Autumn 2020

IFLR

Going round in circles

Confusion over the Libor transition has seen banks waiting for corporate demand before making products available, and corporates waiting to be advised by their banks. With just over a year to go, time is of the essence

Capital raising & Covid-19

Indian bank consolidation

IFLR1000 India & China awards

Special report: Restructuring & insolvency

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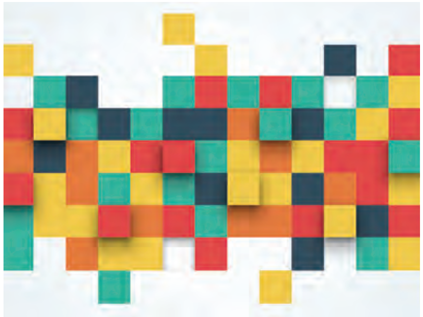


IFLR

Autumn 2020 Vol 88

SUBSCRIPTIONS

UK/Asia hotline
Tel: +44 20 7779 8999

US hotline
Tel: +1 212 224 3570

Email: hotline@euromoney.com

“If I go to one of the 16 banks in our group and ask for a loan, it is still predominantly on a Libor basis”

ABP treasurer Shaun Kennedy explains the Libor transition issues on page 18

The blame game

CONTRIBUTING EDITORS

While regulatory and interest rate specialists – including many IFLR readers – have been living and breathing little else but benchmark reform for some years now, it's not the case for everyone affected.

As John Crabb finds in this issue's cover story on page 18, corporate treasury teams are lagging behind financial services in their transition efforts. That's both understandable and fair, to an extent, considering the limited exposure most have. But for large corporates with multiple financing arrangements, there is plenty of work to be done.

Along with any big market change – and any accusation of a lack of effort – there will be further finger-pointing. In this case, it's corporates claiming that they haven't been offered anything but Libor products from their banks. Meanwhile, banks argue that it's not their role to tell their clients what to do, so if they don't ask for Sonia or SOFR-linked products, the banks won't produce them.

Either way, it would be objectively beneficial for corporate treasurers to be involved in the transition wherever possible. Work towards term replacement rates in various jurisdictions – which regulators initially said would not be an option – is testament to this. Benchmarks are used by a wide variety of market participants for a huge variety of purposes. It's important that all of these voices are heard – and the clock is ticking.

Enjoy the issue,

Lizzie Meager
Managing editor

IFLR

4 & 8 Bouverie Street, London EC4Y 8AX
Email:
[firstname].[surname]@euromoneyplc.com
Customer service: +44 20 7779 8610

EDITORIAL
Managing editor Lizzie Meager
elizabeth.meager@euromoneyplc.com
+44 207 779 8030
Commercial projects editor James Wilson
james.wilson@euromoneyplc.com
+44 132 621 2451
Americas editor John Crabb
john.crabb@euromoneyny.com
+1 212 224 3402
Asia reporter Karry Lai
karry.lai@euromoneyasia.com
+852 2842 6927

EDITORIAL ADVISORS
Peter K Brechan, Simon J Davies, Robert DeLaMater, Robert Dilworth, Bruce Duncan, Phillip Fletcher, David Graham, Ed Greene, Philip McBride Johnson, Michael Kenny, Paul Kruger, James Leavy, Juhani Makinen, John D Moore, Enric Picanyol, Graham Penn, Glen Rae, Gilles Saint Marc, Peter Siembab, Patricia Sindel, Bertil Södermark, Philip Wood, Christian Zschocke

Global head of sales, LMG Richard Valmarana
UK production manager Luca Ercolani
Production editor Josh Pasanisi
Head of editorial David Braid

ADVERTISING
Head of business development
Liam Sharkey
lsharkey@iflr.com
+44 207 779 8384
Business developer Asia Pacific
Anicette Indiana
anicette.indiana@euromoneyasia.com
+852 2842 6966
Business developer EMEA
Sanawa Mtalo
paul.ptaschne@euromoneyny.com
+44 207 779 8339

SUBSCRIPTIONS
Subscriptions hotline
Roxanne Speight
Tel: +44 20 7779 8380
rspeight@euromoneyplc.com

CUSTOMER SERVICES
Tel: +44 20 7779 8610

Printed in the UK by Buxton Press, Buxton, England

International Financial Law Review 2020
ISSN 0262-6969

ONLY ONLINE

GLOBAL In-house sending Covid-19 litigation work to law firms

More than 400 senior counsel and business executives told us how Covid-19 has affected their legal teams – and how they have responded. Our latest survey looks into how law firms can expect to see a wave of Covid-driven litigation work over the next 12 months despite external lawyers being asked to drop rates

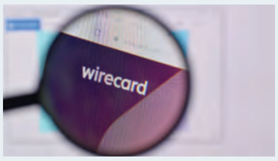
AMERICAS Primer on Ameribor and its role in the Libor transition

Our latest explainer takes a closer look at the alternative rate that has been designed with small to midsized US banks in mind, and the role it plays in the overall Libor transition. The new interest rate benchmark reflects the actual unsecured borrowing costs of banks and financial institutions

ASIA Inside Mongolia's first nomad bond

The Asian Development Bank raised MNT21 billion in a groundbreaking issuance of the world's first offshore MNT-linked bond. Known as a nomad bond, the deal sets a new benchmark for the frontier currency in the international bond market

EMEA Wirecard scandal damages trust in fintech



A number of high profile fintechs and companies have been impacted by the Wirecard scandal, and corporate trust has diminished in European markets following the backlash. Research showed that 73% of German businesses polled are less trusting of nonbank payment suppliers

AMERICAS Using PIPEs to finance SPAC mergers brings challenges

The recent rise in special purpose acquisition companies using private investment in public equities as a means of financing has led to a number of complex legal issues. PIPEs have seen a resurgence in the US capital markets this year

ASIA Podcast: Interview with Anna Wu, founding chair of the HKCC

In this podcast we speak to Anna Wu, the founding chair of the Hong Kong Competition Commission and this year's IFLR Asia-Pacific market reform award winner, where we talk competition law, career challenges, and why young lawyers shouldn't give up. Listen now on Apple Podcasts or Spotify

QUOTES OF THE MONTH

"We've seen some banks take someone in the organisation, give them a hoodie and a new office and tell them to go innovate"

Fintech consultant Kristian Sørensen is sceptical of conventional banks' dabbles with technology

"We don't have any plans to split our stock at this time"

Chipotle CFO Jack Hartung told IFLR that despite speculation, it will not be following in Tesla and Apple's footsteps

"We have to create a platform where your colleagues can show up and support you"

LSEG portfolio director Arlene Foster tells IFLR how financial services can become more inclusive in an exclusive podcast – listen now on Apple Podcasts or Spotify

"The problem is that the people begging the SEC to do this have a fundamental conflict of interest, because they plan to get rich off of those people at their expense"

Dennis Kelleher, CEO of Better Markets, is not too keen on the SEC's changes to accredited investor rules

"Market participants shouldn't assume that the existence of this power in the UK means that it will apply in all of the five Libor currencies"

FCA markets director Edwin Schooling Latter tells Practice Insight that its legislative fix powers on tough legacy are exclusive to the UK – read the full interview at iflrinsight.com

ASIA

Antitrust regulators need more bite

Worry over the powers of Big Tech (Apple, Google, Amazon and Facebook) has been building in recent years. With Covid-19 forcing a huge number of people to work from home – and leaving them with much more time to scroll on their phones – Big Tech's strength has only grown.

Quarterly earnings results back this up: Facebook's second-quarter revenues stood at $18.7 billion, up 11% year-on-year. Meanwhile, Amazon's net sales increased 40% to $88.9 billion in the second quarter of 2020. The CEOs of Big Tech faced a US congressional hearing at the end of July for alleged abuse of their market power to crush competition.

In Asia, other big tech companies are also in the firing line. China's State Council antitrust committee is reportedly considering a probe into Alipay and WeChat Pay, the digital payment apps owned by Ant Group, an affiliate of Alibaba, and Tencent respectively. The move seems a bit late, considering that the two apps already control 93% of the mobile payments sector in China.

The success of China's tech companies, particularly their overseas expansion, has worried US President Trump so deeply that he wants to ban a number of Chinese apps for national security reasons. PRC authorities have expressed disappointment, but have generally been reluctant to engage.

It will be interesting to. see where China decides to take its antitrust law. The Anti-Monopoly Law, passed in 2007, is currently under review by the State Administration for Market Regulation. Proposed changes include fines of up to 10% of the company's revenues in the last year for companies that organise or facilitate monopoly agreements. Fines are also set to increase for breach of merger control conditions from RMB500,000 ($70,400) to 10% of the company's revenues over the last year.

While the changes are only in draft form at this point, it would be a significant move for China, as it would be the first proposed amendment to the law for over a decade. The tech industry has grown by leaps and bounds in that time; the idea of Big Tech barely existed 10 years ago. Alibaba has grown from an e-commerce company in 1999 to one that spans financial services and artificial intelligence. Tencent has gone from a computer gaming company to one of the biggest venture capital investment firms in the world.

Perhaps it's also time for China to think about what it will mean for smaller businesses, as dominant players such as Alibaba and Tencent continue to expand beyond the industries they originated in. The challenge for all antitrust regulators – not just in China – is to keep up with rapidly growing tech companies before their powers grow too great. Some believe it is already too late.

AMERICAS

TikTok's time is nearly up

It's not just within China that Chinese tech companies are being closely watched. Throughout 2020 – with much of the world in some form of lockdown – video-sharing platform TikTok has been the app everyone is talking about, for more of the wrong reasons than the right ones.

Like Huawei before it, TikTok has faced intense scrutiny from the US government on the grounds of national security. Critics maintain that the app owner is harvesting data from across the US and the rest of the world, giving China valuable information at the expense of its millions of users. This idea has spread rapidly: in July, Congress voted overwhelmingly in favour of banning the app from use on federal devices.

In August, things became so heated that President Trump signed an executive order addressing the inherent threat to US national security. Claiming that the app has been downloaded 175 million times, the executive order suggests that TikTok automatically captures huge amounts of information from users, including internet and other network activity information, such as location data and browsing and search histories.

Shortly afterwards it was announced that Microsoft was in talks to acquire the US assets of TikTok – which would separate US users from ByteDance and – accordingly – protect US national security. The potential deal has been ratified by Trump. Soon after, Treasury Secretary Steven Mnuchin confirmed that the Committee on Foreign

Investment in the United States (CFIUS) was scrutinising the deal to ensure that it does not present any additional risk. Originally intended to monitor acquisitions of US companies by others from countries designated as a threat to the US, this is an extension of CFIUS' usual modus operandi. The apparent concern is that ByteDance and, ipso facto, the Chinese government, will maintain some form of control over TikTok even after the acquisition is complete.

The importance of this cannot be underplayed. If TikTok presents as much of a danger to US national security as the White House, Congress, CFIUS and many others have suggested, it is crucial to ensure that the utmost care goes into every aspect of the acquisition. Whether it's Microsoft or another acquirer altogether, ensuring that the former parent company relinquishes control will be a difficult task.

It would likewise be incredibly difficult for the eventual acquirer – even if it is a company with the technical prowess of Microsoft – to prove that the eventual spinoff will be a distinct corporate entity from its former parent. Ensuring that code within the application itself or embedded within its user data does not contain any spyware or delayed reaction malware will be incredibly difficult.

The situation continues to develop. On August 24, TikTok sued the US government for depriving it of due process. The suit suggests that the president has overstepped the mark in issuing the executive order and that the company has no choice but to protect the rights of its community and employees. Given the tense situation, it seems more likely that the application will be removed from the marketplace altogether. The government would simply have to face the wrath of the teenagers.

EUROPE

The paradox of aid

The announcement of the EU's €750 billion recovery fund in July was the perfect embodiment of, arguably, lawyers' most prized phrase: the devil is in the detail.

While the move is undoubtedly positive – that the Commission is so willing to take initiative, and that 27 member states managed to agree on such a big decision – the simple fact is that many are unlikely to take full advantage of the resource.

The same can be said of the various accompanying regulatory packages rolled out throughout the summer, all with one clear goal: to encourage eurozone banks to lend to the real economy.

Market participants generally feel that for member state governments and for banks alike, keeping up appearances is more important than embracing aid. Following the crowd appears to be the name of the game: if every member state uses it, it's fine. If no member state uses it, it's a bit wasteful, but it's also fine. But if a small number do, so the logic goes, there could be reputational damage ahead.

It's important to note that this theory only applies to the €360 billion loans portion of the fund. The remaining €390 billion is reserved for grants; the acceptance of which comes with much less stigma.

For instance, look at the European Stability Mechanism's pandemic credit line, which has been operational since May. The 10-year tool offers a more favourable borrowing rate than many southern European governments are able to command on their own – yet not one has taken it up. Member states appear more concerned by the perception of weakness than they are willing to accept a good deal; likely taking the view that it will cost them more later on.

Plus, even if governments did want to make use of the loans, there are fundamental obstacles preventing them from absorbing and distributing that much capital. For instance, when the 2007-2013 multiannual financial framework ended seven years ago, France and Spain had absorbed 60% of available funds, the UK 57%, and Italy had absorbed just 50%. Because the recovery fund sits alongside the standard 2021-2027 framework – and is highly dependent on member states reaching certain targets and milestones – governments may struggle to allocate the capital accordingly.

It's important to note that as these funds are contingent on the EU itself selling bonds to raise the capital, this pot is not immediately available: the Commission expects around three-quarters of the total funds to be paid in 2023.

That's logical, given the absorption rates of the past and the clear goals the Commission has set for member states. But it does beg the question of just how helpful that cash will be in addressing pandemic-related funding shortfalls facing governments today.

OFF THE

RECORD

"For financial services at least, the office is far from dead. High-end, people-oriented businesses like this will always require coffees and lunches"

A senior banker thinks the pandemic's long-term impact on dealmaking will be minimal

"This is not a good step. It sounds as though the initiative was written by lobbyists"

A development bank source is rattled by the SEC's plans to more closely monitor funds selling ESG products

"If a global pandemic didn't delay the transition, then there's little hope that anything else will"

A rates strategist has bad news for anyone dragging their feet on Libor transition efforts - read the cover story for more info

"Buyside firms aren't interested in scanning prices; that's half the reason you use a broker"

A bank managing director explains why Mifid II's pre-trade transparency initiative has not been particularly successful

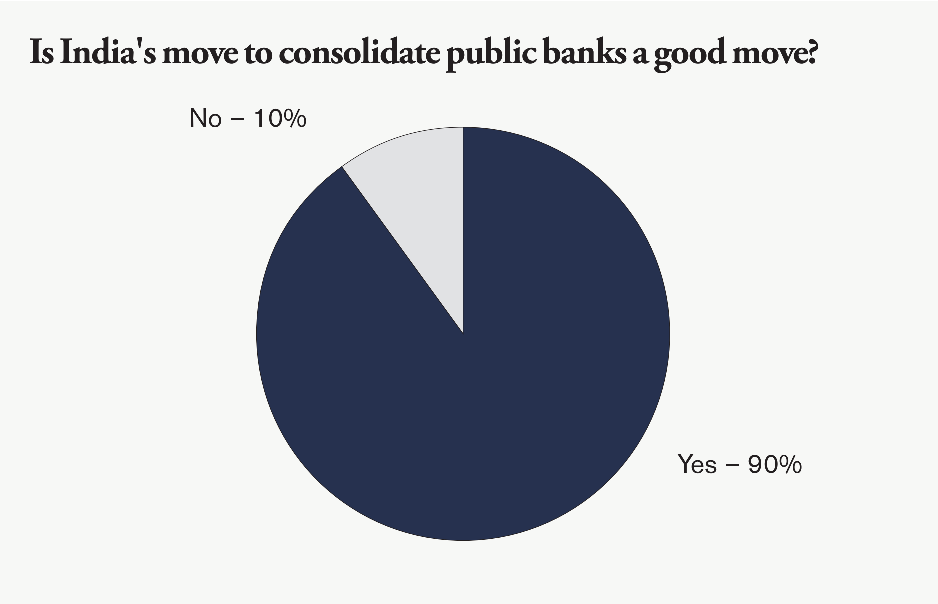
"Covid-19 has highlighted the fact that crises can be real, that they can have social rules, and that all of this is embedded in our wellbeing. Our emotional wellbeing is connected to our economic wellbeing"

A chief sustainability officer makes a direct link between the pandemic and the need to remain focused on ESG projects and initiatives

Stronger together

The Indian government plans to bring the number of public sector banks down from 12 to just four. IFLR readers agree that now is the time

By Karry Lai



According to a poll of IFLR readers, an overwhelming majority (90%) of the market believes that India's move to consolidate public banks is a good one.

The Indian government has plans to bring down the number of public sector banks from 12 to four in one of the biggest consolidation moves in the sector to date. Banking experts say that the exercise is welcome as public banks have been bogged down by bad debts – but ensuring operational synergies is only one of the challenges ahead.

It's also important to note that this is not the first time that India has consolidated its public sector banks. On April 1 this year, the number of public sector banks decreased from 21 to 12. The pandemic has triggered a further need to consolidate as the prolonged economic slowdown hits India.

Why now?

Avijit Banerjee, CEO and managing director at Argon Capital Advisors in Mumbai, says that the role of government should never be to run the banks, but to create frameworks and policies that will enable the efficient functioning of the banking system. He believes that there is no such thing as the right – or wrong – time to propose the initiative.

"Some may argue that the timing for such a move is bad because of the ongoing pandemic, because the bad loans of these state-owned banks, which were at 12.7% of total assets in September 2019, would balloon due to Covid-19," says Banerjee.

METHODOLOGY
IFLR publishes its quarterly poll question on iflr.com. Throughout the quarter, IFLR's editorial team gathers the responses and interviews selected respondents.

But he argues that this presents a fantastic opportunity for the overall banking system to improve. "Not only will it consolidate assets and strengthen the balance sheets of state-owned banks, it will also create market and operational synergies due to the classification and location spread of the customer base of these banks," says Banerjee.

In addition, such divestments will bring in money to government treasury. Banerjee admits that while it's easier said than done – and the banks themselves will have to work out the intricacies – the consolidation of banks will make the system much more efficient, and unlock more value in the long term.

The general counsel at an Indian private bank agrees, adding that with the non-performing loan problems that public banks are faced with, consolidation will create more structure for the industry and present an opportunity to clean up their balance sheets.

Banerjee expects M&A deals where the acquirer will be a private bank or financial institution, which will be followed by an open offer as mandated by the Securities and Exchange Board of India's guidelines.

The general view of IFLR readers is that any improvement in the banking system that presents not just transparency, efficiency and speed, but also an improvement in asset quality, is likely to have a positive cascading effect in all other sectors of the economy.

Rabindra Jhunjhunwala, partner at Khaitan & Co, also says that he doesn't see a better time than now:

The pieces are all starting to come together in the Indian banking sector

when the economy is struggling and in dire need of a shot of liquidity that does not involve increasing taxes.

The government has been clear that the target is to generate liquidity by encouraging banks to consider selling their non-core assets. This indicates that it is not aiming for mere mergers into other public banks, but possible privatisations via disinvestment.

"I see this as a good measure for the banking industry as it reduces the burden on the public deficit while bringing efficiencies," says Jhunjhunwala. "Given that the banks being considered are actual profit-making institutions, the offer will be lucrative for players who are looking to get into the banking industry, and market reaction should be positive in the short run, at least."

Meenal Maheshwari, lead commercial counsel at Indian oil company Essar, says that the consolidation of public banks could prove to be a good move as long as they are not merely paper mergers.

She adds: "The significant pro is putting in place strong risk management policies and processes that the banking ecosystem is in dire need of, such as laying explicit conditions to extend large loans and the due diligence that should be carried out before extending loans, plus the constant monitoring afterwards. A single strong policy should be developed and implemented fiercely across the banks."

Challenges ahead

Looking at the implementation challenges ahead, Jhunjhunwala says that the most pressing challenge is likely to be finding eligible bidders with the right credentials to ensure that the legacy of the institutions is not tarnished. Another challenge will be the integration of public employees into a private institution, and respecting the inherent cultural differences along the way.

The private bank general counsel agrees, adding that ensuring employee and systems integration will be key.

Banerjee adds that the first and the foremost challenge would be de-risking the balance sheets of state-owned banks. The question is who will take care of the burgeoning nonperforming assets, since it will impact valuation. The second difficulty will be market synergies in terms of penetration, cross-selling and upselling opportunities of the expanded customer base.

Operational synergies also need to be considered. "This is going to be the trickiest and most painful to handle, since the potential acquirer and the government will have to deal with the bank employees' unions, who in all likelihood will organise a series of nationwide bank strikes to derail this move," says Banerjee.

This is due to the ingrained fear that such a move will lead to significant job cuts – which opposition political parties are also likely to capitalise on.

Maheshwari adds that if the state-sanctioned merging of public banks is not executed carefully – and if it is only used as a way to bail out the weak banks – the merged entities will find it difficult to raise capital. Minority shareholders would be significantly hurt in the process.

On top of operational and cultural synergies, another barrier that will need to be considered are any potential anti-competitive issues. As the pool of banks serving customers shrinks, it will be essential for the Competition Commission of India to ensure that it limits any behaviour that restricts competition in the financial sector. The consolidation of market power in a few dominant firms may lead to concentration risks. This underscores the need for a strong authority to ensure free and fair competition throughout India's banking sector.

IFLR1000 INDIA AWARDS 2020

All the winners from IFLR1000's inaugural India awards

IFLR1000 has announced the winners of its very first India awards. The research was conducted together with the IFLR team over the course of several months, using IFLR1000 submissions, direct entries to the awards, and conversations with lawyers across India. The research team focused on transactions, looking at their legal innovation, impact, and complexity.

The awards recognise India's most notable deals that closed between May 31 2019 and May 31 2020, as well as the firms, teams, and individual lawyers that moved the market.

"Launching our India awards was an easy decision as the sophistication of legal work in the country has been evident to us through our research for years," says IFLR1000 editor Ben Naylor.

"The level of engagement from the local market – particularly given this incredibly challenging year – has been outstanding. The complexity and volume of work submitted to us made the judging challenging, but it was a highly rewarding process as we are able to recognise some incredibly talented lawyers and firms."

Congratulations to all winning and shortlisted firms, teams and lawyers. A more extensive overview of the winners is available on IFLR1000.com, where readers can also find the India awards winners' presentation.

Deals of the year

Banking & finance

Embassy Office Parks REIT margin financing

This year's winning banking and finance transaction is the $600 million margin financing to Embassy Office Parks REIT in June 2019. The financing consisted of a loan to the REIT, owned by Blackstone and Embassy Group, which was on-lent to the 13 SPV REIT unitholders incorporated in Singapore and Mauritius. Direct Indian security was taken over the REIT units, as well as offshore security over accounts and shares of the borrower and unitholders. It is the first margin financing to an Indian listed REIT. From a structural perspective, it resolved several complex regulatory and enforcement questions for the first time, and produced a first-of-its-kind risk allocation analysis.

Law firms
Allen & Overy
Cyril Amarchand Mangaldas
Kirkland & Ellis
Madun Gujadhur Chambers
Simpson Thacher & Bartlett
Trilegal

Debt capital markets

Greenko Solar bond

The winning debt capital markets deal is the $1.04 billion Greenko Solar bond. This was both the largest ever high yield bond from India, and the largest green bond sold by an Asian entity for two years. The structure sets one of the key high yield benchmark structures for the market. There were several notable structural aspects, one of the most significant being the segregation of the Indian rupee non-convertible debentures from the US dollar notes to meet India's foreign portfolio investment rules. The issuance represents the first high yield through which funds were infused into India via the voluntary retention route, a new investment channel for foreign investors. The deal was also structured, from start to finish, in just 30 days.

Law firms
Ashurst
Cyril Amarchand Mangaldas
Mayer Brown
Shearman & Sterling
Talwar Thakore & Associates
YKJ Legal

Equity capital markets

Sterling and Wilson Solar IPO

The winning equity capital markets deal is the $406 million Sterling and Wilson Solar IPO of August 2019. The listing was a true bright spot in what was a hesitant year for India's equity capital markets. The transaction was the first public offering from a pure-play solar EPC contractor in India; in 2018 it was the world's largest solar EPC solutions provider. There was a huge pre-IPO structuring effort to carve the group out of its former corporate structure, Sterling and Wilson Private. The listing marks the first public offer by a Shapoorji Pallonji group company in 150 years. From a legal perspective, the IPO was the first completed deal under the newly notified SEBI (Issue of Capital and Disclosure Requirements) Regulations of 2018.

Law firms
AZB & Partners
Khaitan & Co
Latham & Watkins
Sidley Austin

M&A

L&T / Mindtree

Larsen & Toubro's (L&T) $1.4 billion acquisition of IT technology and consulting company Mindtree in July 2019 wins this year's M&A deal of the year. The deal was a successful unsolicited hostile takeover, which was opposed by Mindtree's existing promoters. It represents one of the largest hostile takeovers of an Indian listed company ever and is the first example in the IT sector. The deal was consummated via the acquisition of a 20.3% stake from VG Siddhartha and his related entities, a 15% stake on the floor of the stock exchanges, and an open offer for a 31% stake under Indian takeover regulations. The deal overcame substantial challenges, including a complex escrow arrangement, regulatory issues (under the SEBI rules), and attempts to derail the deal.

Law firms
AZB & Partners
Baker McKenzie
Cyril Amarchand Mangaldas
Khaitan & Co
Samvad Partners

Private equity

OTPP and Australian Super / National Investment and Infrastructure Fund

This year's winning private equity deal is the investment by the Ontario Teachers' Pension Plan Board (OTTP) and Australia Super, Australia's largest superannuation fund, into India's National Investment and Infrastructure Fund (NIIF). The investment, completed in August 2019, included a $500 million commitment to NIIF's Master Fund, an agreement to co-invest three times as much ($1.5 billion) in the future, and the acquisition of a 25% stake in NIIF's manager entity. It is one of the largest commitments made in the Indian private equity industry and the first investment into India by Australian Super. The structuring of the governance rights was critical, as investors were becoming part of the management of the fund. This deal has set a template globally for private equity involvement in such assets..

Law firms
Debevoise & Plimpton
Herbert Smith Freehills
Nishith Desai Associates
Trilegal

Project finance

Nagpur Mumbai Super Communication Expressway

This year's winning project finance deal is the Nagpur Mumbai Super Communication Expressway. The deal involved a consortium of lenders, led by State Bank of India, in its financing of the construction and development of a six-lane access-controlled expressway along the Nagpur Mumbai corridor, known as the Maharashtra Samruddhi Mahamarg. The scale of the project is unique for India. The construction and operation aspects themselves were divided into 16 separate packages, each with their own construction contractors. The project included a direct agreement and undertaking from the government of Maharashtra to provide equity support to the lenders. A key achievement was that a project of this scale has been financed in one go.

Law firms
Cyril Amarchand Mangaldas
L&L Partners

Restructuring & insolvency

Essar Steel

This year's winning restructuring deal is a landmark distressed M&A and restructure. Essar Steel's insolvency recovery process entailed two competing bidders for the asset, ArcelorMittal and Nippon Steel Corporation, coming together behind a single bid, proposing a resolution plan, and successfully restructuring Essar Steel to rehabilitate it via an acquisition. The process and the resolution plan were challenged by dissenting creditors, operational creditors and Essar Steel promoters before the National Company Law Tribunal, National Company Law Appellate Tribunal (NCLAT), and Supreme Court. It resulted in precedent-setting Supreme Court decisions regarding resolution applicants under the Insolvency and Bankruptcy Code (IBC), the power of the committee of creditors, the distribution of proceeds, and the treatment of secured and unsecured creditors.

Law firms

Acuity Law
Cyril Amarchand Mangaldas
Indus Law
Juris Corp
L&L Partners
Shardul Amarchand Mangaldas & Co
S&R Associates

Teams of the year

Banking & finance
Cyril Amarchand Mangaldas

Debt capital markets
Cyril Amarchand Mangaldas

Equity capital markets
AZB & Partners

M&A
AZB & Partners

Private equity
Khaitan & Co

Project finance
Cyril Amarchand Mangaldas

Restructuring & insolvency
L&L Partners

Firms of the year

Law firm of the year
Cyril Amarchand Mangaldas

Challenger firm of the year
JurisCorp

Rising star law firm
Veritas Legal

IFLR Women in Business Law award

Zia Mody – AZB & Partners

Lawyers of the year

Banking & finance
Aashit Shah – J Sagar Associates

Debt capital markets
Yash Ashar – Cyril Amarchand Mangaldas

Equity capital markets
Varoon Chandra – AZB & Partners

M&A
Mohit Saraf – L&L Partners

Private equity
Nishant Parikh – Trilegal

Project finance
Santosh Janakiram – Cyril Amarchand Mangaldas

Restructuring & insolvency
L Viswanathan – Cyril Amarchand Mangaldas

IFLR1000 中国 AWARDS 2020

All the winners from IFLR1000's inaugural China awards

The IFLR1000 awards celebrate the most innovative and impactful deals and the best-performing law firms and lawyers across China in 2019. They also recognise where firms and lawyers performed exceptionally well, both locally and nationally. These results are the culmination of six months of research, where the panel analysed hundreds of submissions, surveyed thousands of referees, and interviewed hundreds of lawyers.

The full shortlist and details of the criteria and methodology are available online, as are full write-ups of all the winners.

The awards research was conducted in conjunction with IFLR1000's ranking research into eight regions in China. The law firm rankings, lawyer ratings and firm editorial reviews are all on IFLR1000.com.

Deals of the year

Banking & finance

Consortium / Zhongguancun Dinghao Electronics Building financing

This is the financing of one of the largest foreign commercial real estate acquisitions in Beijing to date.

Its structure will set a template for financings with separate onshore and offshore lending syndicates. In this deal, Shanghai Rural Commercial Bank took up a large portion of the onshore debt but only a small portion of the offshore debt, while assuming account control responsibilities under the onshore loan. Standard Chartered Bank, the agent bank under the onshore/offshore syndicates, contributed a large proportion of the offshore debt but only a small amount of the onshore loan. This implied a complex intercreditor relationship, requiring a bespoke account control arrangement and allocation of agents' responsibilities. A first-ranking mortgage over the property was granted to the onshore syndicate, and a second-ranking mortgage was granted to the offshore syndicate, which constitutes a *Nni bao wai dai* transaction, referring to a cross-border security provided by a non-PRC entity.

Law firms
JunHe – Lenders
Zhong Lun Law Firm

Capital markets

Huatai Securities IPO

This first-of-its-kind transaction required extensive negotiation with regulators from both the UK and China, with the rules of the Shanghai-London Stock Connect regime and the settlement procedures being developed during the progress of the deal. The listing set standards for deposit arrangements for Chinese companies to offer GDRs, which differ from the more established arrangements on the international markets and reflect the special requirements under the laws of the PRC. In addition, as this is the first offering of GDRs with A shares as underlying securities, the settlement procedures and timeframe for the offering were also explored for the first time. As the first offering of GDRs under the Shanghai-London Stock Connect, the listing sets the standard for future offerings, and it was quickly followed by two other proposed offerings under the Stock Connect regime.

Law firms
Fangda Partners – Issuer
King & Wood Mallesons – Underwriters

M&A

China Huaneng / Huaneng Renewables Corporation

The transaction is the largest privatisation of a Chinese state-owned enterprise listed on the HKEX in 2019. It entailed state-owned power producer China Huaneng Group closing a $2 billion acquisition of Hong Kong SAR-listed Huaneng Renewables and de-listing the company. As well as being the largest privatisation, it is also the first successful deal of this kind since the Hong Kong SAR Securities and Futures Commission (SFC) raised the threshold in 2018. Huaneng Renewables Corporation, a Chinese electricity generation company, is a subsidiary of Chinese state-owned enterprise China Huaneng Group, which went public in 2010. The deal was structured as a voluntary conditional offer.

Law firms
Jingtian & Gongcheng
JunHe – Lenders

Restructuring & insolvency

Shanghai CEFC International Group

This was the first case in which bankruptcy proceedings in mainland China were recognised by the Hong Kong High Court, marking a significant breakthrough in the cross-border recognition of cases in the Hong Kong SAR courts. The case is important because the bonds issued by CEFC Shanghai before the bankruptcy proceedings were worth CNY22.1 billion. If this was handled improperly, the case may have had a negative impact across the financial markets in China.

Law firms
Allbright Law Offices
Fangda Partners
King & Wood Mallesons

Impact deal awards

Beijing

Consortium / Zhongguancun Dinghao Electronics Building financing

The acquisition by a consortium led by Ascent Real Estate Investors and Sigma Delta Investment Partners is one of the largest foreign commercial real estate acquisitions in Beijing to date, and it may serve as an example of how to design financing structures where the compositions of the onshore and offshore syndicates are different. The inconsistency between overseas and domestic syndicates and between Chinese banks and foreign banks, as well the different interests of domestic and foreign syndicates, gave rise to complex and novel considerations.

Law firms
JunHe
Zhong Lun Law Firm

Shanghai

Shanghai CEFC International Group bankruptcy

This was the first case that bankruptcy proceedings in mainland China were recognised by the Hong Kong High Court, marking a significant breakthrough in the cross-border recognition of mainland China cases by the Hong Kong SAR courts. The case is important because the bonds issued by CEFC Shanghai before the bankruptcy proceedings amounted to CNY22.1 billion. If handled improperly, the case may have had a negative impact on the financial markets in China.

Law firms
Allbright Law Offices
Fangda Partners
King & Wood Mallesons

Tianjin

Bohai Steel Group bankruptcy

This bankruptcy involved 47 companies and the total liabilities exceeded RMB200 billion, making it the largest reorganisation case for restructuring assets and liabilities in China. The restructuring plan involved a packaged spinoff scheme where the company's assets and debts were split in two. A private entity was created to act as the investor into the restructured steel business; this involved a debt-to-equity swap transaction. The second part involved divesting non-steel parts of the business to asset managers.

Law firms
Commerce & Finance Law Offices
Global Law Office
King & Wood Mallesons

Chongqing

Chongqing Rural Commercial Bank A share IPO

The A-share listing of Chongqing Agricultural Commercial Bank on the Shanghai Stock Exchange has made it a leader in the Chinese capital markets. It was the first A + H-share listed agricultural commercial bank in China; the first A + H-share listed bank in western China; the largest A-share IPO issued in China by a financial institution since 2017; and the largest A share IPO on the main board of the Shanghai Stock Exchange since 2019.

Law firms
JunHe
Commerce & Finance Law Offices

Guangdong

China Merchants Shekou Industrial Zone Holding, Qianhai Land Resumption / Shenzhen Qianhai Development Investment joint venture

This project was unprecedented. It provided a benchmark through its creation of a mechanism enabling strategic cooperation between the government and enterprises for the purpose of land preservation during the transformation of a city. The project broke a multitude of records in the real estate and securities markets. It involved three state-owned companies listed in China and abroad forming an entity with a value exceeding RMB146.8 billion, making it the largest real estate transaction in 2019. The investment project lasted for four years and concerned a development area of 2.9 square kilometres. The overall legal workload for the project was vast, with complex interdisciplinary legal issues and tight schedules, which are unusual in both the real estate and capital markets.

Law firms
DeHeng Law Offices
JunHe

Zhejiang

Zhejiang Hailiang / KME

The target company, KME, is a global leader in the copper industry. This acquisition helps Zhejiang province to further its expansion in the non-ferrous materials industry. The transaction was large in scale, valued at €119 million ($141 million). In addition, the deal had to overcome unexpected challenges which demanded innovative solutions. The deal was also important for Zhejiang province; it attracted the attention of the local government because of its huge value and contribution to local economic development.

Law firms
Haiwen & Partners

Shandong

Hualu Holdings / Shandong Xinhua Pharmaceutical

This transaction is the one of the very first instances of a state-owned enterprise, supervised by the State-owned Assets Supervision and Administration Commission of the State Council (SASAC) of Shandong, absorbing and directly holding a controlling stake in a listed company. It was implemented in accordance with a SASAC of Shandong policy to reduce the number of shell companies.

Law firms
DeHeng Law Offices

Sichuan

Yinji Entertainment & Media bankruptcy

This case is China's first listed company to apply to the court for bankruptcy settlement, at a time when the debtor was facing a delisting. For such cases, there are unclear regulations at the current level of China's regulatory and judicial practices. For example, China only allows listed companies to apply for bankruptcy and reorganisation following approval from the China Securities Regulatory Commission, but it has not clarified bankruptcy settlement rules for listed companies. The case had no precedent to follow.

Law firms
East & Concord Partners

In-house team of the year

China International Capital Corporation（中金公司）

Firms of the year

Beijing
King & Wood Mallesons

Shanghai
Allbright Law Offices

Tianjin
Grandall Law Firm

Chongqing
Solton Law Firm

Guangdong
Zhong Lun Law Firm

Shandong
Wincon Law Firm

Sichuan
Tahota Law Firm

Zhejiang
Dentons

Team of the year

Banking & finance
JunHe

Capital markets
Fangda Partners

M&A
King & Wood Mallesons

Restructuring & insolvency
Fangda Partners

Lawyer of the year

Banking & finance
Liu Fei – Jingtian & Gongcheng

Capital markets
Shi Tiejun – JunHe

M&A
Liu Jinrong – Global Law Office

Restructuring & insolvency
Xu Shengfeng – Zhong Lun Law Firm

Rising stars of the year

Banking

Xu Chunlong – King & Wood Mallesons

Capital markets

Tan Xiao – Dentons

M&A

Huang Qingfeng – Commerce & Finance Law Offices

Restructuring & insolvency

Hou Yunjian – Global Law Office

IFLR1000 China hall of fame

Gong Mulong – King & Wood Mallesons

COVER STORY

Going round in circles

Confusion over the Libor transition has seen banks waiting for corporate demand before making products available, and corporates waiting to be advised by their banks. With just over a year to go, time is of the essence

By John Crabb

Libor. It's everywhere. Fallbacks, tough legacy, zombies, spreads, terms – it's the talk of the town in the financial regulatory arena. Here at IFLR and Practice Insight, it's been keeping us busy for a couple of years now.

But something we don't hear about every day is what it all means for nonfinancial corporates. The most you hear of the plight of the everyday corporate comes as an aside in the 52nd slide at the end of a conference: it's rarely front and centre.

According to data provided by the Alternative Reference Rates Committee (ARRC), there is approximately $200 trillion in Libor exposures outstanding across the banking and financial sector. While the majority of this is concentrated in the derivatives market, the exposure for nonfinancials is also incredibly high.

As well as loans, bonds and derivatives, there are implications for credit agreements, accounting, asset securitisations, supply agreements, long-term capital goods purchases, and employee benefit payments. The International Swaps and Derivatives Association (ISDA) estimates that end users comprise 10% percent of the total

Corporates need to modify systems and procedures to deal with the change, but they aren't committing the resources

derivatives market, and numbers are also high for cash products.

In addition to the financial transactions making up the $200 trillion estimate of Libor exposure, there are an unknown number of commercial contracts referencing the rate that will also have to be renegotiated. For a long-term purchase agreement of a large capital equipment item for example, it is important to understand that the transaction may take several months.

State-of-the-art machines can cost several hundred million dollars and take years to construct. This enters the purchaser and supplier into a multi-year purchase agreement that calls for periodic payments to be advanced by the customer upon the machine manufacturer's completion of designated milestones.

"If, however, production of the machine falls behind schedule and a milestone is missed, the contract will call for a reduction in the purchase price based on a calculation using Libor," says Tom Deas, chairman of the National Association of Corporate Treasurers. "Most of these types of agreements outstanding today were negotiated without any thought of what rates would apply if Libor were no longer quoted, and without fallback provisions."

Many end users have not yet focused on identifying Libor exposures, so they remain largely a mystery. Working with NACT working groups, KPMG found that less than half of the nonfinancial companies in the S&P 500 had made disclosures of their Libor exposures in their 2019 10-K filings, which were made in January or February of 2020.

The list is long, the numbers are high, and the coverage is limited. So, with just over a year to go until the fabled rate's permanent cessation, IFLR looks at the concerns and outstanding issues – this time not for Wells Fargo, HSBC or Barclays, but for WeWork, Volkswagen and Coca-Cola.

Finally, some clarity

A major concern for corporates is that the process of transitioning itself – be it to the secured overnight financing rate (SOFR), sterling overnight index average (Sonia), Tokyo overnight average rate (Tonar) or any other of the other emergent risk-free rates (RFRs) – is incredibly convoluted.

This lack of clarity means that anyone not spending every waking moment on the topic is likely to be left in something of a daze when trying to navigate the best way to handle both new and existing contracts. It also means that corporates are unwilling to venture too far ahead and take the necessary steps to appropriately shift towards new RFRs.

"Everybody is waiting for a lot more clarity before they go back to their organisation and say 'here's what we have to do, and here are the resources we have to commit to do it'," says Deas. "Corporates need to modify systems and procedures to deal with the change, but they aren't committing the resources without more clarity on the end state and what their banks will be doing."

Within every corporation, IT support is a finite resource. Treasury is, in effect, competing against procurement, marketing – or whoever else – to secure a considerable portion of that support. "It has to be acknowledged that right now, corporate treasurers don't know exactly how to make these changes to treasury systems and processes; and so are finding it difficult to develop and lock in implementation resources for a transition plan," adds Deas.

In multinational enterprises, Libor calculations are made and negotiated by corporate treasurers. This means that for the majority, there is little to no awareness of how many contracts reference Libor. It would be best practice for a corporate treasurer to convene a cross-functional team within the business, assigned with the task of introducing methodical processes to identify the affected contracts and create a process to amend them.

Determinations would include looking to see if contracts have foreign elements, particularly in countries with exchange controls that may involve securing agreements with foreign suppliers, and working with central banks and federal authorities.

However, sources say that the majority of nonfinancial corporates are yet to put this much thought or resource into the Libor transition at all. "To be honest, most corporates haven't gone into a lot of detail. For example, a lot of people are waiting on confirmation from the International Accounting Standards Board (IASB) about what the accounting requirements for hedging are going to be," says Sarah Boyce, associate director at the Association of Corporate Treasurers (ACT) in London. "If we were having this conversation in December or January I suspect there might be some more specifics, but at the moment nobody is really close enough, or active enough in the market, to be flagging specific issues."

Corporates are relatively comfortable with new transactions, and are becoming more comfortable with what has come to be known as tough legacy contracts: those that are unable to switch to a new rate before end-2021, for whatever reason. The official sector in both the UK and the US has created a so-called synthetic Libor to handle this problem. "The missing piece at the moment is what happens to deals on the books that go past the end of 2021 – that in theory can be transitioned, but it is not yet certain how," adds Boyce.

The blame game

Another significant concern is that the vast majority of new corporate loans continue to be issued against Libor rather than a risk-free replacement rate. One might think that because it's what companies are most comfortable with, it's what they want. However, sources say that corporates are being forced to use Libor whether they want to or not, because the banks they work with do not have the tools in place to do otherwise.

"Banks not being ready is really holding us back," says Shaun Kennedy, group treasurer at Associated British Ports (ABP), *If I go to one of the 16 banks in our group and ask for a loan, it is still predominantly on a Libor basis*

which has unexpectedly made a name for itself in this arena. ABP has been transitioning for two years and has completed a number of swaps on the UK's new risk-free rate Sonia. It was also the first UK company to move an existing bond over to the new rate – but Kennedy says it is not receiving the support it needs when it comes to loans. "If I go to one of the 16 banks in our group and ask for a loan, it is still predominantly on a Libor basis. This not only prevents us from moving on and doing anything with new RFRs, but also makes it particularly difficult to transition our back book of loans because there is no new market," he explains.

According to Kennedy, the members of his bank group – which come from a number of jurisdictions across the globe – are far from ready to offer RFRs across all the products that ABP deals with. "Different banks are in different places," he says. It's not that banks are to blame – things are rarely that simple – instead, a chicken and egg situation has arisen whereby banks are looking to corporates to see what they want, corporates are looking to banks to see what they have, and everyone is looking to loan market associations for what they might suggest. "Everyone is looking at everyone else wondering what to do. We all know that Libor is going away, but equally we are all waiting for someone else to take the lead," adds Kennedy.

The hare and the tortoise

According to the ACT's Boyce, when it comes to the Libor transition, corporates fall into two buckets: the early adopters, like ABP, and those that are yet to take any serious steps. Unfortunately, the latter camp makes up the vast majority. "What most corporates need is clarity and transparency. They just want to understand what the new world is going to look like for them," she says. "To a large extent, corporates are really dependent on the banks figuring out what products they want to sell so that corporates can then figure out whether or not they are suitable. Putting the early adopters to one side, there has certainly been a bit of a bit of an impasse over the last 12 to 18 months."

Banks are very much still in the process of figuring out what lending will look like in the post-Libor world, and what sort of products they are going to be able to offer to hedge that lending. These are business strategy conversations that banks need to have internally, and until this happens, corporates will be unable to join the conversation with any form of certainty.

"In the early part of this year – certainly in the UK – there was a lot more corporate engagement. The Libor transition was on the agenda for 2020, the larger corporations at least were beginning to have conversations with banks and to consider how to work through the process," says Boyce. "Corporates were asking what to do for new deals and for legacy deals. They have split things into these two buckets quite naturally."

One possible explanation for the lack of action – and one the banks themselves have offered – is that they are simply not in the business of telling customers what to do. While banks don't want anything to do with Libor going forward, it's also important not to be seen to be imposing alternatives on customers. "Corporates are just looking for some sort of guidance but no one is willing to give it to them. We've been going around in circles for a while," says Kennedy.

The virus within us

In the first quarter of this year, Covid-19 put the brakes on these discussions globally. Corporates became far more concerned with liquidity, forecasting, cash management, and anything else that would keep them afloat. "Everything else was parked – including Libor," says Boyce.

Covid-19 has swamped treasury and legal teams. Emergency loans throughout Europe, the UK and the US were all made on the basis of GBP Libor and USD Libor – or another interbank equivalent – because of the urgency inherent in bringing them to market. This means that even more loans were issued with reference to Libor, which has slowed the transition further still for borrowers.

In the US, the Federal Reserve actually decided to withdraw its original term sheet citing SOFR in its Main Street Lending Program (MSLP) and replace it with one referencing Libor. This sudden backtrack sheds some light on the issues the replacement rate has with liquidity and usage, as well as a certain lack of trust from the market. The updated term sheet stipulates that new loans use an adjustable rate of Libor (one or three month) plus 300 basis points; the initial term sheet from April referenced an adjustable rate of SOFR plus 250-400 basis points. The change was made following significant pressure from industry groups such as the American Bankers' Association (ABA) and banks across the country. 'In the midst of a pandemic, with diverse demands on finite management resources, such an abrupt transition to SOFR would deter participation in the MSLP," wrote the ABA.

This lack of readiness can also be seen as a lack of willing, or a fear of the unknown. "This might be because end users have more familiarity with Libor than SOFR," says Antoine Bouvet, rates strategist at ING. "It makes sense. This is a facility aimed at smaller recipients and the less sophisticated end of the market."

Getting things moving

RFR volumes remain low in general: 80% of SOFR issuance is still US government-sponsored. Yet despite Covid-19, the Libor transition has arguably accelerated significantly over the course of the summer, at least in terms of guidance if not actual use cases or liquidity. Corporates have come to terms with the fact that Libor's demise is not far off. There remains a lot left to do, but as some companies see it, the banks are not playing along.

ABP, for example, uses a number of different instruments in its loan programmes – in order to successfully transition, it must be able to access all of those in an RFR format. "Not being able to access certain products has been challenging. We can complain that products are not there, but because not all corporates are demanding it right now there is not a huge amount of pressure on banks to provide it. ABP is just one corporate voice among many," adds Kennedy.

"Most corporates haven't really started to take this seriously. I think most are expecting the hard work to be done for them. We are doing our best to try different things but that is not wholesale across the market," he adds.

ABP is of course not the only company to have made proactive moves. Ford in the US was an early adopter of SOFR, and British American Tobacco (BAT) has also made an important issuance. "But it doesn't feel like all of the market is moving that way," says Kennedy.

In June 2019, Ford sold an auto loan securitisation using fallback language that had recently been released by ARRC. The floating rate tranche of the $1 billion bond accounted for around 12% of the overall issuance. At around $126 million it's not going to move the market – but it nevertheless represents an important step in the eventual transition. "We take our position as leaders in the market really seriously. We wanted to leverage it in support of the transition away from Libor," says Nathan Herbert, global structured finance lawyer at Ford. "It's our obligation to contribute to the programme by demonstrating leadership and becoming the first issuer to adopt the ARRC's recommended fallback language in a securitisation." Despite this early action, fallback language has not been widely implemented.

Adam Schneider, partner in Oliver Wyman's digital and banking practice, emphasises just how important it is for corporates to understand what fallbacks are in place for new contracts: "Most are just looking for a rate they think is acceptable, because right now most corporates are not going to price new product with fallbacks yet," he says. The actual economic consequence for a borrower or lender is very complicated, because it depends on the fallback itself. "Although one party may think a fallback is enforceable, others may not. People from the same firm think different things – what might be in your favour in one instance may move against you depending on where the market is. There are a whole range of possibilities," he adds.

Larger institutions should know fallback numbers in advance as they negotiate future financial contracts. "You are nuts if you don't understand the range of motion between the current rate, the fallback, the ARRC rate, the market rate, and the impact of the credit sensitive rate between now and then," he adds. "You need to know the math. Otherwise, you are taking an obsolete provision of an old contract that you may find favourable. We don't see a lot of answers that don't involve fairly detailed analytics."

In May, BAT announced that it had signed a new £6 billion ($7.9 billion) multicurrency revolving credit facility. The transaction was the first widely syndicated credit facility executed globally to be linked to both Sonia and SOFR.

"Obviously a lot of people are waiting for the market to develop as much as possible. It is helpful that big corporates like BAT have publicly announced their RFR loans, but a lot of others are just sitting on the sidelines waiting for everything to be settled before moving themselves," says Clifford Chance's Julia House. The big driver in the UK now for GBP Libor is the FCA's end-Q3 deadline to make non-Libor alternatives available, adds House. "After the end of Q3 there should be an increase, and after that any amendments to loan documents, be it refinancing a loan or extending it, should hopefully include some kind of hardwired switch mechanic within the documents to deal with legacy issues," she says.

> *The missing piece at the moment is what happens to deals on the books that go past the end of 2021*

End of the beginning, or beginning of the end?

There are a number of things that corporate treasurers can be doing in the remaining months before end-2021 that will assist the transition. Waiting for others to act is not one of them. Closely monitoring the situation is important, especially considering the pace is likely to pick up considerably in the coming months.

Treasurers should also develop a clear understanding of which products and transactions are affected by Libor. "This includes establishing whether maturities extend beyond 2021, and detecting any interdependencies with other products," says Gareth Old, partner at Clifford Chance in the US. "Depending on the organisation, impact assessments may have to be widened beyond core funding and treasury functions to include nonfinancial contracts, such as late payment clauses in commercial contracts, investment agreements, and others." They should also be reviewing both new and existing contracts at the earliest opportunity to ensure that the appropriate steps are being taken.

Consensus suggests that not enough thought has been put into this by corporate treasurers. Now is the time to change that.

> *We are doing our best to try different things, but that is not wholesale across the market*

CORPORATE

MORRISONS DATA BREACH

A sigh of relief

Cleary Gottlieb lawyer Natalie Farmer analyses the Supreme Court ruling on Morrisons' liability for its 2013 data breach

The UK Supreme Court, in a unanimous decision delivered on April 1, overturned the decision of the Court of Appeal which had found that Morrison Supermarkets PLC (Morrisons) could be held vicariously liable for the unauthorised actions of an employee who had deliberately leaked the personal data of thousands of Morrisons' employees online. In its judgment, the Supreme Court explained that the Court of Appeal had "misunderstood the principles governing vicarious liability".

As the threat of class action lawsuits for personal data breaches increases, the Supreme Court's ruling should be welcomed by employers. The EU General Data Protection Regulation (GDPR) sets a low bar for data subject compensation, with 'non-material' damage being sufficient to warrant a payout. Data subjects do not need to demonstrate actual financial loss and may be able to claim compensation for distress associated with an unauthorised disclosure of their personal data. The Supreme Court judgement, therefore, brings welcomed clarity on the extent to which an employer could be on the hook for the actions of a rogue employee.

Takeaways for employers

Helpfully, the Supreme Court determined that:

- An employer will not be liable for the actions of an employee in deliberately causing a data breach while acting beyond the ordinary scope of their employment, provided the employer can demonstrate the necessary standard of care imposed by data protection law has been met, thus avoiding any primary liability.
- When assessing what is within the ordinary scope of employment, more than a temporal or causal link between the authorised acts of the employee and the wrongful disclosure of personal data, will be needed. It is not enough that the employee has the opportunity to

1 MINUTE READ

The UK Supreme Court recently determined that Morrisons Supermarkets PLC was not vicariously liable for a personal data breach deliberately caused by one of its employees. While this judgment is good news for employers, the fact that the Supreme Court did not rule out the possibility of vicarious liability altogether cannot be overlooked. There are plenty of steps employers should take to avoid liability for actions of rogue employees. We explore these steps and the courts' decisions.

It is generally understood that where an employee is processing personal data in the context of their employment, their processing activities are considered to be those of their employer

cause a breach during the course of his/her employment.

- Motivations of an employee will be a relevant part of the assessment. Where an employee is not motivated to further his/her employer's business, but instead is driven by a personal vendetta, this will be taken into account.

However, the Supreme Court's judgment is not all good news for employers. The UK's highest judicial authority did not exclude the possibility of vicarious liability for data breaches altogether. Therefore, in principle, an employer could be vicariously liable to compensate data subjects for the actions of an employee which, for example, amount to a breach of the GDPR, a breach of confidence, or a misuse of private information, where such actions are within the ordinary scope of his employment.

While not specifically considered by the Supreme Court, whether an employer can ever be vicariously liable for a breach of the GDPR by virtue of its employee's actions which take place within the scope of its employment, is debatable. It is generally understood that where an employee is processing personal data in the context of their employment, their processing activities are considered to be those of their employer (i.e., the data controller). An employer would not therefore be vicariously liable for such employee's actions, but instead would be directly liable under the GDPR as the controller of such processing. This is distinct from the situation where the employee acts outside of the scope of their employment, in which case they would be deemed to be an independent data controller and at the same time vicarious liability would be precluded.

While vicarious liability at common law or in equity may still arise, the distinction with the position under statutory data protection law has important implications for potential damages claims (in light of the very low threshold for compensation set by the GDPR). Primarily, therefore, employers should take all steps necessary to avoid a breach of the GDPR as a result of its employees' actions within the course of employment.

Lessons for the future

There are plenty of lessons to be learned from Morrisons' near miss in this case. Not only does this case highlight the increased appetite for claims relating to data security, but also the value a disgruntled employee can seek to destroy in deliberately causing a personal data breach. Businesses need to think carefully about how they treat personal data and who they trust to handle it appropriately. Going forward, to reduce the likelihood of being directly or vicariously liable for employee-made data breaches, it will be crucial for employers to consider the following:

- ***Access to data*** Limit access to personal data files on a need-to-know basis. Consider additional access and authentication protocols for sensitive personal data, data pertaining to disciplinary matters, and financial information such as bank account details. Consider whether it is appropriate to remove or limit access where an employee is subject to serious disciplinary actions.
- ***Selection of skilled employees*** Carefully select employees to be tasked with sensitive or high-volume data handling and ensure that they have the requisite skills to perform their functions without error. This should include appropriate training on internal systems, technologies, procedures and policies.
- ***System security*** Ensure that appropriate technical and organisational measures are in place to secure data. As well as the access limitations described above, consider system safeguards to prevent large volumes of data being exported (either entirely, or without alerting the information security team of the unusual activity). To limit the risk of bad actors taking advantage of human errors and vulnerabilities, invest in state-of-the-art technology to detect external hacks and ensure employees are trained to spot phishing emails and similar scams.
- ***Disaster recovery and crisis management*** Implement effective disaster recovery plans to mitigate the financial and reputational fallout from any accidental or deliberate personal data breaches that employee actions may give rise to. Rehearse your crisis management plans so that, ahead of time, the organisation knows who is responsible for taking steps to secure systems, manage communications, ensure business continuity, and retrieve data where it has been lost or rendered inaccessible.
- ***Accountability and record keeping*** Know who is responsible for data processing activities. Document data processing instructions and the delegation of data handling responsibilities to employees (whether in connection with human resources, information technology, client relationship management, or the execution of internal audits). Ensure that you can identify and evidence actions that go beyond the ordinary scope of employment.
- ***Internal policies*** Ensure that clear and accessible internal policies provide for the appropriate parameters of employees' day-to-day data processing responsibilities.

As the threat of class action lawsuits for personal data breaches increases, the Supreme Court's ruling should be welcomed by employers

Background and breach in the Morrisons case

In November 2013, in preparation for an internal audit, Andrew Skelton (a former senior auditor employed by Morrisons) was provided access to employee payroll data and was put in charge of collating and transmitting the relevant data to Morrisons' external auditors, KPMG. Following transmission of the data to KPMG, as instructed, Skelton made a copy of the data from his work laptop to a personal USB stick. In January 2014 Skelton released the harvested personal data relating to 98,998 Morrisons employees to a publicly accessible file sharing website. The data packet contained details of employees' national insurance numbers, bank account information, and contact details.

Skelton's actions followed internal disciplinary proceedings against him, which the Supreme Court's judgment characterised as having caused Skelton's "irrational grudge against Morrisons, which led him to make the disclosures in question".

High Court and Court of Appeal cases

In 2017, an action brought by a group of approximately 5,500 affected Morrisons employees was heard by the High Court (*Various Claimants v WM Morrisons Supermarket PLC* (2017) EWHC). The claimants argued that Morrisons had both primary and vicarious liability to compensate the employees for the breach of its statutory duty under section 4(4) of the Data Protection Act and misuse of private information.

The High Court found that Morrisons "did not directly misuse any information personal to the data subjects. Nor did they authorise its misuse, nor permit it by any carelessness on their part. If Morrisons are liable it must be vicariously or not at all." However, the High Court did determine that a sufficient connection existed between Skelton's actions and the course of his employment for vicarious liability to arise. In particular, the High Court found that Skelton's actions were part of an 'unbroken chain' of events which began when he was granted access to the data by Morrisons in the course of his duties.

The High Court noted its discomfort in making its judgment in light of the fact that the wrongful acts of Skelton were deliberately aimed at Morrisons, such that the High Court's conclusion "may seem to render the court an accessory in furthering [Skelton's] criminal aims". As part of the judgment, the High Court granted leave for the decision to be appealed.

Morrisons appealed the High Court's decision in 2018 on three grounds: (1) that the DPA excludes vicarious liability, (2) that the DPA excludes causes of action for misuse of private information and breach of confidence, and (3) Skelton's actions in any event occurred outside of the course of his employment, precluding the vicarious liability of Morrisons (*WM Morrison Supermarkets Plc v Various Claimants* (2018) EWCA). The Court of Appeal considered (1) and (2) together, ultimately dismissing both.

With respect to Morrisons' third ground of appeal, the Court of Appeal also affirmed the High Court's judgment that Morrisons was vicariously liable for the actions of its employee, noting that the High Court's characterisation of Skelton's actions as a 'seamless and continuous sequence' or 'unbroken chain' of events commencing with his employment duties, thus giving rise to the vicarious liability of his employer, "is one with which we entirely agree".

> ***The only connection between Skelton's authorised actions and his decision to disclose the data online was that he had been tasked with collating the data***

UKSC judgment

Morrisons appealed again, this time successfully, with the Supreme Court finding that the lower courts had misunderstood the principles governing vicarious liability in four key respects (*WM Morrison Supermarkets plc v Various Claimants* (2020) UKSC):

1. Skelton's public disclosure of the personal data of Morrisons' employees on the internet was neither part of the function of Skelton's employment, nor was it within his field of activities;
2. The fact that the five factors for vicarious liability established in *Various Claimants v Catholic Child Welfare Society* (2013) were present, was not decisive. The factors were designed to be applicable to the scenario of establishing vicarious liability between parties where the wrongdoer and the defendant had a bond that was akin to an employment relationship, rather than an actual relationship of employment as between Morrisons and Skelton;
3. Although there exists a close temporal link and an unbroken chain of causation between the provision of the data to Skelton for the purpose of transmitting it to KPMG and his subsequent disclosure of the data online, a temporal link or causal connection does not alone satisfy the required 'close connection' test required to establish vicarious liability; and
4. Skelton's motivations should not be considered irrelevant. Whether Skelton "was acting on his employer's business or for purely personal reasons" should be considered highly material.

The question of Morrisons' vicariously liable for Skelton's wrongdoing was therefore considered afresh by the Supreme Court, applying the test laid down by Lord Nicholls in *Dubai Aluminium Co Ltd v Salaam* (2002): was Skelton's disclosure of the data so closely connected with acts he was authorised to do that, for the purposes of the liability of his employer to third parties, his wrongful disclosure may fairly and properly be regarded as done by him while acting in the ordinary course of his employment?

The only connection between Skelton's authorised actions and his decision to disclose the data online was that he had been tasked with collating the data and transmitting it to KPMG. The Supreme Court, however, found that the "mere fact that Skelton's employment gave him the opportunity to commit the wrongful act would not be sufficient to warrant the imposition of vicarious liability". The Supreme Court further distinguished the actions of an employee (whether or not misguided) in furtherance of his employer's business, and actions of an employee which are solely motivated by the furtherance of the employee's own interests. The Supreme Court found that in the present case (paragraph 47):

"*it is abundantly clear that Skelton was not engaged in furthering his employer's business when he committed the wrongdoing in question. On the contrary, he was pursuing a personal vendetta, seeking vengeance for the disciplinary proceedings some months earlier. In those circumstances, applying the test laid down by Lord Nicholls in Dubai Aluminium in the light of the circumstances of the case and the relevant precedents, Skelton's wrongful conduct was not so closely connected with acts which he was authorised to do that, for the purposes of Morrisons' liability to third parties, it can fairly and properly be regarded as done by him while acting in the ordinary course of his employment*."

Having established that the conditions for vicarious liability did not exist in the present case, it was not necessary for the Supreme Court to consider whether the DPA excludes such liability. However, as the relevant points had been fully argued, the Supreme Court considered it desirable to express a view. On this question, the Supreme Court agreed with the High Court and Court of Appeal, finding that the DPA did not exclude the possibility of common law vicarious liability being established against an employer who had otherwise complied with its data security obligations under the DPA.

It was argued by Morrisons that: (i) Morrisons performed the obligations incumbent upon it as a data controller; (ii) Skelton was a data controller in his own right in relation to the data disclosed; (iii) the DPA was clear that liability should only be imposed on data controllers where such data controllers had failed to act with reasonable care; and (iv) therefore, the statutory scheme under the DPA could not be reconciled with the imposition of strict liability on Morrisons, the employer of a data controller, for its employee's breach of the DPA or its own breach of duties arising at common law or in equity. However, the Supreme Court found such argument to be unpersuasive, noting that: (a) since the DPA is silent on the position of a data controller's employer, there can be no inconsistency; and (b) that this position is not affected by the fact that the DPA is a fault-based liability regime (imposing liability on the data controller, including for the action of an employee, for failing to take reasonable care) whereas vicarious liability is not based on fault.

Final thoughts

As noted at the outset of this article, while the Supreme Court found that vicarious liability is not precluded by the DPA, its judgment does not go as far as to assess the real likelihood of vicarious liability ever arising under data protection law in the employment context. In light of the fact that an employer is generally considered to be the data controller of any data processing undertaken by its employees within the course of their employment, it follows that an employer must be directly liable for the actions of its employees or not liable under statutory data protection law at all.

Ultimately, whether or not it is argued to have arisen directly or vicariously, employers should concentrate on avoiding liability for a breach of the GDPR or their duty of confidentiality, or for the misuse of private information, through: (i) the execution of comprehensive compliance programmes (ii) regular employee training, (iii) appropriate technical and organisational measures, (iv) careful selection of employees to conduct high-volume or sensitive data processing, (v) the implementation of effective disaster recovery plans, and (vi) clearly delineated and documented data processing roles and functions.

Natalie Farmer
Associate
Cleary Gottlieb Steen & Hamilton, London

CORPORATE

SWISS REORGANISATION

Composition agreements: a guide

Schellenberg Wittmer lawyers explain how composition agreements can benefit distressed businesses

Under Swiss law, a bankruptcy order may be rendered against a distressed business either from the request of a creditor or upon the request of the debtor itself. Such bankruptcy order may be issued based on two different financial situations: in case of insolvency (the distressed business is no longer in a position to repay its debts when due, due to a lack of liquid funds), or in case of overindebtedness (i.e. if according to the last interim balance sheet, the liabilities of a stock company or a limited liability partnership are not covered by the assets). It is worth mentioning that the board of directors of a stock corporation or the managers of a limited liability partnership are even obliged to file for bankruptcy if the company is overindebted: indeed, in such a case, the board or the managers must inform the judge of the overindebtedness, this judge then having no other choice but to render a bankruptcy order.

Bankruptcy, however, is not inevitable. Swiss law provides efficient legal mechanisms that can allow a distressed business to escape from bankruptcy proceedings, meaning that instead of rendering a bankruptcy order, the judge is entitled to open in-court restructuring proceedings. In-court proceedings may also be combined with out-of-court restructuring.

As of today, two types of restructuring proceedings are available for distressed companies. Other mechanisms have been temporarily passed in order to overcome the Covid-19 pandemic, but they are due to be lifted soon and will therefore not be addressed by this analysis. Besides, financial institutions insolvency is governed by other provisions, not addressed here.

The first (composition proceedings) is a formal judicial reorganisation proceeding opened by the judge, requested by the debtor themselves, or a creditor, and supervised by a receiver (trustee) appointed by the court. It has influence only on the claims themselves (reduction, modification of terms) and their repayment. The second (stay of bankruptcy proceedings) is an informal out-of-court reorganisation

Olivier Hari
Of counsel
Schellenberg Wittmer
T: +41 22 707 8178
E: olivier.hari@swlegal.ch
W: www.swlegal.ch

Olivier Hari is highly specialised in general corporate law, transactional matters, finance transactions, companies restructuring, distressed refinancing, distressed M&A, crisis communication, complex national and cross-border insolvency and restructuring proceedings, and related litigation proceedings. His personal experience as board member (chairman) allows him to understand the expectations of directors and other business leaders from a legal perspective. He is also regularly appointed by the courts to monitor and support distressed companies. He is of counsel in Schellenberg Wittmer's corporate & commercial, M&A, capital markets and restructuring & insolvency groups, and is also a Professor of Law (University of Neuchâtel and Geneva). As such, he is the author of numerous publications in the fields of corporate law, capital markets law and insolvency law.

A composition agreement is supposed to bind the debtor and all creditors

proceeding for overindebted businesses that is only opened by the judge under certain circumstances and eventually conducted under the supervision of a receiver appointed by the court, where all the available restructuring techniques can be used.

The composition agreement

Composition agreement with creditors

So-called composition proceedings aim to offer distressed businesses – be they insolvent or overindebted – a formal in-court reorganisation concerning almost all types of debt and all categories of creditors. In a nutshell, in such proceedings, the debtor enters into a kind of agreement (the composition agreement) with almost all of its creditors. The contractual aspect of the arrangement must be put into perspective, as a composition agreement can be prepared and put in place by the creditors and the judge, against the will of the debtor.

Types of composition agreements

There are two different types of composition agreements: ordinary agreements (the distressed business is expected to survive and the legal structure of the debtor remains unchanged) and composition agreements that assign assets to the creditors of to a third party (the distressed company is liquidated and its business activities possibly sold to a third party).

An ordinary composition agreement can be reached among the debtor and its creditors. According to certain composition agreements, the agreed terms of the claims can change. It is possible to postpone the repayment of all claims (so-called moratorium composition agreement), or to reduce the amount of all debts under a composition agreement that would provide for the partial release of the debtor from its debts, in which case the debtors only receive a dividend (so-called dividend composition agreement). The debtor's agreement to these two types of composition is mandatory.

A composition agreement that assigns assets may also be selected. According to this type of composition agreement, the debtor forgoes most or all of its assets to the creditors so that they sell them (a liquidator is appointed), or pursuant to which such assets (often the business itself in its economic acceptation) are sold and transferred to a third party. The proceeds of the sale are distributed to the creditors, and the debtor's agreement is not necessary. Such composition agreements allow a third party to buy the company on relatively favourable terms: in fact, a business can be acquired free of liabilities (but also without any reps and warranties, which is the only downside).

Commencing the proceeding: granting a moratorium

As aforementioned, either the debtor or a creditor can file a request for a short duration provisional composition moratorium aimed at assessing the financial situation of the distressed business, followed by a true mid to long-term moratorium, aimed at preparing the composition agreement.

The provisional moratorium may be granted for a maximum duration of four months. If, during the provisional moratorium, prospects of a reorganisation or the approval of a composition agreement appear, a true moratorium shall be granted, which may last 12 months – or even 24 for complex matters.

The court will simultaneously appoint one or two receivers, whose most important role will be to supervise the debtor and then to assess acceptance of the creditors' composition agreement. The receiver is generally in contact with the creditors and can help the debtor prepare a draft composition agreement. The receiver has to convene the creditors to a meeting, which takes place at the end of the moratorium and allows the creditors to obtain clarification regarding the debtor's situation and to vote on the composition agreement.

The judgment by which the court grants the debtor or creditor a true moratorium must be published in the Swiss Official Gazette of Commerce, whereas a provisional moratorium may stay unpublished, allowing for a silent restructuring.

Composition agreement acceptance: creditors' involvement

A composition agreement is supposed to bind the debtor and all creditors, meaning that all creditors must take part in the acceptance process. In this regard, the creditors whose claims are presented before the moratorium – which are therefore subject to the composition agreement – are asked at the very beginning of the proceedings to file their claim with the receiver.

The stay will not necessarily be published in the Gazette, protecting the distressed company from very bad – and sometimes even disastrous – attention

Creditors that file their claim in due time will then be allowed to vote in favour or against the proposed composition agreement and to receive appropriate related information. Creditors that fail to file their claims on time or at all will not be entitled to take part.

When the draft agreement is ready, the creditors are called to a creditors' meeting, during which the receiver (or receivers) reports on the debtor's financial situation and goes over the draft composition agreement. The composition agreement is deemed to be accepted by the creditors if a qualified double majority votes in favour – both a majority counted per head and a majority counted in terms of value claim must be reached. Those that are not allowed to vote include the secured creditors, for the part of the claim that is effectively secured; the so-called privileged creditors (notably employees' claims, social insurance claims, whose claims must by law be repaid in full); and individuals whose personal relationship with the debtor may lead to a conflict of interest.

Court ratification

Alongside the creditors' acceptance process, the judge must also ratify the composition agreement accepted by the creditors, provided that certain legal conditions are met. In particular, the judge must verify that privileged creditors are repaid in full, the agreement is fair and of a favourable nature, the debtor provides repayment securities and, in cases where the business is transferred to a third party, the third party has warranted the payment due for such a transfer.

The court's ratification entails the binding nature of the composition for all claims brought either before the moratorium, or during the moratorium without approval of the receiver.

A particular case: sale of the business to a rescue company via composition agreement

A business activity may be rescued by the sale of the fixed assets of a distressed business (i.e. the assets that are requested for the business activity) to a so-called rescue company, through a composition agreement with asset assignment. The rescue company is often an ad hoc vehicle founded by the shareholders of the distressed company, the case may be with additional shareholders (or without certain shareholders, which are therefore squeezed). Creditors of the distressed business may be repaid using the proceeds of the sale, but not only: it is also permitted to grant to these creditors participating rights in the rescue company along with the founding shareholders (shares, non-voting equity, profit-sharing certificates).

Mixed: in/out of court restructurings

Judicial framework for extrajudicial restructurings

Mixed restructurings are also permitted in Switzerland. In particular, a debtor may file before the judge an application aimed at getting a moratorium (judicial process) to negotiate and reach with its creditors a consensual private agreement with the intention of adjusting and/or renegotiating its financial obligations.

Judicial frameworks for such mixed restructurings are the composition proceedings from one side and the stay of bankruptcy proceedings from the other.

If a composition moratorium is requested to allow the debtor to take out-of-court restructuring measures without the risk of bankruptcy, the various steps necessary for in-court proceedings won't make sense anymore. It means that the call to creditors, the creditors' meeting/vote and the judge ratification will be avoided, converting the composition moratorium into a pure moratorium.

Stay of bankruptcy proceedings is reserved to overindebted stock companies and limited liability partnerships. If notified of a situation of overindebtedness, the judge shall normally issue a bankruptcy order. At the request of the board of directors/the managers or a creditor, it may decide to postpone the bankruptcy. In this case, the judge shall take all appropriate measures to preserve the value of the assets and may appoint a receiver whose role will be defined in the stay of bankruptcy judgment (mainly debtor's supervision).

The stay of bankruptcy judgment will not necessarily be published in the Swiss Official Gazette of Commerce, protecting the distressed company from very bad – and sometimes even disastrous – attention.

The duration of the moratorium is not limited by law. The typical duration is between six and 18 months. At the request of the company or a creditor, it may be lengthened several times. At the moratorium expiry date, the company must no longer be overindebted. Otherwise, the judge will have no other choice than to issue a bankruptcy order.

Provisions of the Swiss Code of Obligations governing stay of bankruptcy proceedings has been recently changed by the Swiss Parliament. As of consequence, the stay of bankruptcy proceedings shall disappear. The composition moratorium will serve as the only judicial reorganization's framework.

Out-of-court restructuring techniques and measures

All techniques and measures shall be used in order to achieve a unique goal, i.e. successfully restructuring the company (and erasing the overindebtedness arising from the financial statements).

The reorganisation may, for example, be: sale of part of the business (even the profitable part, but the sale must be made at market price and be fair, otherwise creditors may successfully challenge the transaction); rethinking the size of the company or ceasing to engage in certain activities, especially if they are unprofitable; the withdrawal of financial reserves; the re-evaluation of immovable property and participation; the increase of capital through the sale of new shares for consideration; deletion of the whole share capital (by cancelling the share) and, immediately thereafter, increase of the share capital. The company can also try to get creditors to agree to enter into standstill agreements, to write off part or all of their claims, or to subordinate their claims – but the debtor must, to a certain extent, ensure the equality of treatment among the creditors.

Facing Covid-19: past mistakes and lessons learnt

Woo Lyou, legal counsel at **Electronic Arts**, offers his views on Korea's response to Covid-19 and its implications for businesses

As the deadly Covid-19 virus rages on throughout the world, Korea has managed the crisis well so far. For the most part, the public go about their lives as they have before, and businesses continue to operate normally. Such normalcy is partly the product of a painful lesson learned in 2015, when another contagion struck.

The Middle East Respiratory Syndrome Coronavirus (MERS-CoV, more commonly known as MERS), was first reported in Korea in May 2015. Within a month, Korea had recorded the second highest number of test-positive cases in the world. Amid the panic, the government quarantined zoo camels and advised the public against eating camels, even though they are not commonly eaten in Korea.

Various stakeholders failed to mount a coordinated response. The Korea Centers for Disease Control (KCDC) refused to give local governments information on the outbreak because the national government was slow to approve the transfer of such information. Health authorities followed a faulty guideline that required testing of those "who have stayed within two metres *and* for one hour or longer with a patient [emphasis added]". They neglected to test those who were briefly close or those who had prolonged contact from farther away, but it was later discovered that MERS could be transmitted through these types of contacts. Subsequent confirmed cases, as a result, included not only physicians who had briefly interacted with MERS patients, but also a hospital patient who had been in a different wing from MERS patients.

The government was also slow to inform the public on important public health developments, which allowed disruptive and harmful rumours about the disease to spread, such as that rubbing petroleum jelly under one's nose can prevent infections. When the rate of new infections reached zero several months later, there were a total of 16,693 quarantined persons, 186 confirmed cases, and 38 dead. This

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1 MINUTE READ

Various governments have mounted diverse responses against the Covid-19 contagion, ranging from seeking herd immunity to banning travel. Based on the learning from the MERS crisis in 2015, Korea deployed a different set of responses and has managed the situation relatively well. This article discusses the specifics of the government's response, how those responses affect businesses, and regulations relating to Covid-19 to watch out for when doing business in Korea.

Poor handling of the MERS outbreak showed that Korea would not be ready for the next epidemic

Woo Lyou
Legal counsel, Electronic Arts (EA) Korea
Seoul, South Korea
W: www.ea.com

Woo Lyou is a Korean American and is a legal counsel at Electronic Arts Korea. His work focuses primarily on online games. Before joining Electronic Arts, Woo was a foreign attorney at Yulchon LLC, where he advised inbound and outbound clients on intellectual property matters. Woo started his practice at CJ Entertainment and Media – the studio behind the Oscar-winning film Parasite, where he worked on television dramas, movies, and concerts. His primary practice areas include entertainment law and international commercial transactions.

Woo lives in Seoul. He went to Emory University, where he majored in political science and minored in history. He received his JD from Boston University School of Law.

was the largest outbreak of MERS outside of Saudi Arabia.

Poor handling of the MERS outbreak showed that Korea would not be ready for the next epidemic. To prevent another crisis, the government streamlined its infectious disease response protocols, including amending the Infectious Disease Control and Prevention Act (IDCPA) several times from 2015 through 2019.

Improved response

Unfortunately, the opportunity to test the new response systems came soon. In February 2020, Korea again reported the second highest number of confirmed coronavirus cases in the world—this time, it was Covid-19. However, since March, the infection rates have been relatively steady, with the occasional new surge being quickly managed. There are various reasons why the Covid-19 outbreak in Korea was mostly kept under control, but at least some of them are attributable to government response.

First, the information sharing infrastructure among various stakeholders has improved. The IDCPA now requires multilateral sharing of all infectious disease related information among the national government, local governments, hospitals, other medical institutions, and medical professional associations. The revision ensures that hospitals and medical research institutions have the latest information on the development of the disease. Hospitals can allocate treatment resources accordingly, and research institutions can adequately plan the development and production of drugs and other treatments.

Second, the IDCPA now requires the KCDC to set up a standing Emergency Operations Center to collect and disseminate information on infectious diseases, manage the crisis, and take initial measures in emergencies. The Central Disease Control Headquarters (CDCH) has taken on this role, updating the public daily on new developments and making recommendations. For example, when rumours spread that Covid-19 is waterborne and that swimming pools were an infection risk, the CDCH clarified that there is no evidence that Covid-19 is waterborne and that swimming pools only pose a low risk, as long as a distance of two metres can be maintained between people.

Faulty rumours, such as that packages shipped from foreign countries pose infection risks, can have a chilling effect on international commerce. Accurate, up-to-date information reduces such risks.

Third, the health authorities conduct widespread contact tracing and testing. They collect geo-locational data to track all the places or facilities a confirmed patient has visited. Subsequently, they send text messages to all those who have visited the same facility—notifying them to get tested—as well as to those living in the municipality where such facilities are located, warning them against visiting the same area or facility. To mitigate privacy concerns, personal information collected in the process is destroyed after 14 days, and those who disseminate it for a purpose other than stipulated in the IDCPA are subject to criminal prosecution.

Early, widespread testing has suppressed the virus from spreading uncontrollably. As a result, companies can maintain business continuity as they find ways to innovate and adapt to the new normal. It is true that businesses named in the government text messages, and the ones close to those that are named, can suffer severe economic loss. However, the text messages incentivise businesses to implement preventative measures, which, in turn, suppresses the spread overall and stimulates consumption. Additionally, those businesses can reopen after they fulfil certain sanitisation requirements. For example, in early May, over a hundred people were infected within a few days in Itaewon, an area known for fine dining and night life. Some businesses in the area were closed and thoroughly sanitised. They reopened a few days later, and within weeks, Itaewon was again vibrant.

Fourth, the national government establishes and executes strategies for combating infectious diseases. The government used this authority to procure masks and testing kits early. By late January, prior to Covid-19 becoming a major public health concern in Korea, the government, with assistance from private companies, had already developed a testing kit which could deliver results in six hours, and ordered their mass production. By early April, there were more than half a million Covid-19 tests conducted in Korea, a country with a population of fifty-two million. Additionally, in early February, the government purchased the raw materials for N95 masks and supplied them to private companies at a subsidised cost. Despite some early supply disruptions, there were plenty of masks accessible to the public for purchase by April.

Through such efforts, the government procured and supplied over a million N95 masks to medical facilities in March. While the government does not furnish free masks to other businesses, they are widely available to the public at a subsidised cost (approximately $1.25 per unit). Unlike in some other countries, the government does not require employers to supply their employees with free masks. Additionally, businesses do not have to worry about the cost of testing or treating employees for Covid-19; the government bears such costs.

Fifth, unlike many other governments, the Korean government steadfastly avoided lockdowns and generally refrained from travel bans. In February 2020, thousands of new confirmed cases were being reported from one province and some called for a lockdown of the province. However, the government did not lock down the province. Neither did they implement widespread travel bans, instead checking symptoms of those entering the country and requiring them to be quarantined for fourteen days. Many countries that implemented early travel bans or lockdowns have seen substantial surges, indicating their ineffectiveness against Covid-19. Travel bans and lockdowns provide the public with a false sense of security that they are shielded from the virus, while the virus spreads quietly within the community.

Business trips are possible because there are no travel bans, and the 14-day quarantine requirement for entry into Korea may be waived for entrants meeting certain requirements who are pursuing important business, academic, or humanitarian purposes. There is free movement of people and goods across the country. In-person meetings, though advised against, are feasible if necessary.

The Green New Deal

In July, the government unveiled a $62 billion Green New Deal, through which it plans to invest in areas that will lessen the carbon footprint, prevent the spread of infectious diseases and create new jobs. Those areas include 5G telecommunications, remote working systems, high-speed internet infrastructure, drones, automotive vehicles, big data and artificial intelligence, and distance learning.

The government's plan uses the term 'untact', which is a new business term in Korea meaning 'contactless'. Such contactless businesses have already performed well through the pandemic. As people spend more time at home, e-commerce businesses, video streaming services, game studios and publishers, home furnishing businesses, and food delivery services are seeing increased revenues. As funds from the government's plan are infused into the market, companies in the applicable fields are well positioned to capitalise on new opportunities.

In July, the government unveiled a $62 billion Green New Deal, through which it plans to invest in areas that will lessen the carbon footprint

Covid-19 regulations for businesses

Although there is continuity in business overall, the government has placed some burdens on businesses as part of its fight against Covid-19. For example, if an employee is confirmed to have Covid-19, the employer needs to notify all workers in the place of business, including dispatch workers and delivery workers, have the infected employee return home immediately, and notify the health authorities. Then, the employer needs to follow the health authorities' instructions, which include cordoning off and disinfecting areas where the infected person has been. Usually, the company may resume operations after completing the disinfection.

Additionally, there are industry-specific requirements. High-risk operations—such as hospitals, night clubs, and buffets—need to install digital entry trackers to keep track of those who enter, check the symptoms of employees daily, require employees to wear masks, designate a disinfection manager, disinfect shared items daily, and mandate a distance of two metres between employees. All sailors disembarking on any Korean port need to get tested for Covid-19.

Although not legally required, health authorities also recommend that employers establish a monitoring and response plan in case of employee or customer infection. Additionally, employers are encouraged to grant additional paid holidays to employees who cannot work from the office but have respiratory illness symptoms. Businesses are also strongly urged to implement work-from-home procedures or staggered work schedules. Employers should frequently disinfect the workplace and install signage reminding employees to wash their hands and to maintain a two-metre distance. Further, there are industry-specific recommendations. For instance, banking and financial institutions are recommended to forebear interest for six months for customers who are experiencing hardship arising from Covid-19. High-risk facilities are recommended to designate a contact person for health authorities, install partitions, and temporarily shut down shared spaces, such as cafeterias.

Hopeful outlook

As of August, more than 300 have tragically lost their lives to Covid-19 in Korea. Also, a recent surge has strained the economy and the healthcare system. Despite such challenges, Korea's citizens trust their government to respond to the crisis swiftly and effectively, as it has done so far.

Similarly, Korea has fared relatively well economically. While Korea, as a nation dependent on exports, has been affected by decreased worldwide demand for manufactured parts, machinery, and consumer goods, its relatively stable domestic market has mitigated the damage. For example, in June, Korea's automobile exports dropped 37.4%, while its domestic sales rose 41.9%, indicating that the Korean consumer market remains attractive for foreign companies looking to expand their operations. The International Monetary Fund forecasts that Korea's economy will contract by just 2.1% in 2020, compared to 4.9% globally.

Every country has responded to Covid-19 differently, with varying degrees of success. By learning from its mistakes in handling the MERS outbreak, Korea's improved response to Covid-19 has placed it in a good position for recovery in terms of both public health and business.

SOUTH KOREA SPECIAL FOCUS 2020

Comparing pre- and post-Covid restructuring & insolvency trends

Chiyong Rim, Jin Yeong Chung and **Kevin Todd** of **Kim & Chang** examine the latest iteration of Korea's restructuring and insolvency resolution framework

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Before the Covid-19 outbreak, from late 2019 to early 2020, the market was already witnessing a significant increase in the number of companies applying for court-supervised insolvency proceedings, including bankruptcy, an insolvent liquidation proceeding, and rehabilitation, a proceeding somewhat akin to a Chapter 11 bankruptcy proceeding in the US. The number of distressed companies was significantly higher in 2019 compared to 2018. This trend can be partly attributed to the impact that recent failures of large corporations, notably in shipping and shipbuilding, have had on their vendors and suppliers, most of which were small and medium-sized enterprises (SMEs). SMEs was the category of debtor that made up the brunt of bankruptcy and rehabilitation filers in 2019.

The Covid-19 outbreak severely impacted companies in the aviation, hotel, hospitality and off-line retail industries. Yet it is difficult to find court-supervised insolvency proceeding filings in South Korea by companies in these industries. At least in the short term, we do not expect to see a significant increase in such filings, as many of these companies, including large corporations, have received various forms of support from the Korean government. The Korean government mobilised approximately KRW200 trillion (approximately $169 billion), a part of which went to support large corporations impacted by Covid-19, in an effort to revive the economy. Rather, the more imminent issue will be how companies will restructure and take advantage of the government support.

Overall, the number of insolvency cases in South Korea involving corporate debtors has continued to increase each year. The following table presents data collected by the Supreme Court of Korea showing the number of corporate insolvency proceedings brought in Korean courts from 2011 to 2019.

Year of filing	2011	2012	2013	2014	2015	2016	2017	2018	2019
Rehabilitation	712	803	835	873	925	936	878	980	1,003
Bankruptcy	312	396	461	539	587	740	699	806	931

Statutory framework

After the 1997 financial crisis, the South Korean government reformed the nation's bankruptcy law by amending the Corporate Reorganisation Act, the Composition Act and the Bankruptcy Act. Nevertheless, it was apparent that there was a need for a unified bankruptcy law. The National Assembly passed a comprehensive bankruptcy law, and court-supervised insolvency proceedings are now governed by the Debtor Rehabilitation and Bankruptcy Act (DRBA), which became effective on April 1 2006. The DRBA is divided into six chapters:

- Chapter 1 – general provision: jurisdiction, notice, service, management committee, creditors' council and update on corporate registry
- Chapter 2 – rehabilitation proceeding: for all legal entities
- Chapter 3 – bankruptcy proceeding: liquidation proceedings for legal persons and individuals
- Chapter 4 – rehabilitation proceeding for individuals with regular income
- Chapter 5 – cross-border insolvency
- Chapter 6 – penalties

South Korea also offers out-of-court workouts under the Corporate Restructuring Promotion Act (CRPA), which enacted into law the corporate workout procedures that had previously been used by financial institutions for restructuring debtor companies on the verge of insolvency through an out-of-court workout arrangement.

The number of insolvency cases in South Korea involving corporate debtors has continued to increase each year

The Seoul Bankruptcy Court was established on March 1 2017. Under the DRBA, if the number of a debtor's creditors exceeds 300 and the amount of debt exceeds KRW50 billion, then the Seoul Bankruptcy Court will have concurrent jurisdiction over the insolvency proceeding, even if the debtor's main business or place of incorporation is outside Seoul.

The Seoul Bankruptcy Court plays an important role in the insolvency regime in South Korea. Generally speaking, the South Korean legal system is codified and does not adopt the common law principle of *stare decisis* or binding precedents. However, the precedents of the Supreme Court practically have binding force of the law. With respect to insolvency cases, the decisions of the Seoul Bankruptcy Court, with which about 40% of total insolvency cases are filed, carry significant precedential weight in practice, to the extent that they are within the boundary of Supreme Court precedents. After the establishment of the Seoul Bankruptcy Court, newly implemented concepts such as debtor-in-possession, stalking horse and pre-packaged plans have become more frequently employed by both petitioners and the court, and insolvency procedures have become more expedient and more predictable than before.

In the stalking-horse bidding sales process, a debtor enters into an agreement in advance with a potential purchaser of an asset and holds an auction where the aggregate of the purchase price and termination costs sets a base-line price for the bid. Unless there is a higher bid in the auction, the sale is concluded in accordance with the prior agreement. The process has the advantage of having a high probability of securing a purchaser through a private agreement while promoting the fairness of the sale procedure through bidding.

In the case of a rehabilitation proceeding that uses a pre-packaged plan, a rehabilitation plan is drafted and approved by a majority of creditors before the debtor files the petition for commencement of rehabilitation. This process is beneficial to accelerate the rehabilitation proceedings and improve chances for a swift recovery. Given there have been demands for accelerated procedures, it is expected that this pre-packaged plan would be implemented more frequently.

Although the DRBA, in principle, does not recognise priorities among common benefit claims (i.e., generally, claims arising after commencement of a rehabilitation proceeding), loans newly executed with court approval after filing a petition for commencement of rehabilitation proceedings (i.e., DIP loans) are given priority over all other types of common benefit claims. Other common benefit claims are paid *pari passu* in proportion to the amount of each claim. In the DRBA, there was no provision permitting such priority granted to DIP loans in rehabilitation proceedings to be carried over to bankruptcy proceedings, in case a rehabilitation proceeding is converted into a bankruptcy proceeding, making it more difficult to attract lenders willing to provide new funds to the debtor. This was raised as an issue during the rehabilitation and bankruptcy proceedings of the Hanjin Shipping case.

Article 477 of the DRBA was amended in February 2020 to address this issue, providing that the priority granted to a DIP loan in rehabilitation would carry over to bankruptcy if the rehabilitation proceeding is converted to a bankruptcy proceeding. As a consequence of the amendment, DIP loans are now classified as estate claims in an ensuing bankruptcy, and along with wages, have the top priority over other claims, including other estate claims.

The current CRPA is the sixth version of the law, which includes a sunset provision that designates a specific date on which the law will expire unless it is renewed or re-enacted. The fifth version had expired in June of 2018, after which a sixth version was

Chiyong Rim
Senior attorney, Kim & Chang
Seoul, South Korea
T: +82 2 3703 1403
E: chiyong.rim@kimchang.com
W: www.kimchang.com

Chiyong Rim is a senior attorney at the firm and practises in a wide range of insolvency and restructuring areas, with a focus on corporate liquidation, M&A in reorganisation proceedings, and cross-border insolvency cases. He represents private equity funds, corporate clients and both foreign and domestic financial institutions in various reorganisation proceedings. Chiyong also has extensive experience in advising clients on issues relating to personal bankruptcy, corporate reorganisation and workout proceedings, and has used this experience to write books on the topic in both Korean and English.

Jin Yeong Chung
Senior attorney, Kim & Chang
Seoul, South Korea
T: +82 2 3703 1108
E: jychung@kimchang.com
W: www.kimchang.com

Jin Yeong Chung leads the cross-border litigation practice and the insolvency & restructuring practice. He is a senior attorney at Kim & Chang and has successfully represented various foreign and domestic clients in numerous contentious disputes, involving financial products, derivatives, corporate matters, M&A, competition and others. He has also advised numerous large corporations, creditors and investors with regard to various insolvency and corporate restructuring matters.

Kevin Todd
Senior foreign attorney, Kim & Chang
Seoul, South Korea
T: +82 2 3703 1271
E: kltodd@kimchang.com
W: www.kimchang.com

Kevin L Todd is a senior foreign attorney with the firm. He practises primarily in the areas of insolvency & restructuring, insurance, investment management, labour & employment, and international arbitration & cross-border litigation. Kevin has extensive experience in advising both domestic and foreign clients, including creditors, investors, and other interested parties, on issues relating to bankruptcy, company rehabilitation and workout proceedings, and has published extensively and spoken on such issues in a number of forums.

enacted in response to a considerable consensus in favour of the law. The sixth version is set to expire in October of 2023.

Court-supervised proceedings

Court-supervised insolvency proceedings are governed by the DRBA, which offers two kinds of insolvency proceedings for business entities: (i) rehabilitation proceedings under Chapter 2 of the DRBA, primarily for the rehabilitation of insolvent business entities, and (ii) bankruptcy proceedings under Chapter 3 of the DRBA for the liquidation of insolvent business entities.

The goal of rehabilitation proceedings governed by Chapter 2 of the DRBA is to rehabilitate insolvent debtors by restructuring their debts pursuant to a rehabilitation plan approved by the creditors and confirmed by the court. Rehabilitation proceedings are analogous to the Chapter 11 proceedings of the US Bankruptcy Code. However, filing for a rehabilitation proceeding does not itself trigger the formal commencement of a rehabilitation proceeding. A rehabilitation proceeding commences only when the court issues a separate commencement order in response to the filing.

Upon commencement, the court will, in principle, appoint a receiver. In general, the court will appoint the existing management (for example, a representative director) of the debtor to act as the receiver in the rehabilitation proceeding unless the insolvency of the debtor was caused by any wrongdoing or serious mismanagement committed by the existing management, in which case the court will appoint an independent receiver. In practice, the existing management is appointed (or is deemed appointed) as the receiver in most rehabilitation cases; a third party may exceptionally be appointed as the receiver. The receiver has the power to conduct all the debtor's business and manage all of its property, subject to the court's supervision.

In rehabilitation proceedings, creditors are classified into three basic categories: (a) creditors with unsecured rehabilitation claims; (b) creditors with secured rehabilitation claims; and (c) creditors with common benefit claims. Creditors with either secured or unsecured rehabilitation claims are subject to rehabilitation proceedings and generally may not receive payment or repayment of their respective claims other than as provided for in the rehabilitation plan (with certain exceptions, including set-off of claims that are exercised within the claim filing period under the DRBA). However, creditors holding common benefit claims – such as wage claims, those claims that arose after the commencement of the rehabilitation proceedings (with certain exceptions) and those claims that were approved by the court

> ***The newly enacted CRPA has widened the net on the types of creditors which it can bind***

– are not subject to the rehabilitation plan, and may, in principle, receive repayment of their claims when due.

Bankruptcy proceedings governed by Chapter 3 of the DRBA are court-administered proceedings designed to liquidate an insolvent debtor's assets. These are analogous to the Chapter 7 proceedings of the US Bankruptcy Code.

In bankruptcy proceedings, creditors are generally divided into creditors with bankruptcy estate claims and creditors with unsecured bankruptcy claims. Unsecured bankruptcy claims are subject to the bankruptcy proceedings and repaid from the distributions made by the bankruptcy trustee. However, bankruptcy estate claims are repaid from time to time from the bankruptcy estate by the bankruptcy trustee.

Unlike rehabilitation proceedings, in bankruptcy proceedings creditors with secured claims are generally not prohibited from enforcing their security interests in the debtor's assets except for certain procedural limitations. Thus, the proceeds recovered from such enforcement may be applied to the repayment of the secured claims regardless of the bankruptcy proceeding.

Out-of-court restructurings

There are mainly two types of out-of-court restructurings in South Korea: (i) a voluntary workout between the debtor and creditors, and (ii) a voluntary restructuring through a workout process under the CRPA. Until recently, such out-of-court restructurings were preferred by market participants, particularly debtor companies, because they afford more flexibility and generally cause less disruption to the debtor, which could count on receiving financing during the workout from its creditor financial institutions.

Restructuring by means of a voluntary agreement is a restructuring process whereby creditor financial institutions and the debtor voluntarily enter into and implement a private agreement to restructure the terms of existing debts and business of the debtor following a request from the company. In principle, concluding the agreement requires a unanimous affirmative vote of the creditors, although decisions made after entering into the voluntary agreement often require the agreement of creditors holding claims totalling at least three-quarters of the total claim amount. Creditors may set a period during which they will suspend exercise of their claims and conduct due diligence with a view to preparing the restructuring agreement. The restructuring of liabilities under the agreement typically provides for a three to five-year grace period, a reduction of interest rate and a conversion into equity of a certain portion of debt that exceeds the appropriate level the company can service.

Restructuring pursuant to the CRPA is similar to a restructuring by voluntary agreement, especially because the CRPA includes the provision of a three to five-year grace period to restructure liabilities, lower interest rates and convert a certain portion of debt that exceeds the appropriate level the company can service into equity. However, the workout under the CRPA is a more formal, statutory process which still takes place out of court.

Previously, only companies that had received "financial credit" as defined under the Enforcement Decree of the CRPA were eligible for a workout under the CRPA. It was argued that the narrow scope of "financial credit" caused the unsuccessful result of a workout.

Therefore, the newly enacted CRPA has widened the net on the types of creditors which it can bind. Pursuant to the latest version of the CRPA in 2020, workout provisions under the CRPA are binding if there are creditors that hold financial claims against a failing company. To elaborate in detail, a financial claim is defined by Article 2 of the CRPA as a claim that may be exercised vis-à-vis a failing company as a result of the extension of credit to the debtor or a third party. Based on the above definition, even corporate bondholders, in principle, are classed as applicable creditors. Indeed, the exact scope of applicable creditors remains uncertain under this article; further guidance or precedent is required to specify it. In the meantime, non-financial creditors such as trade creditors and tax creditors, are explicitly excluded.

Workout procedures

The main creditor bank of a debtor is required to evaluate the credit risk of the debtor, determine whether the debtor shows signs of financial distress, and if so, may designate such company as a failing company.

Upon being designated as a failing company, the debtor may file a petition with the main creditor bank for either (a) commencement of joint management proceedings under the CRPA or (b) management by the main creditor bank only. For joint management proceedings, a rescue plan and the list of financial creditors is required by the financial creditors' council (Council), a council composed of financial creditors of the failing company.

> ***Filing a petition for commencement of rehabilitation is often listed as an event of default***

The main creditor bank must give a notice of the first meeting of the Council within 14 days of receiving the debtor's petition for joint management, and the first meeting of the Council must be held within 14 days of the date of the notice. At the first meeting, financial creditors resolve to begin joint management and determine the list of participating financial creditors. The Council may decide whether to suspend the exercise of creditors' rights (including enforcement of security) and, if so, the period for such suspension. After the first meeting, the Council may engage an accounting firm or a third-party expert to conduct due diligence on the debtor's assets and liabilities and assess its viability as a going-concern in consultation with the debtor. Taking into account the outcome of the due diligence investigation, the main creditor bank must submit to the Council a joint management plan.

The Council may convene a meeting to consider the joint management plan submitted by the main creditor bank and pass a resolution to approve it. In principle, such resolution requires the approval of financial creditors holding at least three-quarters of the total amount of financial claims against the debtor.

After the joint management plan is approved, the Council and the debtor must enter into an agreement to implement the plan. This agreement is commonly referred to as a memorandum of understanding (MOU). In addition to the joint management plan, the MOU includes a detailed implementation plan, management goals, consent from interested parties (including shareholders and/or the labour union), matters concerning improvement of the debtor's corporate governance structure, and measures to be taken if the debtor fails to perform the MOU, among others. The joint management plan and the MOU usually include matters such as a grace period for exercise of claims, a debt-equity swap and a reduction in interest rates, new credit support, and self-rescue including restructuring of existing business by spin-off, transfer of business, sale of assets and cost reduction.

The joint management process will be terminated under several scenarios. First, if the Council fails to pass a resolution on the joint management plan within the period when the exercise of creditors' rights is suspended, the joint management process is deemed to be terminated. Second, if the joint management is not completed within three years after the MOU is signed, a management evaluation committee will be organised to evaluate the efficiency of the joint management process, and based on the result of the evaluation, the process may be discontinued. Third, if it is determined that the debtor has been relieved of its financial trouble through joint management or that the MOU has been fully performed, the process under the CRPA will be closed.

Thorny issues

A financial creditor that objects in writing to the commencement of joint management under the CRPA or to a debt restructuring by means such as debt-equity swap, reduction of interest rate or extension of new credit, has the right to require assenting financial creditors to purchase its claims. In this case, the purchase price paid for the claims held by a dissenting financial creditor may not be less than the amount that may be recovered by that creditor through liquidation of the failing debtor. In practice, this purchase price tends to be much lower than the face value of the claims.

A workout may help guarantors due to the resulting reduction in principal, which in turn alleviates the guarantors' liability based on the accessory relationship between the principal and the guaranty obligations. In contrast, filing a petition for commencement of rehabilitation is often listed as an event of default, and reducing the amount of debts owed by a corporate debtor under rehabilitation does not affect the liability of a guarantor.

Practical tips for construction companies in applying *force majeure*

Chung Jin Chung, legal counsel at **Korea Gas Corporation**, shares insights for companies in Korea and beyond

Since March 11 2020, 181 countries have implemented travel bans or restrictions on movement of humans and materials. Many countries announced that all new visitors, including labour workers will not be allowed entry or must be quarantined for a certain period (normally 14 days from the date of the entry). Due to the early outbreak of Covid-19 in Korea, 181 countries banned or limited the entry of Koreans. This unprecedented scale of restrictions differentiates Covid-19 from other epidemics.

As Covid-19 continues to hinder, delay, interrupt or prevent construction works, construction companies may find it difficult or impossible to satisfy their obligations. This article shows key clauses that may be used by an affected party for excusing itself from its obligations or claiming extension of time or additional payment.

It must be noted that the following analysis depends on terms and conditions and governing law with specific facts.

Force majeure

Under Korean law, even if there is no black letter law about *force majeure*, there are Supreme Court cases which provide elements of a *force majeure* defence as follows:

1. the cause of the *force majeure* must be beyond the affected party's control; and
2. such an event was not foreseeable or preventable within the affected party's reasonable efforts.

If the affected party finds it impossible to perform its obligation due toa *force majeure* event which is not attributable to the affected party, it will be excused from contractual obligations and the other party shall not be entitled to enforce such obligations against the affected party, except for wilful misconduct or gross negligence of the affected party.

There are few cases to excuse the affected party from its obligations with a *force majeure* defence. For example, there

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1 MINUTE READ

Covid-19 is affecting construction business all over the world. Many construction companies are facing an unprecedented crisis due to government measures to control Covid-19, including restrictions on travel and supply chains. This article will provide guidance for construction companies as they consider which clauses and legal principles may cover their situation related to Covid-19 in Korea and other countries.

Chung Jin Chung
Senior legal counsel, Korea Gas Corporation
Seoul, South Korea
W: www.kogas.or.kr

Chung Jin Chung is a senior legal counsel at Korea Gas Corporation in Korea. He has 10 years' experience, advising companies on their energy projects around the world and has experience across the energy value chain (particularly oil & gas and LNG) in developed markets and emerging markets.

He is a chairman of the Intra-Pacific Energy Coalition; international arbitrator at Korea Commercial Arbitration Board International; chairman for energy & natural resources at the International Association of Korean Lawyers; specialist mediator at the Singapore International Mediation Centre; legal advisor at the Korea Plant Industries Association; member of Marketing & Communication Committee of International Gas Union; and member of the Energy & Industry Committee at the Canadian Chamber of Commerce in Korea.

was a case related to a hotel booking in 2016 at the Jeju District Court. The defendant had an agreement with the plaintiff to book 60 hotel rooms for Chinese tourists. But due to the MERS outbreak, many tourists cancelled their trips to Jeju. The defendant argued that his obligation to use 60 hotel rooms should be excused due to the MERS outbreak which prohibited him to perform his obligations. The court decided that the defendant should not be excused to pay for 60 rooms since his obligation under the agreement was to make payments for the hotel reservation, not to use 60 rooms. Therefore, the MERS outbreak did not lead to impossibility to make payments to the plaintiff.

Korean courts have interpreted *force majeure* with a very strict standard. Korean courts have not determined the outbreak of SARS and MERS as *force majeure*. However, the Ministry of Land, Infrastructure and Transportation issued an authoritative interpretation about Covid-19 as a *force majeure* event under Article 17 of the Standard Contract for Private Construction Projects on February 28 2020. It provides that a contractor can request an owner to extend construction periods and additional payments. The owner must immediately confirm the fact claimed by the contractor and take necessary measures, including additional payments or extension of construction periods considering conditions of the site. In addition, the owner cannot impose liquidated damages.

Even though Korean courts have set a high threshold to satisfy elements of *force majeure*, it should distinguish Covid-19 from SARS and MERS because of the nature and severity of Covid-19, and the significant and strong government measures taken by various countries.

Change in law

If a contract includes a clause to cover a change in law, an affected party might ask for extension of time and/or additional payment according to its contract.

On February 12 2020, the Ministry of Economy and Finance issued the public contract management guideline for Covid-19.According to this guideline, government authorities or public agencies must:

- issue stop work orders on construction or service at sites where performance of work is deemed substantially impaired due to confirmed or presumptive positive cases of Covid-19,extend the deadline for performance as necessary, and increase the contract price to cover additional costs incurred by the contractors; and
- where stop work orders are not issued, exempt contractors from liquidated damages for delays due to unavoidable impairment of performance in work or supply in connection with Covid-19 and adjust the contract price in accordance with the requirements for adjustment.

This guideline is only applicable to domestic contracts between government agencies and private parties, and limited to certain situations of public contracts. According to the guideline, if the government orders an employer to shut down a workplace because of a suspected or confirmed case of Covid-19, the employer must shut down the workplace and will be excused from obligations to pay wages to employees. In addition, the employer can apply for a government subsidy of up to KRW 130,000 ($109) per day to offer paid leave to confirmed or suspected employees.

Even though there are government guidelines, whether the employer can be excused from its obligations depends on the interpretation of the contract. If a contract broadly defines law and includes government guidelines, instruction or interpretation, it may satisfy the conditions under the public contract management guideline.

If a contract has very narrow and strict definitions of law or no definitions, it will be very unlikely to be successful to be exempt from its contractual obligations.

Termination

As a legal principle, a contracting party will be entitled to terminate a contract when there is a significant change of circumstances if the following conditions are satisfied:

1. it is unforeseeable at the time of signing of the contract;
2. a significant change of circumstance has occurred without a fault of a party which acquires a right to terminate; and
3. due to such change, it results in direct contradiction to the principle of good faith if contracting parties are bound by an existing contract.

However, Korean courts are reluctant to allow a contracting party to terminate a contract due to a change of circumstances. For instance, the global financial crisis was not a basis for termination.

Therefore, it will be hard to argue that a contracting party is entitled to terminate a contract due to Covid-19.

Liquidated damages

Under Korean law, if a party claims damages against the other party, it must be the other party's fault. The affected party might argue that he/she should be released from liquidated damages for delays if construction is only delayed due to Covid-19 without a fault of a party and pre-existing delay caused by the affected party prior to Covid-19.

International perspectives

In most countries, legal principles may excuse contractual obligations due to *force majeure* or frustration even though each court applies such principles differently. In the case of an international construction contract, if a party believes that it has been affected by Covid-19, it should firstly consider whether there is a clause to cover *force majeure* under its contract. If the contract contains such a clause, a party must carefully look at whether Covid-19 satisfies the definition of *force majeure* and other conditions under the contract. If there is no clause or Covid-19 does not fall within the *force majeure* clause, a party may seek to rely on the change in law or frustration.

Elements of *force majeure*

The *force majeure* clause expressly regulates for unforeseen and uncontrollable events in a contract. Many contracts include the *force majeure* clause to allocate risks of *force majeure* events affecting a party's obligations to perform its work on time. If the contract includes epidemic or pandemic as a *force majeure* event, after the World Health Organization's (WHO) declaration of Covid-19 as an epidemic on March 22 2020, the affected party might argue that the outbreak of Covid-19 should be one of the *force majeure* events in the contract and trigger the *force majeure* clause.

For example, under New York law, if a contract has express terms and conditions to cover *force majeure* events, a party may be excused from its obligations after the occurrence of a *force majeure* event. However, New York courts may not enforce a *force majeure* clause unless a *force majeure* event is specified in a contract and unforeseeable at the time of signing a contract. In common law systems, there is no precise definition of *force majeure*. Therefore, the affected party should rely on contractual terms. Under civil law systems, there might be a doctrine of *force majeure* which means exceptional and unforeseen events. However, it depends on the interpretation of each country's court.

A common thing to consider is a notice to the other party. A typical *force majeure* clause requires an affected party to provide a written notice within certain period. Even if a party claims under law or there is no requirement for notice, an affected party should consider to provide the other party with a written notice of Covid-19 and its impacts to establish its claim. At the same time, the parties should establish protocol for who bears additional costs to mitigate another outbreak of Covid-19, how the relief may be provided, and which remedies will be granted. If a contract has a notice requirement, the party must strictly comply with the requirement. Even if there is no requirement of the notice, the claiming party should consider providing a written notice to the other party.

Frustration

After a party considers a *force majeure* clause, the next call is frustration. Frustration arises when the parties under a contract become incapable of performance due to an intervening event which makes further performance totally different from what the parties contemplated at the time of execution of the contract. To satisfy incapability of performance, such an event makes it commercially or physically impossible to perform further obligations from the date of frustration, or obligations being radically different than those undertaken at the time of execution of the contract. Therefore, a party cannot invoke the doctrine of frustration when there is delay of schedule, economic hardship, change in market situation, or financial loss to perform its works under a contract. It is a very high and strict standard to establish. To establish frustration under common law, a party has to show that an event or circumstance destroys its original purpose of a contract.

Under English law, *Davis Contractors Ltd* v. *Fareham UDC* [1956] AC 696 provides the general test for frustration as follows:

> "*…So perhaps it would be simpler to say at the outset that frustration occurs whenever the law recognises that without default of either party a contractual obligation has become incapable of being performed because the circumstances in which performance is called for would render it a thing radically different from that which was undertaken by the contract. Non Haec in Foedera Veni. It was not this that I promised to do.*"

Under New York law, the elements for frustration are as follows:

1. an event must be unanticipated, unforeseeable or unexpected;
2. risks related to such event has not been allocated by a contract; and
3. the parties might perform their obligations, but such performance by one party would not provide that the other party is promised to be bargained at the time of signing a contract.

In addition, according to *Restatement Second of Contracts* § 265, a contract is frustrated "*where, after a contract is made, a party's principal purpose is substantially frustrated without his fault by the occurrence of an event the non-occurrence of which was a basic assumption on which the contract was made, his remaining duties to render performance are discharged, unless the language or the circumstances indicate the contrary.*"

If the contract is frustrated due to Covid-19, contractual parties are automatically discharged from further obligations at the date of frustration, but still remain liable for obligations up to the time of frustration. It depends on the governing law of a contract.

Change in law

There are new regulations, guidelines, ordinance from various government on Covid-19 after the WHO's declaration. Some governments only provided guidelines instead of new laws or regulations. Therefore, the affected party should precisely consider wording of the change in law clause to determine what kinds of relief may be allowed under such a clause.

Insurance

Parties should review any insurance policies to assist them. For example, if a party has business interruption insurance, it should analyse the policy, facts surrounding the causation and losses.

During and after Covid-19

There are two different approaches to capture the impact of Covid-19. One approach is to use a *force majeure* clause to include such a pandemic or epidemic. Another approach is to have an independent clause. The reason for an independent clause is that the remedies applicable to normal *force majeure* events and Covid-19 impacts may be different and contractual elements to satisfy the definition of pandemic or epidemic will also be different.

For example, under Korean law, a *force majeure* event should be unforeseeable and beyond a party's control. Since Covid-19 is a known event for future contracts, to avoid the risk that a similar situation in the future is deemed foreseeable and under a party's control, the parties must ensure that such a risk is properly addressed in a contract. Therefore, it is necessary to have a new clause to cover a pandemic or epidemic. When drafting or negotiating such clauses, it is important to exclude a foreseeability element from the definition. The definition should be broad in order to cover guidelines, notes, or interpretations from governments or international organisations. In addition to a new clause, to mitigate its risks, a party must pass its risks related to the epidemic to subcontractors and vendors, including the governing law.

BANKING & PROJECT FINANCE

A guide to cross-border financing in Thailand

Everything you need to know about cross-border financing in Thailand, including market trends, developments and practical tips, by **Sunyaluck Chaikajornwat, Natthida Pranutnorapal** and **Jirapat Thammavaranucupt** of **Weerawong C&P**

In the past, most cross-border financings involving a Thai company consisted in an offshore lender providing financing to a parent of a Thai subsidiary. This structure typically requires security to be provided by the Thai subsidiary. Recently however, several Thai commercial banks have been providing financing to subsidiaries of Thai companies established and operated abroad, for instance in Cambodia, Myanmar, Laos or Vietnam. Classic examples of this might include project financing for a power plant in Myanmar or acquisition financing for the acquisition of shares in Vietnam.

Another notable development has been in Thailand's security interest regime. The implementation of the Business Security Act BE 2558 (2015) (BSA) widened the class of assets that could be taken as security and also solved some issues with using certain types of assets as security. The BSA therefore provides Thai borrowers with more opportunities to access financing and gives lenders more effective security rights. However, this security regulation cannot currently be used in many cross-border financings, as foreign banks only qualify as security receivers under the BSA if they are lenders in a syndicated facility alongside a Thai commercial bank.

Basic framework

If a lender is a financial institution taking deposits in Thailand, it must obtain a licence under the Financial Institution Business Act BE 2551 (2008). A foreign lender simply lending cross-border does not require a licence. While fintech and funding platforms have been progressively developing in the financing market, Thailand only began the process of legalising peer-to-peer (P2P) lending in 2018, by implementing regulations that require a platform operator to obtain a permit before it operates. If a lender does not engage in a lending business (for example, a parent company which on-lends to its

Sunyaluck Chaikajornwat
Partner, Weerawong C&P
Bangkok, Thailand
T: +66 2 264 8000
E: sunyaluck.c@weerawongcp.com
W: www.weerawongcp.com

Sunyaluck Chaikajornwat is a partner in the banking and finance and the mergers and acquisitions practices. He has over 15 years' experience advising major corporations, banks, real estate and investment companies in mergers, acquisitions, joint-ventures and financings in domestic and cross-border transactions throughout South East Asia. His exceptional work in advising clients was recognised in the Asia MENA Counsel Deal of the Year awards in 2016, 2017 and 2018. He obtained an LLB from Thammasat University, a B.Eng from Assumption University, and an LLM from Columbia University School of Law, United States.

Natthida Pranutnorapal
Partner, Weerawong C&P
Bangkok, Thailand
T: +66 2 264 8000
E: natthida.p@weerawongcp.com
W: www.weerawongcp.com

Natthida Pranutnorapal is a partner in the litigation and arbitration practice group at Weerawong C&P. She has extensive experience in corporate transactions, business reorganisation and insolvency. Natthida is recognised as a rising star in restructuring and insolvency by The Legal 500. She is the author of several publications on restructuring and insolvency in Thailand. Natthida obtained an LLB from Thammasat University and an LLM (Merit) (International Business Law) from the University of Essex, UK. She is a Thai barrister-at-law and a notarial services attorney.

Jirapat Thammavaranucupt
Senior associate, Weerawong C&P
Bangkok, Thailand
T: +66 2 264 8000
E: jirapat.t@weerawongcp.com
W: www.weerawongcp.com

Jirapat Thammavaranucupt is a senior associate in the projects and banking practice group at Weerawong C&P. He advises domestic and international clients on capital markets, mergers, acquisitions and public-private partnerships (PPP). He recently advised the Asian Development Bank on public procurement and the Ministry of Finance on PPP in Thailand. He is a regular speaker at training sessions on PPP, corporate governance and anti-corruption law arranged by the Thai Institute of Directors and national law schools. Jirapat has an LLB (1st Class Honours) from Thammasat University and an LLM from the University of Cambridge (Downing College), UK. He is a member of the Lawyers Council of Thailand and a notarial services attorney.

subsidiary), a lending licence is not required.

Security can be taken by way of mortgage, pledge or business security. The following are some key types of assets which can be placed as security:

- **Shares and debt securities:** Security can be taken over shares and debt securities, both in certificated form (by way of pledge) and scripless form (by way of the use of securities as collateral under the Securities and Exchange Act BE 2535 (1992)). A pledge requires a delivery of the written instrument representing the pledged assets to the pledgee. The registration of the pledge in the issuer's share/debenture register is also required to perfect the pledge. Additional actions may be required depending on the type of security pledged. The use of listed or scripless securities as collateral involves special procedures administered through the Thailand Securities Depository Co (acting as the share registrar of Thai listed companies) and a specific securities deposit account.
- **Bank accounts, receivables, and contractual rights:** Security can be taken via (i) a contractual assignment which needs to be made in writing, with a written notice of assignment given to the debtor or consent in writing obtained from the debtor; or (ii) business security under the BSA.

Following the introduction of the BSA, which came into effect in July 2016, contractual rights, inventory, intellectual property, whole businesses and all future assets can be placed as security by way of a business security agreement. Unlike a creditor that takes security by way of assignment, a creditor that accepts business security is regarded as a secured creditor under Thai bankruptcy proceedings. The business security agreement must be made in writing and registered with the business security registration office of the Department of Business Development. The BSA requires that certain prescribed details are specified in the business security agreement, such as the underlying debts and enforcement events.

Nevertheless, a foreign bank not acting through a licensed Thai branch will only be qualified as a security receiver under the

Foreign banks only qualify as security receivers under the BSA if they are lenders in a syndicated facility alongside a Thai commercial bank

BSA if it lends in a syndicated loan alongside a commercial bank licensed in Thailand.

- **Insurance policies:** Security can be taken over insurance policies and generally the parties will require that the lender is named as a (sole) beneficiary in the relevant insurance policy. Additionally, an assignment agreement and business security under the BSA could also be used.
- **Real property:** Security can be taken by way of: (i) mortgage, which must be made in writing and registered with the competent land office in Thailand; or (ii) business security under the BSA, under which real property used in a business (for example, a property development business) may be provided as security by the owner of a real estate project. The perfection requirements mentioned for bank accounts, receivables, and contractual rights will also apply.
- **Plant and machinery:** Security can be taken by way of: (i) mortgage over machinery that has been registered with the Department of Industry; or (ii) business security under the BSA in the case of machinery used in a business. Following the implementation of the BSA, unregistered machinery can be provided as security by way of business security instead of a pledge, which has an impracticable possessory requirement. The formalities for a machinery mortgage are the same as those for a real property mortgage, as is the perfection requirement.
- **Intellectual property:** Security can be taken by way of business security under the BSA. Currently, only a few business security agreements in respect of intellectual property are registered with the relevant authority. This is partly because of the complications involved with appraising the value of intellectual property.
- **Future/after-acquired property and floating charges over all assets:** Under the BSA, security can be taken over future/after-acquired property and all assets of a security provider by way of a business security agreement. In addition to the perfection requirement, in the case where a whole business is provided as security, the security receiver must, when proceeding with the registration, also file the consent of the financial institution which will act as security enforcer on a default.

Lenders should be mindful of several important issues relating to the registration requirements applicable to security interests created in Thailand, including considerations over the timing, expenses and consequences of non-registration. For instance, the failure to register a mortgage – which incurs a mortgage registration fee – will result in the mortgage being void and unenforceable. Pledges of shares or certain other instruments also need to be registered in the share register of the issuing company so that they can be enforced against a third party and the issuing company.

The BSA has also established a new registration regime for business security agreements, using an online registration system with the Department of Business Development. Once registered, a security receiver will be classed as a secured creditor under the Bankruptcy Act.

The security provider's consent is required to register business security agreements. Further, where certain rights are to be provided as business security under the BSA, if the security provider must obtain the consent of any person before transferring such rights to a third person, the security receiver must submit a letter from such person consenting to the transfer by the security provider of the right to a third person together with the application for registration. A written notice to or written consent from the debtor is recommended in order that the assignment or novation be enforceable against the debtor.

Although mortgages, pledges, business securities or guarantees given in respect of loans will be transferred by operation of law upon the assignment of the loans, on a novation the consent to the transfer of security is required from the third-party security provider. In the case of a mortgage and business security, it is generally recommended that the change of mortgagee and business security receiver be registered with the relevant authority following the assignment or transfer.

In the case that the security is provided by a third party, that third-party security provider would generally have the right of subrogation but in practice, this subrogation right is usually waived.

Thai law limitations

The scope of secured obligations under a mortgage needs to be carefully specified in a contract, as Thai law requires that minimum prescribed details of future obligations be clearly specified. Incomplete details may result in certain obligations not being covered by the mortgage agreement.

A universal security agreement can be used to grant security over all assets in Thailand by way of business security under the BSA.

Thai law does not allow for tiers of creditors except where mortgages are granted with different rankings (for example, first mortgage, second mortgage). Therefore, a contractual arrangement among all relevant creditors is needed to tier different classes of creditors under the same security agreement, (for example, an intercreditor agreement).

Thai law does not have the concept of a security trustee. Only the principal and agent concepts are recognised under Thai law. In practice, an agent can be appointed to enter into a security agreement and hold the security interest on behalf of the creditors, and the agent in this transaction will generally be called a security agent. However, it may be necessary for all creditors to be registered as mortgagees.

Guarantees

Any company can grant a guarantee, as long as giving a guarantee is permitted under its company objectives. No regulatory approval is required for giving a guarantee unless the guarantor is a majority foreign-owned Thai company, in which case a foreign business licence is required. Listed companies should consider the corporate governance rules of the Thai stock exchange.

The Thai Civil and Commercial Code (CCC) sets out some statutory limitations concerning guarantees which may affect their enforceability.

For example, the guarantor cannot agree to be jointly liable as a co-debtor with the primary debtor, unless the guarantor is a juristic person and expressly consents to that joint liability. The lender must also comply with required procedures in enforcing a guarantee. Failure to do so will affect the rights of the lender in enforcing the guarantee or in claiming accrued default interest from the guarantor. Certain provisions of the CCC cannot be excluded or varied by contract, and guarantee terms which attempt to do so will be unenforceable.

Enforcement

Local courts usually recognise and enforce foreign law governed contracts, if the foreign governing law is proved to the satisfaction of the Thai court and is not considered contrary to public order or the good morals of the people of Thailand. However, any judgment obtained in a foreign court will not be enforced by a Thai court and the creditor would have to start new proceedings in Thailand. Such a foreign judgment can (at the discretion of the Thai court) be admitted as evidence in new proceedings in a Thai court.

Final foreign arbitral awards can be enforced through Thai courts, provided that the award was issued in a jurisdiction that is a party to the 1958 New York Convention on Recognition and Enforcement of Foreign Arbitral Awards, and subject to the requirements and provisions of the Thai Arbitration Act BE 2545 (2002).

The main factor impacting timing, when enforcing security, is the nature of the enforcement process under Thai law. A pledge must be enforced by way of public auction (or, for listed securities, sale on the stock exchange), and for mortgage enforcement, court proceedings and (save for certain exceptions) a public auction are required. Before enforcement, certain procedures are required (for example, reasonable demand notice to the debtor). According to the BSA, the enforcement procedures are, in principle, less time-consuming as they do not require court involvement, and foreclosure of the secured asset or transfer of the secured asset by the lender is permissible. However, there are currently no precedents relating to enforcement of this type of security.

The scope of secured obligations under a mortgage needs to be carefully specified in a contract

Restrictions on foreign lenders depend on the type of asset. For example, in the case of mortgaged land, a foreign lender should be aware of the restriction under the Land Code which prohibits a foreign entity from owning any land in Thailand. If the security is a pledge of shares in a Thai company, it must be ascertained whether the business of the Thai company is subject to the Foreign Business Act or any specific law regulating that business which imposes foreign ownership restrictions.

Restructuring and bankruptcy

The available insolvency procedures in Thailand are bankruptcy and business reorganisation.

In relation to the former, bankruptcy proceedings may be initiated by a creditor, in normal cases, or a liquidator of a company in the case of liquidation. After the Bankruptcy Court grants a receivership order, all rights and powers relating to management of the debtor's assets and business will be passed to the Official Receiver. Thereafter, the Official Receiver will carry out its duties of determining the debtor's assets and liabilities.

It generally takes around six months for the Bankruptcy Court to issue a receivership order against the debtor, and another six months to one year before the Bankruptcy Court issues a bankruptcy order. A period of discovery and sales of the debtor's assets, generally by public auction, as well as distribution of proceeds thereof to eligible creditors, will continue on a case-by-case basis.

In order to be entitled to a claim in the bankruptcy, unsecured creditors must file a debt repayment application with the Official Receiver within a prescribed time limit.

On the other hand, secured creditors have two options for recovery: to enforce their respective security interests that the debtor has provided prior to the receivership order, without participating in the bankruptcy process; or to file a debt repayment application for repayment in full if the creditor agrees to surrender the secured assets for the benefit of all creditors, or for repayment of only the balance of the debt remaining unpaid if it has enforced its security or agreed to have the secured asset enforced in the bankruptcy proceedings.

The business reorganisation procedure is available to a debtor that is a juristic person and can be initiated by a creditor or a government agency (involuntary case) or by the debtor itself (voluntary case).

After the Bankruptcy Court's acceptance of a business reorganisation petition, an automatic stay or moratorium will bar creditors from seeking enforcement against the debtor's assets, while the debtor can only conduct its normal business operation. Thereafter, the Bankruptcy Court may order the reorganisation of the debtor's business, and appoint a planner, proposed by the filing petitioner or elected by the creditors' meeting, as the case may be. A reorganisation plan will then be prepared by the planner. According to the plan, the creditors will be divided into classes (depending on the security they hold and the characteristics of the debts owed to them) and the terms of debt repayment to each class will be specified therein. The plan will be considered and accepted by the creditors' meeting, and, eventually, approved by the Bankruptcy Court. After such approval, reorganisation of the debtor's business, as well as repayment to the creditors, will commence pursuant to the plan.

A business reorganisation proceeding takes around one year from the filing of the petition to the Bankruptcy Court approving the plan, where there no creditor objections arise. Where here are objections, the period might be extended by another six to nine months. The implementation of the plan itself should take around five years from the date the Bankruptcy Court, this period of which can be extended twice for not more than one year each time.

Clawbacks and stay on enforcement

A transaction prejudicial to creditors of an insolvent company can be revoked by the Bankruptcy Court, provided that the beneficiary of the transaction was aware of the transaction's prejudicial nature. If the transaction occurs within one year prior to filing of petition for bankruptcy or business reorganisation, or thereafter, or is gratuitous, or the insolvent debtor receives less than a reasonable amount of compensation for that transaction, there is a rebuttable presumption that the beneficiary was aware of the prejudicial nature of the transaction.

Undue preference given to any creditor within the three-month period prior to a bankruptcy or business reorganisation petition, and thereafter, can be revoked by the Bankruptcy Court. If the beneficiary creditor is an insider of the debtor, the hardening period will be extended to a year.

Business reorganisation proceedings do provide for a moratorium on the enforcement of lender claims. An automatic stay comes into effect once the court accepts the business reorganisation petition and continues thereafter during the reorganisation proceedings. The stay prevents certain activities, for example, pursuing existing lawsuits by the creditor, filing of civil claims or action against the debtor, or enforcing security or repossessing property owned by the creditor.

CAPITAL MARKETS
CAPITAL RAISING & COVID-19

A capital time to tap the markets

In part one of this two-part series, Baker McKenzie lawyers outline how equity capital markets have come to the rescue of listed companies struggling with the ongoing liquidity crisis. Part two is available at iflr.com

Over the past few months, global stock markets have experienced high levels of volatility and general uncertainty in light of the economic disruptions caused by Covid-19. The unprecedented nature of the coronavirus pandemic and its impact on global economies makes it difficult to predict with any certainty how long Covid-19 will continue to meaningfully affect financial markets. This provides challenges for many listed companies that need to raise capital in the short to medium term, particularly those that require funding on an urgent basis to meet upcoming debt or other contractual commitments, or to simply satisfy ongoing working capital requirements with insufficient other sources of liquidity. As the United States Federal Reserve chair Jerome Powell recently cautioned: "The recovery may take some time to gather momentum, and the passage of time can turn liquidity problems into solvency problems." Notwithstanding stock market volatility, the equity capital markets provide a number of options that many companies will be eager to explore, including private investment in public equity (PIPE) and follow-on equity offerings.

Private investment

As liquidity concerns have crystallised and come under additional scrutiny, businesses are finding it more difficult to secure conventional sources of funding in a timely manner. One possible solution for listed companies seeking to raise capital and boost balance sheets may be a PIPE transaction. Such transactions - in which common or preferred shares or convertible debt, in some cases with warrants, are issued at a set price to investors - allow the issuer to raise capital not otherwise available in the public markets. It can do this more quickly and cost effectively than other more heavily regulated means of equity capital raises, such as public offerings.

1 MINUTE READ

Against the backdrop of the human tragedy the ongoing pandemic has brought, many companies are facing their own battle for survival. The mandatory closures, sheltering and reduced consumer demand from the Covid-19 pandemic poses challenges to corporate revenues and even business viability, triggering the furlough or redundancy of tens of millions of people while others work under radically altered circumstances. In this first of a two-part series covering both equity and debt markets, Baker McKenzie lawyers consider how equity capital markets have been coming to the rescue of listed companies struggling with the pandemic-driven liquidity crisis. Part two is available at iflr.com

The equity capital markets provide a number of options that many companies will be eager to explore

In some jurisdictions, PIPE investments are often coupled with pre-emptive offers to existing shareholders to give such investors the opportunity to provide some of the required funding and avoid significant dilution of their shareholdings. PIPE deals may present a number of advantages to issuers, such as the speed in raising capital (possibly one to two weeks depending upon jurisdiction), lower transaction expenses than public offerings, streamlined pre-transaction disclosure materials (or potentially no such disclosure materials, depending on jurisdiction) and failed transactions not impacting the market, as transactions are disclosed only after definitive investment commitments.

PIPE deals are commonly used in a rescue situation or when market prices do not fully value a company. They often involve relatively short-term investors who will look for a clear exit route. Private equity investors often seek, and in some cases will require, influence over management (such as by obtaining board representation and possibly seeking anti-dilution or negative control rights). In some cases, companies have used a PIPE as a defensive tool with the addition of a substantial investor with rights to board representation aligned with existing management creating additional confidence in the company's leadership. For some issuers, PIPEs may be seen as a last resort given the pricing discount often entailed, and because they may provide governance rights for the investor that a company does not want to relinquish.

The regulation, and thus the use, of PIPEs varies between jurisdictions. In some jurisdictions, including much of Europe, investor sentiment is traditionally opposed to non-pre-emptive offers that dilute existing investors, and there may be significant legal hurdles and institutional investor guidelines issues that complicate the structuring of PIPEs. In those jurisdictions, PIPEs have historically only been used by troubled small-cap companies with limited options to raise capital through traditional financing options (such as underwritten public equity offers, debt and convertible securities offerings, and bank finance).

One particular challenge that a company may need to address when structuring a PIPE relates to any hedging element. When stock markets began their precipitous fall in March, several countries, including Austria, Belgium, France, Italy, and Spain imposed temporary short selling bans. Although such bans were lifted as markets stabilised, they could potentially be reimposed in the future. If the structure of the PIPE has a hedging element (for instance, as a convertible bond or warrant) then consideration will need to be given to whether there is a ban on short selling of the issuer's stock, and what exceptions may be available.

In other jurisdictions, PIPEs have been a longstanding feature of the markets – for example, in the US, the size, diversity and volume of PIPEs increased dramatically during the global financial crisis of 2008-2009, and we are again witnessing a significant spike in the wake of Covid-19. In the US, there is a relative lack of restrictive regulation for PIPEs, particularly for companies whose charters authorise so-called blank check preferred stock. The primary considerations include certain stock exchange mandated shareholder approval for issuances at or above 20% of the outstanding voting stock or certain insider participation, a notification requirement under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, for issues above a certain level (approximately $94 million) and, for foreign investors, notification and approval considerations under the Committee on Foreign Investment in the United States (CFIUS) regulations.

Existing shareholders asked to dig deep

While shareholders typically hope to enjoy the benefits that owning a stake in a company can bring, the flipside is that, during times of financial stress, they may be called upon to support the business by injecting further capital to help ensure a company remains viable and able to continue trading. We are now seeing a wide range of companies making calls on existing shareholders via a variety of follow-on equity offerings (also sometimes referred to as secondary capital raisings, although these usually involve the resale by a shareholder of its existing securities). These include rights offers, open offers and placings, although the exact terminology and options available will vary between jurisdictions.

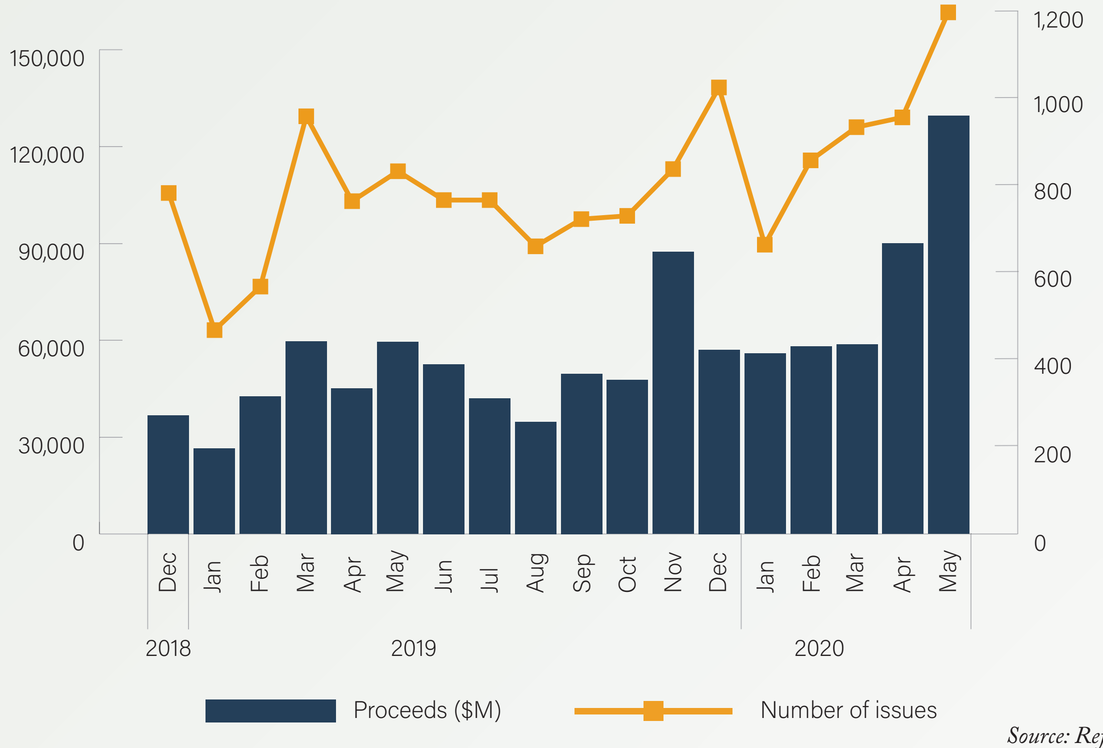
Globally, the number of follow-on offerings increased 20% from 1,805 in the first quarter of 2019 to 2,174 in the first quarter of 2020, with the proceeds raised rising 34% to $172.9 billion. During Q1 2020, there was a steady rise in the number of offerings and the proceeds raised.

As time has passed and the scale of the health crisis and its economic impact have become clearer, companies have been in greater need of capital and liquidity. The result of this is that global issuance volume rose to 1,028 in May 2020, with total proceeds rising significantly, to $129.54 billion. This represents an increase in proceeds of 44% from $90 billion from 835 issues for the previous month, with total proceeds more than doubling from the $59.45 billion from 736 issues recorded in May 2019.

In the UK, the most common structure adopted by companies with premium listings which have undertaken pre-emptive secondary capital raisings in recent years have been rights issues that involve an offer of new shares, for cash, made to existing shareholders on a pre-emptive basis. Pre-emption means that the rights to subscribe the shares are first offered to the existing shareholders in proportion to their existing holding in order to prevent a dilution of the shareholding when the number of shares increases. Shareholders on the

We are now beginning to see a wide range of companies making calls on existing shareholders

Follow-on offerings



Source: Refinitiv

As time has passed and the scale of the health crisis and its economic impact have become clearer, companies have been in greater need of capital and liquidity

register of members at a designated record date are issued with a pro rata entitlement to so-called nil paid rights for no consideration. Nil paid rights entitle the holder to subscribe for the new shares being offered by the issuer at an offer price, which will be set at a – usually significant – discount to the market price to encourage takeup. Rights are also separately tradable securities, so even shareholders who do not participate can extract some value by selling the rights on market during the offer period and so be compensated for the dilution of their shareholding when the additional shares are issued.

For shareholders who take no action, also known as lazy shareholders, underwriters will endeavour to build a book of demand, then place in the market the shares represented by the rights that were not taken up, known as the rump. If the rump placing is successful, attaining a price per share above the issue price, any excess above the issue price (less expenses) is distributed to the lazy shareholders. If the rump placing is not successful, underwriters take any shares unable to be placed (the stick) at the issue price. Issuers like rights issues because, either way, they get the same proceeds as if all shareholders had taken up their rights.

A less common form of pre-emptive issue is an open offer. This allows for a pro rata offer of new shares, for cash, to be made at a narrower discount to the market price than would be the case for a rights issue. An open offer is again made to shareholders on the register of members at the record date but, in contrast to the nil paid rights issued in a rights issue, an open offer entitlement cannot be traded. Except in very rare cases, shareholders who do not subscribe for new shares in an open offer do not receive compensation and are also diluted.

Open offers are less popular with many shareholders due to this inability to trade the right. One advantage to open offers, though, is that where shareholder approval is required, the notice period for the general meeting may run concurrently with the open offer period. If the shareholders vote down the open offer, then the new shares are simply not issued. Underwriters will seek to place any shares representing allocations not taken up by existing shareholders with third party investors.

As an alternative to a pre-emptive issue structure, a placing allows for a non-pre-emptive issue of new shares (or sale of treasury shares) for cash to selected or preferred subscribers. In many jurisdictions, company law provides shareholders with pre-emption rights, and so a waiver of such rights may first be required. Shareholders typically consider pre-emption rights a fundamental anti-dilutive protection measure for shareholders. In a sign of the impact of the Covid-19 crisis on company balance sheets and the urgent need to raise capital to maintain solvency, the UK's Pre-Emption Group issued a statement on April 1 recommending that investors, "on a case-by-case basis, consider supporting issuances by companies of up to 20% of their issued share capital on a temporary basis, rather than the 5% for general corporate purposes with an additional 5% for specified acquisitions or investments, as set out in the Statement of Principles". If a company requires this additional flexibility, then it should consult with major shareholders and fully explain the circumstances underpinning the decision. The recommendation for investors to apply additional flexibility is currently in place on a temporary basis until November 30 2020.

In Australia, the ASX also announced temporary emergency capital raising relief, which was extended in July, also to November 30 2020. Key to the ASX's relief measure is that it will temporarily allow an uplift from the standard 15% placement capacity to 25%, provided that any placement is made in conjunction with a follow-on accelerated entitlement offer or share purchase plan, in each case, at the same or lower price than that offered under the placement.

A placing typically involves a launch announcement, limited marketing (if any), and then a bookbuild undertaken by an investment bank, with the results of the placing being announced ideally prior to market open the next day. It is popular with issuers because they can be undertaken on a relatively tight timetable, as neither a prospectus nor a shareholder meeting is usually required. Several underwriting options are available, including best efforts/reasonable endeavours, backstop, bought deal or various forms of upside sharing. Although in the UK, these have rarely been sized greater than 10% of issued share capital (to comply with guidance) they can now go to 19.9% without publishing a prospectus (based on the EU Prospectus Regulation).

In some jurisdictions, it is common to see a placing combined with an open offer in what is known as a placing subject to clawback. Under this structure, the new shares are placed with institutional investors who effectively underwrite the issue. The placing is subject to an open offer being made to existing shareholders to take up their pro rata entitlements. This, therefore, provides an opportunity for existing shareholders to clawback shares from placees. The price paid for the new shares is usually at a discount to the current market price of the existing shares. Placees will buy shares not taken up by the existing shareholders, thus ensuring the success of the offering.

In the UK, all of the follow-on offerings described above can also be combined with a cashbox structure. No difference is apparent to subscribing investors, as they still pay cash for new shares, but technically the issue of the new shares is for non-cash consideration (being the shares in the cashbox company into which the cash proceeds from the subscribing investors will have been channelled). The advantages of this structure are that it permits an issue of new shares without necessarily requiring a disapplication of statutory pre-emption rights, which can be useful for timing reasons, for convenience (investors in problematic jurisdictions can be excluded), or in order to generate distributable reserves. Employing a cashbox structure to a cash placing as a means of avoiding compliance with statutory pre-emption rights has recently fallen out of favour, although it remains to be seen whether investor bodies and commentators will feel as strongly during turbulent times such as we are currently experiencing.

Recovery and renewal

With the onset of the pandemic in 2020 and the initial shock to markets, both companies and individuals have become more resilient as they adapt to the changing landscape. While government intervention schemes have put the global economy on life support, as we move into the next phases of recovery and renewal, alternative transactions in the capital markets will still present opportunities for both companies and investors to seize capital raising and investment opportunities. As during the global financial crisis, listed entities have turned to such capital markets transactions as an efficient and viable solution to mitigate the uncertainties and pave a way forward, and are expected to continue to do so.

Lisa Fontenot
Partner
Baker McKenzie, Palo Alto
lisa.fontenot@bakermckenzie.com

Kenny Kwan
Partner
Baker McKenzie, Singapore
kenny.kwan@bakermckenzie.com

Roel Meers
Partner
Baker McKenzie, Brussels
roel.meers@bakermckenzie.com

Mark Bell
Lead Knowledge Lawyer
Baker McKenzie, Singapore
mark.bell@bakermckenzie.com

CAPITAL MARKETS
SWISS MARKET RULES

New Swiss financial market rules: a guide

Homburger lawyers explain what financial service providers need to know about the new rules, which are now in effect

On January 1 2020, the Financial Services Act (the FinSA) and the Financial Institutions Act (the FinIA) entered into effect in Switzerland. Numerous provisions of the FinSA and the FinIA, however, did not become effective immediately, because new institutions envisaged under the FinSA and the FinIA were not yet in place. The countdown on certain transition periods provided for by the FinSA and the FinIA has only started to run from the time these new institutions were in place. In the meantime, the Swiss Financial Market Supervisory Authority FINMA (FINMA) has approved these institutions and the transition periods are running.

As a result, Swiss and non-Swiss parties that are subject to these new Swiss financial market regulations are now required to take action. With regard to non-Swiss parties, this will include, in particular, financial service providers that offer financial services to clients in Switzerland (see below, registration bodies and ombudsman's offices) and parties involved in public offers and/or admissions to trading of securities on a trading venue in Switzerland (see below, reviewing bodies).

New institutions under the FinSA and the FinIA

Registration bodies: The registration bodies are provided for in the FinSA. They maintain the registers on which Swiss and non-Swiss client advisers are required to register if they provide financial services in or from Switzerland. The registration bodies are approved by FINMA.

Reviewing bodies: The reviewing bodies are provided for in the FinSA. They are the new Swiss prospectus approval authorities. Prospectuses approved by a reviewing body are required for the purposes of a public offer or an admission to trading of securities on a trading venue in Switzerland. The reviewing bodies are also approved by FINMA.

1 MINUTE READ

The new institutions under the Financial Services Act and the Financial Institutions Act have been approved by FINMA and the transition periods for compliance with the new regulations are running. The new institutions include (a) the registration bodies which maintain the registers of client advisers providing financial services in Switzerland, (b) the reviewing bodies which review and approve prospectuses, (c) the ombudsman's offices which offer a mediation procedure for disputes between financial service providers and their clients and (d) the supervisory organisations which supervise the Swiss asset managers and trustees. The Swiss and non-Swiss parties subject to these new regulations are now required to take action to comply with the new regulations.

Eduard De Zordi
Counsel, Homburger
Zurich, Switzerland
T: +41 43 222 16 57
E: eduard.de_zordi@homburger.ch
W: www.homburger.ch

Eduard De Zordi's practice focuses on banking, financial and capital markets law.

He specialises in particular in offerings of debt securities. He also advises on contract and company law.

Eduard De Zordi is registered at the Bar of the Canton of Zurich and is an authorised issuers' representative at the SIX Swiss Exchange.

FINMA approved BX Swiss Ltd as the first registration body with effect as of July 20

Ombudsman's offices: The ombudsman's offices are provided for in the FinSA. Swiss and non-Swiss financial service providers that provide financial services in or from Switzerland are obliged to affiliate themselves with an Ombudsman's office to provide for a mediation procedure for legal disputes between clients and financial service providers. The Ombudsman's offices need to be recognised by the Swiss Federal Department of Finance.

Supervisory organisations: The supervisory organisations are provided for in the FinIA. They supervise Swiss asset managers and trustees. The supervisory organisations need to be approved by FINMA.

Registration bodies

Client advisers of Swiss financial service providers that are not already subject to prudential supervision, and client advisers of non-Swiss financial service providers that provide services in Switzerland, are obliged to register as client advisers. The registers of client advisers are maintained by registration bodies. The registration bodies also verify that the client advisers have completed the necessary training and further education.

Client advisers of non-Swiss financial service providers which are (a) prudentially supervised outside Switzerland and (b) provide services in Switzerland only to professional or institutional clients (as defined in the FinSA) are exempt from the duty to register as client advisers.

FINMA approved BX Swiss Ltd as the first registration body with effect as of July 20 2020. The approval of further registration bodies is expected.

The FinSA provides for a six-month transition period after the approval of the first registration body for the entry of the client advisers in a register maintained by a registration body. This transition period ends on January 19 2021. In order to meet this deadline, the client advisers need to file their application for entry in a register with a registration body by the end of the transition period.

Reviewing bodies

The reviewing bodies are responsible for the review and approval of prospectuses under the FinSA. The FinSA prospectus requirements apply if securities are publicly offered and/or admitted to trading on a trading venue in Switzerland. An approved prospectus is required before the public offer or application for admission to trading, except in the cases of certain types of securities – such as most bonds – where the review and approval of the prospectus by the reviewing body can occur after the closing of the transaction, but only if a Swiss bank or securities firm confirms prior to the launch of the offering or the application for admission to trading that the most important information on the issuer and the securities is available.

FINMA approved SIX Exchange Regulation Ltd and BX Swiss Ltd as reviewing bodies with effect as of July 1 2020.

Prospectuses of securities that will be listed on SIX Swiss Exchange will typically be submitted to SIX Exchange Regulation Ltd as reviewing body, and prospectuses of securities that will be listed on BX Swiss will typically be submitted to BX Swiss Ltd as reviewing body. However, the approval by either reviewing body is sufficient for the admission to trading on any trading venue in Switzerland.

The FinSA provides for a six-month transition period after the approval of the first reviewing body. During this transition period, the prospectus requirements under the FinSA do not yet mandatorily apply, provided that the Swiss prospectus requirements that were in effect before the FinSA came into effect are complied with. This transition period ends on November 30 2020.

From the end of the transition period, the prospectus requirements of the FinSA need to be fully complied with. Public offers of securities in Switzerland and the admission to trading of securities in Switzerland will require either (a) a prospectus, according to the FinSA and the annexes of the implementing ordinance, approved by a reviewing body or (b) in the case of securities that are eligible for the exception from this ex ante approval requirement, the confirmation by a Swiss bank or securities house that the most important information on the issuer and the securities is available, with the approval of the prospectus to follow after the closing of the transaction.

If transactions are planned in Switzerland between now and November, particular attention needs to be paid to the transition period. The transition period is only available for transactions that are completed by the end of November. If, for example, a transaction was otherwise completed by the end of November but the admission to trading occurred afterwards, such a transaction would be subject to the FinSA prospectus requirements.

Ombudsman's offices

Under the FinSA, clients of Swiss and non-Swiss financial service providers which offer financial services in or from Switzerland shall have an ombudsman procedure available to settle disputes of clients with the financial service providers. For this purpose, the financial service providers are obliged to affiliate themselves with an ombudsman's office recognised by the Swiss Federal Department of Finance.

Currently there are no exceptions to this obligation of financial service providers to enter into an affiliation with an ombudsman's office. However, there is a proposal in the Swiss Parliament to amend the FinSA to provide an exemption for financials service providers which provide services only to professional or institutional clients (as defined in the FinSA).

The Swiss Federal Department of Finance recognized the first four Ombudsman's Offices with effect as of June 24 2020. In the meantime, three further ombudsman's offices have been recognised, and the recognition of further ombudsman's offices is expected.

One of the recognised ombudsman's office is the well-established Swiss Banking Ombudsman, which was set up in 2003 by the Swiss Bankers Association for disputes between members of the association and their clients, long before this was required by the FinSA. Also, now, after recognition as an ombudsman's office under the FinSA, only members of the Swiss Bankers Association are eligible for affiliation with the Swiss Banking Ombudsman. Most of the other recognised ombudsman's offices, such as for example the Swiss Chambers' Arbitration Institution (SCAI), are open for affiliation by all types of financial service providers under the FinSA.

The FinSA provides for a six-month transition period after the recognition of the first ombudsman's office for the affiliation of the financial services providers with a recognised ombudsman's office. The transition period ends on December 23 2020. In order to meet this deadline, financial services providers need to file a completed affiliation request with a recognised ombudsman's office by the end of the transition period.

If transactions are planned in Switzerland between now and November, particular attention needs to be paid to the transition period

Supervisory organisations

Swiss asset managers (other than asset managers of collective investment schemes) and trustees were not subject to regulation in Switzerland (with the exception of anti-money laundering regulations) until the FinIA entered into effect. According to the FinIA, such asset managers and trustees have to be (a) supervised by a supervisory authority approved by FINMA and (b) be licensed by FINMA.

FINMA approved two supervisory authorities (*Organisme de Surveillance des Instituts Financiers* and *Organisation de Surveillance Financière*) with effect as of July 6 2020, and a third supervisory organisation thereafter (*Organisme de Surveillance pour Intermédiares Financiers & Trustees*). The approval of further supervisory organisations is expected.

In respect to asset managers and trustees which became subject to the FinIA at its entry into effect on January 1 2020, the FinIA provides for a three-year transition period to comply with the requirements of the FinIA, including affiliation with a supervisory authority, and to submit a licence application to FINMA. Until the decision from FINMA regarding their licence application, they may continue to conduct their activities, as long as they comply with the applicable anti-money laundering regulations. In addition, such asset managers and trustees were obliged to report to FINMA until June 30 2020.

In respect to asset managers that commenced their activity within one year of the FinIA entering into effect, the FinIA provides for a one-year transition period after the approval of the first supervisory organisation for the asset managers and trustees to join a supervisory authority and file a licence application with FINMA. This transition period ends on July 5 2021. In order to meet this deadline, the asset managers and trustees need to affiliate with a supervisory organisation and submit an application for authorisation to FINMA by the end of the transition period. In addition, such asset managers and trustees are obliged to report to FINMA without delay, as soon as they commence their activities, and satisfy all the requirements of the FinIA with the exception of the affiliation with a supervisory organisation.


CORPORATE INSOLVENCY &
RESTRUCTURING REPORT 2020:
COVID-19 SPECIAL FOCUS

CORPORATE INSOLVENCY & RESTRUCTURING REPORT 2020: COVID-19 SPECIAL FOCUS

Introduction: Lockdown blues

Rebecca Jarvis and Jo Windsor of Linklaters introduce this year's report, which has a special focus on the repercussions of Covid-19

Linklaters

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It quickly became obvious, as countries began to enter into lockdown and many companies were forced to suspend their operations, that a tsunami of insolvencies was likely to follow in those jurisdictions which had been hardest hit by Covid-19, particularly in the event of a second wave of the disease.

Some businesses saw their cashflows dry up with a terrifying rapidity. For those that were already struggling, lockdown was the final straw, with stakeholders taking a view that it was no longer worth fighting to save the business and that the pandemic provided the perfect excuse for closure. The owners of many previously viable businesses chose to mothball all or part of their operations until lockdown ended, only to discover, on emergence, that their business model needed to be significantly adjusted to operate in a world of physical distancing – a problem that was particularly acute in the hospitality, tourism and transport sectors. In other cases, management were confronted with significant liabilities incurred during the lockdown, such as accrued rent or obligations to pay for the supply of no-longer required goods, that had to be urgently addressed.

If this was not difficult enough, pressures on liquidity had an immediate impact on discretionary spend, putting further pressure on the services sector, while consumer confidence was dented by both fear of the disease and fear of its economic consequences, including significant increases in unemployment. It is hardly surprising, in this context, that the first half of 2020 saw a record number of US Chapter 11 bankruptcy filings.

How have legislators sought to head off what, in insolvency terms, might be viewed as a perfect storm? In summary, as illustrated by the chapters in this guide, there has been a three pronged approach, with efforts to provide economic support to hard pressed businesses, the temporary suspension of legislative provisions which could force previously viable companies into insolvency and the

Rebecca Jarvis
Partner, Linklaters
London, UK
T: +44 207 456 4466
E: rebecca.jarvis@linklaters.com
W: www.linklaters.com/en/find-a-lawyer/rebecca-jarvis

Rebecca Jarvis is Linklaters' global co-head of restructuring and insolvency. She has experience in all aspects of non-contentious reconstruction and insolvency work acting for banks, financial institutions, other creditors, corporate clients and insolvency practitioners in relation to recovery, reconstruction or distressed debt problems.

Jo Windsor
Partner, Linklaters
London, UK
T: +44 207 456 4436
E: jo.windsor@linklaters.com
W: www.linklaters.com/en/find-a-lawyer/jo-windsor

Jo Windsor has been working in the field of restructuring and insolvency for over 30 years, specialising in complex cross-border matters. He has been involved in the restructuring of companies in more than 30 different jurisdictions and is the author of many articles addressing specific issues relating to restructuring and insolvency.

It is hardly surprising, in this context, that the first half of 2020 saw a record number of US Chapter 11 bankruptcy filings

introduction of new insolvency legislation aimed at improving the longer-term survival prospects of such companies. Sadly, it often takes a crisis to force insolvency onto the legislative agenda.

Forming a response

Government support initiatives have largely consisted of providing short term financial support to businesses. In the UK, the government has provided loans, deferred tax payments and covered the costs, through the furlough scheme, of employees who would otherwise have been made redundant. In other jurisdictions, such as Hong Kong, companies have benefitted from a temporary moratorium on debt repayments. While such measures allowed struggling companies to survive, the concern going forward is that there will soon be a day of reckoning, as amounts that have been borrowed and payments that have been deferred will need to be repaid or restructured, raising the possibility that government loans may have to be converted into equity stakes.

The temporary suspension of legislative provisions which could force previously viable companies into insolvency can also be viewed as a short term response to the lockdown and its consequences. Examples include France and Germany suspending directors' obligations to initiate insolvency proceedings once their company becomes insolvent and restrictions in the UK on the presentation of winding-up petitions where the relevant company's financial problems are clearly Covid-19 related.

The longer-term response to the impact of Covid-19 has been the introduction, or acceleration, of insolvency legislation, the main aim of which is to give previously viable companies a better chance of survival. At the risk of generalisation, five key trends can be identified in such legislation, some of which clearly draw inspiration from Chapter 11 of the US Bankruptcy Code:

- A desire to limit the ability of shareholders and out-of-the-money creditors to block a restructuring plan which has the support of in-the-money creditors and which a supervising judge considers to be fair and equitable. The widespread introduction of cross-class cram-down procedures, such as those under the Dutch Bill on the Confirmation of Private Plans and the "super scheme" introduced in the fast-tracked UK Corporate Insolvency and Governance Act, reflect this desire.
- The need to give viable companies facing immediate or anticipated financial difficulties an opportunity to prepare a restructuring solution, free from immediate creditor pressure. A model for such protection can be found in the EU Preventative Restructuring Frameworks Directive, which requires a "breathing space" moratorium to be introduced into the legislation of each EU Member State.
- The introduction of light-touch or streamlined insolvency procedures which could be used by struggling SMEs, which may face significant liquidity issues, being heavily represented in sectors such as tourism and hospitality, but which may lack the resources to implement a full restructuring. One example is the Coronavirus Aid, Relief, and Economic Security (CARES) Act, which made important revisions to the US Bankruptcy Code aimed at allowing more struggling SMEs to reorganise their financial affairs in an efficient and cost-effective manner, using a streamlined Chapter 11 procedure.
- A recognition that, while many restructurings over the last decade have focussed on financial indebtedness, the next wave is more likely to include operational indebtedness and that struggling companies should have some legal leverage when dealing with suppliers threatening to take enforcement action or terminate critical contracts. The moratorium discussed

above may assist in such cases, as may the introduction, in some jurisdictions where they did not previously exist, of statutory restrictions preventing supply agreements from being terminated by reason of the counterparty entering into an insolvency procedure.

- An acknowledgment that liquidity will continue to be a major issue going forward, and that prospective lenders should be encouraged to provide funding in appropriate cases, whether by giving new lending statutory priority or by removing deterrents to making funding available to companies facing financial difficulties. In those jurisdictions where there is currently no legislative framework for DIP financing, there have been recent examples of self-help, with existing procedures, such as UK Schemes of Arrangement, being used inventively to create platforms for de facto priority lending.

Where does this leave us, looking ahead over the next year, given that most temporary government support initiatives will cease to apply by the end of that period? It will certainly be an interesting time, with opportunities for those who are in a position to invest or provide liquidity, and challenges for those working with new legislative measures which, in some cases, have been fast-tracked and do not, therefore, answer every question. The challenge for the restructuring and insolvency community is to use the available tools inventively and constructively, limiting, as far as possible, the pain suffered by viable businesses hit by the impact of Covid-19.

Croatia

Branko Skerlev and Mislav Bradvica, Law Office Skerlev
in cooperation with BMWC

Beside the ongoing debates regarding the Extraordinary Administration Proceedings (EAP), which was a tailormade framework to manage the restructuring of Agrokor, market trends show a drop in numbers in both pre-insolvency and insolvency cases. This downward trend originates in the 2015 restructuring and insolvency reform that over-formalised the pre-insolvency process and discouraged debtors from using it. The reform also introduced summary insolvency proceedings for small businesses that are opened and concluded simultaneously if there are no assets available for distribution nor any employees.

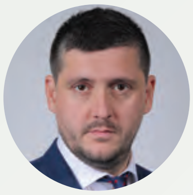
Over recent years, Croatia has been busy wrestling with the restructuring case that emerged when one of its biggest companies, Agrokor, faced collapse. Agrokor was an agricultural, food and retail giant with shares in many subsidiaries. It was intertwined with the whole Croatian economy and had an annual revenue of approximately 15% of the Croatian GDP, as well as being significant source of employment in Croatia. Not long after its financial difficulties were made public, measures were taken to prevent any immediate and future negative impacts of corporate distress within "large systems" on the state's economy. A fast-tracked parliamentary procedure adopted the Act on the Procedure of Extraordinary Administration in Companies of Systemic Importance for the Republic of Croatia (Extraordinary Administration Act).

The "large system" in Croatia represents a company that, independently or together with its subsidiaries or affiliates, has over 5,000 employees and over HRK7.5 billion (€1 billion) in consolidated obligations. The Act stipulates a restructuring via an EAP to ensure liquidity and business stability and to avoid an insolvency filing. An EAP was carried out over Agrokor and its many subsidiaries and affiliates and was successfully concluded at the end of 2018,

Branko Skerlev
Lawyer, Law Office Skerlev in cooperation with BMWC
Zagreb, Croatia
T: +385 5629 767
E: office@bmwc.hr
W: www.bmwc.hr

Branko Skerlev is a partner with at BMWC law firm, where he heads the insolvency/restructuring practice, and a bankruptcy administrator before the Commercial Court in Zagreb, Croatia. Through his career, he has been widely exposed to bankruptcy and restructuring legal matters. As well as advising clients in private practice, Branko has served as a legal advisor to the Croatian State Bank Rehabilitation Agency and as a chief legal adviser for the Croatian leading private equity/alternative investment group, where he handled numerous complex insolvency and restructuring matters.

Branko's other areas of expertise mainly include corporate and M&A, with a special focus on private equity transactions and general investment funds legal issue. Branko is also a lecturer at the Zagreb School of Economics and Management.



Mislav Bradvica
Lawyer, Law Office Skerlev in cooperation with BMWC
Zagreb, Croatia
T: +385 5629 767
E: office@bmwc.hr
W: www.bmwc.hr

Mislav Bradvica is an expert in EU, competition and regulatory law, with an emphasis on antitrust and regulatory litigation. Before establishing Bradica Marić Wahl Cesarec law firm, Mislav chaired Schoenherr's booming Croatian competition department. His experience includes working as a state officer in the Croatian Competition Agency, with special duties concerning cartel, abuse of dominant position and sector inquiry cases.

Mislav's erudition and enormous experience in handling regulatory matters lends our restructuring practice a cutting-edge advisory capability, with a deep capacity for strategic and innovative thinking.

although legal proceedings regarding creditors' claims are still ongoing and many aspects of the EAP itself remain a subject of debate to this day.

One of the hot topics was the inclusion of affiliates and subsidiaries into the EAP regardless of their solvency status. The Constitutional Court ruled that the purpose of the EAP was to examine the solvency of each company involved, since the Extraordinary Administration Act provisions stipulate solely the procedural consolidation of the parties to enable a single proceeding and single settlement for all the debtors involved; no circumstance allows for a unique insolvency estate out of a separate legal entities' assets. Still, it is questionable whether the final settlement also contained the elements of substantive consolidation dismissed by the Constitutional Court and there are many pending lawsuits concerning this issue before the Supreme Court.

Excepting the EAP, Croatia's very own too-big-to-fail restructuring case, another significant development has been the inclusion of pre-insolvency proceedings within the new Insolvency Act, adopted in 2015. Prior to September 2015, pre-insolvency was a combination of administrative and court proceedings, and though it was severely criticized due to the controversies concerning its implementation, it still enabled a rather expedited restructuring. The 2015 insolvency and restructuring reform created many obstacles for pre-insolvency proceedings, resulting in a significant reduction in the number of distressed companies filing a petition and an increase in companies opting for informal settlements with large creditors instead.

Four pillars

The restructuring and insolvency models available in Croatia are pre-insolvency proceedings; insolvency proceedings; insolvency plan; and the EAP. Each of the model is conducted and supervised by a commercial court, but the managing regimes differ from retaining some representation and responsibilities for maintaining business to complete shift in the managing powers.

Pre-insolvency proceedings as a voluntary restructuring model may be initiated by a debtor under condition of imminent insolvency. Imminent insolvency exists if the court determines that the debtor will be unable to fulfil its outstanding monetary obligations upon their maturity. The debtor is "imminently insolvent" if it has unsettled monetary obligations registered with the Financial Agency, or if the debtor has defaulted on salaries, employment-related contributions or taxes for more than 30 days.

The grounds for initiating insolvency proceedings are insolvency and/or over-indebtedness. Insolvency of a debtor is presumed if a debtor has one or more due and unsettled obligations recorded in the register for more than 60 days or if a debtor has failed to pay three consecutive salaries to its employee(s). A company is deemed to be over-indebted when its liabilities exceed its assets. Filing a petition for insolvency proceedings is mandatory within 21 days following the occurrence of either of the prescribed insolvency reasons. A petition may also be filed by the Financial Agency, which is obliged to submit a petition if its records show that a company has one or more registered outstanding payments over an uninterrupted period of 120 days.

Unless the insolvency plan is adopted to restructure a debtor's business, insolvency proceedings are completed after all the debtor's assets are sold, after which the debtor is liquidated.

The insolvency plan is a restructuring model within formal insolvency proceedings which allows for modifications of rules on sale and distribution of the insolvency estate. A proposed insolvency plan may be submitted by the insolvency administrator by the final hearing, at the latest.

The EAP is the restructuring model for companies deemed of strategic importance and applies only to companies or groups with more than 5,000 employees and €1 billion of debt.

Unlike in an insolvency proceeding, which lasts as long as there are assets left to be sold, all the restructuring models are time limited and the restructuring plan must be proposed and adopted within the certain time frame after opening of the proceedings.

Directors' duties

Filing a petition for insolvency proceedings is mandatory within 21 days of the occurrence of either of the prescribed insolvency reasons (as discussed above). Persons obliged to commence mandatory insolvency proceedings who fail to do so are personally liable to creditors for any damage caused by this omission.

Management board members and liquidators could also face criminal liability since failure to initiate insolvency is a felony, with prescribed penalties of a monetary fine or imprisonment of up to two years. However, in practice these sanctions are rarely imposed.

Formal filing

From the day a formal pre-insolvency proceeding is opened to its completion, all pending civil, enforcement, interim measures and administrative proceedings against the debtor are stayed and initiating any such proceedings against the debtor is forbidden. This does not apply to creditors that are entitled to separate satisfaction; creditors with exclusion rights; debtor's former and current employees' claims up to prescribed amounts; security measures in criminal proceedings; and tax proceedings for determining the abuse of rights, since formal opening of pre-insolvency proceedings does not affect those. During this same period, the debtor may only make payments necessary for regular operations and fulfil the obligations attached to post-petition credit (discussed further below).

As for insolvency proceedings, the pending proceedings are suspended, legal disputes regarding the debtor's assets may no longer be filed but all claims must be filed within the insolvency proceedings and examined by the insolvency administrator. The insolvency administrator is entitled to continue any suspended proceedings if a claim has been determined and any creditor whose claim has been disputed by the insolvency administrator may initiate proceedings against the debtor. Also, once the insolvency proceedings have been formally opened, all creditors but creditors with exclusion rights are prevented from enforcing their claims and pending enforcement and interim measures proceedings are stayed.

Commencement of insolvency proceedings also affects some contracts. Namely, mandate and similar contracts relating to the debtor's assets are terminated, lease and employment contracts remain in place and all other contracts that have not been performed by either party in full may be either rejected or adopted by the insolvency administrator. When the insolvency administrator opts for rejection of fulfilment of any such contract, any damages incurred by the contractual counterparty may be filed as an ordinary insolvency claim.

All legal consequences of opening insolvency proceedings also apply to an EAP.

Priority, dissenters and asset sales

The insolvency estate's obligations, including the costs of the insolvency proceedings, maintenance and management expenses, the insolvency administrator's fees, certain employees' claims and other claims stipulated by the Insolvency Act, are payed as they fall due and therefore implicitly have preferential status.

The priority status of other claims is as follows:

- creditors with exclusion rights with proprietary claims regarding certain assets are not affected by the insolvency;
- creditors with separate satisfaction rights have priority over unsecured creditors in settling their claims out of the value of the security;
- creditors with claims of a higher priority are settled before creditors of a lower priority;
- claims arising from employment agreements have higher priority over other claims; and
- claims regarding interests, creditors' procedural expenses, fines, and loans replacing share capital have lower priority than the other claims.

As for post-petition credit, fresh money is not protected if it is granted outside the statutory limitations stipulated by the Insolvency Act regarding pre-insolvency and insolvency proceedings.

The debtor is explicitly forbidden from disposing or burdening the assets in the period after filing a petition until the formal opening of the pre-insolvency proceedings, so is therefore indirectly disabled from borrowing. Once the pre-insolvency proceedings have been opened, approval must be obtained from creditors holding two-thirds of total claims in value to enter into loan or credit agreements. Obligations arising from such loans are paid as they fall due. Where restructuring efforts fail and insolvency proceedings are opened, post-petition creditors have priority over all the other creditors except employees, who have a higher priority rank.

Within insolvency proceedings, the insolvency administrator is entitled to enter into loans, or other credit agreements, to secure financing for the resumption of the debtor's business. Approval of the creditors' committee for such undertakings is only required if a loan would significantly burden the insolvency estate. Creditors with claims arising from any post-petition loan are considered creditors of the insolvency estate and therefore their claims have priority and are paid as soon as they become due. The stipulation resolving the legal position of the providers of post-petition loans was introduced into the Insolvency Act by amendments in 2017 that were prompted by the adoption of Extraordinary Administration Act.

Post-petition crediting is also allowed during an EAP, providing the extraordinary commissionaire has granted approval to managing directors of subsidiaries and affiliates and that the extraordinary commissionaire has obtained approval of the creditors' committee, when required.

As a general rule, the Croatian Insolvency Act asserts the principle of equal treatment of creditors and the priority ranks of claims are established by law. Therefore, involuntary cramming-down of either individual creditors or classes of creditors within the insolvency proceedings is not possible, whether by court or insolvency administrator decision. On the other hand, a cram-down mechanism may occur within pre-insolvency proceedings or insolvency plan proceedings where the majority of creditors binds the minority. Once the legal majorities of votes have been reached and the court has approved a settlement or a plan that lowers the rank of some claims, it becomes enforceable against all the creditors.

The sale of debtor's assets is managed by the insolvency administrator and supervised by the court. However, the creditor's assembly is authorised to determine conditions regarding the disposal of assets and hence may facilitate the sale. If no conditions are set forth, rules which regulate enforcement apply, meaning that assets are sold at public auctions and that the starting price decreases at each subsequent auction. Prior to the sale of significant assets, including entire or a part of an enterprise, approval of creditor's council must be obtained. Although the sale of individual assets prevails, the Insolvency Act also sets out an option for selling the distressed debtor's entire business, a part of it, to ensure its continuation.

The Insolvency Act only enables the recognition of insolvency matters in the narrowest sense

Challenging a debtor's transactions

The Croatian Insolvency Act provides for various grounds for clawback, with different suspect periods ranging from one month to 10 years prior to the opening of insolvency proceedings. Grounds for contesting transactions include, among others, the fulfilment of debt or granting a security that the counterparty could not have claimed or while illiquid, intention to disadvantage creditors including awareness of counterparty, granting security for shareholders' loan and undertaking transactions free of charge or for insignificant reimbursement.

Debtor 's transactions may be challenged before the court either by the insolvency administrator or the creditors. If the voidance motion is successful, transaction will be declared to be without effect and anything that was transferred from the assets of the debtor must be restored to the insolvency estate.

Other considerations

Croatia has somewhat modified insolvency and restructuring regimes for banking and finance sector.

Namely, neither pre-insolvency nor EAP can be initiated over a financial or credit institution, credit union, investment company, investment fund management company, insurance and reinsurance company, leasing company, institution for payments or institution for electronic money. Concerning restructuring and insolvency, some specific rules are also stipulated by the Credit Institutions Act, Capital Markets Act and Insurance Act.

Generally, the key figures in the restructuring and insolvency proceedings are the court, the insolvency administrator and the creditors within the creditors' committee and creditors' council. With only few exceptions, the only governmental institution which could impact the outcome of a reorganisation is the Ministry of Finance – if there is a substantial tax and/or contributions debt and a willingness to reschedule or writing-off such debts.

Additionally, the Government and the Ministry of Commerce can have a significant impact on an EAP since the commercial court appoints the extraordinary commissioner in accordance with a proposal made by the Government, and the Ministry of Commerce appoints the members of the Advisory Board.

Restructuring and insolvency proceedings affecting debtors from banking and financial sectors are subject to approvals and supervision of the respective regulators (the HNB and the Croatian Financial Services Supervisory Agency – Hanfa).

Crossing borders

There are no provisions either within the Insolvency Act or the Extraordinary Administration Act enabling international jurisdiction for pre-insolvency proceedings and EAPs, but only for opening and conducting insolvency proceedings. Therefore, as long as the Croatian courts have jurisdiction, an insolvency proceeding - and nothing else - can be opened in respect of a foreign debtor in Croatia; so, the only statutory restructuring channel open to a foreign debtor is an insolvency plan.

Croatian courts have exclusive jurisdiction regarding insolvency proceedings over debtors whose centre of main interest (COMI), defined primarily as the place of registered office, is situated within Croatia. Nonetheless, Croatian courts also have exclusive jurisdiction if the debtor's registered office is in Croatia but it is proven that its COMI is in another country whose legislation does not recognize COMI as a criterion for its courts' jurisdiction over insolvency proceedings; or otherwise, if the debtor's registered office is in another country but it is proven that its COMI is in Croatia. Croatian courts also have jurisdiction over secondary insolvency proceedings but only regarding debtor's assets situated within Croatia under conditions provided under Insolvency Act.

A foreign court decision concerning the opening of an insolvency procedure and/or the approval of an insolvency plan may be filed by a foreign insolvency administrator or by a creditor to the Croatian court. The court will recognise the decision if it was reached by a foreign body that has international jurisdiction under Croatian law, if the decision is enforceable under foreign law, and if the recognition is not against the rules of Croatian public policy.

As to providing assistance to foreign insolvency and restructuring proceedings, communication and cooperation duty between the courts and insolvency practitioners within the EU is set forth in Articles 41, 42 and 43 of the EU Recast Regulation. As for assistance to foreign insolvency or restructuring proceedings outside the EU, under the Croatian Civil Procedure Act, Croatian courts are obliged to assist foreign courts where stipulated by treaties and under condition of reciprocity, unless the assistance required is contrary to the rules of Croatian public policy. Furthermore, under the Insolvency Act, when secondary insolvency proceedings are opened in Croatia, the insolvency administrator appointed in such proceedings is obliged to cooperate with the foreign insolvency administrator appointed in the main insolvency proceedings.

Should a foreign cross-border business with a COMI in a foreign country and assets in Croatia contemplate a restructuring, the first consideration to is whether the chosen restructuring model will be eligible for recognition in Croatia.

A key potential issue concerns the type of statutory proceedings within which the restructuring is conducted. The Insolvency Act only enables the recognition of insolvency matters in the narrowest sense and some foreign restructuring options fall outside this interpretation. Therefore, the only statutory restructuring that might get recognition in Croatia is the insolvency plan adopted after the formal opening of an insolvency proceeding and its approval by the competent court. On the other hand, if "cross-border" related to other EU member states, the Regulation (EU) 2015/848 (the EU Recast Regulation) might put the debtor in a more favourable position, provided that the chosen restructuring instrument is listed in Annex A.

Also, if under applicable law the cross-border restructuring only covers the assets situated in the country in which the business has its COMI, secondary insolvency proceedings can be opened in Croatia regarding assets situated in Croatia and Croatian law would apply to such proceedings.

Covid-19

On April 30 2020, the Croatian Parliament adopted the Emergency Measures in Enforcement and Insolvency Proceedings Act (Emergency Measures Act). The Act entered into force on May 1 2020 and only applies for the duration of special circumstances that exist as a result of the Covid-19 pandemic, defined as:

> *… an event or a certain condition which could not have been predicted and could not be affected, which threatens the life and health of citizens, property of greater value, significantly damages the environment, disrupts economic activity or causes significant economic damage.*

The intention was to only regulate actions taken during the special circumstances and exclusively caused by Covid-19. However, it is questionable whether the measures might also apply to other future special circumstances caused by a different event.

The application of the Emergency Measures Act expired three months after its implementation, on July 31 2020. At this point, the government exercised an option to extend the application period by a further three months, to October 18 2020.

Regarding insolvency proceedings, according to the Article 6 of the Emergency Measures Act, insolvency events arising during the special circumstances are not a prerequisite for filing petition for insolvency proceedings. Exceptionally, a petition for insolvency may be filed either by the debtor itself unconditionally or by the Financial Agency and the creditors when it is necessary to protect national interests and/or security, environment, or public health.

The other notable measure within the Act that will have an indirect effect on insolvency proceedings is the introduction of a standstill: the suspension of execution of all enforcement against all debtors (legal or natural persons) for a period of three months. Since frozen accounts for an uninterrupted 120-day period due to the unsuccessful execution of enforcement proceedings is a cause for an insolvency application, the standstill may enable debtors to carry out a restructuring within the given period to save the business.

The Hanfa, the financial sector regulator, approved the establishment of the Stability Fund, which is a publicly traded open-end investment fund (UCITS). The Fund has a fixed term of three years and is intended for institutional investors who can bear moderate investment risk and are willing to invest at least HRK1 million kuna ($157,000) over a three-year period. The Hanfa also banned dividend payments by insurance companies and some pension funds until April 30 2021 to protect their liquidity in the context of Covid-19, as well as a recent earthquake that affected Zagreb.

The most notable measure by the HNB has been to reduce minimum reserve requirement for credit institutions from 12% to 9%, with the aim of releasing additional liquidity that should support the banking system against the Covid-19 crisis. Changes were also made in monetary policy, with a decision to purchase the government bonds and enable pension funds, investment funds and insurance companies to trade them to maintain stability in the government securities market. The CNB has also obliged all credit institutions to retain 2019 net profits.

Looking ahead

One of the most welcome changes for the Croatian market would be an earlier petition filing. This would boost the chances of a successful restructuring or at least enhance the creditors' claims satisfaction rate.

Unlike earlier legislation regulating pre-insolvency proceedings, which was seen as owner-friendly, current legislation is very strict. The market has shown a significant decrease in the number of entrepreneurs opting for such a restructuring tool due to the formality of the proceedings, which are exclusively court-governed, have no creditor participation and set a high threshold for adopting a restructuring plan. All of this, absurdly, makes pre-insolvency proceedings less flexible than an insolvency plan. On the other hand, choosing an informal out-of-court restructuring by negotiating with major creditors in any large restructuring may lead to assets being frozen, due to the complexity of negotiating processes.

An over-optimistic and pro-owner approach only served to shut down Croatia's restructuring industry. Its inefficient nature was even indirectly acknowledged by the state, which adopted the Extraordinary Administration Act to avoid the risk of having Agrokor fail to navigate through the existing statutory restructuring models.

Once the suspension of restructuring and insolvency proceedings imposed by the Emergency Measures Act is lifted, a significant increase in the restructuring mandates is expected.

If the legal framework remains unchanged, there is a high probability that most of restructurings will be done out of court, in a less complicated informal manner through direct negotiations between debtors and creditors. We assume that at some point amendments will be made to the Insolvency Act that will lower the thresholds required for the adoption of a restructuring plan or at least equalize them with the thresholds prescribed for the adoption of an insolvency plan.

Further considerations on handling the restructuring of a group of companies will remain. The EAP's high threshold for distressed companies of systematic significance means the EAP is out of reach for many smaller groups of companies that might perhaps have benefitted from its solutions if they were to find themselves in financial trouble.

Denmark

Kristian Gustav Andersson and Anne Hansen-Nord, Lundgrens Law Firm

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The Danish Insolvency Act contains procedural as well as substantive provisions in relation to formal insolvency proceedings.

The formal reconstruction process is often criticised for being both expensive and troublesome. However, the changes proposed by the Danish Bankruptcy Council to the rules on restructuring may, if passed, alleviate these issues. Among other things, the proposals suggest that the requirement for compulsory security in any subsequent bankruptcy proceeding is removed and that employees' guarantee fund coverage must take effect at the very beginning of the reconstruction proceedings.

The Danish Bankruptcy Act distinguishes between bankruptcy, formal reconstruction, and rescheduling of debt. Bankruptcy and formal restructuring proceedings are available for legal entities as well as individuals, while debt rescheduling on its own is only obtainable by individuals. Insolvency proceedings under the Danish Bankruptcy Act can be launched only once a company is insolvent. A company is insolvent when it cannot fulfil its obligations as they fall due, and when this inability to pay is not temporary.

Instead of initiating a formal restructuring process, an insolvent company may seek to enter into an arrangement with its creditors, and in this way obtain a percentage reduction of the debt, a lapse of the claims, a postponement of the payments or a combination of all of these, via an informal restructuring process. It is important that certain creditors are not given preferential treatment at the expense of other creditors, as this may result in legal liability for the management.

Directors' duties

The management of a distressed company is not automatically liable if insolvency proceedings are initiated against the company. The management is only liable, if it has failed to comply with its managerial duties or if the

Kristian Gustav Andersson
Partner, Lundgrens Law Firm
Copenhagen, Denmark
T: +45 2524 5117
E: kra@lundgrens.dk
W: www.lundgrens.dk/en/kristian-gustav-andersson

Kristian Gustav Andersson is head of the reconstruction and insolvency department at Lundgrens. He specialises in advising on insolvency and restructuring matters, including company pledges and other securities. Kristian is a trusted advisor to leading Danish banks, as well as many Danish and international corporate clients. Kristian also acts as trustee, as appointed by major Danish banks in several restructuring and insolvency matters. Kristian has a broad range of experience in M&A and negotiation, where he advises on all types of major transactions.

Anne Hansen-Nord
Director, Lundgrens Law Firm
Copenhagen, Denmark
T: +45 3010 3909
E: ahn@lundgrens.dk
W: www.lundgrens.dk/en/anne-hansen-nord

Anne Hansen-Nord recently joined the reconstruction and insolvency department. With more than 10 years' experience advising on M&A transactions, capital markets and corporate law, Anne is a highly valued advisor on out-of-court restructurings and distressed M&A transactions.

management have violated legal regulations.

The management is obligated to ensure that the company's capital reserves are sufficient to fulfil its present and future obligations as they fall due. If the capital reserves are not sufficient, the management must restore the reserves or file for insolvency proceedings.

However, it is important to note that management often is tasked with complex decisions. Consequently, Danish Law operates with the so-called "business judgment rule". This legal principal is a presumption of innocence if management has acted in good faith and with care, and the management reasonably believed the actions taken were in the best interest of the company.

Formal filing

The formal filing and issue of a bankruptcy or restructuring order has several impacts on the creditors. The creditors are subject to limitations concerning proceedings taken by creditors individually, as the creditors cannot seek satisfaction in the debtor's assets. Therefore, execution or attachment may not be levied against property comprised by the estate.

The trustee can decide to maintain contracts that have not yet been fulfilled, unless this is contrary to the very nature of the contract. In restructuring proceedings, the trustee can additionally decide to maintain a contract that has been terminated within the last four weeks leading up to the initiation of the restructuring, provided that the contractual party has not yet acted upon the termination. If a contract is maintained, all claims arising out if it will be elevated in the estate's priority of claims. If the contract is not maintained, the contractual party may terminate the contract and file its claim.

Priority, dissenters and asset sales

The order of the priority of claims is in general as follows:

- Costs of the estate administration (pre-preferential claims)
- Claims in relation to previous restructuring or liquidation processes (preferential claims)
- Claims from the debtor's employees (preferential claims)
- Certain tax claims (preferential claims)
- Any remaining claims, including invoice claims (ordinary claims)
- Claims of interest, fines, gifts etc. (deferred claims)

Creditors with valid and enforceable security do not form part of the ranking. However, if the security does not fully cover a creditor's claim, they are viewed as an unsecured creditor in relation to the unsecured part of their claim. Post-petition debt or costs incurred by the estate will be considered pre-preferential debt, which will be covered at the same level as costs of the estate administration.

During bankruptcy proceedings, the trustee is responsible for handling the sale of assets. The trustee can carry out the sale as a sale of the individual items or as a sale of the business or of separate branches. The trustee must manage the interests of the estate to the widest extent possible, must manage the sale in such a way that the outcome for the bankruptcy estate and its creditors becomes as favourable as possible.

During a formal restructuring process, the appointed trustee must consent to the selling of the debtor's assets, if the sale significantly impacts the restructuring. Furthermore, a business transfer must be carried out in accordance with a ratified restructuring proposal. Hence, a sale of the business or of one or more of the branches must be approved by the creditors for the restructuring proposal to be valid.

The final restructuring proposal is adopted unless a majority of the creditors participating in the vote, vote against it. Votes are cast in proportion to the amounts of the claims. The compulsory composition will typically include all creditors. This means that creditors may be forced to accept undesirable terms and be crammed down in accordance with an approved restructuring proposal.

A formal restructuring must contain at least a compulsory composition or business transfer. The compulsory composition may take the form of a lapse of the claims or a percentage reduction of these, it may also entail a postponement of payments.

All sectors and industries are subject to the same insolvency and restructuring regime. However, a restructuring containing a business transfer may be subject to approval from the competition authorities if the transfer triggers the merger rules.

Management should continuously assess its company's financial situation to anticipate the tipping point

Challenging a debtor's transactions

Transactions carried out in the period leading up to an insolvency proceeding may be null and void. Claw-back actions can be initiated by the trustee during bankruptcy proceedings or compulsory composition proceedings that are approved in a formal restructuring. Distinction is made between so-called "subjective" and "objective" clawback action rules. Under the objective rules, some transactions carried out may be challenged, irrespective of knowledge of the debtor's insolvency or fraudulent intent. Transactions such as granting of security in respect of old debt and gifts can be challenged after the objective rules, depending on the circumstances.

Under the general subjective rules, a transaction can be challenged if it fraudulently favours one creditor over another, where the debtor's property is withheld from serving the creditors, or where the debtor's debts are increased to the detriment of other creditors. However, a transaction can only be voided if the debtor had already became insolvent due to the transaction and the favoured party knew or should have known of the insolvency and the circumstances causing the transaction to be fraudulent.

Crossing-borders

Petitions for restructuring or insolvency proceedings can only be filed in Denmark if the debtor is engaged in commercial activity domiciled in Denmark or is otherwise subject to the jurisdiction of Denmark. Proceedings cannot be opened in respect of a foreign debtor that does not meet neither of these two requirements.

Danish legal advice on handling of any Danish assets comprised by foreign proceedings will often be relevant for foreign debtors. Additionally, some foreign insolvency or restructuring proceedings receive recognition in Denmark pursuant to Nordic and EU rules.

Generally, Danish assets held by a foreign debtor would be handled alongside any other asset within the debtor's restructuring process. Transfer of certain assets such as shares and real estate must be recorded in accordance with Danish law to have priority over third party transferees acting in good faith. Any creditor rights in Danish assets must be handled in accordance with Danish law, meaning a sale of Danish real property must respect the rights of pledgees and mortgagees as set out in Danish law.

Covid-19

It is important that businesses negatively affected by Covid-19 have a clear overview of their financial situation, including outstanding debts, the most critical contracts and general liquidity needs. This will help a business to address the situation in an effective manner.

A knowledge of relevant government aid packages and a general proactiveness in respect of debtors is likely to increase a company's chances of reaching an instalment agreement with creditors, if necessary.

Furthermore, management should continuously assess its company's financial situation to anticipate the tipping point. This is important, as management may be held liable to pay damages to creditors if they should have realised that there was no reasonable prospect that the company would be able to survive – management must commence insolvency proceedings once it establishes that the point of no return has been reached. Continuous assessment can also help management assess what urgent steps or more long-term changes need to be made. It is also generally beneficial for a company to be transparent with its key stakeholders and creditors.

Beyond the short-term consequences of the Covid-19 crisis, creditors and other stakeholders are now looking into its long-term consequences. The crisis has also meant an increased focus on force majeure clauses as many deliveries have proven difficult.

Various aid packages for businesses have been introduced by the Danish government to help mitigate the negative economic effects of Covid-19. A number of these focus on helping businesses maintain liquidity by postponing the payment of taxes and VAT and by providing government guarantee schemes. The state guarantee covers 70% of bank loans and operating credit, making it easier for businesses to obtain bank loans. While these aid packages focus on maintaining liquidity, others provide compensation for various economic losses that businesses have suffered due to Covid-19.

The two main compensation aid packages cover employee salaries and fixed expenses. If granted, businesses receive between 75% – 90% (with a cap) in salary compensation, for each fulltime salaried employee sent home without work but receiving full salary. The compensation period ended in August 2020 but with the option of being extended to October 30 2020, if businesses are subject to government-enforced closure.

The fixed expenses aid package allows businesses that have experienced a revenue loss of at least 35% to apply for a subsidy to cover certain fixed expenses for a period of up to four months. The subsidy amount is based on actual revenue loss, allowing businesses to receive between 25% – 100% (with a cap) of losses in compensation.

Furthermore, special aid packages applicable to organisers of larger cancelled events, the self-employed and smaller businesses with no more than 25 full-time employees have been introduced to help to cover lost revenue.

Any estates that entered into bankruptcy after March 9 2020 have also benefitted from the abovementioned aid packages. Whether this was the intention of the legislator is uncertain.

Finally, on July 3 2020 the Danish Bankruptcy Council proposed a series of changes to the rules on restructuring, some directly due to Covid-19. The Bankruptcy

The Danish Bankruptcy Council has also recognised that the formal restructuring scheme needs to be revised

Council recommends that the proposed changes are implementation quickly. However, it is still unknown if and when the suggestions will become an actual legislative proposal.

Looking ahead

Many businesses find that the formal restructuring scheme – similar to a US chapter 11 bankruptcy – is too formal in the sense that the procedures hinder in particular a transfer of the business. Also, the procedural scheme makes it an expensive process. A business with its main assets pledged to a bank or another creditor, will have to turn to a third party financing to finance its operations during the reconstruction process. These issues could to some extent be alleviated by the changes to the restructuring scheme recently recommended by the Danish Bankruptcy Council. The Danish Bankruptcy Council has also recognised that the formal restructuring scheme needs to be revised to provide a more workable way for businesses to preserve value.

As a result of Covid-19, in addition to short- and long-term liquidity, creditors are now also looking into a debtors' adaptability and ability to cut expenses on short notice while still maintaining a running business. Expectedly, there will be an increase in the number of distressed M&A transactions in the wake of Covid-19.

CORPORATE INSOLVENCY & RESTRUCTURING REPORT 2020: COVID-19 SPECIAL FOCUS

Hong Kong SAR

James Warboys and Suzi Duncan, Linklaters

Hong Kong SAR does not have a statutory corporate rescue regime. Many restructurings take the form of workouts, implemented by consent or by way of a Hong Kong SAR law scheme of arrangement.

The court appointment of a provisional liquidator, which displaces the company's directors and includes a statutory stay on proceedings, may be used to facilitate a corporate rescue. However, this is a somewhat limited rescue device as a provisional liquidator can only be appointed where the company's assets are in jeopardy. It is often coupled with a scheme of arrangement, which contains no moratorium preventing creditor action.

There are no statutory provisions for the court to provide assistance on cross-border insolvencies and Hong Kong is not party to the UNCITRAL Model Law on Cross-Border Insolvency. The court has the power to recognise and grant assistance to foreign insolvency proceedings under the common law principle of modified universalism and generally takes pragmatic approach in this regard.

The Financial Services and Treasury Bureau has been preparing an amendment bill to introduce a new statutory corporate rescue procedure. It is expected to include provision for a "provisional supervision" regime and an "insolvent trading" law, similar to the wrongful trading regimes of other common law jurisdictions. This has been under consideration for a long period of time and it is currently unclear when the new law will be implemented.

Basic framework

There is only one formal collective insolvency procedure under the Companies Ordinance: liquidation.

Liquidation may be compulsory or voluntary. Voluntary liquidations can be either a members' voluntary liquidation (MVL) or a creditors' voluntary liquidation (CVL). In any form of liquidation, a court supervised liquidator is

James Warboys
Partner, Linklaters
Hong Kong
T: +852 2901 5260
E: james.warboys@linklaters.com
W: www.linklaters.com/en/find-a-lawyer/james-warboys

James is restructuring & insolvency (R&I) and special situations partner at Linklaters. He represents companies, financial stakeholders, advisory firms and insolvency practitioners on transactions across the full spectrum of R&I in multiple jurisdictions and sectors, including distressed M&A, debt-for-equity swaps, liability management exercises, bond restructuring, alternative credit and other new money financings and distressed debt investments.

Suzi Duncan
Managing associate, Linklaters
Hong Kong
T: +852 2901 5167
E: suzi.duncan@linklaters.com
W: www.linklaters.com/en/find-a-lawyer/suzanna-duncan

Suzi is a managing associate in Linklaters' Hong Kong office advising a range of creditors, companies, other stakeholders and insolvency practitioners on all aspects of restructuring and insolvency transactions across multiple jurisdictions and sectors. She has advised on complex restructurings in Europe (from both London and Paris) and Asia (from Hong Kong) and also has experience with distressed debt trading and special situations in the European market.

appointed and the directors lose control.

A compulsory liquidation is commenced by filing a winding-up petition at court and is usually presented on the grounds of insolvency.

MVLs and (subject to one limited exception) CVLs are commenced by shareholder resolution. MVLs are a solvent liquidation process – all creditors are to be paid in full and any surplus distributed to shareholders. CVLs are (generally) insolvent liquidations.

A scheme of arrangement may also be used to achieve a corporate rescue. In the absence of a scheme, any restructuring will need to be implemented consensually, using the contractual powers under finance documentation to implement the solution or otherwise.

Receivership is a secured creditor's enforcement remedy and is not a collective insolvency procedure.

Generally, a group of companies does not receive special treatment. Hong Kong SAR does not have legislation under which a pooling order may be made – companies need to implement restructuring and insolvency procedures on an entity-by-entity basis.

Directors' duties

Generally, the duties of directors to act in the best interests of shareholders transition to a duty to act in the best interests of creditors as a whole when a company is insolvent or in the "zone of insolvency".

The court has power to declare that any persons who were knowingly parties to carrying on the company's business with an intent to defraud creditors are personally responsible for all or any part of the company's debts. Such liability only arises where the company has entered liquidation. Successful actions in this regard are rare, owing to the need to establish actual dishonesty or fraud.

There are currently no wrongful or insolvent trading provisions similar to those in other common law jurisdictions.

Where a company enters into an insolvent liquidation within one year from the date on which payment out of capital was made to a shareholder or a former shareholder in connection with a redemption or buy-back of the company's shares, any director who made the required solvency statement will be jointly and severally liable with the recipient of the funds to contribute assets to the company up to an amount not exceeding the relevant payment out of capital.

Transactions at an undervalue and unfair preferences can be set aside in insolvent liquidation (see below).

There have been no amendments to the law in this regard as a result of the Covid-19 pandemic.

Formal filing

No automatic procedural stay applies: (i) in the period between the presentation of a winding-up petition and the court making a winding-up order (except where a provisional liquidator has been appointed) or (ii) in a voluntary winding up.

When a court makes a winding-up order or a provisional liquidator is appointed over the company, no action or proceeding may be commenced or continued against the company, except by leave of the court. Leave will generally be refused if the issues in the action or proceeding can be dealt with more conveniently and with less expense and delay in the winding up proceedings.

However, this does not prevent a secured creditor enforcing its security through any out of court process, such as the appointment of a receiver. Where a secured creditor's security enforcement involves an action or proceeding, the court's leave must be sought and will usually be given.

The stay in Hong Kong SAR does not prevent counterparties from terminating contracts with the company.

Priority, dissenters and asset sales

Secured creditors' claims, in respect of the proceeds of realisation of assets secured in their favour, rank ahead of all other claims save for: costs of preserving and realising such assets; and preferential claims, when the proceeds of realisation of assets are subject to floating security (if the free assets are insufficient to pay those preferential claims). Preferential claims primarily comprise certain amounts owed to employees and domestic tax liabilities.

For proceeds of realisation of unsecured assets, the payment order in a liquidation or receivership is broadly as follows:

- the receiver or liquidator's costs and expenses;
- preferential claims; and
- unsecured claims (which rank pari passu).

For post-petition credit, a liquidator can raise money on the security of the company's assets without court approval and without sanction from the creditors' committee. A provisional liquidator can raise funds on the security of the company's assets if granted this power by the court. Such funds rank as an expense of the liquidation with super-priority (i.e. payable in priority to the liquidator's remuneration). There is no legislation permitting security granted in respect of such new money to have priority over existing security; any such priority would require the agreement of the relevant secured creditors.

A scheme of arrangement can bind dissenting or non-voting unsecured and secured creditors. While creditors within a class may be crammed down in a scheme, it is not possible to cram down any other class, since each class must vote in favour of the scheme for the court to sanction it and for it to take effect against that class.

A scheme of arrangement can, in theory, impose a solution on both creditors and shareholders without their consent, subject to the requisite numbers of each class voting in favour of the scheme.

There is no specific legislation expressly permitting pre-packaged sales, though we note that (i) pre-packaged sales by receivers are possible (though somewhat uncommon) and (ii) pre-packaged sales by provisional liquidators have been allowed in exceptional circumstances.

There is no legislation which expressly permits credit-bidding or stalking-horse bids, but they are generally permissible.

A liquidator may sell the whole or any part of the business or assets of the company without court approval and without sanction from the creditors' committee. However, a provisional liquidator must apply to the court for permission to sell the company's assets, if such power is not included in the appointing order.

A receiver appointed by the holder of the security will derive his powers from that security agreement, which typically include the power to sell the secured asset without court approval.

There is no legislation which permits liquidators, provisional liquidators or receivers to sell the company's assets free and clear of existing claims.

In December 2019, the court extended recognition and assistance to an insolvency administrator from Mainland China for the first time

It is worth noting that there are some sector-specific regimes. The Banking Ordinance and Insurance Ordinance contain special provisions in respect of authorised institutions and insurers respectively which supplement, modify or dis-apply general corporate insolvency laws. The Financial Institutions (Resolution) Ordinance provides a framework for the orderly resolution of financial institutions. The Insurance Authority, the Monetary Authority and the Securities and Futures Commission act as resolution authorities for the financial institutions under their respective purviews.

Employees, government or regulatory bodies (including, for example, the Hong Kong Stock Exchange in the case of listed companies) may have an impact on the outcome of a restructuring depending on the situation and what is proposed.

A transferee may, in certain circumstances, become liable for employment claims of the transferor under the Transfer of Businesses (Protection of Creditors) Ordinance.

Challenging debtor's transactions

The debtor's transaction s can be challenged on insolvency on the following grounds.

- Transaction at an undervalue: a transaction at an undervalue entered into by the debtor within five years of the commencement of its winding up.
- Unfair preference: a payment to a creditor which puts the recipient in a better position than it would otherwise be if the debtor went into insolvent liquidation and the court were satisfied that the debtor was "influenced by a desire" to create that preference. The clawback period is two years before the commencement of the winding up in the case of a person connected with the debtor and six months in all other cases.
- Floating charge: a floating charge created within 12 months of commencement of the debtor's winding up will be invalid, except where the debtor has received valuable consideration in exchange for its creation. The clawback period is two years for floating charges created in favour of a person connected with the debtor and 12 months in all other cases.

The court will not make any order in respect of any such antecedent transaction (other than where a floating charge has been created in favour of a connected person) unless the debtor was (or became, as a result or the relevant transaction) unable to pay its debts.

The court can also set aside (i) extortionate credit transaction (i.e. transactions requiring grossly exorbitant payments to be made in respect of the provision of credit or otherwise grossly contravening ordinary principles of fair dealing); and (ii) fraudulent conveyances (i.e. dispositions of property with the intent to defraud creditors).

Crossing-borders

The court has discretionary jurisdiction to wind up a foreign debtor as an unregistered company if it is unable to pay its debts or if it is just and equitable to do so. As a matter of common law, the court must also be satisfied that: (i) there is a sufficient connection with Hong Kong SAR; (ii) there is a reasonable possibility that the winding up would benefit the applicants; and (iii) the court will be able to exercise jurisdiction over one or more persons in the distribution of assets.

The court has jurisdiction to sanction a scheme concerning a foreign company where there is a "sufficient connection" with Hong Kong SAR. A connection which is insufficient to satisfy the sufficient connection test for winding up may be sufficient connection to establish jurisdiction to sanction a scheme. A common connection is that the debt is governed by Hong Kong law.

There is no legislative power for the court to recognise and assist foreign insolvencies or restructurings. However, the court will generally recognise and assist foreign

The introduction of the National Security Law in June 2020 has caused some uncertainty as regards the future of business and finance

insolvency practitioners if: (i) the laws of the foreign insolvency proceedings are substantially similar to Hong Kong insolvency law; and (ii) the order sought is available under both the laws of the jurisdiction of appointment and Hong Kong.

There has long been uncertainty as to which countries' systems might satisfy the "substantially similar" test but in December 2019, the court extended recognition and assistance to an insolvency administrator from Mainland China for the first time.

Covid-19 and beyond

Levels of restructurings and insolvencies in Hong Kong SAR have steadily increased over the last few months following a period of political unrest and intervention from the Mainland government. However, levels of insolvencies remain lower than expected as at summer 2020. This is a result, in part, of government stimulus packages and regulatory and political pressure on financial institutions to grant accommodation / forbearance to defaulting borrowers and issuers. It is expected that a material increase in restructurings and insolvencies will occur towards the end of 2020.

The Hong Kong SAR government has provided various financial measures to help individuals and businesses cope, including government-guaranteed low-interest rate loans to SMEs, an employment support scheme which provides subsidies to enable continued payment of wages and subsidies for specific business sectors. Further, in April 2020, the Hong Kong Monetary Authority instructed all banks in Hong Kong to grant six-month loan repayment holidays to SMEs. The majority of measures were initially implemented for a limited period of six months but it is expected that a number will continue as necessary. To date, there has been no change made to insolvency laws similar to those implemented in other common law jurisdictions.

Elsewhere, an amendment bill to introduce a new statutory corporate rescue procedure was expected to be introduced into the Legislative Council in the 2020/21 session. However, the government has been considering proposals for a statutory corporate procedure since 1994 and, given the Covid-19 situation, further delays are expected.

The introduction of the National Security Law in June 2020 has caused some uncertainty as regards the future of business and finance in Hong Kong SAR. Businesses are affected by the measures as well as individuals and growing political pressures and concerns against the backdrop of the ongoing US-China trade war mean that there is potential for an uptick in restructuring and insolvency situations in Hong Kong SAR.

Luxembourg

Armel Waisse, Laurent Henneresse and Christophe Molitor,
Molitor Avocats à la Cour

www.molitorlegal.lu

As with the rest of the world, the Covid-19 pandemic has been affecting the operation of companies registered in Luxembourg in multiple ways. With new challenges lying ahead owing to this unprecedented health and economic crisis, local economic stakeholders have had to revisit their business models and prioritise short-term strategies to ensure the viability of their businesses, particularly by consolidating/improving their cash-flow positions and safeguarding profitable business segments.

In practice, the initiatives taken by businesses are manifold. Where possible, existing contracts with various stakeholders have been renegotiated or terminated. Force majeure and material adverse change clauses (MAC) have been invoked to suspend existing contracts. The internal functioning of several undertakings has also been adapted, with work-from-home policies becoming the new norm where the physical presence of staff at work was not critical. In parallel, online shopping has surged owing to the temporary/partial closure of physical stores. Businesses have also had recourse to the legal tools created by the Luxembourg State to face the crisis, including investment aids and state guarantees.

Basic framework

The most commonly initiated insolvency proceeding in Luxembourg is a bankruptcy proceeding, which aims to realise a debtor's assets and distribute the proceeds to the creditors in accordance with the order of priority as defined by law.

Where the two cumulative conditions for bankruptcy are not met yet – namely, cessation of payment and impairment of creditworthiness – a debtor, which must qualify as a merchant (*commerçant*) or be a commercial company, may apply for one of the three available alternative insolvency proceedings. Depending on the severity of the financial

Armel Waisse
Partner, Molitor Avocats à la Cour
Luxembourg
T: +3522972981
E: armel.waisse@molitorlegal.lu
W: www.molitorlegal.lu/our-team/armel-waisse

Armel Waisse is a partner at Molitor specialising in dispute resolution and banking & finance. She has recognised expertise in corporate and financial law disputes including insolvency matters. Armel is ranked in legal directories for her litigation skills and strategical approach to procedural matters. Armel is also a lecturer at the University of Luxembourg and Luxembourg Bar School. She speaks English and French.

Laurent Henneresse
Counsel, Molitor Avocats à la Cour
Luxembourg
T: +3522972981
E: laurent.henneresse@molitorlegal.lu
W: www.molitorlegal.lu/our-team/laurent-henneresse

Laurent Henneresse is a counsel at Molitor and has expertise in banking, finance and restructuring. He is a dual qualified lawyer in Luxembourg and England & Wales (non-practising solicitor) and has over 10 years of experience in Luxembourg. Laurent specialises in financing, investment management and restructuring and insolvency. He speaks English, French, Dutch and Italian.

Christophe Molitor
Junior associate, Molitor Avocats à la Cour
Luxembourg
T: +3522972981
E: christophe.molitor@molitorlegal.lu
W: www.molitorlegal.lu

Christophe Molitor has a master's degree in corporate law from the University Panthéon-Assas (Paris II) and the University of Humboldt in Berlin. He is currently undertaking an internship as a junior associate at Molitor, working primarily in banking and finance.

difficulties, these are: the suspension of payments (*sursis de paiement*); controlled management (*gestion contrôlée*); or scheme of composition with creditors (*concordat préventif de faillite*).

In practice, the benefits of alternative insolvency proceedings are rarely granted by courts as the applicable legal conditions are seldom fulfilled. This generally leaves judges with little option but to conclude that the applying company is bankrupt. Initiatives such as the bill of law No. 6539 on the preservation of companies and the modernisation of bankruptcy law (Insolvency Bill) and Directive (EU) 2019/1023 of June 20 2019 are expected to endow Luxembourg with more flexible and effective reorganisation tools. Until these impending reforms are enacted, a more consensual approach, based on dialogue between a debtor and its creditors, should be sought to implement contractual debt restructurings where there are reasonable prospects of salvaging a distressed undertaking; however, if both the conditions of bankruptcy are met, a debtor is obliged to file for bankruptcy.

This market dynamic means that the majority of published insolvency judgments in Luxembourg relate to bankruptcies. Since the Luxembourg private law system derives from both French and Belgian law, Luxembourg judges tend to refer to case law in these countries. International contractual restructurings also give rise to very few court cases in Luxembourg, moreover with legal issues at stake often relating to the enforcement of security interests governed by the law of August 5 2005 on financial collateral arrangements, as amended (the 2005 Law).

Bankruptcy proceedings are governed by Articles 437 ff. of the Luxembourg Commercial Code.

The Luxembourg court must declare a debtor bankrupt if it is a merchant (*commerçant*) or a commercial company and the two following cumulative conditions are met: the debtor has ceased to make payments and its creditworthiness is impaired.

The court then proceeds with the appointment of one or several trustees in bankruptcy (*curateurs*) whose office is carried out under the review of a designated supervising judge. The trustee in bankruptcy must represent the interests of the insolvent estate as well as those of the creditors. Its mission is defined by law and consists, among other things, in: (i) initiating claw-back actions and actions for avoidance; (ii) realising the assets of the debtor; (iii) verifying the existence and extent of the claims against the insolvent estate; and (iv) proceeding with the distribution of the assets of the bankrupt according to the priority rules defined by law.

Bankruptcy proceedings commence either once a debtor files for bankruptcy – a debtor must do so within one month after the date of cessation of payments; after the presentation of a petition for bankruptcy by one or several creditors; or *ex officio* by the court, upon request from the Luxembourg State Prosecutor office. The company's management is deprived of managing the debtor's assets once bankruptcy proceedings have commenced.

When a debtor's situation is not yet irremediably compromised, it can turn to one of the three alternative insolvency proceedings, depending on the severity of his financial situation. However, as mentioned above, while these legal procedures exist on paper, they are rarely used in practice owing to the relatively stringent thresholds imposed by the conditions to which they are subject. Further, the failure of any of the three alternative insolvency proceedings will almost invariably lead to bankruptcy.

> *The benefits of alternative insolvency proceedings are rarely granted by courts as the applicable legal conditions are seldom fulfilled*

Alternative options

Luxembourg offers three alternative insolvency proceedings.

The first is the suspension of payments (*sursis de paiement*), whereby the court orders suspension of payments of a distressed debtor for a limited period. The benefit of such a measure is reserved to a debtor that is forced to temporarily cease payments due to an unforeseen event and which presents sound evidence of its financial capacity to meet its liabilities in future. This procedure, which does not apply to certain debts and preferential claims, requires the approval of a majority in number of creditors that together represent 75% of outstanding unsecured debts.

The second is controlled management (*gestion contrôlée*), which aims at either reorganising the business of the debtor or realising its assets under the supervision of the court and of court-appointed commissioners. This procedure is available to debtors that (i) act in good faith and (ii) have lost their creditworthiness or are experiencing difficulties in fulfilling their payment obligations but do not meet the cumulative conditions for bankruptcy. If the debtor passes the preliminary steps of the procedure, court-appointed commissioners are entrusted with the preparation of a reorganisation plan or, as the case may be, an asset distribution plan. The plan is in turn submitted to the creditors. If a majority in number of all creditors representing more than 50% of the debtor's liabilities so consent, the plan will be presented to the court for final approval.

The third is a scheme of composition with creditors (*concordat préventif de faillite*), which aims at finding an agreement between a debtor and its creditors in a last-ditch attempt to avoid a declaration of bankruptcy. Unlike the two other proceedings, a scheme of composition is only available to the debtor that already meets the two cumulative conditions for bankruptcy (is virtually bankrupt). The agreement between the debtor and the creditors must be approved by a majority in number of the creditors representing 75% of the debtor's unsecured liabilities. Thereafter, if the court ratifies it, the arrangement will be binding on all unsecured creditors and those secured creditors who waived their rights of priority to become parties thereto.

There are no group-specific insolvency procedures under domestic law. However, Regulation (EU) 2015/848 of May 20 2015 on insolvency proceedings (Insolvency Regulation) contains a number of rules on the cooperation and communication between insolvency practitioners acting for insolvent entities of the same group.

Directors' duties

Directors of a company facing financial difficulties should be wary of not taking any actions for which they may potentially be held liable (criminally, contractually and/or in tort), should the company be declared bankrupt. Directors should file for bankruptcy within one-month of deadline starting on the date of cessation of payments, as soon as the two cumulative conditions for bankruptcy are met (account being taken of any extension of the deadline owing to Covid-19, as highlighted below). In addition, they should refrain from performing any acts which would be void or voidable further to the exercise by the trustee in bankruptcy of any clawback action or action for avoidance.

Formal filing

Commencement of a bankruptcy entails the immediate suspension of all individual enforcement actions which creditors have initiated against the debtor. A similar suspension applies when the court has approved the opening of the initial phase of the procedure for controlled management (with the appointment of a judge to investigate the debtor's state of affairs) or the conclusion of a scheme of composition with creditors (but in the latter case, only vis-à-vis the unsecured creditors and preferential or secured creditors who have foregone their preferential right or security to cast a vote regarding the approval of the scheme). In the event of a suspension of payments procedure, the court can grant a temporary stay during the investigation phase.

As a matter of principle, any contracts in existence at the date of the bankruptcy, other than staff employment contracts, will remain in force, unless: (i) they are declared null and void by a court further to the exercise of a claw-back action / action for avoidance by the trustee in bankruptcy; or (ii) they contain an automatic termination clause in the event of insolvency of one of the parties. Nevertheless, the trustee in bankruptcy may exercise a cherry-picking right and elect to terminate the contracts that he considers as unprofitable for the bankrupt.

Priority, dissenters and asset sales

The order of priority of creditors in the distribution of a bankrupt entity's assets is defined by law and cannot be varied by the trustee in bankruptcy or by the court.

The claims of secured creditors will be satisfied with the proceeds resulting from the sale of the assets, which were the subject-matter of the security interest. If funds obtained from the sale are insufficient, the unsatisfied part of the claim will rank equally and compete with those of unsecured creditors. In addition, as mentioned above, collateral subject to the 2005 Law remain enforceable according to their terms despite the existence of insolvency proceedings. The same observation can be made in relation to mortgages over the bankrupt's assets.

The order of priority for other creditors is as follows:

- claims incurred as a result of the bankruptcy, which arose after the bankruptcy commences (*créances de la masse*), including judicial expenses, and fees and expenses of the trustee in bankruptcy, debts to the treasury (for example, corporate taxes, income tax, etc.), and salary debts;

Creditors have generally taken a pragmatic approach towards their professional debtors

- preferential claims (for example, certain employee claims, claims secured by a security interest other than financial collateral or a mortgage);
- ordinary unsecured creditors (which can include claims arising from unsubordinated shareholder loans); and
- subordinated claims.

If the funds are insufficient to satisfy all claims in full, they will be distributed *pari passu* (namely, on a pro rata basis). Any funds remaining after satisfaction of all claims, are distributed among the shareholders of the bankrupt company.

Luxembourg bankruptcy rules do not allow creditors to be crammed down, since the entitlement of creditors over the assets of the bankrupt is strictly regulated by law. As far as alternative proceedings are concerned, court-approved reorganisation plans, liquidation plans and arrangements are binding on all creditors that are required to comply with these instruments by effect of law, even if they voted against their implementation.

Luxembourg insolvency law does not provide for an accelerated or otherwise preferential form of asset sale. Pursuant to the Luxembourg Commercial Code, the sale of a bankrupt's assets is performed by the bankruptcy receiver with the prior consent of the delegated judge, or as the case may be, the competent court.

When exercising any claw-back action or action for avoidance which is prescribed by law, the trustee in bankruptcy can request the court to nullify agreements or actions which are void or voidable pursuant to Articles 445 to 448 of the Luxembourg Commercial Code. Accordingly, pursuant to Article 445, specific actions shall be null and void if they took place during the hardening period (i.e. a maximum period of 6 months prior to the date of the bankruptcy judgement) or 10 days preceding such period (such as any disposals of assets without consideration, or any payments of debts which have not fallen due). Moreover, by virtue of Article 448, all acts and payments made at any time by the bankrupt to defraud its creditors may be declared null and void, if the trustee in bankruptcy can establish complicity of a third party (who can be a creditor) as well as the reality of prejudice caused to the (other) creditors.

However, it is worth noting that some contracts, such as those subject to the 2005 Law or the PPG Law are bankruptcy remote.

Some regulated entities in Luxembourg (such as credit institutions and insurance undertakings) are subject to special insolvency and restructuring regimes and are therefore not subject to the ordinary insolvency proceedings existing in Luxembourg. Nevertheless, the applicable laws can authorise the competent court to apply the rule of bankruptcy or as the case may be, only the rules on liquidation of bankruptcy to the winding-up of the regulated entity.

As a matter of principle, governmental or regulatory institutions do not have a say on the manner in which insolvency proceedings are conducted, since oversight of these procedures lies with the judicial courts. However, special powers are vested in Luxembourg regulators in relation to winding-up or reorganisation of certain regulated entities.

Crossing-borders

Luxembourg law does not contain specific provisions regulating cross-border aspects of insolvency cases.

Nevertheless, the Insolvency Regulation, according to which principal insolvency proceedings must be opened in the EU member state where the debtor's centre of main interests (COMI) is situated, allows for secondary insolvency proceedings to be commenced in any other EU member state where the debtor has an establishment. The effects of these secondary proceedings are limited to the territory of that member state and do not have to be liquidation proceedings

The Insolvency Regulation also creates obligations of exchange of information and cooperation between (i) the insolvency practitioners in the main and secondary insolvency proceedings and (ii) the courts having ordered, or having to decide on, the commencement of such proceedings. The Insolvency Regulation also authorises the opening of group coordination proceedings for insolvent entities belonging to the same group, for which a coordinator is appointed.

The advantage of the Insolvency Regulation is that it allows automatic recognition and enforceability of judicial insolvency decisions in the other EU member states. In contrast, while the existence of non-EU insolvency decisions is generally recognised in Luxembourg, any related enforcement actions be taken in Luxembourg (for example, in relation to assets of the foreign bankrupt) are subject to the prior obtaining of the exequatur of the foreign decision.

If the COMI of a foreign debtor is located in Luxembourg, Luxembourg insolvency law should apply. By effect of Insolvency Regulation, main insolvency proceedings may be commenced in Luxembourg.

Covid-19

Creditors have generally taken a pragmatic approach towards their professional debtors. For instance, rather than enforcing claims immediately, the have granted moratoria where the debtor's financial situation was not impaired before the outbreak of Covid-19 and showed prospects of improvement upon resumption of economic activities. Six Luxembourg banks also committed to offer a six-month moratorium on the repayment of loans granted before April 18 2020 to SMEs, the self-employed and liberal professionals, provided they met certain conditions. Some landlords also renounced the payment of some rents in order to help their commercial tenants to get back on track.

In order to support companies and individuals impacted by Covid-19, the Luxembourg State adopted a "stabilisation package", composed of various laws and regulations, which, among other things, provided for state aid, such as repayable state aid and investment aid and created a state-guarantee scheme for eligible loans granted by participating Luxembourg banks. Another important measure concerning Luxembourg insolvency laws was the suspension of the mandatory one-month deadline, imposed on merchants and directors of commercial companies to file for bankruptcy, until December 24 2020. Further, deadlines for payment of certain taxes and the filing of tax returns have been extended.

Finally, a short-term Covid-19 working scheme (*chômage partiel*) for staff has been implemented and is available until December 31 2020. The scheme allows undertakings to take employees concerned off the payroll.

As a general note, businesses should be performing a review of their existing contracts to ensure that any force majeure clause expressly encompasses epidemics such as Covid-19. In addition, MAC clauses should now be more systematically inserted in contracts and cover sanitary crises in order to allow parties to vary or terminate their contractual obligations if the Covid-19 crisis persists.

To date, there have been no permanent legislative changes concerning insolvency and restructuring which are directly linked to the Covid-19 crisis. However, the pandemic has hastened the passing of some laws which facilitate the granting of credit in Luxembourg. These include the law of July 10 2020 on professional payment guarantees (PPG Law), which creates a new type of personal guarantee. A key feature of this guarantee is that it remains valid despite the existence of domestic or foreign insolvency proceedings or reorganisation proceedings over the guaranteed debtor.

Luxembourg has yet to transpose Directive (EU) 2019/1023, which aims to improve the effectiveness of different national regulations on preventive restructuring, insolvency and debt remission. Another pending reform is the Insolvency Bill, which is inspired by Belgian business insolvency legislation and prioritises (where practicable) the preservation/reorganisation of a debtor's business, rather than its winding-up.

The traditional legal environment for insolvency is expected to remain rather static

Looking ahead

The challenges caused by the Covid-19 pandemic may become an opportunity in Luxembourg to accelerate the modernisation of insolvency law. This area of law has generally been seen as rather lagging behind, when compared with Luxembourg business and finance laws, which are generally known for their innovative features and the flexibility they provide to businesses and investors. The introduction of new legal tools would also give formal support to the insolvency practitioners who generally keep on exploring new ways to help companies become solvent again.

Until legislative changes are made to improve the instruments that can be used by directors, the traditional legal environment for insolvency is expected to remain rather static. The temporary measures that have been adopted by the government to counter the negative effect of the Covid-19 crisis should however provide some level of relief to a number of financially pressured businesses in Luxembourg.

Another upward trend that has been observed in court decisions published over the past decades and which may become more popular owing to the crisis may be the shifting of COMI by Luxembourg entities to other jurisdictions whose insolvency systems afford more flexibility to salvage businesses.

The Luxembourg market is also expected to experience a surge in out-of-court debt restructuring deals that more often than not involve the enforcement of financial collateral governed by the 2005 Law. In addition, the use of financial collateral arrangements, coupled with the recent creation of a new type of flexible guarantee under the PPG Law, could also have a positive effect on the granting of credit to businesses, since these efficient tools allow lenders to somehow limit the credit risk to which they are exposed.

CORPORATE INSOLVENCY & RESTRUCTURING REPORT 2020: COVID-19 SPECIAL FOCUS

Portugal

Filipa Cotta, Catarina Carvalho Cunha and Roberto Ornelas Monteiro, VdA

Portugal's insolvency and restructuring practice has shifted significantly over the past decade to meet the Portuguese legislature's strong desire to restructure companies while they are still solvent. A big impetus behind this shift was the severe economic and financial crisis in 2011, which saw several Portuguese companies enter restructuring or insolvency proceedings. While restructuring and insolvency practitioners are still constantly engaged by clients in insolvency-related matters, the core work has turned to assisting clients in restructuring their businesses to stay afloat. The result is that nowadays, companies are much more aware of the mechanisms available to them to avoid insolvency.

Having said this, since no company could have prepared for the complete paralysis over several weeks or months caused by Covid-19, we expect that alongside a significant increase in out-of-court and in-court restructurings, many companies will plunge into insolvency. To date, publicly available numbers suggest an increase in insolvency proceedings, with insolvencies up 8.4% in the first seven months of 2020 and 32.3% in July 2020 alone, compared with the same periods in 2019 respectively.

As a means to avert a wave of insolvencies, in this environment companies are currently not obliged to file for insolvency within the typical deadline from the date they become insolvent and rather, benefit from a stay on this deadline. This measure is expected to last while the exceptional and temporary measures in response to Covid-19 remain in force

In July 2020, the Council of Ministers also approved a draft law to establish an extraordinary procedure (*Processo Extraordinário de Viabilização de Empresa* –PEVE) to enable companies to respond to the pandemic. The PEVE is expected to remain in place until the end of 2021 and aims to provide a simpler and faster restructuring procedure.

Filipa Cotta
Partner, VdA
Lisbon, Portugal
T: +351 213 11 3400
E: fc@vda.pt
W: www.vda.pt

Filipa Cotta is VdA's head of the restructuring & insolvency practice. She has over 20 years' experience and a recognised track record in this area, including in transnational cases in Switzerland, Luxembourg and Brazil, to name a few. She has been involved in some of the most high-profile and recent corporate restructuring and insolvency cases in Portugal.

Catarina Carvalho Cunha
Managing associate, VdA
Lisbon, Portugal
T: +351 213 11 3400
E: acc@vda.pt
W: www.vda.pt

Catarina Carvalho Cunha is a managing associate with the firm's litigation & arbitration and restructuring & insolvency practices. She is actively involved in insolvency and restructuring matters (as well as civil and commercial litigation and arbitration) in a wide range of sectors, notably telecommunications, banking & finance, energy, oil and gas and the automobile one. She regularly advises clients on such matters in Portugal, Angola, Mozambique, Guinea-Bissau, São Tomé and Príncipe, Cape Verde and East Timor.

Roberto Ornelas Monteiro
Trainee, VdA
Lisbon, Portugal
T: +351 213 11 3400
E: rom@vda.pt
W: www.vda.pt

Roberto Ornelas Monteiro is a trainee with the firm's restructuring & insolvency practice where he is actively involved in working and advising clients on insolvency and restructuring related matters. He is also involved in civil and commercial litigation.

In general, all stakeholders are focusing on saving affected companies. Until now, the market has mostly responded with solidarity and we have seen creditors and debtors agreeing on "possible" solutions that are better for both sides. Agreements between debtors and creditors are highly encouraged by the legal steps that the government has been taking since the beginning of the lock down, namely in relation to payment moratoria and credit lines.

Basic framework

The corporate restructuring and insolvency regime in Portugal is framed under the following legal statutes:

- Insolvency and Recovery Code: enacted by Decree-Law no. 53/2004, dated March 18 (as amended over time), on recovery and insolvency judicial proceedings, which encompasses the Special Recovery Proceedings (*Processo Especial de Revitalização* – PER), established by Law no. 16/2012, dated April 20, 2012;
- Extra-Judicial Regime for Corporate Recovery (RERE): enacted by Law no. 8/2018, dated March 2, 2018, providing a specific legal regime for out-of-court recovery agreements;
- Regulation (EU) 2015/848 of the European Parliament and of the Council, dated May 20, 2015, on insolvency proceedings;
- Decree-Law no. 199/2006 of October 25 (as amended over time): governs the liquidation of credit institutions and financing companies with headquarters in Portugal and their subsidiaries incorporated in another State member;
- Decree-Law no. 227/2012 of October 25: (i) foresees principles and rules to be observed by credit institutions when preventing and regularising situations of non-compliance with the credit agreements by the banking customers, and (ii) creates the extra-judicial network to support those customers in the regularisation of those situations;
- Law no. 147/2015 of September 9 (as amended over time): sets out a specific regime applicable to the recovery of insurance and reinsurance companies; and
- Commercial Companies Code: enacted by Decree-Law no. 262/86, dated September 2, 1986.

Recently, we have seen an inclination on the part of Portuguese courts to dismiss restructuring plans that imply significant losses to some classes of creditors in detriment of others, for example plans that seek to repay secured creditors in full while leaving common creditors with 90% haircuts. This, of course, will bear weight on how secured creditors act from now onwards.

Under Portuguese law, there is only one type of insolvency proceeding *(processo de insolvência)*, under which a company can either be: (i) liquidated, in accordance with the statutory/legal regime or through an insolvency plan; or (ii) rescued, pursuant to an insolvency plan. Insolvency is defined as a debtor's inability to pay its debts as they

Acts performed or omitted within the two years leading up to the beginning of the insolvency proceedings may be subject to clawback

fall due. If the debtor is a company, it will also be deemed insolvent when the aggregate value of its liabilities is higher than the value of its assets, as determined on a fair assessment.

Companies that are not yet legally insolvent but face financial distress may either resort to the RERE, which is not a procedure but rather an extrajudicial legal regime or a PER, an urgent judicial procedure aimed at allowing debtors to negotiate a recovery with their creditors.

Groups of companies do not receive special treatment, albeit parties may request that the relevant proceedings be conjoined.

Directors' duties

The debtor's management bodies are under a general duty to file for insolvency within 30 days of the date they acknowledge (or could not ignore) that the company is legally insolvent. For legal entities, there is a presumption that this knowledge exists when an entity has failed to meet certain types of the obligations (tax obligations, rents etc) for three months. As mentioned above, this deadline is currently suspended as a result of the pandemic.

Non-fulfilment of the duty to file for insolvency within the legal deadline may lead the insolvency to be qualified as "culpable". This in turn, may generate civil liability to the relevant debtor's managers and directors and/or specific inhibitions that may be prolonged in time.

Formal filing

The impact on creditors of a formal filing depend on whether the debtor files for recovery or is otherwise adjudicated as insolvent. Should the debtor apply for a PER, then typically, while negotiations ensue, no new proceedings aimed at collecting debt may be launched against the debtor. Pre-existing proceedings of the sort shall be suspended (and terminated as soon as the recovery deal is approved and sanctioned by the court, unless otherwise expressly foreseen in said plan). In a RERE, on the other hand, only proceedings launched against the debtor by the creditors taking part in the procedure will be suspended.

Things differ in an insolvency scenario. To begin with, the insolvency adjudication renders all debtor obligations immediately payable, and creditors are bound to claim their rights within the insolvency proceedings. Regarding contracts which are still ongoing, the rule is that, unless expressly foreseen otherwise, they are suspended with the insolvency adjudication until the receiver takes a stand on them. As to contractual termination rights, under Portuguese law, provisions establishing insolvency as an event of default are, as a rule, deemed null and void.

Priority, dissenters and asset sales

Under Portuguese insolvency law, creditors are grouped into the following categories:

- Secured credits: which are credits secured by *in rem* guarantees (*garantias reais*), including special statutory liens (*privilégios creditórios especiais*). Examples of such guaranteed credits include real estate special statutory liens (such as state credits related with real estate property tax IMI); third-party credits secured by mortgages; income assignments; and pledges and movable assets special statutory liens (such as credits resulting of justice expenses incurred in the interest of the creditors);
- Privileged credits: which are credits secured by general statutory liens (*privilégios creditórios gerais*) over assets integrated in the insolvent estate up to the amount corresponding to the value of the assets granted in guarantee or the general statutory liens. Examples of such privileged credits include labour, tax and social security debts as well as real estate general statutory liens;
- Common credits: which are all credits not included in any other category; and
- Subordinated credits: which are classified as such by virtue of the underlying credit agreement or pursuant to the law. Examples of subordinated credits include credits held by parties in special relationships with the debtor, such as, in the case of an individual, credits held by his/her relatives; in the case of a legal entity, credits held by the administrators, group of companies and controlling shareholders or shareholders in a group relationship. Subordinated creditors have very limited chances of collection, as a result of the ranking established by law.

In the context of restructurings, creditors can be crammed down.

There is no specific process for facilitating the sale of a distressed debtor's assets or business. From the moment the judgment adjudicating the debtor insolvent becomes final and binding and the creditors' assembly convened to discuss the receiver's report is held, the receiver proceeds with the negotiation and sale of the debtor's assets under the rules provided for in the Insolvency Code. As a rule, the purchasers acquire the assets clear of claims and liabilities.

Upon a debtors insolvency, adjudication acts performed or omitted within the two years leading up to the beginning of the insolvency proceedings may be subject to clawback if they are: (i) found to be detrimental to the insolvency estate (namely, actions that reduce, frustrate, obstruct, jeopardize or delay the payment to the debtor's creditors); and (ii) have been carried out in bad faith. The receiver has six months to challenge these actions from the moment he/she becomes aware of them, but may, as a rule, never do so after a two-year period has elapsed from the declaration of insolvency. Bad faith for these purposes is defined as the knowledge, as of the date of the transaction in question, that the debtor was already insolvent, that insolvency proceedings had already been initiated against the debtor or that the transaction in question would be detrimental to the debtor's creditors and the debtor was in an imminent insolvency situation. There is a refutable presumption of "bad faith" if the transaction is carried out in the two years prior to the commencement of insolvency proceedings and is made with certain related parties, even if no relationship existed between them at the time.

There are certain specific actions or transactions, expressly foreseen in the law, that are automatically (*iuris et de iuri*) considered as hindering the insolvency estate and may be cancelled irrespective of other requirements, subject only to the exceptional legal rules that require the existence of bad faith or other mandatory requirements.

It should be noted that credit institutions, financing companies, insurance and reinsurance companies have specific regimes concerning insolvency and restructuring. Furthermore, under Portuguese law, tax and social security credits cannot be affected / altered by way of a restructuring plan. This is so because there is an overriding principle of unavailability of these credits linked with a concern with the State's financial stability. It follows that a plan that foresees anything different that payment of the existing credit in instalments as allowed for in specific tax law, should be dismissed by the relevant judge.

Crossing-borders

Portuguese courts have jurisdiction over restructuring and insolvency proceedings of companies with headquarters registered in Portugal. This means that as a rule, restructuring and insolvency proceedings of foreign debtors will not be lodged with or handled by Portuguese courts. An exception to this rule is of course the secondary proceedings under Regulation (EU) 2015/848 which may be launched in view of protecting the interests the foreign debtor may have in Portugal.

Key considerations for a foreign debtor would depend on whether the foreign debtor is EU based or not. The effects of restructuring or insolvency proceedings instituted in an EU member state (excluding Denmark) are automatically recognised in all other member states, according to Regulation (EU) 2015/848. Proceedings instituted in other foreign countries will have to be reviewed and recognised in Portugal, through recognition proceedings filed with a Portuguese court. Only after the relevant judgment has been successfully subject to this court's review, will the effects flowing therefrom be binding in Portugal.

Covid-19

Other than the measures outlined in the introduction, regulators have moved to support businesses on several echelons by adopting the following measures:

- Simplified lay-off: allows companies to choose between reducing normal working periods and/or suspending employment contracts. The simplified lay-off has a duration of one month and can be extended monthly, in most cases, up to a maximum of three months. This measure is already being phased out and is only in force until September 30, 2020. After that, companies may still resort to other incentives such as (i) the Extraordinary Incentive to the Normalization of Business Activity (a financial support) or (ii) the Extraordinary Support for the Progressive Restart of Activity (a new simplified lay-off, but restricted to normal working period reductions only), both foreseen in the Economic and Social Stabilization Program (*Programa de Estabilização Económica e Social* – PEES) which was recently approved.
- Moratoriums: prohibits the revocation of credit lines and loans contracted from March 27 2020; extends credits with the payment of principal at the end of the contract (together with all its associated elements, namely, interests); and suspends the payment of principal, rents and interests in relation to credits with partial instalments or other cash amounts payable. These measures were initially adopted until September 30, 2020 but have been extended until March 31, 2021.
- Credit lines: four credit lines were made available under the Covid-19 Economic Support Line targeted at micro, small and medium enterprises (MSMEs). In addition, specific measures to support start-ups were adopted, such as the mezzanine funding, a loan convertible into share capital (shareholder loans); and the launch of Portugal Ventures Call for investments in start-ups, financed by several public entities.
- Leases: (i) suspending the effects of termination, lapses due to the course of time, revocation, opposition of renewal and the six-month period to reinstate the lease property after the end of the lease term, of residential and non-residential lease agreements until September 30, 2020. (ii) Commercial tenants may defer the payments of rents due either (a) during the months the state of emergency was in force, (b) during the months in which they were subject to legal or administrative order demanding closure or suspension of the tenants' activity or (c) in the three months following the end of the legal or administrative order demanding for the closure of the leased premises or the suspension of the tenants' activity. In any case, the moratorium may only be applied to rents due up until December 31, 2020, being those deferred rents paid in the form of 24 monthly instalments from January 1, 2021 to December 31, 2022. (iii) In cases of shop use agreements regarding retail and services stores located in shopping centres, no minimum rental amounts are due until December 31, 2020, being only due to the turnover rent, calculated on the sales made by the shopkeeper, and the service charge.

Other than working on the abovementioned draft law, Portugal is committed to transposing EU Directive 2019/1023 of the European Parliament and Council of June 20, 2019 on restructuring and insolvency by July 17 2021. This transposition, and the need to adopt adequate mechanisms to allow companies to swiftly react to situations of significant financial distress, have become the top priorities for ensuring a sound economy.

The economic crises caused by Covid-19 that we are already facing, and which will likely surge up over the coming months, shall certainly present new and challenging hurdles to companies that are already struggling to keep afloat. We expect a significant increase in insolvency and debt restructuring procedures. At the same time, important adjustments to the legal framework (as above) are being put into place – their main goal is to provide companies with tools to react quickly to situations of significant distress. Given this backdrop, it is crucial that companies and economic groups as a whole, fully understand the legal tools at their disposal and the importance of sound restructuring.

Legal advisers are of course vital in this process, providing high quality legal counselling and adding value within the underlying operations. We believe the legal assistance to clients provided in the context of restructuring and insolvency proceedings can be the key to success and will certainly help identify and implement the appropriate legal tools for a successful rehabilitation.

Looking ahead

"Hibernation" or "winter sleep" might be a complete and effective solution to this crisis, especially for MSMEs. Inspired by the principle of "no income, no expenses", this would mean that companies could disappear during a period and return later, when the market is operating under normal or more favourable conditions.

This measure could be implemented through a global moratorium, covering a stay of individual enforcement actions and a suspension of companies' payment obligations, including tax obligations and other legal duties. Directive 2019/1023 of the European Parliament and Council that Portugal is committed to transpose by July 17 2021 foresees a set of measures (articles 6 and 7 of the Directive) that could help to put such a solution into place.

Another possible development could be an amendment to the existing regime, specifically in relation to payments resulting from the liquidation of an insolvent estate's assets as a means to speeding up the access, by creditors, of the available funds. This is the lengthiest part of the insolvency procedure and naturally, all creditors are severally affected by such delay. The PEES actually anticipates mandatory partial payments when the product of the liquidation is equivalent or exceeds €10,000 and we would expect to see this change implemented in the near future.

Additionally, and in what regards restructuring procedures, namely the PER, for years creditors/investors have been claiming that the security that is legally foreseen in the relevant legislation is not enough to attract investors to take the risk of supporting a company that is under restructuring. It follows that a stronger legal security package should increase the investors desire to invest in such distressed companies.

We expect that the PEVE will be implemented in Portugal shortly. This extraordinary and temporary (it has been devised to be in force only until December 31 2021) company viability procedure has been created to allow companies which are facing financial distress or are on the verge of insolvency as a consequence of Covid-19 to restructure themselves, so long as (i) they are not undergoing a PER at the same time and (ii) they are able to show that they are still viable. This procedure enables the court to approve agreements reached out of court between a company and its creditors is classified as urgent (inclusively assuming priority over other urgent proceedings such as PER and insolvency ones) and has a shorter deadline (namely, there is not a phase for the creditors' claims). Should this be successfully implemented we predict that it will be a procedure many companies will turn to.

It is also expected and desirable that more incentives to invest in distressed companies are developed. In this scenario, there are several possible options that can range from tax incentives/reductions to other governmental support or even by just, as referred above, increasing security given to investors in restructuring procedures.

In what regards clients' needs, the trend is a significant increase for daily advice, especially due to the constant legislative changes. On the other hand, we expect to see many companies file for insolvency, especially in the tourism sector, which has taken a huge blow in the past months. We also expect a wave of filings for a second PER, since the pandemic has strongly affected their capacity of complying with the approved plan.

CORPORATE INSOLVENCY & RESTRUCTURING REPORT 2020: COVID-19 SPECIAL FOCUS

South Korea

Junsang Lee, Joon Oh Jo and Myung-Ahn Kim, Yoon & Yang

Unlike in the US or Europe, Korea has not implemented drastic measures against Covid-19, such as compulsory lockdowns, and whether Covid-19 has significantly dented Korea's economic activity remains unclear. However, the country's manufacturing sector relies heavily on exports and these are declining, rendering any likelihood of an economic rebound in the second half of the fiscal year rather uncertain. Some believe that it may well take two or three years for the global economy to recover. The existing quantum of previous orders, together with government subsidies in the first half of 2020, helped Korean businesses to sustain themselves, but as the economy continues to face downside risks, the long-term future remains murky.

Most corporations are experiencing a liquidity crunch. Generally, corporations start to take rehabilitation into serious consideration when they are, or are likely to be, unable to secure the necessary operating funds due to a decline in sales, recovery in account receivables and/or an increase in costs. Covid-19 has forced management teams to tighten control over costs to reduce expenditures to a degree, but the decrease in sales and the recovery of claims appears to be a larger challenge.

While the emergency disaster relief provided by the government has triggered a temporary increase in sales, the impact is inevitably limited, as well as unclear for corporations. If the Covid-19 pandemic continues into the second half of the year, further eroding sales and recovery prospects, corporations are highly likely to encounter serious problems in securing liquidity and operating funds.

Given the above, the number of applications for rehabilitation and bankruptcy will likely increase in the second half of 2020. Management teams may be well advised to closely analyse their financial condition; for example, is it a temporary financial constraint as opposed to a structural

www.yoonyang.com

Junsang Lee
Managing partner, Yoon & Yang LLC
Seoul, South Korea
T: +82 2 6182 8512
E: junslee@yoonyang.com
W: www.yoonyang.com

Junsang Lee is the managing partner at Yoon & Yang LLC. His main practice areas are international arbitration & litigation and cross-border insolvency & restructuring. From 1994 to 2013, he served as a judge for the lower courts and a presiding judge at the Suwon District Court, during which time he handled bankruptcy and administrative cases. He has been constantly recognised as a leading lawyer by various international publications including Chambers & Partners Asia-Pacific, Who's Who Legal Korea, and Benchmark Litigation Asia-Pacific.

Joon Oh Jo
Partner, Yoon & Yang LLC
Seoul, South Korea
T: +82 2 6003 7080
E: jojo@yoonyang.com
W: www.yoonyang.com

Joon Oh Jo is a partner at Yoon & Yang LLC. His practice focuses on M&A, corporate restructuring and corporate recovery and liquidation. Recently, he has been actively involved in international restructuring/insolvency matters. In particular, during Hanjin Shipping's reorganisation procedure, Joon Oh acted as the legal counsel of a subsidiary of MSC, the world's second-largest shipping group based in Switzerland, and provided legal advice regarding the deal involving the Long Beach Container Terminal in the US. Joon is dual licensed both in Korea and in the State of New York.

Myung-Ahn Kim
Senior foreign attorney, Yoon & Yang LLC
Seoul, South Korea
T: +82 2 6182 8359
E: makim@yoonyang.com
W: www.yoonyang.com

Myung-Ahn Kim is a US qualified senior foreign attorney at Yoon & Yang LLC. Her practice focuses on international litigation/arbitration, restructuring, maritime, aviation and trade. Prior to joining Yoon & Yang, she worked at Holman Fenwick Willan LLP (Singapore Office). Myung-Ahn Kim is ranked as a recognised practitioner by Chambers & Partners Asia-Pacific 2020 and Global 2020. She is a member of the California Bar since 2006.

problem with deeper roots? Management will need to decide whether to continue relying on government subsidies or to restructure via rehabilitation. Merely continuing to exist without implementing a fundamental solution will be counterproductive.

In general, since the restructuring of Hanjin Shipping, there have not been any major insolvency cases in Korea. However, recent trends show an increased in the number of rehabilitation applications for business entities operating golf courses. The number of M&As for rehabilitation companies involving stalking horse bids is also on the rise. Industry experts also expect that the number of the bankruptcy and work-out proceedings will increase and that necessary preparations should be made to manage this.

Basic framework

The Debtor Rehabilitation and Bankruptcy Act (DRBA) prescribes procedures for either rehabilitation proceedings or bankruptcy proceedings. Workout programmes (work-out proceedings) are prescribed under the Corporate Restructuring Promotion Act (CRPA).

Insolvency proceedings under the DRBA (rehabilitation and bankruptcy) are led by the court, while rehabilitation proceedings are creditor-led. While insolvency proceedings are uniform procedures that proceed according to the prescribed law, work-out proceedings are based on private agreements. Additionally, insolvency proceedings encompass all creditor claims, while work-out proceedings cover financial institutions' the creditor claims only.

Of the two proceedings (bankruptcy and rehabilitation) comprising insolvency proceedings, rehabilitation proceedings aim to reduce / exempt the creditors' claims on the debtor under financial constraints so as to rehabilitate the debtor. Bankruptcy proceedings on the other hand aim to liquidate the debtor's assets and distribute them to the creditors before dissolving the debtor. Once rehabilitation proceedings terminate, the debtor company is released from the supervision of the court, receiver or custodian and resumes its ordinary business. Once bankruptcy proceedings terminate, the debtor company ceases to exist.

Corporations generally resort to rehabilitation proceedings. However, in the event a corporation is unlikely to be rehabilitated and the reasons justifying its bankruptcy exist, an application for bankruptcy may be filed. Once an application for rehabilitation is filed, the court renders a preservation order for the purposes of freezing the debtor's assets until the decision on the application is rendered. Under the preservation order, the debtor is prohibited from disposing its assets and/or repaying its existing debts.

Directors' duties

The directors of a corporation are not subject to any increased or decreased level of duty during the pendency of the corporations' financial constraints. The fiduciary duty under the Commercial Act continues to apply.

Where a corporation is undergoing rehabilitation proceedings, the right to manage and to dispose of the assets is transferred exclusively to the receiver or custodian. Under the DRBA, the existing managing director of a corporation undergoing rehabilitation proceedings is appointed as the receiver/custodian, unless any extraordinary circumstances dictate otherwise. A receiver/custodian is subject to certain obligations. As is the case for a director, a receiver/custodian bears his/her fiduciary duty to the corporation including the duty to conduct adequate investigation of the claims reported per the rehabilitation proceedings; and the duty to settle the reported claims in accordance with the rehabilitation plan. A receiver/custodian is required to obtain the court's approval in order to dispose of the corporate assets and/or to obtain loan.

Formal filing

Once an application for rehabilitation proceedings is made, the court may render an order prohibiting all rehabilitation claim creditors and secured rehabilitation claim creditors from compulsory enforcement, provisional attachment and auctions to enforce their security interests. This is referenced as a "comprehensive prohibition order".

By way of reference, an Ipso Facto Clause refers to a contractual provision whereby an application filed for the rehabilitation of a contractual party is deemed as the basis for the contract termination or an event of default. As for the validity of the Ipso Facto Clause, the Supreme Court of Korea has ruled that the clause in principle may not be invalid as the contracting parties' freedom to include such term/condition of the contract should be upheld. However, it has also stipulated that an Ipso Facto Clause may be rendered invalid if it contravenes the general principle of public order and decency (Supreme Court of Korea 2005Da38263, September 6 2007).

Priority, dissenters and asset sales

A public-interest claim is the main example of a claim that prevails over other claims in priority. Under the DRBA, a "public interest claim" refers to a type of claim prescribed under the DRBA and is incurred by the receiver/custodian after commencement of the rehabilitation proceeding – such as a claim for employment wages. Unlike the rehabilitation and secured rehabilitation claims, a public interest claim is paid on a rolling basis and prevails in priority over any rehabilitation claim or secured rehabilitation claim.

Previous orders, together with government subsidies in the first half of 2020, helped Korean businesses to sustain themselves

DIP financing is a type of a post-petition credit whereby a debtor-company, upon applying for the commencement of rehabilitation proceedings may, per the court approval, obtain a loan in order to facilitate the procurement of funds

Cramming-down a credit or class of creditors is also possible. During rehabilitation proceedings, the debtor-corporation prepares and submits its rehabilitation plan for approval at the meeting of the interested parties/creditors. A rehabilitation plan requires a two-thirds vote from rehabilitation claim creditors and three-quarters of the vote from secured rehabilitation claim creditors (based on the quantum of claim amount). Subsequently, if the court approves the plan, it becomes valid and effective. Once the court approves the rehabilitation plan, it becomes applicable to all creditors including those who did not consent, and the provisions of the plan take compulsory effect on the respective rights of the creditors.

In June 2020, the government promulgated its plans to operate the Corporate Asset Disposal Assistance Programme, in order to facilitate corporations undergoing liquidity problems in the midst of Covid-19 to sell/dispose of their assets. The programme applies to large corporations as well as mid-to-small size corporations wishing to facilitate the disposal of their assets. The Korea Asset Management Corporation (KAMCO), which has expertise in corporate asset acquisition and management, assists corporations on asset disposals in lieu of the programme. It is expected that corporations applying for the programme will be able to dispose of their assets based on reasonable terms and conditions.

There is no sector or industry with its own modified insolvency and restructuring regime. Corporate insolvency proceedings are regulated under the DRBA whilst the Work-out Proceedings are regulated by the CRBA. Rehabilitation and bankruptcy proceedings are regulated and monitored strictly under the court provision. As the courts take charge of these proceedings, other stakeholders such as the governmental or regulatory institutions do not have a material impact on the outcome. Work-out proceedings are handled and monitored by the relevant financial institutions. Given that financial institutions are regulated by the authorities in the financial sector (namely, the Financial Services Commission – FSC), the opinion of such authorities may be reflected substantially during work-out proceedings.

Challenging a debtors' transactions

The DRBA provides for the "avoidance powers" whereby the debtor may recover its assets that had unjustly been disposed of before the commencement of the rehabilitation proceedings, so as to ensure the effective rehabilitation of the debtor. Based on the avoidance powers, the receiver/custodian (upon the commencement of the rehabilitation proceedings) may reject the effect and validity of the debtor's previous actions taken before the rehabilitation including (i) the actions taken with the knowledge that they would adversely affect the rehabilitation claim creditors, etc and/or (ii) the actions harmful to the equity among rehabilitation claim creditors such as repayment and provision of security interests. The avoidance powers are exercised by the receiver/custodian.

The avoidance powers are applied in bankruptcy proceedings in a substantially same manner.

Crossing borders

Cross-Border Insolvency refers to an insolvency case entailing a cross-border effect over the relations among the debtors

Corporations have delayed filing for rehabilitation in fear of the stigma surrounding the proceedings, only worsening their chances of rehabilitation

and creditors. Based on the UNCITRAL Model Law on Cross-border Insolvency adopted in May 1997, the DRBA (Chapter 5) contains 15 provisions pertaining to cross-border insolvency. In light of this legal framework, the main points for consideration in case a foreign cross-border entity plans to enter into a work-out proceeding or insolvency proceeding in Korea.

A foreign entity or individual has the equal status as that of a Korean entity or individual (Article 2 of the DRBA). The principle of reciprocity is not applied under the DRBA as it incorporates the principle of equality among domestic and foreign nationals.

Whether a cross-border insolvency proceeding may commence in Korea is determined based on the confirmation of Korean jurisdiction over the applicable rehabilitation or bankruptcy case. Where a debtor's main place of business or office is located in Korean, the Korean court has the jurisdiction over the cross-border insolvency. Even in cases where the main place of business or office is situated abroad, the Korean court may still exercise its jurisdiction if the debtor's assets (in case of creditor claims, the reference is made to the place where the legal claims may be filed) are located in Korea – as per Article 3(1) of the DRBA. In sum, the jurisdiction of the Korean courts is upheld in cross-border insolvency cases if (i) a foreign debtor's main place or business or office or (ii) its assets are located in Korea.

The DRBA recognises the validity and effect in Korea of a cross-border insolvency proceeding abroad. The legislation also prescribes the specific procedures, methods and effect of cross-border insolvency proceedings. It also entails a two-fold system whereby the approval process and the support process for a cross-border insolvency proceeding is stipulated.

For a cross-border insolvency proceeding in a foreign jurisdiction to be recognised by the Korean courts, it must obtain the recognition approval in the first place. Once obtained, the recognition approval has the effect of confirming that the foreign cross-border insolvency proceeding is eligible for the "support process" decision of the Korean courts, provided the approval in itself does not bring about a specific legal effect. The court is required to render its decision on the application for the approval of the cross-border insolvency proceeding in a foreign jurisdiction – within one month after the application.

A "support process" in the context of cross-border insolvency proceedings entails: (i) prohibiting compulsory enforcement or preservation of the debtor's assets and businesses situated in Korea; (ii) prohibiting debtor's settlement or repayment; and (iii) appointing a cross-border receiver/custodian in support of the relevant cross-border insolvency proceedings.

Covid-19

There has not been any substantial change in Korean restructuring and insolvency legislation except for a few minor developments.

The Korean Development Bank Act was amended on May 1 2020 to establish the Period Industry Stabilization Fund, which aims to foster employment stability, allocate corporate normalisation proceeds and prevent moral hazard. As such, corporations undergoing temporary financial constrains are eligible for a subsidy under the Fund. This will be in effect until December 31 2025.

Article 15(3) of the Enforcement Decree for the DRBA was amended on June 2 2020. Under the amended Decree, the upper ceiling for a rehabilitation claim and secured rehabilitation claim required for Simplified Rehabilitation Proceedings (namely, a simplified form of rehabilitation proceedings entailing relatively lower costs than standard rehabilitation proceedings and which is available for small-to-mid business entities with a small amount of operating income) was raised from KRW3 billion ($2.5 million) to KRW5 billion. Unlike in standard rehabilitation proceedings, the approval requirements for the Simplified Rehabilitation Proceedings have become more lenient.

Covid-19 infection rates resurged in August 2020. There is a possibility that, in the future, forceful shutdowns may be implemented as a compulsory measure to prevent a further spike in Covid-19. If the pandemic continues, it may in turn have a substantial impact on the legal regime.

Looking ahead

The importance of appropriate timing in an application for and commencement of rehabilitation cannot be overemphasised. In a number of instances, corporations have delayed filing for rehabilitation in fear of the stigma surrounding the proceedings, only worsening their chances of rehabilitation. An accurate and practical assessment of the appropriate timeline for the application by management is highly recommended.

In light of the above, the courts should also prioritise the prompt handling and completion of rehabilitation proceedings. Where debts are settled/paid under a rehabilitation plan and the purposes of the rehabilitation plan are achievable without hindering the implementation of the plan, then the court has the discretion to apply for, or to directly order, the completion of the rehabilitation. This is typically called an "early termination". Incomplete corporate rehabilitation proceedings that linger in the courts hinder corporations' business activities as they prohibit commercial bidding with public entities during the pendency of the rehabilitation proceedings; this may result in a counter-productive outcome where a corporation which needs to quickly rehabilitate via business activities is unable to do so. Accordingly, it may be recommendable for the courts to more actively seek reasonable means to consider and implement an "early termination".

Flexibility in rehabilitation proceedings is improving in order to facilitate a corporate restructuring. For instance, the Korean Rehabilitation Court has adopted P-Plan (Pre-packaged Plan), which allows for the submission of a pre-pack plan prescribed under Article 223 of the DRBA. Where it is possible to settle debt via share or asset sales before the start of rehabilitation proceedings, a debtor-company, having conferred with its creditors, may prepare a pre-pack plan and submit it to the courts together with the application for rehabilitation – thereby facilitating the rehabilitation and a return to normal business.

Korean exports in the second quarter of 2020 declined by 20.2%. As such, rehabilitation and bankruptcy applications in the second half of 2020 are expected to increase, and the role of professionals with relevant expertise will be critical. We also expect that rules around DIP financing will be strengthened.

These precarious times mean that corporate management teams should tread carefully. Entering rehabilitation proceedings does not automatically mean that existing management must cede control over their businesses. As indicated, the DRBA provides that the existing management shall continue to manage the corporation as the receiver/custodian. On a positive note, the number of corporations that have successfully completed rehabilitation proceedings and resumed business is increasing.

Corporate management teams may be well advised to consider the appropriate timing and measures for rehabilitation rather than simply discount it as an option. Competent professionals with relevant expertise may be of assistance.

Switzerland

Stefan Kramer and Stefan Bindschedler, Homburger

In mid-March 2020, due to rapidly increasing numbers of infections in Switzerland, the Swiss government – the Federal Council – declared the epidemic situation in connection with Covid-19 as "extraordinary" and tightened measures to combat its spread. In particular, the Swiss government imposed restrictions on border crossings and ordered that all schools, shops, restaurants and bars, as well as all entertainment and leisure facilities, be closed. It only eased these measures partially and gradually after May 11 2020.

The Swiss economy was dealt a severe blow. Many companies were forced to restrict or even suspend their activities in the wake of these measures, triggering a sharp fall in GDP. The GDP is expected to plunge by approximately 6% over the year as a whole, while unemployment is expected to hit 3.8% (it was 2.3% in 2019). Yet, not least due to the Swiss government's swift response, the majority of Swiss businesses have so far coped relatively well with the adverse economic environment, with no significant increase of the number of new bankruptcy proceedings so far.

Covid-19

To counteract the negative effects of its public health measures, the Federal Council enacted a wide variety of support initiatives to give troubled businesses a hand. Of these initiatives, three broad responses emerged as the most significant.

In the first, the Federal Council adopted and implemented temporary changes to short-time work compensation, extending the entitlement up to August 31 2020 for the following employees, who were previously not covered: (i) fixed-term contract and temporary employees, apprentices and, under certain conditions, employees on call; (ii) persons who work in the business of their spouse/registered partner; and (iii) employees qualifying as

Homburger

www.homburger.ch

Stefan Kramer
Partner, Homburger
Zurich, Switzerland
T: +41 43 222 16 35
E: stefan.kramer@homburger.ch
W: www.homburger.ch/en/lawyers/stefan-kramer

Stefan Kramer is a partner and head of Homburger's restructuring & insolvency team. He regularly works on insolvency-related matters, including recovery and resolution planning and cross-border recognition of insolvency measures. He also advises on all regulatory aspects, including banking and stock exchange regulations and derivatives market regulations.

Stefan Bindschedler
Associate, Homburger
Zurich, Switzerland
T: +41 43 222 12 21
E: stefan.bindschedler@homburger.ch
W: www.homburger.ch/en/lawyers/stefan-bindschedler

Stefan Bindschedler's practice focuses on finance and capital markets law. He regularly advises on syndicated debt financings, buyout financings and financial restructurings. He also advises on regulatory aspects, including banking and stock exchange regulations.

"employer-like", such as shareholders who work as salaried employees.

The application process was also simplified: the waiting period was lifted, the period of authorisation was extended from three to six months and the process in general was facilitated (for instance, with simpler application forms etc.). While certain facilitation measures (such as the prolonged period of authorisation) will gradually be phased out starting on September 1 2020, the simplified application process will remain in place until December 31 2020.

Since short-time work compensation proved an effective instrument to combat the economic impacts of Covid-19, on July 1 2020, the Federal Council prolonged the period of entitlement from 12 months to 18 months, starting from September 1 2020 and lasting until the end of 2021.

A second key initiative was government-backed bridge loans. On March 25 2020, the Federal Council established a secured bridge loan-programme in the aggregate amount to up to CHF20 billion (later upsized to up to CHF40 billion), which was designed to provide secured bridge loans in a rapid and unbureaucratic manner. It consisted of two types of bridge facilities, which could be applied for until July 31 2020:

- Covid-19-Loan: loans up to CHF500,000, 100% (indirectly) secured by the Swiss Confederation by means of a joint surety and granted within a short timeframe, based solely on the information and documentation provided by the applicant and without any further credit checks.
- Covid-19-Loan-Plus: loans exceeding CHF500,000 and up to a maximum of CHF20 million, 85% (indirectly) secured by the Swiss Confederation by means of a joint surety and preceded by a credit check by the relevant lending bank in line with standard industry practice.

The maximum credit amount was limited to 10% of the applicant's turnover in the preceding financial year. Notably, companies (i) with a turnover over CHF500 million or (ii) not being (significantly) economically affected by the pandemic were not eligible.

The interest rate was set at 0.0% per annum, for Covid-19-Loans, whereas Covid-19-Loan-Plus will bear an interest rate of 0.5% per annum on the amount which is (indirectly) secured by the Swiss Confederation.The interest rate on the remaining, unsecured part of the Covid-19-Loan Plus is at the discretion of the parties. The term may extend to up to five years, with the possibility of a hardship-extension for an additional two years with the consent of the government.

Covid-19-Loans and Covid-19-Loans-Plus cannot be used for new investments in fixed assets unless they constitute replacement investments. A borrower is generally no longer permitted to distribute dividends/royalties, reimburse capital contributions, grant or refinance loans or repay intragroup loans (subject to certain exceptions). Non-compliance with these restrictions may trigger civil law liability and criminal law sanctions.

While the relevant ordinance will expire on September 25 2020, it is envisaged that the ordinance will transform it into statutory law in substance. The government has contemplated that certain provisions will be adjusted, for example restrictions (permissibility of new capex), interest, and repayment etc. The Swiss Federal Parliament is set to debate on and enact the relevant statutory law in autumn 2020.

A third key pillar of the government's response was the modified insolvency regime. In mid-March 2020 the Federal Council ordered a stay of enforcement from March 19 to April 4 2020 (prolonged by the statutory enforcement holidays until April 19 2020) and a standstill or extension of the deadlines in court proceedings from March 21 until April 19 2020. On April 16 2020, the Federal Council enacted substantive, temporary measures in relation to the Swiss insolvency regime that are set to remain in force until October 20 2020 and include the following:

- A suspension of the duty of the board of directors to notify the bankruptcy court in case of over-indebtedness in certain circumstances (see below under 'Directors' duties').
- A new Covid-19-Moratorium for small and medium-sized enterprises, which provides such companies with a simple and straightforward procedure to obtain a temporary deferral of their payment obligations in order to reorganize and prepare for the time after the crisis.
- Certain other amendments such as facilitations to enter into a moratorium and an extension of the provisional moratorium to six months.

Basic framework

Under Swiss insolvency laws, there is no group insolvency concept, so each entity must be dealt with separately. However, sector-specific rules may apply. In particular, insolvencies of banks, securities firms, insurance companies, collective investment schemes and fund managers are subject to special insolvency regimes.

Enforcement proceedings are generally not initiated *ex officio*, but rather require a petition. The debtor itself must initiate insolvency proceedings in the event of overindebtedness (*i.e.*, when its liabilities exceed the value of its assets (see below under 'Directors' duties')). If a creditor seeks to initiate insolvency proceedings, it must file an enforcement request with the competent debt collection office and pass through an introductory phase. As a rule, this introductory phase is mandatory; in extraordinary circumstances, however, the debtor, a creditor or the statutory auditors can directly apply for declaration of bankruptcy to the bankruptcy court.

Broadly, the Swiss Federal Debt Enforcement and Bankruptcy Act (DEBA) provides for three types of debt enforcement:

1. Enforcement of unsecured claims against individuals will, subject to the below, be pursued by way of seizure and realisation of assets belonging to the debtor to the extent necessary to cover the claim.
2. Enforcement of unsecured claims against individuals and legal entities registered in the Swiss commercial register will lead to bankruptcy proceedings opened against the debtor. In limited circumstances, bankruptcy proceedings are available also for individuals not registered in the commercial register. Once bankruptcy proceedings have been opened, all the debtor's assets form an estate over which the debtor can no longer dispose. The estate is then realised, and the proceeds are distributed among the creditors, taking into account their claims' value and priority.
3. Enforcement of secured claims both against natural persons and against legal entities might have to be pursued by way of realisation of the collateral.

To avoid bankruptcy, debtors facing financial distress may be able to apply for a Covid-19 Moratorium or a moratorium under Swiss corporate law. In addition, as an alternative to bankruptcy proceedings, the DEBA provides for statutory composition proceedings, which allow for a restructuring of the company with a view to continuing its business on a sounder basis and for liquidation of the company in a manner that is more beneficial to creditors than bankruptcy proceedings. Composition proceedings provide for the ability to achieve reorganisation during a moratorium by way of a composition agreement between the debtor and its creditors. Eventually, any composition agreement needs to be approved by the competent court and thereafter becomes binding on all creditors.

Directors' duties

In case of a substantiated concern of over-indebtedness, the board of directors of the relevant company has to procure that an (audited) interim balance sheet be drawn up based on (i) liquidation values and (ii) going concern values. For purposes of this calculation, unlike Covid-19-Loans-Plus, any Covid-19-Loans will temporarily not be taken into account until at least March 31 2022, and the interim balance sheet must not be audited for the period until October 20 2020. If such interim balance sheets show over-indebtedness, the board of directors must notify the bankruptcy court without delay. Non-compliance with this obligation may expose the board of directors to both civil law liability and criminal law sanctions and the statutory auditors have the obligation to notify the competent court in such case.

The board of directors need, however, not file for bankruptcy if: (i) creditors with claims in an aggregate amount not lower than the amount of the over-indebtedness subordinate their claims against the claims of all other creditors; (ii) if there is a substantiated likelihood for an informal workout within a relatively short period of time; or (iii) under the Covid-19 modified insolvency regime, if there is a prospect that the over-indebtedness will be eliminated by December 31 2020, provided that the debtor was not already over-indebted on December 31 2019. Despite the Covid-19 modified insolvency regime expiring on October 20 2020, we believe that companies may continue to rely on this exemption until the end of the year under the conditions specified therein.

While the criterion of over-indebtedness is based on a balance sheet test (rather than a liquidity test), the loss of the going concern assumption leads to an obligation to account for liquidation values, which will, in turn, typically result in over-indebtedness. Under Swiss law, such going concern assumption is lost if it is intended or probably inevitable that all or some activities of the company will cease in the next 12 months. To that effect, the board of directors must examine the current economic situation and future business development with a budget and a liquidity plan, taking into account the order book, the situation vis-à-vis lenders, the procurement of liquidity through the sale of assets, etc. As as soon as the debtor loses such going concern assumption for accounting purposes, going concern values become irrelevant and the test is exclusively based on liquidation values. In times of financial distress, the board of directors must therefore intensify its supervision and monitoring activities in general and place enhanced scrutiny on the ongoing assessment of the going concern assumption.

The board of directors generally has a fiduciary duty to safeguard the interest of the company and, as such, in times of financial distress, must convene regularly and prepare restructuring and/or refinancing strategies as well as contingency plans. If the prospects of successful restructuring and/or refinancing fade, its fiduciary duty shifts, however, towards safeguarding the interests of the creditors.

Challenging a debtor's transactions

The insolvency administration and certain creditors may, under certain conditions, void transactions. A transaction that is detrimental to the debtor's creditors may be voided in the following cases:

- The debtor has made a gift or a disposal of assets without any or with a disproportionate consideration, provided that the debtor made such transaction within the last year prior to the seizure, the opening of bankruptcy proceedings or the granting of a moratorium.
- In addition, certain actions are voidable if performed by the debtor within the last year prior to the seizure, the opening of bankruptcy proceedings or the granting of a moratorium, provided that the debtor was already (recognizably) overindebted at that time: (i) granting of security for already existing claims, provided that the debtor was not previously obliged to grant such security, (ii) payment of a monetary obligation in any way other than by payment in cash

UK

Rebecca Jarvis, Jo Windsor and Paul Sidle, Linklaters

The UK has a highly flexible corporate restructuring and insolvency environment and has, in the last decade, claimed its rightful place alongside New York as a key international hub for high value complex restructurings.

It remains to be seen, of course, to what extent this will be impacted when the Brexit transition period expires at 11pm on December 31. Recognition in the EU has been particularly relevant in the growth in the use of UK schemes of arrangement and will play a role in the new restructuring plan process (more below), which is being seen as a viable international restructuring tool. However, with the UK Court of Appeal recently affirming the inability of foreign restructuring processes to compromise English law obligations, the prevailing use of English (and New York) law debt in international finance and the certainty offered by the UK's court system and case law, the UK's restructuring and insolvency framework will remain attractive.

Legal developments in 2020 have largely been dominated by the government's response to the Covid-19 pandemic through a wide-ranging package of measures introduced by the Corporate Insolvency and Governance Act 2020 (CIGA), passed at the end of June. Its introduction of the new restructuring plan is aimed at keeping the UK relevant against other international reforms. Practitioners will watch with keen interest as jurisprudence develops in connection with the cross-class cram down mechanism.

In other non-Covid-19 related developments, public concern around the small minority of potential abuses and widely publicised cases dealing with pension issues have resulted in proposed new criminal offences in the Pension Schemes Bill. Their scope is broad and could deter efforts to undertake financial restructurings for a distressed group with a defined benefit pension. Further, in a move criticized by some in the restructuring and insolvency community, the Finance Act 2020 will make HMRC a "preferential creditor"

Linklaters

www.linklaters.com

Rebecca Jarvis
Partner, Linklaters
London, UK
T: +44 207 456 4466
E: rebecca.jarvis@linklaters.com
W: www.linklaters.com/en/find-a-lawyer/rebecca-jarvis

Rebecca Jarvis is Linklaters' global co-head of restructuring and insolvency. She has experience in all aspects of non-contentious reconstruction and insolvency work acting for banks, financial institutions, other creditors, corporate clients and insolvency practitioners in relation to recovery, reconstruction or distressed debt problems.

Jo Windsor
Partner, Linklaters
London, UK
T: +44 207 456 4436
E: jo.windsor@linklaters.com
W: www.linklaters.com/en/find-a-lawyer/jo-windsor

Jo Windsor has been working in the field of restructuring and insolvency for over 30 years, specialising in complex cross-border matters. He has been involved in the restructuring of companies in more than 30 different jurisdictions and is the author of many articles addressing specific issues relating to restructuring and insolvency.

Paul Sidle
Counsel PSL, Linklaters
London, UK
T: +44 20 7456 4698
E: paul.sidle@linklaters.com
W: www.linklaters.com

Paul Sidle is a senior professional support lawyer at Linklaters. His focus is on English and international restructuring and insolvency, including the resolution of financial institutions.

for certain taxes owing to it that a business had already deducted from customers and employees before its insolvency (such as VAT or PAYE). While HMRC will still rank behind certain employee-related claims, they will rank ahead of floating charge holders.

Basic framework

Formal collective insolvency procedures under the Insolvency Act 1986 (the Act) consist of:

- company voluntary arrangements (CVA) – used to rescue a company. More recently, it has been used to deal with obligations under unprofitable leases. It is unable to bind secured creditors without their consent;
- administration – ostensibly a corporate rescue process, although more often used to rescue the business through a going concern sale – frequently arranged in advance of filing and known as a pre-pack; and
- liquidation – a terminal procedure typically resulting in the piecemeal sale of assets (rather than the business), distribution of the proceeds to creditors and dissolution of the company. In a solvent liquidation, surplus proceeds are returned to shareholders.

The Act also contains a standalone moratorium procedure – recently introduced by the CIGA reforms. It is available to distressed but viable debtors, focused on company rescue. Directors remain in place subject to the oversight of a "monitor". The procedure is likely to be restricted in practice to SMEs.

Liquidation (except for the solvent type), administration and the standalone moratorium require the company to be insolvent, tested on a current or near future inability to pay debts as they fall due or on a longer-term basis where the company's liabilities exceed its assets.

Receivership is a secured creditor's limited enforcement remedy.

Large financial restructurings are usually achieved without recourse to an insolvency filing, being implemented either consensually, by using a Companies Act cram-down mechanism or by using contractual powers under an intercreditor agreement, aligned with an enforcement sale.

The Companies Act 2006 contains two procedures for corporate restructuring: a scheme of arrangement; and a restructuring plan, as introduced by CIGA.

Although similar procedurally, only a restructuring plan may impose a solution on a dissenting *class* of creditors and its voting mechanics are simpler as there is no numerosity test. It is, however, new and its cross-class cram down provisions remain untested. Unlike a scheme, a debtor looking to use a restructuring plan must show it is experiencing, or likely to experience, financial difficulties and the purpose of the plan is to eliminate those difficulties. However, there is no requirement for a debtor to be formally insolvent to use the scheme or restructuring plan process.

English insolvency law operates along legal entity lines. There is no concept of a single group insolvency proceeding and limited scope for treating the assets of one group company as belonging to another group company.

Directors' duties

Directors of English companies must comply with a range of statutory, common law and fiduciary duties, including a duty, where a company is facing financial difficulties, to have regard to the interests of creditors. This requirement is reinforced by statutory wrongful trading provisions, breach of which could lead to personal liability and/or disqualification. In particular, liability may arise if the court is satisfied that the director knew (or should have known) in pre-insolvency proceedings that the company had no reasonable prospect of avoiding going into insolvent liquidation or administration; and once that became clear, the director did not take every step to minimise the potential loss to creditors that they should have taken.

As a result of the Covid-19 pandemic, the Act provides that the Court should assume that a director was not guilty of wrongful trading during the period March 1 –September 30 2020. The blanket protection does not, however, extend to, among others, the directors of banks and insurance companies. Directors' other statutory and common law duties also continue to apply, so the relaxation is not as helpful as it appears at first glance.

Formal filing

Until recently, only suppliers of utilities, communications and IT-related services were affected by English insolvency law provisions imposing conditions and restrictions on a supplier's contractual rights on the customer's insolvency. CIGA has since introduced a provision applying to supplies of goods or services more generally. Taken together, insolvency practitioners now have broad powers to limit the terms suppliers can impose on insolvency and to restrict the exercise of existing termination rights. There are, however, limits to what the provisions can achieve in practice.

Filing for administration automatically gives rise to a broad stay preventing, for example, the commencement or continuation of legal proceedings or secured creditor enforcement action. The moratorium may only be lifted with the consent of the administrator or the court. It does not, however, apply to certain financial collateral arrangements.

When a company enters the standalone moratorium procedure, the company benefits from a payment holiday for some "pre-moratorium debts" – although the company must continue to pay (among other amounts) scheduled finance repayments, rent for the period during the moratorium and employees. The company must also meet all new "moratorium debts" (for example, trading costs arising during the moratorium under a new supply contract). As well as a payment holiday, the procedure gives rise to restrictions similar to those found in the moratorium in administration.

There is a limited procedural stay in liquidation, but it does not prevent secured creditor enforcement. A CVA does not give rise to a stay, although the proposal voted on by creditors may provide for one.

The court has discretion to grant a temporary stay of creditor action where a scheme is being implemented and appears to have a reasonable chance of success with majority creditor support.

For large financial restructurings, financial creditors often contractually refrain from bringing disruptive action or agree to a temporary stay to assist stability during the negotiation of a consensual deal.

Priority, dissenters and asset sales

Insolvency expenses, which could include insolvency funding, rank ahead of (i) preferential debts (primarily, certain amounts owed to employees and, possibly from December 2020, certain amounts owed to HMRC); (ii) the 'prescribed part' (an amount, depending on the date of the charge but not exceeding £800,000, set aside from floating charge realisations to satisfy claims of unsecured creditors); and (iii) floating charge (but not fixed charge) claims and unsecured claims. In some circumstances, where a liquidation or administration follow an unsuccessful standalone moratorium, certain pre-moratorium debts and moratorium debts may take priority over the insolvency expenses.

A CVA can bind unsecured dissenting or non-voting creditors, but only a scheme or restructuring plan can bind secured claims. Creditors within a class may be crammed-down in a scheme and restructuring plan, but only in a restructuring plan – provided certain protective conditions are met – may the court sanction a plan notwithstanding the dissent of one or more classes (albeit a cross-class cram down is, at the date of writing, untested under English law).

A restructuring plan can in theory impose a solution on both creditors and shareholders without their consent. Notably, certain corporate provisions relating to pre-emption rights and allotment are disapplied in a restructuring plan which would seem to allow, for example, a debt for equity swap to be imposed without having to effect an enforcement sale/pre-pack.

A pre-pack sale is not a special type of insolvency procedure but generally refers to:

- a sale of the business and/or assets of an insolvent company (usually by an administrator);
- where the preparatory work (for example, identifying the purchaser, and negotiating the terms of the sale) takes place before appointment; and
- the sale is concluded almost immediately after appointment without court or creditor sanction, and often with little or no formal marketing of the business or assets being sold. Administrators must, however, be able to explain to the company's creditors why the insolvency sale was entered into.

In practice, a pre-pack to a secured creditor would usually involve the purchase by a SPV owned by the secured creditors. The consideration will likely involve a release and/or an assumption of all or some of the secured liabilities by the SPV (with the secured creditors, in effect, "bidding their debt").

It should be noted that modified insolvency regimes are typically found in the financial industry (such as the special resolution regime for banks) or the utilities, transport and health sectors. In some sectors or industries, special factors may become relevant in an insolvency situation, for example where the business operates in a highly regulated or politically sensitive area (for instance prisons, schools etc). The Act may also be modified in its application to certain types of company or bodies (partnerships or insurers), although they have no separate special insolvency regime as such.

Employees, pension trustees, government or regulatory bodies could all have an impact on the outcome of a restructuring depending on the situation and what is proposed.

The Act enables a liquidator or administrator to set-aside a range of pre-insolvency transactions, including transactions at an undervalue, preferences, extortionate credit transactions, certain floating charges and transactions defrauding creditors. The 'look-back' period during which transactions are at risk ranges from six months to two years depending on the circumstances. That may, in effect, be further extended by six months in certain compulsory liquidations based on winding-up petitions presented between April and September 2020 (this is a specific amendment).

Crossing borders

The English court has the ability to wind-up a foreign debtor based on a "sufficient connection" test. It is not a particularly difficult threshold to satisfy, as there is no minimum asset requirement and being party to English governing law documents may suffice. However, during the Brexit transition period, the English court's insolvency jurisdiction is restricted by Regulation (EU) 2015/848 on Insolvency Proceedings (EIR). Where the EIR applies, jurisdiction and the recognition and effect of insolvency proceedings throughout the EU must be determined by the location of a debtor's centre of main interests (COMI) or the existence of an "establishment". COMI is the place where the debtor conducts the administration of its interests on a regular basis and which is ascertainable by third parties. For a corporation, there is a rebuttable presumption that its COMI is the place of its registered office. Ultimately, COMI is fact specific and is a more stringent test than "sufficient connection".

After the expiry of the Brexit transition period, the position in the UK remains subject to final legislation. As a starting point, the English court will be able to base jurisdiction on the simple "sufficient connection" test. While the EIR is expected to become retained UK law, the majority of its provisions will likely be repealed. Rather than restrict the English court's insolvency jurisdiction, the retained EIR will afford the English court the flexibility to base jurisdiction for the opening of English insolvency proceedings on a debtor's UK COMI/establishment. If jurisdiction were based on a UK COMI/establishment, rather than simply "sufficient connection", this could improve the chances of a UK insolvency process obtaining recognition in an EU27 state, for example.

In addition, it may be possible to commence insolvency proceedings by the provision of assistance under the three methods listed below.

Before the end of the Brexit transition period, the EIR will continue to apply in the UK as regards recognition of EU proceedings. The English courts may also assist in insolvency matters by way of:

- section 426 of the Act which enables the English court to give wide assistance to the courts of certain designated jurisdictions (mainly common law countries; they do not include the US), subject to judicial discretion;
- the Cross Border Insolvency Regulations 2006 (CBIR) which focus on the recognition of and co-operation between foreign insolvency proceedings, but unlike the EIR do not allocate insolvency jurisdiction; and
- the court's inherent power to recognise and grant assistance to foreign insolvency proceedings under the common law, although recent judicial authority has shown it is limited in scope.

After the expiry of the Brexit transition period, the position in the UK remains subject to final legislation

Covid-19 and beyond

Insolvency levels (as at summer 2020) remain suppressed due to the various support measures taken by the UK government. On their expiry, however, a significant uptick in restructuring and insolvency situations is widely expected.

The UK Government has implemented a broad array of support measures in response to Covid-19. These include, for example: providing direct support to corporates through a range of targeted financing and asset purchase facilities; offering credit support schemes to encourage bank lending to both SMEs and larger corporates; creating a job retention scheme supporting the use of furlough by employers; various sector focussed stimulus packages; reducing HMRC enforcement activity; restricting the use of remedies available to commercial landlords; and temporarily easing account and other filing obligations.

The recent restructuring and insolvency reforms introduced by CIGA will need time to fully bed themselves in. There may also be further changes required as any practical issues arise owing to the speed with which the legislation was enacted. The new restructuring plan has the potential to offer a one-stop solution for large businesses seeking to effect a financial and operational restructuring and we expect jurisprudence to develop in this area.

CORPORATE INSOLVENCY & RESTRUCTURING REPORT 2020: COVID-19 SPECIAL FOCUS

United States

Robert Trust, Christopher Hunker and Maximilian Ferullo, Linklaters

Like many jurisdictions, the US has seen a surge in bankruptcy filings amid the Covid-19 pandemic. Retailers – already burdened by unfavourable lease obligations and a general shift in consumer preference to e-commerce – have borne the brunt of the crisis. In the first two quarters of 2020, nearly 20 major retailers sought Chapter 11 protection in the US, including high-profile brands such as JC Penney, Neiman Marcus, J Crew, Pier 1 Imports, John Varvatos, True Religion, Modell's Sporting Goods and GNC.

The energy sector has also seen a dramatic increase in Chapter 11 filings. During the first half of 2020, 40 energy companies filed for Chapter 11 – the most since 2016. While these two sectors made up the largest share of filings in the first half of the year, Chapter 11 filings were up for nearly every industry, which highlights the unprecedented impact of the Covid-19 pandemic.

Companies in trouble, including those adversely impacted by the pandemic, will find that the US environment for corporate restructuring cases is very accommodating. The US enjoys the advantage of an experienced judiciary comprised primarily of former restructuring lawyers. The US also has a well-established statute – the US Bankruptcy Code – and a sophisticated advisory community that is accustomed to using the US Bankruptcy Code's tools to resolve complex domestic and cross- border corporate restructuring cases.

Even still, significant emergency relief measures have been proposed or implemented in response to the current economic crisis. With passage of the Coronavirus Aid, Relief, and Economic Security (CARES) Act in March 2020, Congress sought to offer relief to troubled companies dealing with the impact of Covid-19. The CARES Act made important revisions to the US Bankruptcy Code for small businesses. By temporarily increasing the debt

www.linklaters.com

Robert Trust
Partner, Linklaters
New York, US
T: +1 212 903 9217
E: robert.trust@linklaters.com
W: www.linklaters.com/en/find-a-lawyer/robert-trust

Robert Trust regularly advises clients in connection with Chapter 11 restructurings, out-of-court workouts, acquisitions of troubled companies and the structuring of corporate and credit transactions.

Christopher Hunker
Counsel, Linklaters
New York, US
T: +1 212 903 9267
E: christopher.hunker@linklaters.com
W: www.linklaters.com

Christopher Hunker has significant experience advising key constituents in corporate reorganizations, restructurings and liquidations.

Maximilian Ferullo
Associate, Linklaters
New York, US
T: + 1 212 903 9356
E: maximilian.ferullo@linklaters.com
W: www.linklaters.com

Maximilian A Ferullo is involved in all facets of corporate reorganisations and out-of-court restructurings.

threshold for businesses eligible to participate in the streamlined Chapter 11 procedures established under the Small Business Reorganization Act of 2019 (SBRA), Congress sought to enable small businesses to reorganize in a more efficient and cost-effective manner.

US bankruptcy courts, operating as courts of equity, have also taken the practical impact of the crisis into account. In several recently filed retail cases, including *Pier 1 Imports*, *Modell's*, and *J. Crew*, bankruptcy courts took the highly unusual step – over the objections of their landlords – of allowing the debtors to defer payment of post-petition rent during the period when operations at its stores were limited by state mandated "stay-at-home" orders.

Basic framework

The US Bankruptcy Code provides two primary types of insolvency cases for financially distressed corporate debtors: Chapter 7 and Chapter 11. A debtor does not need to be insolvent to commence a Chapter 7 or Chapter 11 case. Chapter 11 is a reorganisation regime used frequently by corporate debtors because it provides an opportunity to reorganise as a going concern. Typically, in a Chapter 11 case, the debtor's management and board of directors remain in place, and the debtor attempts to confirm a Chapter 11 plan of reorganisation.

Chapter 7 bankruptcies are liquidation proceedings in which a court-appointed trustee shuts down the business, liquidates the assets, and then distributes the proceeds to creditors. It is less common for a large company to file a Chapter 7 case because the company will likely not remain as a going concern.

Directors' duties

In general, directors and officers owe fiduciary duties of loyalty, care and good faith to the company and shareholders for which they serve. As a company begins to experience financial distress, it is important that the board of directors hire legal and financial advisors to assist them in discharging their duties. Although those duties do not shift to a particular group of stakeholders when a company is in financial distress, the board's actions will often be scrutinised by creditors particularly if the company subsequently files for bankruptcy protection.

The duties owed by directors and officers have not changed as a result of the pandemic. However, a company's officers and directors would be prudent to consider how the unique challenges presented by the crisis affects their existing duties. Companies that have been performing well previously but are now experiencing financial distress primarily because of the pandemic would benefit from legal counsel and financial advice about their fiduciary duties and how best to discharge them in these uncertain times.

The filing of a bankruptcy petition has an immediate impact on the rights of creditors and affords debtors certain protections during the pendency of the case. Upon becoming a debtor under Chapter 7 or Chapter 11, the debtor enjoys the statutory protections of an automatic stay. The automatic stay is a pervasive worldwide injunction that protects a debtor and its assets wherever located from litigation, lien enforcement, declaration of acceleration and other actions (judicial or otherwise) that attempt to enforce or collect a prepetition claim or otherwise affect the debtor's property.

The automatic stay remains in effect while a bankruptcy case is pending unless one of the narrow exceptions applies or the court terminates or modifies the stay upon a party's request. The US Bankruptcy Code contains an exception for certain protected financial contracts. A provision in a contract that provides for its termination upon insolvency or bankruptcy is generally unenforceable.

Priority, dissenters and asset sales

The US Bankruptcy Code contains a detailed priority scheme. Certain prepetition claims are designated as priority claims, including employee wages earned within 180 days of the bankruptcy case (subject to

There is tremendous uncertainty going into the next 12 months. The ultimate toll the virus will take on US businesses remains unclear

a statutory cap), contributions to an employee benefit plan and taxes owed to governmental authorities. Priority claims are senior in right of payment to general unsecured claims. A Chapter 11 plan cannot be confirmed unless it provides for the payment of priority claims in full in cash.

The US Bankruptcy Code provides inducements to lenders to provide post-petition financing to a financially distressed company. The debtor can grant a priming lien on its assets that ranks senior to certain pre-bankruptcy liens and a superpriority administrative claim that ranks senior in right of payment to all other administrative and priority claims. A debtor's ability to obtain debtor-in-possession (DIP) financing is a major advantage of the US Bankruptcy Code because it usually facilitates a debtor's reorganisation.

The US Bankruptcy Code permits a debtor to bind dissenting creditors and shareholders to a confirmed Chapter 11 plan and cram down a class of creditors or shareholders that does not vote to accept a Chapter 11 plan.

A dissenting creditor or shareholder will be bound by a confirmed Chapter 11 plan if the class in which the dissenting creditor or shareholder sits votes to accept the plan. Often times, shareholders' existing interests are extinguished under a Chapter 11 plan and the class of existing equity holders is conclusively presumed to reject the Chapter 11 plan without an opportunity to vote. Whether or not a class of shareholders has an opportunity to vote on a Chapter 11 plan depends largely on whether there are sufficient assets to pay creditors in full.

A Chapter 11 plan of reorganisation can be crammed down on a class of creditors or shareholders that does not vote to accept a plan, if a debtor can show, among other things, that: (i) at least one impaired class of creditors has voted to accept the plan; (ii) the plan does not discriminate unfairly against the dissenting class; and (iii) the plan is fair and equitable with respect to each impaired dissenting class (meaning that the proposed Chapter 11 plan complies with the absolute priority rule).

The US Bankruptcy Code provides a debtor with the authority to sell its assets outside the ordinary course of business. Any asset sale outside the ordinary course of business must be approved by the US Bankruptcy Court after notice and a hearing. A debtor's decision to sell assets outside the ordinary course of business is reviewed by the US Bankruptcy Court under the deferential business judgment standard. The US Bankruptcy Code induces potential buyers to acquire an asset from a debtor by permitting the assets to be sold free and clear of liens, claims and interests if certain statutory requirements are met. If a debtor decides to sell its assets, it often seeks a stalking horse purchaser whose bid will usually be subject to an auction process.

Other considerations

Various other key stakeholders, such as the Pension Benefit Guaranty Corporation (PBGC) and other governmental or regulatory agencies (including state and federal taxing authorities), could all have an impact on the outcome of a restructuring depending on the circumstances of each case. For example, a debtor's failure to satisfy minimum funding requirements or attempts to terminate pension plans may result in significant claims by a plan trustee or the PBGC, a governmental agency that regulates pension plans and guarantees certain pension benefits.

Certain sectors and industries have their own or modified insolvency regimes. Different insolvency regimes exist under federal and state law to resolve national and state-chartered banks and other financial institutions, such as insurance companies, securities brokers and commodities broker. Insolvency regimes applicable to financial institutions generally require that a governmental regulator or trustee assume management of the business to wind down the business and satisfy claims in accordance with statutory priorities. In addition, the passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act in the aftermath of the financial crisis introduced another insolvency regime, known as the Orderly Liquidation Authority, which is applicable to financial institutions identified as systemically important.

Challenging a debtor's transactions

The US Bankruptcy Code permits a debtor to challenge certain pre-bankruptcy transactions after it commences a case. The US Bankruptcy Code provides a two-year look-back period from the petition date to challenge any transactions in which the debtor transferred assets (i) with an intent to hinder, delay, or defraud creditors (known as actual fraudulent transfer) or (ii) for less than reasonably equivalent value at a time when it was insolvent (known as constructive fraudulent transfer).

The US Bankruptcy Code provides a 90-day look-back period to challenge any alleged preferential transfers made by a debtor. The look-back period is one year if such transfers are made to a debtor's insider. A preference occurs when a debtor makes a transfer on account of antecedent debt at a time when it is insolvent that permits the creditor to recover more than it would have recovered in a hypothetical Chapter 7 case.

Crossing-borders

Non-US companies can commence a bankruptcy case because the threshold for establishing debtor eligibility under the US Bankruptcy Code is low. A foreign company is eligible to be a debtor under the US Bankruptcy Code if it has a place of business or property in the US. US Bankruptcy Courts have interpreted the property requirement broadly, holding that maintaining a bank account in the US or establishing a retainer with US counsel is sufficient.

Chapter 15 of the US Bankruptcy Code incorporates the Model Law on Cross-Border Insolvency to facilitate cooperation between US and foreign courts in cross-border insolvency cases. Recognition will be granted if certain statutory conditions are met and affording comity would not be manifestly contrary to US public policy. If the statutory requirements for recognition are satisfied, a foreign debtor can obtain the protection of the automatic stay in respect of its property located within the territorial jurisdiction of the US. US Bankruptcy Courts also have discretion to provide additional assistance, including recognising and enforcing approved schemes of arrangement or sauvegarde plans and related third party releases.

Covid-19 and beyond

Passage of the CARES Act as well as certain actions taken by the Federal Reserve have likely tempered the full impact of the Covid-19 pandemic on companies of all sizes and across all industries. The Paycheck Protection Program (PPP), a $669 billion business loan program established under the CARES Act, allowed certain businesses to apply for low-interest loans to retain workers and continue to operate. Unemployment benefits offered to qualifying individuals have likely bolstered sluggish consumer demand.

Much of the relief provided in the CARES Act has either expired or is set to expire in the coming months. It is unclear whether and to what extent these governmental initiatives will be extended to further mitigate the impact of the Covid-19 pandemic. To date, Congress has been unable to agree on a further stimulus package to extend the protections afforded to businesses under the act, including the PPP loan program, or the unemployment benefits offered to qualifying individuals under the Act.

- As such, heading into a presidential election year, there is tremendous uncertainty going into the next 12 months. The ultimate toll the virus will take on US businesses remains unknown.
- Many have compared the current downturn to the economic crisis of 2008 due to the massive unemployment, government stimulus and historically low interest rates. While lessons learned from 2008 will be instructive, there is significantly more liquidity available to businesses today. The Federal Reserve has implemented an aggressive direct lending program, and banks are well-capitalized and ready to expand lending. Many businesses will have access to cash while dealing with the impacts of the pandemic.

Under any scenario, we believe it is likely that US bankruptcy filings will continue to occur at a significant level over the next 6 to 12 months. Retail and energy sectors are likely to continue to face challenges and – absent further government intervention – filings are likely to increase dramatically in industries such as transportation, hospitality, and healthcare. Questions also remain as to the ultimate impact the pandemic will have on municipal governments. Rising deficits at the state and local government level will be something to watch as the federal government has so far balked at any form of relief for state and local governments whose revenues have been hard hit by the effects of the virus.

CHINA
JunHe

Juyi Lu

Latest regulations to further open up finance

The National Development and Reform Commission (NDRC) and the Ministry of Commerce (Mofcom) recently jointly issued two negative lists, both of which took effect on July 23 2020. The negative lists remove the restrictions on foreign shareholdings in securities companies, fund management companies, futures companies, and life insurance companies.

This is one of many measures aimed at further opening up China's financial sector in recent years. With opening up on the fast track, the market response has been positive, and foreign financial entities are entering the Chinese market at a much quicker pace. Here we briefly summarise the key regulatory updates and corresponding market movements.

This round of initiatives to open up financial services in China is a follow-up of its promise when it joined the WTO, following which the restriction of foreign shareholding ratio in the Chinese financial sector has been completely lifted.

We also note that foreign financial entities intend to play a larger role in life insurance and asset management in particular.

As the Covid-19 pandemic continues to sweep across the world, the global finance services industry has been hit hard. Compared to heightened and ongoing uncertainty in the EU and US, China has worked through it successfully, and seen its economy bounce back to growth.

In addition, as a result of rapid development over the past few decades, China has an expanding middle class in dire need of financial solutions.

- The various regulatory releasements in the Chinese financial sector offer potentially exciting opportunities for foreign businesses. More attention should and will be paid to the newly relaxed areas, especially life insurance and asset management.

Regulations	Market
In March 2018, the People's Bank of China (PBOC) liberalised market access restrictions for foreign payment institutions.	In September 2019, PayPal's PRC subsidiary obtained the first online payment service licence by a foreign-invested company.
In July 2019, the China Banking and Insurance Regulatory Commission (CBIRC) issued 11 measures for opening up, including encouraging foreign financial institutions to participate in the establishment of, and invest in the shares of, wealth management subsidiaries of commercial banks, as well as allowing foreign financial institutions to form investment pension management companies, etc.	In March 2019, the CBIRC approved the Sino-British joint venture Hengan Standard Life to prepare for the establishment of the first foreign-invested pension insurance company.
From April 1 2020, restrictions on foreign shareholding ratios of fund management companies was removed nationwide.	On the same day, BlackRock and Neuberger Berman became the first foreign entities to submit applications to set up mutual fund management companies in China.
From December 1 2020, restrictions on foreign shareholding ratios of securities companies will be removed nationwide.	In 2019, Nomura and JP Morgan won approval to set up new securities joint ventures in China. In 2020, Morgan Stanley and Goldman Sachs have received regulatory approval to buy majority stakes in their joint ventures in China.
From January 1 2020, restrictions on foreign shareholding ratios of life insurance companies was removed nationwide.	In January 2020, Allianz established a subsidiary as the first wholly foreign-owned insurance company in China.
In January 2020, the China-US trade agreement was published, which requires non-discriminatory participation in financial services.	On February 14 2020, Oaktree Capital, the first foreign distressed debt manager to establish a wholly-owned unit in China, established its subsidiary in Beijing.
In February 2020, PBOC, together with other authorities, further announced policy support for the Shanghai Lingang New Area, including the establishment of fintech companies.	In July 2020, HSBC announced that it was working with authorities to establish a fintech service company in Lingang.
In May 2020, PBOC, together with other authorities, announced 26 further measures to support the trade and financial sectors in the Guangdong-Hong Kong-Macao Greater Bay Area.	Since 2019, Standard Chartered Bank, HSBC, and other foreign-owned commercial banks have opened branches in the Greater Bay Area.

- Despite the policy advantages for foreign entities investing in the wealth management subsidiaries of commercial banks, we notice, from public news, that no foreign entity has moved into this area – which may be a new opportunity.
- When pursuing their onshore presence in China, foreign businesses may consider leveraging the financial policy advantages of the Shanghai Lingang New Area and the Greater Bay Area.

The latest regulations have sent a positive signal to foreign entities that China is moving towards a more open financial market for foreign participants. We believe that subsequent regulations will be issued for further liberalisation, the ultimate goal of which is national treatment. It is time for foreign businesses to act to re-evaluate their strategy in China.

JunHe
26/F HKRI Centre One, HKRI Taikoo Hui,
288 Shimen Road (No.1), Shanghai, PRC
T: +86 21 2208 6210
F: +86 21 5298 5492

COLOMBIA

Brigard Urrutia


Carlos Fradique-Méndez and Miguel Londoño

New investment regime for pension funds

The Colombian Ministry of Finance and Public Credit and the Financial Regulation Unit recently published a draft decree to reform the legal investment regime applicable to pension fund administrators, insurance, and capitalisation companies.

The proposed amendment seeks to reflect some of the guidelines set by the Capital Market Mission back in 2019. In this regard, the document introduces enhanced flexibility in the investment regime, granting entities greater freedom in the management and investment processes. An example of this is the abolition of specific investment limits applicable to certain assets or to an individual issuance, allowing the pension fund's investment committee and board of directors to set forth such restrictions.

Likewise, the reform proposes changes related to infrastructure private equity funds, establishing new criteria for them to be deemed as eligible investments. Similarly, the risk management control is transformed, shifting the investment limits measurement from the oversight of investment vehicles such as private equity funds, to the direct revision of the underlying assets in which these vehicles invest.

Although the draft decree will be subject to comments and adjustments derived from the opinion and perspective of the local industry, the proposal raises other important issues – such as the possibility of these institutional investors to invest in debt funds, and the incorporation of a more lenient regime that may contribute to meet the goals set by the Capital Market Mission, and to strengthen the local economy.

Brigard Urrutia
Calle 70 Bis No. 4 - 41
Bogotá, Colombia
T: +571 3462011 Ext.8650
W: www.bu.com.co

CYPRUS

Elias Neocleous & Co


Elena Christodoulou and Ioannis Sidiropoulos

Measures to tackle tax evasion

Cyprus is committed to staying abreast of all international and EU initiatives aimed at tackling tax evasion. To this end, Cyprus is making significant efforts to upgrade its tax legislation, in order to comply with both the guidelines of the OECD and the legislation of the EU.

It has already adopted general anti-abuse rules at a domestic level, and amendments to the relevant legislation are expected to provide increased, and more specific, powers to the tax authorities by giving them the power to impose tax liability, calculated in accordance with income tax legislation, to those who do not adhere to, and/or fail the valid commercial and economic reality test.

As part of this continuous effort, Cyprus has already incorporated into its domestic law (effective as of January 2016) the anti-avoidance provisions of the EU Parent – Subsidiary Directive (Directive 2015/121/EU – PSD GAAR). Cyprus has never applied withholding tax, so the amendments included in the directive did not have a direct effect in Cyprus.

BEPS/EU anti-abuse initiatives

On April 5 2019, the House of Representatives also approved legislation implementing the EU Anti-Tax Avoidance Directive (2016/1164/EC), (ATAD) in Cyprus with the aim of improving the internal market's ability to deal with cross-border tax avoidance practices.

The provisions relating to interest deductibility rules, controlled foreign companies (CFCs) and general anti-abuse rules (GAAR), as included in ATAD, entered into force on January 1 2019. GAAR rules only apply to corporate transactions.

On July 3 2020, the remaining two amendments for full implementation of the ATAD were published in the Official Gazette of the Republic.

The first concerns the introduction of an exit tax regime (ATAD I), which applies retroactively from January 1 2020. As exit taxes affect taxable assets and, given that certain assets are specifically exempt from the imposition of any Cypriot tax (e.g. securities), the imposition of exit tax is not expected to have material consequences.

The second is related to hybrid mismatches (ATAD II) and also applies retroactively from January 1. The so-called reverse hybrid mismatches rule will apply from January 1 2022. Issues of hybrid mismatches arise, for example, in cases where an entity or arrangement is regarded as a taxable entity under the laws of one jurisdiction and whose income or expenditure is treated as income or expenditure of one or more other persons under the laws of another jurisdiction.

At present, the only segment of Cypriot tax legislation that targets hybrid mismatches concerns dividends and income funds. According to this, dividends received by a Cyprus tax resident entity are subject to corporate tax if a tax deduction has been claimed for them at the level of the payer. The relevant amounts will not be tax exempt, and will be taxed as normal corporate income at a rate of 12.5%.

Tax treaty instructions/MLI

Furthermore, on January 22 2020, the ratification document of the Multilateral Convention on the Implementation of Tax Treaties (MLI) was published in the Official Gazette, together with the position of Cyprus and an explanatory statement.

Cyprus has approved the minimum actions as defined by the MLI, including

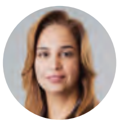
Article 7 (on abuse of the Treaty). Article 7 contains a GAAR based on the Principal Purpose of Transactions or Arrangements (PPT) as well as an additional option to supplement the PPT with a simplified Limitation on Benefits (LOB). In addition, Cyprus has chosen to apply paragraph 4 of the same article, in cases where the competent authority determines that such benefits would have been granted in the absence of the transaction or arrangement.

With the above legislative actions, Cyprus demonstrates its commitment to support international efforts to tackle tax evasion practices. Existing and new structures will need to ensure and display the by now well known, globally accepted substance requirements. Failure to adhere to these requirements may result, inter alia, in the recharacterisation of incomes, double taxation, monetary penalties/prosecutions, and the application of controlled foreign corporation rules. Therefore, clients are advised to review their structures and seek to understand how these developments may affect them.

Elias Neocleous & Co
Neocleous House, 195 Makarios III Avenue
1-5th floor, Limassol, CY, CY-3030, Cyprus
T: +357 25110110
F: +357 25110001
E: info@neo.law
W: www.neo.law

EGYPT

ALC Alieldean Weshahi & Partners

Dr Bahaa Alieldean and Dr Elham Mabrouk

Opportunities after the storm

For many of us in Egypt, Covid-19 was an abstraction on the horizon in early March as we were bailing out after a once-in-a-lifetime thunder-storm tore through the capital city. The streets had not yet dried out in many neighbourhoods when our reality was again transformed as curfews and RT-PCR tests for coronavirus, quarantine centres and closed borders became part of our daily lives.

A clear and early response to Covid-19 from both policymakers and businesses has left Egypt in a strong position

With the first wave of Covid-19 now behind us in Egypt, seasoned business executives are looking for new opportunities as they guide their companies through their second global economic crisis in just over a decade. Some of the most compelling opportunities are to be found in our very young and fast-growing market for non-bank financial services (NBFS) thanks to enlightened steps taken by the regulator at the height of the crisis.

Weathering the storm

A clear and early response to Covid-19 from both policymakers and businesses has left Egypt in a strong position. Our government imposed restrictions in early March: closing borders, enforcing a nighttime curfew, and shuttering houses of worship, among many other initiatives. Nationwide quarantine centres, Covid-19 treatment facilities, and the rapid buildout of testing capacity, all helped to minimise the human toll of the virus.

In parallel, the government earmarked more than EGP 100 billion (about \$6.3 billion, or approximately two percent of GDP) to shore up the health system and social safety net – and to support businesses and day labourers alike. The Central Bank of Egypt launched an unconventional EGP 20 billion programme to directly purchase securities on the Egyptian Exchange. Businesses and consumers got payment holidays on mortgages, leasing contracts, car payments and credit card debt. Companies in at-risk industries including tourism, aviation and media, got tax relief.

In parallel, business leaders managed a delicate balancing act of keeping their people safe while still delivering essential goods and services. With the last of the major lockdown measures having been relaxed on July 1 when the nation's borders reopened, the focus of executives across the nation has turned to rebuilding.

Securitisation – with a twist

Companies and investors looking for new opportunities will find them in recent decisions from Egypt's securities regulator, the Financial Regulatory Authority (FRA), which has oversight of all non-bank financial markets in Egypt.

We call the first securitisation with a twist. Securitisation has long been on the menu for companies in Egypt with securitisable assets, particularly those in real estate and automotive finance. Our firm helped create the legislation that made securitisation possible in Egypt in 2005, and we have advised on more than 35 bond issuances – most recently including the New Urban Communities Authority's in its EGP 4 billion bond, which was placed with local and foreign investors including the European Bank for Reconstruction and Development.

As the saying goes: the regulator giveth, and the regulator taketh away. NBFS companies accepted the six-month payment holiday ordered by the FRA at the height of Covid-19 – and were rewarded when the regulator offered them a new avenue to seek financing going forward.

Under a late June decision, the regulator will allow NBFS to raise funds from both institutional and – for the first time – retail investors, through a new type of transferrable value fund. These funds will be permitted to raise capital to invest in the acquisition of portfolios of assets held by consumer, mortgage and lease finance, as well as microfinance. The fund builds on a 2015 law that provided legal grounds for the creation of an Egyptian registry of movable collateral.

It's welcome news for players in an increasingly competitive industry who are looking for lower-cost alternatives to bank finance. Just days after the announcement, we filed on behalf of one of our clients to incorporate an EGP 2.5 billion transferrable value fund.

Islamic (and other) finance is now live in Egypt

While we're particularly excited about how transferable value funds could help sustainably grow Egypt's very young and fast-growing NBFS market, the opportunities don't stop there.

For generations, Islamic and corporate finance have been ephemeral creatures of the conference circuit in Egypt – much talked about, and rarely seen in the wild, even as they became staples of the global mainstream.

Thanks to Covid-19, they are now firmly on the investment menu. This spring, one of the country's larger real estate players pulled off Egypt's first corporate *sukuk*. Our team is now working on an EGP 2.5 billion *sukuk,* and we're aware of perhaps a half dozen in the pipeline. So, too, are more exotic instruments (by Middle East standards), including green bonds, where both the government and our country's largest private sector bank are preparing offerings.

However challenging 2020 has been for our community, this much is clear: in Egypt, a solid legislative base and a prudently aggressive approach to regulation are creating new avenues for growth as we look to leave this year behind.

ALC Alieldean Weshahi & Partners
5 Abd Elkawy Shams, Dokki,
Giza, Egypt
T: +202 3336 4313
W: www.alc.law

JAPAN

Nagashima Ohno & Tsunematsu

Takuya Kogashiwa

Amendment of Renewable Energy Special Measures Act

In recent years, many loans and investments have been actively extended for large-scale photovoltaic power generation projects in Japan. The Renewable Energy Special Measures Act (Act No. 108 of 2011), which forms the foundation of such projects, was amended on June 12 2020, and it will, in large part, take effect on April 1 2022.

This article reports (i) measures in relation to certification expiration, and (ii) the disposal cost reserve system, both of which are included in the amendment, since these are likely to attract the keen interest of investors and banks considering funding for solar power projects that have already been officially certified.

Expiration of certification

Under the current feed-in-tariff (FIT) system, a business operator which has obtained certification of a power generation business plan for a large-scale photovoltaic project is eligible to sell the generated electricity for a certain procurement period (typically, 20 years) at a predetermined procurement price (which has been on a declining trend).

However, projects that have been granted certification with a relatively high procurement price and that have not started power generation, while at the same time reserving grid capacity and thus blocking a new project from efficiently utilising it, have been considered problematic, and several measures have in the past been implemented to cope with the practice.

Further to those measures, the amendment stipulates that, if the power generation is not commenced within a certain period from the date of the relevant certification of the power generation business plan, such certification shall expire and, as a result, the grid capacity reserved by the relevant project will be released.

The details of the system were left to a Cabinet Order or an Ordinance of the Ministry of Economy, Trade and Industry (METI). If the targeted project has not yet been started and there is a probability that the certification for such project will expire after implementation of the amendment, this will lead to a lack of fundamental conditions for funding. Therefore, banks have become hesitant to extend loans for such projects.

Under such circumstances, on July 22 2020, a committee established by METI revealed a policy stating:

> "With regard to a photovoltaic power generation project with a capacity of 2MW or more that has already been granted the Certification of Power Generation Business Plan, if the Notification of Construction Plan has been received by the relevant authority without any deficiencies by April 1 2022 (which indicates that the power generation is expected to be commenced without fail), the risk of expiry of the certification before the commencement of power generation shall be substantially eliminated."

Strictly speaking, it is necessary to enact an order or ordinance in order for the above-mentioned policy to obtain legal effect; however, it seems likely that the relevant order or ordinance will be issued reflecting the policy. Therefore, financers who are considering providing funds for large-scale photovoltaic power generation projects which have already obtained certification and have not yet started operations are expected to experience a certain degree of relief.

Disposal cost reserve system

The amendment stipulates that a certified operator supplying electricity from renewable energy power generation facilities in a certain category must reserve for a certain period a certain amount of money as expenses required for dismantling, removing, disposing, etc. of power generation facilities. According to the interim report presented in December 2019 by a working group established by METI, all solar power generation facilities with a capacity of 10kW or more that have obtained certification under the FIT system are expected to be subject to the disposal cost reserve system.

In principle, such reserves are to be directed externally, by payment to the Organization for Cross-regional Coordination of Transmission Operators (OCCTO). Since it is necessary to wait for the enactment of the relevant orders or ordinances to ascertain the specific content of the system, financers are recommended to pay close attention to the future policymaking process in relation to certain topics, such as the mechanism for the refund of the disposal cost reserve from OCCTO, which may bear a relation to the method of creation and foreclosure of the security interest over the right to claim the refund.

Nagashima Ohno & Tsunematsu
JP Tower, 2-7-2 Marunouchi, Chiyoda-ku,
Tokyo 100-7036, Japan
T: +81 3 6889 7000
F: +81 3 6889 8000
W: www.noandt.com

MACAU SAR

Riquito Advogados


João Nuno Riquito and Daniel de Senna Fernandes

Turning payment tides

Changes in Macau SAR's financial services sector – which have only been expedited by the pandemic and other recent events – are hiding in plain sight, from cashless payment methods to the rise of AI [artificial intelligence] advisors and chatbot support.

Some of these changes are also reflected in Macau SAR's economic market, as residents explore new and unfamiliar payment instruments. These changes have prompted the publication of new regulations aiming at further protecting the interests of residents (namely Macau SAR's Cybersecurity Law, e-Governance Law, and amendments to the Cybercrime Prevention Law, which have all been published in the past year). Naturally, such regulations have further enhanced the residents and public bodies' trust of online payment services.

In light of the coronavirus outbreak, brick-and-mortar operations have recently witnessed a decline, in line with the Monetary Authority of Macau's recommendation for residents to use online banking solutions over traditional over-the-counter services. Meanwhile, government bodies that interact with the public are gradually adopting electronic payment systems, thus encouraging residents to prefer digital over physical means of payments. Such solutions include cashless and mobile payments.

Based on the statistical results for the second quarter of 2020 regarding mobile payments, one could state that mobile payments in Macau SAR are growing in popularity. Such a conclusion becomes evident upon comparison of the registered number of transactions quarter-to-quarter and year-on-year (a 49% increase and 576% increase, respectively).

Taking into account the currently available mobile payments' applications and financial institutions that promote such means of payment in Macau SAR, it becomes evident that the financial system is evolving, albeit in a relatively conservative fashion, especially considering the incorporation of new banks in Macau SAR that adopt a more modern and technology-based approach in their modus operandi.

It is undeniable that mobile payments are becoming increasingly popular as we witness the development of a more modern, technology-inclined, digital economy. In fact, considering the returns generated and transferred to Macau SAR pursuant to the Guangdong-Macau Development Fund (RMB400 million ($57.8 million)) and the future launch of a joint cross-border financial management project between the Macau Monetary Authority, the Hong Kong Monetary Authority and the People's Bank of China, it seems that a cashless future is in the making, as any assessment of Macau's financial system must take into account its integration in the Greater Bay Area.

According to the Financial System Act of Macau, only licensed entities may provide payment services, notably the issuance and management of means of payments such as e-wallets. However it must be noted that, despite the lack of specific regulation regarding e-wallets, e-money and virtual banks, some entities are authorised to provide e-wallet functionality to their clients, thus allowing them to perform mobile payments with previously deposited funds.

The 30-year-old Financial System Act seems to translate, at first glance, into an outdated financial system; however, although rules for virtual banking or payment institution licences are not expressly spelled out, businesses interested in delivering products and services in these sectors may be authorised to conduct their operations, provided that certain requirements are met.

Against this backdrop, it seems that the developing framework has laid the groundwork for a digital economy with diversified services and products, allowing Macau SAR's economic market to become ever more competitive, without neglecting anti-money laundering and know-your customer regulations which, unsurprisingly, modern technology may assist in enforcing.

Riquito Advogados
Suite 1104 AIA Tower, 251A-301 Av.
Comercial de Macau, Macau SAR
T: +853 2838 9918
F: +853 2838 9919
E: jnr@riquito.com
W: www.riquito.com

PANAMA

Alfaro Ferrer & Ramirez

Juan Antonio Alfaro

New regime for limited liability entrepreneurship companies

As part of the Panamanian government's plan to reactivate the economy following the Covid-19 crisis, it is currently promoting a new regime known as limited liability entrepreneurship companies (LLEC).

At the core of the regime will be various incentives aimed at entrepreneurs to encourage them to formalize their businesses, by giving them access to benefits that should increase competitiveness and promote growth.

The new regime will become effective within one year of its publication in the Official Gazette. Although at the time of writing, the law that governs LLECs is still awaiting sanction by the executive body, this is the last stage in its approval process, and it is expected to be completed any day now.

This new corporate vehicle, although somewhat similar to Panamanian limited liability companies (LLC), will have a particular difference in the fact that LLECs can be created by a single individual, whereas LLCs must have at least two partners. The creation of LLECs primarily seeks to reduce red tape, to substantially lower the costs of creating and operating a company, and to give emerging enterprises the opportunity to enter the market.

The regime will apply to entrepreneurs who, without necessarily being innovative, generate local, national, or international value, or socioeconomic benefits. Only Panamanian micro companies (those with gross income or annual invoicing up to the sum of $150,000) and small companies (those with gross income or annual invoicing between $150,000.00 and $1,000,000) are eligible.

Among the most relevant benefits and incentives given to LLEC´s , we should

The regime will apply to entrepreneurs who, without necessarily being innovative, generate local, national, or international value

mention the following : (a) costs to incorporate LLECs are lower than those of other corporate vehicles available under local laws; (b) during its first four years, the LLEC´s will be exempted of the payment of the annual corporate tax and use of fiscal printer, (c) during its first two years, the LLEC´s will be exempted of income tax; (c) the regime creates a one-stop-shop administrative office through which LLECs will be able to digitally submit all the documentation required by the different administrative authorities; (d) bidders in public contracting that subcontract part of their work to an LLEC will have an additional score of five percent in those bids; (e) invoices issued by LLECs must be paid within 30-days, with a one percent monthly interest rate in case of late payments; and (f) a 50% reduction in import duties levied on equipment and raw materials needed for their business.

As expected, and due to the intended target of the new regime, it does have limitations. For example, LLECs will not be able to engage in commercial activities such as operating bars, discos, hotels, and the commercialization of alcohol or tobacco. Plus, one person cannot be part of more than one LLEC.

Apart from proving entrepreneurs with a legal framework aimed at incorporating their businesses in a faster and more efficient way, it is also expected that the new regimen will promote the creation of new jobs as well as strengthen the country´s economy behind the initiatives and creativity of the entrepreneur sector. .

Alfaro Ferrer & Ramirez
AFRA Building
Samuel Lewis and 54 Street
Panama City, PO Box 0816-01085
Republic of Panama
T: +507 263 9355
F: +507 263 7214
www.afra.com

PORTUGAL

Morais Leitão Galvão Teles Soares da Silva & Associados

Luís Branco and Un I Wong

The response to Covid-19 and its implications to the financial sector

In the context of the public health emergency and the classification of the coronavirus as a pandemic by the World Health Organization, countries have launched unprecedented measures to protect their economies against the impact of Covid-19.

In Portugal, the government has implemented a series of measures to support the financial sector through the exceptional framework approved by Decree-Law no. 10-J/2020 of March 26 (Decree-Law), with the aim of protecting the credits and cash flow of families, companies, private institutions of social solidarity and other entities of the social economy.

The Decree-Law was subsequently amended by Law no. 8/2020 of April 10, Decree Law no. 26/2020 of June 16 and Law no. 27-A/2020 of July 24, by means of which the deadline for adherence to moratorium measures and its application period were extended to September 30, 2020 and March 31, 2021 respectively.

Portugal is one of the countries that has implemented the longest moratoriums in Europe. Pursuant to the Decree-Law, the beneficiary individuals/entities may opt for the following moratorium measures in relation to credit arrangements, for the period in which these measures are in force (from March 27, 2020 to March 31, 2021):

- prohibition on total or partial revocation of agreed lines of credit and loans, in the amounts approved at the date of entry into force of the Decree-Law;
- extension for all loans in force on the date of entry into force of the Decree-Law where payments of capital are due at the end of the loan term. The extension of the loan term applies to all related elements of the loan including interest, and any guarantees, including those provided by way of insurance or securities; and
- suspension, with respect to partial repayments of loan capital or other loan instalments, of the payment of capital, rents and interest due in respect of loans reaching maturity during that period. Under this arrangement, contractual payment plan for the instalments of capital, rent, interest, commissions and other charges are automatically extended to ensure that there are no charges arising from the implementation of the extension (other than those that may arise from the variability of the interest rate). The extension also applies to all related arrangements, such as any security granted in relation to the loan.

In the context of the protection mechanisms of the credit exposure established for this exception period, extending the payment term shall not give rise to:

- contractual breach;
- activation of early repayment clauses;
- suspension of interest due during the extension period, which will be capitalised in the loan amount with reference to the time when they are due at the rate of the current contract; and
- ineffectiveness or termination of security granted by entities benefiting from the measures or by third parties, namely the effectiveness and validity of insurance, sureties and/or guarantees.

Data recently revealed by the Bank of Portugal show that requests for adherence to moratoria on credit made between the end of March 2020 and June 2020 covered 841,856 contracts, being 741,623 contracts to which the moratoria was applied, in which 44% were housing credit contracts and other mortgage loans, 26% were consumer credits, and 30% were credit contracts with enterprises, individual entrepreneurs and others.

Although the government's moratorium measures may mitigate the impact of the recession, it is a temporary solution. In case the Covid-19 pandemic continues, the economic and financial consequences could extend far beyond the expected end of the moratorium period which might result in deterioration in asset quality and profitability of Portuguese banks, as nonperforming loans may increase due to the breakdown of the economy and the decline in the capacity of households and businesses to repay the debts. It is, therefore, important that the moratorium measures are accompanied by other supportive measures to boost the Portuguese economy as well as to foster the liquidity of different economic players, so that the concerns surrounding bad loans may be alleviated.

Morais Leitão Galvão Teles Soares da Silva & Associados
Rua Castilho, 165
1070-050 Lisboa, Portugal
T: +351 213 817 400
F: +351 213 817 499
W: mlgts.pt

SLOVAK REPUBLIC

Futej & Partners


Daniel Futej and Daniel Grigel

Changes to the Commercial Code

Foreign nationals from non-EU countries will be able to set up as sole traders in Slovakia without obtaining a temporary stay permit

Upcoming changes to the Commercial Code in the Slovak Republic primarily concern the commercial register and simplification of the process for winding up and liquidating companies.

The new legislation requires the authenticated signature of a property owner on the consent to register a company at that address; if there is more than one owner, authentication is required for the signatures of the majority co-owners (calculated based on the percentage of ownership). Where a company establishes its registered office in a property it owns, no consents are necessary, and the commercial register staff will verify ownership through the land register database.

The amendment also standardises a single designation for branch offices of foreign and Slovak entities. The practice has been to use two different designations, however, currently the single designation 'branch' will apply to both situations. Registration of a branch in the commercial register will be voluntary.

However, registration will be useful for those companies that want their current or future branch managers to have the power of representation externally, i.e. toward third parties. The manager of a branch will only have the power of representation if their name is entered along with the branch into the commercial register. All existing branches that are registered in the commercial register will be required to confirm the accuracy of their registered data by September 30 2021; failure to do so will result in automatic deletion from the commercial register after that date.

Another welcome change is the absolute ban on registering any types of restrictions and limitations in the commercial register with respect to the acts of directors on behalf of a company. Under Slovak law, any restrictions or limitations on the director(s) of a legal entity to act externally on behalf of a company, such as provisions in the internal corporate documents that set an upper financial threshold or enumerate specific 'permitted' legal acts/transactions, have no legal effect outside the company.

At most, a violation of such internal limits placed on directors, the management board, and other corporate bodies could establish the right of the company to seek compensation from these persons. Nevertheless, commercial registers were often not unified in their practice, allowing some businesses to enter a variety of restrictions and limits on directors (e.g., concluding contracts only up to a certain value, etc.), and third parties often felt legal uncertainty when trading with the company in question. Companies will have one year to remove these types of restricting/limiting entries from the commercial register.

After October 1 2020, sole traders will no longer be registered in the commercial register. This registration has been a requirement for non-EU foreign sole traders, as their licence to do business in Slovakia only became effective upon the entry into the commercial register. This change should make it easier for these persons to conduct business in Slovakia, as in most cases they can begin their business activities immediately upon registration with the local trade licensing office – and unlike the commercial register, the trade licensing office does not require the issuance of a temporary stay permit in Slovakia.

This means that foreign nationals from non-EU countries will be able to set up as sole traders in Slovakia without obtaining a temporary stay permit, provided that they are in the country legally, for instance under a visa-free regime. The amendment requires all submissions to the commercial register to be made electronically; submissions in paper form will not be accepted.

Beginning October 1 2020, a person who is the subject of debt enforcement may not establish a limited liability company, transfer their ownership interest in a company to another member or a third party, or acquire an ownership interest in a company. Likewise, this person will be prohibited from becoming the managing director of a limited liability company. One important note is that the limitation concerning directorship will not apply to persons who are currently managing directors who may already be the subject of enforcement proceedings; these persons will not lose their positions as a result of the enforcement.

Futej & Partners
Radlinského 2
811 07 Bratislava
Slovak Republic
T: +421 2 5263 3161
F: +421 2 5263 3163
E: futej@futej.sk
W: www.futej.sk

One may legitimately wonder how the principles retained in that ruling will apply to other financial services

SWITZERLAND
Bär & Karrer

Frédéric Bétrisey and Tamara Grigoras

Retrocession fees harder to keep

Retrocession fees designate the commissions paid to a financial intermediary by a third party – a bank, for instance – as an incentive for selecting services or products sponsored by them. Switzerland regulates the admissibility of retrocession fees differently from other jurisdictions, and most requirements have been set by case law. This article outlines certain aspects of the legal Swiss regime surrounding retrocession fees in the light of a recent ruling of the Swiss Federal Supreme Court (SFC), which has put an end to some uncertainty while opening the way to new legal debates.

Wealth managers are bound to their clients by an agency contract, under which the agent agrees to render a service to the principal without guaranteeing a result. The wealth manager is bound by several obligations, including a duty to transfer to the client all items acquired within the performance of the service (see article 400(1) of the Swiss Code of Obligations (CO)). The restitution duty arises from the general duty of loyalty of agents to their principals, and also extends to the benefits indirectly obtained by the agent when rendering the service, including those originating from third parties, such as retrocession fees.

In a landmark decision of March 2006, the SFC ruled that retrocession fees were subject to the obligation to restitution. Furthermore, it confirmed that a client could waive the statutory right to obtain retrocessions, provided that he/she had been fully and truthfully informed thereon (informed waiver requirement). In another decision dated August 2011, the SFC ruled that a waiver could be granted *ex ante*, but that an informed waiver implied, in such case, that the agent disclose the order of magnitude of the expected retrocessions. According to the SFC, such order of magnitude *could* be expressed by way of a percentage of the client's assets managed by the wealth manager.

It was still unclear whether the order of magnitude of retrocession fees could be disclosed in a different manner. This year, however, the SFC eventually clarified this case law. In a ruling dated May 13 2020 (4A_355/2019), it considered insufficient a clause in a wealth management agreement defining the amount of possible retrocessions on the basis of the amount invested in funds and other financial products. In the SFC's view, such information does not enable the client to know the precise parameters on which the calculation is based, nor to compare the expected retrocessions with the fees agreed with the client for the wealth management service.

According to the SFC, the contract must indicate the amount of possible retrocessions within a certain range, as a percentage of the managed assets, so that the information disclosed enables the client to appreciate the composition of the agent's remuneration and identify the conflicts of interest which the asset manager may face and which may encourage him/her to enter into or multiply transactions not serving the client's interests. This ruling, therefore, sheds light on the type of information required from a wealth manager for a court to uphold a client's waiver of the statutory right to obtain retrocessions.

The May 2020 SFC ruling was rendered in application of Swiss contract law in connection with a wealth management matter. One may legitimately wonder how the principles retained in that ruling will apply to other financial services, such as execution-only relationships where the service, while being limited to the receipt and transmission of client orders, is subject to the same limitations on retrocession fees (as confirmed by article 26 of the Swiss Financial Services Act, a new law that came into force on January 1 2020).

To be in line with case law, the information on retrocession fees in respect of such service could state the amount/scale of the expected retrocessions on an individual transaction basis, allowing for a comparison with the corresponding transaction fee. No doubt that adjustments will be necessary inasmuch as the investment decisions for such service (similarly to pure advisory service) lie solely with the client. Nevertheless, it remains unclear how such case law will apply to all-in fee arrangements, which cover a broader range of services than those to which the retrocession fees relate.

Bär & Karrer
Brandschenkestrasse 90
CH-8002 Zurich, Switzerland
T: +41 58 261 50 00
F: +41 58 261 50 01
E: frederic.betrisey@baerkarrer.ch
W: www.baerkarrer.ch

Closing conditions

The lighter side of the past month in the world of financial law

Hardly working

It's been said before, it will be said again: the scale to which the workforce has been forced to bring the office home in 2020 has been unprecedented. Offices have been boarded up for months. Bedrooms, spare rooms, garages, kitchens, living rooms – all rooms – have been converted into makeshift offices.

One thing that has arguably improved is work-life balance. Although for some the office and the bedroom have merged into a single entity, removing commutes has freed up a lot of time for everyone. in New York City, the average commute time is 43 minutes; in Hong Kong SAR it's about 37 minutes. Meanwhile workers in London average a whopping 74 minutes each way. That is a lot of time – or it was. For many office workers, the average commute has been reduced to less than a minute.

The legal sector is no different. Just more than half of UK legal workers reported that their work-life balance has increased significantly. Around a quarter feel more compelled to work under remote conditions, and workplace bullying, too, has dropped significantly. As offices begin to open back up, 44% of those surveyed are dreading having to go back. The story is double-edged of course; that means 56% are not. Whichever camp you're in, once offices do open, it's not going to be the same as it once was.

It's all about trust

Before the pandemic, the global economy was strong and employment rates were high. People were cautiously optimistic: even some millennials began to think that maybe, just maybe, one day they might be able to think about buying a home of their own. Maybe.

But, despite the positivity, research from the 2020 Edelman Trust Barometer revealed that not one of the four societal institutions measured – government, business, NGOs or media – are trusted by the majority of the two million respondents.

According to the survey, which was conducted in late 2019, the cause of this paradox is to be found in people's fears about the future and the role they will play in it. The report suggest that this should act as "a wake-up call for our institutions to embrace a new way of effectively building trust: balancing competence with ethical behaviour".

This has not always been the case. Previous years have seen very different results and concerns for respondents. Trust at work was the main concern in 2019; in 2012 it was the fall of government; while 2009 saw a major fall in trust in business. It's fairly safe to say that respondents will have new concerns when the 2021 results are published. Given the rollercoaster this year has been so far, it would be brave to hazard a guess at what they might be.

The quarter in numbers

$177.52	the rise in price of a single Tesla stock in August
465 days	left of Libor at time of press
80 million	TikTok users in the USA
241	IPOs already completed in the second half of 2020
$14.9 billion	Total's financing commitment for Mozambique LNG project
17 years	trading history of Hong Kong SAR's Honia index
52%	proportion of UK lawyers who say working from home has improved their work-life balance
29 million	worldwide Covid-19 cases at time of press

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BenchMark Litigation &
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COUNTRY CORRESPONDENTS

BRAZIL

Tel: +55 11 3089 6500
www.cesconbarrieu.com.br

CENTRAL AMERICA

Tel: +502 2339 3139
www.consortiumlegal.com

CHINA

Tel. +86 10 8519 130
www.junhe.com

COLOMBIA

Tel. +571 346 20 11
www.bu.com

CYPRUS

Tel: +357 25 110110
www.neo.law

DOMINICAN REPUBLIC

Tel: +1 809 541 5200
www.phlaw.com

JAPAN

Tel: +81 3 6889 7000
www.noandt.com

MACAU SAR

Tel: +853 2838 9918
www.riquito.com

MYANMAR

Tel: +959 73040763
mm.rajahtannasia.com

NIGERIA

Tel: + 234 8023156979
www.faa-law.com

PANAMA

Tel: +507 263 9355
www.afra.com

THE PHILIPPINES

Tel: +63 2 982 3500
www.syciplaw.com

SLOVAK REPUBLIC

Tel: +421/2/5263 3161
www.futej.sk / www.yoonyang.com

SOUTH KOREA

Tel: +82 02 772 2700
www.hmplaw.com

SWITZERLAND

Tel: +41 58 261 50 00
www.baerkarrer.ch

THAILAND

Tel: +662 838 1750
www.kap.co.th

VIETNAM

Tel: +84 4 3946 0870
www.jurists.co.jp

IFLR INTERNATIONAL BRIEFINGS
MAGAZINE | COUNTRY CORRESPONDENT

ASIA PACIFIC Business developer
Anicette Indiana
anicette.indiana@euromoneyasia.com
+852 2842 6966

EMEA Business developer
Liam Sharkey
lsharkey@iflr.com
+44 207 779 8384

AMERICAS Business developer
Allie Strick
alexandra.strick@euromoneyny.com
+1 212 224 3494

Copy manager
Ahmed Hadi
ahmed.hadi@iflr.com
+44 (0) 20 7779 89