Home Thoughts, From Abroad - Restructuring Recognition (and Recognition of Restructuring)

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Where a company's liquidation is necessary, deciding who or where is best placed to administer an orderly wind down for the benefit of creditors can be difficult: the shortfall of assets in an insolvency will highlight jurisdictional differences in approach as to questions of priority, frequently territorial rather than universalist.

However, certain restructuring processes have by necessity been forged under the banner of a liquidation process[1], in which case the appropriateness of a particular jurisdiction's primacy can be in danger of distortion. A tension can certainly arise if a debtor company espouses the possibility of a restructuring for which it needs negotiation breathing space; but creditors prefer a winding up before further asset erosion and/or to investigate matters leading to the company's present predicament: where that division is evident across two different jurisdictions the issue is underscored.

The global trend, including in "creditor friendly" jurisdictions, is towards corporate rescue where appropriate and available. For jurisdictions with more anachronistic frameworks, it is nevertheless desirable for an approach to be adopted that can facilitate restructurings, albeit not at the expense of creditors when an abuse of claims moratoria is evident.

Accordingly, it is preferable for courts to avoid limiting the application of recognition principles to full-blown liquidations:

"… even without a winding up, the court could, on ordinary principles of private international law, have recognised as a matter of comity the vesting of the company's assets in an agent or office-holder appointed or recognised under the law of its incorporation."[2]

Introduction of the restructuring officer regime in the Cayman Islands[3] highlights the ongoing importance of recognition outside liquidation, albeit under the umbrella of laws relating to insolvency proceedings.

COMI Island - development of recognition approaches

Since the general retreat from an expansive view of modified universalism in 2014 by the U.K.'s Privy Council decision in *Singularis*[4], jurisdictions have continued to consider adoption of the UNCITRAL Model Law on Cross-Border Insolvency (the **"Model Law"**), which contains provisions regarding recognition of foreign insolvency proceedings by an adopting jurisdiction; and some divergence from the U.K.'s common law position has been seen.

Prior to Singapore's adoption of the Model Law, the Singapore High Court in *Re Opti-Medix*[5] recognised a Japanese bankruptcy trustee appointed to companies incorporated in the BVI, relying on common law principles. However, the recognition was considered available as a result of the company's centre of main interest (**"COMI"**) (a concept available under the Model Law), whereas the common law had traditionally recognised foreign insolvency processes in the relevant company's jurisdiction of incorporation; and the Singapore High Court effectively dismissed Lord

1. For example, Bermuda; (until replacement with a new restructuring officer regime) the Cayman Islands; and (until the Hong Kong Court of Appeal's decision in *Re Legend International Resorts Ltd* [2006] 2 HKLRD 192) Hong Kong have all utilised light-touch provisional liquidation regimes to enable restructurings to be implemented with the benefit of a moratorium on creditor claims
2. Per Lord Sumption in *Singularis Holdings Limited v PricewaterhouseCoopers* [2014] UKPC 36 at [12]
3. See the Cayman Islands Companies (Amendment) Act, 2021, which came into force on 31 August 2022
4. See footnote 2
5. [2016] SGHC 108

Collins' doubt expressed in *Rubin v Eurofinance SA*[6] that it would be open to courts to introduce a new basis for recognition of foreign insolvency proceedings at common law.

Application of a COMI test gives rise to a question as to whether it should be supplemental to, or in place of, the jurisdiction of incorporation test. The consideration becomes particularly pertinent in circumstances where liquidators are appointed in both the jurisdiction of incorporation and an alternative COMI jurisdiction, when the question of which test takes precedence will arise. This also leads to the compelling question: would a jurisdiction that asserts that the COMI test supplants, and/or is given precedence over, any incorporation test therefore accept that it should recognise a foreign liquidator of a company incorporated in its own jurisdiction?

In the *Global Brands* case[7], the Hong Kong court indicated that if a liquidation is not taking place in the relevant company's COMI, it would expect to decline recognition and assistance sought in Hong Kong unless the liquidator is appointed in the company's place of incorporation, in which case "managerial assistance" could be given, provided that the application is limited to recognising the liquidator's authority to represent the company and seeking orders that are incidental to that authority (otherwise, only the recognition and more limited, specifically prescribed assistance may be given).

The shift in recognition approach may to some degree be perceived as the result of concerns over potential abuses of light touch provisional liquidation arrangements merely to gain a moratorium in circumstances where no real restructuring is being pursued. However, there is a limited batch of such cases and it is understood that *bona fide* restructurings with creditor support will continue to find assistance in the courts. The COMI based approach in Hong Kong is likely driven more particularly by the permission under the Mainland-Hong Kong insolvency cooperation arrangement[8] for Mainland courts to recognise Hong Kong appointed liquidators over companies whose COMI is in Hong Kong.

Common law recognition for restructurings

There is nothing surprising in the proposition that recognition and assistance may be applied in relation to foreign insolvency processes to implement debt restructurings for going concern businesses rather than liquidation; but perhaps trying to force certain of the underlying recognition principles into restructuring processes involving liquidators has muddied some of the waters.

In *Singularis*, Lord Collins noted[9] the common law principle that assistance may be given to foreign office-holders in insolvencies with an international element and cited the English court's stated position with regard to the United States' debtor-in-possession regime, Chapter 11:

"This court … will do its utmost to co-operate with the US Bankruptcy Court and avoid any action which might disturb the orderly administration of [the company] in Texas under Chapter 11" Banque Indosuez SA v Ferromet Resources Inc [1993] BCLC 112, 117."

Reforms to the Cayman Islands restructuring and insolvency legislation were welcomed into force on 31 August 2022. The amendments to Part V of the Cayman Islands Companies Act (**"Companies Act"**) introduced a new restructuring officer regime available to companies in financial distress, which can be accessed without the need to present a winding up petition to the Grand Court of the Cayman Islands (the **"Cayman Court"**). Upon filing the application seeking the appointment of restructuring officers, companies will be able to obtain an immediate and standalone restructuring moratorium on unsecured creditor action which will have extraterritorial effect (as a matter of Cayman Islands law), within which a restructuring may be proposed and implemented (by way of a Cayman Islands scheme of arrangement, a restructuring process in any foreign jurisdiction or consensually, as between affected stakeholders).

Whether a Cayman Court appointed restructuring officer will be recognised in a foreign jurisdiction is a matter for the relevant foreign court. However, the substantial similarities between the new restructuring regime and the previous provisional liquidation process through which restructurings were latterly and successfully implemented suggest that restructuring officers appointed under the amended Companies Act will be afforded recognition and assistance in jurisdictions that have implemented the Model Law in some form, such as New York.

The recent ruling in *In re Modern Land (China) Co Ltd*[10] (**"Modern Land"**) by the United States Bankruptcy Court for the Southern District of New York confirms the comity shown to foreign insolvency proceedings by the US Bankruptcy Court and that a scheme of arrangement properly

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6. [2013] 1 AC 236
7. *Provisional Liquidator of Global Brands Group Holding Ltd v Computershare Hong Kong Trustees Ltd* [2022] HKCFI 1789
8. Record of Meeting on Mutual Recognition of and Assistance to Bankruptcy (Insolvency) Proceedings between the Courts of the Mainland and of the Hong Kong Special Administrative Region
9. At [19]
10. *In re Modern Land (China) Co.,* 22-10707 (MG) (Bankr. S.D.N.Y. July 18, 2022)

sanctioned by the Cayman Court is able to compromise and discharge debt obligations that are governed by New York law.

Having obtained the Cayman Court's sanction of its scheme of arrangement with certain creditors, Modern Land filed a motion in the United States Bankruptcy Court to have the scheme recognised as either a foreign main or foreign non-main proceeding pursuant to Chapter 15 of the U.S. Bankruptcy Code. However, between the scheme process being initiated in the Cayman Islands and the scheme convening meeting being held, the Hong Kong Court of First Instance handed down two decisions, the inferences of which might have affected Modern Land's ability to restructure successfully its relevant notes obligations via the Cayman scheme of arrangement (as a matter of New York law). The first was *Rare Earth*[11], followed by *Global Brands*[12].

The fact scenario in *Modern Land* was essentially the same as the offshore scheme scenario described in Harris J's obiter comments in *Rare Earth*, in which His Lordship suggested that the Hong Kong Court would not treat the New York law debt as being discharged by a Cayman Islands scheme of arrangement coupled with Chapter 15 recognition in the United States, on the basis that the rule in *Gibbs*[13] requires the substantive alteration of contractual rights to be sanctioned by some substantive provision of the relevant law of the debt obligations and that recognition under Chapter 15 operates procedurally to prevent action by a creditor against a debtor's property in the United States, but does not appear as a matter of U.S. law to discharge the debt.

However, in *Modern Land*, Judge Martin Glenn confirmed that an order made pursuant to Chapter 15 can discharge U.S. law governed debt as a matter of U.S. law; and noted[14] the debtor's argument that:"*…denial of recognition of the Debtor's COMI in the Cayman Islands may leave the Debtor "with the alternative of converting a highly consensual Scheme into a Cayman liquidation in an effort to obtain such chapter 15 recognition at a later date.*" … [and] that this "*…would not maximize the value of the Debtor's assets, as it would divert additional funds towards an entirely new insolvency process in an effort to potentially achieve the relief requested…" in the Motion. (Id.) Such an outcome would clearly diverge from Chapter 15's stated goal of maximizing the value of the debtor's assets, as well as facilitating the rescue of a financially troubled business. Further, recognition of the Cayman Proceeding would promote cooperation between the American and Cayman courts, by helping facilitate the Cayman Proceeding and maximizing the chances of a successful reorganization.*"

It was indicated that it was an "incontrovertible" fact that the holders of the relevant notes understood Modern Land is a Cayman Islands company and that those holders expected its debts would be restructured pursuant to the law of the Cayman Islands. With over 99% in number of holders of the notes to be restructured attending and voting at the convening meeting representing approximately 95% in value of the outstanding principal of the notes, Judge Glenn found the "*definitive creditor expectations and overwhelming creditor support solidify a finding of COMI in the Cayman Islands*".[15]

It was noted that Modern Land also had substantial debt governed by Hong Kong law and the judge found that "*[t]he Court has no reason to address the COMI of any insolvency or scheme proceeding involving creditors with claims other than the holders of the Existing Notes [which were governed by New York law]. Creditor expectations in such a case would point to a COMI somewhere other than the Cayman Islands*".[16]

Canny Cayman

The new standalone restructuring moratorium introduced by the recent amendments in the Cayman Islands restructuring and insolvency legislation is specifically included in Part V of the Companies Act with a view to ensuring that the proceeding will be "*pursuant to a law relating to insolvency*" for the purpose of the Model Law. The appointment of a restructuring officer requires not only that the company is or is likely to become unable to pay its debts on a cash flow basis but also that there is an intention to present a compromise or arrangement to creditors of the company (or classes thereof) and the procedure is collective given the effect of the moratorium on all unsecured creditors. It is anticipated that Chapter 15 recognition of the restructuring officer proceedings and corresponding moratorium in the United States will be available on a similar basis to that routinely given in respect of light-touch provisional liquidator restructurings previously; and the procedure's inclusion within the Cayman Islands' restructuring and insolvency laws provides the opportunity for recognition and assistance by English courts pursuant to section 426 of the Insolvency Act 1986. Further, English law governed debt may now be capable of compromise via a Cayman Islands restructuring officer scheme

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11. *Re Rare Earth Magnesium Technology Limited* [2022] HKFCI 1686
12. See footnote 7
13. *Antony Gibbs & Sons v La Société Industrielle et Commerciale Des Métaux* (1890) 25 QBD 399 – the principle drawn from this case is broadly that a debt governed by one law cannot be discharged or compromised by a foreign insolvency proceeding under another law
14. Page 28 of the judgment
15. Page 31 of the judgment
16. Page 35 of the judgment

of arrangement[17] and section 426 recognition, as the restructuring officer regime is akin to English administration (which would have the effect of overriding the application of the rule in *Gibbs*).

Common law recognition should be available in other relevant jurisdictions but the degree to which assistance, including a moratorium, will be available will depend on the relevant jurisdiction in which it is sought and whether an equivalent restructuring moratorium is available there.

In *African Minerals*[18], the Hong Kong court was prepared to assume that assistance could be granted to English law administrators (rather than liquidators), although the court left that point open and refused assistance broadly because Hong Kong does not have available an equivalent moratorium on enforcement of security. Whilst Hong Kong does not have an equivalent to English law administration, the moratorium that arises upon commencement of a Hong Kong provisional liquidation is arguably equivalent to that upon commencement of a Cayman restructuring officer appointment: neither affects the rights of secured creditors (where English administration and Chapter 11 proceedings impede enforcement of security). Accordingly, there are reasonable arguments to assert that recognition and assistance of a restructuring officer process should be possible in Hong Kong.

Further, section 104(3) of the Companies Act has also been amended to allow a company to apply for the appointment of provisional liquidators more generally. It is conceivable that one basis on which such an application would be made is with a view to increasing the likelihood of recognition and assistance in a foreign jurisdiction if this is deemed difficult for Cayman Court appointed restructuring officers (for example where a provisional liquidation restructuring regime remains a more settled basis, based on extant case law).

Conclusion

So far as possible, COMI assertions to avoid suspect restructuring arrangements or for more protectionist considerations should not preclude ongoing recognition and assistance in respect of genuine rescue processes that have material creditor support.

17. That is, under sections 91I and 91J of the Companies Act
18. *Joint Administrators of African Minerals Ltd v Madison Pacific Trust Ltd* [2015] 4 HKC 215

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