitration clause.

Second, while a receiver may disclaim agreements, the authority to disclaim is not unlimited. Where a disclaimer is disputed, the receiver is to consider, among other things, equitable considerations and interests in in the context of the receiver's value maximization exercise. The court will similarly consider the equities between the parties if the disputed disclaimer is brought to court for determination. The appropriate balancing of these interests will be a continuing consideration in future cases. If there were compelling reasons to objectively favour an arbitration process over a court process (such as efficiency or speed), this would be a relevant factor for consideration.

Third, drafters of arbitration clauses in the Canadian context should consider including secondary jurisdiction clauses to respond to situations where arbitration provisions are not enforceable or are disclaimed.

Parties with an interest in these issues will be watching closely for any further guidance from the Supreme Court of Canada.

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Fair's fair... but is it, really? Regulating UK insolvency office-holders' conduct

Mark Craggs

Norton Rose Fulbright's Financial Restructuring and Insolvency team commonly advises clients on insolvency office-holders' conduct-related issues in different jurisdictions. These issues often concern whether or not insolvency office-holders – either themselves as clients or "across the table" from other stakeholders, principally creditors – should be acting in a certain way; and whether particular courses open to the office-holders, if followed, might harm others' interests in a way which is capable of being restrained by the court.

It is necessary in these cases to consider the applicable standards of conduct and advise accordingly. This is not as hard as it may seem since, invariably, it involves asking simply what is unfair. But is it really so simple? What does fairness mean in this context and how can insolvency office-holders avoid falling into bear-traps?

Lehman Brothers Australia

Last year, the UK Court of Appeal handed down judgment in the *Lehman Brothers Australia* case (*Lehman Brothers Australia Limited (in liquidation) (scheme administrators appointed) v Macnamara and others* [2020] EWCA Civ 321), on which Norton Rose Fulbright in the UK acted for the liquidators of Lehman Brothers Australia (**LBA**) on LBA's successful appeal relating to adjustment of its claim in the administration of the principal European hub in the Lehman Brothers group, Lehman Brothers International (Europe) (in administration) (**LBIE**). The case concerned the question of whether or not the UK administrators of LBIE were entitled to rely on release provisions of a settlement agreement entered into between LBIE and LBA and to refuse to vary LBA's proof of debt in LBIE's administration, where there had been a common error in calculating the settlement sum which had later come to light.

In giving judgment and reversing the Judge at first instance, the Court of Appeal unanimously confirmed the applicable standard of conduct is a simple one of fairness, and that it would have been unfair to allow the administrators of LBIE to rely on the release provisions and to refuse to vary LBA's proof of debt.

We advise regularly on the implications of the decision, which has had significant repercussions for insolvency practitioners and has subsequently been cited and relied upon in numerous cases (e.g. *HMRC v Sanders* [2021] EWHC 1843 (Ch) and, outside the insolvency context, *365 Business Finance Ltd v Bellagio Hospitality WB Ltd* [2020] EWCA Civ 588). The application of certain applicable principles – notably, the so-called principle (or rule) in *Ex parte James* – in other jurisdictions (e.g. Australia, Singapore and Bermuda), and the persuasive nature of UK authorities in those jurisdictions, means that the reach of the judgment is global, even by Lehman Brothers standards.

The facts and LBA's case

The facts can be stated briefly. In 2014, LBA and LBIE agreed to settle their mutual claims on the terms of a standardised and largely non-negotiable settlement agreement, in a form proposed by the UK administrators to over 2000 creditors of LBIE. In the course of the reconciliations involved in agreeing the settlement sum, and following a change in personnel on the LBIE team, an error was introduced into the relevant spreadsheet by LBIE which went unnoticed by LBA, such that LBA's claim had been understated by £1.67 million. (The error involved a Euro-denominated bond that should have been held by LBIE for LBA, but which was not, instead being shown to be denominated in Australian dollars, such that the conversion of LBA's claim against LBIE into pounds sterling for the purposes of LBA's proof of debt was carried out on an incorrect basis.) The recitals to the settlement agreement recorded the basis on which the settlement sum had been arrived at – by setting off mutual claims – but its operative provisions referred only to the result of the calculations. The liquidators of LBA noticed the claim two years later and immediately raised it with the administrators of LBIE, seeking a variation of LBA's proof of debt. The administrators advised them formally to write and articulate the basis on which a variation was sought, which they did. The administrators refused to vary LBA's proof in reliance on broad release provisions in the settlement agreement and on the basis that, if they had agreed, other creditors might be encouraged to re-open bargains reached with LBIE. In the event, it transpired that there was no evidence that the "floodgates" would open in the way that had been suggested.

LBA's case was advanced on the basis both of the principle in *Ex parte James* and paragraph 74 of Schedule B1 to the UK Insolvency Act 1986, under which creditors can apply to court to restrain proposed conduct on the part of administrators that would unfairly harm their interests. The principle in *Ex parte James* derives from the case of the same name in which the English court found that insolvency office-holders – as officers of the court – were not entitled to rely on the then-applicable principle that money paid under a mistake of law is not recoverable.

High Court

At first instance, Mr Justice Hildyard threw out LBA's claim, on the basis that the applicable standard of conduct to be avoided under *Ex parte James* was "unconscionability" and not unfairness, and that neither *Ex parte James* nor paragraph 74 could be invoked (*"as a magic wand"*) so as to interfere with contractual obligations freely entered into, unless there was a contractual basis for rectification. This approach overlooked recent Supreme Court authority, in the *Nortel* case, where Lord Neuberger had referred to the applicable test as being one of unfairness. In reaching his decision, the Judge dismissed a test of fairness as being *"an ultimately subjective standard"*, capable of becoming an *"unruly horse"*, and therefore rejected LBA's *"siren call"* for variation of its proof of debt.

In an earlier LBIE-related case, the same Judge had referred to the principle in *Ex parte James* in the course of argument as a *"sort of general palm tree"*.

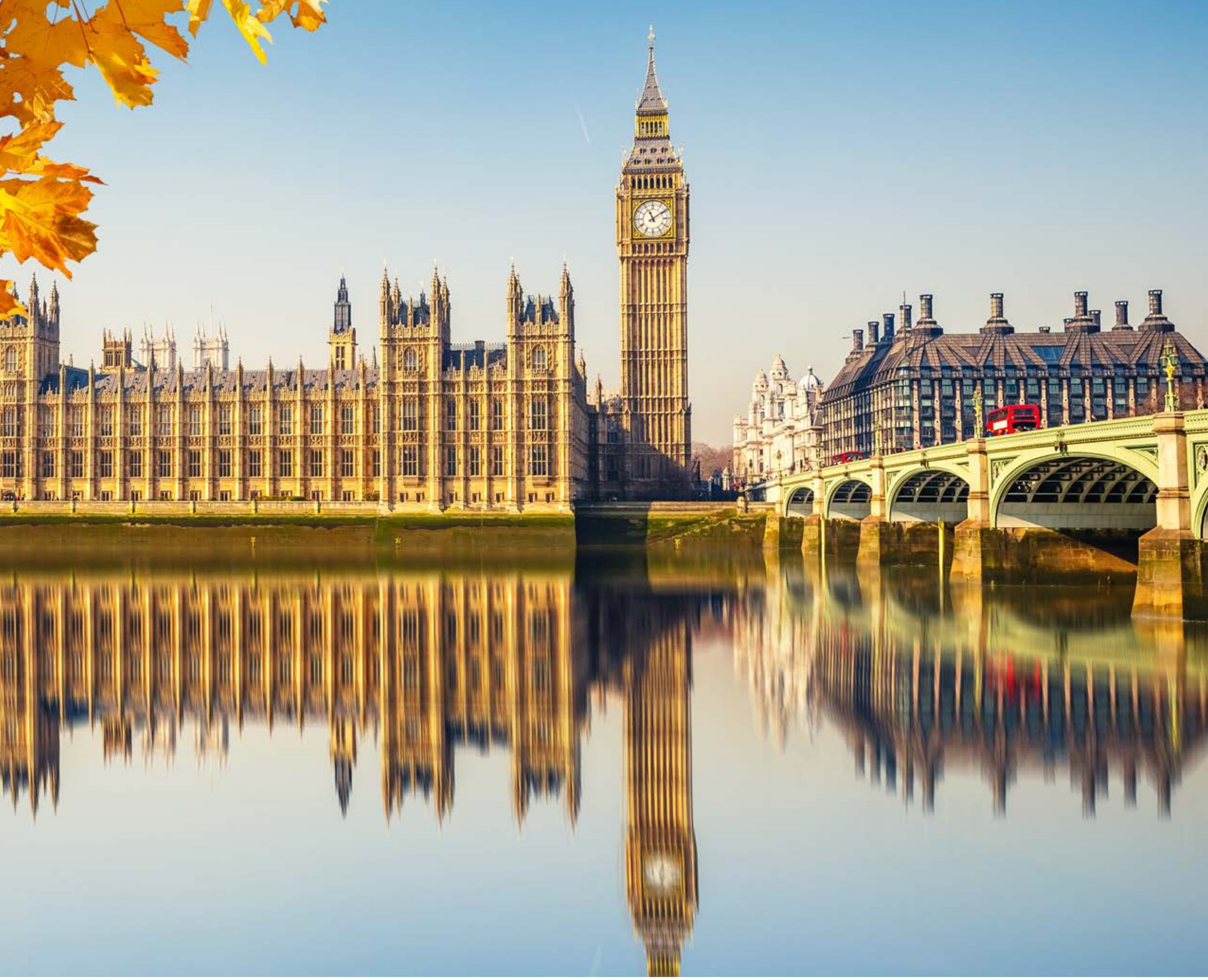
Court of Appeal

The Court of Appeal reversed the Judge's decision, identifying the correct threshold test for the application of the principle in *Ex parte James* as being one of unfairness, consistently with Lord Neuberger's remarks in *Nortel*. Lord Justice David Richards (with whom Newey and Patten LJJ agreed) observed that many different terms had been used in the past to describe the principle but that this was not surprising on the basis that the principle does not have a statutory basis and in light of the evolution of the standards expected by society. Rejecting the notion of fairness being an *"unruly horse"*, he noted that *"the courts are very familiar with applying a standard of fairness in many different context, including in the contexts of administrations under paragraph 74…"*. In terms of the justification for the principle, his Lordship noted that *"As a public authority and given its role in society, the court is expected to apply standards to its own conduct which may go beyond bare legal rights and duties"*. Further, since insolvency office-holders such as administrators are officers of the court, they act on behalf of the court in carrying out their functions and will therefore be held to the same standards by the court. Contrary to the finding at first instance, David Richards LJ held that the court applies the standard of fairness on an objective basis. In doing so, he noted that *"As a regulated profession, insolvency practitioners may feel aggrieved at a challenge to their conduct or proposed conduct on this basis and may be tempted to argue that the challenge is an attack on their personal integrity. This would be a misapprehension on their part"*. This had been critical to the way LBA's case was framed: no wrongdoing on the part of the administrators of LBIE had been alleged; it was argued – successfully, ultimately – that they had simply got it wrong.

So far as paragraph 74 is concerned, the Court of Appeal held, too, that the applicable standard is one of fairness, as mandated by the statutory language. In particular, the Court rejected the suggestions made by the Judge that the requirement for unfair harm justifying intervention under paragraph 74 has additional conditions, notably where particular acts cannot be justified by creditors' interests and/or is discriminatory in effect.

The Court of Appeal concluded that there is no principle to the effect contended for by the Judge that neither *Ex parte James* nor paragraph 74 can be invoked to prevent an administrator from relying on rights under a contract freely entered into by both parties (per David Richards LJ, at [87] and [90]):

> In all cases the rule in *Ex parte James*, and in at least some cases paragraph 74, will be invoked to restrain an officeholder from relying on his strict legal rights. Those rights may arise at common law or in equity or under statute, and, in my judgment, there are no grounds for excluding contractual rights from the scope of either the rule in *Ex parte James* or paragraph 74. Whether reliance on



strict contractual rights should be restrained will, as in all these cases, depend on the facts of the particular case.

…

The judge's statement of general principle that neither the principle in *Ex parte James* nor paragraph 74 is applicable to contractual rights cannot, in my judgment, stand.

The Court dismissed an argument advanced on behalf of the administrators that granting the requested relief to LBA would be an unfair one-way bet in LBA's favour, on the basis that the administrators are subject to paragraph 74 and, as officers of the court, to the principle in *Ex parte James*, but neither would apply to LBA. In this regard, David Richards LJ noted that (at [101]):

It is… in the very nature of the rule in *Ex parte James* that it controls the conduct of officers of the court, who are expected to observe higher standards than other parties. There is nothing unfair in that. On the contrary, it gives effect to a basic principle governing the conduct of the court and its officers. As for paragraph 74, it is by its terms applicable only against administrators.

In summary, the Court of Appeal allowed LBA's appeal, concluding that LBA was entitled to the variation of its proof of debt on both bases sought: *"no right-thinking person would think it fair for the administrators to stand on their strict contractual rights and refuse to correct a shared mistake for which they were as responsible as LBA"* (per David Richards LJ, at [103]). Accordingly, it was held that (per David Richards LJ, at [95]):

In the absence of significant contrary considerations, no legitimate reason existed for the administrators not to correct the common mistake admittedly made by them and by LBA. In the absence of such considerations, no statutory purpose was served by not correcting the error. Leaving matters as they were would deprive LBA of its true entitlement on the agreed basis of valuing claims and would give the estate a corresponding windfall, albeit of a small amount in the context of the LBIE estate.

Commentary and practical pointers

The Court of Appeal's decision is commendable in that it reserves to the court the ability to restrain its own officers in appropriate circumstances. This may be necessary in cases where, judged objectively, officers of the court have acted unfairly to harm the interests of other parties, including where strict reliance on the terms of a contract – whether or not in a standard, non-negotiable form – by an insolvency office-holder is capable of causing unfair harm to the creditor counterparty. On a practical level, our experience is that the judgment has had positive consequences for everyday insolvency practice, both in the UK and further afield; and it has served, in certain instances, to encourage insolvency office-holders to explore means of resolving disputes other than litigation, to the benefit of stakeholders generally.

There are a number of practical lessons to be drawn from the case, for both insolvency office-holders and their advisors, including the following:

- in general terms, so long as insolvency office-holders are acting in a way mandated by their statutory and other duties, they will be justified in doing so. However, in exercising their powers on matters where it is permissible to use discretion, they need to be careful that their proposed course is not capable of causing, or likely to cause, unfair harm to creditors or others;
- everyone makes mistakes. Even if it appears superficially attractive to adopt an entrenched position on a particular matter where a mistake has occurred, there is always merit in stepping back and taking stock of the situation by reference to an insolvency office-holder's duties and the course that would be mandated by complying with those duties; doing so can help avoid unnecessary, protracted and expensive litigation with potential costs exposure for the insolvent estate;
- insolvency office-holders are under a duty to ascertain creditors' claims. While the use of settlement agreements for the purposes of agreeing claims might be justified in certain cases (for example, where the agreement of claims as liquidated amounts and regularising the terms on which claims can be transferred or assigned to others), this practice can never be a surrogate for the proof of debt process; in other words, it will not be possible for office-holders essentially to "contract-out" of the proof of debt regime and rely on contractual restrictions that would not ordinarily be available to them (especially where this is done on a "take-it-or-leave-it" basis); and
- in the context of concurrent insolvency proceedings relating to companies in the same group where there are or have been complex claims reconciliations processes between different estates (and often across international borders), there is merit in appointed office-holders (and/or the relevant debtors) adopting a pragmatic approach to the resolution of differences between them and any errors that might subsequently come to light. In some cases, the approach to be taken might be assisted by the terms of any cross-border insolvency protocol to which the relevant parties are signatories.

Although the *Lehman Brothers Australia* case provides welcome clarity on the principle in *Ex parte James*, certain anomalies remain in relation to the extent of its application, including with respect to office-holders who are not (or are no longer) officers of the court, such as liquidators in a creditors' voluntary liquidation (particularly where the company has transitioned to creditors' voluntary liquidation from administration). It is outside the scope of this article to consider those issues, although some guidance in the case of administrators who have vacated office has recently been provided in *Re Rhino Enterprises Properties Limited* [2021] EWHC 2533 (Ch). It is to be hoped that further clarity on the extent of the principle in *Ex parte James* will be obtained in future cases, now its meaning and scope have been firmly established.[1]

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1 Norton Rose Fulbright has successfully represented clients on a number of other Lehman Brothers-related cases in the case of the long-running group insolvency proceedings, including *Re Lehman Brothers International (Europe) (in administration)* [2012] UKSC 6 (the "Client Money" case), *Re Lehman Brothers International (Europe) (in administration)* [2012] EWHC 2997 (Ch) (the "Extended Liens" case) (in both cases, acting for the trustee for the liquidation of Lehman Brothers Inc.) and *Lehman Brothers International (Europe) (in administration) v ExxonMobil Financial Services B.V.* [2016] EWHC 2699 (Comm) (acting for ExxonMobil Financial Services).

Proposed legislation may trip-up international bankruptcy filings in the United States

Michael Berthiaume

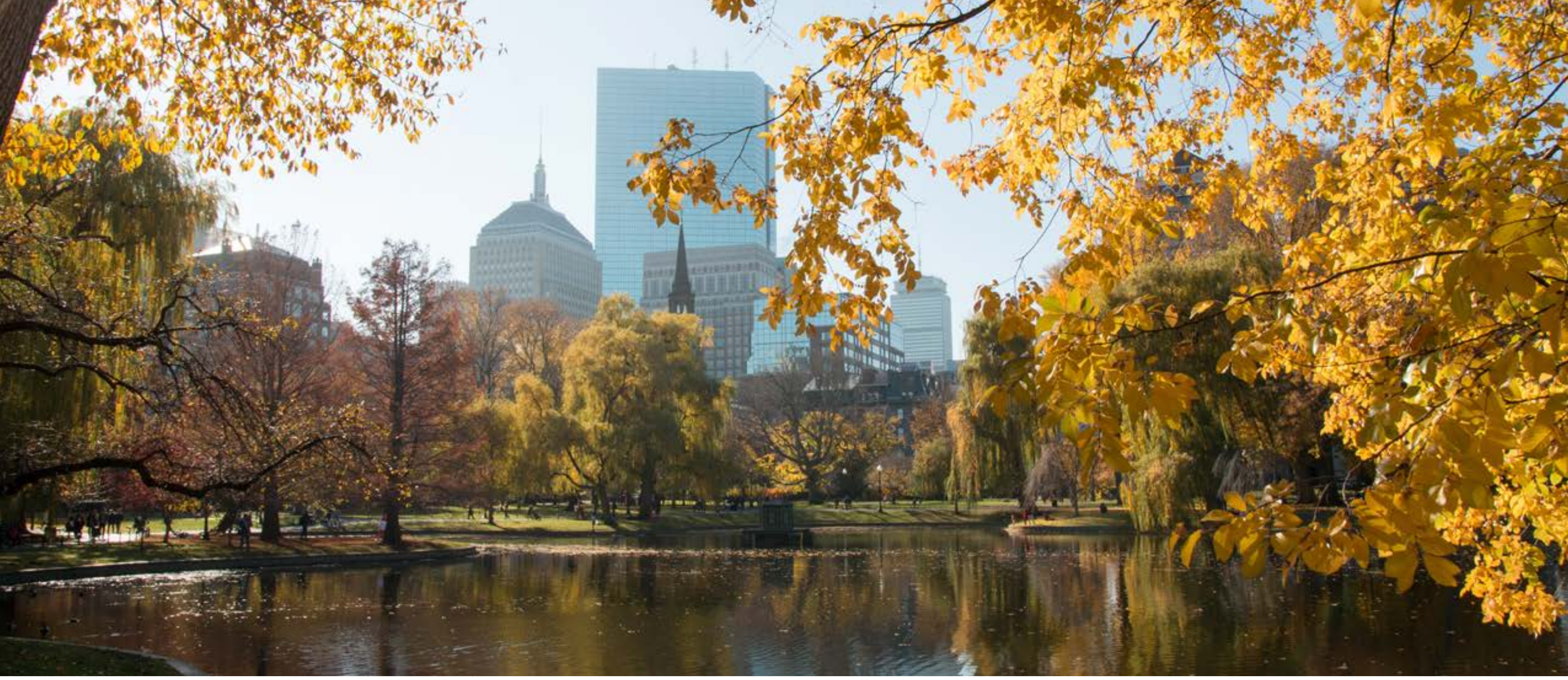
Since enactment, Chapter 11 under the United States Bankruptcy Code has proven a safe haven for international debtors. The opportunity to restructure an entity's debts in the United States has been a particularly effective device, prompting international corporations to file in the US in lieu of local insolvency proceedings, in large part due to the advantages of the US court system and Chapter 11's proven track record. However, recently proposed legislation geared towards reforming the US Bankruptcy Code's venue statute may have the unfortunate, even if unintended, consequence of restricting an international debtor's ability to file bankruptcy in the US.

For years, international corporate debtors have sought out protection under the US Bankruptcy Code because it provides protections that are (or at least were) otherwise unavailable in many other jurisdictions around the globe. Notably, a restructuring in the US allows management to stay in control of the company, envisions an immediate and worldwide injunction against all creditor actions, encourages and facilitates new financing, and allows restructuring plans to move forward without unanimous creditor support. Moreover, beyond the US Bankruptcy Code itself, US Bankruptcy Courts tend to move more quickly and be more reorganization friendly than those in other jurisdictions.

A large driver of the US Bankruptcy Courts' popularity has been ease of access. The statutes that define the parameters of who can be a Chapter 11 debtor, and what court may oversee the restructuring, are extremely broad. Any entity that is domiciled in the US, has a place of business in the US, or has property in the US, may avail itself of Chapter 11. *See* 11 U.S.C. § 109. A debtor further may file its petition in any venue where it is domiciled (*i.e.* incorporated), where its principal place of business in the US is located, where its principal assets in the US are located, or in any venue where any of its affiliates can file. *See* 28 U.S.C. § 1408. In contrast to other countries, the debtor need not be a domestic company to file for bankruptcy in the US Importantly, no threshold or minimum amount of assets located in the US is required to qualify. In fact, courts have considered bank accounts, attorney retainers, and even causes of action owned by a foreign debtor as property in the US for purposes of eligibility. This has allowed many international companies to restructure their debts in the US even though they hold very little assets in the US.

Proposed changes to the venue requirements in the US Bankruptcy Code could threaten the US Bankruptcy Courts' command of international restructurings, and do so at a time when many of the US' perceived competitive advantages are diminishing. Specifically, on June 28, 2021, H.R. 4193 was introduced with the purpose of amending the venue statute and modifying these venue requirements. On September 23, 2021, its Senate companion bill was announced with substantially identical language. Both propose to eliminate the ability to "forum shop" by excluding a debtor's place of incorporation from the venue analysis, and—alarming to international debtors—excluding cash or cash equivalents from the "principal assets" equation. Additionally, any equity interest in an affiliate will be deemed located in the same location as the principal.

Support for this venue reform has been fueled, in part, by testimony in Congress. Generally, this testimony has been focused on controversial third party release provisions implemented in recent mass tort cases such as Purdue Pharma, Boy Scouts of America, and many Catholic diocese bankruptcies. These provisions frequently force creditors to release non-debtor third parties as part of the debtor's plan of reorganization, even though such releases are arguably not permitted, at least in some circuits, by the Bankruptcy Code. Testimony before Congress asserts that, because of the generous nature of the current venue provisions, debtors are able to manufacture jurisdiction in favorable courts merely by setting up bank accounts or securing a mailing address in the venue of their choice. In effort to stamp out this behavior, the proposed legislation claims to limit "forum shopping" by prohibiting entities from filing in any venue except where their corporate headquarters or principal physical assets—



excluding cash and equity interests—are located. Ostensibly, these bills would promote the filing of Chapter 11 cases in other US districts, and steer cases away from the favored courts in New York, Delaware and Texas. In so doing, creditors and stakeholders purportedly will be afforded more opportunities to participate in the bankruptcy proceedings.

Despite their laudable purpose, these proposed amendments could have unexpected and potentially adverse consequences when viewed from an international restructuring prospective. While congressional testimony and other commentators assume that venue reform would merely ensure that domestic companies would file in a different jurisdiction within the US, it is a distinct possibility that international debtors may pass on the US Bankruptcy Courts altogether.

First, some international debtors may simply be denied access to US Bankruptcy Courts. Without the consideration of cash accounts as an avenue toward eligibility, many foreign corporations without tangible assets in the US may not qualify to file a Chapter 11 bankruptcy in any US jurisdiction. Second, even if they do qualify, international debtors may not be able to count on access to the usual and convenient reorganization friendly jurisdictions. Instead, being tied to the location within the US of their tangible assets, foreign entities may be forced to rely less frequented bankruptcy jurisdictions to guide their restructuring. Given the complex issues frequently at play in an international restructuring case, this may cause the debtor and creditors some uncertainty. This uncertainty, in turn, may motivate international debtors to file in their own countries, or in other more advantageous countries, instead.

Notably, this proposed venue reform comes at a time when many countries are emulating the US and revamping their own restructuring laws. As discussed in previous editions of this International Restructuring Newswire, several international jurisdictions have reformed or have proposed to reform their restructuring laws with the design of attracting international debtors:

- **Italy:** Set to take effect in September of 2021, the Italian Code of the Business Crisis and Insolvency seeks to create a means to identify a debtor's pending financial crisis and manage insolvency with the aim of overcoming financial distress and restoring profitability to the company. In a departure from their previous restructuring system which emphasized liquidation, the new Code's goal is to restructure and preserve the entity as a going concern. Thus, debt restructuring agreements may be approved with as little as 30 percent approval from the overall debt. However, unlike the US, Italy's new Code will not feature an *automatic* stay of enforcement actions by creditors. Instead, the debtor must request the imposition of an injunction from the court.
- **Canada:** In February of 2021, a Canadian court extended the country's approval of third party release provisions. In Canada, businesses generally reorganize under the traditional insolvency statutes of the Companies' Creditors Arrangement Act (**CCAA**). Third party releases under the CCAA—while hotly contested in the US—are a common aspect of restructuring plans. Canadian law also provides an alternative to a CCAA restructuring via the Canada Business Corporations Act (**CBCA**), which offers a more streamlined approach, but without some of the benefits of the CCAA. The recent court decision makes clear, though, that despite the CBCA's more limited nature, third party release provisions may still be acceptable. Therefore, companies may still avail themselves of a less cumbersome restructuring available under the CBCA, while still receiving the benefits of third party releases.
- **The Netherlands:** Effective as of January 1, 2021, the Dutch Act on Court Confirmation of Extrajudicial Restructuring Plans has created a debtor-in-possession procedure conducted outside of formal bankruptcy proceedings. Based on the US' Chapter 11 process, this scheme takes place

with limited court involvement, but still allows for a debtor in possession, provides for a stay as to certain creditors, allows the debtor to invalidate ipso facto clauses, sell unencumbered assets in the ordinary course of business, and otherwise restructure its debts in a cram-down plan of reorganization.

- **Germany:** Effective as of January 1, 2021, Germany's new Act on the Stabilization and Restructuring Framework for Businesses provides for pre-insolvency restructuring proceedings. Prior to its enactment, German companies had no option to restructure their debts through the courts. Now, distressed companies can call upon German courts to restructure their debts and otherwise preserve the going concern value of their business by using many of the same tools available in the US, such as maintaining control of their business, imposing cram down restructuring plans, and implementing collection moratoriums.
- **Australia:** Effective in January 2021, the Corporations Amendment (Corporation Insolvency Reforms) Act 2020 marked the most significant corporate insolvency reform in Australia in nearly thirty years. Inspired by Chapter 11 of the US Bankruptcy Code, this new structure simplifies the debtor-in-possession restructuring process largely in effort to help small and medium sized businesses. While prior law was long criticized as too expensive and too complex because of its "one size fits all" approach, this new legislation incorporates the debtor in possession model, and provides for a streamlined liquidation process when necessary**.**
- **United Kingdom:** In June 2020, the United Kingdom enacted the Corporate Insolvency and Governance Act of 2020 (**CIGA**). Similar to other countries, the UK describes these reforms as the most wide-ranging amendments to its insolvency laws in a generation. Notably, CIGA provides for a collection moratorium, invalidates certain provisions of pre-insolvency contracts, and allows entities to propose an arrangement with shareholders and creditors, all of which permits the formation of a cram-down plan similar to what may be accomplished under Chapter 11 of the US Bankruptcy Code.
- **Singapore:** In 2017, Singapore adopted enacted the Companies (Amendment) Act 2017 (Singapore), which made major legislative changes to the restructuring provisions of the Singapore Companies Act (Cap 50) 2006. The new legislation is modelled after Chapter 11 of the US Bankruptcy Code, and affords the benefits of an automatic stay and the granting of super priority to new financing, as well as permits both cram-down plans and pre-packaged plans. As a result, the law has significantly enhanced the restructuring tools available in Singapore courts and propelled Singapore as a leading hub for insolvency in the Asia-Pacific.
- **India:** In May of 2016, India enacted the Insolvency and Bankruptcy Code, which completely overhauled the bankruptcy laws in India. This legislation seeks to incentivize further investment in the country by providing greater certainty and efficiency to the restructuring process. Further, in November of 2019, the Indian Government expanded the scope of the law to make more entities eligible for restructuring.

Given these recent changes, international debtors now have more options than ever. Even without the proposed restrictions on eligibility, foreign entities may less need to flock to the US as before. Further, should the US' venue laws be amended to prevent easy filings in certain convenient and beneficial venues, international debtors may begin to consider other locales. Simply put, without careful consideration of possible unintended consequences, venue changes in the US could cause foreign entities and their creditors to take their restructurings elsewhere.

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