New York vs London; **who will restructure Europe's hi yield loans?**

Continuing a series on the future of financial restructurings in Europe, Global Turnaround interviewed lawyers from a top global firm on who will be the winners and losers over the next few years; specifically, who will restructure the distressed European corporates who refinanced themselves since the financial crisis using the US high yield market?

Will it be UK-based advisers using the English Scheme of Arrangement? Or US-based firms using Chapter 11? Or a combination of local proceedings and US Chapter 15 recognition?

Here's the theory:

Many big European corporates that became distressed following the global financial crisis managed to stave off restructuring or even insolvency by refinancing in the US high-yield markets. Much of this activity was of the 'amend and pretend' variety. These corporates didn't tackle their underlying operational problems, but rather used the high-yield markets to 'kick the can down the road'.

However, when the time comes to refinance these high-yield issues, the very fact that these corporates have not tackled their underlying problems suggests that they will need restructuring.

So the questions are: Who will do this restructuring? With what tools? And in which venue?

Susan Kelly, Squire Patton Boggs

Nava Hazan, Squire Patton Boggs

London market advisers have done well since the global financial crisis using the ultra-flexible English law Scheme of Arrangement. Susan Kelly, head of Squire Patton Boggs' restructuring practice in the UK and Europe, notes that:

"The UK courts have in the past few years taken a ground-breaking approach when approving Schemes of Arrangement for non-UK companies, stretching from Europe to the Middle East and even Vietnam (with Vinashin).

"For instance, the 'sufficient connection' test linking a debtor with the UK has been progressively weakened," says Kelly. Even non-UK corporates with non-English loan documentation have been able to use Schemes.

"Secondly, Schemes are easy to enforce in the US if you can obtain Chapter 15 recognition."

Nava Hazan, a partner with Squire Patton Boggs in New York and an expert on Chapter 15 and cross-border insolvencies, says choosing where to anchor a restructuring "depends on the facts of each case and the specific goals of the restructuring." Chapter 11 has been used to restructure foreign corporates in numerous cases, most recently in the shipping industry.

However, Hazan acknowledges that, although Chapter 11 is an extremely effective tool to successfully restructure a company, one drawback to Chapter 11s are their cost, and that Chapter 15s may be cheaper and more efficient in certain circumstances.

> "But Chapter 15s lack at least one powerful aspect of Chapter 11," says Hazan.

Chapter 11 enables you to launch preference actions and fraudulent transfer actions under US law that are unavailable under Chapter 15. "These could be very important in a case," says Hazan.

"Practitioners have been very creative in their approach," she adds. "The US and UK common law systems are both very flexible."

The courts have been pretty liberal in allowing foreign corporates to avail themselves of the US and UK restructuring process, she says. "So you have opportunity to be creative and to restructure a company potentially in different countries."

Stephen Lerner, Squire Patton Boggs

Stephen Lerner, global head of Squire Patton Boggs' restructuring and bankruptcy practice, compares English law Schemes to US Chapter 11 prepacks, as all the negotiating is done beforehand, which can reduce the costs when compared to a typical Chapter 11.

Lerner's firm currently represents a gold mining company headquartered in Canada that has some of its mining operations in Elko, Nevada. When the company got into trouble it entered a CCAA proceeding in Canada together with a Chapter 15 in Reno, Nevada.

"Others might have filed for Chapter 11," says Lerner. But, he says, "we filed a Chapter 15 instead."

Hazan adds:

> "We counselled the debtor to use Chapter 15 because it would be more cost-effective than Chapter 11 in that particular case."

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In the event both a Chapter 11 and a foreign main proceeding are filed, a protocol is generally negotiated to enable the respective courts in each country to work together smoothly, says Hazan. "Judges have got used to this", she says, "especially for cases concerning the US and Canada".

And even when restructuring professionals may prefer to file in a large, well-resourced bankruptcy venue like New York or Delaware, says Hazan, often they are compelled to go elsewhere because of the statutory rules with respect to venue. Lerner stresses: "As a firm, we regularly work across offices, we aren't stuck in silos. That way we are more efficient in cross-border restructurings."

Chapter 11 reform: will it ever happen?

If so, will it make a big difference?

Lerner recalls a big reform attempt about 17 years ago by the National Bankruptcy Review Commission, a report was prepared, and nothing very significant came of it.

The last big reform came with the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA), which made Chapter 11 more creditor-friendly, says Lerner.

> "One big problem is that there is no lobby group for distressed companies."

"If you're a distressed company, the last thing you want to do is draw attention to your plight," he adds.

If you have recently emerged from trouble you don't want to draw attention to it. Whereas on the creditor side, says Lerner, you have banks, insurance companies and trade creditors, all with deep pockets for lobbyists in Washington.

For instance, says Lerner, one of the most significant changes in the BAPCPA reforms was the introduction of a strict limitation of 210 days after filing for the decision to extend a lease for a tenant or not.

"This does not give you a lot of time if you are a retailer, and you may have dozens or even hundreds of stores to decide on," he says. This has had serious consequences.

"There has not been a single retail bankruptcy since 2005 in which the company has not subsequently been sold or gone out of business."

This in turn has led to a backlash from lawyers representing debtors, says Lerner. "They want to level the playing field for debtors. But any change in legislation is likely to take a long, long time."

The Judiciary is keeping a close eye

Susan Kelly makes two final points: "Decision-making about which jurisdiction to anchor a restructuring in is becoming more sophisticated." Debtors take into account where best to deal with potentially difficult stakeholders like trade creditors and syndicates.

Secondly, says Kelly, "the Judiciary is keeping a very close eye on this area."

For instance, she mentions the recent financial restructuring of Zlomrex, a French financing vehicle for Cognor, a large Polish scrap metal and steel products group.

In February, Zlomrex completed the restructuring of 118 million euro of senior secured high yield notes due in 2014. The deal used an English Scheme to restructure New York notes. This was after Zlomrex moved its COMI from France to England to establish a sufficient connection with the UK. At least one of the noteholders was within the English jurisdiction too.

The Scheme documents proposed to waive the need for a Chapter 15 application in the US. The Judge made it clear he was uncomfortable with that, says Kelly.

He did not want to allow a creditors' meeting to consider approving a Scheme which would not be effective in the US. The best way of confirming that a Scheme is going to be effective in the US is to obtain Chapter 15 recognition for it. Making an English Scheme involving significant US interests conditional upon seeking Chapter 15 recognition is a good mechanism for reconciling the two jurisdictions.

In other words, the Judge did not want to give any US counterpart "the impression of blithely overriding New York law rights and any legitimate interests of the New York court" says Kelly.

After the creditors' meeting and sanction hearing, Zlomrex's advisers applied for and obtained Chapter 15 recognition for the Scheme, presumably influenced by the judge's remarks.

Kelly concludes that restructuring professionals on both sides of the Atlantic will have to take great care of these subtleties if they want to compete in this particular arena.

Chapter 11 filings fall by a third

If you thought the US bankruptcy market was quiet, it just got even quieter. The latest figures for Chapter 11 filings show them falling by 34 per cent in July 2014 compared to the same period last year.

This comes against the background of a general improvement in the US economy.

Total bankruptcy filings in the US, including individual as well as commercial, fell 12 per cent in July 2014 over July of last year, according to the American Bankruptcy Institute (ABI).

Total commercial chapter 11 filings fell by just over a third to 357 filings in July 2014 from the 539 commercial filings in July 2013.

Samuel J. Gerdano, ABI executive director, commented:

"Consumers and businesses continue to steer away from the financial relief of bankruptcy amid high filing costs and low interest rates."

> "Bankruptcy filings for this year will likely fall below 1 million for the first time since 2007."

Chapter 11 filings in July also fell by 26 per cent compared to the previous month, when 481 debtors applied for bankruptcy protection.

No wonder so many American law firms are opening restructuring and insolvency practices in London and elsewhere in Europe. There are thin pickings at home.