**CASE STUDY 1**

For the purpose of this Case Study response:

* “**Company**” means Flow Management Holding BV.
* “**Group**” means the entities shown in the structure chart on page 1 of the Case Study under Lease Group Holding United Kingdom Ltd..
* “**shareholder**”, unless the context requires otherwise, means Lease Group Holding United Kingdom Ltd..
* “**UBOs**” means the Johnson Family, LLS Private Equity Fund Ltd. and Cinderella Investment Ltd., and any respective shareholders thereof.
* Unless another reference is provided, references to “**Adriaanse and Kuijl**”, “**Mellahi and Wilkson**”, “**Pajunen**” or “**Sudarsanam and Lai**” are references to the respective articles listed on page 9 of the Case Study.

**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?**

***What is financial distress?***

As per Mrs Justice Falk in *Re Sturgeon Central Asia Balanced Fund Ltd (in liquidation)* [2019] EWHC 1215 (Ch): “*It is also wholly unclear how financial distress might be determined, or what the threshold is*.”[[1]](#footnote-2)

Granted, one might reasonably confine Falk J’s observations as being limited to determining the meaning of financial distress in the application of the cross-border recognition of the UNCITRAL Model Law for Cross-Border Insolvency adopted by the UN Commission on International Trade Law on 30 May 1997 (the **Model Law**) as implemented in England and Wales (and Scotland) by the Cross-Border Insolvency Regulations 2006. However, there seems to be a general reticence to seek to provide too rigid a meaning to the concept. Indeed, even the World Bank Institute’s “Resolution of Financial Distress: *An International Perspective on the Design of Bankruptcy Laws,*”[[2]](#footnote-3) does not seek to define financial distress. In their research, Sudarsanam and Lai also acknowledge that there are a range of definitions, some based on change in accounting ratios and others on stock return. They adopted the former definition.[[3]](#footnote-4)

That said, looking at the common use of the phrase (any situation where an individual’s or company’s financial condition leaves them struggling to pay their bills),[[4]](#footnote-5) and even the use of the phrase within the Model Law (“*debtors experiencing severe financial distress or insolvency*”), the concept of “financial distress” can reasonably be considered to be akin to the circumstances that exist when a company “*is or is likely to become unable to pay its debts within the mearing of section 93*” (s91B of the Companies Act (2023 Revision)). In other words, the point at which, if nothing is done, the company can be considered insolvent and at risk of being wound up.

***What financial distress was Flow Management suffering?***

The Institute of Chartered Accountants in England and Wales contends there are six warning signs that a firm is in financial distress and needs to implement recovery measures: (1) cash flow; (2) high interest payments; (3) defaulting on bills; (4) extended debtor or creditor days; (5) falling margins; and (6) unhappiness.[[5]](#footnote-6)

When judged against this criteria, the available factual information arguably indicates that the only signs of financial distress exhibited by December 2013 were (a) falling margins and (b) a negative cash flow. These issues seem most heavily attributed to (i) formula errors; and (ii) accounting treatment. Or put another way, when analyzed in the context of organizational failure, these are problems that arose from internal (or organizational) factors rather than external (or environmental) factors.

Granted, as time went by, the Group started to suffer from additional “warning signs.” However, by that point, it may be difficult to pinpoint whether those triggers were caused by the original failings or poor implementation of the improvement plan. One exception being the issues at subsidiary levels: While the conclusion is drawn (reasonably early) that the business is viable, no attention seems to have been given to identifying in which subsidiary losses were occurring, and whether that was due to a specific market or product lines (i.e. issues that might be occurring because of external factors) or poor management or inefficiencies (i.e.internal factors).

***Internal v external factors***

Mellahi and Wilkinson argue that “*any attempt to explain organizational failure will not be complete unless the interplay between the contextual forces and organizational dynamics is taken into account*.“[[6]](#footnote-7) This seems fair: Nothing, particularly in international business, happens in a vacuum.

At first blush, there is attraction to the organization studies and organizational psychology literature which in essence lays the blame of corporate failings at the door of management. Adriaanse and Kuijl also say that the causes of financial difficulties mainly relate to poor management.[[7]](#footnote-8)

In the case of Flow Management, it would seem fair to say that its problems were indeed mainly attributable to poor management. The work of third parties identified that the business’s issues were not viability but visibility as to what was actually going on within the Group. The fact that the management had not instigated a sufficiently robust system to ensure timely and accurate financial information was being provided to them was a significant and, potentially, the root cause of the key issues.

***Could Flow Management’s problems have been prevented?***

In circumstances where it is concluded that the root causes of the problems were internal rather than external then, yes, prevention seems a possiblity. It is open to management, even those with long tenure, to constantly, and critically, re-evaluate their approach to ensure that they are not slipping into the pitfalls associated with Groupthink Theory, Upper Echelon Theory, Curse of Success and/or Threat Rigidity Effect Theory. Indeed, had management been doing this, the issues at subsidiary level would likely have been identified sooner.

Mellahi and Wilkinson identify that a criticism of the OS/OP perspective is over-reliance on internal factors when considering the causes of failure.[[8]](#footnote-9) However, even if the management had been successful in implementing great strategic maneuvers that navigated external challenges, their lack of oversight as to what was actually happening within the business would always have ultimately led to failure at some point because leadership decisions would be being effected based on incorrect assumptions.

**2. 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?**

Before addressing perceived advantages and disadvantages of out-of-court workouts, it is important to note that it is not possible to compile one objective list. Rather, certain factors and consequences could be perceived as a possible advantage or disadvantage based on an interested party’s perspective and ultimate goal. The below general response is therefore prepared from the perspective of the company/debtor and their management, with the following preliminary points:

* ***Costs***: Significant costs are usually incurred regardless of whether an informal or formal process is undertaken. Some consider that informal processes are more cost effective because there are limited “necessary” costs (e.g. there are no court fees or court mandated payments, more freedom as to the engagement of professional advisors, less risk of being forced to pay third parties’ costs etc.). However, the costs of informal processes can add up, particularly if the debtor is picking up the costs of creditor committees and their representatives. Further, if the informal process fails, the debtor will then likely bear the burden of a formal process as well.
* ***Preservation of market value***: Research conducted by Gilson, John and Land indicates that shareholders tend to see better returns where out of court restructurings take place.[[9]](#footnote-10)

**General advantages for the company and the incumbent management**

Adriaanse and Kuijl posit that the advantages of informal reorganizations can be summed up with the terms “*flexibility, silence and control*”:

* ***Flexibility:*** With stakeholder buy-in (this being the key – and sometimes difficult to attain - element), almost any solution is possible with an out-of-court arrangement.
* ***Silence:*** The relative privacy of out-of-court restructurings enables parties to communicate more freely.
* ***Control:*** The ability of the management to retain control of the business throughout the negotiations and, sometimes, through the restructuring.

Other advantages, some of which are tacitly incorporated Adriaanse and Kuijl’s terms, but which nonetheless warrant separate mention are:

* ***Less stigma / Less negative publicity:*** Bankruptcy filings, winding up petitions, together with ancilliary documents and evidence filed in any court proceedings are (usually) public record, and can be used to generate bad press. Furthermore, there remains a stigma attached to being involved in court proceedings that can be difficult to shake, even if the approach made to the court is to seek assistance to restructure rather than wind down.
* ***Less chance of default being triggered:*** The commencement (or even threat of commencement) of insolvency proceedings (or similar) is often enough to trigger default or acceleration procedures in respect of debt that would not otherwise be due in the short term. Subject to the scope of these clauses, out of court negotiations will usually not trigger them.

**General disadvantages for the company and the incumbent management**

* ***(Usually) no moratorium during negotiations:*** Therefore, while debts remain unpaid or covenants are breached in any financing agreements, a company remains at imminent threat of enforcement action from a disgruntled creditor.
* ***Requires consensus amongst all stakeholders – which can be difficult to achieve:*** Unlike court procedures, which can usually force a variation to existing legal rights with only a majority (or other stipulated percentage) approval of a relevant class of creditors, consensual workouts require the agreement of all of those affected. This can be problematic, not only in terms of winning over hearts and minds, but also practically in ensuring there are timely and meaningful communications with all relevant stakeholders.
* ***Non-binding*:** Whatever progress is made during negotiations; the benefits are unlikely to be realized until a deal has been finalised.
* ***Limited legal protection:*** Particularly in a cross-border scenario, there is usually no protection that steps taken without court sanction cannot be unwound. If a stakeholder can show prejudice to their, or the debtor’s position, or an actionable preference (under the relevant law), there are real risks that arrangements can be unwound and the individual actors run the risk that personal action is taken against them. For example, in the Cayman Islands, pre-insolvency transactions can be challenged if they constitute a voidable preference, a disposition at an undervalue, fraudulent trading; or a fraudulent disposition.
* ***Little control over what information makes its way into the public domain:*** If a debtor has a large stakeholder group (for example, a listed company, or a publicly traded bond), it can be difficult to balance the need to be transparent with any desire to ensure potentially damaging information does not make it into the public domain. Even with the use of confidentiality agreements, with a large stakeholder body, it can be practically difficult to ensure that information remains confidential.

**The Cayman Islands regime**

The vast majority of the general advantages and disadvantages outlined above apply to considerations of whether to pursue a formal or informal process in the Cayman Islands.

One of the primary challenges faced by debtors in trouble in Cayman has been that they cannot obtain a moratorium, even to put in place a scheme of arrangement, without first presenting a winding up petition. This frequently caused issues with cross-default provisions on financing arrangements. To help alleviate this issue, last year, a new restructuring officer regime was introduced which allows a company (but not any other stakeholder) to present a restructuring officer petition.[[10]](#footnote-11) Benefits of this regime include the protection of a moratorium upon presentation of the petition (albeit secured debts remain enforceable) and the ability for the management to remain in place throughout the restructuring process (a so called “debtor in possession regime”). Although it is yet to be tested, the new regime also purports to enable the compromise of foreign debt (i.e. to side step the rule in *Gibbs*). It remains to be seen whether this will be effective. Furthermore, there is no cross-class cram down in the Cayman Islands, which can provide a reasonable amount of power to dissenting creditors.

**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.**

One thing is clear from the reading material: There is no “one size fits all” solution to the issue of corporate turnarounds. As identified in the academic works, there are various factors that lead to corporate demise. Consequently, there are myriad factors – both internal and external – that contribute to whether a successful turnaround can be achieved. That said, there are some common themes indicating that certain steps, if applied thoughtfully (including as regards timing) can increase the likelihood of success. For the most part it seems as though the Company, and its advisors, sought to implement the various techniques identified in the research, but it is more doubtful that these steps were implemented effectively and in a timely manner.

Adriaanse & Kuijl identify that most restructuring processes consist of stabilizing, analyzing, repositioning and reinforcing. These phases need not be sequential, but a necessary early step is to identify the critical problems which require immediate action, with a view to increasing cash flow.[[11]](#footnote-12) In the case of the Group, the obvious issue they had was the inadvertent underpricing (and therefore a lower than necessary cash flow). Immediate actions were taken to rectify this, by renegotiating with customers and implementing spending cuts.

The Company then undertook an analysis of the causes of the problems and compiled projections and calculations for the future (essentially, phase 2). This was embarked upon with the assistance of third-party professionals. An important part of this phase should have been reinforcing or reinstating the confidence of stakeholders. However, it is apparent this was not done as well as it could have been:

* The failure to produce reliable data about past activities or to accurately project revenue for the coming months led to the Banks doubting the management and the long-term viability of the Group. Further, while it is apparent that there was some engagement with the shareholder, it is not clear that sufficient action was taken to ensure their engagement with the process. In particular, given that the shareholder was likely little more than a shell company, more traction would likely have been gained if there had been direct engagement with the UBOs. As per Pajunen’s research regarding stakeholder influence on organizational survival a possible failing in the Flow Management process was the seeming inability to recognise / utilize the potential importance of shareholder and its UBOs. Adriaanse and Kuijl consider that whether a rescue operation will be successful depends upon: (1) the active attitude and involvement of the key stakeholders, including transparency; (2) speed and adequacy of the reorganization of the operations; and (3) the injunction of risk-bearing capital.[[12]](#footnote-13) By failing to engage with the shareholder / UBOs, the Company made it much more difficult to obtain risk-bearing capital in a timely manner.
* One strategy that may not have been fully explored by the Company is the benefits that could have been obtained from conducting a more significant asset restructuring, or doing so earlier. The Group appears to have operations around much of Europe, the United States, Australia and South Africa. While there will be global factors which affect all of these markets, there are also likely to be local factors (for example, tax changes, political influences) that affect the viability of the business model in each of these markets. The “foreign subsidiaries” were identified at one point has having made losses of €6.3 million. Ideally further analysis would have been undertaken to identify which of the subsidiaries was failing and why.

Sudarasanam and Lai’s research (regarding conditions for a successful turnaround) identifies the range of turnaround strategies as: managerial restructuring, operational restructuring, asset restructuring and financial restructuring.

Although the Company ultimately implemented a debt for equity swap, Sudarasanam and Lai’s research indicates that when considering the necessary changes to be made during a restructuring, a financial restructuring is the least necessary for ensuring success.[[13]](#footnote-14) Rather, the key component is a managerial restructuring.[[14]](#footnote-15) And the Company did indeed implement management changes reasonably early in the process (albeit, arguably, these changes could have been made even sooner).

The Company also undertook an operational restructuring (one of the other routes to turnaround identified by Sudarasanam and Lai) by its cost reductions (redundancies), revenue generation (re-negotiations with suppliers) and operating asset reduction strategies (selling surplus stock).[[15]](#footnote-16) Again, these changes were implemented, necessarily, reasonably early in the process.

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

It is possible that Banks C and D were frustrating the process with a view to creating sufficient pressure to persuade the Group to pay down their debt, or at least, part of the debt. That said, in some jurisdictions, such conduct, even if it achieves its aim, can be risky because any repayment might end up being susceptible to legal challenge.

It is also possible that for internal risk management and/or compliance and/or internal target reasons, the Banks were prepared to take a haircut on their debt repayment in return for obtaining the money in the short term.

Less likely, although still a possibility, was that Banks C and D were being uncooperative in the negotiations as a strategy for coercing the shareholder and/or the UBOs into cooperating / providing the requested capital injection. The possible rationale being that if formal insolvency procedures were instigated, the shareholder (and the UBOs) would likely not receive any return. Whereas, by injecting further capital there was a possibility of retaining (and increasing) the value of their investment.

As the other Banks’ advisor one would:

1. Likely question whether Banks C and D had access to additional information that was causing them objectively to reach a different view on the viability of any restructuring, and seek to obtain any other information not available to one’s own clients.
2. Seek to find a way to ensure that the creditor position was united in the negotiations with the Company and the shareholders / UBOs. This could include considering with one’s own clients:
   1. Whether to buy out the debt of Banks C and D, or whether to broker a deal for a third-party (or shareholder) purchase of the debt.
   2. Seeking to change the negotiation structure so that communications with the Company (or its shareholder and UBOs) are funneled through a coordinator, and only once a consensus position has been reached amongst the Banks.

**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)?**

Adriaanse and Kuijl succinctly described the eight principles as:[[16]](#footnote-17)

1. Deferment of payment is voluntarily agreed to (‘standstill period’ by creditors);
2. The debtor ensures that the relative positions of the creditors are maintained;
3. The debtor refrains from any action that may jeopardize the proceeds for the creditors;
4. Creditor committees are set up, if so required;
5. The debtor provides the creditors with relevant information;
6. Reorganization proposals are made in the light of the applicable law;
7. The parties treat all information confidentially;
8. New financing during the process will be given priority status.

In one way or another, each of these principles was attempted during the Flow Management process (save, arguably, for principle 4). The real point of interest is the extent to which these attempts were effective, or effectively deployed at the most appropriate time, so as to achieve maximum beneficial effect. Or, as put in the commentary: “*Most importantly, time is crucial in resources and works. When a debtor is experiencing financial difficulties, delay prolongs commercial uncertainty, increases the costs of the process and potentially erodes value.*”[[17]](#footnote-18)

**Principle 1: Deferment of payment is voluntarily agreed to (‘standstill period’ by creditors)**

Key aims of this principle are (a) to give the Company/debtor some breathing space; and (b) to ensure that all relevant creditors are brought into the process.

There is no evidence that the Company has significant or relevant creditors beyond the four Banks that the Company met with on 16 November 2013 (albeit, in terms of key stakeholders with influence, the shareholder, management and, potentially, the UBOs and lead employees / client liaisons at key operating subsidiaries, are also relevant). By at least December 2013, the Company already has the turnaround consultant’s report concluding that the business is viable and that the estimated turnovers are realistic. It is around this period that there is evidence of discussion regarding entering into a standstill agreement (**SA**). However, it is not until mid-August 2014, that an SA is eventually entered into.

Given that a key purpose of the standstill period is to enable creditors to obtain and evaluate information about the debtor, it might have been better had the SA been entered into before the end of 2013. This could have assisted in the Company being more transparent in its dealings with the Banks and should have prevented Banks C and D from acting in the way that they did during early 2014.

**Principle 2: The debtor ensures that the relative positions of the creditors are maintained**

A key purpose of this principle is to ensure that no single creditor takes action for their own benefit or purpose while the parties are trying to seek a consensual way forward. This principle protects both the debtor (comfort that their attempts are not being undermined) and the creditors (comfort that their interests are not being prejudiced while good faith negotiations continue for the benefit of all).

Each of the Banks refrained from taking any steps to enforce their claims during the standstill period. However, in the period prior to the SA, it is arguable that Banks C and D were breaching this principle. This again lends support to the proposition that the SA may have been more effective had it been entered into earlier.

That said, even before the SA was entered into, the Banks were essentially operating a moratorium on their claims (as referred to on page 13 of the Statement of Principles II). The fact that the Banks’ reticence to take action was linked to concerns regarding the enforceability of their security does not diminish the fact that the benefits sought to be derived by adherence to this principle were nonetheless being obtained.

**Principle 3: The debtor refrains from any action that may jeopardize the proceeds for the creditors**

This principle is basically the other side of the coin to principle 2. Here, the focus is on the debtor not taking any destructive action.

Assuming that the sale of surplus assets around October 2014 was completed at market value, there is no evidence to suggest that this principle was not adhered to.

**Principle 4: Creditor committees are set up, if so required**

The underlying rationale to this principle appears to be efficient and cost-effective communication and negotiation been the debtor and the different classes of creditors.

For the Group, there are a limited number of creditors, all of whom are sophisticated operators. On one view, and certainly from the creditors’ perspective, there was initially limited benefit in appointing a co-ordinator, given the associated costs and the need to agree arrangements regarding the operation of any committee and limitations on the liability of the co‑ordinator. However, from the Company’s perspective, there may have been benefits in there being a co‑ordinator (subject to costs). This could have enabled the co-ordinator to deal with the brunt of the disagreement between the Banks, and to seek to find a consensual position before presenting that view to the Company. Further, the benefit to the creditors would have been (a) ensuring that their position was presented to the Company as a united front; and (b) allowing the Company the time to focus on identifying the causes of the issues and coming up with solutions, rather than having to spend the time and resources on negotiating with the separate creditor positions.

**Principle 5: The debtor provides the creditors with relevant information**

This is an important principle to ensure that creditors are properly able to assess their position and make an informed decision as to whether to support the debtor’s proposals or whether to ultimately revert to enforcing their rights through formal processes.

It is clear from the Case Study that the Banks were displeased with the provision of information to them.[[18]](#footnote-19) However, the poor information flow / changing information appears to be a consequence of management’s own lack of understanding of the situation rather than through any intentional limitation on the flow of information to the creditors.

Potentially the situation could have been improved if the accounting firm investigating the procedures within the Group, or the turnaround consultants had been appointed by the creditors rather than the Company. However, in reality, if the root cause was the Group’s own systemic and entrenched failings in the way in which it was operating, there would be little/no material difference in the throughflow of information to the creditors based solely on whose appointee was undertaking the investigative work.

**Principle 6: Reorganization proposals are made in the light of the applicable law**

This principle seems in essence to be an extension of principle 5, but instead of the focus being simply on the provision of necessary information, the key purposes are to ensure that (a) proposals being made reflect the realities of the legal frameworks within which the parties are operating; and (b) in the event a compromise is reached, the parties (both debtor and creditor) are properly apprised of any concessions that they would be making under the turnaround proposals.

The Case Study does not provide explicit confirmation that this principle was adhered to. To assess this, it would be necessary to understand details regarding the structure of the debt and the security, and the rights that might be available to debtors and creditors in each of the jurisdictions in which the Group companies were incorporated and/or were operated and/or under the applicable law of the contracts. However, given that the Company had engaged relevant professionals, and the Banks would have been analyzing and assessing their options, it seems reasonable to conclude that this principle must have been adhered to.

It is possible that there might be a different analysis for the shareholders albeit, in the vast majority of jurisdictions, shareholder protection is not a consideration in workout scenarios.

**Principle 7: The parties treat all information confidentially**

The purpose of this principle appears to be twofold: (a) to achieve parity between stakeholders; and (b) protection of the company’s information, so as to encourage the sharing of all necessary and relevant information.

In most cases, tensions will arise in the application of this principle, particularly if (i) the debtor is publicly listed and trading is continuing; or (ii) a creditor is a trade competitor of the debtor.

In the Case Study, while there are few indicators of explicit adherence to this principle, it seems likely that due to the few creditors and their (likely) equal sophistication and experience, that this principle was implicitly adhered to.

**Principle 8: New financing during the process will be given priority status**

The rationale for this principle appears to a desire to balance (a) a need to reasonably justify the injection of additional cash so as to avoid prejudicing existing creditors in the event that a turnaround is not possible; with (b) a need to incentivize the possible lender / investor to provide funds to a distressed situation, if such funding is considered necessary.

The fact that (i) option 1 in the October 2014 scenarios suggested providing security for any further shareholder contribution; and (ii) some security was provided for the additional working capital; shows that the parties were alive to this principle and were essentially acting in accordance with it.

The ultimate turnaround package did not need to utilize this tool – presumably because the relevant parties reached the view that, in the circumstances, additional funding in exchange for further subordination of rights was a less preferable outcome to a reduction in the Group’s liabilities.

**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?**

As per Shelton, D:[[19]](#footnote-20)

“*Soft law is a type of social rather than legal norm. While there is no accepted definition of “soft law,” it usually refers to any written international instrument, other than a treaty, containing principles, norms, standards, or other statements of expected behavior. Soft law “expresses a preference and not an obligation that state should act, or should refrain from acting, in a specified manner.” (Gold 1996: 301). This “expressed preference” for certain behavior aims to achieve functional cooperation among states to reach international goals (Lichtenstein 2001: 1433).*”

In addition to INSOL’s Statement of Principles, other “soft laws” include:[[20]](#footnote-21)

* European Communication and Cooperation Guidelines for Cross-border Insolvency[[21]](#footnote-22)
* The World Bank’s Principles for Effective Insolvency and Creditor/Debtor Regimes[[22]](#footnote-23)
* The United Nations Commission on International Trade Law (**UNCITRAL**) Model Laws on Cross-Border Insolvency and/or on Enterprise Group Insolvency[[23]](#footnote-24)
* the American Law Institute (**ALI**) - International Insolvency Institute (**III**) Global Principles for Cooperation in International Insolvency Cases[[24]](#footnote-25)
* The Judicial Insolvency Networks’ (**JIN**) Guidelines[[25]](#footnote-26)
* The so-called “Recofa” guidelines, developed in the Netherlands.[[26]](#footnote-27)

These guidelines and protocols arguably derive from different “categories” of standard setting organisations.[[27]](#footnote-28) However, due to the fact that soft law is not, by its very nature, binding, such classification has little relevance save to the extent that it might affect the parties or a court or government’s willingness to pay heed to the propositions.

In contrast to INSOL’s Statement of Principles, the primary focus of the vast majority of other soft laws relate to court-to-court communications and cooperation in cross-border insolvency and restructuring proceedings.[[28]](#footnote-29) True, certain principles or guidelines will likely be of relevance to any attempted turnaround situation, but are the parties really going to be seeking to pick and choose principles as part of what are essentially commerical negotiations? The consequence of this is that, at best, these other soft laws are of tangential relevance to debtors and creditors seeking to negotiate a consensual work out.

Furthermore, even if other soft laws (or even the INSOL Statement of Principles) were utilized by the parties, the issue would remain that soft laws are - by their very nature – not binding.[[29]](#footnote-30) Therefore, if it were ever necessary for a party to seek assistance from a court, that court would likely pay heed only to the law which is binding in its jurisdiction and would not see compliance with soft law as sufficient if that law conflicted with relevant binding law.

In circumstances where the route chosen by the parties necessarily requires consensus (ie an agreed workout), it follows that it is not hugely problematic that there is no rigid framework that applies to their negotiations. This could, for example, be compared to *ad hoc* arbitrations: There is (or, at least, in the early days, there was) no explicit rule book that set out the procedure to be followed, but guided by the overriding agreement/goal of having their dispute resolved through arbitration, the parties found a way through.

What is more important is that no parties unknowingly agree to, or take a step, that would put them in significant legal difficulties in a particular jurisdiction. Such problems can be avoided by engaging suitably qualified professionals to assist.

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

The process undertaken by the Group and its stakeholders combined a legal restructuring (making use of existing laws to change the organizational structure and reduce debt) with a spin‑off.

The restructuring agreement spins out the viable business into a new structure that is owned by the Banks and the management (the **New Shareholders**). This is a reasonably tried and tested methodology in restructurings. This process will likely be undertaken by inserting the new company, Flow Management Holding BV II BV (**New Co**), as a 100% subsidiary of the Company and transferring the shares of each of the Company’s six subsidiaries (the **Op Cos**) to the New Co before transferring ownership of the New Co to the New Shareholders.

It may be that the arrangements are structured such that the transfer of shares to the New Shareholders is treated as consideration for the compromise of the Company’s various debts to the Banks (ie the waivers of the working capital). This is known as a debt-for-equity swap. Alternatively, the parties will use a court sanctioned scheme of arrangement to confirm the transaction to minimize the risk that it can subsequently be challenged.

Following the reorganization:

* The New Co is the holding company of what is supposedly a viable operation. The Banks/Consortium extend new working capital to the New Co concurrently with the transfer of the shares. Assuming all goes to plan, the New Co will be sold on by the Banks in a reasonably short amount of time so that the Banks can in effect realise the return of the money that they originally lent to the Company.
* Assuming that all of the employees needed to operate the ongoing businesswere employed by the operating subsidiaries, the change of ownership in those companies should have no impact on their employment.
* The shareholder will continue to hold its shares in Lease Cayman Real Estate Ltd. and Lease Truck Repair Sweden Holding Ltd. (the **Remain Cos**). If the Op Cos had contractual arrangements with the Remain Cos, those agreements will remain in place and should continue to be honoured. If the arrangements between the Remain Cos and the Op Cos had been operating on an informal basis, it will be important for the New Co to ensure these arrangements are formalized (to the extent they are key to the continuing success of the operations).
* The Company will no longer own the Op Cos, but it will still have any cash that it had in its bank account(s). The plan envisages that these monies will be paid out to the providers of the original working capital under pre-existing pledges. A decision will need to be made as to whether payment can / should be made under the pledges prior to the Company commencing the liquidation process, or whether it will afford both the Company’s directors and the relevant creditors greater protection if this payment is made within a court supervised insolvency process.

In the event, it appears that the New Co’s operations did not perform as well as expected in the short term (albeit this under performance may well be linked to the difficulties with valuing assets, particularly in a restructuring situation – see Broekema and Adriaanse[[30]](#footnote-31)). However, the lenders of the working capital postponed the refinancing to provide a window for the New Co to produce anticipated good results, with a view to ensuring that the proposed sale can still take place.

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

For the purpose of this question, the “restructuring process” is understood to be the arrangement entered into on 4 July 2023.

The Company will likely want to commence proceedings in the jurisdiction of its choosing, ideally one that mitigates the risk of the restructuring agreement being derailed by some of the issues identified below.

An analysis will likely need to be undertaken to determine where the “centre of main interests” (**COMI**) lies. Assuming the Company’s registered office is in the Netherlands, and given that it will have no subsidiaries at the time of entering into the insolvency process, COMI will likely be the Netherlands, which would make the Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (recast)*[[31]](#footnote-32)* applicable. However, the analysis need not end there, and there may be options for the main proceedings to be commenced outside of Europe.

Historically several states within the United States have been considered reasonably debtor friendly[[32]](#footnote-33) and, even without significant trading history or creditor base in the US, it is usually possible to persuade the Court to take jurisdiction over a bankruptcy even if it was not the principle place of a company or its group’s operations (albeit with the caveat that US Chapter 11 proceedings are notoriously expensive). In fact, most jurisdictions have mechanisms to enable the winding up a company incorporated outside of that country, though few accept jurisdiction so easily as the United States.[[33]](#footnote-34)

In most jurisdictions, it is not only the Company that has standing to apply for its liquidation. Usually, anyone who stands to make any recovery for the process is able to apply. Therefore, if a creditor considers that it might obtain a better return under a specific regime, they might apply for the winding-up/liquidation/bankruptcy proceedings to be commenced in that jurisdiction. It can then become a race between the Company and a determined creditor to obtain a winding-up/liquidation order in the jurisdiction that they consider to be most favourable to them.

Further, under most insolvency regimes, the management no longer retain control of the company. Rather, it is usually an independent professional who ultimately reports to the Court. Ordinarily, both the company and stakeholders will have an opportunity to say who they would prefer to be appointed, and it can lead to disagreement.

Depending upon the jurisdiction in which the Company enters formal insolvency proceedings, it is possible that:

* the repayment of the €25 million in January 2015 and/or any priority payment of the pledges could be set aside and/or clawed back.[[34]](#footnote-35)
* anti-deprivation (or similar) principles may apply to invalidate the transfer of the New Co.
* the Company’s attempts to waive the claims against the New Co and the Op Cos may be considered invalid and a liquidator could be free to pursue perceived viable claims against those entities.
* the purported waiver of the claims against the Company may not be considered valid, leaving the Banks and the shareholder with the possibility of pursuing any claims they consider to be viable (with the intention of increasing their share of any payout in the eventual liquidation).
* the pledges may not be considered valid or sufficient to permit the providers of the original working capital to be paid out ahead of other creditors; and all creditors may instead be paid out *parri passu.*
* domestic creditors may be treated more preferentially than foreign creditors.
* the liquidators’ authority to act on behalf of the Company may not automatically be recognised in a jurisdiction in which they wish to take action. It may therefore be necessary to obtain recognition and/or instigate ancillary proceedings and/or navigate the sometimes-intractable difficulties of trying to reconcile incompatible laws of several jurisdictions.
* even once a winding-up/liquidation order has been granted in one country, a creditor may still attempt to take action in another country (even if there is a purported world-wide claims moratorium).

**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]**

As described by Jennifer Payne, “*Moratoria are traditionally regarded as having two benefits. The first is to deal with the ‘common pool’ problem. If there is no stay, then creditors may seize assets that are useful for the carrying on of the debtor’s business and this could jeopardise the prospects of a successful restructuring. … The second is that a moratorium can deal with the ‘anti-commons’ problem, ie it can block actions by individual creditors who are seeking to frustrate the wishes of the majority. While moratoria can be potentially very valuable in promoting the rescue of a company or business, a balance is required between the benefits to the company and the creditors as a whole on the one hand and the rights of the individual creditors on the other.*”[[35]](#footnote-36)

In practice, this usually means providing the debtor with an opportunity to overcome temporary liquidity problems and/or to propose a settlement to its creditors.

Informal moratoria can be achieved through contractual arrangements i.e. standstill agreements. However, such mechanisms are often considered inferior to court mandated moratoria. In Flow Management a standstill agreement was utilized, to good effect to enable the October 2014 strategies to be put together without risk of a single creditor taking action. However, it seems unlikely that subsequently seeking a formal moratorium in late 2014 was going to be particularly beneficial – not least because in many regimes available at that time, moratoria were rarely available in support of restructurings (as opposed to liquidations / winding-ups).

**The Cayman Islands regime**

Back in 2014, there would likely have been severe risks associated with seeking a formal moratorium. For example, take the Cayman Islands regime[[36]](#footnote-37) as it was back then:

* A moratorium could only be obtained when a winding up order had been made or if a provisional liquidator was appointed (section 97(1) of the Companies Act (2023 Revision) (**CA**)).[[37]](#footnote-38) The moratorium purports to have extra-territorial effect[[38]](#footnote-39) (albeit the effectiveness of this remains in question). However, it would not apply to prevent the enforcement of security rights (section 142(1) of the CA), either in Cayman or another jurisdiction. The priority of competing security interests was (and remains) fact-specific and depends on the nature of the security interest granted and the lex situs of the underlying asset subject to the interest.
* A moratorium would not apply even if a scheme of arrangement had been applied for, unless a provisional liquidator was first appointed.
* To obtain a moratorium, it was necessary to first present a winding-up petition (even for the appointment of a provisional liquidator). The step of presenting the petition often triggered default provisions in financing arrangements, thereby potentially putting the Company in a worse position.

In 2022, the restructuring officer regime was implemented in Cayman. This now enables a company to apply for the appointment of a restructuring officer to assist with the presentation to creditors of a restructuring plan and the implementation thereof. Importantly, this regime imposes a moratorium upon presentation of the restructuring officer (**RO**) petition (section 91G(1) of the CA), providing a debtor with immediate protection. There is no time limit on the moratorium save that it ceases when the RO is no longer appointed. A moratorium imposed under the restructuring regime still carves out the enforcement of security rights (section 91H of the CA).

In circumstances where much of the Group’s assets were pledged, a formal moratorium (at least one obtained in Cayman) would therefore have little to no value, whether in 2014 or if the same scenario existed today.

Even if the security was found to be unenforceable, a moratorium which could only be obtained following commencement of formal insolvency proceedings (as was the case in 2014) was likely to be of little value to a company that wanted to effect a sale in a “controlled” manner, as the commencement of the winding up proceedings would likely have been value destructive.

**Recent developments in other jurisdictions**[[39]](#footnote-40)

In the context of the Company, a Dutch company, it is worth mentioning the “de Wet homologatie onderhands akkoord ter voorkoming van faillissement” (or, the **WHOA**). The WHOA is a scheme that came into force on 1 January 2021 which provides a mechanism for the Dutch court to sanction “private compositions to avoid bankruptcy.” It does not provide for an automatic moratorium, but a company may request the court to grant a moratorium against individual enforcement actions by creditors, including filings for involuntary bankruptcy or for a suspension of payments, for a maximum period of four months (with a possibility to extend for another four months). The court will grant a moratorium if it *prima facie* appears that: (a) the moratorium is necessary for the continuation of the business of the company during the preparation of and the negotiations in relation with the composition; (b) the moratorium is within the joint interest of the creditors of the company; and (c) the moratorium is not materially detrimental to the interests of any of the creditors whose interests are affected by the moratorium. It is possible for the Dutch court to attach conditions to the moratorium.

The Netherlands were not alone in implementing such reforms in the wake of COVID. Following the amendments to the EU Directive on restructuring and insolvency, some member states (and the United Kingdom) have adopted new norms on moratoria.

**\*\*\*\*\* END \*\*\*\*\***

1. Available at [High Court Judgment Template (uncitral.org)](http://www.uncitral.org/docs/clout/GBR/GBR_170519_FT.pdf) [↑](#footnote-ref-2)
2. [www.citeseerx.ist.psu.edu/document?repid=rep1&type=pdf&doi=4382862e2ba4c34de4b64b7944f4556c0eeb800c](http://www.citeseerx.ist.psu.edu/document?repid=rep1&type=pdf&doi=4382862e2ba4c34de4b64b7944f4556c0eeb800c), accessed 22 November 2023. [↑](#footnote-ref-3)
3. # And as quoted by Briggs J in Re Sturgeon Central Asia Balanced Fund Ltd (in liquidation) Carter v Bailey and another (as foreign representatives of Sturgeon Central Asia Balanced Fund Ltd) *[2020] EWHC 123 (Ch)* in his review of her judgment

   [↑](#footnote-ref-4)
4. CFI Team, “Financial Distress”, [www.corporatefinanceinstitute.com/resources/commercial-lending/financial-distress/](http://www.corporatefinanceinstitute.com/resources/commercial-lending/financial-distress/), accessed 22 November 2023. [↑](#footnote-ref-5)
5. ICAEW, “Six signs that a business is in distress”, <https://www.icaew.com/regulation/insolvency/understanding-business-restructuring-and-insolvency/six-signs-that-a-business-is-in-distress>, accessed 22 November 2023. [↑](#footnote-ref-6)
6. Page 34. [↑](#footnote-ref-7)
7. “*i.e., inadequate reaction of management of both internal weaknesses and strengths, even as external threats and opportunities – and excessive costs structures (fixed and variable costs), 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 by management).*” [↑](#footnote-ref-8)
8. Page 31. [↑](#footnote-ref-9)
9. Referenced on page 147 and footnote 25 of Adriaanse and Kuijl. [↑](#footnote-ref-10)
10. Sections 91A to J of the Companies Act (2023 Revision), with consequential amendments also made to the Companies Winding Up Rules (2023 Consolidation). [↑](#footnote-ref-11)
11. Page 140. [↑](#footnote-ref-12)
12. Page 149. [↑](#footnote-ref-13)
13. Page 187. [↑](#footnote-ref-14)
14. Page 184. [↑](#footnote-ref-15)
15. Page 185. [↑](#footnote-ref-16)
16. Their summary was in respect of the first iteration of the Statement of Principles, but these core concepts are reflected in iteration II published in 2017. [↑](#footnote-ref-17)
17. Page 5 of Statement of Principles II. [↑](#footnote-ref-18)
18. See page 6 of Case Study I, first unnumbered paragraph “*Although the provision of information has improved, the banks are at that moment disappointed with the progress of the reorganisation*”. [↑](#footnote-ref-19)
19. Dinah L. Shelton, Soft Law in HANDBOOK OF INTERNATIONAL LAW (Routledge Press, 2008), page 3. [↑](#footnote-ref-20)
20. Further examples are provided at section 4 (on pages 8 – 10 of 20) of Wessels, Bob and Boon, Gert-Jan, Soft Law Instruments in Restructuring and Insolvency Law: Exploring Its Rise and Impact (February 1, 2019). Tijdschrift voor vennootschapsrecht, rechtspersonenrecht en ondernemingsbestuur 2019-2, Available for download at SSRN: <https://ssrn.com/abstract=3397874>, accessed 23 November 2023. [↑](#footnote-ref-21)
21. The report can be downloaded following this link, which appears to derive from the INSOL website: [google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=&ved=2ahUKEwiW94K0qduCAxWuW0EAHS-ACS8QFnoECBYQAQ&url=https%3A%2F%2Fwww.insol-europe.org%2Fdownload%2Fdocuments%2F1113&usg=AOvVaw393w3-P5HowlGRptx\_QImu&opi=89978449](https://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=&ved=2ahUKEwiW94K0qduCAxWuW0EAHS-ACS8QFnoECBYQAQ&url=https%3A%2F%2Fwww.insol-europe.org%2Fdownload%2Fdocuments%2F1113&usg=AOvVaw393w3-P5HowlGRptx_QImu&opi=89978449) [↑](#footnote-ref-22)
22. <https://documents1.worldbank.org/curated/en/518861467086038847/pdf/106399-WP-REVISED-PUBLIC-ICR-Principle-Final-Hyperlinks-revised-Latest.pdf>, accessed 23 November 2023. [↑](#footnote-ref-23)
23. [www.uncitral.un.org/en/content/working-group-v-insolvency-law](http://www.uncitral.un.org/en/content/working-group-v-insolvency-law), accessed 23 November 2023. [↑](#footnote-ref-24)
24. [www.iiiglobal.org/file.cfm/159/docs/ALI-III%20Global%20Principles%20booklet\_0.pdf](http://www.iiiglobal.org/file.cfm/159/docs/ALI-III%20Global%20Principles%20booklet_0.pdf), accessed 23 November 2023. [↑](#footnote-ref-25)
25. [www.jin-global.org/jin-guidelines.html](http://www.jin-global.org/jin-guidelines.html), accessed 23 November 2023. [↑](#footnote-ref-26)
26. Reference to these guidelines are made in the Insol Europe Survey Insolvency Regulation in the Netherlands 2016 and Bob Wessel’s blog “2022-11-doc4 Towards a review of the Dutch IP profession”, [www.bobwessels.nl/blog/2022-11-doc4-towards-a-review-of-the-dutch-ip-profession/](http://www.bobwessels.nl/blog/2022-11-doc4-towards-a-review-of-the-dutch-ip-profession/), accessed 23 November 2023. [↑](#footnote-ref-27)
27. Wessels and Boon suggest that the institutions can be separated into (1) International intergovernmental standard-setting organization (e.g. UNCITRAL and World Bank); (2) other global, regional and local standard-setting organisations (such as INSOL, III, ALI and the European Legal Institute); and (3) informal standard setters (for example, Working Groups for CoCo Guidelines): See slides from their presentation at the TvOB Conference on 9 May 2019, [EU PRIVATE INT’L INSOLVENCY LAW FRAMEWORK (uitgeverijparis.nl)](https://www.uitgeverijparis.nl/documenten/tvob_sym_19/wessels_2019-05_final_-_presentation_tvob_soft_law_instruments_in_restructuring_and_insolvency.pdf), accessed 23 November 2023. [↑](#footnote-ref-28)
28. As put by Casasola, O and Madaus: “*Protocols are a practical attempt to adapt the scopes of national insolvency law to the global dimension of businesses in distress. They function as a bridge between jurisdictions in order to overcome issues of coordination and communication between insolvency proceedings that are opened in different countries and involve the same debtor or corporate group*.” – See page 2 ofCasasola, O and Madaus, S (2022) Cross-border Insolvency Protocols: Cooperation, Coordination, and Communication Duties under the European Insolvency Regulation Recast. European Business Law Review, 33 (6). pp. 839- 880, available at [www.eprints.whiterose.ac.uk/193385/1/Cross-border%20Insolvency%20Protocols%20-%20Casasola%20Madaus%20-%20author%20manuscript%20.pdf](http://www.eprints.whiterose.ac.uk/193385/1/Cross-border%20Insolvency%20Protocols%20-%20Casasola%20Madaus%20-%20author%20manuscript%20.pdf), and referring to Fabian Andreas Van de Ven, The Cross-Border Insolvency Protocol; What Is It and What Is in It? From a European Union Perspective [www.academia.edu/15056737/The\_Cross\_Border\_Insolvency\_Protocol\_what\_is\_it\_and\_what\_is\_in\_it\_From\_a\_European\_Union\_Perspective](http://www.academia.edu/15056737/The_Cross_Border_Insolvency_Protocol_what_is_it_and_what_is_in_it_From_a_European_Union_Perspective). [↑](#footnote-ref-29)
29. In some countries, some of these (and other) guidelines are elevated beyond “soft law,” and have in fact been incorporated – in whole or in part - as legally binding. Examples include:

    * The adoption of the JIN Guidelines. See their website for countries which have adopted the guidelines. These include The District Court Midden-Nederland, certain US states, the Cayman Islands and myriad other common law territories.
    * The UNCITRAL Model Laws, which have been adopted in whole, or in part, in many jurisdictions across the globe.

    However, at the point of incorporation into local law, it is no longer appropriate to term them “soft law”. [↑](#footnote-ref-30)
30. Broekema M.J.R. & Adriaanse J.A.A. (2022), Valuation Ambiguities under the European Directive on Preventive Restructuring Frameworks: Insights from the Netherlands, The European Business Valuation Magazine 1(1): 4-10 [↑](#footnote-ref-31)
31. [EUR-Lex - 32015R0848 - EN - EUR-Lex (europa.eu)](https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32015R0848), accessed 24 November 2023. [↑](#footnote-ref-32)
32. Texas, Delaware, Southern District of New York, to name a few. [↑](#footnote-ref-33)
33. For example, the Grand Court of the Cayman Islands has jurisdiction to wind up a company incorporated outside of the Cayman Islands if the company (i) has property located in the Cayman Islands; (ii) is carrying on business in the Cayman Islands; (iii) is the general partner of a limited partnership; or (iv) is registered as a foreign company in the Cayman Islands. See section 91 of the Companies Act (2023 Revision). [↑](#footnote-ref-34)
34. There is an interesting discussion at Chapter 6 of the Rescue of Business in Insolvency Law produced by the European Law Institute in 2017 (from page 276 of the pdf) comparing claw-back and safe harbour rules across various European (and former European) regimes, <https://www.europeanlawinstitute.eu/fileadmin/user_upload/p_eli/Publications/Instrument_INSOLVENCY.pdf>, accessed 23 November 2023. [↑](#footnote-ref-35)
35. J. Payne, The UK Restructuring Moratorium, 26 January 2021, <https://blogs.law.ox.ac.uk/business-law-blog/blog/2021/01/uk-restructuring-moratorium>, accessed 22 November 2023. [↑](#footnote-ref-36)
36. For the purpose of this discussion, the focus is solely on moratoria in respect of civil claims, although it is noted that a stay can be sought of any criminal proceedings against the Company – see section 97(1A). [↑](#footnote-ref-37)
37. “*When a winding up order is made or a provisional liquidator is appointed, no suit, action or other proceedings, other than criminal proceedings, shall be proceeded with or commenced against the company except with the leave of the Court and subject to such terms as the Court may impose.*” [↑](#footnote-ref-38)
38. *Re Madison Niche Opportunities* FSD 35 and 36 of 2015 (ASCJ), unreported, 30 May 2016 and *Re Ardent Harmony* FSD 54 of 2016 (ASCJ), unreported, 31 May 2016*.* [↑](#footnote-ref-39)
39. Articles reviewed; each of which was accessed and/or downloaded on 23 or 24 November 2023: Prof. Reinhard Bork, Pre-insolvency moratoria – a legal comparison, European Insolvency and Restructuring Journal Academic Article EIRJ 2021-9, [Restructuring & Insolvency Laws and Regulations Report 2023 Netherlands (iclg.com)](https://iclg.com/practice-areas/restructuring-and-insolvency-laws-and-regulations/netherlands); [dutch-scheme-of-arrangement.pdf (loyensloeff.com)](https://www.loyensloeff.com/dutch-scheme-of-arrangement.pdf); [The UK Restructuring Moratorium | Oxford Law Blogs](https://blogs.law.ox.ac.uk/business-law-blog/blog/2021/01/uk-restructuring-moratorium); [a-guide-to-restructuring-and-insolvency-procedures-in-europe.pdf (cliffordchance.com)](https://www.cliffordchance.com/content/dam/cliffordchance/briefings/2019/07/a-guide-to-restructuring-and-insolvency-procedures-in-europe.pdf); [UK Corporate Insolvency And Governance Bill | DLA Piper](https://www.dlapiper.com/en-gb/insights/publications/2020/09/uk-corporate-insolvency-and-governance-bill); and [2022-11-doc4 Towards a review of the Dutch IP profession - Prof. Dr. Bob Wessels](https://bobwessels.nl/blog/2022-11-doc4-towards-a-review-of-the-dutch-ip-profession/). [↑](#footnote-ref-40)