NORTON ROSE FULBRIGHT

International Restructuring Newswire

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

Q2/Q3 2020

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Attorney advertising.

To our clients and friends:

The COVID-19 pandemic has brought untold pain and suffering throughout the globe with no end in sight. Not only has it taken its toll in terms of deaths and illnesses but the economic impact has been severe. Unemployment has skyrocketed and businesses have been terribly affected, with shutdowns and loss of sales. The impact has been felt everywhere. The Organization for Economic Cooperation and Development warned in its recently issued report that the world economy is facing the most severe recession in a century and could experience a halting recovery. And, in a news conference I just watched today, the US Federal Reserve chair, Jerome Powell, warned that the depth of the downturn and the pace of the recovery remained "extraordinarily uncertain."

All of this suggests that restructuring and insolvency professionals should expect a very busy time in the days and months ahead. In this issue of the *International Restructuring Newswire*, we offer some analysis and guidance on developments in some of the various jurisdictions where Norton Rose Fulbright lawyers practice insolvency law. These articles focus on changes and developments that courts and practitioners are implementing to deal with the fallout from the pandemic.

In Australia, our lawyers review the voluntary administration process and how the courts are exercising their discretion to adapt the process to the COVID-19 pandemic. We also take a look in the UK on recent judicial developments in the law relating to restructuring through administration, with a particular focus on the government's Job Retention Scheme and recent relevant cases. The economic impact of the pandemic will be weighing heavily on global businesses. As such, we take a fresh look at recent developments relating to the recognition and enforcement of foreign insolvency proceedings. A number of recent court decisions have provided new guidance in this area of the law in the US and we separately review the European perspective on determining COMI, the key concept of center of main interests. In that regard, in this issue, we also comment on the first case out of Hong Kong granting recognition and assistance to bankruptcy administrators appointed in insolvency proceedings in mainland China. And in Canada, our lawyers review the recent amendments to the Companies' Creditors Arrangement Act, generally known as the CCAA.

We hope you all find this issue to be helpful as we all navigate through these difficult and turbulent times.

Stay safe,

Howard Seife
Global Head
Bankruptcy, Financial Restructuring and Insolvency

In the news

Montreal team successfully represents interveners in litigation funding case before the Supreme Court of Canada

On May 8, 2020 the Supreme Court of Canada released its reasons in 9354-9186 *Québec Inc. v. Callidus Capital Corp.*, 2020 SCC 10, where for the first time Canada's highest Court specifically dealt with and approved litigation funding agreements in the context of formal insolvency proceedings. Sylvain Rigaud, Arad Mojtahedi and Saam Pousht-Mashhad from our Montreal office represented the Insolvency Institute of Canada and the Canadian Association of Restructuring Professionals. Sylvain Rigaud commented this key ruling for the *American Lawyer.*

INSOL World

Radford Goodman, Alison Goldthorp and Mark Craggs's article "The Changing Nature of Insolvency Disputes" was recently published in the Q1 2020 edition of *INSOL World* (of which Mark Craggs is co-editor). There is a Younger Members Spotlight interview with Matt Thorn in the same edition.

The Lawyer (UK)

Matthew Thorn is featured in the June edition of *The Lawyer* as a part of their article titled "Forged in fire: the new partners of 2020."

State Bar of Texas (Bankruptcy Section)

April 29, 2020 – Dallas, Texas

Laura Smith participated in a webinar for the State Bar of Texas (Bankruptcy Section) – "Getting the Deal Done: Practical Considerations in Real Property Sales Under Section 363".

INSOL International – Webinar

May 5, 2020

Scott Atkins, INSOL Vice President, participated in a webinar discussing issues currently being faced in Australia and Singapore as a result of the COVID-19 pandemic. INSOL Fellows Ian Fox (Dentons) and Debby Lim (BlackOak) also participated in the program.

Aircraft Finance and Leasing: COVID-19 and Moratoria Webinar

May 21, 2020

Mark Craggs presented on a Norton Rose Fulbright webinar together with Alison Baxter and Kenneth Gray, on moratoria introduced in different jurisdictions in response to the COVID-19 crisis and their consequences for financial restructurings.

INSOL International – Focus on Aviation Webinar

June 16, 2020

Mark Craggs will be presenting on a webinar organised by INSOL International on cross-border restructurings in the aviation sector.

Non-Performing Loans & Regulatory Capital Webinar

June 17, 2020

Mark Craggs and Matt Thorn will be presenting on a webinar with members of the Financial Services team in London and guests from KPMG dealing with non-performing loans and their regulatory capital treatment. The webinar is the first in a series focusing on the legal and regulatory responses in different countries as they emerge from the COVID-19 lockdown and seek to resume normal business.

ABI Southeastern Conference

July 26, 2020 – Amelia Island, Florida

Jason Boland will participate on a panel at the 25th Annual ABI Southeastern Conference in the Ritz-Carlton, Amelia Island, on the topic of "Energy Restructuring: What's New in the Second Wave".

Voluntary administration and the evolving judicial approach to the reallocation of financial risk in the face of COVID-19

Laura Johns, Jonathon Turner, Tim Mornane and Shelley Merenda

Under Australian law, voluntary administration is intended to be a fast and efficient process to facilitate the restructuring, sale or, if necessary, liquidation of an insolvent company. The objective of the process is the maximisation of the chances of the company, or as much as possible of its business, continuing in existence or, if that is not possible, results in a better return to creditors and members than would be achieved by an immediate winding up of the company.

A key benefit of the Australian administration process is flexibility and the ability to reach a variety of outcomes. The process is controlled by an insolvency professional who, pursuant to the Corporations Act 2001 (Cth) ("Act"), is personally liable for the debts of the company that are incurred during its voluntary administration. This includes rents for leased property, which is used or retained after an initial period of five days from the commencement of the administration, referred to as the 'grace period.'

The burden of personal liability for insolvency professionals weighs heavy and where the assets of the company may be insufficient to meet future debts, the prospect of the company continuing to trade and avoiding liquidation may be adversely impacted. However, reflecting the flexibility of the process, the law responds by permitting voluntary administrators to seek relief from the Court in respect of any obligations that may apply in a voluntary administration (colloquially known as "447A orders").

These orders can both exclude or limit a voluntary administrator's personal liability for debts and also permit the deferral of rental payments. Such orders represent a material shift in the usual allocation of financial risk in a voluntary administration. They are potentially detrimental to landlords and lessors as debts owed to them increase, without the benefit of the usual priority that post-appointment debts, for which the administrator also is personally liable, would be afforded and without the ability to take other steps to recover their property due to the statutory moratorium. As a consequence, they have been historically rare.

However, the COVID-19 pandemic and the challenge it imposes on businesses and the economy as a whole is without doubt unprecedented. It has implications on a global scale. While legislative responses to this crisis have been well documented, it is becoming increasingly apparent that the Courts, across a multitude of jurisdictions, will also have an important role to play in seeking to ensure business survival.

We will explore approaches taken by Australian Courts in relieving administrators of personal liability for payment of rent and the deferral of rent. Further, we will consider whether these decisions demonstrate a willingness of the Courts to respond to the unique circumstances arising from COVID-19, by facilitating the external administration of companies in a way that is unprecedented with a focus on broader economic interests as well as the interests of creditors.

Relief against personal liability and deferral of rent

Section 447A of the Act affords the Courts the power to *"make any such order as it thinks appropriate about how this Part is to operate in relation to a particular company".*

In recent years, applications under this section generally have become a common feature of voluntary administrations as it affords the Court incredibly broad powers in relation to the assets and liabilities of an insolvent company. However, orders extending the grace period before administrators become personally liable for rent or other liabilities and consequent orders for the deferral of rent have been less commonly obtained.

Voluntary administration is intended to be a swift and efficient regime so to depart from the usual rule, the Court has to be satisfied that there is a good reason for the extension and that the extension will result in a better outcome for creditors as a whole.

The rationale for extending the initial grace period is generally that the administrators are unable to make a decision as to whether it was in the interests of the company to continue to use or occupy the leased property within the prescribed five-day period. This might be based on the size and complexity of the administration or some other practical obstacle to the administrators deciding to accept personal liability for the relevant leased property.

In agreeing to the deferment of rent or the relief of personal liability for rent, the Court has always had particular regard to the risk of potential prejudice to lessors and landlords. In particular, the potential for the outstanding liability owed to the landlords and lessors to materially increase in circumstances where recourse is limited to the insolvent entity, without assurance of payment in priority to any other creditors.

Increasing applications for relief

Pre-COVID-19, whilst applications for extensions of the initial grace period were not novel, there were less than a dozen written judgments in the last ten years. However, post-COVID-19, there have been four judgments in as many weeks and it must be expected that there will be many more to come.

What is clear from these four recent decisions is that the existing principles about whether a timely assessment of leased assets could reasonably be conducted by the administrators within the grace period and whether the extension was likely to assist with achieving the objectives of the voluntary administration continue to be of primary relevance.

However, in reaching its decision in *Eagle in the matter of Techfront Australia Pty Limited (administrators appointed)*, the Court acknowledged that it was apparent that public institutions such as the Court must do all they can to facilitate the continuation of the economy. The business in question operated in an industry that had been significantly adversely affected by government restrictions imposed due to COVID-19 and the Court had due regard to the difficulties faced by it.

This may reflect an interesting extension to the reasoning applied in pre-COVID cases where a key consideration was the ultimate benefit to creditors and stakeholders. It is arguable that the Courts will now also take into consideration not just public interest, but also specifically the benefit to the economy as a whole by ensuring business survival, notwithstanding the prejudice particular orders may cause to lessors and landlords in the short term.

The powers of the Court were again tested following the appointment of voluntary administrators to the Virgin Australia Airlines Group, which operates a passenger and cargo airline business domestically and internationally.

The administrators were granted a four-week extension of the grace period, in light of the size and complexity of the Virgin's affairs and extensive lease holdings, and delays caused by the restrictions imposed by State and Federal governments to control the spread of COVID-19.

In reaching its decision, the Court commented that:

> *"The COVID-19 pandemic is causing great disruption to the whole Australian community and the economy……the COVID-19 pandemic, and the consequent restrictions on the movement and behaviour of people, is a reason to apply flexibility in the application (and perhaps adaptation) of existing laws, and to exercise any discretion residing in a court to ensure that the Australian community and economy are supported during this time of crisis."*

And it is not just new voluntary administrations where assistance is needed

The COVID-19 circumstances have not only impacted new voluntary administrations but the broad and extensive disruption to normal service has led to issues arising in existing voluntary administrations which have required the assistance of the Court in relation to personal liability for rent and the deferment of rental payments.

In January 2020, the Colette Group, a midmarket fashion accessories retailer, appointed voluntary administrators. The administrators continued to trade the business, closing only around a quarter of the Australian stores.

The administrators initially met lease obligations after the expiry of the five-day grace period as they sought to sell or recapitalise the business. However, despite initial strong interest, by late March, all interested parties withdrew from the process, due primarily to the impact of COVID-19, as sales had suffered a significant decline and stores had closed.

The administrators found themselves in the unenviable position where they remained in possession of the remaining stores but could not trade, with a monthly rental liability in excess of A$1 million. The administrators approached the Court seeking relief and the extension of the grace period.

In a novel application of its powers, the Federal Court initially made orders excluding the personal liability of the administrators for an additional two-week period despite the grace period having long expired and the administrators having been paying rent.

The administrators were also excused from having to cause the company to pay rent during that period, giving the administrators comfort against a possible claim of unreasonable or improper conduct in the future. Subsequently, on the further application of the voluntary administrators, the period was extended by a further three weeks (on similar terms).

Noting the extraordinary circumstances caused by COVID-19, the Court accepted that the administrators' strategy of 'mothballing' the business

for two months was likely to lead to a better outcome for creditors as a whole than the immediate shut down of the business, particularly while the "*physical, legal and economic landscape*" continued to evolve.

The evidence before the Court indicated that the administrators had attempted to negotiate a rental reduction with landlords but these attempts had not resulted in a substantial rental saving and at that time, it was unclear what form any government intervention in respect of commercial lease liabilities would take, but it was unlikely to extend to a suspension of the administrators' personal liability.

The Court considered that the extension was in the best interests of creditors as a whole as it was unlikely that the lessors would be able to re-lease the premises for the extended period and there was no value to the lessors in the immediate shut down modelling performed by the administrators. The Court was satisfied that the orders preserved the prospect that a commercial outcome could later be achieved in the "mothballing" scenario.

Similar considerations arose in the hearing for a second extension. The Court accepted the administrators' evidence that the best prospect for maximising a return to creditors remained the 'mothballing' scenario to allow for a managed winding down or sale as opposed to the immediate shut down scenario. This was supported by evidence that there had been progress in the sale process in that original and new parties had come forward and expressed interest in acquiring the business.

In the Colette Group decisions, consistent with its usual approach, the Court assessed the applications with the objectives of voluntary administration in mind: would the order sought give rise to a prospect of a better return to creditors? However, there is a shift in the way that the Court has allowed applications of extensions of the grace period to be made in that the orders were made some weeks after the initial five-day grace period had expired, after the administrators had decided to continue the leases and after they had accepted personal liability for payments due under them.

It is not yet clear, whether and in what other situations the Court might be prepared to grant relief for liabilities already adopted by the voluntary administrator, as a consequence of the impact of COVID-19 on the business in voluntary administration. However, it would be reasonable to conclude that the Court's powers to grant relief are likely to be tested at this time.

Commercial Leasing Principles

Another as yet untested question relevant to the issue of liability for rental payments and the deferral of rental payments is how the various interim legislative changes for commercial leasing might impact the availability of relief and the ability of a landlord to be able to demonstrate sufficient prejudice.

Between the first and second applications in the Colette Group, the Australian National Cabinet (being a cabinet comprising the state and territory governments) had released the "Mandatory Code of Conduct – SME Commercial Leasing Principles During COVID-19" ("Code") and agreed that it would be legislated in each Australian state. As at the time of writing steps have been taken to enact the Code to some extent in all but one of the Australian states and territories.

While the specifics of how the Code is to be applied vary from state to state, the Code sets out guiding principles for consideration by landlords when dealing with eligible tenants. The overarching principles of the Code include the concept that landlords and tenants share a common interest to ensure business continuity.

Eligible tenants are those with an annual turnover of up to A$50 million who are experiencing financial distress or hardship as a consequence of COVID-19. The Code requires a landlord to provide rental relief to a qualifying tenant by the same proportion as the loss of revenue experienced by the tenant by way of rental waiver and deferral of rent. It also prevents landlords from terminating leases or calling on bank guarantees for unpaid rent.

While this was yet to be enacted by any Australian state and territory at the time of the second Colette Group decision, it was noted that the Code could impact the liability that could accrue as there may be a material difference in the rent payable under the leases and the rent payable under the Code but did not comment on how that might impact the orders it would be prepared to make.

The mandated package provides a significant level of protection for tenants and leaves landlords without much by way of immediate leverage (as they are precluded from calling on bank guarantees or terminating leases). However, it does not in itself relieve a voluntary administrator of personal liability for the balance of the rental payments that may still be due and other outgoings.

It remains to be seen precisely how the Courts will exercise its broad discretion to grant relief such as in the matters of Virgin and the Colette Group, where the company in question is eligible for the protection of the Code.

One has to expect that it will become increasingly difficult in this circumstance for landlords to argue that they have been prejudiced by a decision of the Court to relieve an administrator of personal liability or defer rental payments, if they are otherwise obliged to provide relief to tenants under the Code and are already sharing the pain to ensure business continuity.

What about other jurisdictions

It is not just in Australia where the Courts are attempting to provide practical assistance to insolvency professionals and companies in an insolvency process during the COVID-19 pandemic.

In the United States, certain retailers in chapter 11 cases have confronted similar issues. In *In Re Modell's Sporting Goods, Inc.*, the US Bankruptcy Court for the District of New Jersey suspended the chapter 11 cases of the company, a sporting goods retailer that was shutting down. The impact of the government's response to the COVID-19 pandemic meant that Modell's was unable to generate sufficient revenue to conduct an orderly going out of business and asset sale process. Emergency relief was granted under section 365(d)(3) of the US Bankruptcy Code, which permitted Modell to abate rent and other lease obligations for a period in excess of the statutory limit provided for under the Bankruptcy Code.

An article exploring a similar decision of the United Kingdom Court of Appeal also appears in this edition of Insolvency Newswire and provides an interesting comparison.

Conclusion

If the last two months provide any indication, it appears that the voluntary administration process and the powers of the Court under section 447A of the Act will be tested frequently and potentially beyond their existing limits.

Decisions made by administrators before the COVID-19 pandemic may need to be reassessed and the assistance of the Court sought to ensure the objectives of the voluntary administration process can be achieved. This may not only relate to decisions to accept personal liability for leased assets after the end of the grace period.

Landlords may find that it is increasingly difficult given the COVID-19 circumstances to demonstrate sufficient prejudice so as to avoid orders deferring rent and relieving personal liability being made. Administrators hold a strategically strong position in that if negotiations with landlords fail there remains an option of an application to the Court to ensure a better ultimate return to all creditors. However, landlords may find power in working together to agree protocols and regimes with the administrators or seeking a limited personal liability arrangement to ensure any rental payments enjoy priority to the extent there are available assets.

More broadly, post-COVID-19, stakeholders can expect the Court to have consideration as to how the exercise of its discretion will best ensure that the Australian community and economy are supported in these extraordinary times.

Laura Johns, Jonathon Turner and Tim Mornane are partners in our Sydney office and Shelley Merenda is special counsel in our Perth office in the firm's financial restructuring and insolvency group.

Recent judicial developments in the law relating to administration in the UK in the COVID-19 crisis as of May 2020

Alison Goldthorp

The COVID 19 crisis ("Crisis") has led to an unprecedented slowdown of business in the UK, as in the rest of the world, and to the announcement of extensive government support packages for businesses and individuals in the UK introduced at high speed to provide urgent support to businesses to avoid insolvencies on a large scale.

As businesses explore, apply for, and then evaluate the impact of the government funding packages available to them, the number of insolvency filings has actually fallen in the last couple of months. An increased number of formal insolvencies are expected as the lock down in the UK eases and as businesses have difficulties in funding the re-start of operations.

There have been several judicial decisions in the last month relating to the interaction of the government schemes and the UK insolvency processes. These decisions evidence the desire of the judiciary to support the efforts of the government to save businesses and jobs as part of the rescue culture, evidenced by the speedy manner in which the judiciary has dealt with the hearing of the applications and the handing down of decisions to the applicants, given the urgency of the situation.

At the same time the government has introduced a bill setting out new insolvency legislation including two new restructuring procedures: first the ability for directors to apply for a standalone moratorium in order to facilitate the rescue of the business. This would allow the company to continue to trade under the supervision of a monitor (who needs to be a qualified insolvency practitioner) for an initial period of 20 business days which can be extended for a further 20 days, and with court/creditor approval for up to a year. A new reorganisation plan is also to be introduced similar to the existing Scheme of Arrangement but with the ability to cram down dissenting classes of creditors if approved by the court. There is also a prohibition on serving statutory demands and the making of winding up orders for businesses affected by the Crisis until 30 June 2020 or 30 days from the coming into force of the new legislation. These measures are expected to become law very quickly in July 2020 to assist with the rescue of businesses in the Crisis.

Government Job Retention Scheme (JRS)

The JRS was introduced by the government as a temporary scheme to support businesses whose operations have been severely affected by the Crisis and to prevent mass redundancies in light of the Crisis. It allows businesses affected by the Crisis to furlough employees for periods of at least 21 days, and to apply for a payment of 80 percent of an employee's "reference pay" up to a maximum payment of £2,500 per month for the furlough period, on the basis that the employer agrees that he will not make the employee redundant during that period.

Guidance on the operation of the JRS was first issued by the government on 26 March 2020 and has been revised on many subsequent occasions ("Guidance").

In addition the HMRC issued a Directive on 15 April 2020 ("Directive") which sets out the operational mechanics of the JRS. Frustratingly, the Directive contradicted the Guidance in a number of ways, although the ongoing revisions of the Guidance have since dealt with many of these issues, in particular as regards whether the employee needs to consent to the furlough, and the treatment of holiday pay and sick pay. It is necessary to continually review the revisions to the Guidance to understand the way in which the JRS is evolving.

In terms of consent to the furlough, the Guidance is now that formal consent is not required but the confirmation of furlough needs to be in written form, for example by e mail from the employer. Employees can take holiday when furloughed, but holiday pay is at pre-furlough entitlement under their contract of employment, so an Administrator would need to top up the payment unless the terms of employment were varied by consent. As regards sick pay, the Guidance now states that the employer cannot claim statutory sick pay and under the JRS at the same time.

The JRS was originally available for a three month period from 1 March 2020. It was then extended for a further month to 30 June 2020 and then to October 2020, in light of the phased exit from lockdown. The extensions are to support businesses which are initially unable to operate fully or at all in the initial phases of the relaxation of the lock down process. The government has said that businesses will need to contribute to the cost of the scheme from August 2020 onwards and draft proposals setting out how this will work will be published shortly. This is likely to result in the need for employers to enter into restructuring discussions or a restructuring or insolvency process if they are unable to pay the required contributions.

The Guidance says that the JRS is available to Administrators and says:

> "*We would expect the administrator only to access the scheme if there is a reasonable likelihood of rehiring the workers. For instance, this could be as a result of an administration and pursuit of a sale of the business*"

The Guidance does not specifically mention the use of the JRS in other insolvency procedures such as liquidation, company voluntary arrangements, and bankruptcy. Given the comments regarding the access to be on the basis that there needs to be a "*reasonable likelihood of rehiring"* the employee, it would not be available in insolvency procedures where the business is likely to be closed down. Businesses are sometimes continued by a provisional liquidator or a liquidator in a compulsory liquidation, or by the supervisor of a company voluntary arrangement or CVA, so it may be that they would be able to make a successful application to the JRS on the basis that their role is analogous to an administrator seeking to sell or save a business, but that would depend on whether there was a reasonably likelihood of a further period of ongoing trading in the future involving the furloughed employee.

How does an Administrator deal with furloughed employees and the JRS?

The question of the application of the JRS in administration has been considered in two recent cases involving the administration of the restaurant chain Carluccio's and the retailer Debenhams.

In the Carluccio's case, the Administrators were appointed prior to the furloughing of any employees. The Administrators made an application to court for directions regarding the application of the JRS and the furlough process. Judgment was handed down by the Honourable Mr Justice Snowden on 13 April 2020[1].

The position in Debenhams was different as the employees were already on furlough at the time of the appointment of the Administrators. The Administrators applied for directions regarding the application of monies received from the government in relation to the JRS, and regarding a number of other matters including whether the contacts of employment of the employees on furlough were adopted by the Administrators. Judgement was handed down by the Honourable Mr Justice Trower on 17 April 2020[2]. The decision was then appealed, and the decision of the Court of Appeal was handed down on 6 May 2020 with judgement being given by Lord Justice David Richards.

Adoption of employment contracts in administration

In both the Carluccio's case and the Debenhams Case the key issue before the court was whether the Administrators would be considered to have adopted the contract of employment of the employee if an application to the JRS was made and/or a payment was made to the employee of monies received by the company as a grant under the JRS during the administration. This was important in light of the fact that if the contract of employment was adopted, the payment under the JRS would be of 80 percent of the employees "reference pay" up to a cap of £2,500 a month, leaving 20 percent of that "reference pay" and any additional amounts payable in excess of the cap, unpaid, with those amounts being a potential super priority claims in the administration in accordance with Paragraph 99 of Schedule B1 Insolvency Act 1986, unless the employee agreed to a variation of their contract of employment. As a result, in both cases, the Administrators sought the agreement of the employee to limit any payments accruing in the administration in the furlough period under the contract of employment to any amount paid by the government under the JRS by way of a grant to the company in administration.

In both cases the Administrators argued that if the employment contracts were found to be adopted, any potential exposure of the company in administration to make further payments in addition to the amounts received from the JRS, was likely to lead to a decision to make more employees redundant, thus undermining the rescue culture.

The leading decision in which the legal issues relating to the adoption of contracts of employment were considered in detail by the Court of Appeal and the House of Lords is the case of *Powdrill v Watson: Re Paramount Airways No 3 1994*[3]. The Court of Appeal found that the Administrators had adopted the contracts of employment as a result of their conduct. They could not limit their liability by sending letters to the employees and could not pick and choose the liabilities that they would be responsible for paying as super priority claims during the administration period. The company in administration was therefore required to pay all amounts accruing under the employment contracts since the appointment of the Administrators. This decision was seriously damaging to the use of administration as a rescue procedure, and immediate changes to insolvency law were introduced to limit the categories of payments under the employment contract which would attract super priority. Adoption requires some conduct by the Administrators, which amounts to an election to treat the

1 **In the matter of Carluccio's Limited (in administration) 2020 EWHC 886 (Ch).**

2 **In the matter of Debenhams Retail Limited (in administration) 2020 EWHC 921 (Ch).**

3 **Powdrill v Watson (Paramount Airways Limited) 1995 2AC 394**

contract of employment with the company as giving rise to a separate liability in the administration. Importantly, adoption does not amount to assumption of personal liability by the Administrators.

Following the Paramount case and the consideration of similar issues arising in administrative receiverships, the insolvency legislation was amended by the introduction of Section 19(5) Insolvency Act 1986 which is now Paragraph 99(5) Schedule B1. This provides that Administrators have 14 days to decide whether or not to adopt a contact of employment and their conduct in that period cannot amount to adoption. Following the expiry of the 14 day period, if the contract is adopted, amounts in respect of holiday pay, sick pay, contribution to pension schemes and wages under the contract are payable during the period of employment in the administration. Other claims under the employment contract are preferential claims, for example for arrears of wages or holiday pay, and claims for notice and redundancy pay are unsecured claims. The decision was upheld by the Honourable Mr Justice Laddie in *Re Antal International Limited 2003*[4] where the Judge found that conduct is required to amount to an election to treat the contracts of employment as continuing even after the 14 day period has expired, so there is no automatic adoption on the 15th day if the employee is not made redundant.

The Carluccio's case

Carluccio's went into administration on 30 March 2020, and at that time no employees had been furloughed. The company operated 70 restaurants across the UK and had around 2000 employees. The Administrators had decided on their appointment to "mothball" the business during the lockdown period and at the same time seek to sell the business to achieve purpose (b) in Paragraph 3(1) Schedule B1 Insolvency Act, and received expressions of interest in the business. The Administrators sought various directions on the consequences for them as Administrators if they were to make applications under the JRS in relation to the employees of the company. Directions were given by the Honourable Mr Justice Snowden on 13 April 2020.

At the time of the application the Guidance had been published (it has since been revised a number of times), but the Directive was not in place. The application was unopposed and in the time available there was no time to join a representative employee, but some submissions were made in writing by Counsel instructed by one of the unions representing some of the employees.

The Administrators sought a direction that they would not be adopting the contracts of employments of the employees by making the application to the JRS, and the payments to the employees under the JRS. A key submission made to the court was that there was no adoption as no services were being provided by the employees to the company whilst on furlough, so the facts were very different to the Paramount case, where services were provided to the company in administration.

4 Re Antal International Limited [2003]2 BCLC 406

The Administrators also asked for directions regarding the mechanism for making payments to the employees in accordance with the provisions of the Insolvency Act and Rules.

The Administrators had sent letters to the employees following their appointment, informing them that they were to be put on furlough and asking them to agree to a variation of their terms of employment to accept "*such portion of your regular wages with the grant [from the JRS] will cover*" as their contractual entitlement for the period of the furlough leave. The letter also made clear that the company would only be able to pay the employees when it got the grant from the government, and that if the employee did not consent to the variation within a short period of time, the Administrators would need to consider making the employee redundant.

As a matter of employment law, the employee needs to agree such a variation to their terms of employment, and absent such agreement, the company in administration had a potential exposure to pay the balance of the entitlements under the contracts of employment which were not covered by a grant from the JRS, to the employees as super priority claims in the administration. Further, if there was no consent from an employee to any variation to the terms of his employment to reduce wages, then this would be an unlawful deduction under the Employment Rights Act 1986. Subsequent consent by the employee cannot alter the position in relation to deductions from wages made prior to the consent being given.

The Judge referred to the analysis of adoption by Lord Brown Wilkinson in the Paramount case. He considered whether the fact that no services were being provided by the employees during the furlough period meant that Paragraph 99(5) could not apply. He commented that the employees were still available for work and would return to work in the event that a buyer was found. The employees would also continue to be bound by the terms of the contract of employment during the furlough period, including any restrictive covenants which would, for example, prevent them from working for a competitor, which could be valuable for a potential purchaser of the business. He found that Paragraph 99(5) could therefore be interpreted to permit the JRS to be given effect and to support the rescue culture.

As to the question of adoption, the Judge found that there was sufficient conduct by the Administrators to constitute adoption of the contracts of employment as a result of them acting upon the varied contracts of employment, (for the employees who had consented to the variations), or the existing contract of employment, (for those who had not responded), on the earlier of:

(a) making an application under the JRS; or

(b) making payment to the employees under their employment contracts.

In terms of the payment mechanism for the monies received from the JRS, the Judge considered that the monies could be paid to the employee using Paragraph 66 or Paragraph 99(5) of Schedule B1 Insolvency 1ct 1986. His finding was that Paragraph 99 was the preferable mechanism for payment in light of his findings on adoption.

The Debenhams case at first instance

Debenhams operated 142 stores in the UK and went into administration in 2019 and then into a CVA to compromise payments under leases with the various landlords and to implement a store closure programme. The CVA was continued in operation until the Crisis. On March 25 2020 prior to the administration the company wrote to 13,000 store-based employees informing them that the government required them to close the stores and they were being furloughed until further notice from the next day. The letter said that they would receive 80 percent of their usual monthly wages up to a cap of £2,500, and the company would not pay any additional amounts accruing under their contracts of employment. A further 867 employees were placed on furlough in the period from March 26 2020 to the date of the administration.

On April 9 2020 the Administrators were appointed, with significant numbers of employees already furloughed. Immediately following their appointment the Administrators sought the express consent of the employees to the furloughing and the pay reduction in letters sent by email to employees on April 10 2020. As at the date of hearing there were 12,700 consents, 4 objections and 359 employees had not responded. Further consents were coming in all the time to the Administrators.

The Administrators sought a number of directions in relation to the employees and the JRS.

As in the Carluccio's case the concern of the Administrators was that the additional potential super priority claims for the 20 percent of salary, salary above the monthly cap of £2,500 and holiday pay payable at the original rates in the employment contracts, for the employees who had not consented to the variation of their contracts of employment, would not be covered by the grant from the JRS. Prior to the hearing, these claims were estimated to amounted to about £3 million, and would be payable as super priority claims as administration expenses prior payment of the Administrators' fees.

The Administrators submitted that the decision on adoption should wait until the furlough period had ended. The Administrators argued that to support the rescue culture and to enable the business to be rescued there should be no adoption as that could result in more redundancies if the Administrators were potentially exposed to make payments of additional amounts under the contracts of employment.

Judgement was given by the Honourable Mr Justice Trower. He did not accept that consent of the employees who had not responded in a short time frame to a potentially significant change in terms of employment could be inferred/deemed from silence.

The Judge found that the acts of participation in the JRS and the payment to the furloughed employees constituted an election in the form described by Lord Browne Wilkinson. The Administrators could not possibly procure the Company to participate in the JRS without procuring it to pay the equivalent amount to the employee. The obligation to do so arises under the continued contract of employment which the Company in administration is required to honour as a condition of participation in the JRS.

The decision of the Court of Appeal in Debenhams

The Court of Appeal found that there was adoption, in light of the actions taken by the Administrators, but was concerned that the finding of adoption would mean that Administrators may consider they have to make redundancies in order not to incur liabilities not covered by the JRS.

The court considered that it as an objective test as to whether there was adoption, and the intention of the Administrators was irrelevant. They endorsed the decision of the Honourable Mr Justice Laddie in *Re Antal 2003* which referred to the need for conduct on behalf of the Administrator:

> "*which could be treated as an election or could be regarded as him exercising a choice as to whether or not the contracts of employment were to be adopted…..*"

Lord Justice David Richards commented*:*

> *"It is necessary to look at the facts and decide."*

The Court of Appeal considered the relevant facts here were as follows:

1. The Administrators will continue to pay the wages of the employees under the employment contracts and the income chargeable to income tax.
2. The furloughed employees are bound by contracts of employment and remain available to provide employment and obliged to provide employment to the company as and when the stores reopen.
3. In continuing to pay the employees the Administrators were acting in accordance with the objective of rescuing the company as a going concern in accordance with Paragraph 3(1) of schedule B1, and the Administrators rely on Paragraph 66 of Schedule B1 to continue to pay the remuneration of the furloughed employees but to do so they must think:

> *"that it is likely to assist achievement of the purpose of administration"*

The Court of Appeal considered that the fact that the furloughed employees were not carrying on work was a significant fact, but not sufficient of itself to mean there was no adoption. The JRS had been devised by the government to provide for a payment by the company and not a payment direct to the employee, so:

> *"the legal consequences of the Scheme must be decided by reference to its actual terms"*

The Court of Appeal said:

> "*We can see that there may be good reasons of policy for excluding action restricted to implementation of the Scheme from the scope of "adoption" under paragraph 99 but such exclusion cannot be accommodated under the law as it stands*".

So in effect, the conclusion is that law reform is needed to exclude the JRS from the scope of adoption, but this seems unlikely, given that the government is trying to reduce the reliance on the JRS in the coming months.

In terms of comments on the mechanism for payment under the Insolvency Act, the Court of Appeal disagreed with the Honourable Mr Justice Snowden that paragraph 99 should be interpreted to include the contract of furloughed employees. It accepted the submission by Counsel for the Administrators that Paragraph 66 is more appropriate and

> *"the most obvious source of authority for these payments"*,

as the steps that the Administrators are taking are "*likely to assist achieving of the purpose of administration*".

> "*In contrast paragraph 99 operates only where a person ceases to be the administrator, although it may well be the case, as Trower J observed that authority can also be derived from Paragraph 99"*

Practical consequences of the decisions

- Given the potential exposure of the Administrators to super priority claims under any unvaried employment contracts, the Administrators should if at all possible prior to appointment seek the written consent of as many employees as possible prior to appointment of administrator to the furlough and to the variation of the contract of employment to payment only of amounts received by the company in administration under the JRS, and to a reduction in holiday pay.
- Administrators need to review regularly whether there is a "reasonable likelihood of rehiring the employee". A rolling three week review is needed for the Administrators to ensure that the company should be continuing to use the JRS.
- Administrators should make careful notes of their thought processes and decisions to be able to demonstrate the reasonableness of their decisions at a later date.
- If the employees were furloughed before the Administration, but the Administrator then considers that there is no reasonable likelihood of rehiring some or all of the employees following his appointment, the Administrator should consider making the employees redundant immediately and returning any grant payment from the JRS relating to that employee after they have made them redundant, bearing in mind the strict obligation that funds received must only be used for the purposes of the JRS. Some commentators have argued that the cash

received is held in effect on a Quistclose trust or a resulting trust in accordance with the provisions of Paragraph 2.4 of Guidance.

The end of the JRS and the impact of the JRS on consultation for redundancies

When the JRS is withdrawn, or the employee comes off furlough, the obligations of the employer to make payments under the adopted employment contracts will resume. In the alternative, the Administrators will need to make the employee redundant with no notice, with their claims for redundancy and notice being treated in accordance with the provisions of the Insolvency Act as preferential or unsecured claims. The Guidance does suggest that notice pay can be paid to employees on furlough, however this would be at odds with the obligation on the Administrator only to use the JRS if there is a reasonable likelihood to rehire the employee, and could expose the Administrator to potential liability for additional notice pay not covered by the grant from the JRS, if that were provided for in the contract of employment.

The consultation obligations re redundancy under TUPE and UK employment legislation remain notwithstanding the fact that the employees are on furlough. These sit uneasily with the Administrators indicating that it is reasonably likely that the employee will be rehired, and with the way in which Administrators seek to achieve the purpose of administration and rescue or sale of the business.

Practically it will be difficult to consult with employees on furlough if they are not contactable on email on by telephone. The Administrator should make reasonable efforts in the circumstances to consult with the employees on possible redundancies. It is also important to remember that there is potential criminal liability for failure to file collective consultation form HR1.

One practical suggestion would be to use the initial letter to the employees informing them of their appointment, the furlough, and requesting consent to variation of the terms of employment, as also referring to consultation and beginning the consultation process.

Claims for inadequate or lack of consultation can result in the making of a protective award against the company which is an unsecured claim.

Conclusion and the impact of the JRS on the rescue culture

The current focus in the UK is on saving businesses and rescuing companies. The JRS is forming a large part of this effort, by the government currently supporting the wage payments of over seven million employees in over one million businesses under the JRS.

It is to be hoped that the government makes an exception for companies in administration from the contribution obligations to be introduced later in the year, as otherwise this could significantly affect the number of businesses which survive and are restructured or sold using the administration process in the coming months.

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Overview of the key Chapter 15 decisions in 2019

James Copeland and Francisco Vazquez

Chapter 15 of the Bankruptcy Code provides a mechanism pursuant to which a foreign insolvency, liquidation, or debt restructuring (known as a "foreign proceeding") may be granted recognition in the United States. In 2019, foreign debtors and their trustees, liquidators and administrators, acting as "foreign representatives," filed more than 70 Chapter 15 cases to, among other things, enjoin litigation against the debtor, preserve a debtor's assets, and pursue claims in the US. The Southern District of New York was the preferred Chapter 15 venue with 34 filings, followed by the Southern District of Florida with 14 filings. The Chapter 15 cases filed in 2019 were ancillary to foreign proceedings pending in the following 20 foreign jurisdictions: Al Maghreb al Agsa, Belize, Brazil, British Virgin Islands, Canada, Cayman Islands, China, France, Germany, Guernsey, Hong Kong, India, Indonesia, Ireland, Mexico, Russia, South Korea, the Netherlands, New Zealand, and the United Kingdom.

During 2019, US courts issued several interesting decisions in the Chapter 15 context that are the focus of this "year in review" article. This article begins with a discussion of a trio of decisions analyzing the "center of main interest" or "COMI" element. The article then examines a decision addressing the scope of discovery in the Chapter 15 context and the ability of a court to enforce its own orders. The article continues with discussions focused on decisions concerning the importance of demonstrating a pecuniary interest in a Chapter 15 case and issues concerning a foreign representative's personal exposure to litigation. It concludes with an analysis of a decision highlighting Chapter 15's requirement that courts consider creditors' and a debtor's respective interests in granting certain discretionary relief.

Recognition of a foreign proceeding under Chapter 15

There are two types of foreign proceedings under Chapter 15: (i) a "foreign main proceeding," which is defined as a foreign proceeding pending in the country where the debtor has its COMI, and (ii) a "foreign nonmain proceeding," which is defined as a foreign proceeding pending in a country where the debtor has an "establishment," which means "any place of operations where the debtor carries out a nontransitory economic activity." Arguably, the distinction is significant because upon recognition of a foreign main proceeding, the debtor and the foreign representative automatically receive certain protections, including the benefits of the automatic stay. Courts, however, have noted that the distinction may not be material because a court has discretion to grant similar relief upon recognition of a foreign nonmain proceeding. Nevertheless, a court must determine the location of a debtor's COMI and/or establishment when ruling on a Chapter 15 petition.

Guidance for determining a group member's COMI

Under the Bankruptcy Code, a corporate debtor's registered office (*i.e.*, its place of incorporation) is presumed to be its COMI, but this presumption is rebuttable. Determining where a debtor's COMI lies or the location of a debtor's establishment is fact intensive and courts will consider, among other things, the debtor's nerve center, location of operations and assets, and creditor expectations. When a debtor is a member of a group of companies, it may be more difficult to determine a debtor's COMI because its operations and affairs may be commingled with others. In *In re Serviços de Petróleo de Constellation S.A.*, 600 B.R. 237 (Bankr. S.D.N.Y. 2019), the bankruptcy court addressed some of those difficulties when it considered a request for recognition of Brazilian reorganization proceedings of a group of companies under Chapter 15.

Constellation Oil Services Holding S.A., a Luxembourg company, is the ultimate parent of a group of companies known as the "Constellation Group," which operates principally in and from Brazil. Facing financial distress, members of the Constellation Group commenced reorganization proceedings ("*recuperação judicial*") in Brazil. Certain Constellation debtors filed Chapter 15 petitions for recognition of the Brazilian proceedings as foreign main proceedings or foreign nonmain proceedings with the New York bankruptcy court. A creditor objected to recognition as foreign main proceedings, arguing that the COMI of all of the debtors was located in Luxembourg, where the parent company's registered office was located. The bankruptcy court disagreed, holding that the location of a debtor's COMI was not dependent on the COMI of its parent. Instead, COMI should be determined on a debtor-by-debtor basis for each member of the Constellation Group.

In this instance, finding that the statutory presumption had not been rebutted, the bankruptcy court found that the parent company's COMI was Luxembourg. Accordingly, the parent's Brazilian proceeding could not be recognized as a foreign main proceeding. The court, however, found that the parent had an establishment in Brazil premised on the activities of the parent's subsidiaries. According to the court, given that the parent was a holding company with minimal operations, the activities of its subsidiaries should be considered. Because most of the parent's subsidiaries' operations were located in Brazil, the court found the parent had an establishment in Brazil and, therefore, recognized the parent's Brazilian proceeding as a foreign nonmain proceeding.

Turning to the other debtors, the court noted that several were registered in the British Virgin Islands or the Cayman Islands, and therefore their COMI was presumed to be outside of Brazil. However, the court found that the evidence was sufficient to rebut that presumption. In particular, five of the six offshore debtors were operating subsidiaries that maintained and operated offshore drilling rigs located in Brazil. Moreover, based on the evidence presented, creditors reasonably expected that any restructuring of the offshore debtors would occur in Brazil, and the nerve-center (*i.e.*, where day-to-day operations were managed) of each was in Brazil. Consequently, the court found that Brazil was the COMI of those debtors. The sixth offshore debtor, which was registered in the British Virgin Islands, was the parent company of most of the operating companies. Because the offshore parent's functions were limited to "own[ing] equity in subsidiaries, guarant[ying] debt and centraliz[ing] certain treasury function to support subsidiaries operating and generating in Brazil," and creditors supported a Brazilian restructuring, the court found that Brazil was the offshore parent's COMI. Accordingly, the bankruptcy court recognized the offshore debtors' Brazilian proceedings as foreign main proceedings notwithstanding that they were registered elsewhere.

A range of activities can support a COMI finding

US courts have adopted a flexible approach to determine a foreign debtor's COMI, finding that a broad range of activities can support fixing COMI in a particular jurisdiction. In *In re Ascot Fund Ltd.*, 603 B.R. 271 (Bankr. S.D.N.Y. 2019), the US Bankruptcy Court for the Southern District of New York analyzed the COMI of Ascot Fund Ltd, an investment fund organized under Cayman Islands law, which, through its affiliate Ascot Partners (incorporated under Delaware law), invested substantially all of its assets with Bernard L. Madoff Investment Securities, LLC. After years of litigation, the funds entered into a settlement with the BLMIS estate, pursuant to which Ascot Partners would receive certain payments. Thereafter, an investor in the fund disagreed with the proposed distribution methodology for those recoveries. In the face of that dispute, Ascot Fund went into liquidation in the Cayman Island and its liquidators filed a petition for recognition of the Cayman proceeding as a foreign main proceeding under Chapter 15. The investor objected, arguing that Ascot Fund's COMI was New York, not the Cayman Islands.

Under Chapter 15, Ascot Fund's COMI was presumed to be in the Cayman Islands, where its registered office was located. Still, the bankruptcy court noted that the guiding principle for determining a debtor's COMI is "where the debtor conducts its regular business, so that the place is ascertainable by third parties." Further, COMI is determined as of the time that the Chapter 15 petition is filed, but courts can examine the period between the "initiation of the foreign liquidation proceeding and the filing of the Chapter 15 petition" to ensure that COMI has not been manipulated. The bankruptcy court found that Ascot Fund had been actively managed from the Cayman Islands both before and after the liquidation proceeding (which had been pending for nearly four months), and contrary to the investor's argument, such activity was not merely ministerial. For example, Ascot Fund's board of directors conferred regularly in the Cayman Islands, directors resided or were based in the Cayman Islands, and before and after the Cayman Islands liquidation, the fund had employed an administrative-services company, which had offices throughout the world, including the Cayman Islands. Moreover, the court was not persuaded that, as the investor argued, New York was Ascot Fund's COMI. According to the court, Ascot Fund's only significant activity in New York post-liquidation was being "dragged into" and participating in certain litigation. Moreover, Ascot Fund "had not carried on any investment activity in New York or anywhere else for over ten years." Given the lack of evidentiary support to rebut the presumption, the court found that Ascot Fund's COMI was the Cayman Islands and recognized the proceeding as a foreign main proceeding.

A foreign proceeding cannot be recognized if the debtor does not have its COMI or an establishment in the situs of the foreign proceeding

As emphasized by the US Bankruptcy Court for the Western District of Pennsylvania, a court will not recognize a foreign proceeding if there is insufficient evidence to support a finding that the debtor has its COMI or an establishment in the situs of the foreign proceeding. *See Beveridge v. Vidunas (In re O'Reilly)*, 598 B.R. 784 (Bankr. W.D. Pa. Mar. 22, 2019). There, the Bahamian trustee of a debtor filed a petition seeking recognition of a Bahamian proceeding under Chapter 15. A creditor objected to recognition arguing that (i) the Bahamian proceeding was not a foreign proceeding as defined by the Bankruptcy Code, and (ii) the debtor, who lived in France, did not have its COMI or an establishment in the Bahamas. The bankruptcy court dispensed with the first argument, finding that the Bahamian proceeding satisfied all of the elements of a foreign proceeding. In particular, the Bahamian proceeding was "collective" because all creditors had a right to participate therein. Moreover, there is no *per se* rule precluding recognition of a proceeding governed by a law that does not mirror US law. The court, however, was persuaded by the creditor's second objection.

Following the rational of decisions from the Second and Fifth Circuits, the Pennsylvania bankruptcy court held that the location of a debtor's COMI or an establishment should be determined as of the Chapter 15 filing date, not the date that the foreign proceeding commenced. In this instance, the debtor, a senior citizen in poor health, lived in France and had no physical presence in the Bahamas when the Chapter 15 petition was filed. Accordingly, the court concluded that the debtor's COMI was in France. Given the lack of any existing ties in or evidence of the debtor's intent to return to the Bahamas, the court found that the debtor did not have an establishment in the Bahamas. Accordingly, the court denied the petition for recognition.

Discovery issues in a Chapter 15 case

Chapter 15 offers an array of tools to assist foreign representatives in identifying and collecting assets for administration in foreign insolvency proceedings, including the authority to conduct broad discovery of a foreign debtor's property and affairs. The US Bankruptcy Court for the Southern District of New York's decision in *In re Markus*, 607 B.R. 379 (Bankr. S.D.N.Y. 2019) highlights the reach and utility of Chapter 15's discovery provisions. Following the recognition of a Russian bankruptcy proceeding, the foreign representative sought and obtained orders authorizing him to obtain discovery from the debtor and her counsel under Chapter 15. The debtor, who was incarcerated in Russia, and her US counsel, ignored the discovery requests. Upon the foreign representative's request, the bankruptcy court imposed sanctions on the debtor's counsel. According to the court, the debtor's incarceration did not justify counsel's refusal to comply with the discovery orders and requests. Moreover, counsel was not excused from discovery simply because the documents were in the possession of the debtor's agents and attorneys outside the US. The bankruptcy court had "exceedingly broad" discretion to grant relief, including enabling a foreign representative to take broad discovery concerning a debtor's property and affairs, as long as the requirements of Chapter 15 are satisfied. Moreover, there is no jurisdictional limitation on discovery available under Chapter 15. Accordingly, a foreign representative could be allowed to obtain "broad discovery" concerning the debtor's "worldwide financial affairs," notwithstanding that such information may be located outside the US.

On appeal, the debtor's attorney challenged the bankruptcy court's decision to allow discovery, as well as the award of sanctions and fees. The US District Court for the Southern District of New York did not reach the question of whether the bankruptcy court erred in authorizing discovery because the debtor and her attorney failed to timely appeal the applicable order. *Markus v. Rozhkov*, No. 19-CV-09611 (LJL), 2020 WL 1659862, at *12-*13 (S.D.N.Y. Apr. 3, 2020). The district court, however, did partially vacate the order imposing sanctions for "imposing [a] lump-sum retroactive sanction[ ] [that] was improperly criminal in nature" and remanded that portion of the order imposing the payment of attorneys' fees to permit the bankruptcy court assess whether it was issued pursuant to proper authority.

Limitations on relief available to parties in Chapter 15 cases

In the Second Circuit, which includes New York, an "aggrieved person" has standing to pursue an appeal. An aggrieved person is "a person directly and adversely affected pecuniarily by the challenged order of the bankruptcy court." As noted by the Second Circuit in *Wiener v. Ocean Rig UDW Inc. (In re Ocean Rig UDW Inc.)*, 764 F. App'x 46 (2d Cir. 2019), the appellant has the burden of demonstrating that it is an aggrieved person. There, the appellant, a purported shareholder of a debtor, appealed the order of the US Bankruptcy Court for the Southern District of New York granting recognition to Cayman Islands proceedings. On appeal, the district court found that the debtor was insolvent and unable to pay its creditors in full, and there would thus be no recovery to shareholders under Cayman Islands law. According to the district court, recognition did not adversely affect the shareholder pecuniarily and therefore it dismissed the appeal. On further appeal, the Second Circuit came to the same conclusion and reaffirmed the principle that an appellant must demonstrate that it is an aggrieved person before it can proceed with its appeal.

On similar grounds, the US Bankruptcy Court for Southern District of Florida denied a request for discovery from a foreign representative in a Chapter 15 case. As an initial matter, the foreign representative argued that nothing in Bankruptcy Rule 2004 or Chapter 15 authorized parties other than the foreign representative to seek discovery in a Chapter 15 case. The bankruptcy court refused to address that issue. Instead, it denied the request after finding that the discovery proponent was neither a creditor nor a shareholder of the foreign debtor and never appeared in the foreign proceeding. Given the lack of a pecuniary interest in the case, the court found that the discovery proponent could not show that "cause" existed for permitting it to proceed with discovery in the Chapter 15 case.

Protecting foreign representatives from suit in Chapter 15 cases

The *Barton* doctrine is a common law rule that bars suits against court-appointed fiduciaries in any venue without first obtaining leave of the appointing court. Traditionally, the *Barton* doctrine has been applied to state-court receivers, but courts have extended its protections to lawsuits against bankruptcy trustees. The bankruptcy and district courts in a case emanating from the liquidation of Irish financial institutions analyzed the applicability of the *Barton* doctrine in a Chapter 15 case. *McKillen v. Wallace (In re Irish Bank Resolution Corp. Ltd.)*, No. BR 13-12159-CSS, 2019 WL 4740249 (D. Del. Sept. 27, 2019).

The Irish Bank Resolution Corporation held the remaining assets of two Irish banks that were nationalized following the 2008 financial crisis. As the Irish economy continued to decline after the global financial crisis, the Irish government determined that it was necessary to wind down the IBRC. Thereafter, the Delaware bankruptcy court entered an order granting recognition to the Irish proceeding as a foreign main proceeding. Consequently, all persons and entities were enjoined from taking any action against the IBRC or its assets in the US. Following recognition, the foreign representatives sued a former client of one of the banks in Ireland. In response, the former client filed a motion seeking a declaration that his suit against the foreign representatives in their individual capacities was not subject to the Chapter 15 stay or the *Barton* doctrine or, alternatively, requesting relief from the Chapter 15 stay. The client wanted to assert, among other things, claims for alleged violation of Chapter 15, breach of fiduciary duties, and fraud and misconduct in the Irish proceedings. All of the allegations concerned actions taken by the foreign representatives in Ireland, which the former client argued adversely affected their US business interests. The bankruptcy court denied the motion. The bankruptcy court first addressed the *Barton* doctrine and found that it was not the "appointing court" as its role in Chapter 15 was only to "recognize[ ], not appoint[ ]" foreign representatives. The bankruptcy court noted that, absent at least some precedent, invoking the doctrine as the sole reason to deny relief in this case "would be a very expansive application of *Barton*." Instead, the bankruptcy court extended the automatic stay to the foreign representatives, finding a "significant identity of interests" between the IBRC and the foreign representatives, and then denied stay relief based on a balancing of potential harms and further found that the court lacked subject matter jurisdiction over acts that happened in Ireland. The former client appealed, but the Delaware district court affirmed.

The district court declined to decide the applicability of the *Barton* doctrine in a Chapter 15 case, including whether the doctrine applies extraterritorially. The district court further observed that US bankruptcy courts cannot appoint replacement foreign representatives, such that removing the foreign representatives would "essentially leave IBRC unable to administer assets in the United States and unable to take any action in the ongoing Chapter 15 proceeding." The district court noted that, "[w]ithout foreign representatives, IBRC would lose the ability to effectuate its own foreign proceeding and protect its assets within the United States, to the immediate detriment of IBRC"; thus there was "such an identity between the debtor and these third-party defendants that a judgment against [the foreign representatives] individually 'will in effect be a judgment or finding against the [d]ebtor.'"

Protecting parties' interests in Chapter 15 cases

Chapter 15 provides courts and foreign representatives with substantial flexibility in crafting relief to meet the needs of a particular case. However, there are some important limitations. In particular, Bankruptcy Code section 1522 provides that "[t]he court may grant relief under section 1519 or 1521 . . . only if the interests of the creditors and other interested entities, including the debtor, are sufficiently protected." The court addressed this requirement in *In re ENNIA Caribe Holding N.V.*, 596 B.R. 316 (Bankr. S.D.N.Y. 2019).

After the US court granted recognition to the Curaçao proceeding as a foreign main proceeding, the foreign representative requested an order entrusting the foreign representative with the administration, realization, and distribution of approximately US$240 million held in accounts in the names of the debtors at Merrill Lynch in the New York. The non-debtor parent of the debtors objected to the motion, arguing that it was not "sufficiently protected." The bankruptcy court acknowledged that it could not grant the requested relief unless all interested parties were sufficiently protected. It adopted a balancing test to analyze that requirement.

In this instance, the court was satisfied that interested parties were sufficiently protected because the debtors and all creditors and other parties would benefit from the debtors' improved liquidity. The court was convinced that the funds being entrusted would be used to rehabilitate and finance the debtors' business, which would clearly benefit the debtors and its creditors. Moreover, absent the relief, the potential harm to the debtors and "most importantly, to the [d]ebtors' creditors" was far greater than any potential harm to the parent. The court therefore concluded that the relief was necessary to effectuate the purposes of Chapter 15 and to protect the debtors' assets given their growing liquidity concerns.

Conclusion

Chapter 15 is a useful tool for a foreign representative to administer a foreign proceeding. As highlighted above, US courts are generally inclined to cooperate with a foreign representative and a foreign court if the requirements of Chapter 15 are satisfied. A US court, however, will not simply rubber stamp a foreign representative's request for relief in a Chapter 15 case.

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Re CEFC Shanghai International Group Limited: The first case of Hong Kong Court's recognition and assistance of bankruptcy administrators in mainland China

Daniel Ng

Key Points

In *Re CEFC Shanghai International Group Limited (HCMP 2295/2019)* ("Decision"), the Hong Kong court has for the first time granted recognition and assistance to bankruptcy administrators appointed for a company in insolvency proceedings in mainland China ("Mainland").

The Decision will have a significant impact on insolvency cases spanning the Mainland and Hong Kong (and elsewhere). Given the size of the Mainland economy and the international scope of many Mainland enterprises, we can expect to see an increasing number of applications for recognition and assistance by Mainland insolvency officeholders in Hong Kong and other jurisdictions.

In connection with the Decision, however, the Hong Kong court signalled that it views cross-jurisdiction recognition as a "two way street"–namely that one would expect Mainland courts to also recognise and provide assistance to non-Mainland insolvency proceedings given the transnational business conducted by many Mainland businesses and Article 5 of the Enterprise Bankruptcy Law which envisages the possibility of recognition of foreign liquidations by Mainland courts. How the Mainland courts will approach applications for recognition and assistance by foreign liquidators and more generally how receptive they are to the principle of modified universalism is an open question.

Stay tuned for further developments as the Hong Kong court reacts to how Mainland courts approach these issues in the future.

The legal context

It is clear that the Hong Kong court has the power to wind up a foreign incorporated company under section 327 of the Companies (Winding Up and Miscellaneous Provisions) Ordinance. However, the difficulty is that generally the so called three core requirements must be satisfied namely:

a. There is sufficient connection with Hong Kong.

b. There must be a reasonable possibility that the winding-up order would benefit those applying for it.

c. The court must be able to exercise jurisdiction over one or more persons in the distribution of the company's assets. The court has held that this 3rd requirement may be dispensed with in exceptional circumstances where the connection with Hong Kong is so strong and the benefits of a winding up order for the creditors of a company are so substantial.

Further, winding up petition proceedings are generally expensive and time-consuming.

Therefore, a generally cheaper and quicker alternative is for a company to enter into foreign insolvency proceedings and then to seek the recognition and assistance of the Hong Kong courts.

While Hong Kong is not a party to the UNCITRAL Model Law on cross border insolvency and Hong Kong's insolvency legislation does not contain provisions dealing with cross-border insolvency, the Hong Kong court has made clear in its 2014 decision of *Joint Official Liquidators of A Company v B & C* that it has power to recognise and grant assistance to foreign insolvency proceedings.

The underlying principle is the "principle of modified universalism" derived from the English case law, which in general terms requires the courts to, so far as is consistent with justice and public policy, cooperate with the courts in the country of the principal liquidation to ensure that all the company's assets are distributed to its creditors under a single system of distribution. This is to ensure fairness between creditors such that no one should have an advantage because such a creditor happens to live in a jurisdiction where there are more assets or fewer creditors.

Since the 2014 decision, the Hong Kong court has received a large number of applications for recognition and assistance. Many of these applications concern insolvency proceedings in common law jurisdictions such as the

Cayman Islands, Bermuda and the British Virgin Islands as many Hong Kong listed companies are incorporated in one of those jurisdictions. In the decision of *Re Mr Kaoru Takamatsu* in 2019, the court has also recognised and provided assistance to a trustee in bankruptcy appointed in Japan, a civil law jurisdiction.

The law is well-settled that the Hong Kong court will recognise foreign insolvency proceedings that comply with the following criteria:

a. The foreign insolvency proceedings are collective insolvency proceedings in the sense that it is a process of collective enforcement of debts for the benefit of the general body of creditors.
b. The foreign insolvency proceedings are opened in the company's country of incorporation.

Upon recognition of the foreign insolvency proceedings, the court will grant assistance to the foreign officeholders by applying Hong Kong insolvency law. However, there are limits to the power that can be granted to the foreign officeholders as follows:

a. The power of assistance is not available to enable foreign officeholders to do something which they could not do even under the law by which they were appointed.
b. The power of assistance is available only when it is necessary for the performance of the foreign officeholder's functions.
c. An order granting assistance must be consistent with the substantive law and public policy of the assisting court.

As the law is well-settled and there has been an increasing number of applications for recognition and assistance, the court has developed a standard-form recognition order and such applications may be granted quickly on a written application.

Background of the Decision

The company involved in the Decision is CEFC Shanghai International Group Limited (the "Company") which is a Mainland-incorporated investment holding company and is part of a conglomerate whose business includes capital financing, petroleum refining and infrastructure. Pursuant to an order of the Shanghai No 3 Intermediate People's Court, the Company went into insolvent liquidation and administrators were appointed ("Administrators") under the Enterprise Bankruptcy Law ("EBL"). The Company has substantial assets in Hong Kong which include a claim against its Hong Kong subsidiary, amounting to some HK$7.2bn "(HK Receivable").

After their appointment, the Administrators discovered that a creditor of the Company obtained a default judgment against the Company in Hong Kong. To enforce the judgment, the creditor obtained a garnishee order nisi in respect of the HK Receivable. In order to prevent the creditor from obtaining a garnishee order absolute, the Administrators made an urgent application to the Hong Kong court for recognition and assistance, supported by a letter of request from the Shanghai court.

Decision – recognition and assistance

The court found that the case satisfies the relevant principles for making an order of recognition and assistance:

a. The Company's liquidation in the Mainland is a collective insolvency proceeding shown by the fact that the liquidation proceeding encompasses all of the debtor's assets.
b. The powers sought by the Administrators are consistent with the insolvency law in the Mainland and the standard recognition order set out by the Hong Kong court in previous cases. In particular:
    - The Administrators' powers and duties under Article 25 of the EBL correspond to a Hong Kong liquidator's powers and duties.
    - Article 9 of the EBL provides that after a bankruptcy application is accepted by the people's court, the preservation measures against the debtor's property shall be removed and the enforcement proceedings shall be suspended. This corresponds to the stay of proceedings upon the making of a winding-up order by the court under the Hong Kong insolvency regime.
    - Article 113 of the EBL sets out the requirement of pari passu distribution of the debtor's assets which is also consistent with the Hong Kong insolvency regime.

Although the court held that recognition and assistance do not require reciprocity to be demonstrated, the court noted that the foreign jurisdiction under consideration should also aim to promote a single bankruptcy when faced with the insolvency of a company with assets and creditors in jurisdictions other than its own. Otherwise multiple liquidations would need to be undertaken in different jurisdictions undermining the underlying rationale for providing recognition and assistance. The court noted that while it is not clear at present what attitude the Mainland courts will take under the EBL to foreign liquidations, it is clear that Article 5 of the EBL envisages that there will be recognition of foreign liquidators.

Decision – stay of proceedings

Consistent with the court's standard form recognition order, the court also imposed a stay on all the proceedings against the Company in Hong Kong, including the garnishee proceedings. The court held that such stay should be imposed even though the creditor has obtained the garnishee order nisi in Hong Kong before the commencement of the Mainland liquidation. Such an approach would generally be consistent with the principles that bankruptcy proceedings should have universal application to ensure fairness between creditors.

Discussions

There have been discussions in Hong Kong about potential reforms to its insolvency and restructuring regime for more than 20 years. However, while other jurisdictions such as Singapore have made significant changes to its insolvency and restructuring regime in order to promote itself as an international centre for restructuring, no significant reforms have so far been implemented in Hong Kong. It has recently been reported in the press that the Hong Kong government intends to hold a new round of consultation in the coming months and to introduce a draft corporate rescue bill to the Legislative Council in the first half of the 2020-21 legislative session. This is welcome news to the insolvency and restructuring community given the long history of the introduction of the corporate rescue bill since the Law Reform Commission's first recommendation in 1996 before the onset of the Asian financial crisis, and the failure to pass the same in subsequent years despite multiple modifications in 2003 through the SARS outbreak and 2008 through the global financial crisis. While details of the draft bill have not been published as at the date of this publication, they will likely include a statutory corporate rescue procedure with a statutory moratorium on all legal actions and proceedings against a company for a certain period while an independent third party (known as the provisional supervisor) is appointed to take temporary control of the company, consider options for rescuing the company and prepare proposals for a voluntary arrangement within a specified period for creditors' approval. A reform to the law is urgently needed especially in light of the significant economic impact brought by the Hong Kong anti-government protests, the US/China trade war and the coronavirus outbreak.

Against this background of Hong Kong's inertia in reforming its insolvency and restructuring regime, there is an active body of case law from the Hong Kong court on recognition and assistance of foreign insolvency proceedings. The Decision marks a milestone in the development of such case law. Given the size of the Mainland economy and that Mainland enterprises increasingly have assets located overseas, we can expect to see an increasing number of applications for recognition and assistance by Mainland insolvency officeholders in Hong Kong and other jurisdictions. As noted in the Decision, there are in recent years at least two cases of recognition of Mainland insolvency proceedings in the US under Chapter 15 of the United States Bankruptcy Code. Mainland officeholders may have greater ease of access to assets of Mainland enterprises located outside of the Mainland. On the other hand, while Article 5 of the EBL clearly envisages the possibility of recognition of foreign liquidators by the Mainland courts, it remains to be seen how the Mainland courts will approach applications for recognition and assistance by foreign liquidators and more generally how receptive they are to the principle of modified universalism. As noted at the end of the Decision, this will in turn have a knock on effect on the extent of assistance provided by the Hong Kong court to Mainland administrators.

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The centre of main interest is in the eye of the beholder – The perspective from Europe

Oliver Sutter

The term "centre of main interest" is a legal term introduced in the UNCITRAL Model Law on Cross-Border Insolvency and thus included in the EU directive 1346/2000 ("Directive"), which deals with cross-border insolvency proceedings within the member states of the European Union and, in particular, which member state is responsible for the main insolvency proceeding.

In its basic interpretation, the centre of main interest is the location where the debtor administers its business and which, as such, is "recognizable" by a third party. Albeit the definition seems to be reasonably simple to understand and decide upon, the reality is that the term "centre of main interest" is one of the terms most disputed by insolvency law scholars, insolvency practitioners and insolvency courts.

The legal assumption is that the centre of main interest of a corporation or establishment is where it has its statutory seat. This legal assumption may only be set aside, if there are objective circumstances that can be recognized by a third party and which establish a different centre of main interest deviating from the jurisdiction of the statutory seat of the relevant corporation or establishment. While this seems to be a reasonably practical starting point, this legal assumption may either (i) not be required at all in the case where the centre of main interest is without doubt (e.g., the only factory building in state X) or (ii) relatively easy to be set aside in a case where the statutory seat is in state X while all business, assets etc. are located in state Y. European law as well as the corporate laws of various EU member states add further legal issues to what should be a matter of the facts and circumstances.

As the corporate laws of various European jurisdictions allow for a company's governing documents to make a distinction between the statutory seat and the actual business address, the benefit of the basic legal assumption is, however, rather limited. While Germany had in the past always applied the principle that a corporation or establishment is governed by the laws of its incorporation, various other member states of the European Union always have adopted the principle that a corporation or establishment is governed by the laws of the jurisdiction where its business is actually seated. For certain corporations such as limited liability companies (a "GmbH") even Germany now has adopted the principle that a GmbH may be incorporated under German law, maintain a statutory seat in Germany but may have its administrative seat (i.e. headquarters and principal place of business) in another state, thereby overcoming the legal issue that based on the doctrine of establishment a GmbH would cease to exist as a going concern, based on the previous interpretation of German law.

This is even more relevant on a European law level as one of the founding principles of the European Union is the free movement of goods and of people, which also applies to corporations. The European Court of Justice decided in various cases that a corporation can be established under the laws of state X and then move to state Y to conduct business out of state Y (and only out of state Y).

If this was not enough complexity already, the discussion has been added to by some insolvency lawyers who actively seek to shift the centre of main interest to what they believe to be a more favourable jurisdiction for an insolvency proceeding. In the past (and before a revision of the German Insolvency Code introduced a proceeding very similar to a US chapter 11-proceeding) it was not uncommon for private equity sponsors or, in certain cases, other holders of controlling interests, to take action to move the centre of main interest to England, where as the laws of England and Wales allow for a scheme of arrangement which was deemed to be more flexible than one of the proceedings available under the German Insolvency Code.

While it may of course be difficult (and probably prohibitively costly) to move factory buildings from state X to state Y to alter the centre of main interest, simpler measures may have the same effect in respect of parent companies holding a group of subsidiaries spread across Europe. Even if the centre of main interest of the parent may be clearly in one jurisdiction, this does not result in all members of a group having the same centre of main interest, even if a certain member of the group represents the majority of the consolidated assets, EBITDA and/ or turnover of the group. Each member of the group has its individual centre of main interest which is to be derived from its own relevant circumstances. However, the jurisdiction in charge of conducting the insolvency proceeding of the ultimate parent company of a group of companies may still be the most relevant proceeding as the ultimate parent remains the (direct or indirect) shareholder of the other members of the group. So any distressed investor interested in acquiring the group as a going concern would usually be interested in acquiring (intermediate) holding companies, which control the other members of the group. This is in particular true in the case where the (intermediate) holding company or any relevant finance vehicle of a group is insolvent while the operational entities remain solvent.

Holding companies usually do not have relevant fixed assets so the location of their centre of main interest needs to be derived from other, and far more intangible, circumstances. Relevant criteria may be home addresses of managing directors, location(s) where board meetings and meetings of similar corporate bodies are held, the location where relationships with suppliers and customers are managed and/ or services are delivered. These criteria may be indicated by simple triggers like phone numbers and email addresses. A phone number starting with "+49" and an email address ending with ".de" objectively refer to Germany as place of business and, from the perspective of a third party, are easily "recognizable" as such and as a direction to Germany as the location where business relationships are administered.

Unless all criteria indicate the same centre of main interest, a court and/ or insolvency lawyer needs to weigh the different criteria objectively and come to a conclusion in light of the relevant criteria. If for example the corporate address is moved from state X to state Y, which may be a matter of fact given the change of address, this may still be insufficient where this could not be clear to a third party, eg. having one's business address moved to the location of a subsidiary residing on a large industrial site with various buildings and other structures may not be sufficient to identify where the business is conducted now. Similarly, having one's business address in state X but management decisions constantly adopted in state Y should indicate that the centre of main interest of such holding is in state Y. For an enterprise having its business address in state X, management decisions being adopted in state Y but all factory buildings located in state Z the outcome may however be different.

While there have been a few decisions from national courts of EU member states, there is currently a matter involving a sponsor led group of companies that may involve such practical and legal complexity as to give the German Federal Supreme Court and/or, potentially, the European Court of Justice a forum to further clarify what criteria are to be applied when analyzing the centre of main interest.

In this case, the relevant SPV ("SPV") being the ultimate parent shareholder of the enterprise was established in state X and continued to have its statutory seat there as well. Almost all business, however, was conducted in state Y. When insolvency of the SPV was imminent, the SPV relocated to state Z. The SPV had no assets in State Z other than the controlling stake in another entity. Such stake was financed by various debt instruments to be (re)paid by dividends received by the SPV from the group of companies it controlled. Before the SPV could file for insolvency in state Z, certain of its creditors filed a proceeding in state Y based on the argument that the de facto "real" business of the SPV was conducted in state Y, and that its centre of main interest was therefore in state Y.

The relevant insolvency court at first declined to open proceedings in state Y, but when the management and business address of the SPV was moved to state Y it finally opened proceedings. The decision was upheld by the relevant regional court and is now with the Supreme Court for review. As the question is ultimately a question of EU law, it is rather likely that the Supreme Court will pass on certain questions to the European Court of Justice to ensure that its verdict is in line with European law. While these proceedings are still ongoing there are other proceedings in state X and state Z still running in parallel.

Multiple and competing main insolvency proceedings is exactly what the EU Directive had intended to avoid by allocating the main insolvency proceeding to one individual member state of the European Union. Yet this is ultimately the result of the vagueness of the decisive issue: What is the centre of main interest?

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Practical implications of the recent amendments to the CCAA

Peter Choi

The *Companies' Creditors Arrangement Act* (the "CCAA"), Canada's primary restructuring legislation for larger businesses, has been the subject of a collection of substantive amendments that came into effect on November 1, 2019.

The CCAA provides courts with authority to, among other things, grant stays of proceedings in favour of debtor companies and various other interested parties, and approve interim lending arrangements. The stay prevents potentially adverse parties from commencing, continuing or enforcing claims or enforcing other remedies. Interim lending arrangements can provide funding for the continued operation of the debtor's business and for the costs of the restructuring process and can be secured by a court-ordered super-priority charge.

The CCAA amendments include specific and material modifications to these key aspects of CCAA restructuring proceedings:

a. 10-day initial stay: The duration of the initial stay of proceedings is reduced from 30 days to 10 days.
b. Reasonably necessary relief: The relief provided by an initial order granted on the first day of the proceedings must be "reasonably necessary" for the continued operations of the debtor company in the ordinary course of business during this 10-day period.
c. Reasonably necessary interim financing: Interim financing secured by a court-ordered charge will only be approved to the extent "reasonably necessary" for the continued operations of the debtor company in the ordinary course of business during the initial 10day period.

Longer term relief is now deferred to a subsequent hearing.

These amendments may have broad impacts upon the sequencing and speed of Canadian restructuring proceedings. For example, steps to advance pre-packaged restructuring plans and sale processes may not be able to proceed at the initial hearing. In addition, debtors and their lenders may not be able to implement comprehensive interim financing arrangements at an initial hearing as they would have in the past.

Lenders, insolvency practitioners and other market participants now have some guidance on the court's application of these new amendments in practice. On December 23, 2019, Lydian International Limited ("*Lydian*") and certain of its affiliates engaged in gold exploration and development activities sought protection from their creditors under the CCAA. Given the holiday season, the Applicants requested that the court immediately grant a second order following the initial order to extend the stay period beyond the initial 10-day period.

In the *Lydian* proceedings, the Ontario court has directed that:

- Relief to be granted in an initial hearing under the CCAA should now, whenever possible, be limited to maintaining the *status quo* and stabilizing current operations during the initial 10-day stay period. Accordingly, the court declined to grant the request for a stay extension at the initial hearing, though the court implemented practical solutions for the hearing of the comeback motion given the holiday season.
- The practice of granting "wide-sweeping relief" at the initial hearing should be altered too in light of the recent amendments.
- The ensuing 10-day period allows for a stabilization of operations and a negotiating window, followed by a comeback hearing where the request for expanded relief can be considered, on proper notice to all affected parties.
- Court-ordered charges to secure professional expenses and director and officer indemnities, which are typically granted at the commencement of insolvency proceedings in order to ensure that both restructuring professionals and directors and officers remain engaged, were appropriate and should be approved.
- Absent exceptional circumstances, the court did not believe it was desirable to entertain motions for supplementary relief in the period immediately following the granting of an initial order.

The court explained that this approach was consistent with the objectives of the amendments which include improving participation of all players (including those players who may not have been at the table in the negotiations leading up to the insolvency filing).

Following the introduction of the CCAA amendments there was a great deal of speculation regarding the court's approach to the new amendments and whether the more flexible provisions of the CCAA may be used to work around the practical implications of the amendments. Courts initially took varying approaches to these issues. The court in *Lydian* has taken a firm line on (i) the 10-day initial stay period; and (ii) the requirement that any relief granted in the initial order be reasonably necessary for the continued operations of the debtor company in the ordinary course of business during that period, though flexibility may remain to accommodate exceptional circumstances.

The court commented that following the granting of the initial order, a number of steps can be taken and negotiations can commence or continue, including but not limited to:

- Notification to all stakeholders of the CCAA application
- Stabilization of the operation of debtor companies
- Ongoing negotiations with key stakeholders who were consulted prior to the CCAA filing
- Commencement of negotiations with stakeholders who were not consulted prior to the CCAA filing
- Negotiation of DIP facilities and super-priority charges
- Negotiation of Key Employee Incentives Programs and Key Employee Retention Programs
- Negotiation with key suppliers.

It was not uncommon, prior to the recent amendments, for an initial order to include provisions that would affect some or all of the aforementioned issues and parties. This will likely no longer be the case.

This is an important consideration for restructuring companies. For example:

- Liquidity and Interim Financing: Debtor companies may need to prepare for creditor protection further in advance of a liquidity shortage to allow additional time for a comprehensive DIP financing arrangement to be approved, or negotiate shorter term financing to be used solely for the initial 10-day period.
- Pre-packaged Plans and Sale Processes: Steps to approve sale processes or a meeting process for a pre-packaged plan of arrangement may need to build in additional time for approvals following the initial hearing.
- Key Employee Incentive Programs and Key Employee Retention Programs: These arrangements were often approved at an initial hearing to ensure continuity at key employee positions. Debtor companies may need to consider alternative means to keep key employees engaged during the initial 10-day stay period.

When considering possible approaches to a CCAA restructuring, debtor companies, lenders and their respective advisors will need to fully consider the impacts of the amendments and the guidance provided by the court in *Lydian*.

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