**Case Study Module A**

1. **What were in your opinion the causes of financial distress at Flow Management (see e.g. Mellahi & Wilkinson, 2004)?**

As per the above mentioned paper, financial distress can be included in the definition of organizational failure. Some of the symptoms detailed in the paper and present in the Flow Management case include shrinking financial resources and negative profitability.

Organizational failure can be explained through two differentiated theories. These theories explain that causes for organizational failure can be classified depending on whether they are originated by external factors (IO/OE perspective), in the case of industrial organization (IO) and organizational ecology (OE), or internal factors (OS/OP perspective), in the case of organizational studies (OS) and organizational psychology (OP).

The IO perspective assumes that negative external environment to the firm may generate failure. Negative environments may be produced by be produced by technological, regulatory, economic or demographic nature. These include changes in costumer tastes, cyclical economical changes, rivalry between existing and new competitors and uncertainty due to new technology applicable to products and internal processes. This perspective follows three believes: (i) external environment pressures and constraints firms’ strategies therefore resulting in failure; (ii) firms operating in same markets follow similar strategies, and; (iii) firm managers are business rationale and their decision making is in the best interest of their organization. The relationship between organizations and their environment can be explained through three factors: (i) dynamism, which increases uncertainty and, therefore, mortality because of difficulty by firms to predict situations that may affect their business, choosing to engage in short term strategies, bad investments and high risk decisions; (ii) munifence, meaning that failure occurs in scarcely resource environments, and; (iii) complexity in the relationship between the firm and its stakeholders and other players in their market.

The OE perspective refers as causes to the termination of a firm due to the so called population and organisational ecology which assume four factors for failure: (i) population density, which refers to the rate between the number of firms operating in a market and the population in the same market through two antagonist concepts, legitimation and competition. Increase in population density validates the way market practices by firms and improves the capability of firms to attract resources therefore reducing failure. On the same hand, increase in population density increases competition between the same firms, therefore increasing failure; (ii) industry life cycle, which states that failure is cyclical in efficient markets and cannot be avoided. This may be caused by absence of technological innovation enhancing value of the firm, demand peaking and supply not meeting with demand requests; (iii) organization and age, where new firms have a greater tendency towards failure than established firms. Established firms have advantages over new firms, as follows: routines and management structures do not need to be learned and processed as it is assumed they are already in place and are effective, client engagement exists, there is no stress over capital raise needs, tax and law regulations are already learnt and there is greater labour competition in new firms. This stress applicable to new firms can also apply to old firms suffering from major changes though there is theoretical discrepancy with this statement, and; (iv) organization size, as failure is reduced when size is increase, despite all firms facing higher failure rates when organization maturity approaches.

OS/OP failure causes lie on the belief that management actions are the single most important cause to failure of an organization. These actions may be directly related to the personal characteristics of the management team, as managers are humans and their conditions affect the organisation. The following theories can be used to explain causes of failure: (i) groupthink theory, where individual or external ideas are dismissed in order to obtain cohesion by the group; (ii) upper echelon theory, expressing the idea that the demographic characteristics of the management team affect decisions. Specifically, homogeneity in the decision making team may be a negative characteristic due to ineffectiveness to determine causes of failure and tenure or seniority in a management position may bias the manager to consider that failure is caused by external factors that can be internally controlled, ignoring internal causes and continuing with negative habits inside the organization. On the other hand, change in management or succession faces contradict studies; (iii) curse of success, as positive routines may turn into negative habits, and; (iv) threat rigidity effect theory. This theory explains that managers tend to continue the same business approach when a crisis develops, therefore negating its causes and effects until they have reached such size that means they can hardly be tackled. The following psychological factors can explain to this behaviour: (i) denial of the situation, including causes, effects and accountability; (ii) rationalisation of their conduct and behaviour; (iii) idealization of a manager’s previous behaviour thus damaging possible amendments to the distress situation; (iv) fantasy as imagining as achievable impossible to obtain goals, and; (v) symbolization of persons or ideas.

There is certain proof in the paper to dismiss external causes for the financial distress situation. We are told that there is a business structure that operates properly and that demand and forecast for the company’s services is real and adequate to the company’s plan.

In my opinion, causes for financial distress in Flow Management Work can be initially (16 November 2013) summarized as follows: (i) wrongfully issued management bonus for 3 million euros; (ii) contingency gain wrongfully booked thus a 1.6 million euros correction for 2012 needs to be registered; (iii) book profit for 2.8 million euros needs to be written off in 2013, and; (iv) loss of 5.4 million euros due to basic miscalculations in cost price.

Causes to explain the financial distress at this point are all internal. Mismanagement of the firm can easily be pointed out to explain the wrongful issuance of the bonus. This is obviously a direct consequence of their decision. It can also be pointed out to explain the other causes, though they may not be caused by their direct decisions but to the internal organisation and business decision making process in the firm. Above causes (ii), (iii) and (iv) are all part of bad accounting. Managers are in charge of the personnel hiring and, in last instance, they are liable for a bad selection of the personnel in charge of the whole accounting process of the firm. Despite managers not being accountants themselves, they do review and prepare the accounts and propose them for approval to the shareholders at the general meeting taking place every year. Managers can be held liable for gross inaccuracies in the firm’s books, being this such case.

Managers are also to blame for an inefficient information system. Relations with stakeholders seem to be missing.

Proof to the terrible internal accounting job is the appointment by the Banks of an independent firm to review the accounts on 1 December 2013. HoldCo is requested to monthly financial reports and UkCo is requested to improve solvency rating, proposing selling of the assets as opposed to raising cash, bank’s preference.

These numbers and practices, though, as bad as they are, do not justify the very negative results for 2011-2013.

Maybe this is not the case but creditors’ risk assessment, considering the circumstances, is, to say the least, suspect.

**Could the financial distress have been prevented? If yes, explain how. If no, why not?**

The easy answer here would be to say yes but in my opinion we do not have enough information in order to assess precisely if financial distress could have been prevented. Wrongdoing by the management team is obvious but it does not mean that financial stress could have been avoided. I am speaking about preventing the situation, not resolving the situation, which is very different.

Insolvency is defined by the inability to pay debts. It is originated by negative cash flows. Flow Management is in an imminent insolvency situation due to their inability to repay Banks their debts.

If we were to remove the management wrongdoing that caused the distress and prior to the financial distress situation we were to implement the proposed measures to resolve the situation, including price increases and spending cuts, we still have no certainty on whether the company would have been able to avoid the failure.

As Adriaanse & Kuijl, 2006, explain, regarding the causes of financial difficulties it can be concluded that the problems mainly relate to poor management – i.e., inadequate reaction on both internal weaknesses and strengths, even as external threats and opportunities – and excessive cost structures, as well as the presence of inadequate management information systems within the company (as a result of which important, early warning signals of imminent decline are missed my management).

**2. What are in general advantages and disadvantages of an out-of-court restructuring (workout) as compared to a formal bankruptcy procedure?**

As defined by Adriaanse & Kuijl, 2006, an informal reorganization is a reorganization that takes place outside the statuary framework with the objective of restoring the health of a company in financial difficulties within the same legal entity. This will mostly consist of a business and a financial restructuring.

A formal reorganization includes all possibilities or reorganization laid down by the insolvency law or which take by using the legal methods and possibilities.

The advantages of an informal reorganization can be summed up with the following terms: (i) flexibility, informal reorganizations are less rigid. “Tailor-made” solutions can be elaborated; and, if necessary deviations can be engineered for the relative positions of creditors. It can be agreed that new funding which is made available takes priority from current positions and guarantees. Although most current laws also theoretically also offer this possibility, in Spain new funding needs to adapt to the regulation in place and, therefore, existing creditors need to accept it in order for it to be protected as desired by debtor and creditor; (ii) silence, as they take place in relative silence. In public procedures stakeholders will approach the company with reserve, which may lead to unwillingness in aiding in a future turnaround. A race to collect can easily develop which frequently leads into petitioning for liquidation of the debtor, and; (iii) control, during this process management can run this process independently, without the intervention of the court or the appointment of trustees. This save costs and grants the possibility of those intervening in the process to adapt its speed to their needs. Destruction of company value is not present when informal reorganizations take place as confidence in the company by stakeholders and investor remains higher.

Adriaanse & Kuijl, 2006 also lay out the possible disadvantages of an informal process, which appear to be in the field of investors/takeover candidates pulling out at latest moment and an insufficient supply of information from the company to its stakeholders during this process.

Other disadvantages may include a breach of trust between the company and its creditors due to various reasons: financial results which deviate from prognostication, managers failing to observe agreements with creditors and absence among the creditors of confidence in management and viability of the company, passive attitude by managers and shareholders towards the reorganization, insufficient strategic, operational and financial measures taken, company is unable to provide sufficient insight into the actual financial situation and the company is unable to find risk bearing capital in time.

Summed up, problems tend to occur because of execution problems but not because of the process itself.

**More specific, what are the advantages versus disadvantages in your country?**

Regarding Spanish Insolvency Law, I conclude similarly to what Adriaanse & Kuijl, 2006 conclude: insolvency legislation, in itself, does not have a significant impact on the chances of success of a rescue operation.

In Spain reorganisation processes, albeit being in pre insolvency stages, usually need the approval of the Court. These are called restructuring plans. For the purpose of answering this question, we will call them out of court restructuring. They are not as quick and their content has certain restrictions but they are way quicker than in court proceedings and allow to change the conditions or structure of the debtor’s assets and liabilities, or its equity. The plans may also involve the transfer of assets, business units or of the whole company.

Restructuring plans allow the possibility of cramming down all types of creditors (financial, commercial and even holders of public law credits that meet certain requirements) with the approval and shareholders of insolvent companies. The court sanction of the restructuring plan can extend its effects to all credits affected by the plan.

To facilitate debt restructuring at an earlier stage, the debtor can notify the Court that negotiations have been opened with creditors when it is foreseeable that if a restructuring plan is not agreed, the company will be unable to regularly meet its obligations falling due in the following two years. Notice enables the temporary suspension of individual, judicial or out-of-court enforcement over the assets required for the debtor to continue its business activity during the negotiation of the restructuring plan, among other measures designed to safeguard the company’s activity

Also, it will still be possible to seek a pre-insolvency solution in cases of imminent insolvency, which has been redefined as the foreseeable inability to meet obligations falling due in the following three months. Current insolvency is still considered to be a financial state in which it is possible to seek a pre-insolvency solution.

If insolvency is declared after a plan is court sanctioned, protection is granted against clawback actions to acts carried out in the context of promoting or implementing the plan. Specifically, it protects transactions necessary for the negotiation of the plan to be successful, transactions necessary to implement the plan, and interim financing and new money. As well as protection against clawback actions, interim financing and new money could be given preference for payment under certain conditions. Both types of protection are also provided for in cases where interim financing and new money have been granted by persons closely related to the debtor company, although stricter requirements must be met.

Even before filing a request for insolvency proceedings, debtors whose circumstances indicate a likelihood of insolvency or who are in a situation of imminent insolvency or current insolvency may request the court to appoint an independent expert responsible for collecting offers for the purchase of on-going businesses (pre-pack). On filing for insolvency proceedings, the debtor company will also submit a written binding offer from a creditor or third party to purchase one or several on-going businesses. After the debtor has filed for insolvency and submitted the binding offer, the judge will follow the process in accordance with the law so that the creditors may make themselves known and any interested party can submit an alternative binding offer. If several offers are submitted, the judge will select the one that most benefits the proceedings. If the workers submit an offer that is equal to or higher than the offers submitted by other parties, the judge will give priority to the workers’ offer as long as it is to the benefit of the insolvency, considering, among other criteria, the continuity of the company, the on-going business and the job positions.

There are two types of full in court proceedings: in court reorganisations (“*Concurso de Acreedores*”) and liquidation processes, which are a phase of the judicial process in the case no reorganisation is achieved (95% of insolvency cases). All of the above measures can be replicated in the judicial stages of the reorganisation process.

**3. Were the turnaround/reorganization approaches as presented in the reading material (see e.g., Adriaanse & Kuijl, 2006, Pajunen, 2006, Sudarsanam, S, Lai, J., 2001, Schmitt, A., Raisch, S., 2013) applied in this case? If yes, explain in what way. If no, detail what in your opinion should have been done differently.**

The turnaround/reorganization in the case was not in line with the approach presented in the reading material.

Any approach should be done in the frame of an established plan. A plan requires a study of the situation in order to understand the causes of the failure and the direction the company must take in order to make a successful turnaround. This is simply not done. All measures and ideas are thrown along the process without, it seems, a thoughtful idea.

Sudarsanam, S, Lai, J., 2001 state that top management change is widely quoted as a precondition for successful turnarounds. It is difficult for existing management to change habits and execute necessary but radical reforms on the firm.

A change in management is evidence to stakeholders that something positive is being done to improve the firm’s performance, even though the cause of poor performance may have been beyond management control.

Pajunen, 2006 explains that a direct effect of the appointment of a CEO was that the process became more production oriented. In this case, new administrators were appointed in the beginning of the reorganization process by creditors and representatives for the creditors and the non-preferred shareholders were also appointed as members of the board. In this case of success, administrators were given full power to manage the firm.

In our case, In January 2014 we are informed that a new CFO will be appointed at HoldCo, the CEO of HoldCo is replaced in the middle of April 2014, by mid-June we are informed that Banks want to appoint a CRO, later appointed, long after the financial distress is originated and the reorganization process started.

Pajunen, 2006 also explains that in order to enhance the chances of the organization’s survival the support of influential stakeholders has to be ensured. To do this, it is proposed: (i) the more secured the continuing support of governing stakeholders in an existence-threatening crisis; (ii) frequent and open communication between managers and governing stakeholders will tend to increase the probability of survival; (iii) personal relationships between managers and governing stakeholders; (iv) management’s unlocked brokerage position between governing stakeholders; (v) consensus on long term goals among governing stakeholders, and; (vi) governing stakeholders association of management with good firm performance is positively related to organization survival.

In our case, communication between management and stakeholders are inefficient during the crisis and the reorganization process. Management fails to inform about the causes of the crisis in time, fails to inform precisely about the company situation during the process and long term goals for both company and stakeholders seem to change during the process and are never aligned.

Adriaanse & Kuijl, 2006 explain the factors that determine the success of a rescue operation:

(i) active attitude by management and shareholders with regard to the informal reorganization; (ii) involvement of important interested parties in the reorganization process; (iii) adequate and speedy reorganization of the business operations; (iv) transparency with regard to the financial situation and the intended informal reorganization, and; (v) injection of risk-bearing capital.

Informal reorganizations, the case being one, are especially successful when the company is able to recognize its business operations quickly and adequately and, thereby, to restore profitability. This process must go hand in hand with the introduction of risk bearing capital.

A good relationship between the company and its primary stakeholders appears to be vital. Reorganizations only have a chance of success when these interested parties can be convinced of the future viability of the company and the abilities of the management. A transparent approach to the problems is important.

When the parties can be convinced that the going concern value is higher than the forced sale value, the willingness to cooperate and chances of success increase.

With the exception of (ii), none are present in the case. There might seem to be an active attitude by stake holders, as Banks are invited to the board of HoldCo. It is too late, therefore board was passive prior to calling this board meeting. The whole process looks messy, unprofessional and very slow until actual proposals are presented. Transparency is simply not there, with financial results changing and forecasts being wrong. Risk bearing capital finally is injected to the company but, again, too late and without a plan being proposed. The plan is proposed after the first injection of cash, which does not make much sense from a debtor standpoint. Adopt measures to restore balance sheet, propose the plan, maybe inject cash in order to demonstrate engagement with the reorganization process and then close the agreement.

Only information we have about valuations are the ones that refer to the recovery in case of liquidation scenario. There is no on-going business valuation to support the plan and the actions taken by all parties.

Sudarsanam, S, Lai, J., 2001 explain that operational restructuring is generally the first turnaround strategy implemented by a financially distressed firm, as there is no point on assessing the strategic health if the firm goes bankrupt in the near term. Efficiency measures are directed at both maximizing output (revenue) and minimizing input (resources such as inventory). Cost reduction may be sufficient where the firm is weak operationally.

In our case, certain operational measures are taken in this line. There is a general cost saving strategy and an intention to increase prices since the start of the reorganization process. The implementation of both measures looks to be effective.

This stage of the process aims to stabilize operations and restore profitability by pursuing strict cost and operating asset reductions. In our case, despite the measures executed, the firm still does not produce profit.

Also Adriaanse & Kuijl, 2006 explain the main features of a business restructuring, which can be defined as a comprehensive plan which aims to restore the operational profitability of a company in financial difficulties:

(i) stabilizing, which means identifying the critical problems which require immediate action in order to stabilize the situation. The emphasis in this phase is to increase the cash flow, this means increasing the incoming and reducing the outgoing;

(ii) analysing, as it is necessary for the company to look at its prospects in the long term. In order to restore confidence with the relevant parties, drawing up with a detailed reorganisation plan is necessary. Some of the relevant matter to be included in the plan are: (a) a strategic and financial analysis to find the causes of the financial distress; (b) an inquiry into the actual financial position and an assessment as to whether or not the company still offers sufficient basis for recovery; (c) proposed measures and the calculated effects thereof on long term exploitation overviews and balance projections; (d) cash flow projections in the short and long term from which it appears that the obligations entered an to be entered can be performed; (e) cash flow projections which show a future projections in the liquid assets.

(iii) repositioning or value recovery process, where objectives which have been established are feasible and that management reports to the interested parties in an open and timely manner. This process pursues regain confidence, therefore supplying information is vital, and;

(iv) reinforcing, both in the field of management and the balance sheet, which could be achieved by transferring the company to a third party.

Financial restructuring is connected with the reinforcement of the balance sheet. Usually obligations towards the asset are excessive, interest and repayment obligations cannot be met and reorganization costs are usually involved. Funding from outside the company will often be requested. Measures, therefore, will consist in deferments or remissions of current financial obligations and generating additional cash.

Just one of the measures proposed is executed in phase (i), cutbacks in expenditure. There is no optimization of the stock, which we do not have information about and there is no action regarding the collection of receivables.

Phase (ii) does not exist. Measures implemented do not respond to any profound analysis or assessment and no plan is proposed by the company until June 2014.

A recovery plan as said in phase (iii) is not executed. There are no objectives established that we know about and communication with stakeholders is poor and intermittent.

Phase (iv) is also a failure. Management is removed albeit but late, balance sheet still is negative and assigning the company to a third party fails, probably because everything has been managed poorly, including approach by the creditors and other stakeholders. Actually, third party interest is withdrawn due to the situation of the company and after the agreement is signed and possible investors decide that, purchase should occur in an event of liquidation and not in the frame of a reorganisation plan.

**4. Banks C and D seem to frustrate the process at a certain point. What could have been the (rational and/or opportunistic) reason(s) for them to behave like that?**

From a rational point of view, in my opinion, frustration stems from lack of confidence in the debtor and their management and from the lack of organization of the process.

Lack of confidence is caused by the inefficient communication system between parties involved and because of the erratic behaviour of the management, including false data and wrong predictions.

Lack of organization due to the absence of a plan or an idea that structures the process, including the inexistence of a standstill period at the beginning of the process that helps parties to structure a reorganisation plan.

From an opportunistic point of view, their behaviour makes sense. If there is no confidence and there no organised process, it is justified for them to act individually and without thinking of a global solution that might benefit them more. An uncontrolled race to collect, in which each creditor pursues his own interests demanding direct payment might ensue, in the words of Adriaanse & Kuijl, 2006. Such conduct will cause an inevitable loss of value to the business, including the possibility of the company filing for insolvency, eliminating the chance the creditor had to gain any kind of advantage.

**What would you have done in that situation in your role as advisor of the other two banks?**

The Statement Principles reflect on this. The First Principle reads as follows: “*Where a debtor is found to be in financial difficulties, all relevant creditors should be prepared to co-operate with each other to give sufficient (though limited) time (a “Standstill Period”) to the debtor for information about the debtor to be obtained and evaluated and for proposals for resolving the debtors financial difficulties to be formulated and assessed, unless such a course is inappropriate in a particular case*.”.

In accordance to this principle, the approach by Banks should have been coordinated. Co-operation between them should occur at all times during the process. From the information we have, all banks have similar interests and their credits are in the same class, therefore conforming one class of creditors and conflict of interest not existing.

The right thing to do here is for Banks jointly to grant the cooperative debtor a standstill period, in order to review and understand the situation. After reviewing and understanding the situation, a plan can be put in place in order to help the debtor to resolve its financial distress and maximize the Bank’s recovery.

In my opinion, the standstill period should have been granted by Banks, upon agreeing to discuss the company’s situation, this is, 1 December 2013, after all being called for a meeting and being informed about the situation of the company. Prior to this meeting and this decision, the Banks had no information about the situation of the company in order to commence the period. It is also important to determine the duration of this period. In my opinion, three months is enough but monthly extensions can be called by the creditors, if needed, due to the complexity of the situation.

Inefficient communication and erratic behaviour by the management should have been tackled immediately. First, appointing an interim manager/CRO or an independent firm which should have been in charge to conduct the process. After this appointment, it is understandable to think communication will be channelled in a more effective way.

At this moment, communication and information are fluid and accessible and Banks are working together. Next step is to evaluate the existing information in order to decide to propose a reorganisation plan if it makes sense or let the business fall and pursue the needed legal action, including against old management. Whatever option maximizes recovery to my client.

**5. Which of the eight principles of the ‘Statement of Principles for a Global Approach to Multi-Creditor Workouts II’ can be found in the workout process of Flow Management (explicit or implicit)?**

*“FIRST PRINCIPLE: Where a debtor is found to be in financial difficulties, all relevant creditors should be prepared to co-operate with each other to give sufficient (though limited) time (a “Standstill Period”) to the debtor for information about the debtor to be obtained and evaluated and for proposals for resolving the debtor’s financial difficulties to be formulated and assessed, unless such a course is inappropriate in a particular case.”*

Implicitly, we can observe this First Principle might be found as Banks decide to act jointly in December 2013. Discrepancies between them start in March 2014 as there is no standstill in place despite their intentions to produce one and are clearer in June 2014 when C and D threaten to act individually and terminate the agreements with the company. A Standstill Agreement is finally signed in August 2014. In the end, all Banks sign the restructuring agreement.

*“SECOND PRINCIPLE: During the Standstill Period, all relevant creditors should agree to refrain from taking any steps to enforce their claims against or (otherwise than by disposal of their debt to a third party) to reduce their exposure to the debtor but are entitled to expect that during the Standstill Period their position relative to other creditors and each other will not be prejudiced. Conflicts of interest in the creditor group should be identified early and dealt with appropriately.”*

There is no explicit evidence of the existence of a standstill agreement until August 2014 although Banks decide to act together before that. If we assume there is an agreement between Banks, in June 2014 Banks C and D threaten to initiate individual action against the Debtor, probably breaching their intercreditor agreement if it were to be in place.

Banks A and B think about purchasing C and D’s position in March 2014 which probably is not a breach of the supposed intercreditor agreement. Any agreement between banks should foresee the possibility of them trading their position.

Conflicts of interest between Banks are not manifested and cannot be assumed as there is no evidence to point them out.

*“THIRD PRINCIPLE: During the Standstill Period, the debtor should not take any action which might adversely affect the prospective return to relevant creditors (either collectively or individually) as compared with the position at the Standstill Commencement Date.”*

All actions described by the debtor since November 2014 and until August 2014 can be included in the ordinary course of the business. After August 2014 and the signing of the Standstill Agreement, in October 2014 the company sells surplus assets. This probably is consented by Creditors as it exceeds what is considered the running of its ordinary business.

*“FOURTH PRINCIPLE: The interests of relevant creditors are best served by co-ordinating their response to a debtor in financial difficulty. Such co-ordination will be facilitated by the selection of one or more representative co-ordination committees and by the appointment of professional advisers to advise and assist such committees and, where appropriate, the relevant creditors participating in the process as a whole”*

I do not appreciate the role of a coordinator or an agent to the creditors in the reorganisation process. The appointment of the CRO due to Bank A insisting to it, albeit a facilitator to the success of the process, does not fit as a coordinator o agent.

*“FIFTH PRINCIPLE: During the Standstill Period, the debtor should provide, and allow relevant creditors and/or their professional advisers reasonable and timely access to, all relevant information relating to its assets, liabilities, business and prospects, in order to enable proper evaluation to be made of its financial position and any proposals to be made to relevant creditors.”*

The communication and information process is a mess during the whole process. The Standstill Period starts in August 2014 but the financial distress is communicated in November 2013 and subsequent information from the company to the creditors is erratic, to say the least. After 2014 it is stated that the provision of information has improved and a restructuring agreement is signed on July 2015 therefore we can understand that it was efficient since that moment.

*“SIXTH PRINCIPLE: Proposals for resolving the financial difficulties of the debtor and, so far as practicable, arrangements between relevant creditors relating to any standstill should reflect applicable law and the relative positions of relevant creditors at the Standstill Commencement Date.”*

The reorganisation plan which is agreed to by all parties reflects the positions of the financiers involved as it is explicitly stated.

*“SEVENTH PRINCIPLE: Information obtained for the purposes of the process concerning the assets, liabilities and business of the debtor and any proposals for resolving its difficulties should be made available to all relevant creditors and should, unless already publicly available, be treated as confidential.”*

There is no reason to think that the information was not treated confidentially by any party.

*“EIGHTH PRINCIPLE: If additional funding is provided during the Standstill Period or under any rescue or restructuring proposals, the repayment of such additional funding should, so far as practicable, be accorded priority status as compared to other indebtedness or claims of relevant creditors.”*

No fresh money is granted before the signing of the restructuring agreement. Additional working capital loans by Banks C and D is not considered this way.

**6. Suppose it is not possible to convince other creditors to adopt the Statement of Principles in a given situation, are there any other possibilities for “soft law” to use (perhaps specifically in your country/region)? If yes, explain in what way. If not, do you see any alternative (informal) possibilities?**

In Spain all creditors can act together if they agree to and are free to set up the clauses that will regulate their conduct in a reorganisation process. It does not happen very often. It happens less when the trading of the debt occurs and international funds are present in a restructuring as a consequence of them purchasing the debt from original lenders. Interests between creditors differ and it is difficult to reach agreements that do not consider differences between their positons.

Agents or committees can be seen in syndicated financing, where creditors set up their relationship in case the debtor breaches the financing contract and in the issuance of bonds, where there is an initial agreement in place between original bondholders regulating their relationships and where a committee acts as a representative.

Other than this, creditors need to set up their relationships voluntarily.

**7. Explain in detail the essence and result of the restructuring agreement as signed on the 4th of July 2015.**

Agreement must be signed by all parties involved. Involved means assuming contractual obligations. Contracts cannot bind parties that do not consent ie sign the contract.

The restructuring agreement main point is keeping the on-going business alive. It does this by accommodating the operating companies, OpCos, in a newly formed entity, Dutch OpCo II. When keeping the business alive the labour needed to develop the activity is also maintained and therefore it is a benefit to the whole society. Accommodation is of companies and not shares, therefore the new entity being an operating company.

Owners of Dutch OpCo II include creditors and board members, with no information about the economic reasoning to allocate shares this way.

Dutch HoldCo is liquidated and claims against the company by Banks and by UkCo are cancelled.

Dutch HoldCo and UkCo cancel their claims against Dutch OpCo II and the OpCos.

Banks C and D write off all of their additional working capital debt against Dutch OpCo.

Banks A, B, C and D keep a claim of 240 million euros against Dutch OpCO and waive an amount of 97.5 million euros.

A 55 million euro loan is cancelled against Dutch OpCo.

Banks A, B, C and D get pledges over most of the assets of Dutch Opco in Dutch OpCo II, to guarantee repayment of 240 million euros.

Other creditors, including other financial creditors and UkCo get no security rights therefore it is expected they will lose all amounts.

OpCo II will try to be sold as an on-going concern to a third party. Sellers will be creditors and board members which received the shares of OpCo II.

This is basically the result of the Restructuring Plan. We have no economic reasoning behind it i.e. about the valuation of the business, allocation of shares and financial reasons for haircuts. There is also no information about how the new entity plans to recover value in the long term.

**8. Which (potential) legal and/or non-legal cross-border issues – if any – do you recognize in the Flow Management restructuring process?**

We are informed about a restructuring process involving a UK Shareholder holding a Dutch Holding company with international subsidiaries, not all in the European Union.

Existing insolvency risk, we should first address how Insolvency Law works in every country.

UK Shareholder is the owner of the shares of the Dutch HoldCo. The Dutch HoldCo will be liquidated. This process is unknown so we do not have information about it. The Dutch HoldCo will be legally extinguished and the shares will disappear. Applicable law will be the one of the country of the company being liquidated.

Dutch HoldCo is the owner of the shares of every subsidiary company, OpCos. Dutch HoldCo goes into liquidation so it will have to liquidate this shares. These shares are worth nothing, apparently, as the on-going businesses for every OpCo are accommodated in Dutch OpCo II. If this is the case, every OpCo will have to be liquidated, judicially or not judicially. If there are no assets and no claims, it will be done out of Court in accordance with the Corporate law of each country.

If claims remain against these subsidiaries, it will be done judicially under the insolvency Court in the country of each subsidiary. We do not have information about the managers and intercompany operations but there might be risk of clawback actions and liabilities of those involved and management.

From the information we have, there is only one debtor in the organisation process, the Dutch OpCo. Liabilities from Dutch OpCo are assumed by Dutch OpCo II, new entity incorporated. There is no cross border issue here.

Securities over assets granted by Dutch OpCo II to creditors will be subject to Dutch law if the assets are located in Netherlands. If not, applicable law will be the law where the asset is located.

Since there is no Court intervention, the restructuring agreement can be subject to whatever law parties agree to.

If Dutch HoldCo II files for insolvency and enters a liquidation process before the Court, it will have to be under Dutch law and Courts.

**9. In October 2014 four scenarios have been drawn up. Why was or wasn’t calling for a moratorium (see scenario 4) a good option given the situation at that time? [you are allowed to give your opinion based on your own countries’ Bankruptcy Act; be as detailed as possible]**

In Spain all judicial proceedings (in court reorganisations and liquidations) are very slow due to heavy activity and little resources by the Courts. This means every decision takes a lot to me made as it needs the acceptance of the Court. Proceedings are not agile even if it in the best interest of all parties to advance with the situation. This includes the in court acquisition of on-going businesses.

The timing of the Courts also drives away possible new money. Investors are uncertain on when the money will be repaid.

Viable on-going businesses that fall into a judicial proceeding might deteriorate and will not be able to find an answer in the time needed.

Judicial proceeding also impacts the valuation of an on-going business due to concern by stakeholders but also opportunistic interest by possible investors.

Reorganisations are quicker and more effective outside the judicial system.

Pre pack deals to sell on-going businesses have been incorporated to our legislation with the approval of the latest insolvency act in September 2023. With intention of keeping businesses and labour alive, the company can organise a competitive process to sell the on-going business with the intervention of an independent expert who will coordinate the whole process. The company will communicate the best offer to the Court at the same time it seeks its liquidation. If approved by the Court, the company enter a liquidation process and the purchaser will acquire the on-going business.

Despite this, out of court reorganisation is always cheaper and quicker and the Court offers no benefit to set off these benefits.

**Carlos A. Grande**