International Corporate Rescue

Published by:
Chase Cambria Company (Publishing) Ltd
4 Winifred Close
Barnet, Arkley
Hertfordshire EN5 3LR
United Kingdom

www.chasecambria.com

Annual Subscriptions:
Subscription prices 2017 (6 issues)
Print or electronic access:
EUR 730.00 / USD 890.00 / GBP 520.00
VAT will be charged on online subscriptions.
For 'electronic and print' prices or prices for single issues, please contact our sales department at:
+ 44 (0) 207 014 3061 / +44 (0) 7977 003627 or sales@chasecambria.com

International Corporate Rescue is published bimonthly.

ISSN: 1572-4638

ARTICLE

Bermuda's 'Light-Touch' Approach to Cross-Border Restructuring

Nicole Tovey, Partner, and **Benjamin McCosker**, Associate, Taylors (in association with Walkers), Bermuda

Introduction

Bermuda has no direct equivalent to the statutory moratorium against creditor action that applies to an insolvent English company in administration proceedings pursuant to Schedule B1 to the Insolvency Act 1986, or to an American corporate reorganisation pursuant to Chapter 11 of the United States Bankruptcy Code. This legislative gap has been enthusiastically filled by the Bermuda Supreme Court's interpretation of the power to appoint liquidators or provisional liquidators under section 170 of the Companies Act 1981 (the 'Act') as including the power to appoint provisional liquidators for restructuring purposes. This article explains how for almost twenty years now, *de facto* debtor-in-possession, management-led restructurings have been facilitated in Bermuda by reference to this bespoke restructuring regime.

'Light-touch' provisional liquidation for restructuring purposes

The power of the Bermuda Supreme Court (the 'Bermuda Court') to appoint provisional liquidators is typically employed in circumstances where a company's assets need to be preserved and protected pending the hearing of a winding up petition where there is evidence of actual or potential misapplication or dissipation of company assets. However, this provisional liquidation jurisdiction can also be invoked to assist in the context of cross-border restructurings in circumstances where provisional liquidators are appointed on a 'light-touch' basis.

The distinguishing feature of a Bermuda 'light-touch' provisional liquidation is that provisional liquidators are appointed – oftentimes on the company's own petition – to independently oversee a restructuring process, with a focus on protecting creditors' interests. The ultimate restructuring can manifest itself in various ways, although an equity injection by a 'white knight' investor, a purchase of distressed debt by a third party and/or a scheme of arrangement whereby the company makes a compromise or arrangement with its members and/or creditors pursuant to section 99 of the Act are typically involved. Regardless of what form the restructuring ultimately takes, the company has the benefit of a statutory moratorium, or stay, on proceedings being brought against the company which automatically arises upon the appointment of provisional liquidators and continues for as long as the provisional liquidators remain in office.[1] This is a particularly valuable protection for imperilled boards of companies in the zone of insolvency, where creditor threats to commence proceedings against the company can distract from the primary task of implementing a financial or operational restructuring to ensure that the company may continue as a going concern.

It is not the role of the 'light-touch' provisional liquidators to ultimately determine whether or not a certain restructuring proposal should be pursued. That is of course a question for the creditors and members of the company.

Typically, evidence should be shown to the Bermuda Court at the appointment stage that there is a viable restructuring proposal and a good prospect that certain creditors of certain value will be either supportive of the proposal or have indicated that they are willing to wait and see what the company will propose and accordingly do not wish for a winding up order to be made immediately. Subsequent to the appointment of the provisional liquidators, if the necessary creditor support cannot be obtained and a satisfactory restructuring proposal cannot be agreed upon, the provisional liquidators would report this to the Bermuda Court and, in most cases, a winding up of the company would ensue.

Jurisdictional foundation for the 'light-touch' provisional liquidation regime

The foundation for the provisional liquidation restructuring jurisdiction was set out in the 1999 judgment of Ward CJ (as he then was) in *Re ICO Global Communications (Holdings) Ltd* as thus:

Notes

1 Note that secured creditors may enforce their security notwithstanding the moratorium, except for in circumstances where a contractual standstill has been negotiated between the relevant secured creditors and the company.

> 'I am satisfied that the Court is given a wide discretion and had jurisdiction under section 170 of the Companies Act and Rule 23 of the Companies (Winding-Up) Rules 1982 to make such an Order. Under it the directors of the Company remained in office with continuing management powers subject to the supervision of the joint provisional liquidators and of the Bermuda Court'.[2]

In the 2006 decision of *Discover Reinsurance Co v PEG Reinsurance Co Ltd,* Kawaley J (as he then was) characterised the 'light-touch' provisional liquidation regime as part of a 'legal quid pro quo':

> '[I]n circumstances where no suspicions about the integrity of the directors really exist, the provisional liquidator is appointed as part of legal quid pro quo for receiving the benefit of the stay on proceedings that the appointment guarantees, Bermuda law presently lacking a formal equivalent of the US Chapter 11 regime or the English administration proceedings'.[3]

Later, in the 2016 decision *In the Matter of Up Energy Development Group Limited*, Kawaley CJ described the advantages of the Bermuda 'light-touch' provisional liquidation regime in the following terms:

> 'It is the involvement of JPLs, embedded with the restructuring troops, which relieves this Court of the burden shouldered by US Bankruptcy Court judges of resolving a myriad of disputes between the restructuring protagonists…All conflicts are typically resolved before the scheme document is finalized, out of court, with the JPLs playing a generally unheralded but crucial mediating role. They bring a high degree of efficiency and economy to Bermudian restructuring proceedings which would likely be lost in a proceeding without the usual appointment'.[4]

Most recently, in another decision of Kawaley CJ *In the Matter of Z-Obee Holdings Limited,* reference was made to the fact that the Bermuda Court 'had an established practice of appointing JPLs to manage a restructuring…', and that 'it is too well established today for this Court to depart from in the absence of full and compelling arguments for doing so…'. The then Chief Justice concluded with the remark that 'the winding up jurisdiction is still being used to fulfil the primary purpose of the winding up jurisdiction: protecting the best interests of the general body of unsecured creditors'.[5]

The 'light-touch' provisional liquidation regime in practice

The appointment of 'light-touch' provisional liquidators to a Bermuda company is preceded by the presentation of a winding up petition to the Bermuda Court, pursuant to section 163 of the Act. Such petition can be presented by the company itself, or by any creditor or contributory of the company.[6] The petitioner will simultaneously make an application by summons for the appointment of provisional liquidators, and will typically by that summons propose a form of order setting out the 'light-touch' powers to be granted.

In making its application for the appointment of provisional liquidators, the petitioner will identify its proposed appointees and typically adduce evidence as to their suitability for the role. The Bermuda Court will be astute to ensure that the proposed appointees are not only competent, but are also capable of winning the confidence of both the creditors and the company. As Hellman J observed in *In the matter of Opus Offshore Limited*:

> 'the efficiency of any restructuring within a provisional liquidation depend[s] in large part upon good will and collegiality reigning across the joint provisional liquidator and management restructuring teams'.[7]

Where there is a conflict between the petitioner (if not the company itself) and the company as to the selection of provisional liquidators, the Bermuda Court will have regard to the nominees' respective qualifications and experience, as well as the existing relationship (if any) between the nominees and the company and creditors and any potential conflicts which could arise therefrom. In the *Up Energy* matter, for example,[8] concerns were raised by the petitioner as to the independence of the company's nominee given their prior appointment by the company as independent restructuring advisers. In the event, the Bermuda Court appointed the petitioner's nominee as the Bermuda-based liquidator, and the company's nominees as the Hong Kong-based officeholders. This not only ensured that all relevant interests were evenly-represented by the provisional liquidators, but also facilitated the division and delegation of the very significant restructuring work required to be undertaken by the company, which was incorporated in Bermuda but had its operations

Notes

2 [1999] Bda LR 69 at [6].
3 [2006] Bda LR 88 at [20].
4 [2016] SC (Bda) 83 Com (20 September 2016) at [24].
5 [2017] SC (Bda) 16 Com (21 February 2017).
6 Section 163(1) of the Act.
7 [2017] SC (Bda) 14 Com (17 February 2017) at [73], citing with approval the *dicta* of Kawaley CJ in *Up Energy*, note 5 above at [11].
8 Taylors in association with Walkers acts for the joint provisional liquidators of Up Energy Development Group Ltd.

in mainland China and was listed on the Hong Kong Stock Exchange.

Ultimately, the choice of provisional liquidators is a matter for the Bermuda Court's discretion, and in exercising its discretion the Bermuda Court will elect the liquidators 'most likely to command the confidence of a majority of those who will seek to prove in the liquidation'.[9]

The powers of the provisional liquidator are not circumscribed by statute and instead are expressly set out in the court order appointing the provisional liquidator. Accordingly, there is scope for the provisional liquidation regime to be used with real flexibility in the context of a restructuring and the suite of powers which will be granted to the provisional liquidator will vary on a case-by-case basis depending upon how much control over the process the provisional liquidator is intended to have. Typical powers granted to 'light-touch' provisional liquidators in aide of a potential restructuring include the powers to:

1. approach, engage, consult and negotiate with third parties, shareholders and/or creditors of the company with a view to obtaining funding for a proposed restructuring;
2. liaise with creditors, management and shareholders of the company, as well as relevant third parties, with a view to implementing a scheme of arrangement to be entered into as between the company and its creditors and/or its members; and
3. make available to relevant third parties certain books and records of the company in order to facilitate a restructuring proposal, subject to acceptable confidentiality arrangements.

Alongside these usual powers will be certain duties owed by the provisional liquidators beyond the ordinary duty of provisional liquidators to preserve the *status quo* pending a determination by the Bermuda Court as to whether the company should be wound up. For example, the order appointing the provisional liquidators will typically require that the provisional liquidators will consult with the company on an ongoing basis with respect to the restructuring efforts under negotiation and their perceived prospects of success – as Kawaley CJ observed in *Up Energy*, one of the fundamental roles of the provisional liquidators is to 'give confidence to both creditors and the Court that the restructuring process which emerges is a credible one'.[10]

In all cases, the provisional liquidators, as officers of the Bermuda Court, must advise the Bermuda Court if they form the view that the proposed restructuring is no longer viable.

Company management will typically retain some degree of control over the day-to-day administration of the company during the period of provisional liquidation. The precise degree of control will depend upon the petitioner's desire to see the company's management remain involved. If there are allegations of fraud or other forms of impropriety on the part of the company's management, the Bermuda Court will not permit a 'light-touch' provisional liquidation to proceed.[11]

In the event that a successful restructuring is achieved, an order will be sought from the Bermuda Court for the dismissal of the winding up petition and the discharge of the provisional liquidators from office. However, if the restructuring is unsuccessful, the Bermuda Court will make an order for winding up and appoint permanent liquidators over the insolvent company.

Company-driven versus creditor-driven restructuring

A distinguishing feature of Bermuda's 'light-touch' provisional liquidation jurisdiction is that it can be invoked by either creditors or by the company itself, acting by its board of directors.[12] Oftentimes a straightforward creditor's petition will evolve into a company-driven provisional liquidation appointment and restructuring upon the company's opposition to the petition and demonstration that a viable prospect of restructuring exists which would be in the best interests of the company's stakeholders, in lieu of a winding up.

The order setting out the provisional liquidators' powers will necessarily reflect the manner in which they have been appointed and at whose instigation the appointment was made. Some 'light-touch' appointments will be 'lighter' than others. For example, orders for the appointment of provisional liquidators following the filing of a winding up petition by a creditor of a company will typically provide for comprehensive and low-level access by the provisional liquidators to the company's books and records, as well as entitling the provisional liquidators to receive advance notice of, be consulted prior to and sometimes attend meetings of the board and of company management.

Notes

9 *In the matter of Opus Offshore Limited*, above note 7, at [94] per Hellman J.

10 Note 4, above, at paragraph 28.

11 *Discover Reinsurance Co*, above note 3.

12 Compare the current position in the Cayman Islands, where absent a special resolution passed by shareholders or a specific authorisation in the company's articles of association, the directors of a company may not petition for the winding up of the company: *Re China Shanshui Group Limited* [2015] (2) CILR 255; see also *In the matter of CHC Group Ltd* (Grand Court, unreported, 24 January 2017).

What about foreign restructuring proceedings?

The 'light-touch' provisional liquidation regime in Bermuda has evolved alongside and in furtherance of the Bermuda Court's endorsement of the concept of modified universalism, or the recognition and assistance of foreign insolvency proceedings. In *Re ICO Global*, Ward CJ (as he then was) was faced with the all-too-familiar situation of an international liquidation with various actions being undertaken in many jurisdictions simultaneously. Speaking in support of the provisional liquidators' pursuit of a Chapter 11 plan of reorganisation, His Lordship wrote:

> 'this Court should co-operate with Courts in other jurisdictions which have the same aim in relation to the affairs of the company. It is not a question of surrendering jurisdiction so much as harmonisation of effort'.[13]

The Bermuda Court's view on the interaction between local insolvency proceedings and broader global restructuring efforts aligns with the position taken by Lord Sumption in the Privy Council appeal in *Singularis Holdings Limited v PricewaterhouseCoopers*, namely that the court of the company's incorporation should recognise that alternative, foreign forums may be most appropriate for orderly insolvency processes, and is at liberty to provide assistance to enable such foreign insolvency processes to continue expeditiously.[14] The Bermuda Court has consistently shown itself willing to make orders for the appointment of 'light-touch' provisional liquidators in order to assist the progression of a cross-border restructuring:

1. *In Re C & J Energy Service Ltd No. 42239* – The Bermuda Court made orders to effectively 'short circuit' the formal winding up process in circumstances where the company's affairs were being administered, and all known debt and equity interests had been extinguished, in Chapter 11 proceedings in the United States Bankruptcy Court for the Southern District of Texas, Houston (the 'Texas Court') and ancillary proceedings under the Canadian Companies Creditors Arrangement Act in Alberta, Canada;[15]
2. *In Re Matter of Energy XXI Ltd* – The Bermuda Court appointed provisional liquidators and shortly thereafter granted the provisional liquidators' application for a recognition order in relation to Chapter 11 proceedings underway in the Texas Court;[16] and
3. *In Re Z-Obee Holdings Ltd* – The Bermuda Court appointed provisional liquidators for restructuring purposes with the same broad powers already conferred upon them by the High Court of the Hong Kong Special Administrative Region.[17]

'Light-touch' provisional liquidation restructuring – the Bermuda advantage

The primary purpose of Bermuda's 'light-touch' provisional liquidation regime is to permit a company the time and breathing space to implement a restructuring, under the watchful eyes of the provisional liquidators and the supervision of the Bermuda Court, which may result in the return of the company to solvency and allow it to continue as a going concern for the benefit of all its stakeholders. The availability of this regime is a tremendous asset for companies incorporated in Bermuda and promotes certainty and predictability in cross-border restructuring matters, including in cases where the shares of the company in question are publicly listed or the company has its operations in jurisdictions other than Bermuda.

Notes

13 Above note 2 at [8].
14 [2015] 2 WLRC 971.
15 [2017] SC Bda 20 Com.
16 [2016] SC Bda 79 Com.
17 Above note 5.

International Corporate Rescue

International Corporate Rescue addresses the most relevant issues in the topical area of insolvency and corporate rescue law and practice. The journal encompasses within its scope banking and financial services, company and insolvency law from an international perspective. It is broad enough to cover industry perspectives, yet specialized enough to provide in-depth analysis to practitioners facing these issues on a day-to-day basis. The coverage and analysis published in the journal is truly international and reaches the key jurisdictions where there is corporate rescue activity within core regions of North and South America, UK, Europe Austral Asia and Asia.

Alongside its regular features – Editorial, US Corner, Economists' Outlook and Case Review Section – each issue of *International Corporate Rescue* brings superbly authoritative articles on the most pertinent international business issues written by the leading experts in the field.

International Corporate Rescue has been relied on by practitioners and lawyers throughout the world and is designed to help:

- Better understanding of the practical implications of insolvency and business failure – and the risk of operating in certain markets.
- Keeping the reader up to date with relevant developments in international business and trade, legislation, regulation and litigation.
- Identify and assess potential problems and avoid costly mistakes.

For more information about *International Corporate Rescue*, please visit www.chasecambria.com