COHEN & GRESSER

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ROUNDTABLE September 2021

CORPORATE BANKRUPTCY & INSOLVENCY LITIGATION

The corporate bankruptcy & insolvency litigation landscape has experienced a turbulent period over the past year and a half, largely a consequence of the extreme circumstances created by the COVID-19 pandemic. Against this backdrop, many businesses have sought arrangements and restructuring plans in an attempt to avoid corporate bankruptcy. However, as government COVID-19-related stimulus is withdrawn and the true financial impact of the pandemic becomes clear, the focus turns to which businesses will remain in crisis or fold, and which are able to restructure and survive. As the battle lines are drawn, disputes are sure to rise. ■

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Daniel Tabak is a litigation partner in the New York office of Cohen & Gresser LLP. He has extensive experience representing parties in bankruptcy and bankruptcy litigation and, in particular, has obtained favourable results asserting and defending against fraudulent conveyance claims. He also represents clients in the financial industry and other industries in commercial litigation, where he has successfully resolved cases at both trial and appeal levels.

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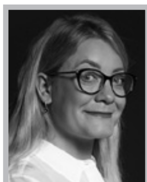

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FW: Could you provide an overview of the most significant trends in the corporate bankruptcy & insolvency litigation arena over the past 12 months or so?

Huntriss: In the UK, a significant trend is the enactment and use of a whole new piece of legislation – the Corporate Insolvency and Governance Act 2000 – during the immediate and unfolding financial consequences of the coronavirus (COVID-19) pandemic. The new act has had a seismic effect in the UK, opening up the options available to creditors and debtors alike. The most fundamental permanent change was to introduce a new tool – a restructuring plan – which, among other things, allowed for cross-class cram down. Other trends in litigation in this area have been a consequence of the extreme circumstances created by COVID-19. We have seen a large number of restructuring processes dealing with the immediate change in spending patterns, mainly in the retail, hospitality and travel sectors. However, while English courts were involved, in variously contentious cross-creditor spats, the true wave of post-pandemic insolvency litigation has not yet started. If anything, the cases we have seen this year have involved sticking plasters, doing enough to get companies through the short-term but not eliminating the need for a further process in the future.

Durrer: In the US, we have witnessed an increase in so-called 'lender-on-lender violence' in the past year. Creative liability management with respect to covenant-lite debt can cause this type of litigation or 'violence', which typically takes the form of asset-stripping transactions in J. Crew, for example, or uptiering transactions, in the case of Boardriders. An asset-stripping transaction is where an issuer transfers property to an unrestricted subsidiary, thereby rendering such property unencumbered. An uptiering transaction is where a group of requisite lenders vote to modify a credit instrument to permit the issuer to obtain a super senior lien facility, and that group of lenders exchange their debt for that senior facility. The litigation arises when the other lenders who were impacted by the transaction complain. These forms of transactions became possible due to the substantial amount of covenant-lite debt that has spawned in recent years.

Rogan: There has been a significant uptick in challenges to restructuring tools over the last 12 months. Successful challenges against UK schemes of arrangement and company voluntary arrangements (CVAs) have historically been few and far between; however, the last 12 months has seen a number of schemes failing at the sanction stage in the face of stakeholder challenges. Likewise, there has also been a successful challenge to the new restructuring plan, which has only been on the statute books for just over a year. Notwithstanding the number of challenges, the CVA has emerged largely unscathed, albeit an element of one CVA was successfully challenged while another is still subject to appeal. What is clear is that restructuring tools are being deployed in ever more creative ways, pushing the boundaries of the limitations imposed by statute and judicial precedent.

Bagon: There has been a significant increase in the number of UK companies, particularly those with significant lease liabilities, using CVAs, schemes of arrangements or the new restructuring plan, to implement court-sanctioned restructurings – attracted in many cases by the ability to bind non-consenting minority interests to court-sanctioned restructurings. That has led to an increase in litigation by compromised parties seeking to challenge the terms imposed on them or the procedures used. The restructuring plan is a new procedure which is being closely monitored by practitioners, especially in relation to the courts' interpretation of the regime and the application of the new cross-class cram down process. The growth in litigation funders established for the specific purpose of investing in bankruptcy-related cases has also continued, with several new funds entering the UK market.

Boynton: The past 12 or so months have been one of the most significant periods in living memory for bankruptcy litigation. We have seen the first uses of the new restructuring plan process, testing parameters, major CVA challenges and unprecedented interference with private contractual relations as the UK government legislated to prevent the use of statutory demands and winding-up petitions in circumstances where the obligor cannot pay for reasons related to COVID-19 – with most hearings held entirely virtually. We have also seen increased frequency of challenges to schemes of arrangement and restructuring plans. Now that the Rubicon of interference with contractual relations has been crossed, and given the wider political headwinds and consideration of the state's role in trade and commerce, including the debates over state aid and trade policy in the UK, it will be fascinating to see whether this interventionist approach continues or whether this type of action is a *sui generis* response to the unique challenges presented by the pandemic.

Whibley: Creditors seeking to stop proposed restructurings has been a major theme. Challenges to the New Look and Regis CVAs in the UK continued a line of disputes between retailers and landlords on whom they wish to impose rent reductions. For example, in New Look, certain landlords tried, unsuccessfully, to persuade the court that it should decline to sanction the CVA, even though it had received the required majorities of votes. It seems to have been a hard-fought attack on the proposal, arguing that the proposal did not meet the statutory requirements because, among other things, it really involved several different arrangements, there were 'material irregularities' in the voting process and in the content of the proposal, and the challenger landlords were unfairly prejudiced by the proposal. Some of the leading early examples of restructuring plans have also been challenged, and effectively litigated.

Kitt: The last 12 months for practitioners with an insolvency focus have been somewhat of a period of limbo. Practitioners have been awaiting UK government announcements to see what new measures aimed at promoting business

rescue have been created, whether those already in place have been effective, will cease or will be continued and if so, until when. During this period, four things have stood out. First, the way that the insolvency courts have continued to operate remotely and, arguably more effectively than they did before. Second, how creditors have had to look more creatively at debt enforcement in the absence of the usual winding up petition procedure. Third, the continued evolution and expansion of litigation funding and insurance options. Finally, the use of England & Wales' new restructuring plan and the court's evolving approach to sanction of those plans.

Tabak: The COVID-19 pandemic has made bankruptcy litigation take place remotely and allowed bankruptcy practitioners to practice from anywhere and in any court. In addition to the effect of remote litigation on the mechanics of the litigation process, there are also contradictory impacts on dispute resolution. On the one hand, the feeling that we are all in this together against a joint problem has provided some perspective and helped bring about consensual resolutions in some matters. On the other hand, bankruptcy litigators are going up against people they may have never met in person, which has an impact on the interpersonal dynamics that help achieve resolutions. When you share a meal with someone, you think of them in a more friendly way. That is not happening now. So far, I am seeing the desire to work together having a stronger effect on settlements, but that may change.

FW: In what ways does the corporate bankruptcy & insolvency process differ from other types of litigation? To what extent do issues of cost and speed impact on the process?

Durrer: Bankruptcy litigation in the US differs from other litigation in several meaningful ways. First, bankruptcy litigation routinely occurs over a period of days or weeks, whereas other litigation typically continues over a period of years. Second, while cost is always a core element of litigation, the impact of cost in bankruptcy litigation is unique. For example, even where a creditor has a strong legal position, such a creditor may be unwilling to incur legal fees to recover mere pennies. Likewise, certain parties in interest can terrorise other stakeholders in a bankruptcy by threatening expensive litigation that will deplete distributable value for all. Finally, just as in baseball, where all ties are called in favour of the baserunner, the same is true for debtors in bankruptcy where 'close calls' are often determined in the debtors' favour.

Rogan: The dynamic of restructuring litigation is fundamentally different to most types of litigation. Any challenge to the distressed debtor's restructuring has to be weighed against the possibility of cutting off one's nose to spite one's face as a result of precipitating an insolvency, rather than a going concern, return. The threat of implementing a restructuring through a process is key to a distressed debtor being able to corral its stakeholders and bring them to the table to negotiate a consensual solution. Likewise, the ability for stakeholders to threaten to disrupt any process is often key to ensuring a seat at the negotiation table and a division of the debtor's restructuring surplus. The ability of debtors and their stakeholders to be able to fund costs, and for the debtor to continue in the face of delays to its restructuring timetable as a result of stakeholder actions, is a key determinant of parties' leverage in restructuring negotiations and their ability to drive the shape of the restructuring solution.

Bagon: Bankruptcy and mainstream civil litigation processes in the UK are broadly similar: judicial rather than jury decisions, case work performed by solicitors, oral submissions made by barristers and decisions subject to the same appellate process. On a more granular level, a number of key differences emerge, including procedural differences arising from bankruptcy litigation being governed by the Insolvency Rules 1986 and specific court practice directions, differences in terminology, and differences in the parties to the litigation. Additionally, corporate insolvency cases are generally heard under the specialist insolvency and companies list, which forms part of the High Court of Justice – the Business and Property Courts of England and Wales division. Bankruptcy litigation is generally brought by an insolvency officeholder and will range from adversarial proceedings, including asset recovery and claims against connected and unconnected parties, to more procedural matters, such as seeking directions from

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VAN C. DURRER II
Skadden, Arps, Slate, Meagher & Flom LLP

the court on points of law or conduct of the estate.

Boynton: In most litigation, parties need only consider their own positions and the strength and merits of their own cases. In contrast, in an insolvency context, claimants must also have regard to what is financially achievable from the perspective of the company and, perhaps more importantly, their fellow creditors. The strength of the claim is just one element of the claimant's leverage influencing whether it will achieve a 'successful' outcome. Other relevant factors include the claimant's position in the capital structure, other creditors' claims and who can enforce first, whether there is a moratorium and what constraints and exceptions apply, the type of process the company proposes, whether new money is needed, and what assets a group has and in which jurisdictions they sit. A liquidity crisis may constitute good grounds for expedition of the process.

Whibley: Some insolvency disputes, such as claims against a company's directors, have similar procedure, timing, cost rules and funding options to other litigation. Challenges to restructuring processes are different. Challengers are not starting a claim but intervening in ongoing proceedings to prevent a process from going ahead. Procedure is more streamlined than conventional litigation – typically it will have only one hearing, with procedural arrangements worked out between the parties. There may be expert evidence as well as fact evidence, but no standard disclosure. A restructuring proposal might take months to implement, but a creditor's challenge to it might be resolved in just a few weeks. Timing is often driven by a need to act to avoid insolvency, which may itself be the issue in dispute. Cost implications vary, and may depend on the identity of the challenger, acceptance that there is an issue which needs to be resolved, and whether a regulator expects the company to pay.

> **"THE SIGNIFICANT LEVEL OF FISCAL STIMULUS AND FINANCIAL SUPPORT PROVIDED BY THE UK GOVERNMENT HAS LED TO A HISTORIC LOW NUMBER OF CORPORATE BANKRUPTCIES."**
>
> PAUL BAGON
> RPC

Kitt: The crucial difference between insolvency litigation and other types of litigation is that insolvency processes are essentially class actions – where an insolvency practitioner brings litigation, he or she is almost always litigating for the benefit of several creditor stakeholders who, in some cases, must be consulted or provide sanction to proceed. In actions brought by insolvency practitioners, the existence of these stakeholders calls for greater scrutiny on whether the litigation is in their best interests, what its risks are, what its potential costs are, how they can be funded and whether those costs are worth incurring considering the potential upside. Speed is a factor in that creditors demand quick results, but English courts cater for this with various summary forms of procedure for certain types of proceedings.

Tabak: The bankruptcy context pushes parties toward resolution more than in civil litigation in three key ways. First, there is an underlying view that a successful bankruptcy is one resulting in a successful reorganisation. There is a palpable feeling of accomplishment when a disputed issue is resolved consensually. Second, with a debtor entity and all its constituencies hanging in the balance, there is much more of an imperative to resolve issues quickly. The system and process will bog down if too many issues are contested for too long. Finally, an important lesson of bankruptcy litigation is that your adversary today may be your friend tomorrow on a different issue in the same bankruptcy. It is a bad idea for a litigator to scorch earth in any matter, and that is especially important in the bankruptcy context.

Huntriss: The context of insolvency and restructuring litigation is so different from other types of litigation. Yes, a dispute will often be 'party a' versus 'party b', but it is playing out across a broader set of circumstances of the financial distress of the debtor. There are also very specific rules and regimes – generally, the relevant statutory insolvency regime – and officeholders bring their own set of rules. All of these sector-specific issues hugely impact on the litigation in this space. In terms of cost and speed: speed will also depend on the underlying circumstances of the particular insolvency. Parties and the court can move very quickly where they need to, to rescue a company or to implement a pre-pack administration. Litigations in insolvencies can also take a long time to resolve – Lehman disputes are still before the UK and US courts. And as with all litigations, costs are always relevant, although courts are aware of keeping costs proportionate and not imposing unnecessary and unjustified costs on parties that may already be in financial difficulties. Usually, the main benefit of costs pressure is the secondary distress

market that can come in and acquire interests or fund litigations.

FW: Have you seen any common issues arising in corporate bankruptcy & insolvency processes in today's market? In what ways do these issues complicate bankruptcy litigation?

Boynton: An issue which is always there, but which is particularly acute in the current market, is the likely alternative to any bankruptcy and insolvency process and what assumptions a company and its advisers use when formulating this. Given the unique nature of the current recession, and potential or likely changes to consumer behaviour in light of COVID-19, it is far more difficult than usual for businesses to predict what their business will look like once the pandemic recedes. This makes it incredibly difficult to accurately forecast funding needs and to restructure effectively. There are two consequences of this. Firstly, there is large scope for debate about the alternative comparator for any creditor who wishes to object to a restructuring process. Secondly, it may well be that companies go through a process but receive only a temporary respite from their problems if their assumptions prove to be too aggressive.

Bagon: The significant level of fiscal stimulus and financial support provided by the UK government has led to a historic low number of corporate bankruptcies. There has also been a relaxation of wrongful trading rules and the temporary suspension of certain creditor enforcement rights. As a consequence of these measures, the comparatively small number of corporate insolvencies that have occurred have tended to involve enterprises that are no longer viable in a market in which there are few potential purchasers, resulting in the insolvent companies swiftly entering liquidation and dissolution. This trend has impacted bankruptcy litigation in two key areas. Firstly, there has been a scarcity of claims in the market. This is not an unexpected development as there is a natural lag between insolvency filings and the litigation of claims. Secondly, bankruptcy claims against directors for misfeasance or breach of fiduciary duty generally require the import of a reasonableness test. The unexpected and unprecedented challenges caused by COVID-19 may mean that it will be more difficult to establish that a director's conduct during the pandemic was unreasonable and for a claim to be upheld.

Whibley: The UK's restructuring plan, which includes a power to 'cram down' classes of creditors that have not voted in favour of the proposals, is a source of disputes – a key difference between restructuring plans and schemes of arrangement. To nobody's surprise, the power to cram down dissenting creditors has already become a source of disputes. An example is the unsuccessful challenge to the Virgin Active restructuring plan. Cram down requires parties to demonstrate that the affected creditors would be no worse off under the proposed plan than in the relevant alternative scenario. A group of landlords tried, without success, to persuade the court that they might be better off under the true alternative. Meanwhile, the court declined to sanction the Hurricane Energy restructuring plan, accepting a similar challenge. The need to establish and prove the relevant alternative looks set to be a common complicating factor where companies want to rely on cram down.

Kitt: Litigation funding has, over the last 10 years, given insolvency practitioners the ability to bring litigation that otherwise could never have proceeded. That has been a game changer and the global reach and availability of funding options is ever-expanding in today's market. But, with litigation funding comes complexity. First and foremost is the impact on net return. The significant percentage of damages that funders require by way of return can be off-putting. We are therefore seeing increased competition from the range of insurance products on the market, the use of assignments and law firms' appetite to take more risk. Second is speed. Funders require cases, their risks and their costs to be presented with some rigour. That is understandable and it is fair to say that funders are improving in streamlining their processes, but complex cases can still take some time to complete. Funders and insurers also increase the number of stakeholders standing behind the litigation and therefore add to the complexity of reporting obligations and the management of competing interests.

Huntriss: Bankruptcy and insolvency processes are usually cross-border, and

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so parties are continuing to have to see how their commercial outcomes can be delivered to take into account different requirements and procedures in different jurisdictions. It is increasingly rare to encounter a contentious insolvency which does not cross borders in this way. Brexit has complicated the position in terms of UK and European insolvencies, with parties having to work out through litigation how different UK restructuring tools will travel in the post-Brexit age. Recent decisions on restructuring plans have begun to give some guidance, but there are still unanswered questions.

> IT IS TRITE, BUT IMPORTANT, TO SAY THAT THE PARTIES NEED TO TRUST ONE ANOTHER. CREDITORS ARE GENERALLY GOING TO BE DISAPPOINTED AND OFTEN ANGRY THAT THEY WILL NOT RECOVER ALL THAT THEY ARE OWED IF A COMPANY ENDS UP IN AN INSOLVENCY PROCESS.
>
> RICHARD BOYNTON
> Kirkland & Ellis International LLP

Tabak: I am seeing more and faster pre-packaged bankruptcies in the US, and an increasing number of these pre-packs are moving within hours from filing to confirmation. These cases, from a variety of industries, are often paying general unsecured creditors in full, which obviously has the advantage of avoiding some disputes that would otherwise arise, including by mooting any clawback litigation. There are real benefits to pre-packs in efficiency, speed, and cost, particularly when a sizeable corporate bankruptcy costs tens of millions of dollars in fees. The downside to speed, as in other contexts, is a question of whether things are moving too fast to be done correctly and fairly to all. But unless and until a pre-pack is rejected or blows up badly post-confirmation, I think they are here to stay.

Rogan: Disclosure, valuation and entitlement to the restructuring surplus are core interlinked issues at the heart of today's restructuring market. The level of information which stakeholders have access to drives their ability to formulate a credible view on valuation, which in turn determines their entitlement to the restructuring surplus. Valuation is an art rather than a science and it is an uphill struggle for stakeholders to mount a credible valuation challenge in light of their asymmetrical access to information. Recent judgments show that stakeholders need to make a significant investment to mount a challenge and seek appropriate disclosure to ensure that they are able to put forward credible expert valuation supporting their position. To the extent that stakeholders are unable to demonstrate that they are 'in the money', there is very limited scope for a challenge.

Durrer: Choice of forum and venue can often play a material role in the outcome of bankruptcy litigation. When a stakeholder prefers an alternative forum to the one chosen by the debtor, for example, sometimes the stakeholder will pursue a litigation to alter the forum or venue. For instance, recently, the National Rifle Association (NRA) attempted to use bankruptcy to derail an effort by the New York state attorney general to investigate the organisation. Likewise, a Singapore holding company owning a variety of hotels in the US filed for Chapter 11 bankruptcy in Delaware, following which its lenders filed a motion to divert the cases to Singapore. Finally, in the Stoneway Capital case, the stakeholders were locked in a fight between whether the company's reorganisation would occur in the US or Canada. These efforts can complicate reorganisations due to the distraction and expense.

FW: How have recent court rulings impacted on the corporate bankruptcy & insolvency litigation space? How are the issues involved in such cases likely to affect how parties conduct themselves going forward?

Bagon: Recent litigation trends suggest that disgruntled creditors are increasingly unwilling to accept the first option offered by debtors and that the courts are increasingly putting debtors to task to demonstrate that there are no better alternatives available. When considering whether to sanction restructuring procedures, courts have traditionally focused on the legal rights that would be affected and been unwilling to consider the commercial terms of the restructuring on the basis that these are better assessed and evaluated by the sophisticated commercial participants directly. However, in recent decisions the courts have shown a greater appetite to probe commercial issues. This is particularly evident in the court's examination of the counterfactual position, often a base-case insolvency, against which the proposed restructuring is compared.

Tabak: While we are due for a significant US Supreme Court bankruptcy decision, perhaps on make-whole payments or third-party releases, there have been recent influential decisions on fraudulent transfers. Opinion diverges widely on whether fraudulent transfer law should apply to shareholders who received payments in a leveraged buyout. In

Merit Management, the Supreme Court seemingly narrowed the safe harbour for settlement payments that went through financial institutions as intermediaries, but it left open a big loophole where a financial institution acted as an agent for either the transferor or transferee. The Second Circuit busted that loophole wide open in the *Tribune* case. In recent Madoff litigation, the Second Circuit held that subsequent transfers made overseas are subject to claims under the Bankruptcy Code, and it heard arguments this year on the remarkably nebulous concept of good faith. The upcoming decision could have significant effects on fraudulent transfer law in all contexts.

Kitt: The cases around the sanctioning of restructuring plans have undoubtedly been the 'talk of the town' so far in 2021. But we have taken a keen interest in three UK Supreme Court judgments in the cases of *Manchester Building Society, Khan v. Meadows* and *AssetCo.* In circumstances of corporate collapse, the auditors, with their insured pockets, are often high up the list as litigation targets. These three Supreme Court decisions restate English law on how losses are to be assessed in negligence cases, framing a new test around a six-point plan. The most important take-aways for those bringing audit negligence cases in an insolvency context is being clear about the counterfactual test that is applied, the recoverability of trading losses, and whether in cases of the most clear and obvious fraud, damages will be reduced more than we have seen previously on account of contributory negligence. The interplay between the developing law in this area and the various government consultations into the future of the audit industry is an interesting area to watch.

Rogan: Restructuring processes depend on stakeholders being provided with sufficient information in order to allow them to make an informed decision as to how to exercise their vote on the process. Recent decisions have shown that the courts will carefully consider whether this obligation has been appropriately discharged. In relation to the English scheme, the court will be very slow to second guess the fairness of the commercial deal put before the scheme creditors, relying heavily on creditor democracy, provided that the vote is rational and representative of the class. However, the cross-class cram down mechanic within the new restructuring plan requires greater oversight to ensure whole creditor classes are not treated unfairly. This sets the scene for the potential for valuation disputes to become a more common feature in restructurings. At the same time as providing debtors with greater leverage, it also provides them with greater responsibility and may ultimately produce a more collaborative approach to devising equitable restructuring solutions which do not lead to value destructive valuation disputes.

Huntriss: We have a very proactive set of English judges in the insolvency litigation space. They are all relatively recent additions to the bench, and all bring a wealth of experience to the cases they preside over. Cases in the last year have been overseen by a very involved judiciary that is not afraid to call out bad party behaviour, and in particular parties not doing what they say they are doing. The judges are also willing to drive forward the legislative tools they are given, to address the practical holes in it. It is a great asset of the English court system.

Whibley: Virgin Active provides the test for whether a creditor in a cross-class cram down would be 'no worse off' than in the relevant alternative. This will be a key battleground on cram downs, and companies will focus on producing compelling evidence of the likely alternative, its consequences for dissenting creditors, and comparing those alternative outcomes with outcomes under the proposed plan. In Amigo Loans, the court declined to sanction a scheme of arrangement, accepting the Financial Conduct Authority's (FCA's) objections that some creditors lacked the necessary information or experience to appreciate the alternative options, or to understand the compromise they were being asked to make. This will likely increase companies' focus on how to communicate complex proposals to audiences lacking sophisticated understanding of financial restructurings, and what support or guidance it might be appropriate to offer.

> "IN COMPLEX CASES, A VIABLE SOLUTION DEPENDS ON THE UNDERSTANDING AND CREATIVITY OF THE TEAM OF DIRECTORS AND ADVISERS PUTTING THE PROPOSAL TOGETHER, AND THEIR SKILL IN EXPLAINING AND PROMOTING IT."
>
> KEVIN WHIBLEY
> Freshfields Bruckhaus Deringer LLP

Durrer: Recent litigation in the Neiman Marcus Chapter 11 filing may have a lingering impact on bankruptcy litigation. There, a member of the official committee of unsecured creditors actively engaged in a campaign to discourage a rival bidder from

bidding on assets that such member's hedge fund wanted to procure for itself. The rival bidder blew the whistle, the member was charged with fraud and pled guilty to one charge earlier this year. In May 2021, the member was sentenced to six months in prison. The member's attorney remarked that it was "unfortunate and in many ways tragic" that the member's actions resulted in a positive result for the stakeholders the member was convicted of betraying. We expect that this sentence may cause estate fiduciaries to be more rigorous and conservative when it comes to conflicts of interest in the context of fiduciary duties.

> THE CROSS-CLASS CRAM DOWN MECHANIC WITHIN THE NEW RESTRUCTURING PLAN REQUIRES GREATER OVERSIGHT TO ENSURE WHOLE CREDITOR CLASSES ARE NOT TREATED UNFAIRLY.
>
> ALEX ROGAN
> Eversheds Sutherland LLP

Boynton: Major lessons from recent judgments include the following. First, have an alternative to a restructuring plan. The company must ensure that this relevant alternative is robust and defensible; both Amigo's scheme and Hurricane Energy's restructuring plan fell at this hurdle, with the court declining sanction. Second, courts have repeatedly emphasised the need for adequate disclosure to be made to interested parties who might wish to participate in the process. To the extent that there ever was any leeway in this respect, there is not now. Third, in terms of timetable, debtors must strike a delicate balance: avoid holding a proverbial gun to the court's head in seeking judgment urgently against the backdrop of a 'burning platform', and yet avoid going so early that the court concludes the debtor still has options and should not be permitted prematurely to bind dissenting stakeholders, as in *Hurricane*.

FW: How would you characterise the evolving dynamic between various creditors in the corporate bankruptcy & insolvency process? To what extent do you see multiple parties collaborating to reach a viable solution?

Kitt: We do not regard the dynamic as between creditors, as opposed to between creditor and debtor, as a particularly evolving one. In our experience, creditors still generally act in their own interests to maximise their recoveries rather than trying to work as a collective to maximise returns. That is a generalisation, however, and it does depend on the make-up of the creditor group. For example, we have seen more collaboration among financial institutions as creditors than with creditors from other industries. The UK restructuring plan procedure, which involves placing creditors into classes, requires collaboration among that class, albeit potentially at the expense of other classes that become adverse and can, under this new procedure, be 'crammed down'. It is very possible that we will see more collaboration among creditors given the dire debt situation that COVID-19 is likely to create.

Rogan: A notable feature of the recent CVAs and restructuring plans is that landlords are becoming more organised. Commercial landlords in the UK face an unprecedented level of outstanding rental arrears which have been reported to be in the region of £6bn. This is forcing landlords to be more active in the face of restructuring proposals and to challenge debtors with counter valuations, as well as tabling their own counter proposals to secure a seat at the negotiation table and ensure that they are in a position to capture the restructuring surplus, rather than allowing it to leak to existing equity or third parties.

Huntriss: Parties will collaborate, and courts will continue to encourage that, but to an extent creditor classes will always clash and fight for their value, particularly where the value breaks. Collaboration, encouraged through court and officeholder processes, will have most use in circumstances where the interests of the parties can somehow be accommodated. Proactive advisers can really assist.

Whibley: The cram down available in restructuring plans increases potential creditor disunity. That is against a backdrop of increasingly frequent disagreements between landlords and other unsecured creditors, particularly in CVAs. There has not been much obvious effective collaboration among landlords, and that may be a reason why they have had little success. By contrast, the aircraft lessors in the Virgin Atlantic and Malaysia Airlines restructurings have used common counsel and taken a united position, and they may be happier with their outcomes. Constructive collaboration between creditors with different interests is not always a realistic expectation. In complex cases, a viable solution depends on the understanding and creativity of the team of directors and advisers putting the proposal together, and their skill in explaining and promoting it, as well as on an open minded

and pragmatic approach from creditors and other stakeholders.

Durrer: Chapter 11 bankruptcy is a fishbowl and a crucible. As a fishbowl, it provides transparency and therefore trust and confidence. As a crucible, it can forge consensus by bringing all stakeholders together in one community and leveraging that transparency for the good. This routinely happens even in contentious situations such as in the Purdue Pharma or Neiman Marcus Chapter 11 cases. That said, we are witnessing two different evolutions, one good and one bad. In the face of the pandemic, we have happily seen creditors supporting borrowers in a crisis that was no fault of management. On the other hand, due in part to the lack of a true downcycle since the turn of the century, some financial institutions' representatives lack the creativity and intuition that comes from experience. That can make a negotiated collaboration more difficult to achieve.

Boynton: We have seen many situations where ad hoc groups have been formed at an early stage. If such groups are formed quickly and are material, they can have a material effect upon the restructuring process and provide a company with a counterparty with which to negotiate key aspects of its plans. Such groups, provided they speak with a common voice, can be incredibly effective. We have seen much less intercreditor collaboration. This may be unsurprising given different and perhaps directly competing interests, but we have not seen, for example, classes of creditors joining forces to propose a different alternative to liquidation from that proposed by the company. The relationship between companies and their landlords remains, as a sweeping generalisation, difficult; the threat of a CVA, or restructuring plan, has done little to encourage collaboration, in our experience.

Tabak: Official committees of unsecured creditors serve an important role in US bankruptcies because individual creditors often do not have an incentive to closely monitor a bankruptcy case, much less take action, due to insufficient resources or financial interest in the bankruptcy. Through the committee, different creditors and creditor groups can collaborate. In that regard, it is critical that the committee represent all the major groups of creditors. Unfortunately, the selection of the committee by the Office of the United States Trustee is an opaque process. Sometimes, the committee can be dominated by a single type of creditor, which often leaves other creditors without a genuine voice. I am also seeing ad hoc groups of creditors forming, but these are generally groups of creditors, like bondholders, who have sufficient stakes and resources to act individually and are doing so collectively to share expenses.

Bagon: Unlike the US bankruptcy code, in England creditor committees are seldom formed outside of the largest corporate insolvency cases. Creditors generally rely upon the appointment of impartial and independent officeholders to protect their interests in a context in which creditor committees' powers are largely advisory. This often means that creditors do not feel the need to incur the time and cost associated with participating in a creditors committee. In contrast, due to the debtor-in-possession model under Chapter 11 proceedings, creditor committees are commonly used to hold debtors to account, and committees are empowered to appoint independent advisers to assist with this process. In a restructuring context, it is relatively common for lenders and noteholders to form committees with differing levels of formality. The motivation for forming creditor committees in restructurings is often to create 'strength by numbers' leverage with committee members collectively holding the requisite level of votes to carry or block a consensual restructuring.

FW: With many parties emerging unsatisfied from a corporate bankruptcy & insolvency dispute, what are the most significant factors that need to be observed to reach as positive an outcome as possible for all those involved?

Tabak: The most significant factor, by far, in achieving a positive outcome for involved parties is whether a bankruptcy is likely to end with an ongoing business. If so, parties can focus on increasing the size of the pie rather than simply fighting for the pieces of it. If the parties believe that they have a role to play with a reorganised entity, bankruptcy litigation can result in more consensual resolutions because the process lends itself to compromise, the experienced participants are skilled

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and creative in finding compromises and, unlike what we often see in non-bankruptcy litigation, the cause of the dispute is more likely to be about finances than emotions and personal animus, which often get in the way of settlements. Transparency is a significant secondary factor in making compromise possible, because parties need to feel confident in their decision to pursue a long-term outcome with a reorganised entity.

> ONCE GOVERNMENT FUNDING BEGINS TO BE WITHDRAWN, WE WILL START TO SEE WHICH BUSINESSES ARE IN CRISIS AND WHICH ARE ABLE TO RESTRUCTURE AND SURVIVE.
>
> FIONA HUNTRISS
> Boies Schiller Flexner LLP

Whibley: Pragmatism is arguably the most significant factor. In insolvency, nobody is getting what they want. For many creditors the best available outcome will involve being paid less than they are owed. If a party has enough exposure to an insolvency for it to be worthwhile investing in optimising the outcome, they need to pick legal, commercial and financial advisers who will approach these matters in a creative and flexible way, supporting them in spotting and implementing the best solution. It is unlikely to be good enough to simply litigate aggressively. Often the company or its shareholders and supporters are making new money available and dissenting creditors simply say they do not agree, or the offer is not good enough. Dissenting creditors should consider carefully whether their position would be stronger if they offered to participate in new money, either alone or with one of the myriad funds seeking scarce distressed investment opportunities.

Boynton: It is trite, but important, to say that the parties need to trust one another. Creditors are generally going to be disappointed and often angry that they will not recover all that they are owed if a company ends up in an insolvency process. A company needs to recognise that and ensure that creditors understand that the alternative to a company's proposal would be even worse for them: and that means open, honest communication about what the company can and cannot afford at an early stage. Once creditors understand what is, and is not, possible, it is important that they are realistic about the position. It is difficult for a company to negotiate with creditors who refuse to accept that difficult decisions must be made, and the almost inevitable result of that dynamic is less communication, a process which has less support, a potential challenge and more money spent on legal fees for the company and creditors.

Durrer: The factors that are most observed in successful resolutions of insolvent or distressed company situations are candour, pragmatism and out-of-the-box thinking. Candour or transparency creates a level playing field where every stakeholder shares equal access to information. Pragmatism represents real-world problem solving. The parties, armed with the same foundational information, must approach the situation realistically. This includes an understanding or awareness of timing and what various parties can, and cannot, agree to or perform. Finally, creativity is often required to bridge those last few gaps.

Huntriss: Early communication, continued through the process, can help parties reach a positive conclusion. Alongside that, you need an eye on commercial outcomes and not just legal outcomes. One of the most satisfying things about litigating in this space is the need to be commercial and drive 'real life' outcomes, and parties and their advisers are best equipped to do this when they keep their eyes up and consider the ever-shifting landscape rather than just being focused on the end of a court case.

Rogan: Stakeholder trust in the restructuring process is the key factor in achieving positive restructuring outcomes. This is achieved through early and transparent engagement with stakeholders. Stakeholders should be provided with sufficient information to allow them to engage actively and positively with the process, rather than being left behind as a problem to be dealt with at the implementation stage through a restructuring tool. Likewise, stakeholders need to engage constructively and realistically with each other to avoid mutually destructive outcomes.

Bagon: Successful restructurings require fulcrum creditors to agree a meaningful compromise. Consequently, the first step of a restructuring process involves determining where value breaks, as this in turn determines where the fulcrum creditors lie in a capital structure. There is no single established and recognised methodology under English law for establishing the value of a distressed business. It is therefore important at the outset for the debtor and creditors to agree in principle the value of the underlying business. A significant number of bankruptcy disputes in early-stage

restructurings arise from disagreements regarding whether certain classes of creditors are 'out of the money' and can therefore be disregarded for the purposes of restructuring discussions. This can lead to a stalemate position, particularly in structures where the security trustee is caught in the middle of a creditor dispute.

Kitt: I agree with the question to the extent that it is an obvious truth that in an insolvency scenario, many creditors will suffer losses that cannot be recovered either at all, or in part. They therefore start from a position of disappointment. To lift that disappointment, the process then becomes one of managing expectations, regular communication, collaboration with other stakeholders where that is possible, being clear on potential risk and reward, making the costs of recovery actions as low as possible, and creativity and agility in potential recovery techniques and claim possibilities. Litigating over schemes or restructuring plans has a different dynamic because there is a real hope that the underlying business can be saved – still the creditor may be looking at less than a full recovery, but it is a more positive scenario than litigating post liquidation because the whole point is that the creditor should be less worse off as a result of the process.

FW: How do you expect the corporate bankruptcy & insolvency litigation arena to unfold in the months ahead? What overriding trends and developments will continue to dominate this space?

Whibley: Two big issues to consider are the economic changes caused by the COVID-19 pandemic, and the economic and legal changes caused by Brexit. Regarding COVID-19, England is reopening but much has changed, and it appears many people will continue to work at home some days each week. That means change for the economic ecosystems in English cities and towns. It is difficult to predict how this will play out, but one foreseeable consequence is commercial landlords will continue to be squeezed in financial restructurings. Brexit's economic fallout is not yet visible because there has been a pandemic obscuring our view. An immediate legal issue is that the legal basis for recognising new English insolvencies in the EU and vice-versa has not yet been resolved. That sounds like a very technical legal issue, but for complex cross-border insolvencies it is a potential source of doubt and therefore dispute.

Boynton: We expect restructuring plans and schemes generally to remain the preserve of larger companies, with CVAs being the tool used most often in the mid-cap space. A much higher percentage of such processes than previously are being challenged and we see that trend continuing. A major UK development will be the introduction of a binding arbitration scheme for rent arrears in periods in which the tenant was forced to close owing to COVID-19 restrictions. More broadly, a key question is how and when governments will lift temporary pandemic-related support measures for companies. This includes not only insolvency-related and forfeiture restrictions, but also government-backed loans, tax reliefs and furlough schemes, among others, against a backdrop of rising interest rates over the medium term. It is clear that temporary support cannot last forever, but also that simultaneous, swift withdrawal of support would likely lead to significant increases in insolvencies. The unwinding of current measures will be a critical theme in the coming months.

Durrer: We expect the COVID-19 pandemic to have a lasting impact on how bankruptcy litigation is practiced. Specifically, we anticipate that some measure of virtual hearings and status conferences will continue for the foreseeable future. The benefits of such an approach are obvious: there are huge savings in terms of time and professional fees. The disadvantages are more nuanced. First, virtual hearings substantially impair the parties' ability to settle disputes 'on the courthouse steps' or in the corridor outside the courtroom. Second, some courts have already adopted procedures whereby parties can determine for themselves whether they wish to participate in person or remotely. Just as with telephonic participation in live court hearings in the past, the party who participates remotely is at a material disadvantage in the proceeding. It will be interesting to see which courts continue remote hearings and in what fashion.

Huntriss: There are going to be major developments. We are going to start to see the true financial impact of the pandemic, which will inevitably create a huge amount of insolvency and bankruptcy litigation. Once government funding begins to be withdrawn, we will start to see which businesses are in crisis and which are able to restructure and survive. Any increase in interest rates will also have a significant impact. All of these things will continue the trends of aggressive creditor and debtor behaviour to squeeze value, using the full armoury that is available to them, including UK schemes of arrangement and restructuring plans. On top of all of this, we are going to continue to see the impact of Brexit, as the insolvency community reacts and learns how English insolvency and restructuring tools travel across borders.

Rogan: The restructuring plan will come to the fore as the restructuring tool of choice for medium as well as large cap companies. This may take some time as the parameters of this new restructuring tool are tested in large cap restructurings, and a body of judicial precedent is developed around the application of principles relating to the fairness of restructuring plan proposals. This body of judicial precedent will provide practitioners crafting restructuring plan proposals with greater certainty around their parameters, minimising execution risk and cost. On the international restructuring front, Brexit remains a spectre over London's position as an international restructuring centre. Recent judgments would suggest that the scheme of arrangement is capable of maintaining its position as the go-to restructuring tool of choice for cross-border restructurings. Nevertheless, it remains to be seen whether the restructuring plan will enjoy the same level of cross-border recognition and be able to deliver cross-

border restructurings with the same degree of certainty.

Bagon: Current trends suggest that bankruptcy litigation, particularly in relation to restructurings, is likely to remain an active area. This trend has been catalysed by the introduction of new restructuring procedures in the UK and debtors, often using the pretext of COVID-19 pursuing increasingly aggressive restructurings, which are being resisted and challenged by well-capitalised institutional investors. It is also anticipated that insolvency related litigation will increase once government COVID-19-related stimulus is withdrawn, and the relaxation of wrongful trading rules and the temporary suspension of certain creditor enforcement rights are reversed. This trend however, is unlikely to emerge for some time due to the lag between insolvencies occurring, officeholders conducting investigations and the identification and prosecution of claims. The large number of specialist litigation funders focused on bankruptcy claims should mean that claims with strong legal merits and good prospects of enforcement recoveries are likely to be taken forward. Consequently, courts and lawyers look likely to remain busy for the foreseeable future.

Kitt: The months ahead must see an end to the ban on winding up petitions and with that, however it is managed, is likely to come a deluge of actions. The courts will inevitably have difficulty coping with any sort of cliff-edge and no doubt forms of alternative dispute resolution (ADR) will be encouraged. A mandatory ADR process in the form of binding arbitration has been proposed to resolve landlord and tenant disputes over the now jaw-dropping levels of rent arrears. I think we will continue to see developments in the case law on the sanctioning of restructuring plans, particularly focusing on the 'relevant alternative' test, with the *Hurricane Energy* case potentially going to the Court of Appeal. Finally, the full extent of the impact of Brexit, and the loss of the EU Insolvency Regulation in the UK is yet to be seen. Will we see a shift in centre of main interests, additional legislation passed to fill the void, or will European courts in any event reveal a continued willingness to recognise English insolvency proceedings?

Tabak: The most obvious development will be process-related. I expect bankruptcy courts to move rather slowly and unevenly toward in-person proceedings. There is an incentive for courts, like the Houston bankruptcy court, that have seen a recent increase in large bankruptcies to be perceived as user-friendly by conducting entire cases remotely. I suspect that will continue, while Delaware and New York return to in-person proceedings more quickly. While the pandemic-influenced feeling of all being in this together will wane, I hope that, even without the personal contact that I consider so important, the general imperative toward consensus still helps litigators resolve issues when that is the best solution. ■

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