**INSOL INTERNATIONAL**

**GLOBAL INSOLVENCY PRACTICE COURSE 2021/2022**

**CASE STUDY II**

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**A. Proposed Strategy**

My advice has been sought by Benedict Maximov on how to facilitate a deal with KuasaNas (**KN**), in which it will acquire a majority (51%) stake in the F1 racing team, to be relocated to Malaysia, in return for the provision of annual funding of USD 200m. On the basis of the facts presented, it is assumed that this advice is given as at 1 January 2019.

A pre-condition to the deal going ahead is that the insolvency issues affecting the companies in the Efwon group are dealt with promptly, so that the proposed investment by KN passes a Malaysian government review. There are other operational issues which will also need to be addressed in relation to the relocation of the team to Malaysia, including the securing of the Sepang GP racetrack for practice and training, and the engagement of new drivers who are qualified to obtain the requisite Super Licences.

The cause of the problem facing Mr Maximov and the Efwon group is that key assets in Romania have been frozen, particularly the future broadcasting revenue, and winding up proceedings have been filed by the current Romanian drivers, seeking substantial compensation for injuries sustained in the 2018 competition. The domino effect of the freezing orders will be to cause defaults in payments to the upstream financiers in the US and Monaco, which will place Mr Maximov’s assets at risk of enforcement by the US lenders, who otherwise have no security of value to recoup their loans.

Value destruction for Mr Maximov and the lenders will be minimised by a reorganisation plan which results in the injection of new funds from KN, and the continuation of the business of F1 racing by a new Malaysian based team, in which KN holds a 51% stake. The reorganisation is complicated by the global structure of the group’s operations, the current court actions in Romania, and also the need to transfer the FIA licence to the proposed team in Malaysia.

One option would be a direct share sale from Mr Maximov to KN of a 51% stake in the group as currently structured, together with legal action in Romania to remove the freezing order and fight the winding up application there. However, this will leave the group at risk of financial collapse, and will not ensure that the FIA licence can be transferred to a Malaysian team, which will not satisfy the preconditions for the KN deal.

The alternative strategy, and the one recommended in this Advice, is a reorganisation of the Efwon group in which a new Malaysian company is established, which will hold the FIA licence and operate the team. Ownership of that company will be split 51% as to KN, and 49% as to Mr Maximov and potentially the current lenders to the Efwon group under a debt-for-equity swap as part of the reorganisation. Otherwise, the loans from the current lenders will be novated wholly or partially to the new Malaysian company, with fresh security being granted by it directly over its revenues. The existing Efwon group companies can then be placed into liquidation, and the securities granted by Mr Maximov released as part of the reorganisation and/or under a debt-for-equity swap.

For the reasons discussed in detail in this Advice, each of these outcomes can be achieved by use of the following insolvency mechanisms (in 2019):

a) the opening of reorganisation proceedings in the US under Chapter 11 of the Bankruptcy Code (11 USC) (**Chapter 11**), which is available both to individual and corporate debtors;

(b) the appointment of a Voluntary Administrator (**VA**) in England under the *Insolvency Act* 1986 (**IA**) and the use of a Scheme of Arrangement (**Scheme**) under Part 26 of the *Companies* Act 2006 (**CA**), noting that in 2022, another procedure is available by means of a Restructuring Plan under CA Part 26A;

(c) reliance upon the European Union Insolvency Regulation (**EUIR**) and the UNCITRAL Model Law on Cross-Border Insolvency (**MLCBI**) to bring ‘secondary’ proceedings in Romania by way of assistance to the ‘main’ proceedings in England and the US;

(d) reliance, potentially, upon the European Judgments Regulation (Brussels Recast) (**EJR**) for enforcement of an English Scheme within Europe.

The impact of Brexit in 2020 is that English proceedings no longer obtain any benefits under the EUIR or the EJR. In that case, the strategy proposed would be limited to the opening of Chapter 11 proceedings for all entities, together with reliance on the MLCBI in relation to assistance in Romania. Put another way, the effect of Brexit demonstrates that it is the benefits of the EUIR and EJR that provide the rationale for conducting proceedings in both England and the US, even though parallel proceedings may introduce some complexity into the reorganisation process.

In framing both the strategy and this Advice, there is a difficult question to be resolved about Efwon Romania, and where it should be the subject of reorganisation proceedings – in the US under Chapter 11 or in England by a Scheme. The competing considerations may be summarised as follows:

(a) The advantage of Chapter 11 in the US, is that the US Court has the power to order a transfer of the FIA licence from Efwon Romania to the new Malaysian subsidiary, even if the licence is subject to a non-assignment clause, and to override any automatic termination provisions or *ipso facto* clauses (11 USC 365(e), (f)). As the ability to operate the team in Malaysia is a precondition to the KN deal, it favours the reorganisation of Efwon Romania in the Chapter 11 proceedings.

(b) The advantage of English proceedings is the ability of the VA to use the EUIR to recover the broadcast moneys, by means of secondary proceedings in Romania, so that those moneys can be used to service or repay the debts owed to the lenders as part of the English Scheme.

In the analysis that follows, I recommend including Efwon Romania in the Chapter 11 proceedings to obtain an immediate stay on proceedings in Romania (11 USC §362) and prevent any termination of the FIA licence. Thereafter, the relationship between the proceedings in the US and England in relation to Efwon Romania can be reviewed in light of further facts as they become known (see Section G below), which will allow the overall strategy to be fine-tuned, in order to achieve the desired outcome of consummating the KN deal.

**B. Necessity for Insolvency Proceedings**

A threshold issue in this case is whether insolvency proceedings are needed to effect the reorganisation of the Efwon group, to facilitate the future involvement of KN. This question has been partially answered in Section A, in relation to a possible share sale strategy by Mr Maximov directly to KN within the existing group structure, which was rejected due to the risk of corporate collapse as a consequence of the freezing orders in Romania.

In any event, there is a prima facie case for the opening insolvency proceedings to effectuate a reorganisation, and facilitate the investment of KN. There are two main sources of ongoing revenue for the group – broadcast and other revenue paid by FIA to Efwon Romania, and sponsorship revenue currently provided by Kretek to Efwon Hong Kong. If the broadcast revenue is not paid to the upstream companies (Efwon Trading and Efwon Investments), the respective lenders in Monaco and the US will likely call defaults and seek to wind up those companies. If this imperils the ongoing operations of the group, it may have the further consequence of a loss of the remaining Kretek sponsorship, which will create further liquidity and insolvency related issues for the group.

Although a reorganisation plan to facilitate the entry of KN as a 51% shareholder could be potentially be achieved by an informal reorganisation being agreed by each of the stakeholders - Mr Maximov, the lenders, the drivers and the FIA - without the opening of insolvency proceedings, this would be a high risk option.

Agreement between all the stakeholders, including as to a standstill to enable a plan to be formulated, would be a less expensive option than insolvency proceedings, but only if the stakeholders were able to agree and cooperate. Although informal reorganisations are said to operate in the ‘shadow of the law’, the divergent interests of these stakeholder groups create a significant risk that any one of them might use liquidation proceedings to seek to improve their negotiating position in relation to any reorganisation. Given the aggressive legal actions by the drivers in Romania, the possibility of an ‘informal reorganisation’ seems highly unlikely.

The better approach will be to seek to reach agreement on a reorganisation plan within the framework of insolvency proceedings, so that the reorganisation is not held hostage to one or more dissenters, at the risk of not implementing a fair and reasonable plan. If a high degree of consensus emerges during the process, this will result in a faster and cheaper outcome. Again, the drivers’ actions in Romania, and the possibility of national differences emerging between the Romania team’s interests and those of KN in Malaysia in relation to relocation of the team, suggests that disagreements will surface relatively quickly.

There are also a number of specific insolvency tools and procedures that are available to assist and facilitate the proposed reorganisation and entry of KN. Relevantly to KN, these include (i) provisions for a moratorium on enforcement action by creditors, (ii) prohibitions on contractual termination of the FIA licence by FIA, (iii) the ability to assign the FIA licence from Efwon Romania to a new Malaysian company, (iv) the ability to establish a new corporate structure for the group, and (v) the ability to compromise all existing claims by stakeholders by the potential use of cram down mechanisms to deal with dissenters. These matters are explained in further detail in Section E below.

Another feature of insolvency proceedings, which may be relevant to timing, is the importance of the first mover benefit in opening insolvency proceedings in Europe, because of the recognition rules that apply under the EUIR. At the present time, the drivers have only filed winding up proceedings in Romania. For the purposes of EUIR Art.19, the recognition rules operate to give primacy to the first judgment that opens insolvency proceedings. In Romania this will not occur until there is an appointment of an insolvency judge and a certified insolvency practitioner (Wood 2019). It may therefore be important to open insolvency proceedings in England, with the appointment of a VA under IA Sch.B1 para 31 before any Romanian appointments are made, to assert primacy of the English proceedings as the ‘main proceedings’ under Arts.3 and 19 of the EUIR in respect of Efwon Romania, so that the proceedings in Romania become ‘secondary proceedings’ under Art. 34. This analysis is complex, because it also raises issues about any Chapter 11 stay in relation to Efwon Romania. These issues are discussed in further detail in Section I below. However, for present purposes, it is sufficient to point out the risk of delaying the opening of insolvency proceedings in the hope that an informal reorganisation might be achieved without insolvency proceedings.

**C. Venue for the Insolvency Proceedings**

The strategy outlined in Section A recommended the opening of insolvency proceedings in both the US and England for the purpose of undertaking the restructure of the Efwon group to facilitate the entry of KN. The reasons for this recommendation are set out in this Section.

*Reorganisation Laws*

The first issue to be considered is the availability of laws that will permit the reorganisation of the Efwon group. There are three main options on the facts presented, with their advantages and disadvantages discussed in Section E below:

(a) ***United States*** – Chapter 11 provides a well-known and powerful tool for reorganisation of global businesses, as well as providing protection for Mr Maximov as a guarantor. Proceedings under Chapter 11 can be filed by a ‘debtor’ (11 USC §1121). A ‘debtor’ includes a person ‘who resides in or has a domicile, a place of business or ‘property in the US’ (§109). This definition has a very broad reach, and has been held to include a foreigner who placed $194 in an attorney’s trust account for the purpose of commencing the proceedings: *In re McTague*, 198 B.R. 428 (Bank. WDNY 1996).

Mr Maximov must join in the Chapter 11 proceedings personally to protect his assets from enforcement action by the US lenders, as the filing of a petition by Efwon Investments and the approval of a Plan for that company under Chapter 11, will not automatically protect him as a guarantor (Wood, 2019, p.648): *In re Larry Ralph Gentry*, No 13-1441 (10th Cir, 2015).

**(b) *England*** – the primary reorganisation tool in 2019 was the Scheme of Arrangement under CA Part 26, which is also a well-known and powerful tool for global reorganisations. Schemes are not limited to insolvency or pre-insolvency cases, and may be proposed by a VA (CA s.896(1)), who may be appointed by Efwon Trading or its directors (IA Sch.B1, para 22). The other main reorganisation options available to a VA are (i) a ‘pre-pack’ sale; or (ii) a company voluntary arrangement (**CVA**)(Van Zweiten 2018, 11-01). The Scheme is the most flexible of these options for a global business to give effect to the strategy in Section A, and also has the benefit of being enforceable overseas as a court order, unlike a CVA (Wood 2019). A ‘pre-pack’ sale will not be appropriate, as it will not remove the effect of the Romanian freezing orders over the FIA licence and assets that need to be transferred to the new Malaysian company.

Like Chapter 11, any reorganisation of the US lenders’ debts under an English Scheme will not release the guarantees and securities granted by Mr Maximov (Van Zweiten 2018, 12-26). Nor can Mr Maximov be a party to the English Scheme as an individual. These are further reasons why he should bring Chapter 11 proceedings to protect his personal position.

In 2020, a new reorganisation tool, the Restructuring Plan, was introduced into CA Part 26A specifically for pre-insolvency and insolvency reorganisations, which would not require the appointment of a VA in this case, principally because Part 26A makes provision for a moratorium upon the filing an application under Part 26A (CA s.901H) .

**(c) Romania –** as at 2019, in Romania the reorganisation possibilities were limited. One possibility was a ‘judicial reorganisation’ that takes place within formal insolvency proceedings, and is conducted by an insolvency judge and a certified insolvency practitioner. A second possibility, known as the ‘ad hoc mandate’ involves a court appointed attorney, with limited powers, who enters into confidential discussions with creditors to try to reach agreement on a voluntary rescheduling plan. The third possibility is a ‘preventative concordat’, which is conducted by a court-appointed ‘conciliator’ who seeks to develop a recovery plan for reorganising the debts of the company over a 24 month period, that includes a cram down provision if at least 75% of creditors by value agree (Wood, 2019). None of these options offer the reorganisation flexibility of Chapter 11 or an English Scheme or Restructuring Plan for a global business, and one commentator has stated that ‘preventative concordats’ are used in only about 2-3% of cases in Romania (CMS 2022) For these reasons, Romania is not proposed as the jurisdiction for opening reorganisation proceedings.

The stated facts indicate that in 2020 Romania proposed to implement the European Directive 2019/1023 (**EU Directive**) to institute a preventative reorganisation framework. This directive has already been implemented or proposed in various European countries, including The Netherlands, Spain, Italy and France. As a Directive only, there is no standard model for how the Directive is to be implemented, although it is intended to have many of the features found in Chapter 11. Further, even if it replicated Chapter 11 entirely, it would be unchartered territory for a new law in Romania to allow its Courts to make orders with extra-territorial effect affecting property in the US owned by a US citizen. Applying a ‘universalist’ mind-set, this may not present a major problem; however, the practical risk is that any US enforcement court would take a ‘territorial’ approach and refuse to recognise any such orders made in Romania. For this additional reason, even if it applied the EU Directive, Romania would not be recommended as the reorganisation venue.

Different considerations apply in relation to ‘secondary’ or assistance proceedings which are commenced under the EUIR or MLCBI in support of the ‘main’ reorganisation proceedings. These issues are addressed further in Sections H and I below.

*Centre of Main Interests (COMI)*

The second issue to be considered in respect of a global business is the identification of the Centre of Main Interests (**COMI**) of the companies and group under consideration. The principle that underpins the EUIR and the MLCBI is that the ‘main’ insolvency proceedings should be opened at the COMI, to promote universal scope in the conduct of proceedings and the avoidance of ‘forum shopping’: see EUIR Recitals (23), (29).

However, an important practical difference between the EUIR and the MLCBI is that the EUIR has prescriptive rules for determination of the COMI, whereas the MLCBI does not. Under Art. 3(1) of the EUIR, the COMI is the place where the debtor company conducted its administration on a regular basis, being a place that was objectively ascertainable by third parties. There is a rebuttable presumption in relation to the place of the registered office. Goode states that ECJ case-law has placed significant weight on the ability of third parties to ascertain the place of administration, rather than formalities such as a company’s registered office(Van Zweiten 2018, 15-44).

The UNCITRAL Guide to Enactment of the MLCBI (2014) seeks to assimilate the position under the MLCBI to that of the EUIR in relation to the ascertainment of the COMI, having regard to the central role played by the Virgos-Schmit Report in the formulation of Art. 3 and the recitals to the EUIR. However, in the Guide’s notes on Art.16 of the MLCBI, UNCITRAL makes it clear that the responsibility for determining COMI is the responsibility of the court receiving a request for assistance, which introduces a greater element of uncertainty than exists under the EUIR.

In relation to each of the individual companies, the following preliminary conclusions can be stated:

(a) **Efwon Investments** – it is likely to have its COMI in the US for the purposes of the MLCBI. That is where it is incorporated, and where it appears to have borrowed $250m from the US lenders. It is reasonable to assume that the US is the place where its administration occurs.

(b) **Efwon Trading** – as this company is incorporated in England, there is a rebuttable presumption under the EUIR that England is its COMI. In addition, Efwon Trading has subsidiaries in Romania and Hong Kong, which together form the main operations of the group, through team racing and fund-raising. It is, therefore, reasonable to assume that the COMI of Efwon Trading and its subsidiaries is England, being the place of administration of the operating part of the group.

(c) **Efwon Romania** – as this company is incorporated in Romania, there is a rebuttable presumption under the EUIR that its COMI is in Romania. However, there is a good argument, to be investigated further, to the effect that England is the COMI of Efwon Romania, as the place where the central administration of the affairs of Efwon Romania takes place, which is also ascertainably by third parties as such (EUIR Art 3(1)). A finding to this effect will have important ramifications in relation to the relationship between the English courts and the Romanian courts under the EUIR, in determining which proceeding is the ‘main’ proceeding and which is the ‘secondary’ proceeding in relation to Efwon Romania. This is further addressed in Section I below.

A group of companies may have one or more COMIs, depending on how the group is structured and administered. Here, the relationship between Efwon Investments and Efwon Trading is unclear, as to whether Investments is the holding company of Trading, or whether they are merely sister companies owned by the same shareholder, Mr Maximov. This is a matter for further investigation. However, on the facts presented, Efwon Investments appears to have had only a limited role in raising funds, whereas Efwon Trading appears to have been the operational hub of the group, for the reasons set out above.

*Jurisdictional Requirements*

Separately from an analysis of the COMI, in order to open proceedings, any jurisdictional requirements of the *lex concursus* (place of the proceedings) must be satisfied. Specifically:

(a) ***In the US***, the Court has jurisdiction over individuals and corporate “debtors”, as noted above. Consistently with the definition of ‘debtor’ in §109(a), each of Mr Maximov and Efwon Investments will be a ‘debtor’ entitled to file a Chapter 11 petition. The non-US based companies in the Efwon group can take advantage of the low threshold requirement to file Chapter 11 proceedings by placing money in a US attorney’s trust account for the purpose of bringing those proceedings, consistently with the judgment in *Re McTague*.

(b) ***In England***, there are two matters to consider:

(1) ***VA.*** As an English company, Efwon Trading or its directors are entitled to appoint a VA under IA Sch.B1 para 22. By doing so, the VA will take control of the affairs and assets of Efwon Trading, including its shareholding in Efwon Romania and Efwon Hong Kong.

(2) ***Scheme or Restructuring Plan***. The English court has jurisdiction over any Scheme (or in 2022 Restructuring Plan) proposed by Efwon Trading as an English company. In respect of foreign companies, the English court will accept jurisdiction if a ‘sufficient connection exists between England and the company or its obligations. This is an evaluative test, depending on the facts of each case (see eg. *In the matter of Rodenstock GmbH* [2011] EWHC 1104 (Ch)). The subsidiaries of Efwon Trading will meet this test, as subsidiaries of an English company. If necessary, this could be satisfied for Efwon Investments by ensuring that the loan agreement between Efwon Trading and Efwon Investments was governed by English law, even if that occurs by amendment to the loan agreement immediately prior to the Scheme (Pilkington et al 2021).

Thus, the jurisdiction requirements can be satisfied for both the US and England as reorganisation venues for the Efwon group. The only material point of difference between the two is that only the US also permits Mr Maximov, as an individual, to file a petition as part of the reorganisation process. In England, the processes are reserved for companies.

**D. Potential Impediments to Proceedings**

The US and England both operate on a common law system, where the role of the courts is to determine disputes raised by the parties to the proceedings, rather than initiate its own investigations or enquiries. Thus, if the party opening the proceedings can establish a prima facie basis for jurisdiction, the court will not enquire further as to the validity of that claim.

Thus, the potential for an impediment to proceedings taking place will involve a stakeholder analysis, to identify what, if any, objection a stakeholder might take to jurisdiction in either the US or England, and on what basis. The most likely challengers will generally be parties that may suffer from a substantive or procedural disadvantage from the proposed proceedings in the forum chosen by the debtor.

In the present case, it would be prudent to anticipate the following challenges:

 (a) ***Romanian drivers*** – any reorganisation undertaken in the US or England is likely to involve some diminution of their rights, compared to a winding up in Romania, where they will have a primary claim on the broadcasting proceeds. For this reason, they are likely to oppose proceedings being opened in both jurisdictions, and also oppose any ‘secondary’ proceedings brought in Romania by way of assistance to the English or US courts under the EUIR or MLCBI.

(b)  ***FIA*** – the FIA may seek to challenge the US proceedings to avoid the effect of §365, which will limit FIA’s control over the Romanian licence, and its proposed transfer to the new Malaysian company. If, after commencing the Chapter 11 proceedings on behalf of Efwon Romania, the FIA agrees to the transfer of the licence to the new Malaysian company, it may be better to pursue the reorganisation of Efwon Romania in an English Scheme to take advantage of the EUIR and EJR if needed.

(c) ***Lenders*** – the main concern of both the US lenders and the Monaco lender will be the potential for loss of rights by reason of a ‘cross-class cram down’ in Chapter 11 proceedings (§1141), discussed in Section E below. It is not possible to tell, at this stage, whether that possibility will emerge from the negotiations about the reorganisation plan either in the US or England.

Even where a stakeholder is considering a challenge to jurisdiction, the grounds for challenge in both the US and England are limited:

(a) ***In the US***, the primary basis for a challenge to jurisdiction is the abstention power under 11 USC §305. This power is only available if the Court is persuaded that ‘the interests of creditors and the debtor would be better served’ by dismissal (or suspension) of the proceedings. The test usually applied on a challenge under §305 is the ‘totality of the circumstances’, which includes a series of factors such as whether there is an alternative forum to protect the interests of both parties, and whether US proceedings are necessary to reach a just and equitable solution: *In re Northside Mainland Servs., Inc.,* 537 B.R. 192, 203 (Bankr. D. Del. 2015).

It is difficult to see any potential challenge succeeding in relation to any Chapter 11 proceedings concerning the Efwon Group. Given the desirability of the proposed reorganisation, and the need for the powers provided by the US Bankruptcy Code to facilitate the reorganisation, this is not a case where the aims of the reorganisation could be achieved in another court, and certainly not in Romania. If the reorganisation does not proceed, the ultimate risk of insolvency is borne by Mr Maximov, a US citizen. For this reason, any challenge to the US Court’s jurisdiction is likely to fail.

(b) ***In England***, there are two main opportunities for challenging jurisdiction in respect of a Scheme. The first occurs at the first hearing, where jurisdiction may be challenged on the basis that no ‘sufficient connection’ exists between the foreign companies in the group and England. For the reasons already given, that challenge will likely fail. The second occasion arises as the second, or confirmation, hearing of the Scheme. It is the practice of the English court to consider whether the Scheme will be enforceable in all jurisdictions to which it applies, before approving the Scheme: *In the matter of Magyar Telecom BV* [2013] EWHC 3800 (Ch). Here, the main potential jurisdiction of concern would be Romania, and any concern would be overcome by the EJR and the fact that one of the scheme companies is a UK domiciled company.

The other possibility that should not be dismissed entirely is that one of the stakeholders might seek an anti-suit injunction to restrain the filing of proceedings. This is a procedure rarely used, and Ho (2003) argues that it should not be used to undermine international efforts at coordinating cross-border insolvencies, where they are otherwise appropriate.

For these reasons, there is no material impediment to reorganisation proceedings being opened in the US and England, to give effect to the strategy identified in Section A above.

**E. Advantages and Disadvantages of the Proposed Proceedings**

There are some important differences both in procedure and substantive powers available in the US and England in respect of the reorganisation process, although the outcome is the same – namely, approval of a reorganisation plan. In this section I highlight some of the most important differences, to identify the advantages and disadvantages of commencing proceedings in each of the US and England, which are ranked in order of importance to fulfil the strategy in Section A.

*Moratorium and Debtor in Possession*

The first and most fundamental factor in this case is the need for a moratorium, given the impending urgency of a reorganisation in light of the Romanian freezing order. The purpose of the moratorium is to prevent enforcement action that will lead to a potential loss of control of the group, and the likelihood that there will be no reorganisation plan developed as the group is broken up, to the detriment of the stakeholders.

A primary advantage of Chapter 11 is that it provides a moratorium on enforcement action in respect of the debtors, including Mr Maximov as a guarantor, who file Chapter 11 proceedings, whilst leaving each of those debtors in control of their assets and business (11 USC §362, 1108). In addition, the ‘debtor’ has an exclusive 120 day period in which to file its Plan, which may be extended out to 18 months (§1121).

Here, a moratorium is required in relation to each of Mr Maximov and Efwon Investments to prevent any enforcement action by the US lenders, and by Efwon Romania to prevent any further enforcement action being taken in Romania, particularly in relation to the FIA licence. Commencing Chapter 11 proceedings on behalf of all three ‘debtors’ will be within jurisdiction as stated in Section C above, and by doing so a moratorium will apply immediately.

A moratorium is also required in relation to Efwon Trading to protect it against actions by the Monaco lender. While it could also open proceedings under Chapter 11, it will be better, strategically for Efwon Trading to open proceedings in England, to take advantage of the EUIR. A moratorium is not available for a Scheme. Thus, in 2019, the appointment of a VA has been recommended, as a moratorium will apply upon the appointment of a VA by the company or its directors: IA Sch.B1 paras 42-44.

By contrast, in 2022, a moratorium is available on the opening proceedings for a Restructuring Plan under CA s.901H, and so a VA would not be required. The new CA Part 26A is still limited to companies, and so Mr Maximov would still require the protection of Chapter 11 proceedings to obtain a moratorium in respect of his personal position.

*Contractual Issues - Ipso Facto Clauses and Assignment*

Having obtained a moratorium on enforcement, the most critical commercial issue for the KN deal is the transfer of the FIA licence to a new Malaysian company. As the FIA licence is a contractual right of Efwon Romania, there are two important issues to consider in relation to the restructuring Plan:

(a) ***First***, it is critical that the FIA licence is not terminated upon the opening of insolvency proceedings, by reason of an *ipso facto* or other clause. As previously mentioned, a feature of the Chapter 11 proceedings is that such clauses are void (§365(e)). As at 2019, there was no equivalent provision in relation to an English VA, or Scheme, which strongly suggests that Efwon Romania needs to be brought within the Chapter 11 proceedings in the US. This position was changed in 2020 by the introduction of IA s.233B by the *Corporate Insolvency and Governance Act* 2020.

(b) ***Second***, the preferred outcome for KN is that the new Malaysian company hold the FIA licence, rather than the licence remaining in the existing Romanian company. As noted above, Chapter 11 permits this to occur under an approved Plan, notwithstanding any non-assignment clause in the FIA licence (§365(f)). Whilst an assignment can be ordered as part of an English Scheme, there is no express power in the English legislation to override non-assignment clauses, potentially setting up a conflict at the enforcement stage if the FIA challenges the English court’s ruling in a non-English enforcement proceeding. The risk of such an outcome means that any Scheme could fail and KN’s pre-condition would not be satisfied, and is therefore not recommended. It provides a further reason why Efwon Romania should be restructured under Chapter 11, unless of course FIA advises that it will approve a voluntary transfer of the licence to the new Malaysian company without a court order.

*Classes and Cross-Class Cramdown*

The third issue of significance in considering each of the potential reorganisation jurisdictions is how the Courts will address dissenting stakeholders. Here, there is an important difference between the Chapter 11 and English procedures in relation to ‘cram downs’. In particular, Chapter 11 allows for ‘cross-class cram downs’ under 11 USC 1141. On the other hand, the English Scheme only allows for cram downs within a class, as all classes must approve a Scheme before it can be presented to the Court for sanction (CA s.899). By contrast, in 2022, a ‘cross-class cram down’ is permissible in England in relation to Part 26A Restructuring Plans, by treating all stakeholders in a single class (CA s.901G).

This difference, whilst important, should not be overstated, due to the different way classes are formed in the US and England. In England, classes tend to be constituted on the widest possible basis to minimise the risk that a Scheme will fail because one or more classes fail to reach the requisite threshold. On the other hand, in the US, classes tend to be narrowly constituted, as the ‘cross-class cram down mechanism’ needs only one impaired class to vote in favour of the Plan (§1129), and smaller classes provide a greater opportunity to tailor the plan to achieve that classes’ acceptance of the Plan. Chapter 11 seeks to minimise the risk of abuse of the ‘cross-class cram down’ rule by imposing additional requirements under §1129(b) that the plan be ‘fair and equitable’ and not ‘discriminate unfairly’ against dissenting classes.

In this case, in England, the proponents of any Scheme would seek to formulate two classes – creditors and shareholders. The test for class formation in England is concerned to ensure that there is no material difference between the rights (as opposed to the interests) of the class members, in terms of their old rights and their new rights under the Scheme: *Re Apcoa Parking Holdings GmbH* [2014] EWHC 3849 (Ch).

In the present case, all of the creditors at the level of Efwon Trading are unsecured, including the US lenders, the Monaco lender and the Romanian drivers. To that extent, it may be argued that they could all be classified in the same class. However, there are differences between three groups in terms of the character of their existing rights and as to their future rights, which may require more than one class of creditors, which in turn will raise the potential problem that there is no cross-class cram down under a Scheme in England.

*Debtor in Possession Financing*

The facts in the present case do not suggest a need for financing during the reorganisation process, as sponsorship moneys are still apparently being provided by Kretek, and at some point the broadcasting moneys will be received.

However, it may be noted that a mechanism is available in Chapter 11 proceedings for the ‘debtor’ to seek debtor-in-possession financing, which is then accorded a super-priority in relation to repayment by the Court (§364). A limited priority may be achieved by a VA in England, who chooses to borrow money for the purposes of the administration. That priority ranks below a fixed charge but is higher than a floating charge, and is only available upon cessation of the office: IA Sch. B1 para 99. If new or temporary funding is likely to be required during the reorganisation process, Chapter 11 offers a better alternative than England.

*Other Procedural Features*

It is not necessary for the purpose of this Advice to examine all the other features of the procedures under Chapter 11 and an English Scheme or Restructuring Plan. Each jurisdiction has disclosure obligations, meeting requirements, and a Court hearing to consider the Plan. Although the language of the different statutory provisions vary, the essential test in both jurisdictions involves a consideration of the fairness of the Plan, in the sense that the Court’s powers of approval are not being used to unfairly discriminate or oppress particular stakeholders. One difference that may be significant in some cases is the broader availability of discovery in support of the US process than in England. However, none of these factors individually or collectively favour or disqualify the US or England as the appropriate reorganisation venue in this case. As discussions begin with each of the stakeholders in relation to the formulation of a Plan, this may change in relation to perceptions about costs, timeframes or the importance of some of the factors referred to earlier.

*Effect of the Plan*

In both the US and England, the effect of the Court’s sanction or approval of the Plan or Scheme is to create new obligations in accordance with the Plan and to resolve and discharge all prior claims against the individual or company concerned: (11 USC §1141 in the US; CA s.899(3) in England). This will resolve an important pre-condition stated by KN in relation to its proposed investment in the group, as it will remove all pre-existing insolvency risks associated with the group companies that form part of the Plan or Scheme.

As mentioned earlier, one advantage of the English Scheme (as at 2019) is that it is enforceable within Europe as a judgment of the English court under the EJR, subject to certain pre-conditions being satisfied in relation to the jurisdiction of the English court (Allen & Ovary 2015). As the Scheme in this case would include Efwon Trading, an English company, the Scheme should be enforceable under the EJR.

**F. DECISIVE FACTORS**

The analysis of advantages and disadvantages in Section E leads to three possibilities in relation to the opening of reorganisation proceedings: (i) Chapter 11 only, (ii) England only, or (iii) parallel proceedings in the US and England. Each of these possibilities is considered below. The possibility of reorganisation proceedings in Romania can be eliminated in 2019 because of the limited nature of the options available, as previously considered in Section C.

*US Chapter 11*

There are four decisive factors in favour of Chapter 11 proceedings. As discussed in Section E above, these are: (i) Chapter 11 applies to individual ‘debtors’, in this case Mr Maximov, as well as corporate ‘debtors’; (ii) the availability of a moratorium whilst leaving the debtor in control of the reorganisation process; (iii) the powers available to the US Court to preserve and transfer the FIA licence to the new Malaysian company; and (iv) the potential availability of the ‘cross-class cram down’, if needed.

At a minimum, therefore, Chapter 11 proceedings should be opened by Mr Maximov and Efwon Investments to stay any enforcement actions by the US banks whilst the reorganisation plan is developed and proposed. These proceedings should also be opened in relation to Efwon Romania to stay any further enforcement action in Romania, and to preserve the FIA licence from any termination action pending the reorganisation.

What is not presently clear about the proposed Chapter 11 proceedings is whether the other group members should be party to these proceedings, including Efwon Trading and Efwon Hong Kong. As at 2019, the disadvantage of joining Efwon Trading is that the reorganisation plans will lose any benefits that could arise under the EUIR and EJR. However, post-Brexit, there is no reason to open proceedings in England, and all companies should file for Chapter 11 relief, and be dealt with together.

In relation to Efwon Hong Kong, there are insufficient facts to know whether it too should open Chapter 11 proceedings. The only issue here is whether the reorganisation proceedings will have any effect on Kretek’s current sponsorship arrangements. If there is any risk to that arrangement, then it would be prudent for it to also open Chapter 11 proceedings to prevent any *ipso facto* or other termination of that contract (§365). Otherwise, there may be merit in having that company form part of the Scheme proposed for Efwon Trading, its parent.

*English Proceedings*

There is one decisive factor in favour of English proceedings in 2019, being the appointment of a VA and the proposal of a Scheme. That is, the availability of the EUIR and potentially the EJR to assist with the reorganisation process. Even though it is proposed that Efwon Romania file Chapter 11 proceedings in the US, it would be open to argue that the COMI of Efwon Romania is England, for the reasons stated in Section C above. As such a VA appointed to Efwon Trading in England could seek to exercise rights under the EUIR to obtain assistance from the Romanian courts, which will have a firmer foundation than an equivalent request made by the US Court under the MLCBI. This is discussed in further detail in Sections H and I below.

The aim of the English proceedings would therefore to be to access all existing sources of funding – being the broadcast revenue and the remaining Kretek sponsorship moneys, and implement a Scheme to address all creditor claims in respect of those moneys. The Scheme could also include provisions for the capitalisation of the new Malaysian company, novate existing lending arrangements with that new company and/or make provision for debt-for-equity swaps for the lenders as part of that capitalisation process. These orders would then be enforceable by means of the EJR if required.

The only potential disadvantage of the English proceedings is the loss of control by Mr Maximov over the process, as the Scheme would be proposed by an external VA, compared with the central role played by the debtor-in-possession under Chapter 11. That said, it can be expected that Mr Maximov will play an important role in the formulation of the Scheme, as the sole shareholder of the group, as he or his interests will constitute a separate class that must approve any Scheme that is proposed.

*Parallel Proceedings*

The existence of parallel proceedings for the reorganisation of the Efwon group is not unusual, and there are good reasons for the use of the two jurisdictions in this case in 2019. By contrast, as previously noted, in 2022, there is no advantage to opening proceedings in England, due to the loss of access to the EUIR and EJR as a consequence of Brexit.

It is reasonable to assume that there will be a coordinated approach by Mr Maximov and his advisers to the parallel proceedings. The only real point of overlap will arise in relation to Efwon Romania. Directions may be obtained in the US Court to permit Efwon Romania to participate in the English Scheme, without losing its rights to access the benefits of Chapter 11, in terms of transferring the FIA licence to the new Malaysian company. This is a matter of detail that will be capable of resolution between the lawyers and advisers involved. However it is entirely possible that this issue will be resolved, if FIA accept the inevitability of the exercise of power by the US Court to transfer the licence to the new Malaysian company, and FIA agrees to that occurring voluntarily. If the FIA does so, the Efwon Romania can withdraw from the Chapter 11 proceedings, and take part in the English Scheme directly.

The other issue of potential overlap concerns the US lenders. As the Chapter 11 proceedings are required by Mr Maximov, it seems appropriate to open Chapter 11 proceedings for Efwon Investments. The US banks will be represented, in a proxy sense, by Efwon Investment’s interest in the Scheme as a creditor of Efwon Trading. This too is a matter for directions in the US Court and drafting of the Scheme by the advisers. Again, it is possible that the US lenders might agree a compromise position with Mr Maximov that removes the need for the Chapter 11 proceedings, in which case Efwon Investments could join the English Scheme proceedings, bringing all parties before the English court directly, in the one Scheme proceeding.

**G. Further Facts Required**

There are four main facts that will assist in providing a definitive answer to finalising the advice about where the reorganisation proceedings should be opened.

***First***, where are the main administrative functions performed for each of the companies in the group. This is relevant to determining the question of the COMI under the EUIR and MLCBI. It is possible that the group has two COMIs – one for Efwon Trading and its subsidiaries, and one for Efwon Investments. The location of the COMI for Efwon Romania will be of critical importance to the determination of which proceedings for that company are the ‘main’ proceedings and which proceedings are ‘secondary’ proceedings. The most immediate impact of this determination will be in relation to obtaining the funds payable for the broadcasting revenue and the other operational assets.

***Second***, what are the terms and conditions of the FIA licence, particularly in relation to whether it can be assigned or novated from Efwon Romania to the new Malaysian company without a court order. If the FIA licence is not subject to termination on the opening of insolvency proceedings, and is capable of being assigned to the new Malaysian company, there will be no need to open Chapter 11 proceedings in relation to Efwon Romania – as these are key reasons for seeking relief under Chapter 11 in relation to Efwon Romania.

***Third***, what are the terms of the Kretek sponsorship arrangements with Efwon Hong Kong, and is Chapter 11 protection required to prevent any termination of those sponsorship arrangements. This involves similar considerations in relation to *ipso facto* type clauses, as has been considered in relation to the FIA licence.

***Fourth,*** what are the connecting factors, if any, between the loans of the US lenders and England. This issue only arises if it is proposed to conduct the group reorganisation by means of a Scheme in England, and it is necessary to give further consideration to the ‘sufficient connection’ test between England and Efwon Investments. As mentioned above, any problem that is identified is capable of cure by an appropriate amendment to the financing terms.

In addition, although it is not strictly a factual investigation, it would be useful to initiate discussions with some or all of the stakeholders, once the proceedings have been opened, to ascertain their attitude to the proposed reorganisation, so as to identify potential supporters and also potential points of opposition. The process of seeking this information may provide further assistance in simplifying the strategy outlined in this Advice, with a view to have all reorganisation proceedings take place in a single court.

**H. Application of the EUIR and MLCBI**

As indicated previously, the main role to be played by the EUIR and MLCBI is in relation to addressing two issues that arise in relation to Romania, which is subject to both instruments. Each of these instruments provides for the provision of assistance by one court (here Romania) in support of an insolvency proceeding in another court (here, England under the EUIR, and the US and England under the MLCBI).

***First***, and most importantly during the reorganisation process, is ability of these instruments to overcome the current freezing order in Romania over the broadcasting proceeds and other assets of Efwon Romania. The proceeds will be important to provide liquidity to the group, and also to provide money for the purposes of making payments to the US lenders and the Monaco lender as part of the reorganisation Plan.

***Second***, and relevantly to the success of the proposed reorganisation plan, will be the transfer of any assets located in Romania that are relevant to the ongoing operation of the F1 racing team, upon its proposed relocation to Malaysia. The transfer of the FIA licence is a matter that will be dealt with separately as part of the Chapter 11 Plan or by the voluntary agreement of FIA. However, the continuity of the team’s performance, including through the use of assets owned by Efwon Romania, will be important to ensuring the team can continue to compete in the F1 racing series during the reorganisation process, to generate future broadcasting revenue and ensure the flow of sponsorship moneys from Kretek.

**I. Relevant Provisions of the EUIR and MLCBI**

The scheme of both the EUIR and the MLCBI involves the identification of ‘main’ proceedings, which as previously mentioned depends upon the identification of the COMI of the company concerned. For the reasons given in Section C, this Advice assumes that the COMI for Efwon Romania is England (under the control of Efwon Trading) or potentially the US (under the control of Mr Maximov). If that is correct, the ‘main’ insolvency proceeding will be that opened in either England by the appointment of the VA, or in the US by the filing of Chapter 11 proceedings in respect of Efwon Romania.

*EUIR – Secondary Proceedings*

The main provision of relevance in the EUIR for the proposed strategy is Art.19 which provides that a judgment opening proceedings in one member state will be automatically recognised in another member state ‘from the moment it becomes effective’. Here, the appointment of a VA in England to Efwon Trading, which must be done by filing a Notice of Appointment with the Court (IA Sch.B paras 29, 31), becomes immediately effective for the purpose of EUIR Art 19.

The important step in the argument is that the appointment of a VA to Efwon Trading is effective not only in respect of Efwon Trading, but also effective to open insolvency proceedings for Efwon Romania, given that it is a subsidiary of Efwon Trading and it has its COMI in England. This argument is supported by the second clause in Art 19(1) which provides for automatic recognition ‘*where on account of a debtor’s capacity, insolvency proceedings cannot be brought against that debtor in other Member States*’. Specifically, here, there is no ability to open insolvency proceedings in England by the appointment of a VA to a Romanian company.

If the appointment of the VA to Efwon Trading operates to open insolvency proceedings in respect of Efwon Romania, then Art. 19(2) provides that the only proceedings that may be opened in Romania are ‘secondary’ proceedings. This situation would give rise to an interesting question about whether any such application could be made by the VA, in light of the stay of proceedings against Efwon Romania as a consequence of the Chapter 11 proceedings. This may be resolved by seeking a variation of that stay in the US to permit the secondary proceedings to be opened (11 USC §362(d)). This assumes that the Romanian court would recognise the US stay, without a concurrent application under the MLCBI for that recognition. This problem is more likely to be theoretical than real, given the likely cooperation between the debtors in the Chapter 11 proceedings and the VA, in seeking to obtain assistance from the Romanian court for the proposed reorganisation.

In relation to the broadcasting revenue and the other assets of Efwon Romania, the VA may not remove those assets due to the freezing order which was filed pending the opening of insolvency proceedings in Romania. This precise situation is addressed in Art.21(1) as an exception to the general power that the ‘main’ insolvency practitioner has to remove assets out of the ‘secondary’ jurisdiction.

There is no exact statement in the EUIR as to what the ‘main’ insolvency practitioner is to do in relation to the frozen assets, although Art. 38 recognises the Romanian court’s power to lift temporary stays after consideration of the competing interests involved. The most likely course will be for the Romanian court to open secondary insolvency proceedings under Arts. 34 and 37, or for the VA to give an undertaking to the Romanian court under Art. 36 to distribute any Romanian assets in accordance with Romanian law. The likely intention or effect of these provisions is that the Romanian assets, being the broadcasting revenues and other operating assets, would be available to meet the Romanian creditors, being the drivers and any other trade creditors.

Assuming that secondary proceedings are opened in Romania, for the satisfaction of the Romanian creditor claims, there are two other important powers available to the VA that may be of relevance: (i) under Art.47 the VA has the power to propose a reorganisation plan under Romanian law for the local creditors; and (ii) under Art.48 once the assets in Romania are found to be sufficient to meet all Romanian claims, the remaining assets may be transferred to the VA (as the insolvency practitioner in the ‘main’ proceedings). If, as might be expected, the broadcasting revenues will significantly exceed the claims of the drivers, the VA may use one of these two mechanisms to ensure that the surplus funds and operating assets are made available for inclusion in the English Scheme. There are significant matters of detail to be resolved by the VA and the insolvency advisers to achieve this outcome, but, in principle, this will assist in framing the Scheme and the approach of the VA to the recovery of these assets.

*EUIR – Group Proceedings*

The other provisions in the EUIR that may be of relevance concern the opening of insolvency proceedings in respect of a group of companies (Ch.5). These provisions will be applicable if the Romanian court does not recognise the English proceedings as the ‘main’ proceedings for Efwon Romania. The essential principle in Chapter 5 is one of cooperation to facilitate the effective administration of the proceedings (Art.56) and includes cooperation and communication between the courts and between the practitioners involved (Arts.57 and 58).

Additionally, the EUIR makes provision for the opening of group coordination proceedings (Art. 61). Under Art. 62 there is a priority rule that gives priority to the court in which an application is first made to open group coordination proceedings, with the intention that a group coordination plan be developed and agreed between the insolvency practitioners involved (see Art.72). Goode questions whether there will be much take up of these provisions in practice. Certainly it seems to add a layer of complexity to the reorganisation of this group, which has a relatively limited number of stakeholders, and a single business (Van Zweiten 2018).

*MLCBI*

The approach of the MLCBI to cross-border cooperation is much less prescriptive than that of the EUIR. It is principally relevant for the purpose of this Advice in relation to the proposed Chapter 11 proceedings opened for Efwon Romania, although it is also available to the VA in respect of Efwon Romania.

Like the EUIR, the MLCBI distinguishes between the ‘main’ proceeding, which is based on the debtor’s COMI, and proceedings in the place of recognition (although these are not called ‘secondary’ proceedings). Under MLCBI Art.9, a ‘foreign representative’ has standing to apply to the Romanian court, and is entitled under Art.11 to participate in a Romanian proceeding regarding Efwon Romania as the ‘debtor’. In this case, the foreign representative would be the debtor as trustee under the Chapter 11 proceeding.

Critically, under Art.15, the foreign representative may apply for recognition of the Chapter 11 proceedings, a stay of proceedings in Romania against the debtors assets under Art.20, and relief under Art.21, which includes the entrusting of Romanian assets to the foreign representative provided the Romanian court is satisfied that the interests of Romanian creditors will be protected (see also Art.22). There are also provisions for communication, cooperation and coordination (Arts. 25-30).

Again, on the question of stays, there will be an issue whether the Romanian court will automatically accept the world-wide stay of the US Court on the filing of Chapter 11 proceedings by Efwon Romania. Alternatively, the Romanian court may require the debtor, as the ‘foreign representative’ in the Chapter 11 proceedings, to make an application for recognition as a ‘foreign main proceeding’ to obtain a stay under Art. 20 of the MLCBI.

The provisions of the MLCBI depend upon the Romanian court adopting a ‘universalist’ view of the US Chapter 11 proceedings for their efficacy. On the critical issue of the potential transfer of the Romanian assets to the US Court for administration, Art. 21 does not require the US to be established as the COMI of Efwon Romania, as the qualifying description is that of a ‘foreign proceeding’ and not a ‘foreign main proceeding’. However the ability of the ‘foreign representative’ to obtain that relief depends upon the discretion of the Romanian court, as indicated by the word ‘may’ in the opening words of Art. 21.

This brief analysis of the MLCBI demonstrates the potential value of being able to rely upon the EUIR if possible to take control of the Romanian assets, and bring them into the reorganisation plan as quickly and efficiently as possible.

**J. Impact of Brexit**

For the reasons mentioned above, Brexit has a significant impact upon the proposed reorganisation strategy, and in particular the need for proceedings in England. Under the Brexit Withdrawal Agreement, the exit occurred on 31 January 2020, although the EUIR continued to apply to where the main insolvency proceedings were opened prior to 31 December 2020. As stated in Section F above, a decisive factor in favour of opening English proceedings was the ability of the English VA to use the EUIR to seek to overcome the impact of the Romanian freezing orders in relation to the assets of Efwon Romania.

Once the EUIR advantage of English proceedings is removed, the better course will be to conduct the reorganisation of the entire Efwon group in Chapter 11 in the US. As such the reorganisation can be done in one court, without the need for an external administrator (VA) being appointed in England, and where all debtors, including Mr Maximov are parties to the proceedings. The only caveat to that conclusion is if the factual investigations reveal that the COMI of the group is in England, in which case English proceedings may be preferred for the whole of the corporate group to maximise the prospects of successfully relying on the MLCBI in Romania. In that case also, the only Chapter 11 proceedings that might be considered are proceedings in respect of Mr Maximov only, as he would not be a party to the English proceedings.

**K. Conclusion**

Otherwise, pre-Brexit, for the reasons provided in this Advice, reorganisation proceedings should be opened in the US under Chapter 11 for at least Mr Maximov, Efwon Investments and Efwon Romania, and in England by means of a VA and a Scheme for at least Efwon Trading. Depending on the factual inquiries made, as recommended in Section G, Efwon Hong Kong can be added to either the Chapter 11 proceedings or the English scheme proceedings.

No reorganisation proceedings are recommended to be opened in Romania. Rather, secondary proceedings for Efwon Romania will be opened there under either or both of the EUIR and MLCBI to ensure that the Romanian assets form part of the reorganisation process and Plan. Consideration can also be given to the possibility of group coordination proceedings in England under the EUIR.

If the advice is given in 2022, post-Brexit, a single set of reorganisation proceedings should be opened under Chapter 11 in the US for Mr Maximov and all group companies. There would be no particular advantage in opening Part 26A proceedings in England post-Brexit unless some particular factual circumstance suggested otherwise, in which case a Chapter 11 proceeding in relation to Mr Maximov may also be required, to protect his position in the US.

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