1. **What were in your opinion the causes of financial distress at Flow Management (see e.g. Mellahi & Wilkinson, 2004)? Could the financial distress have been prevented? If yes, explain how. If no, why not?**

Financial distress and ultimately organisational failure can occur for a number of reasons and there are competing schools of thought regarding the role that internal factors and external factors play in such scenarios. On the one side of the debate, external environmentalists see a "deterministic role" of the external environment whilst organisationalists lean towards a more "voluntarist perspective" of business failure, whereby managers play a pivotal role in the cause of business distress[[1]](#footnote-1).

Flow Management (the “Company”), faced a series of underlying issues, which caused its financial distress, based on the information provided in the Case Study literature. Fundamentally, a lack of accurate financial information appears to be the root cause of the challenges faced by the Company in 2013.

**Internal Factors**

The 2012 financial statements were materially misstated. There was a loss of EUR 5m generated in this financial year, as opposed to a EUR 3m profit which was reported by the Company in the financial statements.

Furthermore, a “formula error” was the cause of the requirement to down grade the 2013 results (with a loss of EUR 5.4m incurred in the year, against the reported results of a EUR 8m profit). This lack of accurate management information concerning the true financial performance and position of the Company was central to the deepening financial distress which the Company faced during the Case Study.

Whilst financial restatements and errors in isolation, are not unusual or necessarily the root cause of financial distress, the fact pattern in the Case Study suggests a more fundamental failure of the management team to develop a suitably robust financial control environment. In effect, the Company's management were operating without access to accurate financial data, which is patently essential when making strategic decisions regarding the business and formulating plans to deal with the evolving and deteriorating financial position of the Company.

For example, based on inaccurate information which showed the business had been profitable in 2012, the management of the Company made uninformed decisions around the payment of managerial bonuses. The Company management also appeared unaware of the loss making foreign subsidiary operations in the wider group until the engagement of an independent accounting firm in December 2013.

This lack of accurate financial information prevented early turnaround measures being implemented by management, arguably as early as 2012. This might have allowed a strategy to be implemented to turnaround the underperforming business units prior to the end of 2013. Further systems should have been in place to ensure pricing errors in the cost pricing calculation were quickly identified and rectified before material losses were incurred by the business without the knowledge of management.

The losses accrued as a result of the unidentified underperformance made it necessary for a financial restructuring to occur in 2015 in order to address the contamination of the balance sheet owing to the accumulated losses generated by the business, which had taken place in the two years prior.

The poor financial control and reporting systems are controllable internal business environmental factors, which could have been addressed thereby potentially preventing the financial distress experienced by the Company in the Case Study. At the very least, the degree of financial distress could have been mitigated with timely and accurate financial information provided to management. Acting competently, the management ought to have been able to take measures to improve profitability prior to the 2013 crisis materialising.

Furthermore, as the situation deteriorated in 2014 and negotiations with the banks progressed, the inability of the management team to provide accurate and reliable financial information undoubtably undermined the restructuring process and heightened the financial distress being faced by the Company.

The need for the appointment of a new CFO in January 2014 and the subsequent replacement of the CEO in April 2014 suggests that management may not have been competent and lacked the expertise to address the underperformance of the Company. This ultimately culminated in the appointment of a CRO in August 2014 to lead the restructuring.

**External Factors**

Looking at the other side of the academic debate from an external environmentalist perspective the independent review dated December 2013, suggests that the Company was viable and had sufficient market share to achieve its estimated turnover.

The response of customers to the price rises needed to rectify the accounting error also suggests that the external uncontrollable environmental factors in this scenario were not critical to the financial distress experienced by the Company particularly when compared to the internal factors discussed above.

The underperformance in the subsidiaries and overseas branch operations might have been attributable to wider external factors but there is reasonable evidence to suggest that had such underperformance been identified sooner, timely action could have been taken to manage these issues for example by addressing the sales mix or reducing costs as was attempted later in the Case Study.

Even if the external factors impacting certain subsidiaries or branches had been insurmountable, if the organisational systems had been in place, measures might have been taken early to dispose of the loss making enterprises or close unprofitable branches, protecting the wider business, which had been assessed as viable by independent parties.

**Conclusion**

In my view, the facts presented by the Case Study suggest that the managers played a pivotal role in the cause of business distress, following the "organisationalist view". In a scenario where miss-management seems so apparent in terms of the driver of financial distress, it is difficult to make a plausible argument that the situation of the Company in 2013 was caused principally by external environmental factors and that management had a passive role to play in events leading up to the crisis in December 2013.

Nevertheless, in my experience both environmental and organisational factors often have an impact on organisational failure and each scenario is somewhat fact specific. In general, we should not discount the industrial organisation and organisation ecology side of the debate around organisational failure[[2]](#footnote-2) as environmental factors can be a critical cause of business failure even if they were not overly apparent in the Case Study. Both internal and external factors can be contributory to organisational failure and there is a danger of overly focusing on either side of the scholarly debate, as these factors rarely operate in isolation.

To my mind, the proposed integrative framework theorised by Mellahi & Wilkinson[[3]](#footnote-3) is a useful conceptual framework to depict how external and internal environments interact, resulting in organisational failure.

Certainly, in the Case Study scenario, the balance tips towards the internal factors as the main cause of failure however it is easy to see how in others scenarios the opposite may be true, for example where a perfectly competent management team is faced by a fundamental external environment shift such as say government legislative changes, technical innovations or a global pandemic, which lead to financial distress and potentially failure.

1. **What are in general advantages and disadvantages of an out-of-court restructuring (workout) as compared to a formal bankruptcy procedure? More specific, what are the advantages versus disadvantages in your country?**

Out-of-court restructurings can broadly be defined as any informal reorganisation outside of a formal legal framework. Conversely, formal bankruptcy procedures are undertaken in accordance with specific statutory requirements prescribed therein[[4]](#footnote-4).

Formal bankruptcy procedures vary from jurisdiction to jurisdiction and there are different processes applicable within each of those jurisdictions, dependent on the facts of the case. Not all bankruptcy procedures are focused on business restructuring and survival the most obvious being a liquidation process. In the Cayman Islands the Companies Act (2023 Revised) (the “Act”) provides for both a company restructuring under the "Restructuring Officer Regime" (Section 91A-91J of the Act) as well as "Official Liquidations" (Section 104-110 of the Act).

For the purpose of this question, I have focused on a comparison between the advantages and disadvantages of an informal out-of-court reorganisation as opposed to a formal reorganisation under the "Restructuring Officer Regime" in the Cayman Islands.

Fundamentally, the assumption is that the key advantage of any reorganisation (be it formal or informal), is that it will return a better value to stakeholders in comparison to a formal bankruptcy (liquidation) process. This logic is underpinned by the idea that the going concern enterprise value of the business exceeds the liquidation value of its individual assets.

**Informal restructuring/reorganisation process**

In regard to the core question of the relative advantages and disadvantages of an informal reorganisation vs a formal reorganisation - these can be somewhat circular. Principally, the informal process benefits from its relative flexibility, silence and control[[5]](#footnote-5). From a Cayman Islands perspective, such informal out-of-court restructuring options would be available to debtors and creditors.

There are distinct advantages in certain scenarios to the flexible nature of an informal process, allowing for creative solutions to be developed with stakeholders. For example, it allows companies and their creditors to negotiate and agree on the terms of a restructuring, including any conditions necessary to their positions, by mutual consent. This removes the requirement for the terms of a reorganisation to align with any pre-conditions which are set in a formal bankruptcy process, such as a minimum write down of debt by compromising creditors. I would tend to agree with Adriaanse, J.A.A., & Kuijl, J.G. that the possibilities of an informal reorganisation are far broader and that this flexibility is advantageous.

Adriaanse, J.A.A., & Kuijl, J.G. argue that informal processes also benefits from a relative lack of publicity when compared to a formal court process. They cite the public nature of in court restructuring procedures leading to suppliers and financiers as well as clients approaching the company with a degree of reserve and an unwillingness to enter new contracts[[6]](#footnote-6), all of which can be value destroying and detrimental to the prospects of a successful restructuring. Ultimately, a public process may prompt creditors to protect their positions and result in a "race to collect",[[7]](#footnote-7) leading to liquidation petitions and or secured creditors potentially looking to realise their security.

Whilst there is logic to the argument that an informal restructuring benefits from a lesser risk of publicity, ultimately any restructuring will require consultation with key stakeholders in order to be successful, hence the development of initiatives like the Statement of Principles for a Global Approach to Multi-Creditor Workouts II[[8]](#footnote-8) which aim to facilitate consultation between the debtor and key creditors.

Consequently, the advantage of a lesser risk of publicity can be overstated, given the need for consensual buy in from key stakeholders in an informal reorganisation. From a practical perspective, there is always likely to be a risk of a "race to collect" occurring when reorganization plans are disclosed to key stakeholders. The lack of a moratorium in an informal process is a key disadvantage in this regard (assuming that a standstill agreement has not been reached between the debtor and creditors, albeit again at the outset the financial plight of the debtor will need to be disclosed before any informal standstill agreement is reached).

From a company perspective an informal process has the added advantage of leaving incumbent management fully in control of the process, allowing them to independently run the company without oversight from the Court, trustee or in the Cayman Islands a Restructuring Officer. There are consequentially material cost savings which would typically result from an informal process, particularly in the Cayman Islands.

**Formal restructuring/reorganisation in the Cayman Islands**

In the Cayman Islands, the Restructuring Officer Regime allows a fairly flexible arrangement to be negotiated between the company and its creditors. There is no "statutory percentage" requirement i.e. there is no set "percentage of debt" that must be waived by ordinary creditors as part of a scheme of arrangement.

The Restructuring Officer Regime contains provisions for the imposition of a moratorium from the point at which an application is filed for the appointment of a Restructuring Officer, with the Grand Court of the Cayman Islands [[9]](#footnote-9). The moratorium provides (among other things): (i) breathing space for the company and the appointed restructuring officer to develop a viable restructuring plan; and (ii) a degree of protection from enforcement action from any disgruntled unsecured creditors. It is noted that, similarly to the winding up of a company, the moratorium imposed under the Restructuring Office Regime has no impact on a secured creditor (whether the security is over the whole or part of the assets of a company) and they are entitled to enforce this security without the leave of the Grand Court.

The Regime provides that a subject company may make an application for the appointment of a restructuring officer: (i) *ex parte* (i.e. without notice); and (ii) for the appointment of that restructuring officer on an interim basis, pending the hearing of the petition.[[10]](#footnote-10) Notwithstanding this, it should not be seen as a “silent” process. In the event that the Grand Court makes an order appointing an interim restructuring officer, the Grand Court is required to set out the manner and timeframe in which such notice should be given to creditors, including contingent creditors or prospective creditors and the company’s contributories[[11]](#footnote-11).

This more public approach may be a disadvantage in some scenarios, given that all creditors will be put on notice of the financial position of the company and, in turn, this might impact their appetite to trade with the subject company. However, this particular disadvantage is often outweighed by the benefits and protection afforded by the moratorium and automatic stay on all claims against the debtor, which it brings upon filing.

Key suppliers and creditors would, in most circumstances, need to be on notice of any informal restructuring in any event owing to their strategic importance to the company and likely levels of debt owed, devaluing the theoretic merits of a silent informal process. The exception to this argument would be in situations where the informal restructuring was limited to financial creditors only leaving trade creditors unaffected and therefore potentially not requiring consultation in regards to the financial plight of the company and its required restructuring.

The Restructuring Officer Regime gives the court discretion to prescribe the powers of the restructuring officer in the appointment order. This includes the manner and extent to which such powers will modify the function of the board of directors[[12]](#footnote-12). As such, there is at least scope within the Cayman Islands formal legislation for a degree of management control to remain with the incumbent directors and officers of the company, and so the advantage of an informal process may be less significant in this regard, albeit the formal process will inevitably remain a costly process even if the court limits the restructuring officers role.

One additional benefit of a formal restructuring over an informal route is there may be provisions in the formal restructuring legislation which allow dissenting minorities to be compromised as a class where there is general support amongst the class for a compromise arrangement (i.e a scheme of arrangement). This can significantly increase the prospects of achieving a successful restructuring and reduce the risk that dissenting creditors obstruct an otherwise fair and realistic restructuring plan. In comparison, an informal restructuring will require consent from all stakeholders in a compromise scenario irrespective of their relative position.

Certain jurisdictions, such as the EU, under the Directive on Preventive Restructuring Framework, have adopted further provisions to allow for the so called "cross class cram down of creditors", where certain conditions are met[[13]](#footnote-13).

Under the Cayman Islands legislation, where the statutory voting threshold has been met and the Court has sanctioned a scheme, it will be binding on all affected stakeholders within the same class regardless of whether or not they voted in favor or not. The threshold per the Act is 75% in value of those voting (in person or by proxy) in each class to approve a proposed scheme. There is currently no cross-class cram down enshrined in Cayman Islands legislation[[14]](#footnote-14).

**Conclusion**

From my perspective, both informal and formal processes have their advantages and disadvantages both in general and in relation to a Cayman Islands Restructuring Officer regime. Again each scenario will require a case-specific assessment of what is the more favorable route for a company to take.

Often, the critical factor will be the degree to which non co-operative stakeholders might seek to disrupt the process or have the ability to do so. In Cayman specifically, I would conclude that from a cost and flexibility perspective the informal process has clear advantages to the appointment of a restructuring officer. However, in reality, the need for the protection of a moratorium will in many circumstances necessitate a more formal restructuring option is advantageous or at least provides more certainty within which a viable restructuring proposal can be developed.

1. **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.**

*Adriaanse & Kuijl, 2006,*

This article examines informal reorganisations with reference to both a Dutch and Russian Federation perspective. Adriaanse & Kuijl identify two processes which make up an informal reorganisation 1) business restructuring and 2) financial restructuring. Business restructuring is further broken down between Stabalising, Analysing, Repositioning and Reinforcing.

Taking each in turn, the four phases of business restructuring have been applied to varying degrees in the Case Study, as follows:

Stabalising – relates to critical factors which require immediate action to stabalise a distressed situation, with an emphasis on cash flow. The underlying aim of this phase of a restructuring is to prevent a further downwards spiral and stop further cash leakage from the company. This strategy can be seen clearly in the plans put forward by Flow Management in December 2013, in particular, the agreement to price rises with key customers, making 130 staff redundant and identifying other extra savings in the business. Each of these steps are intended to boost short-term cash flow and cut losses in the immediate term.

Analysing – the development of a credible reorganisation plan, which demonstrates that value can be created for stakeholders, alongside a restoration of long-term profitability. As the restructuring continued into 2014, plans were produced by Flow Management in or around March 2014, which looked at measures identified by Adriaanse & Kuijl as being important to the restoration of long term profitability. This included increasing turnover and cutting back costs, evaluating the business mix and divesting of non-core businesses outside of the Benelux. The engagement of a CRO (Chief Restructuring Officer) is also a good example of the practical steps which might be undertaken in the "Analysing" phase, as the restructuring starts to focus on longer term plans to turnaround operations and profitability.

Repositioning - involves the implementation of the restructuring plan developed in the Analysis phase. This includes the reporting of financial results and the impact of the restructuring plan to interested parties in a timely manner to restore confidence in the Company and it’s restructuring.

In this Case Study it seems the "Repositioning" phase of the restructuring was undermined by the continued deterioration in the financial position of the Flow Management (the “Company”) and worsening of the trading performance in the period which went against the financial projections which had been relayed to stakeholders in previous stages of the restructuring. As such it is clear from the Case Study that confidence in the restructuring and viability of the business in general deteriorated during this phase, as can be seen by the attitudes of Banks C & D during 2014.

Reinforcing –bolstering both management personnel and the balance sheet as the restructuring continues. In this Case Study the transfer of the operating entities to a new “clean” shell in July 2015, is a good illustration of the reinforcement concept. There are also several changes to the management team, such as the replacement of the CEO which are demonstrable examples of the "Reinforcing" phase of a restructuring, as envisaged by Adriaanse & Kuijl.

Alongside these informal business restructuring phases, Adriaanse & Kuijl also identify that it is often a requirement and indeed a necessity for a financial restructuring to occur in addition to a business restructuring. In many cases, the accumulated losses from the past cannot be removed simply by improving current cash flows (even after a successful business restructuring) and the company will not always be able to clear away the “burden” of the past[[15]](#footnote-15).

Again, demonstrable examples in the case study of financial restructurings designed to bolster the balance sheet and re-capitalise the business include: 1. both shareholders and creditors looking to support the informal restructuring, either with additional capital injections and unsecured loans on behalf of the shareholder, 2. re-terming and extending loan facilities on behalf of the banks, 3. the ultimate agreement by the banks to a partial write-down of their debts and an equity exchange in July 2015.

*Pajunen, 2006,*

This Article provides a theory and a historical case study that illustrates how the most inﬂuential stakeholders can be identiﬁed and managed during organisational survival. One of the central conclusions of the study, is the critical nature of such stakeholder management in an organisations' survival.

In the Case Study, as the restructuring progresses, the failures of Flow Management to adequately communicate and engage with the banks as key stakeholders, adversely impacts the progression of the restructuring. Outside of the management team and shareholders, the banks are the key influential stakeholders and are clearly critical to any successful restructuring occurring. This influence stems from the banks’ ability to provide or limit liquidity alongside their security pledges (assuming they are valid).

The banks critical position in the reorganisation is demonstrated by the outcome of the July 2015 restructuring, which ultimately resulted in the control of the business passing from the historic shareholders to the banks via the transfer of assets to Flow Management Holding II BV.

*Sudarsanam, S, Lai, J., 2001,*

This research examined the frequency, timing and intensity of the use of the prescribed strategies including operational, asset, managerial and financial restructuring in 166 financially distressed UK firms. The conclusions illustrate that recovery and non-recovery firms adopt similar sets of strategies following financial distress, but their strategic choices diverge over time. Recovery firms choose investment and acquisition to improve their position, whereas non-recovery firms are more internally focused on operational and financial restructuring.

The Case Study illustrates some of the common internally focused operational and financial restructuring methods being adopted by Flow Management, which are associated with non-recovery firms. There is limited evidence of Flow Management looking to compliment the internally focused changes with external strategies aimed at leading the business out of difficulty.

The evaluation and reassessment of the product mix in 2014 by Flow Management might be argued to be an external strategy however further details would be needed in the Case Study before any conclusions were reached in this regards.

*Schmitt, A., Raisch, S., 2013*

This paper seeks to clarify the nature of retrenchment and recovery strategies and highlights their dual importance in a successful turnaround. Schmitt and Raisch define "retrenchment" as being a strategy focused on increasing efﬁciency through cost and asset reductions. On the other hand, "recovery" concentrates on improving a ﬁrm’s market position through strategic change. Their theory is that whilst the two strategies appear contradictory, in certain circumstances they are also complementary. Consequently, the integration of the two strategies allows for improved effectiveness in turnaround situations[[16]](#footnote-16).

As highlighted previously, in the Case Study Flow Management’s turnaround plan included clear retrenchment strategies, including the sale of non-core assets (350 cars), non-core business units, redundancies and other cost cutting measures. However, there are limited signs that a dual approach was adopted in the Case Study.

The review of the product range and business mix could be seen as the commencement of a recovery strategy as defined by Schmitt and Raisch. Nevertheless this is a limited example of measures adopted in the Case study which might be seen as focused on a change to something new from an operational perspective and overall the restructuring plan adopted by Flow Management seems to have been heavily influenced by retrenchment as opposed to recovery strategies.

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

It would appear from the Case Study that Banks C & D were originally supportive of the strategy to act jointly and in a controlled manner when the original crisis broke in December 2013. However, by the middle of February 2014 Banks C & D had become frustrated with the process and factions were developing within the banking group (collectively Banks A, B, C & D).

This frustration grew throughout 2014 with the two banks (C & D) threatening to withdraw credit at the end of June 2014. In comparison, Banks A & B were more supportive of the informal restructuring process and exploring consensual restructuring options with the board and shareholders of Flow Management.

The rational for this divergence in thinking within the banking group (Banks A & B vs Banks C & D) was likely driven by the different economics of each bank's individual position, relative to Flow Management (the “Company”), throughout the restructuring process.

The banks each had distinctive individual exposure and obligations to the Company and as a consequence, none was in the same position economically in the event of a business failure scenario. The final financial restructuring, which was agreed in July 2015, highlights the deviation in each banks position. For example, one of the key limbs of the restructuring entailed Banks C & D writing off 100% of the additional working capital facilities which they had provided during the restructuring. In comparison, Banks A & B had either been repaid the additional working capital they had provided or were not obliged to provide such funding under their facilities. In fact, the Case Study explicitly notes the varied outcome for each bank from the July 2015 restructuring was reflective of the relative positions of the financiers involved.

It seems reasonable to therefore conclude the interests of the banking group in the Case Study may not have been entirely aligned given the outcome was seemingly less favorable to Banks C & D. Given the variance in each bank's relative economic position it was arguably rational for Banks C & D to be less supportive of a consensual informal restructuring, in comparison to Banks A & B.

In a restructuring, liquidation and other financial models are developed to allow for creditors to assess their respective positions relative to the debtor and for this to be used to calculate debt-equity and write downs[[17]](#footnote-17). It would be entirely rational for the two banking groups to have entirely differing views and appetites towards progressing the restructuring in a scenario where their obligations and exposures were different.

The uncertainty over the security pledges held by each of the banks and their potential unenforceability, which was discovered at the start of the crisis, would likely also have impacted certain bank's behaviors, by compounding the relative differences between Banks A & B and Banks C & D’s position in the event of a liquidation scenario.

Each financial institution would also have its own internal dynamics which could impact the level of their individual support of a financial restructuring. For example, capital ratios and other local regulations and legislation might have an impact on behaviors and attitudes of financial creditors albeit this is not touched upon in the Case Study materials.

In addition to the economic rationale for a split in attitudes with in the banking group, the importance of credibility and personal relationships between the key stakeholders within a restructuring might impact the level of support for a reorganisation. It is important that restructuring plans are realistic, particularly so because the interested parties, such as financial institutions and other creditors will take decisions on the basis thereof[[18]](#footnote-18).

In the Case Study the ever changing and deteriorating financial picture in 2014 will have brought into question the credibility of the Flow Management board of directors and their ability to develop a viable restructuring plan for the business. With potentially more at risk in comparison to Banks A & B, Banks C & D may have been reluctant to support and fund the management driven and controlled informal restructuring, which was being developed prior to July 2015.

Aside from the understandable economic drivers to the banks' attitudes, the potential for a discounted debt sale might have been a more opportunistic reason for the unconstructive attitude of Banks C & D during the restructuring. Their strategy may have been to delay and frustrate the progression and development of a restructuring plan, in order to provide additional leverage in the negotiations with Banks A & B resulting in the disposal of their positions at a more favorable rate. Had this been successful it might have provided a means for Banks A & B to control the restructuring process absent any dissent from Banks C & D. Albeit this would have meant further exposure and deployment of capital on their behalf in relation to the Flow Management situation and there is insufficient information in the Case Study to appraise the potential merits of this strategy from the perspective of Banks A & B.

**Advice to Banks A & B**

As an advisor to this side of the banking group, I would analyse the financial models in order to appraise the potential price point of a debt purchase. I would also advise Banks A & B to explore the merits of establishing a sub-committee to coordinate their responses to the debtor more effectively and efficiently with Banks C & D.

Professional advisers could have been appointed to the committee and would likely have assisted with aligning the interests of the respective banks by ensuring they were appraising both the restructuring scenarios and liquidation scenarios on a consistent and uniform basis. This would have helped both a debt sale or accelerated the restructuring in general by providing uniform information amongst the banking group upon which decisions and negotiations could be based.

Further, as set out in Principal Four of the Statement of Principles for a Global Approach to Multi-Creditor Workouts II, one of the benefits of a co-ordination committee is it can help resolve disputes or disagreements between the relevant creditors by facilitating discussions among those concerned[[19]](#footnote-19). This is something which would have been practical to implement in this scenario.

Given the inter creditor issues, separate legal advice would typically need to be obtained by the respective banks, however, the main work of information gathering, processing and evaluation could be done as a whole which would reduce the costs to each party and allow for a level of consistency of information amongst the banking group which might assist in facilitating a collective approach to the restructuring[[20]](#footnote-20).

I would also seek to highlight Principal One of the Statement of Principles for a Global Approach to Multi-Creditor Workouts II and the rationale for including all financial creditors within the class regardless of the size and exposure of their facilities. Principal One stresses that even though in a particular case one financial creditor might be less exposed than others and therefore have less interest in any rescue attempt (as may be the case between Banks A & B and Banks C & D), this relative position might be reversed in another case. Financial creditors should, as a matter of principle, be prepared to support other financial creditors’ attempts to rescue businesses unless it is to their commercial disadvantage to do so[[21]](#footnote-21).

1. **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.*

The standstill agreement entered into in August 2014 between the company and four banks provided 120 days for management to draw up sales scenarios and liquidation scenarios. This collective granting of a limited time by all relevant creditors (i.e. the banking group) to allow the company time to obtain and evaluate information for the purpose of developing four proposals for the resolution of the debtors’ financial difficulties. This approach closely follows the First Principal.

Whilst a formal standstill agreement was not reached with Flow Management until August 2014, it is also arguable that throughout the process (commencing in December 2013), the banks co-operated to the extent that they gave the Company time to evaluate the situation and formulate proposals to restructure the business.

***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.*

The withdrawal of the credit facility in June 2014, which was used by Banks C & D as leverage appears contradictory to the Second Principal, because it might have been a precursor to enforcement. As identified in the Second Principal, the continued provision of facilities by relevant creditors is an essential feature of the standstill. In this regard, it appears that the Second Principal was not complied with at this stage of the Case Study.

However, at no point in the processes did any enforcement action occur. When the formal standstill was agreed this would have included an agreement in line with the Second Principal for all relevant creditors not to seek to enforce their claims.

The potential debt sale from Bank C & D, which was explored in the Case Study, would fit within the context of the Second Principal.

Further, it would appear from the final financial restructuring in July 2025 that there were potentially inter-creditor agreements in place given “the contents of the financial restructuring agreement reflect the relative positions of the financiers involved”. This would be reflective of the Second Principal that each creditor’s position relative to each other was not prejudiced by the standstill which proceeded the restructuring.

**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.

It appears that Flow Management were prepared to allow the banks to appoint independent accountants to investigate the company at the outset of the financial crisis in 2013.

Proposals from the company were also provided to the banks as the restructuring progressed and the banks were able to conclude in October 2014 that a going concern scenario was the best outcome. This suggests that the banks as relevant creditors were provided relevant information and time to access the same during the process in accordance with the Fifth Principal.

**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.

Again there is an implied sharing of information with in the banking group within the Case Study which would be applicable to the Seventh Principal.

**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.

Prior to the signing of the restructuring agreement in July 2015, in January 2015 EUR 25m was paid back to providers of (additional) working capital. This implies that such funding had been given priority and was effectively repaid as a pre-condition to the subsequent restructuring in line with the Eighth Principal.

**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?**

The Statement of Principles is perhaps the most well-known and commonly adopted “soft law” framework concerned with assisting and facilitating cooperation between creditors in an out-of-court restructuring scenario. However, it is not the only non-binding set of guidelines which have been developed, and importantly, endorsed by reputable international institutions concerned with the facilitation and improvement of the conditions required to allow for successful restructurings.

It may, therefore, be possible to convince creditors to adopt an alternative framework in order to facilitate the restructuring. The London Approach for example was one of the earliest widely followed out-of-court work out models. Similar to the Statement of Principals which followed, it deals with certain general, non-binding principles describing how creditors should respond with a guiding objective to facilitate the restructuring of viable firms[[22]](#footnote-22).

The main guidelines of the London Approach are:

* Bank creditors should be supportive when they receive information that a borrower is in financial difficulties.
* Decisions about the debtor’s longer-term future should only be made on the basis of comprehensive information that is shared among all bank creditors and other relevant parties.
* Banks should work together to reach a collective view on whether, and if so, on what terms, the debtor should be given a financial lifeline.
* The seniority of claims should be recognized, but there should be equal treatment for all creditors of a single category.[[23]](#footnote-23)

In the last two decades the London Approach in practice in the United Kingdom has been more limited[[24]](#footnote-24) and if a “soft law” alternative framework could not be identified and agreed by creditors it may still be possible to develop an alternative framework unique to a specific situation leveraging the flexibility inherently found within a voluntary informal out of court restructuring process.

Creditors may opt to negotiate their own guidelines to which they agree to be voluntarily bound as opposed to adopting the prescribed non-binding guidelines like the Statement of Principals or London Approach.

In practice this would most likely see separate standstill agreements being reached between the creditor group and the debtor and inter creditor agreements negotiated between the respective creditors. The benefit to this approach is that it can be specifically tailored to the relevant facts and dynamics of a situation and there is opportunity to accommodate specific concerns of key creditors which might increase the prospects of obtaining buy-in from disgruntled creditors and increase the prospect of a successful informal restructuring. Notwithstanding the benefits of this approach, in practice this is likely to be a time consuming and costly process, when compared to the adoption of a pre drafted and internationally endorsed Framework.

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

The 4 July 2015 restructuring agreement (the “Agreement”), was in essence a financial restructuring. Financial restructuring is the reworking of a firm’s capital structure to relieve the strain of interest and debt repayments and is typically separated into two strategies: equity-based and debt-based strategies[[25]](#footnote-25).

In this scenario, the focus of the financial restructuring was primarily directed towards a debt-based strategy. Gilson (1989, 1990) defines debt restructuring as a transaction in which an existing debt is replaced by a new contract, with one or more of the following characteristics: (1) interest or principal reduced; (2) maturity extended; (3) debt-equity swap[[26]](#footnote-26).

The Agreement incorporated both characteristics (1) and (3) of a debt restructuring. It may also have included item (2) in regards to a maturity extension in relation to the surviving working capital facility provided by the banks, although this is not clear on the facts provided. Certainly the subsequent postponement of the refinance from November 2016 to July 2017 would fall into this category.

The implications of the Agreement are illustrated in the diagram below:



With reference to the diagram, the banks along with certain members of the board received shares in New Co, Flow Management Holding II BV (Item 2 of the Agreement) following:

1. the transfer of the all operating subsidiaries to New Co (item 1)
2. the write off of the Banks EUR 55m loan (item 7);
3. waver of the additional working capital provided by Banks C & D (item 5); and
4. cram down of the legacy working capital facility (item 6).

This combined EUR 185m debt write down by the Banks was in exchange for the enterprise value of the Operating Subsidiaries, which were transferred to New Co. as going concerns. This left the Shareholders with ownership of an empty shell company, Flow Management, which was to be liquidated (Item 3).

In order to protect the New Co. and the banks as its shareholders from any potential claims made by the liquidator or Shareholder of Flow Management, the Agreement provided for the cancellation of claims (item 4).

Without this, the Banking Group and New Co may have been at risk of claims made in relation to the transfer of the trading subsidiaries at an undervalue or preference. Similarly, the Agreement contained provisions to protect against claims from New Co. or the Banks against the Shareholder or Flow Management (item 3).

Contractual protection against all claims by all parties (illustrated as a green “claims wall” in the above diagram), forms an essential part of the debt-equity transaction of this financial restructuring, giving each party comfort that that the Agreement will represent a final resolution of the issues. Absent such releases it is unlikely a consensual informal restructuring of this nature would be viable.

The full write off of Banks C & D’s debt and the loans in comparison to a cram down in the legacy working capital facility, suggest that the former two instruments were underwater in all scenarios in relation to this facility, as was the equity.

As outlined above nearly all of the key terms and conditions of the Agreement were aimed at addressing the balance sheet issued caused by the previous 18 months of underperformance and providing liquidity for the business going forwards. Unlike the business restructuring measures which had been implemented prior to the Agreement, the focuses of the restructuring in July 2015 was exclusively aimed at the firm’s capital structure.

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

The United Nations Commission on International Trade Law, *Possible Future Work* states that “Cross-border insolvency is the term frequently used for insolvency cases in which the asset of a debtor are located in two or more States or where foreign creditors are involved[[27]](#footnote-27).

The Flow Management Case Study involves a group structure comprises entities which are incorporated in a number of different jurisdictions, it also includes foreign branches (non-legal entities). The group trades in several jurisdictions including Benelux, France, Spain, UK, South Africa and USA. It also holds majority interests in subsidiaries incorporated in Cayman and Sweden.

As a result, the assets and liabilities of Flow Management which are located across multiple jurisdictions will likely be subject to different and at times competing or self-interested, local (insolvency) laws and legal processes within the jurisdictions in which the group operates and is structured. Any restructuring would therefore need to account for the unique issues faced by a debtor with assets and liabilities which are subject to different local legislations.

For example, in the Case Study 3,000 staff employed by the group will be subject to different local employment legislation and any liabilities to staff members will potentially be awarded varying degrees of priority and protection within either a restructuring or an insolvency scenario depending on the location of the individual creditor.

Historically, national insolvency laws have not kept pace with the global expansion of trade and investment meaning they are often ill-equipped to deal with cases of a cross-border nature. This frequently leads to issues such as inadequate and unharmonious legal approaches which are not conducive to a fair and efficient administration of cross-border insolvencies[[28]](#footnote-28).

Traditionally and absent agreement between the respective jurisdictions in terms of how local insolvency legislation will accommodate a cross-border situation, it has been challenging to conduct orderly and predictable restructuring processes given that the laws and legal processes of one jurisdiction typically have no extra territorial effect.

For example, in the Case Study, sufficient care would need to be taken to ensure that the mutual releases granted as part of the July 2015 restructuring were effective in all jurisdictions in which the claims and assets are situated so as not to fall into the trap of focusing on one jurisdiction, such as the Netherlands where the center of main interest was stated to be located.

These legal issues will be present to varying degrees in most cross-border situations and result in uncertainties, conflict and inefficiencies, which would not ordinarily occur within a domestic restructuring within a single jurisdiction and under one set of insolvency laws and principals binding on the entire structure.

From an insolvency law perspective, the differences in underlying legislation between the location of assets and / or liabilities, also raises fundamental issues of how insolvency proceedings should progress. In the Flow Management restructuring, a formal insolvency process was avoided. Notwithstanding this, the underlying legislation would still be relevant and could have presented difficulties, given the importance of the insolvency scenario modeling (a likely key underlying component to the eventual restructuring in July 2015).

Territorialist principles favour separate insolvency proceedings in the various countries in which assets are located. In contrast, the universalist principal favours a single procedure, grounded in the country in which the head office is located or place of incorporation is situated[[29]](#footnote-29). With the expansion of international trade and cross boarder insolvency issues there has been a general move away from the Territorial approach, which is seen as value destructive and a deterrent to international trade expansion.

UNCITRAL Model Law on Cross-Border Insolvency and the EC Regulation on Insolvency Proceedings 2000 both seek to encourage co-operation and coordination along the universalist principal between jurisdictions when dealing with cross-border restructurings. The earlier “comity” principals which were developed in British Commonwealth countries and the United States of America also aided in making cross-border insolvencies more predictable and transparent between jurisdictions[[30]](#footnote-30).

Nevertheless, despite the development of initiatives to improve the predictability of cross-border restructurings and insolvency processes, there remains no uniform approach. Consequently, multijurisdictional restructurings and insolvencies continue to create complex and unpredictable scenarios Given the fact pattern presented in the Case Study, this would be applicable to Flow Management.

One example of the challenges which persist when dealing with a cross-border restructuring, is the potential lack of clarity regarding the center of main Interest, COMI. This is a key concept in the Model Law and other legislation aimed at improving efficiencies in cross-border situations. Whilst the Model law does not strictly define COMI, Article 16 3 of the Model Law does presume, in the absence of proof to the contrary, that the debtor’s registered office is the debtor’s COMI[[31]](#footnote-31).

In the Case Study, both the operations and registered office are situated in the Netherlands. However, this may not always be the case for other restructuring scenarios leading to further legal and practical issues where jurisdictions have competing claims for COMI and which ought to take the primary role in the context of the various proceedings which might be commenced involving the company. In some instances this may lead to parallel and competing insolvency processes being commenced in separate jurisdictions further adding to the costs and uncertainty which are inherent within a cross-border restructuring process and undermine the prospects of a successful restructuring outcome.

**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]**

The principal benefit of a moratorium is that it provides a reprieve from creditor enforcement actions (which can ultimately lead to an uncontrolled insolvency process and is likely to be value destroying), allowing the management of a distressed company a period of time to explore restructuring options and negotiate terms with key stakeholders in the business. This temporary relief from creditor enforcement action can be a valuable tool when considering restructuring options in a scenario where the liquidation outcome is likely to be worse for stakeholders with an economic interest in the process, in comparison to a restructuring which will preserve the going concern value in whole or in part of the debtors’ enterprise.

In the Case Study, the independent turnaround consultancy concluded that Flow Management had a viable business at the start of the restructuring. Shortly after the October 2014 scenarios the banks also concluded that a going concern situation still remained the best outcome. This indicates that the restructuring presented a more favorable return for stakeholders when compared to the liquidation model.

While certain jurisdictions provide for a statutory moratorium which allows “breathing space” to a debtor before the onset of formal insolvency, in many jurisdictions a statutory moratorium on creditors’ claims is available only as part of a formal insolvency process[[32]](#footnote-32). Under the Cayman Islands Companies Act (2023 Revised) (the “Act”) an automatic moratorium on claims against the debtor is provided for under both the Restructuring Officer Regime (Section 91A-91J) as well as during Official Liquidations (Section 104-110).

Scenario 4 described in the Case Study is akin to a "pre-pack sale" in a UK administration, where the business is sold in a controlled manner under protection of a moratorium via a court process. This is similar to a scheme of arrangement under the Restructuring Officer Regime in Cayman, whereby a more favourable return for creditors is achieved by maintaining the going concern value of the enterprise and avoiding a liquidation or break up scenario.

The moratorium under the Restructuring Officer Regime provides both a statutory framework for a restructuring to occur and protection for the debtor from any disgruntled creditors looking to wind the company up prematurely (particularly before a restructuring proposal can be fully developed).

Applying the Restructuring Officer Regime to the facts of the Case Study, whether it would have been a suitable strategy will turn on the validity of the security pledges held by the principal creditors. The facts presented in the Case Study suggest that the pledges may not have been valid, meaning that the banking creditors would have been classified as ordinary unsecured creditors under the Act.

As noted in the answer to Question 2, the Restructuring Officer Regime explicitly has no impact on a creditor who has security over the whole or part of the assets of a company, and the protection of the moratorium is applicable only to unsecured creditor claims. Consequently, in the event that the bank pledges were invalid, the moratorium obtained under an application for a Restructuring Officer in the Cayman Islands, would arguably have been a good option for Flow Management in October 2014.

Conversely, given that the key creditors in the Case Study were all financial institutions which held security against the debtor, had the security pledges been valid, there would have been good grounds for discounting the Restructuring Officer Regime and associated moratorium. Ultimately if the financial institutions held valid pledges, the Company could not have obtained the relief required, in order to develop a restructuring proposal in the form of an orderly going concern sale.

In addition, the merits of exploring the moratorium option would also depend on the mechanism by which the relief is sought under the applicable local legislation. One feature of the new Restructuring Officer Regime in Cayman is that a winding up application against the company does not need to be made.

This had not been applicable to the pre-2022 legislation in the Cayman Islands, where a winding up petition was required in order to make an application for a restructuring to take place. This could be (and was) a deterrent to debtors looking to facilitate a restructuring given the negative connotations associated with commencing insolvency proceedings and the implications for going concern value. Debtors were often deterred by the prospects of having to either encourage a friendly creditor or for the directors to make a winding up application in order to seek the appointment of provisional liquidators, which prior to the Restructuring Officer Regime, had been the principal formal restructuring legislation in the jurisdiction.

Nevertheless even under the Restructuring Officer Regime there is a requirement for the company to either be or likely to become unable to pay its debts and to petition the Court for relief[[33]](#footnote-33). As such, there is likely to be concerns depending on the options available as to whether seeking the moratorium protection may close off or devalue other restructuring options that might be available at a given time.

At the time the scenarios were being considered in October 2014, there appeared to be other valid options, which might have avoided the costs and value destruction which would follow any formal proceeding necessary to obtain a moratorium. Certainly scenario 1 and 2 might have been derailed by the commencement of a formal restructuring process, even if in Cayman this could be done without the need to file a winding up petition. As such, this might have been a good reason why a moratorium was not pursued more actively at the time.

Scenario 1 involved an extension of the stand still period which would have effectively created a temporary moratorium of 180 days (subject to conditions being met regarding progress of the business restructuring). This scenario may have therefore been seen as more favorable to other options, given that it effectively institutes a moratorium for the business, whilst avoiding the costs of a formal process.

Consequently, seeking a formal moratorium might not have been viewed as a favorable option in early October 2014. In particular, there remained potentially viable scenarios which would have avoided the need for the commencement of a formal (court) process either vial a refinancing (Scenario 1) or sale of the business (Scenario 2).

It was only when revised financials were received at the end of the month that both scenarios 1 and 2 became impracticable and fell behind the debt-equity scenario and formal insolvency process in terms of realistic restructuring options available to Flow Management.

This assessment could have changed at any time and had it been evident in October 2014 that one of the creditors was unsupportive of the restructuring and might look to enforce their position, then this assessment might easily have been reversed in favor of a moratorium (assuming the relief was available given the potentially secured nature of the debt as discussed previously).

Banks C & D were evidently more aggressive in their approach to the restructuring. However, they did have the opportunity to enforce their position prior to the formal standstill agreement signed in August 2014 and did not do so. At the time, therefore, the additional comfort of a moratorium may not have been deemed beneficial in comparison to the downside, given the dissenting banking groups' previous reluctance to enforce their position.

Finally, had the banks wanted to force Scenario 3 onto the debtor without the support of the debtor and it’s shareholder (as is eluded to in the Case Study), they could not have benefited from the moratorium afforded to the company by the Restructuring Officer Regime in Cayman given it does not allow a creditor to file an application to appoint an RO[[34]](#footnote-34).

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