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Strategic Considerations for Multinational Distressed Companies and Their Investors: When to File, What to File and Where to File

OUTLINE OF KEY CONSIDERATIONS

A multinational distressed company's ability to maximize its restructuring potential requires careful planning and an understanding of the issues raised by competing and potentially co-equal insolvency regimes. The following outline identifies key factors that inform strategic considerations for multinational distressed companies and their investors when determining when, what and where to file to implement their cross-border restructuring objectives.

I. When to File: out-of-court workout versus court-supervised proceedings

Most modern legal regimes provide some form of statutory framework in which a company can restructure its business. A formal court-supervised restructuring proceeding, however, may not always present the best reorganization prospects. An out-of-court workout may provide a more efficient and less costly platform. When to file a bankruptcy case or pursue an out-of-court workout accordingly presents the initial and one of the most challenging questions a distressed company and its investors face. Considerations to analyze include: the company's rehabilitation prospects; the form of available workout; process drivers; and stakeholder leverage.

A. Company prospects – can it be rehabilitated?

A company's rehabilitation prospects informs any decision to pursue an out-of-court restructuring or filing court proceedings. Identifying the source of a company's distress, and analyzing the tools necessary for its recovery, will drive the filing decision. At its core, this requires an understanding of whether the company is viable, and if so, how it can be restored to profitability.

1. Is the company's business viable? Certain factors to consider when identifying the business drivers underlying the company's distress include:

   a) Slower industry declines vs. sudden, nonrecurring shocks

   b) Nature of the enterprise

      (1) Manufacturing

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(2) Financial

(3) Real estate

(4) Transportation / regulated entity

(5) Conglomerate

2. What is the company's financial condition? Certain factors to consider when analyzing the company's financial health include:

a) What are the company's immediate financial needs?

(1) Near term maturities

(2) Covenant defaults

(3) Trade / general liquidity

b) What are the company's long-term financial fixes and does it have an exit strategy?

c) How does the complexity of the company's capital structure affect its workout potential?

(1) Secured vs. unsecured debt

(2) Upcoming maturities

(3) Existence and use of derivatives by and against the company

(4) Structural and contractual priorities

(5) Existence of cross-defaults (credit and operating agreements)

(6) Differing yields

(7) Number of issuances

(8) Concentration of debt holders

(9) Identity of debt holders (original, distress investors, government)

(10) Existence and use of factoring or securitization facilities

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d) What impact does the company's organizational structure have on its restructuring objectives?

(1) Simple TopCo / HoldCo structure

(2) Need for structural reorganization (*e.g.*, to address post-merger amalgamation with poorly integrated divisions, legal groups and accounting systems)

(3) Existence of special purpose entities or bankruptcy remote entities that cannot be filed or easily restructured

3. What is the company's geographic blueprint? Certain factors to consider when analyzing the company's geographic spread and the legal regimes in which it operates include:

a) Location of center of main interests / headquarters

b) Nature of supply and distribution chain: number, concentration and location of critical vendors and customers

c) Where are physical assets situated?

d) Which country's legal regime governs

(1) Operations

(2) Sales

(3) Minimal jurisdictional contacts

B. Identifying the company's restructuring goals – what needs to be fixed?

When to pursue an out-of-court workout versus a formal filing also depends on what the distressed company most needs to change. Is the business sound but the balance sheet overleveraged? Does it require significant operational fixes, such as reducing over-capacity or streamlining production, that may require consolidation or asset divestiture? Identifying both near-term and long-term restructuring goals – what must be fixed and what should be fixed – further informs the decision of when to file. Areas to consider here include:

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1. Balance sheet

2. Scope of operational fix: division / product specific vs. more enterprise-wide re-positioning

3. Existence of material litigation (commercial tort, environmental)

4. Existence of legacy pension and union liabilities

C. What restructuring tools exist?

Any restructuring effort requires an understanding of the company's restructuring options. What out-of-court platforms exist? How do they differ from court-supervised proceedings? What are the benefits and drawbacks of the different approaches? The following provides an overview of U.S. options:

1. Benefits of an out-of-court workout

a) Speed

b) Lower administrative costs

c) More control over process (no official creditors committee; generally less litigious and adversarial; formulating restructuring proposal potentially less complicated than statutory process)

d) Less adverse publicity

e) Not as much management diversion (operating in chapter 11 requires significant management involvement in court process, including potential court appearances, and non-ordinary course transactions require court approval)

2. Benefits of a court-supervised process

a) Automatic stay or other injunctive relief

(1) Stops most creditor enforcement actions

(2) May halt interest accrual

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b) Ability to bind dissenting creditors

c) Opportunities for debtor-in-possession financing

d) Exclusive period in which to file a reorganization plan

e) Specialized and centralized forum for resolving disputed, contingent and unliquidated claims

f) Availability of release and exculpation clauses

g) Avoidance actions

h) Contract modification, assumption/rejection and assignment opportunities

i) Potentially favorable tax treatment

j) Known forum for asset divestitures / acquisitions

k) Claims adjustment

(1) Subordination

(2) Avoidance

(3) Penalties / fines

(4) Substantive consolidation

l) May provide streamlined platform for distributing value to stakeholders through issuance of new securities (*e.g.*, section 1145 of the Bankruptcy Code)

3. Consider factors that can determine whether an out-of-court workout will succeed, including:

a) Debt holders: who are they and how widely is the debt held?

(1) Bank syndicate

(2) Public bonds

(3) Institutional holders vs. street holders

(4) Government or regulatory oversight

(5) Pension trustee / PBGC

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b) How good are investor relations and the company's level of trust with key stakeholders? Does the company have an ability to produce credible financial information and forecasts?

c) Financing the process: how will the company pay for its restructuring?

(1) Cash reserves

(2) Refinance existing facilities

(3) Availability of, and need for, new credit

(4) Asset sales

d) Can the company afford the restructuring?

(1) Financial expenses

(2) Ordinary course of business expenses

(3) Extraordinary costs

(4) Legal and professional advisors

(5) Publicity and revenue impact

e) How do the company's current and future liabilities inform its restructuring prospects? Some factors to consider when analyzing whether an out-of-court workout will fully address liabilities include:

(1) Existence of disputed claims to be resolved

(2) Contingent and unliquidated claims

(3) Significant past-due trade

(4) Customer relations and claims

(5) Employee claims and liabilities

f) Operational drivers – *i.e.*, what impact will the workout have on the company's business – also inform whether to pursue an out-of-court workout. These drivers include:

(1) Management depth and ability to navigate the process

(2) Need to restructure, reject or cure contracts

(3) Employee and labor relations

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(4) Trade / vendors / supplier interests

(5) Customer expectations

(6) Existence and role of regulatory authorities

g) Impact on balance sheet

D. Types of out-of-court workouts in the U.S.

1. Forbearance / refinance

2. Modifying funded debt

3. Exchange offers

4. Informal wind-downs (*e.g.,* assignment for the benefit of creditors)

5. Other (Non-U.S. jurisdictions may embrace extra-judicial workout proceedings that are self-governing or subject to widely held expectations or protocols)

E. Implementation and Process: planning and timing the out-of-court workout

Whether in or out of court, a successful corporate restructuring requires significant planning and effective negotiation. A distressed company and its investors often engage a restructuring team that includes key management personnel, legal and financial advisors, and crisis management professionals. The restructuring team will conduct extensive legal and financial due diligence, and assist the company with developing a sound business and restructuring plan. Planning and timing the out-of-court workout entails numerous steps, including:

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1. Timing (how far in advance? how initiated?)
    a) Negotiating standstills and forbearance agreements
    b) Exit strategy
    c) Stabilizing operations and cash flow
2. Assembling the restructuring team
    a) Management
    b) Legal
    c) Financial advisor / investment bank
    d) Accounting / tax advisors
    e) Crisis manager / restructuring officer
    f) Public relations
3. Due diligence
    a) Legal
    b) Financial
    c) Operational
4. Developing a business and restructuring plan
    a) Review business
    b) Identify necessary changes
    c) Projections
    d) Enterprise value
    e) Allocation of value
    f) Financial projections and debt capacity
5. Identifying and addressing management concerns
    a) Director & officer fiduciary duties across legal regimes
        (1) Operating in the "zone of insolvency": in many European countries, directors of an insolvent company

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must commence insolvency proceedings or risk personal liability to creditors[1]

(2) Most non-U.S. insolvency regimes replace or disempower management upon commencement of formal proceedings. This "debtor in non-possession" outcome also influences out of court work-out dynamics[2]

b) Legislative framework (*e.g.*, Sarbanes-Oxley / Foreign Corrupt Practices Act)

c) Retention / replacement of executive talent

d) Labor relations

F. Stakeholders: understanding dynamics and leverage

A successful out-of-court workout depends in large part on the company's universe of stakeholders, and their willingness to work with the company. A distressed company should identify key stakeholders: those entities necessary to deliver a confirmable plan. Appreciating stakeholder concerns, being responsive to their economic, legal and business incentives, further promotes a company's ability to successfully negotiate a workout.

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1 Douglas P. Bartner*, Restructuring In and Out of Court*, 1347 PLI/Corp H 732 (2002).

2 Nathalie Martin, *Common-Law Bankruptcy Systems: Similarities and Differences*, 11 AM. BANKR. INST. L. REV. 367, 390-402 (2003).

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1. Lenders (institutional/revolver lenders; hedge fund/term lenders) face a number of issues when dealing with distressed borrowers. These impact their negotiating flexibility and include, for example:

a) Economics (are they original holders or distressed investors?)

b) Existence of potential lender liability actions

c) Intercreditor agreements

d) Lien priorities and asset allocations between and among lenders

e) Type of lending relationship (secured / unsecured, term, asset-based, factoring arrangement or securitization, etc.)

f) Necessity of collective action through a syndicated facility

2. Bondholders bring their own unique dynamics to any workout situation. These include:

a) Economics (are they original holders or distressed investors?)

b) Location in the corporate structure (are they structurally senior or junior to other stakeholders? do special corporate structures exist, such as a ULC or joint venture arrangement, that uniquely affect certain bond issues?)

c) Are any of the bonds guaranteed and by whom?

d) Existence of intercreditor agreements

e) Concentration of holders within an issue or across issues

f) Necessity of collective action to direct indenture trustee; otherwise, likelihood of concerted action (ad hoc groups)

3. General unsecured creditors also face legal and practical challenges.

a) The existence of potential avoidance actions against unsecured creditors, including preference actions against trade creditors, may affect their willingness to extend prepetition credit and negotiate more favorable commercial terms with a company during the pre-filing period

b) Uncertainty (some creditors may prefer the certainty of chapter 11 treatment, including its creditor protections, over a less transparent out-of-court process)

c) The existence of a liquid market for trading bankruptcy claims may influence negotiating dynamics with trade creditors (a

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prepetition trade creditor may sell its claim leaving the company with an unknown third party as the economic stakeholder in a subsequent bankruptcy filing)[3]

4. Activist investors seeking to influence change through acquisition of distressed debt (bank and bond debt) also affect the dynamics of corporate restructuring. Activist investors' efforts to obtain control in distressed situations may shape the role of management and ability of management to retain control over the company's future.[4]

5. Finally, tax considerations will affect all stakeholders and must be considered.[5]

a) Bankruptcy provides potentially more favorable federal income tax treatment of cancellation of debt ("COD") income to the debtor

b) A company may preserve future net operating losses ("NOLs") and other tax attributes in bankruptcy

c) Members of consolidated tax groups may not align with those corporate entities in need of financial or organizational restructuring (consider whether the IRS may have recourse against non-filing legal entities within a consolidated tax group)

d) Restructuring debt may have significant tax consequences to debt holders (*e.g.,* basis in new post-emergence securities)

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[3] *E.g., ReGen Capital I, Inc.* v. *UAL Corp. (In re UAL Corp.)*, 635 F.3d 312, 324 (7th Cir. 2011) (purchaser of a pre-petition unsecured claim arising from executory contract is not entitled to a "cure" that would pay it 100 cents on the dollar for the contract claim and noting that the claims trader "held only an assigned claim, it had nothing to offer [the debtor] in return for assumption. [The contract counterparty] AT&T had no incentive to insist on an early and final assumption decision or full cure that would provide it with no benefit at all.")

[4] Michelle M. Harner, *The Corporate Governance and Public Policy Implications of Activist Distressed Debt Investing*, 77 FORDHAM L. REV. 703, 760-66 (2008) (concluding that activist investors have increasingly rendered restructuring in the U.S. and U.K. more "management neutral" as the distressed investor assumes a controlling stake in the company and becomes the dominant negotiating force in the restructuring process, thus resulting in management not remaining the party principally designing and insisting on a particular restructuring plan).

[5] B.N.A Tax Management Portfolios, *The Decision to File for Bankruptcy*, TMFEDPOR No. 790 § II, 20XX WL 4741500 (FEDERAL) (Tax Management Inc., 2010).

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e) Tax sharing agreements between corporate groups within an enterprise, and with former group members no longer owned by the company, may exist

G. Potential for failure and subsequent bankruptcy filing

In an informal workout, a company faces the risk that a group of creditors may file an involuntary petition against the company. Out-of-the money creditors, for example, who can expect little or no recoveries if the company contemplates (or is rumored to contemplate) a "cramdown plan," may feel they have nothing to lose by filing an involuntary petition. A company may also simply not succeed in enticing or coercing a consensual restructuring without court protection. Accordingly, a distressed company pursuing an out-of-court workout should do so with the knowledge that a formal bankruptcy case may nonetheless result, and should plan accordingly.[6]

II. What to File: identifying appropriate bankruptcy relief in the U.S.[7]

Once a distressed company decides to file for bankruptcy relief, it needs to identify the type of bankruptcy process it wants to pursue. The Bankruptcy Code provides various forms of relief, including liquidation under chapter 11 and chapter 7 and restructuring under chapter 11. Chapter 11 cases themselves, come in a variety of flavors.

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[6] Harner, *supra* note 3, at 765-66. Indeed, in the U.S., companies and stakeholders negotiate knowing that chapter 11 provides a backstop. *Id.* ("As one of Granite Broadcasting's preferred shareholders explained in an email regarding his failure to respond to Silver Point's proposed out-of-court restructuring plan, 'I'd rather fight in [Chapter] 11. I'd rather have a battle.'")

[7] A company's formal bankruptcy options will differ from country to country. Many jurisdictions now recognize court-supervising restructurings in some form in addition to the more traditional liquidation of assets upon insolvency. *See, e.g.,* GETTING THE DEAL THROUGH – RESTRUCTURING & INSOLVENCY 2011 IN 50 JURISDICTIONS WORLDWIDE, (Law Business Research Ltd. 2010) (providing a comparative international analysis in key areas of insolvency law). A review of U.S. Bankruptcy Code options illustrates types of available statutory relief and the related considerations a company and its investors may consider when selecting a form of bankruptcy filing.

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A. Forms of chapter 11 relief: prepaks to freefalls

1. Prepackaged chapter 11 case

   a) Chapter 11 plan prepared, distributed and solicited before filing

   b) Pre-filing solicitation requirements[8]

      (1) Adequate disclosure that complies with applicable nonbankruptcy law, rule or regulation versus

      (2) "adequate information" as required by the Bankruptcy Code[9]

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[8] 11 U.S.C. § 1126(b).

[9] 11 U.S.C. § 1125.

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c) Chapter 11 plan filed on the petition date[10]

d) Debtor must distribute disclosure document, but no court approval of disclosure statement required[11]

2. Pre-arranged / pre-negotiated chapter 11 case

a) Chapter 11 plan negotiated with creditors and shareholders before filing but formal solicitations obtained after filing

b) Court approval of disclosure statement required for post-petition solicitation, but acceptances of plan may be solicited from a claim or interest holder if solicitation complies with applicable non-bankruptcy law and if holder was solicited prior to the commencement of the case in a manner that complied with applicable non-bankruptcy law.[12]

c) Use of lock-up agreements and term sheets

3. Conventional chapter 11 case

a) Conventional

b) "free fall"

4. Section 363 sales outside of chapter 11 plan[13]

a) Section 363 authorizes sale of all or substantially all of the company's assets outside the ordinary course of business[14]

b) Governed by "sound business reason" test[15]

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[10] 11 U.S.C. § 1121(a).

[11] 11 U.S.C. § 1126(b).

[12] 11 U.S.C. § 1125(g).

[13] *See, e.g., In re Motors Liquidation Corp.* (*f/k/a General Motors Corp.*), 09-50026 (Bankr. S.D.N.Y. 2009); *In re Old Carco* (*f/k/a Chrysler LLC*), 09-50002 (Bankr. S.D.N.Y. 2009); *In re Lehman Brothers Holdings Inc.*, 08-13555 (Bankr. S.D.N.Y. 2008).

[14] 11 U.S.C. § 363(b)(1).

[15] *See In re Lionel Corp.,* 722 F.2d 1063 (2d Cir. 1983); *In re Delaware & Hudson Ry. Co.,* 124 B.R. 169, 176 (D. Del. 1991).

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(1) Sound business reason exists for sale

(2) Sale price is fair and reasonable

(3) Adequate and reasonable notice

(4) Good faith (*e.g.,* no collusive bidding)

(5) Debtor must seek the "highest or best" offer

c) Cannot constitute *sub rosa* plan[16]

(1) Court will <u>not</u> approve a sale or sale process that dictates the substance of a debtor's restructuring plan or constitutes a *de facto* plan[17]

(2) Sale process should not circumvent creditor protections embodied in plan confirmation requirements[18] (*e.g.,* good faith, equal treatment, best interests, feasibility)

5. Benefits of prepaks, prenegotiated plans and section 363 sales

a) Speed – can be as little as 30 to 60 days

b) Lower cost

c) Certainty

d) Full panoply of conventional bankruptcy protections

e) Ability to bind dissenting classes

B. Overview of Chapter 11 Plan Confirmation Requirements.

The Bankruptcy Code imposes minimal requirements for confirmation that apply to all chapter 11 plans, whether they arise in prepackaged, prenegotiated or conventional chapter 11 cases.

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16 *See In re Braniff Airways,* 700 F.2d 935, 949 (5th Cir. 1983).

17 *Id.*

18 *Id.*; *see* 11 U.S.C. § 1129.

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1. Plan acceptance

a) Creditors: acceptance by creditors holding at least two- thirds in amount and more than one-half in number that cast votes[19]

b) Shareholders: acceptance by shareholders holding at least two-thirds in amount of allowed interests that cast votes[20]

c) Unimpaired classes are conclusively deemed to accept the plan and no solicitation is required[21]

d) Classes of claims or interests that do not receive or retain property under the plan on account of such claim or interest are deemed to reject plan and no solicitation is required[22]

2. Consensual confirmation vs. "cram-down." A debtor can confirm a plan consensually, or over the classes of creditors that reject the debtor's plan, if certain conditions are satisfied.

a) Consensual: plan accepted by each class of impaired creditors and interest holders, and section 1129 otherwise satisfied

b) Cram-down: plan can be confirmed over impaired, rejecting class if plan does not discriminate unfairly and is fair and equitable (absolute priority rule) with respect to each dissenting, impaired class[23]

3. "Best Interests" test – any chapter 11 plan must meet this standard

a) Holders of impaired claims or interests who do not vote to accept the plan must "receive or retain under the plan on account of such claim or interest property of a value, as of the effective date of the plan, that is not less than the amount that such holder would so receive or retain if the debtor were liquidated under chapter 7 [of the Bankruptcy Code] . . . on such date."[24]

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19 11 U.S.C. § 1126(c).

20 11 U.S.C. § 1126(d).

21 11 U.S.C. § 1126(f).

22 11 U.S.C. § 1126(g).

23 11 U.S.C. § 1129(b)(1).

24 11 U.S.C. § 1129(a)(7)(A).

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b) Test focuses on individual creditors, not classes[25]

c) Requires evidentiary showing and typically, expert testimony demonstrating a hypothetical chapter 7 liquidation as of the effective date of the plan[26]

4. Absolute Priority Rule and "cram down"

a) Plan must be "fair and equitable"[27] – requires that a plan must provide either that an impaired non-accepting class of creditors be paid in full with respect to their claims, or that no interest junior to that class of creditors receive any distribution under the plan with respect to the junior claimants' prepetition claims or interests.[28]

b) Plan cannot "discriminate unfairly"[29] – requires in general that a dissenting class will receive relative value equal to the value given to all other similarly situated classes (*e.g.,* a plan may not segregate two similar claims or groups of claims into separate classes and provide disparate treatment for those classes).[30]

5. A chapter 11 plan must be feasible

a) Plan can only be confirmed if it "is not likely to be followed by the liquidation, or the need for further reorganization, of the debtor or any successor to the debtor under the plan, unless such liquidation or reorganization is proposed in the plan."[31]

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25 *E.g., In re Am. Family Enterprises*, 256 B.R. 377, 403 (D.N.J. 2000); *In re Stone & Webster, Inc.*, 286 B.R. 532, 544-45 (Bankr. D. Del. 2002); *In re Toy & Sports Warehouse, Inc.*, 37 B.R. 141, 150 (Bankr. S.D.N.Y. 1984)

26 *E.g., In re Adelphia Commc'ns Corp.*, 368 B.R. 140, 252 (Bankr. S.D.N.Y. 2007).

27 11 U.S.C. § 1129(b)(2).

28 *E.g., Toy & Sports Warehouse,* 37 B.R. at 152.

29 11 U.S.C. § 1129(b)(1).

30 *See, e.g., In re Johns-Manville Corp.*, 68 B.R. 618, 636 (Bankr. S.D.N.Y. 1986); Kenneth N. Klee, *All You Ever Wanted to Know About Cram Down Under the New Bankruptcy Code*, 53 AM. BANKR. L.J. 133, 142 (1979).

31 11 U.S.C. § 1129(a)(11).

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b) Requires evidentiary showing, typically through reasonable projections demonstrating sufficient cash flow to fund plan and maintain operations[32]

6. Dish Network Corp. v. DBSD North Am. Inc. (In re DBSD North Am. Inc.), 634 F.3d 279 (2d Cir. 2011)

a) Rejects "gifting" plans

b) Creditors should be mindful that actions taken during bankruptcy could result in designation of their plan votes

C. Breadth of Relief: who needs to file within the corporate group?

In addition to identifying the type of bankruptcy relief a company needs, the company must also consider which entities within its corporate group will benefit from judicial protection, and the scope of protection such entities require. A company may not need – or want – to file every entity in its corporate group. Moreover, some legal entities are restricted from filing, or would impose structural challenges to plan confirmation. In some instances, the company may have little practical choice in the matter. Factors that influence whether any particular entity should file for bankruptcy protection include:

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[32] *E.g., F.H. Partners* v. *Inv. Co. of the Southwest, Inc.* (*In re Inv. Co. of the Southwest, Inc.*), 341 B.R. 298 (10th Cir. B.A.P. 2006).

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1. Is the entity a guarantor of an obligation that needs restructuring? [33]

2. Does the entity require protection in connection with cross-defaults under contractual obligations triggered by participation of related entities in the bankruptcy filing (financial and operational, *e.g.,* leases)?[34]

3. Does the entity need financing or is it necessary to provide financing for the corporate enterprise?[35]

a) Participation in centralized cash management systems

b) Ownership of unencumbered assets

c) Impact of related entity filings on operations, revenue and ability to obtain financing for independent operations

4. Are there any restrictions on the entity to prevent its filing? (*e.g.,* bankruptcy remote entities)

D. Chapter 11 versus Chapter 15: ancillary versus plenary proceedings

A multinational enterprise faces the additional question of what type of bankruptcy proceeding, in which jurisdiction, best serves its objectives. The Bankruptcy Code offers plenary restructuring relief through chapter 11. It also provides ancillary relief in aid of foreign insolvencies through chapter 15. Towards that end, chapter 15 offers a portal through which the representative of a foreign estate can avail itself of certain bankruptcy protections, including the automatic stay. Chapter 11 and chapter 15 relief are not coextensive, however. Given the meaningful differences between the relief each chapter provides, a multinational enterprise must understand the interplay between the statutory protections, and how they would impact the company's restructuring potential. The same analysis applies in foreign jurisdictions.

1. Chapter 15 versus Chapter 11

a) Scope of stay

(1) Chapter 11: automatic upon filing petition and has extraterritorial reach[36]

(2) Chapter 15: not automatic and limited in geographical scope (to assets located in the territorial jurisdiction of the

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33 *See* COLLIER, BUSINESS WORKOUT GUIDE, (Mathew Bender 2009) P.6.05.

34 *Id.*

35 *Id.*

36 11 U.S.C. § 362.

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U.S.);[37] immediate relief requires an application for preliminary injunction

b) Availability of debtor-in-possession financing ("DIP Financing")

(1) Chapter 11: governed by section 364 of the Bankruptcy Code and includes significant creditor protections (*e.g.*, priming liens and adequate protection); case law is well developed[38]

(2) Chapter 15: not expressly contemplated and applicability of chapter 11 DIP Financing protections remains untested and is questionable

c) Ability to use other statutory provisions in a chapter 15 proceeding?

(1) Section 363 sales

(2) Avoidance actions

[37] 11 U.S.C. §§ 1519, 1520, 1521; *see In re JSC BTA Bank*, 434 B.R. 334 (Bankr. S.D.N.Y. 2010).

[38] 11 U.S.C. § 364.

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d) Can Chapter 15 relief exceed that available in Chapter 11? U.S. bankruptcy courts have enforced relief in the U.S. under foreign law that otherwise would not be available under chapter 11[39]

2. Non-statutory injunctions protecting foreign non-debtors also exist

a) Courts have statutory authority to issue injunctive relief under the Bankruptcy Code and title 28 of the U.S. Code[40]

b) Courts have applied injunctive relief to nondebtors where an "identity with the debtor" exists (*e.g.*, officers and directors, controlling shareholders, indemnifications by the debtor); *In re Lyondell Chem. Co.*, 402 B.R. 571 (Bankr. S.D.N.Y. 2009); *In re Truvo USA LLC,* Ch. 11 Case No. 10-13513 (Bankr. S.D.N.Y. 2010) (Gonzalez, J.); *In re Canwest Global Commncs Corp.*, Ch. 15 Case No. 09-15994 (Bankr. S.D.N.Y. Nov. 3, 2009)

(1) The *Lyondell* and *Truvo* injunctions protected non-U.S., non-debtor affiliates from creditor actions on a temporary basis

(2) However, there are practical concerns with this type relief and injunctions may not be recognized by foreign courts or may be ignored by foreign-based creditors beyond the reach of U.S. courts

3. Other considerations informing the use of Chapter 15 versus Chapter 11

a) Type of company

(1) Corporate group versus discrete legal entities[41]

(2) Location of assets and operations

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[39] *See, e.g., In re Metcalf & Mansfield Alt. Invs.*, 421 B.R. 685 (Bankr. S.D.N.Y. 2010); *In re Ephedra Prods. Liability Litigation,* 349 B.R. 333 (S.D.N.Y. 2006).

[40] 11 U.S.C. §§ 105, 362; *see also* 28 U.S.C. § 157(c).

[41] Even where methods exist to centralize the administration of insolvent companies between nations, barriers exist when legal regimes fail to adequately address the insolvency of corporate groups. *See* Alesia Ramney-Marinelli, *Overview of Chapter 15 Ancillary and Other Cross-Border Cases*, 82 Am. Bankr. L.J. 269, 29-93 (Spring 2008) (discussing challenges of insolvencies affecting affiliated corporate groups operating under European insolvency regulations).

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(3) Nature of commercial enterprise (finance, manufacturing etc.)

b) Nature and scope of restructuring

(1) Prepackaged bankruptcy / expedited process

(2) Immediate action versus longer term restructuring

(3) Asset preservation / divestiture and recovery

(4) Necessity of coordinated global proceedings

c) Stakeholder preferences and expectations

(1) Lenders (pre and post-petition)

(2) Other Creditors (suppliers, customers, etc.)

(3) Government

(4) Shareholders

III. Where to File: defining the cross-border filing blue print

A. Anticipating issues arising from filing full-blown court proceedings in U.S. and foreign jurisdictions: how to manage co-equal cases

Filing full-blown co-equal bankruptcy proceedings for the same legal entities in two or more jurisdictions raises numerous logistical and technical challenges for a company. It also dramatically increases the cost and complexity of its restructuring. The application of any country's insolvency law will vary from case to case. Filing blueprints take many forms: an ancillary case in one jurisdiction focused exclusively upon asset protection located in that jurisdiction; a plenary case in one jurisdiction with ancillary cases in other jurisdictions; a plenary case in one jurisdiction with a parallel plenary case in another jurisdiction; and a plenary case in one jurisdiction with out-of-court or informal work-outs in another jurisdiction.[42]

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[42] *See, e.g.,* Mike Sigal et al., *The Law and Practice of International Insolvencies, Including a Draft Cross-Border Insolvency Concordat*, 1994 ANN. SURV. OF BANKR. LAW 1 (1994)

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1. Conflicts of law and comity: which law applies?[43]

a) Judicial sovereignty

b) Use of cross-border protocols

c) Extra-territorial reach of judicial actions and legislation: to what extent will one country's judgments and insolvency legislation affect assets and actions in another country?[44]

d) Consider both "inbound" (*e.g.,* where a foreign insolvency representative comes to the U.S. seeking judicial relief) and "outbound" relief (*e.g.,* where a U.S. debtor seeks relief in a foreign jurisdiction)[45]

e) Reciprocity[46]

f) Other doctrines or legal limits may exist that impact the relief available in any given nation (*e.g.,* the act-of-state doctrine, forum non conveniens, etc.)

2. Equally applicable statutory schemes may generate substantive conflicts that need to be resolved, for example:

a) Cross-border claims resolution

(1) Priorities

(2) Regulatory schemes (environmental, pension, labor, etc.)

(3) Customer and trade expectations (*e.g.*, 20-day goods)[47]

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[43] *See, e.g., id.*

[44] *Id.* (discussing jurisdictional conflict in the insolvency of Maruko, Inc. between U.S. and Japanese bankruptcy courts where the Japanese court's jurisdiction was limited to assets located in Japan, while U.S. court had global jurisdiction over assets.)

[45] *Id.*

[46] *E.g.,* Charles Booth, *Drafting Bankruptcy Laws in Socialist Market Economies: Recent Developments in China and Vietnam*, 18 COLUM. J. ASIAN L. 93, 142 (2004) (discussing reciprocity requirement in draft Chinese insolvency law).

[47] *See* 11 U.S.C. § 503(b)(9).

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(4) Establishing bar dates and claims protocols

(5) Different legal regimes apply to allowance and adjudication of disputed claims

(6) Coordinating creditor recoveries in multiple proceedings[48]

b) Asset sales and effectiveness of sale orders

c) Solicitation, voting, and disclosure requirements for restructuring plan

d) Plan confirmation requirements

e) Available avoidance actions and differing standards

3. The nature of the governing restructuring regime affects options and impacts stakeholder actions – restructurings in some countries are done outside formal legal proceedings or under materially different forms of court-supervision[49]

a) debtor-in-possession

b) receivor / liquidation

c) administrator

d) other judicial officer (*e.g.*, monitor)

4. Differing legal frameworks impact timing and process. A country's bankruptcy system will reflect unique cultural and economic philosophies. Thus, even countries sharing similar legal frameworks (*e.g.*, common law jurisdictions) will have insolvency regimes with marked differences in philosophy and practice. Many non-U.S. bankruptcy laws historically were punitive towards debtors, viewing bankruptcy as a moral and personal failure. Even modern regimes retain punitive elements that reject the "fresh start" philosophy of U.S. practice, and foreign countries remain skeptical of

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48 *See, e.g.,* 11 U.S.C. § 1532 (establishing a rule of payment for creditors in concurrent proceedings).

49 *See, e.g.,* Ziad Raymond Azar, *Bankruptcy Policy: A Review and Critique of Bankruptcy Statutes and Practices in Fifty Countries Worldwide*, 16 CARDOZO J. INT'L & COMP. L. 279 (2008); Bartner*, supra* note 1.

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the U.S. "rescue culture" and "debtor-in-possession" model, often favoring more creditor-driven "liquidation cultures."[50]

a) U.S. adversarial system creates hold-up potential[51]

(1) Zealous advocacy and individual enforcement of rights

(2) Litigious and emphasizes due process

(3) Drawn-out proceedings and use of judicial process for hold-up value may increase cost and subvert restructuring goals for the benefit of individual creditors

b) Pragmatic approach common in non-U.S. jurisdictions may provide less predictability

(1) Greater reliance on judicial action and oversight[52]

(2) More summary proceedings may be viewed as providing fewer individual protections for the benefit of the group

(3) May be less costly than U.S. proceeding, however, use of administrative officials may render the process more bureaucratic; moreover, reliance on administrative officials with limited commercial experience or "skin in the game" may materially extend duration of the case and delay distributions

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[50] Martin, *supra* note 2 at 369-75; *see also* Paolo Manganelli, *The Evolution of the Italian and U.S. Bankruptcy Systems: A Comparative Analysis*, 5 L. BUS. & TECH. L 237, 237 (2010) ("Until the late 20th century, Italian bankruptcy law remained primarily a punitive system, designed to punish a delinquent debtor rather than facilitate its rehabilitation or reorganization.")

[51] *See, e.g.,* Harner, *supra* note 3.

[52] Ziad, *supra* note 48, at 370-71 (analyzing the court's role and creditor participation in various insolvency regimes and suggesting that creditors, not judges, are better positioned to make decisions whether a debtor's going concern is higher than its liquidation value); Sigal, *supra* note 41 (noting that the Canadian "CCAA is an example of a judge-made reorganizational system which is almost entirely driven by court discretion.")

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c) More consensually-driven processes may conflict with structured statutory frameworks like the U.S. Bankruptcy Code. Consider:

(1) U.S. Bankruptcy Code and Rules are prescriptive and rest on well-developed body of case law

(a) Provides certainty and predictability

(b) Arguably lacks flexibility and proves more costly

(2) CCAA statute shorter and relies on greater judicial interpretation[53]

(a) More flexible

(b) Less certainty

(c) Lack of predictability illustrated by recent decision from Court of Appeal for Ontario, granting pension claims priority over DIP Lender liens. Indalex Limited (Re), 2011 ONCA 265

(3) "London Approach" and administration under U.K. law[54]

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53 Sigal, *supra* note 41 (noting that "while Chapter 11 has detailed procedures and rules which are applicable to all reorganizations, CCAA reorganizations proceed in an ad hoc fashion and the rules are made up as the reorganization proceeds.")

54 Harner, *supra* note 2, at 766 (discussing "London Approach").

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(a) Stakeholders attempt to effect restructuring solution without resort to formal proceedings[55]

(b) Follow the "London Approach" code of conduct based on informally enforced understandings

(c) Formal administration – management replaced

d) Other countries are increasingly adopting aspects of U.S. chapter 11 reorganization proceedings in addition to liquidations, but each jurisdiction varies meaningfully in terms of statute and practice and across geographic regions; generally, no wholesale adoption of U.S. chapter 11 exists[56]

e) Nascent bankruptcy statutes, or piecemeal insolvency legislation, may exist in some countries that increase complexity, prove unpredictable, and complicate efforts to coordinate global proceedings[57]

5. Director and officer liability in bankruptcy. Different theories exist with respect to management displacement in bankruptcy. As well, in some countries, directors and officers may face personal and sometimes criminal liability for actions taken while the company operates during insolvency.[58] The degree of retained management control, and executive liability while in the "zone of insolvency," greatly impacts negotiating dynamics and the willingness to enter into certain restructuring transactions.

a) Management displacement may include (i) complete replacement, (ii) keeping management in place but with diminished powers and under court supervision, (iii) subjecting management to

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[55] *Id.* at 753 (noting that an "out-of court debt-for-equity exchange generally is not an option for large public companies in the United States. In the United Kingdom, on the other hand, a public company such as Jarvis may accomplish a complex debt-for-equity exchange with little or no substantive court involvement.")

[56] *See, e.g.,* Manganelli, *supra* note 49; Adrian Doble, *Restructuring Opportunities and Challenges in Central and Eastern Europe*, 25-SEP AM. BANKR. INST. J. 32 (2006); Charles Booth, *Drafting Bankruptcy Laws in Socialist Market Economies: Recent Developments in China and Vietnam*, 18 COLUM. J. ASIAN L. 93 (2004).

[57] Booth, *supra* note 52.

[58] Manganelli, *supra* note 49.

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creditors' confidence vote, and (iv) debtor-in-possession as default in the absence of fraud[59]

b) Directors' and officers' liabilities may vary materially between jurisdictions, with some countries rendering directors and officers civilly and criminally liable for transactions executed while the company is in the insolvency zone[60]

6. Financing the cross-border restructuring: a company's ability to finance its reorganization will drive any successful cross-border restructuring. Managing liquidity and financing operations while paying professional fees and developing a restructuring plan often present some of the company's greatest challenges when operating under court supervision in co-equal cases spanning multiple jurisdictions. The following must be considered:

a) Cash management (closed cash systems; value leakage) and importance of intercompany cash flows and allocation of expenses in funding foreign affiliates

(1) SGA

(2) Intercompany debt

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59 Azar, *supra* note 48, at 291-92.

60 Manganelli, *supra* note 49, at 244 (noting that directors of a bankrupt company under Italian law may be held criminally liable if it is shown they executed a high-risk transaction during the pre-insolvency period).

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b) Foreign currency exchange rate effects

c) Lender preferences

7. Developing a cross-border restructuring plan: a cross-border case will often involve coordinated restructuring plans across jurisdictions – conceived as interdependent documents that, together, effectuate a comprehensive restructuring of the company. Achieving this result requires careful consideration of:

a) Cross-border enterprise valuation (governing law; asset creation and valuation; ownership; etc.)

b) Defining and organizing corporate groups

c) Availability of substantive consolidation

d) Subordination of claims (statutory; contractual)

e) Availability of avoidance causes of action

f) Plan consideration and distribution

g) Preserving and maximizing tax attributes

h) Involvement of different sovereigns and national interests[61]

8. Different statutory fiduciaries and stakeholders may exist in different legal regimes and have conflicting roles

a) Existing management as "debtor in possession" not universally accepted concept

b) Statutory creditors committee

c) U.S. trustee

d) Foreign statutory actors (monitor, liquidator, administrator)

e) Ad hoc committees

f) Examiners and statutory trustees to displace management

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[61] Consider, for example, how national interests affected restructuring proceedings in the following cases: the U.S. Treasury's role as lender in the restructuring of General Motors, the F.D.I.C.'s role as receiver in the sale of Washington Mutual's assets, the liquidation proceedings of Lehman Brothers Inc. under SIPA and the role of the Securities Investor Protection Corp., and the Quebec government's role in financing Abitibi-Consolidated Inc.

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9. Multiple filings exponentially increase restructuring costs and may extend the duration of the cases

a) Engagement of multiple professionals (legal, financial, other)

b) Entails multiple judicial proceedings that may prove duplicative (*e.g.*, plan confirmation, asset sale hearings, etc.)

c) Multiple professionals may extend the length of time a company remains in bankruptcy[62]

10. If the company files in multiple jurisdictions, including under the Bankruptcy Code, can it get out of the U.S. case?

a) Conversion (chapter 15 to chapter 11 or chapter 7)

b) Dismissal (chapter 15 or chapter 11 to nonbankruptcy law)

B. Jurisdiction and Venue: who may file and where?

Identifying the appropriate jurisdiction and venue in which to file bankruptcy within any given country presents a final consideration for distressed companies about to file formal proceedings. Considerations include statutory requirements for eligibility (that is, *who* can be a debtor?) as well as limits on venue (that is, *where* can you file?)

1. Threshold considerations: statutory requirements must be satisfied. In general, no uniform global system exists that allows a company to select a lead jurisdiction for reorganizing a multinational corporate group.[63]

a) Eligibility requirements: who can be a debtor?[64]

(1) Corporations

(2) Partnerships

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[62] Martin J. Whitman and Fernando Diz, DISTRESS INVESTING: PRINCIPLES AND TECHNIQUE, 66 - 68 (Wiley Finance 2009). Notably, a study of recent U.S. chapter 11 cases concluded that the number of professional firms retained by the various parties in the case proved the only statistically meaningful factor associated with the duration and cost of the chapter 11 case. *Id.* Neither the size of the company nor the complexity of its capital structure effected the duration and cost of the chapter 11 cases in the study to the same extent as the number of law firms and financial advisers engaged by the parties. *Id.*

[63] Bartner*, supra* note 1, at 733.

[64] 11 U.S.C. § 109.

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(3) Limited liability companies

(4) Other business organizations

(5) Some entities not eligible to file (banks, insurance companies)

b) Venue requirements: where can you file?

(1) In the U.S., a corporation can file under chapter 7 or chapter 11 generally in any jurisdiction containing its domicile, residence, principal place of business or principal assets, or in which there is a pending case under title 11 concerning an affiliate of the corporation[65]

(2) In the U.S., a chapter 15 case may be commenced in the district (a) in which the debtor has its principal place of business or principal assets in the United States; (b) if the debtor does not have a place of business or assets in the United States, in which there is pending against the debtor an action or proceeding in a Federal or State court; or (c) in a case other than those previously specified, in which venue will be consistent with the interests of justice and convenience of the parties, having regard to the relief sought by the foreign representative.[66]

2. Strategic considerations in determining where to file

a) Location of company's assets

b) Location of stakeholders (creditors, management, lenders, shareholders, employees etc.)

c) Availability of financing

d) Judicial experience and expertise managing large cases

e) Substantive differences between jurisdictions

(1) Available first day relief

(2) Local rule requirements

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65 28 U.S.C. § 1408.

66 28 U.S.C. § 1410.

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(3) Case precedent (*e.g.*, management incentive plans, critical vendor relief, majority / minority view on substantive issues[67])

(4) Availability of Releases

IV. Conclusion

The maximization of enterprise value and business preservation comprise core goals of any multinational enterprise restructuring. To maximize reorganization potential, a multinational enterprise and its investors must carefully analyze when, what and where to best pursue their reorganization objectives. This requires a detailed appreciation of the company's in-and out-of-court restructuring options, the restructuring method most appropriate for the company's legal and capital structure and reorganization needs across different legal regimes, an understanding of different filing options in different countries and how they may interact, the creation of a rational filing blueprint, and an understanding of restrictions on venue options.

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[67] *Compare, e.g., IUE-CWA* v. *Visteon Corp.* (*In re Visteon Corp.*), 612 F.3d 210 (3d Cir. 2010) (following minority view and holding that section 1114 requires payment of all retiree welfare benefits during pendency of case, regardless of whether applicable benefit plan permitted unilateral termination of benefits under nonbankruptcy law) *with LTV Steel Co.* v. *United Mine Workers* (*In re Chateauguay Corp.*), 945 F.2d 1205 (2d Cir. 1991) (nonbankruptcy law contractual termination provision enforced during chapter 11 case notwithstanding section 1114).

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