AMERICAN BANKRUPTCY INSTITUTE

2021 Caribbean Virtual Insolvency Symposium

Welcome and Judicial Round & Round

Hon. Gerardo A. Carlo-Altieri (ret.)
GACarlo & Assocts. | San Juan

Hon. Marvin Isgur
U.S. Bankruptcy Court (S.D. Tex.) | Houston

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U.S. Bankruptcy Court (S.D. Fla.) | Miami

AMERICAN BANKRUPTCY INSTITUTE

2020 Virtual Winter Leadership Conference

Peace Bridge, or Bridge of Sighs: Cross-Border Mediation of Insolvency-Related Disputes

Presented by the Mediation and International Committees

Jacob A. Esher
MWI-CBI | Boston

Hon. Barbara J. Houser
U.S. Bankruptcy Court (N.D. Tex.) | Dallas

Kyle J. Ortiz
Togut, Segal & Segal LLP | New York

E. Patrick Shea
Gowling WLG International Ltd. | Toronto

Dr. Annerose Tashiro
Schultze & Braun GmbH | Achern, Germany

Simon Thomas
Goodwin Procter LLP | London

CONCURRENT SESSION

2020

Peace Bridge or Bridge of Sighs: *Cross-Border Mediation of Insolvency Related Disputes*

December 3, 2020 at 4:15 – 5:30 p.m. E.T.

AMERICAN BANKRUPTCY INSTITUTE
Winter Leadership Conference.
3 - 4 December 2020

Panelists
Patrick Shea – Gowling, Toronto [Moderator]
Simon Thomas – Godwin Proctor, London
Annerose Tashiro – Schultze Braun, Frankfurt
Kyle Ortiz – Togut, Segal & Segal, New York, NY
Hon. Barbara Houser – U.S. Bankruptcy Court for the Northern District of Texas
Jack Esher – CBInsolvency, LLC, Boston, MA

2020 VIRTUAL WINTER LEADERSHIP CONFERENCE

Co-Sponsors: Mediation Committee
International Committee

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Title: *Peace Bridge or Bridge of Sighs*: *Cross-Border Mediation of Insolvency Related Disputes*

Program Blurb:

The negotiation of a successful restructuring is always challenging. Even when all constituencies are convinced of the benefits of a restructuring vs. a liquidation (which is not always the case), each constituency has its own goals and agenda. These factors are complicated in cross-border restructurings because of both "hard" or "legal" and "cultural" or "soft" differences. Over the last several years, mediation has become more and more prevalent in helping parties to a restructuring bridge the gap. In the United States, mediation is commonplace in bankruptcy cases, being used to resolve issues ranging from claims allowance to complex multi-party plan dispositive disputes. Mediation has also gained ground in the resolution of insolvency disputes in other jurisdictions around the world. As the global insolvency community has started to recognize the advantages of attempting a restructuring over immediately defaulting to a liquidation scenario, the use of mediation to resolve insolvency disputes or the hybrid med/arb process has become more prevalent. The use of mediation in cross-border insolvency cases has also gained credibility through recent pronouncements of the European Union and UNCITRAL, as well as the development and implementation of the Singapore Convention and the JIN Guidelines. Through a mock mediation, the panel of experienced judges and cross-border mediators and practitioners from various jurisdictions will illustrate the pitfalls and benefits of using mediation to resolve cross-border insolvency disputes. Panelists will also discuss how mediation morphed during the COVID-19 pandemic from a face to face system, to a virtual one through Zoom and other teleconferencing technologies.

Panel Hypothetical

Global Manufacturing, Inc. is a holding company incorporated in Delaware with its principal place of business in Dallas, Texas. Global's corporate officers and senior management, legal and accounting departments and consolidated purchasing operations are all located in Dallas.

Global has three operating subsidiaries: Wild North, Corp. located in Toronto, Canada, Westminster plc located in Manchester, UK and Rhine AG located in Frankfurt, Germany. Each of these entities manufactures goods which are sold globally. Each has its own employees and senior management.

Global Manufacturing has a senior secured credit facility with Mega Bank, guaranteed by Wild North, Westminster and Rhine, each of which has been the primary recipient of the loan proceeds.

While Wild North, Westminster and Rhine each nominally contract for their own raw materials and supplies, purchasing is actually done on a consolidated basis through Global in Dallas, enabling the companies to negotiate better pricing.

Global has filed for bankruptcy in the United States, along with its three foreign subsidiaries. Additionally, Wild North has filed a proceeding pursuant to the Companies' Creditor Arrangement Act ("CCAA") in Toronto, Westminster has filed a Company Scheme of Arrangement in London and Rhine has filed a proceeding under the German Insolvency Act in Frankfurt.

After numerous hearings before the applicable courts and numerous communications between the presiding judges, a cross-border protocol was developed pursuant to which, among other things, it was agreed that the determination of which entity was liable for which unsecured supplier claims would be determined in the United States.

After a hotly contested hearing at which creditors from around the world were permitted to express their objections and concerns, the U.S. Bankruptcy Court presiding over the cases has referred the supplier claims to mediation. The Hon. Barbara Houser, another sitting Bankruptcy Judge, has been appointed the mediator.

While customarily it is the parties who develop the mediation procedures without the input of the mediator, in this case, because of the number of foreign creditors who did business with Wild North and Rhine who are not familiar with mediation, a pre-mediation conference has been convened with the parties and the mediator to develop the parameters and procedures for the mediation.

MEDIATION OF INSOLVENCY-RELATED MATTERS IN THE UNITED STATES

How is mediation used in Chapter 11 cases in the U.S.

- Distinct matters such as claim objections, preference litigation and other types of contested matters where a large amount is at stake or there are a large number of similar cases where the court establishes a process that includes mediation (which is mandatory) as part of the resolution procedure to minimize the number of matters that go to trial
    - Such mediation is usually court-ordered and a mandatory part of the process
    - Sometimes it is the parties who seek it out
    - Some courts are very receptive to using this procedure (SDNY); some courts are not – not because they are opposed to mediation but because they will not order parties to do it (SD TX)
    - Effectively used in *Lehman* case for both mortgage indemnification claims and derivative swap claims, where massive numbers of lawsuits were filed, there were issues of law that were identical for each despite factual differences, and it would have been impossible to try every case.
    - These are usually two party disputes.
- Dispositive Issues relating to plan formation or to resolve an issue that would be highly contested and could impact confirmation of a plan. Used in *Adelphia* and *Tailored Brands* to resolve contested issues on asset distribution and valuation which could have significantly impacted or even scuttled confirmation.
- The Mediation Process
    - Picking the mediator
    - Getting parties to accept it as a dispute resolution method
    - Conflicts
    - Confidentiality
    - Good faith
    - Enforcement of agreement (cross-border component)
    - Styles

MEDIATION IN CANADIAN INSOLVENCY

E Patrick Shea, LSM, CS
Gowling WLG, Toronto, Ontario, Canada

Introduction. The adoption of a structured process that permits parties the opportunity to consensually resolve disputes with the assistance of a neutral third party can, in appropriate circumstances, increase the efficiency and reduce the cost of insolvency proceedings. This is important where time and money are at a premium. Mediation will not, of course, always be successful and litigation may be necessary to resolve disputes. The allocation dispute in the cross-border insolvency of Nortel Networks Inc. is an example of a situation where a mediated settlement was not possible, and litigation was necessary. While not an example of a successful mediation, Nortel is an example of the financial impact on stakeholder recoveries of the failure of parties to reach a negotiated settlement[1]. Even where mediation is not successful at resolving a dispute, it can narrow the issues that must be resolved through litigation[2].

This paper will, in a summary fashion, explore the opportunities that exists for mediation in Canadian insolvency proceedings and the jurisdictional basis for courts in Canada to facilitate mediation in the domestic and cross-border insolvency context. Examples will be provided of specific circumstances in which mediation has been used both successfully and unsuccessfully to resolve disputes with the objective of increasing the efficiency and reducing the costs of insolvency proceedings for the benefit of stakeholders.

Canadian Insolvency Regime. The Canadian insolvency regime is centered around two pieces of Federal legislation, the *Bankruptcy and Insolvency Act*[3] and the *Companies' Creditors Arrangement Act*[4]. The BIA provides for the both the liquidation–through bankruptcy–and the reorganization of insolvent corporations and individuals. The CCAA, on the other hand, provides only for the reorganization of insolvent corporations or corporate groups that have debt in excess of $5 million[5].

Under the BIA, both liquidations and reorganizations take place with a relatively small degree of court intervention. The Act contains extensive provisions that deal with almost all of the matters involved in the liquidation or reorganization of a debtor including the criteria for commencing proceedings, the administration of the estate once a proceeding has been commenced, the rights of the secured and unsecured creditors of the debtor, the procedures for proving claims, priorities among the various creditors, and the augmentation of the estate. The CCAA stands in stark contrast to the BIA. The original CCAA—which was enacted in the mid-1930's—provided only a framework for the debtor's reorganization and left many of the matters codified in the BIA to be dealt with by the court on a case-by-case basis. The CCAA has been amended and expanded over the years, but the manner in which a CCAA reorganization is administered is still determined to a very large extent by the courts, although in many instances the court supervising a CCAA proceeding is called upon to approve or sanction negotiated resolutions rather than resolve

[1] See *Nortel Networks Corporation (Re)*, 2017 ONSC 673 (CanLII).
[2] See *4519922 Canada Inc. (Re)*, 2015 ONSC 124 (CanLII).
[3] R.S.C. 1985, c. B-3 (the "**BIA**").
[4] R.S.C. 1985, c. C-36 (the "**CCAA**").
[5] CCAA, s. 3(1).

disputes.

Courts and Jurisdiction. There is no stand-alone "bankruptcy" or "insolvency" court in Canada. Both the BIA and the CCAA assign jurisdiction to the Superior Courts in each of the provinces[6]. The BIA provides that the specified courts in each of the provinces are "invested with such jurisdiction at law and in equity as will enable them to exercise original, auxiliary and ancillary jurisdiction in bankruptcy and in other proceedings authorized by this Act..."[7]. The CCAA provides the court supervising a proceeding under the Act with extremely broad jurisdiction. Section 11 of the CCAA provides:

> *11. Despite anything in the Bankruptcy and Insolvency Act or the Winding-up and Restructuring Act, if an application is made under this Act in respect of a debtor company, the court, on the application of any person interested in the matter, may, subject to the restrictions set out in this Act, on notice to any other person or without notice as it may see fit, make any order that it considers appropriate in the circumstances.*[8]

In terms of procedure, the BIA and the regulations promulgated under the BIA–the *Bankruptcy and Insolvency Act General Rules*[9]–contain fairly extensive procedures that are applicable where proceedings are commenced under the BIA. Where, however, the BIA and the General Rules are silent with respect to procedural matters, the ordinary court procedures applicable in the province where the proceeding is taking place apply[10]. The CCAA, by way of contract, does include detailed procedures applicable to proceedings under the Act and the rules of civil procedure in the province where the proceeding is commenced are applicable. As a result, there tends to be more procedural variation across Canada in CCAA proceedings than in BIA proceedings.

In many provinces, panels of Judges have been established to deal with insolvency matters. In 1991, the Commercial List was created in the Toronto Region for the hearing of actions, applications and motions involving commercial matters, including insolvency. The objective of the Commercial List is, in essence, to increase the efficiency and reduce the cost of insolvency proceedings for the benefit of all stakeholders. To this end, the Commercial List Practice Direction specifically refers to the use of mediation and others forms of alternative dispute resolution:

> *It shall be the duty of the case management judge and the obligation of counsel to explore methods to resolve the contested issues between the parties, including the resort to ADR, at the case conferences and on whatever other occasions it may be fitting to do so.*

On the Commercial List pre-trial conferences with a Judge are generally required in significant matters with a view to narrowing the issues that are to be determined. A common aspect of these pre-trial conferences is judicial mediation.

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[6] BIA, ss. 2 "court" and 183, and CCAA, s. 2(1) "courts".
[7] BIA, s. 183(1).
[8] CCAA, s. 11.
[9] C.R.C. c. 368. (the "**General Rules**")
[10] General Rules, s. 3.

Mediation by Proposal Trustee/Monitor. Under both the BIA and the CCAA, a licensed insolvency practitioner must be appointed to oversee the reorganization. Under the BIA the practitioner is referred to as a "Proposal Trustee" and under the CCAA the practitioner is referred to as a "Monitor". While there are a number of specific functions assigned to the Proposal Trustee and the Monitor[11], in practical application the specific role played by the Proposal Trustee or the Monitor in a reorganization varies from case-to-case. It is, however, common for the Proposal Trustee or Monitor to participate in the development of the plan and for the Monitor or Proposal Trustee to act as a *de facto* mediator to facilitate the consensual resolution of disputes between the debtor and stakeholders with respect to the contents of the plan and other issues[12]. The Proposal Trustee or Monitor acts as an Officer of the Court and is required to be neutral as between the various stakeholders and is well-suited to mediate disputes arising in the proceeding.

Use of Mediation in Canadian Insolvency Proceedings. Parties to disputes that arise during the course of proceedings under the CCAA or the BIA may elect to use mediation to resolve their disputes. In the CCAA reorganization of Essar Steel Algoma Inc. a dispute arose between Essar Steel and Cliffs Mining Company with respect to the supply by Cliffs Mining of iron ore pellets. A pre-filing dispute between Essar Steel and Cliffs Mining had led to litigation and the purported termination by Cliffs Mining of a long-term supply contract. The litigation and termination of the supply contract were instrumental in Essar Steel's decision to commence insolvency proceedings. Subsequent to commencing proceedings under the CCAA, Essar Steel and Cliffs Mining reached a mediated resolution to reinstate the supply agreement. The mediated settlement was approved by the court[13]. In the Alberta reorganization of Poseidon Concepts Corp., for example, an order was made approving a mediation process to address claims relating to the review, audit and restatement of the debtor's financial statements in an attempt to advance the reorganization[14]. Unfortunately, the mediation was not successful.

There are some specific issues that arise in Canadian insolvency proceedings that are particularly suited for judicial or extra-judicial mediation:

> **Assignment of agreements.** The BIA and the CCAA both provide for the forced assignment of agreements and require as a condition of any assignment that all monetary defaults be cured by a date to be specified by the court[15]. Mediation can assist the parties in reaching agreement on the quantum of the monetary defaults as well as how and when they will be "cured".
>
> **Supply arrangement.** Where reorganization proceedings are commenced, the expectation is that the debtor will operate on a cash-on-delivery basis. Suppliers are not obliged to

[11] See BIA, ss. 50(5)-(10) and CCAA, s. 23.
[12] See BIA, s. 50.5. The form of Model or Template Initial Order used in Ontario provides the Monitor with the ability to "advise the Applicant in its development of the Plan and any amendments to the Plan".
[13] See *Essar Steel Algoma Inc.(Re)*, 2017 ONSC 12 (CanLII). See also discussion in *Canadian Red Cross Society / Société Canadienne de la Croix Rouge, (Re)*, 2000 CanLII 22488 (ON SC) relating to the use of mediation/arbitration to resolve pension-related issues in the CCAA proceeding.
[14] See attached **Appendix A**. See also See *4519922 Canada Inc. (Re)*, 2015 ONSC 124 (CanLII) where mediation narrowed the issues and permitted the development of a term sheet outlining a plan.
[15] BIA, ss. 84.1 and 66, and CCAA, s. 11.3(4). The BIA and the CCAA also provide for the disclaimer of agreements: BIA, ss. 65.11 and 65.2, and CCAA, s. 32.

provide credit to the debtor and can demand immediate payment in cash for goods and services supplied to the debtor[16]. This can strain the debtor's cash flow and it is common practice for the debtor to attempt negotiate to arrangements with its suppliers and mediation can also be employed to address going-forward supply issues.

Retail insolvencies. In the retail insolvency context, the key dispute that typically arises in Canada is as between the landlord(s) and the other stakeholders. The landlord wishes to preserve its broader interests and, in many cases, protect the interests of other tenants in the premises. The other stakeholders typically want to maximize the value of the debtor's assets, including the lease(s). This requires a balancing of the rights of the landlords and the rights of the debtor. The legal issues are typically well defined and understood and mediation can be employed to assist the parties in reaching a mutually agreeable resolution that balances their respective interests in a timelier manner than litigation.

Labour Relations Matters. The BIA and the CCAA do not permit a reorganizing debtor to disclaim or modify a collective agreement. Where a debtor requires amendments to a collective agreement as part of a reorganization, the debtor may apply to the court for an order authorizing the debtor to serve a notice to bargain notwithstanding that the collective agreement has not expired[17]. The court does not, however, have jurisdiction to amend a collective agreement at the request of the debtor (or the union).

The legislation applicable to the collective agreement will typically provide for the use of alternate dispute resolution to reach a collective agreement. In Ontario, the *Labour Relations Act, 1995* provides for the appointment by the Ministry of Labour of a Conciliation Officer or Conciliation Board to assist the parties to negotiate a collective agreement[18]. The Act also provides for the appointment of a mediator by the Ministry of Labour[19].

Mediation has been employed by the Court to resolve pre-filing grievances where the employees of a debtor are unionized. In the CCAA reorganization of AbitibiBowater Inc., for example, the Court appointed a "grievance claims officer" to mediate grievances under the collective agreement that were included in the claims' procedure[20]. Mediation has also been employed to deal with other issues involving disputes between a debtor and its union. In the CCAA reorganization of Air Canada, for example, a mediator was appointed to assist the debtor and its union to come to a resolution on the terms for a new collective agreement that would permit the debtor to successfully reorganize[21].

Determination of Claims. One of the key areas where mediation can—and often is—employed in a Canadian insolvency proceeding is in connection with the determination of

[16] BIA, s. 65.1(4) and CCAA, s. 11.01. Note the CCAA does contemplate that "critical" suppliers may be ordered to supply goods or services in credit: CCAA, s. 11.4.
[17] BIA, s. 65.12 and CCAA, s. 33.
[18] *Labour Relations Act*, 1995, SO 1995, c 1, Sch A ("LRA"), ss. 18 and 21.
[19] LRA, ss. 19(1) and 35.
[20] See *Kenny* v *Bowater Maritimes Inc.*, 2014 CanLII 26544 (NB LA). A similar procedure was adopted in the CCAA reorganization of Air Canada.
[21] See discussion in *Gélinas, Bellemare, Grivas*, 2006 CIRB 365 (CanLII).

claims against an insolvent debtor. Where creditors are only able to recover cents on the dollar, reducing the costs of determining disputes with respect to the amount owing has the potential to increase recoveries for creditors.

BIA. The BIA establishes a statutory claims procedure that leaves little room at the initial stages for mediation, although mediation is possible at the appeal stage of the process. The BIA requires that the trustee appointed to administer a bankruptcy or oversee a reorganization examine and determine the quantum of all proofs of claims filed against the debtor and provides the trustee with the jurisdiction to make any inquiries necessary to determine the claims filed against the debtor[22]. In the case of contingent or unliquidated claims, the trustee is required to determine whether the claim is "provable" and the quantum of the claim[23]. The trustee has the theoretical ability to seek advice and directions from the Bankruptcy Court with respect to claims, but in practice the trustee determines the claims based on information provided by the creditor and, if necessary, advice provided by counsel retained by the trustee[24]. The trustee's determination with respect to a claim is binding unless the creditor appeals the determination to the Bankruptcy Court[25]. An appeal by a creditor of the trustee's determination with respect to a claim proceeds as a Motion before the Bankruptcy Court[26]. At this stage, the Bankruptcy Court may refer the parties to mediation to resolve some or all of the issues.

CCAA. The claims procedure under the CCAA is quite different than what is contemplated by the BIA. The CCAA leaves the procedure by which a claim is proven and the procedure for determining disputes with respect to a claim to be established by the court on a case-by-case basis and the court has broad jurisdiction to determine how disputes with respect to claims ought to be determined. The CCAA provides only that where a claim is not admitted by the debtor "it is to be determined by the court on summary application"[27].

The standard practice in CCAA proceedings is for the court, on the application of the debtor, to establish a procedure for creditors to file claims and for any disputed claims to be determined. A common practice that has developed is for the court to appoint a "Claims Officer"–typically a retired judge or practitioner–to determine disputes. In the context of determining a claim, the Claims Officer may attempt to mediate a resolution[28].

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[22] BIA, s. 135. Note that the claims procedure in the BIA is in a part of the Act that deals with bankruptcy but is also applicable in reorganization proceedings. See BIA, s. 66.
[23] BIA, s. 135(1.1).
[24] At one point in time the BIA claims procedure required that the trustee apply to the Bankruptcy Court to have contingent or unliquidated claims determined, but that procedure was replaced with the current procedure. The trustee does, however, have the general ability to seek advice and directions from the Bankruptcy Court.
[25] BIA, s. 135(4). Note that another creditor or the debtor can apply to the Bankruptcy Court to a have a claim reduced or expunged: see BIA, s. 135(5).
[26] General Rules, s. 11.
[27] CCAA, s. 20(1).
[28] See *Montreal, Maine & Atlantic Canada Co. (Montréal, Maine & Atlantique Canada Cie) (Arrangement relatif à)*, 2015 QCCS 1472 (CanLII)

The courts have also exercised their jurisdiction under the CCAA to order that claims disputes be mediated. In the CCAA reorganization of Muscletech Research and Development Inc., for example, the claims procedure established by the court contemplated some claims would be mediated[29].

Receiverships. While there is no legislation that establishes the procedure to be employed to determine creditor claims where a receiver is appointed, the Courts generally exercise their jurisdiction to establish claims procedure that resemble the procedures adopted in CCAA proceedings. There do not, to date, appear to be any reported cases the address mediation in the context of a claims' procedure established where a receiver is appointed.

Avoidance Proceedings. There are a variety of provisions in the BIA that can be used to attack pre-bankruptcy transactions to increase the funds available to creditors[30]. These provisions are also applicable in reorganization proceedings under the BIA and the CCAA[31]. Avoidance proceedings typically proceed as applications or actions under the applicable provincial rules of civil procedure. Mediation can be, and often is, employed as a means of reducing the cost of avoidance proceedings by resolving or at least narrowing the issues to be determined.

Approval by the Court. In mediation, the parties to the dispute ultimately control the outcome in the sense that they must agree to any solution of their dispute. In the insolvency context where third parties may be impacted by a mediated resolution, it is often necessary to have the resolution agreed to as among the direct parties to the dispute made binding on non-parties. It is common practice to have mediated resolutions approved by the court–the role of the court in this context is not to second-guess the resolution, but to ensure that the resolution is fair to other impacted stakeholders.

Cross-Border Mediation. Canada has adopted a slightly modified version of the UNCITRAL Model law on Cross-Border Insolvency in both the BIA and the CCAA[32]. Under both the BIA and the CCAA, once a foreign proceeding has been recognized, the court is required to "cooperate, to the maximum extent possible, with the foreign representative and the foreign court involved in the foreign proceeding"[33]. This provides the court with broad jurisdiction to authorize or direct the cross-border mediation of disputes in cross-border insolvency proceedings. Even outside of formal recognition proceeding, Canadian courts have recognized the benefits of using mediation to resolve disputes in the cross-border insolvency context. In *Roberts* v. *Picture Butte Municipal Hospital*[34], which pre-dates the current cross-border insolvency regime, the Alberta Court of Queen's Bench stayed litigation proceedings in Canada to permit the claim of a plaintiff to be determined in accordance with a plan of reorganization filed by the defendant under the *United*

[29] See *Muscletech Research and Development Inc. (Re)*, 2006 CanLII 27997 (ON SC). In the reorganization of Nortel Networks Corporation mediation was also employed, although without success: see, for example, *Nortel Networks Corporation (Re)*, 2015 ONSC 1354 (CanLII).
[30] See BIA, ss. 95-101.
[31] BIA, s. 101.1 and CCAA, s. 36.1.
[32] BIA, Part XIII and CCAA Part IV.
[33] CCAA, s. 52(1).
[34] 1998 ABQB 636 (CanLII).

States Bankruptcy Code. The plan contemplated that mediation would be used to determine disputed claims. Mediation was also employed in the cross-border insolvency of Nortel Networks Corporation[35].

Mediation in Personal Bankruptcy. Mediation is a statutory part of the Canadian personal bankruptcy regime.

> **Surplus Income.** The Canadian personal bankruptcy regime includes provisions that require a bankrupt to pay a portion of his or her post-bankruptcy income that is surplus to their needs to the trustee for the benefit of creditors. The amount of the surplus income that a bankrupt must pay is determined based on criteria established by the Superintendent of Bankruptcy–the government body responsible for the administration of the Canadian insolvency regime[36]. The BIA contemplates that mediation will be attempted to resolve disputes with respect to surplus income before resort is made to the Bankruptcy Court[37]. The mediation is conducted through the Office of the Superintendent of Bankruptcy in accordance with procedures that are prescribed by the Regulations to the BIA[38].
>
> **Conditions of Discharge.** Where an individual bankrupt is applying to be discharged from bankruptcy, the Bankruptcy Court has the jurisdiction to impose conditions that must be fulfilled by the bankrupt[39]. Creditors as well as the trustee have the right to oppose an application by a bankrupt seeking a discharge and to seek that conditions be imposed on the bankrupt[40]. Where a discharge is opposed only on the grounds that: (a) the bankrupt failed to pay amounts s/he was required to pay to the trustee; or (b) the bankrupt had the financial means to restructure, but chose bankruptcy instead, the BIA requires that the issues be mediated[41]. If a mediated resolution is reached, that resolution forms the basis for the bankrupt's discharge[42]. It is only if mediation is not successful or the bankrupt fails to comply with his or her obligations under the mediated resolution, that the Bankruptcy Court becomes involved[43].
>
> In practical application, discharge applications are typically disputed on a number of grounds in addition to assertions that the bankrupt should have paid more to the trustee or could have reorganized, and, for that reason, mediation is not commonly used to resolve discharge-related disputes.

Arbitration Clauses. It is not uncommon for the parties to an agreement to agree that disputes under the agreement by arbitration. It is generally accepted that the Court has jurisdiction to override such provisions[44].

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[35] See Nortel Networks Corporation (Re), 2017 ONSC 700 (CanLII), para 2
[36] BIA, s. 68.
[37] BIA, ss. 68(6) – (10).
[38] *Bankruptcy and Insolvency Act General Rules*, CRC, c. 368, s. 105. See **Appendix B**.
[39] BIA, s. 172(1).
[40] BIA, ss. 168.2, 170(1) and 170(7).
[41] BIA, s. 170.1(1).
[42] BIA, s. 170.1(4).
[43] BIA, s. 170.1(3).
[44] See the discussion in *Petrowest Corporation* v *Peace River Hydro Partners*, 2019 BCSC 2221 (CanLII).

Farm Debt Mediation Act. While the core pieces of insolvency legislation in Canada are the BIA and the CCAA, Canada has legislation – the *Farm Debt Mediation Act*[45] – that is available only to insolvent farmers. The FDMA is based on mediation of disputes between farmers and their creditors. The FDMA permits insolvent farmers to apply to a government official for a stay of proceedings and the appointment of a mediator to mediate a mutually acceptable resolution between the farmer and its creditors[46]. The general objective of the FDMA is to permit insolvent farmers with an opportunity to demonstrate to creditors the long-term viability of their operations[47].

Where a farmer applies for and is granted relief under the FDMA, a government-appointed administrator conducts a review of the farmer's financial situation and prepares a report. The administrator then appoints a mediator whose role it is to mediate a resolution between the farmer and its creditors. Unlike the BIA, the FDMA does not include comprehensive procedures for mediations.

The efforts to mediate a resolution under the FDMA are "protected" by a stay of proceedings that prevents creditors from enforcing their debts as against the farmer[48]. The general concept is that so long as the mediator is making progress and no creditor is being prejudiced by the delay in exercising its remedies the stay will be extended.

Unfortunately, the mediation process under the FDMA is not often used in practice. The inability to impose a solution, particularly in light of the availability of the BIA and the CCAA, limits the practical utility of the FDMA as a means to reorganize. However, the FDMA also includes provisions that restrict the rights of secured creditors as against farmers and is often relied upon as a basis to limit a secured creditor's enforcement rights.[49]

[45] SC 1997, c. 21 (the "**FDMA**"). See also *The Family Farm Protection Act*, CCSM c F15
[46] FDMA, ss. 5 and 6.
[47] See *M & D Farm Ltd.* v. *Manitoba Agricultural Credit Corp.*, [1999] 2 SCR 961, 1999 CanLII 648 (SCC)
[48] FDMA, ss. 12 and 13.
[49] FDMA, s. 21.

Appendix A

Poseidon Mediation Order

I hereby certify this to be a true copy of
the original ORDER
Dated this 15 day of October 2013
for Clerk of the Court

Clerk's stamp:

CLERK OF THE COURT
FILED
OCT 15 2013
JUDICIAL CENTRE
OF CALGARY

COURT FILE NUMBER	1301-04364
COURT OF QUEEN'S BENCH OF ALBERTA	
JUDICIAL CENTRE	CALGARY

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, RSC 1985, c C-36, AS AMENDED;

AND IN THE MATTER OF POSEIDON CONCEPTS CORP., POSEIDON CONCEPTS LTD., POSEIDON CONCEPTS LIMITED PARTNERSHIP, AND POSEIDON CONCEPTS INC.

DOCUMENT	**MEDIATION ORDER**
ADDRESS FOR SERVICE AND CONTACT INFORMATION OF PARTY FILING THIS DOCUMENT	Kenneth T. Lenz Bennett Jones LLP 4500, 855 – 2nd Street SW Calgary, Alberta T2P 4K7 Ph. (403) 298-3317 Fx. (403) 265-7219 File No.: 11866.66
DATE ON WHICH ORDER WAS PRONOUNCED	October 11, 2013
NAME OF JUSTICE WHO MADE THIS ORDER	The Honourable Justice Strekaf

UPON the application of PricewaterhouseCoopers Inc. (the "**Monitor**") as court appointed monitor of Poseidon Concepts Corp., Poseidon Concepts Ltd., Poseidon Concepts Limited Partnership, and Poseidon Concepts Inc. (collectively, "**Poseidon**");

AND UPON having read the 17th Monitor's Report, dated October 10, 2013, and the pleadings and proceedings filed in these CCAA proceedings;

AND UPON noting the Order dated September 27, 2013, which, among other things, enhanced the Monitor's powers to permit the Monitor to prosecute and pursue claims on behalf of Poseidon;

AND UPON noting the consent of the secured lenders of Poseidon, namely The Toronto-Dominion Bank, as agent for itself and HSBC Bank Canada, The Bank of Nova Scotia, and National Bank of Canada (the "**Lending Syndicate**"), the consent of Franz Auer, Joanna Goldsmith and Marian Lewis,

being the representative plaintiffs (the "**Class Action Plaintiffs**") in the Actions commenced against Poseidon, Scott Dawson, Lyle Michaluk, Matt MacKenzie and Harley Winger (collectively, the "**Poseidon Defendants**"), respectively, in the Court of Queen's Bench of Alberta, Action No. 1301-00935, in the Superior Court of Ontario, Action No CV-12-46873600CP, and in the Superior Court of Quebec, Action No. 500-06-000633-129 (collectively, the "**Class Actions**"), the consent of the Poseidon Defendants and the consent of the Monitor, and the consent of the Plaintiff (the "**U.S. Plaintiff**") in the action commenced and pending in the United States District Court for the Southern District of New York styled *IN RE POSEIDON CONCEPTS SECURITIES LITIGATION*, having Court File Number 12-cv-1213 (DLC) (the "**U.S. Action**");

IT IS HEREBY ORDERED THAT:

THE MEDIATION PARTIES

1. Subject to any further Order of this Court, the Class Action Plaintiffs, the Lending Syndicate, the Monitor, the Poseidon Defendants and any other Eligible Person (defined herein) (collectively, the "**Parties**," each being a "**Party**," to the Mediation) shall participate in a mediation (the "**Mediation**") to address any claims, rights, obligations, or disputes resulting from, relating to, or with respect to the preparation, review, audit and restatement of Poseidon's financial statements and any other related matters (the "**Restatement**").

2. Any other person or entity that may have, or may be subject to, any claims, rights, obligations, or disputes resulting from, relating to, or with respect to the Restatement (an "**Eligible Person**") may also participate in the Mediation upon:

   (a) the acceptance and delivery of a Mediation Notice in accordance with, paragraphs 10 to 14 of this Order;

   (b) further Order of this Court; or

   (c) the consent of the Class Action Plaintiffs, the Lending Syndicate, the Monitor and the Poseidon Defendants,

   and thereupon shall be considered a Party to the Mediation.

3. All Parties to the Mediation shall participate in the Mediation in person and with representatives present with full authority to settle the claims (including any insurer whose policy may afford coverage for any of the claims) or, if not practicable, through counsel or other representatives, subject to those counsel or other representatives having access to representatives with full authority, and undertaking to promptly pursue instructions with respect to any proposed agreements that arise from the Mediation.

4. Pursuant to this Court's Order dated May 30, 2013 (the "**Representation Order**"), the Class Action Plaintiffs are representatives for the class as defined in the Representation Order (the "**Representation Class**"), and shall have full authority to settle any claims, rights or disputes relating to the Representation Class resulting from, relating to, or with respect to the Restatement.

5. The US Plaintiff may participate in the Mediation through his counsel and shall be a Party to the Mediation. The U.S. Plaintiff shall have full authority to settle any claims, rights or disputes resulting from, relating to, or with respect to the Restatement relating to the members of the class contemplated in the U.S. Action that are not members of the Representation Class. No notice of the Mediation to the class contemplated in the U.S. Action is required.

THE MEDIATION

6. The Mediation shall be conducted by the Honourable George W. Adams, Q.C. or, if Mr. Adams is unavailable, by such other mediator as may be agreed upon between the Class Action Plaintiffs, the Lending Syndicate, the Monitor and the Poseidon Defendants, or as may be appointed by a further Order of this Court (the "**Mediator**").

7. The Mediation shall be held in Calgary, Alberta, at a location to be agreed upon between the Class Action Plaintiffs, the Lending Syndicate, the Monitor and the Poseidon Defendants.

8. The Mediation shall be held on three (3) consecutive mutually available dates in April or May 2014, or such other dates agreed upon between the Class Action Plaintiffs, the Lending

Syndicate, the Monitor and the Poseidon Defendants. Additional dates may only be added, and adjournments of any dates may only be accepted, with the prior written consent of the Parties to the Mediation or a further Order of this Court.

9. The costs, fees and expenses of the Mediation, including facility fees and mediator's fees, shall be split equally by the Class Action Plaintiffs (1/3), the Lending Syndicate (1/3), and the Poseidon Defendants (1/3), and any other Party to the Mediation unless otherwise agreed to by the Parties to the Mediation in writing.

MEDIATION NOTICES

10. By October 31, 2013, any Party to the Mediation may send a notice (the "**Issuing Party**") in the form attached as Schedule "A" (the "**Mediation Notice**") to any proposed respondent to request their participation in the Mediation. Such Issuing Party shall provide a copy of such Mediation Notice to all other Parties to the Mediation.

11. If the proposed respondent agrees to participate in the Mediation, as described in this Order and the Mediation Notice, the proposed respondent shall unconditionally sign the Mediation Notice and return the signed Mediation Notice to the Issuing Party by no later than November 30, 2013.

12. Such proposed respondent may deliver the signed Mediation Notice to the Issuing Party by email, fax or courier.

13. Upon delivery of the signed Mediation Notice to the Issuing Party, the proposed respondent, the Class Action Plaintiffs, the U.S. Plaintiffs, the Lending Syndicate, the Poseidon Defendants and the Monitor shall negotiate the documentary production rights and obligations of the proposed respondent. If an agreement is reached, the proposed respondent shall become a Party to the Mediation for all purposes and subject to all the benefits and obligations of the Mediation and this Order. If an agreement is not reached, the proposed respondent shall not become a Party to the Mediation and shall not participate in the Mediation.

14. Upon receipt of a signed Mediation Notice, the Issuing Party shall send a copy to all Parties to the

Mediation and the Mediator.

STATEMENT OF ISSUES

15. By November 15, 2013, any Party to the Mediation that has not already delivered a Statement of Claim to a Party to the Mediation against which it seeks relief, shall deliver a Statement of Issues to all other Parties to the Mediation and to the Mediator, which shall be in a format similar to a Statement of Claim and shall identify the party against which it believes it has a claim, set out the relief sought, and set out the factual and legal basis for the claim.

16. Any Party who wishes to do so, may deliver to all of the other Parties to the Mediation a Reply, by no later than December 15, 2013.

PRE-MEDIATION DOCUMENT DISCLOSURE

17. No later than January 31, 2014, Class Action Plaintiffs, U.S. Plaintiffs, and the Lending Syndicate shall deliver to each other and to the Poseidon Defendants and to the Monitor all non-privileged records in their possession, power or control relevant to the Restatement and any other issues that arise from the Statements of Issues or Reply thereto delivered by any of the Parties to the Mediation.

18. Poseidon shall deliver to Class Action Plaintiffs, U.S. Plaintiffs, the Monitor and the Lending Syndicate all non-privileged emails and attachments and electronic documents in its possession, power or control responsive to the list of custodians, date range and search terms set out in Schedule "B" to this Order. The Poseidon Defendants other than Poseidon shall have the option of delivering to Class Action Plaintiffs, U.S. Plaintiffs, the Monitor and the Lending Syndicate either: (a) all non-privileged records in their possession, power or control relevant to the Restatement and any other issues that arise from the Statements of Issues or Reply thereto delivered by any of the Parties to the Mediation; or (b) all non-privileged emails and attachments and electronic documents in its possession, power or control that meet both of the following

criteria: (i) relate in any way to Poseidon; and (ii) are responsive to the list of search terms and to the date range set out in Schedule "B" to this Order.

19. Wherever possible, the Parties shall produce all records electronically, in native files types, with preserved metadata.

20. Any Party to the Mediation may submit a reasonable request to another Party for further production of relevant and material records subject to considerations of proportionality. Parties must make best efforts to respond to such requests as soon as possible.

21. Without limiting the generality of the foregoing, the Parties to the Mediation shall be entitled to disclose in the Mediation all records in their possession, power or control that may be subject to obligations of confidentiality with any other Party to the Mediation.

22. If a Party to the Mediation claims privilege over any document that would otherwise be producible under this Order, that Party will provide the other Parties to the Mediation with a list identifying the categories of documents over which privilege was claimed. A detailed privilege log identifying all privileged documents individually is not required.

23. Any disagreement with respect to claims of privilege on a category by category basis will be resolved in a one day arbitration before an arbitrator mutually agreeable to the Parties to the Mediation, failing such agreement, by an arbitrator appointed by the Court. The decision of the arbitrator will not be subject to judicial review or appeal. The decision of the arbitrator will be binding on the Parties solely for the purposes of the Mediation.

24. If a settlement of all claims is not reached at mediation, all documents over which privilege was claimed but which were produced pursuant to a ruling of the arbitrator will be returned to the Party that produced the documents and there shall be no waiver of privilege, or allegation of waiver of privilege, in any other proceedings.

25. The decision of the arbitrator shall not be referred to, relied upon, or referenced in any respect in any other proceedings and shall not form the basis for any plea of issue estoppel or any other

estoppel. Rather, any dispute regarding privilege shall be re-litigated as though it was being decided for the first time.

26. Disclosure of any privileged document or documents pursuant to the production requirements in paragraphs 17-18 of this Order shall be deemed to be inadvertent, and shall result neither in the waiver of any privilege over the document or documents, nor over any related documents or documents designated as privileged by the producing party, unless the producing Party indicates in writing that it intends to waive such privilege. The recipient of any such privileged document will return the privileged document to the producing party upon request of the producing party without delay.

CONFIDENTIALITY

27. Unless otherwise agreed in writing, or the Court orders otherwise, all information or records prepared for or in the Mediation, including Statements of Issues, Mediation Notices, and responses to Mediation Notices, and all written or other form of documentary material provided to, or prepared by the Mediator, the Parties to the Mediation, or third parties including the documents produced pursuant to paragraphs 17-26 of this Order:

(a) are protected by without prejudice / settlement privilege;

(b) must be treated by all participants in the Mediation as confidential;

(c) can only be used for the purposes of the Mediation;

(d) cannot be revealed or disclosed to anyone other than a Party to the Mediation, its legal counsel, its insurers and its experts;

(e) cannot be referred to, presented as evidence or relied upon on in any subsequent application or proceeding of a judicial or quasi-judicial nature for any purpose whatsoever including, but not limited to, impeachment; and

(f) are not admissible in any application, action, or proceedings of a judicial or quasi-judicial nature whatsoever.

28. Any communication made, document produced or created, or evidence given in the Mediation shall be subject to absolute privilege, as if delivered or made in a judicial proceeding. The fact that a communication is made, a document produced or created, and evidence given shall not be deemed to be an admission of relevance, nor an automatic waiver of any privilege, whether solicitor-client or otherwise, that would ordinarily attach to such communications, documents or evidence in the ordinary course of litigation.

29. The discussions, settlement negotiations, or any disclosures, including the Mediator's file, made during or for the purposes of the Mediation, are inadmissible in any other proceedings for any purpose. In particular, the Parties to the Mediation shall not rely on or introduce as evidence in any other proceedings the following:

(a) any views or proposals expressed or suggestions made by or to the other Parties or the Mediator in respect of the possible settlement of the matter, whether orally or in writing;

(b) any admissions or apologies made by any of the other Parties in the course of the Mediation, whether orally or in writing;

(c) the fact that any of the other Parties indicated willingness to accept a proposal or recommendation for settlement made by the Mediator; and

(d) any information provided to the Mediator in the course of the Mediation.

30. In order to preserve the confidentiality of the Mediation process, the Parties shall not file any documents or notices described in this Order with the Court, unless otherwise specifically directed by this Order or a further Order of this Court, however, no Party to the Mediation shall seek a Court Order to permit any such documents or notices to be filed with the Court.

31. In the event that the Parties to the Mediation (or any of them) reach a settlement, the terms of the settlement will be admissible in any Court or other proceeding required to approve or enforce it.

32. Any proved material breach of the confidentiality provisions of this Order shall be subject to the full range of sanctions available to the Court.

33. In the event that the Mediation is terminated without a settlement having been reached among all of the Parties, nothing in this order shall be construed as limiting the disclosure obligations of any party to a class proceeding or class action that has been commenced in the United States or Canada in relation to the Restatement.

MEDIATION BRIEFS

34. No later than three weeks prior to the Mediation, each of the Parties to the Mediation shall submit to each other and the Mediator a Mediation Brief, which details the significant facts, legal issues, and settlement position of the Party.

INSURANCE

35. At least one (1) month prior to the Mediation, each of the Parties to the Mediation against which a claim has been asserted by Statement of Claim or in a Statement of Issues shall disclose the following information to the Party that asserted such claim, all of which will be provided on a confidential and without prejudice basis:

(a) The remaining limits on any responsive insurance policies; and

(b) A summary of any reservation of rights asserted by the insurers in respect of such insurance policies.

TERMINATION OF THE MEDIATION

36. The Mediation shall be terminated only on the occurrence of any of the following circumstances:

(a) A signed Declaration by the Mediator, filed with this Court, that a settlement has been reached between some or all of the Parties;

(b) A signed Declaration by the Mediator, filed with this Court, that further efforts of Mediation are no longer considered worthwhile;

(c) At 11:59 p.m. on the third day of the Mediation or at such later time as may be agreed to by all Parties; or

(d) By further Order of this Court.

STANDSTILL

37. None of the Parties to the Mediation shall commence or pursue any claims or proceedings resulting from, relating to, or with respect to the Restatement or any other issues that arise from the Statements of Issues or Reply thereto delivered by any of the Parties to the Mediation against any other Party to the Mediation between the date of this Order and the termination of the Mediation under paragraph 36 of this Order.

38. Subject to paragraph 39 of this Order, the running of time for any limitation period that applies to any claim that has been or could be asserted by any Party against any other Party relating to the Restatement shall be suspended from the date of this Order until the date that is sixty (60) days after the termination of the Mediation under paragraph 36 of this Order (the "**Standstill Period**").

39. With respect to any claim that has been or could be asserted by any Party against any other Party relating to the Restatement that would be governed by Québec law, the Parties to the Mediation shall be deemed, by consenting or agreeing to become a Party to the Mediation, to:

(a) agree that they are renouncing to the benefit of time elapsed for the prescription which has begun with respect to any claim, recourse, cause or right of action that any Party may assert against any other Party relating to the Restatement;

(b) agree that following the date of this Order, the prescription not already acquired for any claim, recourse, cause or right of action that any Party may assert against any other Party relating to the Restatement begins to run again for the same period; and

(c) agree that other than renouncing to the benefit of time elapsed, the Parties do not waive any other argument, position or defence that may otherwise be asserted by them in any legal proceedings.

40. Nothing in this Order shall preclude the Petitioner in the proceeding commenced and pending in the Quebec Superior Court, District of Montreal, styled *Kegel v National Bank of Canada*, having Court File Number 500-06-000642-138, from prosecuting that proceeding.

STAY OF PROCEEDINGS

41. Subject to any further Order of this Court, paragraph 13 of the CCAA Initial Order is hereby amended to extend the Stay Period to May 30, 2014.

AMENDMENT AND VARIATION OF ORDER

42. Any of the procedures or deadlines specified in this Order may be amended or varied by agreement in writing of all the Parties to the Mediation or further Order of this Honourable Court.

ASSISTANCE OF OTHER COURTS

43. This Court hereby requests the aid and recognition of any court, tribunal, regulatory or administrative body having jurisdiction in Canada or in the United States, to give effect to this Order.

J.C.Q.B.A.

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SCHEDULE "A"

Clerk's stamp:

COURT FILE NUMBER	1301-04364
COURT OF QUEEN'S BENCH OF ALBERTA	
JUDICIAL CENTRE	CALGARY
	IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, RSC 1985, c C-36, AS AMENDED;
	AND IN THE MATTER OF POSEIDON CONCEPTS CORP., POSEIDON CONCEPTS LTD., POSEIDON CONCEPTS LIMITED PARTNERSHIP, AND POSEIDON CONCEPTS INC.
DOCUMENT	NOTICE OF CLAIM AND REQUEST FOR MEDIATION (MEDIATION NOTICE)

TO: [Proposed Respondent]

RE: Notice of Claim and Request to Participate in Mediation ("Mediation Notice")

Date: •

This Mediation Notice is provided to you in accordance with the Mediation Order dated October 11, 2013 (the "**Court Order**") granted in the Court of Queen's Bench of Alberta, Action No. 1301-04364, respecting Poseidon Concepts Corp., Poseidon Concepts Ltd., Poseidon Concepts Limited Partnership, and Poseidon Concepts Inc. (collectively, "**Poseidon**"). A copy of the Court Order is attached. All undefined capitalized terms in this Mediation Notice have the meanings ascribed to them in the Court Order.

Pursuant to paragraph 10 of the Court Order, the undersigned requests that you participate in the Mediation to address claims against or involving you resulting from, relating to, or with respect to the restatement of Poseidon's financial statements and any other related matters (the "**Mediation Claims**").

Pursuant to paragraph 13 the Court Order, if you accept this offer to participate in the Mediation by endorsing this Mediation Notice and delivering the same to the undersigned, you will be required to negotiate with the Class Action Plaintiffs, the U.S. Plaintiffs, the Lending Syndicate, the Poseidon Defendants and the Monitor to determine your documentary production rights and obligations. If an agreement is reached, you shall become a Party to the Mediation for all purposes and subject to all the

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benefits and obligations of the Mediation and this Order. If an agreement is not reached, you shall not become a Party to the Mediation and shall not participate in the Mediation.

By signing and delivering this Mediation Notice to the undersigned, and only if you become a Party to the Mediation, you agree to a standstill of all limitation periods in respect of all Mediation Claims made or brought by any and all Parties to the Mediation as set out in paragraphs 37-40 of the Mediation Order as set out below:

STANDSTILL

1. None of the Parties to the Mediation shall commence or pursue any claims or proceedings resulting from, relating to, or with respect to the Restatement or any other issues that arise from the Statements of Issues or Reply thereto delivered by any of the Parties to the Mediation against any other Party to the Mediation between the date of this Order and the termination of the Mediation under paragraph 36 of this Order.

2. Subject to paragraph 39 of this Order, the running of time for any limitation period that applies to any claim that has been or could be asserted by any Party against any other Party relating to the Restatement shall be suspended from the date of this Order until the date that is sixty (60) days after the termination of the Mediation under paragraph 36 of this Order (the **"Standstill Period"**).

3. With respect to any claim that has been or could be asserted by any Party against any other Party relating to the Restatement that would be governed by Québec law, the Parties to the Mediation shall be deemed, by consenting or agreeing to become a Party to the Mediation, to:

   (a) agree that they are renouncing to the benefit of time elapsed for the prescription which has begun with respect to any claim, recourse, cause or right of action that any Party may assert against any other Party resulting from, relating to, or with respect to the Restatement;

   (b) agree that following the date of this Order, the prescription not already acquired for any claim, recourse, cause or right of action that any Party may assert against any other Party resulting from, relating to, or with respect to the Restatement begins to run again for the same period;

   (c) agree that other than renouncing to the benefit of time elapsed, the Parties do not waive any other argument, position or defence that may otherwise be asserted by them in any legal proceedings.

4. Nothing in this Order shall preclude the Petitioner in the proceeding commenced and pending in the Quebec Superior Court, District of Montreal, styled *Kegel v National Bank of Canada*, having

Court File Number 500-06-000642-138, from prosecuting that proceeding.

Pursuant to paragraph 11 of the Court Order, the offer extended to you by way of this Mediation Notice shall expire if you do not sign and deliver this Mediation Notice to the undersigned by November 30, 2013.

[Issuing Party – Name, Title and Contact Information]

[Proposed Respondent] hereby agrees to participate in the Mediation and to all of the terms set forth in this Mediation Notice and in the Court Order dated October 11, 2013.

For and on behalf of
[Proposed Respondent]

Date: ●

[Name, Title and Contact Information]

SCHEDULE "B"

CUSTODIANS

1. Scott Dawson
2. Harley Winger
3. Dean Jensen
4. Neil Richardson
5. Lyle Michaluk
6. Cliff Wiebe
7. Matt MacKenzie
8. David Belcher
9. Sonja Sanborn
10. Doug Robinson
11. Stacey Kolenick
12. Joann Vispo
13. Kristen Schmid
14. Stacey Manista
15. Allyson Finstein
16. Jessie Heppenstall
17. Michelle Rye
18. Joe Kostelecky
19. Brad Wanchulak
20. Todd Studer
21. Brian Swendsen
22. Angus Jenkins
23. Jim McKee
24. Kenneth J. Faircloth

25. Wazir (Mike) Seth
26. Ryan McKay
27. Jenna Farquhar
28. Carrie Howell
29. Mitch Kersten
30. Cheryl Schell
31. Brian Erickson
32. Steve Swinson
33. King Schmeltzer
34. Ron Swinson

DATE RANGE

July 1, 2011 to April 9, 2013

SEARCH TERMS

	SEARCH TERM
1.	Allowance
2.	"Bad debt"
3.	Uncollectible
4.	Collectible
5.	Impaired OR impairment
6.	"Revenue recognition" OR "rev recognition" OR "rev rec"
7.	"EBITDA guidance" OR "EBITDA forecast"
8.	Profitability AND (analysis OR review OR report)
9.	"Revenue target"
10.	"Aged listing"
11.	"Aged account"
12.	"Aging report"

	SEARCH TERM
13.	"DSO" OR "Days Sales Outstanding"
14.	"Field ticket"
15.	Ticketing
16.	Billing AND (issue OR problem OR concern OR complaint)
17.	Invoicing
18.	Discrepancies AND (revenue OR contract OR price OR pricing OR term sheet)
19.	Complexities AND transaction
20.	"Credit approval"
21.	"Reverse revenue"
22.	Reversal
23.	"Credit check"
24.	"Cash deposit"
25.	"Watch list"
26.	"Revenue cycle"
27.	"Accounts Receivable" OR "AR" OR "A/R" OR "receivables" OR "receivable"
28.	Arrears
29.	"Write-off" OR "write-down"
30.	Auditor
31.	KPMG
32.	Caldwell
33.	"Interim review" OR "quarterly review"
34.	"Subsequent event"
35.	"Representation letter" OR "rep letter"
36.	"Management letter" OR "MLP" OR "ML"
37.	"Audit committee"
38.	"Financial statements"
39.	"Long-term contract" OR "long term contract"
40.	"Minimum commitment"
41.	"Take or pay"
42.	"Day to day"
43.	"Client base" OR "customer base"

	SEARCH TERM
44.	"Signed contract"
45.	TD
46.	Syndicate
47.	Lenders
48.	Bonus
49.	"Stock options"
50.	Warrants
51.	Backdate OR backdating
52.	"Internal Control"
53.	ICFR
54.	"Financial Reporting"
55.	Disclosure AND (problem, issue, concern)
56.	"Accounting personnel"
57.	Material AND (misstatement OR misrepresentation)
58.	Fraud
59.	Risk AND (revenue OR accounting OR audit)
60.	"Red flag"
61.	Weakness
62.	"National Bank" OR "NBC" OR "NBF"
63.	Sandy OR Edmonstone
64.	"Lawrence Bloomberg"
65.	"Louis Vachon"
66.	"Luc Paiement"
67.	"Ricardo Pascoe"
68.	"Greg Colman"
69.	"Connected issuer"
70.	"Due diligence"
71.	"Use of proceeds"
72.	Dividend
73.	"Accelerated program"
74.	"Capital budget" OR "capital program"

	SEARCH TERM
75.	"Special Committee" OR "SC"
76.	"The Committee"
77.	Investigation
78.	Investigate
79.	Restate OR restatement
80.	Overstate
81.	"Ernst & Young" OR "EY" OR "E&Y"
82.	"Interim report"
83.	OSC
84.	ASC
85.	SEC
86.	RCMP
87.	Whistleblower
88.	"Insider trading"
89.	"Non-public information" or "non public information"
90.	"Commitment Letter"

Appendix B

BIA Mediation Procedures

105 (1) For the purposes of subsections 68(8) and 170.1(2) of the Act, the procedures governing a mediation are as set out in this section.

(2) For the purposes of this section,

(a) the bankrupt and the trustee are always parties to the mediation;

(b) the trustee may act either personally or through a representative;

(c) an opposition to discharge made by a creditor or the trustee, referred to in subsection 170.1(1) of the Act, is deemed to be a request by the creditor or the trustee, as the case may be, for mediation; and

(d) a creditor who requests mediation is a party to the mediation.

(3) For the purpose of conducting a particular mediation, the Superintendent shall designate as mediator

(a) an employee of a Division Office, including Division Offices other than the one for the bankruptcy division in which the proceedings were commenced; or

(b) any other person with training or experience in mediation and whom the Superintendent considers qualified.

(4) On receipt of a request for mediation from a trustee under subsection 68(6) or (7) or 170.1(1) of the Act, accompanied by the most recent income and expense statement in prescribed form completed by the bankrupt, the official receiver shall refer the matter to the mediator, who shall set the time and place for the mediation. The time set for the mediation must be within 45 days after the official receiver received the request for mediation.

(5) The mediator shall conduct the mediation with all parties physically present, unless the mediator decides to conduct the mediation by telephone conference call or by means of any other communication facilities that permit all persons participating in the mediation to communicate with each other.

(6) The mediation must be held at the Division Office, at any other place that is designated by the mediator, or, if the mediation is conducted otherwise than with all parties physically present, at any combination of places necessary for that purpose.

(7) The mediator shall send a copy of the notice of the mediation, in prescribed form, to the bankrupt, to the trustee and to any creditor who requested mediation, at least 15 days, or any shorter period that may be agreed to by all the parties concerned, before the date set for the mediation.

(8) If, at any time before the mediation has started, the mediator believes on reasonable grounds that the mediation cannot proceed at the time scheduled, the mediator shall reschedule it, setting a new time and place.

(9) Except when it would constitute a second adjournment, the mediator shall, subject to subsection (13), adjourn the mediation at any time during the mediation if

(a) a party requests an adjournment and the mediator believes on reasonable grounds that the mediation would benefit from further negotiations or the provision of additional information;

(b) the mediator believes on reasonable grounds that one of the parties, other than the trustee in the case of a mediation requested by a creditor under subsection 170.1(1) of the Act, cannot continue the mediation for a certain period of time;

(c) all the creditors who were informed of the mediation in accordance with subsection (7) or (11) fail to appear at the mediation and the mediator believes on reasonable grounds, with respect to at least one of those creditors, that the non-appearance is neither a delaying tactic nor intended to bring the mediation into disrepute;

(d) in the case of a mediation requested by a creditor under subsection 170.1(1) of the Act, a party, other than the trustee, who was informed of the mediation in accordance with subsection (7) or (11) fails to appear at the mediation and the mediator believes on reasonable grounds that the non-appearance is neither a delaying tactic nor intended to bring the mediation into disrepute; or

(e) in any case other than the one referred to in paragraph (d), a party, other than a creditor, who was informed of the mediation in accordance with subsection (7) or (11) fails to appear at the mediation and the mediator believes on reasonable grounds that the non-appearance is neither a delaying tactic nor intended to bring the mediation into disrepute.

(10) If a mediation is rescheduled or adjourned, the new date set must be within 10 days after the date on which the rescheduling or adjournment occurs.

(11) If a mediation is rescheduled or adjourned, the mediator shall inform the parties of the new time and place.

(12) At any time during the mediation, the mediator shall, subject to subsection (13), cancel the mediation if

(a) there is an outstanding opposition to the discharge of the bankrupt by a creditor or the trustee on a ground referred to in paragraphs 173(1)(a) to (l) or (o) of the Act;

(b) the mediator believes on reasonable grounds that a party is abusing the rescheduling procedures;

(c) there has already been an adjournment and

(i) there is a request for adjournment under paragraph (9)(a), or

(ii) one of the circumstances referred to in paragraphs (9)(b) to (e) occurs;

(d) the mediator believes on reasonable grounds that one of the parties, other than the trustee in the case of a mediation requested by a creditor under subsection 170.1(1) of

the Act, cannot continue the mediation at all;

(e) all the creditors who were informed of the mediation in accordance with subsection (7) or (11) fail to appear at the mediation and the mediator believes on reasonable grounds, with respect to all of those creditors, that the non-appearance is a delaying tactic or is intended to bring the mediation into disrepute;

(f) in the case of a mediation requested by a creditor under subsection 170.1(1) of the Act, a party, other than the trustee, who was informed of the mediation in accordance with subsection (7) or (11) fails to appear at the mediation and the mediator believes on reasonable grounds that the non-appearance is a delaying tactic or is intended to bring the mediation into disrepute; or

(g) in any case other than the one referred to in paragraph (f), a party, other than a creditor, who was informed of the mediation in accordance with subsection (7) or (11) fails to appear at the mediation and the mediator believes on reasonable grounds that the non-appearance is a delaying tactic or is intended to bring the mediation into disrepute.

(13) Despite paragraphs (9)(b) and (d) and (12)(d) and (f), the absence of one or more creditors who requested mediation, or the inability of one or more creditors who requested mediation to continue the mediation, is not a ground for adjourning or cancelling the mediation if at least one creditor who requested mediation is present at the mediation, or is able to continue the mediation, as the case may be.

(14) In the case of a mediation under section 170.1 of the Act, if all of the creditors who requested the mediation cause the cancellation of the mediation under paragraph (12)(e),

(a) the opposition to discharge on the part of each of those creditors on a ground referred to in paragraph 173(1)(m) or (n) of the Act is deemed withdrawn; and

(b) the issues submitted to mediation are deemed to have been thereby resolved for the purposes of subsection 170.1(3) of the Act.

(15) For greater certainty, if

(a) a mediation under section 68 of the Act is cancelled under any of paragraphs (12)(a) to (g), or

(b) a mediation under section 170.1 of the Act is cancelled otherwise than under paragraph (12)(e),

the issues submitted to mediation are deemed to have not been thereby resolved for the purposes of subsection 68(10) or 170.1(3), as the case may be, of the Act.

(16) If a mediation is cancelled, the mediator shall send to the Division Office and the parties a notice of the cancellation, in prescribed form, setting out the grounds for the cancellation.

(17) No mediator or party to a mediation shall disclose to the public any confidential information concerning an issue submitted to mediation, unless the disclosure is

(a) required by law; or

(b) authorized by the person to whom the confidential information relates.

(18) If agreement is reached by all parties at the mediation, a mediation settlement agreement, in prescribed form and including all terms and conditions of the settlement reached, must be signed by the parties, and the mediator shall send copies of the agreement to the Division Office and the parties. The agreement is binding on the parties, subject to any subsequent court order.

(19) All payments made by a bankrupt under a mediation settlement agreement must be made to the trustee and deposited into the estate account.

(20) If the parties fail to reach agreement at the mediation, the mediator shall issue a notice in prescribed form to the effect that the issues submitted to mediation under subsection 68(6) or (7) or 170.1(1), as the case may be, of the Act were not resolved, and shall send that notice to the Division Office and the parties.

MEDIATION IN INSOLVENCY PROCEEDINGS: THE EUROPEAN UNION PERSPECTIVE

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Mediation in the European Union

In European Union there has been attention on mediation since 1998, when the European Commission made a Recommendation about alternative dispute resolution in consumer disputes.[50] In 2001, the Commission published a second Recommendation about the consensual resolution of consumer disputes.[51] Subsequently, a Green Paper on ADR has been delivered[52], a Code of Conduct for Mediators was designed, and in 2008 the Mediation Directive entered into force.[53] *Directive 2008/52/EC of the European Parliament and of the Council of 21 May 2008 on certain aspects of mediation in civil and commercial matters (after this the Mediation Directive)*[54]

The Mediation Directive should contribute to the proper functioning of the internal market, in particular as concerns the availability of mediation services. The Directive seeks to facilitate access to alternative dispute resolution (ADR) and to promote the amicable settlement of disputes, by encouraging the use of mediation and by ensuring a healthy relationship between mediation and judicial proceedings.

Article 2 of the Mediation directive defines mediation as a "structured process, however, named or referred to, whereby two or more parties to a dispute attempt by themselves, on a voluntary basis, to reach an agreement on the settlement of their dispute with the assistance of a mediator. This process may be initiated by the parties or suggested or ordered by a court or prescribed by the law of a Member State". This definition is broad enough to cover insolvency matters as well. The Mediation Directive highlights that mediation can contribute to preserving an amicable and sustainable relationship between the parties. These benefits are even more pronounced in cross-border situations.

The Mediation Directive applies to cross-border disputes in civil and commercial matters covers disputes in which at least one of the parties is domiciled in a Member State other than that of any other party on the date on which they agree to use mediation or on the date mediation is ordered by a court. The principal objective of this legal instrument is to encourage the recourse to mediation in the Member States. For these purposes, the Mediation Directive encompasses five substantive rules:

[50] Commission Recommendation 98/275/EC, 30 March 1998
[51] Commission Recommendation 01/310/EC, 4 April 2001
[52] COM (2002) 196m April 2002 (Green paper on alternative dispute resolution in civil and commercial law)
[53] B. Wessels, S. Madaus, Rescue of Business in Europe, Oxford University Press, 30 January 2020 - Law - 1552 p.
[54] Directive 2008/52/EC of the European Parliament and of the Council of 21 May 2008 on certain aspects of mediation in civil and commercial matters *available at https://eur-lex.europa.eu/legal-content/en/ALL/?uri=CELEX:32008L0052*

- Member State have to encourage the training of mediators and to ensure high quality of their services.
- Every judge has the right to invite the parties to a dispute to attempt a mediation first if she/he considers it appropriate given the circumstances of the case,
- Agreements resulting from mediation can be rendered enforceable if both parties so decide. Such agreements can be approved by a court or certified by a public notary.
- Mediation takes place in an atmosphere of confidentiality. The provisions of the Directive require that the mediator is not obliged to give evidence in court about what took place during mediation in a future dispute between the parties to that mediation.
- The parties do not lose their possibility to go to court as a result of the time spent in mediation: the time limits for bringing an action before the court are suspended during mediation.[55]

While the mediation continues to develop in Europe, there is still a cultural roadblock in favour of arbitration and other adjudicative processes. In its 2016 Report on the application of Directive 2008/52/EC on certain aspects of mediation in civil and commercial matters, European Commission stated that certain difficulties were identified concerning the functioning of the national mediation systems in practice. These difficulties are mainly related to the lack of a mediation "culture" in the Member States, insufficient knowledge of how to deal with cross-border cases, the low level of awareness of mediation and the functioning of the quality control mechanisms for mediators. Further, the mediation is not yet sufficiently known, and a "cultural change" is still necessary to ensure that citizens trust mediation. The report also highlights that judges and courts remain reluctant to refer parties to mediation.[56]

Implementation of the Mediation Directive in the EU Member States

In 2016, the EU Parliament's Briefing Note titled "Achieving a Balanced Relationship between Mediation and Judicial Proceedings" analysed whether the purpose of the Mediation Directive as provided in Article 1, the "balanced relationship between mediation and judicial proceedings", had been achieved.[57] In its conclusion, the Note stated that "the key goals of the Directive remain far from being achieved." The mediation in the EU Member States is still used in less than 1 per cent of the cases in civil and commercial litigation. It appears that the only EU Member State, which has achieved more or less considerable progress in using mediation is Italy. The Italian legislator has adopted an opt-out mediation model, applicable to about 15% of all civil and commercial cases. In those cases, mediation is now playing a very significant role.[58] Following Italian example, Romania and Greece attempted to introduce similar legislative provisions introducing a

[55] EU overview on mediation *available at* https://e-justice.europa.eu/content_eu_overview_on_mediation-63-en.do

[56] Report from the Commission to the European Parliament, the Council and the European Economic and Social Committee on the application of Directive 2008/52/EC of the European Parliament and of the Council on certain aspects of mediation in civil and commercial matters available at https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52016DC0542 at p.4

[57] Giuseppe De Palo & Leonardo D'Urso, Achieving a Balanced Relationship between Mediation and Judicial Proceedings (2016)

[58] Giuseppe De Palo, A Ten-Year-Long "EU Mediation Paradox" When an EU Directive Needs To Be More …Directive (2018) *available at* www.europarl.europa.eu/RegData/etudes/BRIE/2018/608847/IPOL_BRI(2018)608847_EN.pdf

requirement to attend a mediation information session before trial. However, in Romania, the Constitutional Court ruled this legislative initiative as limiting access to justice and thus unconstitutional. In the case of Greece, the latest piece of legislation aimed at implementing the EU Mediation Directive was adopted in November 2019. The new Greek Mediation Law provides that an initial first attempt to mediate will have to be followed in most civil and commercial cases over 30000 EUR value (as of March 15, 2020) and in most family law ones, namely the ones that refer to private rights that can be freely disposed of (since January 15, 2020).[59]

German Mediation Act (MediationsG)

German Mediation Act (*Mediationsgesetz*), which entered into force in July 2012, transposes the European Mediation Directive into German domestic law. The German Mediation Act covers all forms of mediation in Germany, irrespective of the form of dispute or the place of residence of the parties concerned. It promotes mutual dispute settlement by including a number of different incentives in the official procedural codes (e.g. the Code of Civil Procedure, *Zivilprozessordnung*). Henceforth, for example, when parties bring an action in a civil court, they will have to say whether they have already sought to resolve the issue via out-of-court measures, such as mediation, and whether there are specific reasons for not considering this course of action.[60] In 2017 the German Federal Government published an assessment report which provided, that despite the efforts of the legislator to incentivise conflicting parties to explore mediation the number of mediations in Germany remained at a consistently low level.[61]

Mediation and the EU legislation on insolvency

The Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings[62]

The Regulation on insolvency proceedings in its Article 72 contains a reference to mediation in a provision regarding the coordination of the insolvency of groups of companies ("Tasks and rights of coordinators"): "2. The coordinator may also: (a) be heard and participate, in particular by attending creditors' meetings, in any of the proceedings opened in respect of any member of the group; (b) mediate any dispute arising between two or more insolvency practitioners of group members".

[59] Haris Meidanis, Greece: Mediation Going Compulsory: And They Lived Happily Ever After? *available at* http://mediationblog.kluwerarbitration.com/2020/02/19/greece-mediation-going-compulsory-and-they-lived-happily-ever-after/

[60] Mediation in Member States – Germany available at https://e-justice.europa.eu/content_mediation_in_member_states-64-de-en.do?member=1

[61] Bericht der Bundesregierung über die Auswirkungen des Mediationsgesetzes auf die Entwicklung der Mediation in Deutschland und über die Situation der Aus- und Fortbildung der Mediatoren (Juli 2017) *available at* https://www.bmjv.de/SharedDocs/Artikel/DE/2017/071917_Bericht_Mediationsgesetz.html

[62] The Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings *available at* https://eur-lex.europa.eu/legal-content/en/TXT/?uri=CELEX%3A32015R0848

Commission Recommendation of 12 March 2014 on a new approach to business failure and insolvency (2014/135/EU) [63]

The European Commission highlighted the relevance of mediation to all civil and commercial matters, including the insolvency proceedings. The European Commission, in its Recommendation on a new approach to business failure and insolvency, tried to introduce two new actors in the area of insolvency – a mediator and a supervisor. It has also encouraged the appointment of mediators by courts where they consider it necessary in order to assist the debtor and creditors in the successful running of negotiations on a restructuring plan.
The Commission Recommendation of 12 March 2014 on a new approach to business failure and insolvency read as follows: (No. 17) To promote efficiency and reduce delays and costs, national preventive restructuring frameworks should include flexible procedures limiting court formalities to where they are necessary and proportionate in order to safeguard the interests of creditors and other interested parties likely to be affected. For example, to avoid unnecessary costs and reflect the early nature of the procedure, debtors should in principle be in control of their assets, and the appointment of a mediator or supervisor should not be compulsory but made on a case-by-case basis.

Further Section II B "Facilitating negotiations on restructuring plans" provided:

> "Appointment of a mediator or a supervisor
> 8. Debtors should be able to enter a process for restructuring their business without the need to formally open court proceedings.
> 9. The appointment of a mediator or a supervisor by the court should not be compulsory, but rather be made on a case-by-case basis where it considers such appointment necessary: (a) in the case of a mediator, in order to assist the debtor and creditors in the successful running of negotiations on a restructuring plan;"

These provisions were later confirmed in Recital 18 and Article 5 of the proposed Restructuring Directive, prepared by the European Commission[64].

Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks[65]

In the final text, which was adopted as EU Directive on preventive restructuring frameworks, such a reference to mediation was deleted. It appears that the legislator was not willing to introduce new terms into the legislative landscape. Thus, instead of introducing two new types of actors, i.e. a

[63] Commission Recommendation of 12 March 2014 on a new approach to business failure and insolvency (2014/135/EU) *available at* https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014H0135
[64] Proposal for a Directive of the European Parliament and of the Council of 22 November 2016 on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures and amending Directive 2012/30/EU *available at* https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX%3A52016PC0723&from=DE
[65] Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks, on discharge of debt and disqualifications, and on measures to increase the efficiency of procedures concerning restructuring, insolvency and discharge of debt, and amending Directive (EU) 2017/1132 (Directive on restructuring and insolvency) *available at* https://eur-lex.europa.eu/eli/dir/2019/1023/oj

mediator and a supervisor, the legislator preferred the term "practitioner in the field of restructuring" to identify the people and bodies who may take a leading role in facilitating, organizing or supervising restructuring plans.

According to Article 2 of the Directive on preventive restructuring frameworks, the 'practitioner in the field of restructuring' means any person or body appointed by a judicial or administrative authority to carry out one or more of the following tasks: (a) to assist the debtor or the creditors in drafting or negotiating a restructuring plan; (b) to supervise the activity of the debtor during the negotiations on a restructuring plan and report to a judicial or administrative authority; (c) to take partial control over the assets or affairs of the debtor during negotiations.

Conclusion

The analysis of the EU legislation on insolvency and EU efforts to introduce alternative dispute resolution mechanisms provides that, in principle, mediation may have considerable potential concerning insolvency proceedings in Europe. However, the Member States are still reluctant to introduce mediation as a separate or formal stage of the insolvency proceedings. Such reluctance may well be explained by the lack of a mediation "culture" and the low level of awareness of mediation. The EU Mediation Directive leaves doors open for the use of mediators in insolvency proceedings. The EU Regulation on insolvency proceedings reserves mediation only to a limited number of situations related to coordination of the insolvency of groups of companies. The latest EU Directive on preventive restructuring frameworks, despite efforts of the European Commission, does not contain a direct reference to mediation though one could read between the lines of Article 2 that a 'practitioner in the field of restructuring' who would take on a role as a mediator or who facilitates or steers a mediation process would fall within the frame of the definition.

MEDIATION IN ENGLAND & WALES

Simon Thomas, Partner, Goodwin Procter (UK) LLP

What is mediation and why should parties use it?
Mediation is a flexible form of alternative dispute resolution (ADR), in which a neutral third party assists parties to work towards a negotiated settlement of their dispute, with the parties retaining control of the decision whether or not to settle and on what terms.

There are numerous benefits to engaging with mediation, for example it can help parties work through a deadlock situation that can be created by competitive or positional negotiation; it can help preserve or enhance business relationships; produce outcomes that might not be possible via determination by the court or arbitration; and empower parties to actively participate in the process and control the outcome.

What are the primary sources of law relating to mediation in England & Wales?
The Civil Procedure Rules (CPR) are the primary source of law for mediations in England & Wales. In particular, the parties should have regard to the pre-action protocols that outline the steps that parties take prior to issuing a claim in the courts.

Is there any obligation to mediate in England & Wales?
In England & Wales mediation is a voluntary process. If a party refuses to mediate and such refusal is considered unreasonable, the refusing party runs the risk of court sanctions, namely an adverse costs order.

When can parties mediate in England & Wales?
Mediation can take place at any stage from before issuing court or arbitration proceedings through to appeal. However, getting the timing right will give mediation the best chance of proving cost-effective and successful. The optimum time will differ according to the nature of the case in question and relevant factors may change over time.

Is the mediation process confidential?
Yes, mediation is usually confidential, and the mediation agreement will typically require the parties to treat all discussions and documents as confidential and without prejudice. The confidentiality of the process can avoid issues being made public that the parties want to keep private, as might happen in court proceedings.

What is the mediation style in England & Wales?
There are different styles of mediation in England & Wales, but the most common is facilitative mediation in which, unlike a judge or arbitrator, the mediator will not decide the case on the merits but will work to facilitate agreement between the parties.

What happens at a typical mediation in England & Wales?
The mediator usually has discussions with the lawyers (or the parties if they are not legally represented) in advance of the mediation to ensure that any formalities have been complied with, and to identify the key issues. This helps to ensure that no time is wasted at the mediation.

A typical commercial negotiation will usually involve the mediator greeting the parties on arrival at the mediation session and showing each party to its own private room. Usually, the mediator will formally open the mediation with a joint session, attended by all parties and their lawyers. During this session, the mediator provides an overview of the process, their role and the procedure. Each party then has an opportunity to make an opening statement, giving its perspective on the dispute and highlighting points of particular concern. After the opening, the mediator will have private discussions with each party to assist in the negotiating process.

Ultimately, this may result in the parties reaching a settlement that is either documented at the mediation or shortly thereafter, usually in the form of a settlement agreement. Alternatively, the parties may use the discussions at the mediation as a springboard for further settlement talks after the mediation.

How successful is mediation in England & Wales?
Mediation does not always result in a settlement, but it generally has a high success rate. Mediators who responded to a recent mediation audit carried out by the CEDR in July 2018 reported that just over 74% of their cases settled on the day, with another 15% settling shortly thereafter.

Who pays the cost of mediation in England & Wales?
Who should bear the cost of the mediation is a matter for agreement between the parties? The parties commonly agree to share the mediator's fees and expenses and bear their own legal costs.

What is the future of mediation in England and Wales?
One of the fundamental principles in the CPR is what is known as the "overriding objective" which introduced proportionality to court proceedings, putting parties under pressure to resolve disputes cost effectively. Alongside the introduction of costs management, the obligation to produce costs budgets and a more robust approach to case management and compliance with court orders and directions, means that more parties are viewing the litigation process with less appetite than before and are considering alternative ways of resolving disputes (such as mediation) as a quicker and more cost effective resolution.

In December 2018, the Civil Justice Council, set up a working group to consider issues around ADR and published a report. This report set out 24 recommendations, many of which were directed at introducing more forceful methods to encourage parties to use ADR, though falling short of making mediation compulsory.

How are England & Wales positioned to use mediation in cross-border disputes?
There are international accords which may influence the future of mediation in England and Wales in cross-border disputes. For example, the United Nations Convention on International Settlement Agreements resulting from Mediation, also known as the "Singapore Convention", opened for signature in Singapore on 7 August 2019. The Convention seeks to facilitate international trade by furthering the promotion of mediation as a fast and cost-efficient way of resolving international disputes. At its opening, the Singapore Convention was signed by 46 countries, including China, India and the United States of America. It is currently unknown whether the United Kingdom will enter into the Singapore Convention now it has left the European Union on 31 January 2020.

How is mediation used in insolvency in England & Wales?
By its very nature, insolvency brings about disputes. In terms of litigation of claims, in most cases there are limited assets available and mediation provides a potentially more cost-effective and quicker option to settle disputes rather than pursuing litigation through the court system. Accordingly, mediation is becoming increasingly common as a means of resolving litigation claims in an insolvency context.

One area where mediation, in its formal sense, is not currently used is in respect of financial restructuring. Consensual restructuring outcomes (which avoid liquidation) are achieved without using a formal mediation process. In this scenario, utilising a formal mediation process would not fall within an insolvency practitioners' standard restructuring tool kit.

However, in practice, the skills of a mediator are those which are commonly deployed by insolvency professionals when trying to facilitate restructurings in order to maintain continuity of trading and business rescues, thereby avoiding liquidation.

In terms of the similarity of the role, insolvency practitioners are independent officers of the court and will deploy many of the same skills as mediators in trying to reach an acceptable outcome by building consensus through objectivity.

Examples in practice, whereby a consensual restructuring is agreed and liquidation is avoided, include insolvency professionals agreeing a Company Voluntary Arrangement (CVA) with a company's creditors. In order for the CVA proposal to be carried it requires sufficient support from the Company's creditors. Accordingly, whilst a formal mediation process is not utilised to avoid a liquidation scenario, the same outcome is achieved using a similar set of skills.

THE SINGAPORE CONVENTION ON MEDIATION

Jacob A ("Jack") Esher*
CBInsolvency LLC

THE SINGAPORE CONVENTION IS TO MEDIATION AS:

a. **Getting to Yes is to negotiation**
b. **The Model Law is to cross-border insolvency**
c. **The Hague Convention is to court-approved agreements**
d. **The New York Convention is to arbitration**
e. **All of the above**
f. **None of the above**

TODAY'S quiz (answer below) is about the recent United Nations Convention on International Settlement Agreements Resulting from Mediation - first signed on August 7, 2019 in Singapore by 46 countries (or "States") - also known as the Singapore Convention. One of the 46 countries is the US and most of the others are Asian, while European countries, the UK, and others are likely to join soon.

So what is it and why do we care? In a nutshell, the Convention provides an expeditious enforcement path for out-of-court international mediated settlement agreements resulting from commercial disputes ("IMSA's") in those countries that adopt it, similar to what the New York Convention does for arbitrations. To qualify for this protection, the Convention applies to IMSA's as to which either (i) two or more parties have places of business in different States, or (ii) the place connected with the subject matter of the IMSA or place where the obligations under the IMSA are to be performed are different from the parties' States. Consequently, the Convention could apply to, for example, two US parties with a dispute over a foreign investment or contract – a broader scope than what one might have assumed. But it does not apply to IMSA's reached through court proceedings, insolvency-related or otherwise, provided the IMSA is enforceable as a judgment (more on this below). Consequently, for our purposes, the Convention will have maximum utility in out-of-court restructurings and for the resolution of discrete disputes prior to initiation of an insolvency proceeding.

The Convention addresses a problem that has concerned the international dispute resolution community for years – namely, how to make enforcement of IMSA's as robust as arbitration award enforcement. Prior to this Convention, parties were sometimes reluctant to invest time and cost into mediation because there were no enforcement procedures in place. Enforcement of a mediated agreement would require the initiation of court proceedings the same as a mere contract would – "might as well start there if you might end up there anyway" was a common response. To avoid protracted court proceedings and the possibility of appeals, parties might choose arbitration over mediation because arbitration had the benefit of the long-standing New York Convention on arbitration award enforcement – there would be very few obstacles a party could interpose to their counterparty's enforcement of an arbitration award in a country that had signed on to the NY Convention. IMSA's will soon have similar protection.

Of course, most mediated agreements do not engender enforcement problems to begin with since the resolution is voluntary. However, when you start to have parties from different countries involved, the risk of noncompliance does increase. One of the work-arounds that developed, particularly in Singapore, was an "arb-med-arb" procedure – a mediation would be convened as an arbitration, conducted as a mediation, and an agreement, if reached, would be fashioned as an arbitration award so as to have the benefit of the NY Convention. To avoid overlap with the New York Convention for arbitrations, the Singapore Convention does not apply to mediated settlements reached through an arbitration process, so this process may continue to be used for some time until the Singapore Convention becomes operative in the relevant States.

Similarly, and as mentioned above, to avoid overlap with the Hague Convention for court judgments, the Singapore Convention does not apply to an IMSA that was approved by a court or concluded in the course of proceedings before a court, provided it is enforceable as a judgment in the State of that court. Since the Convention will not apply to a mediated agreement approved in a court-administered or supervised insolvency proceeding, foreign enforcement in countries that have adopted the UNCITRAL Model Law will likely first require that the foreign representative of the proceeding in which the mediated agreement was approved seek recognition of the foreign proceedings. Upon recognition, the foreign representative can seek enforcement of orders entered in the foreign proceeding, whether resulting from mediated settlement agreements or otherwise.

However, the Singapore Convention may be useful as a planning tool to consider before insolvency proceedings are initiated. An out-of-court mediated settlement among a debtor and some or all of its creditor constituencies could be reached outside of the U.S. and enforced in the U.S. in a non-bankruptcy court of appropriate jurisdiction under the Singapore Convention without need for a Chapter 15 case. In that regard, note that the Convention has enforcement exceptions such as for agreements which are contrary to the enforcing state's public policy (similar to Chapter 15), and agreements arising from a process that did not comply with basic mediation standards, such as mediator impartiality.

Whether an IMSA that goes beyond a simple two-party monetary resolution – for example an agreement between a debtor and a class of creditors embodying a complex out-of-court restructuring – can benefit from expedited enforcement remains to be seen. No doubt, creative parties will test the boundaries of the new Convention.

The Convention is notable as another step in the development of mediation as a preferred dispute resolution process generally, and the continuing growth of court and nation acceptance of it. The Convention will become effective after it has been ratified or otherwise entered into force by three signatories, and becomes effective 6 months after ratification in any State.

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United Nations Convention on International Settlement Agreements Resulting from Mediation

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UNITED NATIONS COMMISSION ON INTERNATIONAL TRADE LAW

United Nations Convention on International Settlement Agreements Resulting from Mediation

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Contents

Resolution adopted by the General Assembly on 20 December 2018

[on the report of the Sixth Committee (A/73/496)]

73/198. United Nations Convention on International Settlement Agreements Resulting from Mediation

The General Assembly,

Recalling its resolution 2205 (XXI) of 17 December 1966, by which it established the United Nations Commission on International Trade Law with a mandate to further the progressive harmonization and unification of the law of international trade and in that respect to bear in mind the interests of all peoples, in particular those of developing countries, in the extensive development of international trade,

Recalling also its resolution 57/18 of 19 November 2002, in which it noted the adoption by the Commission of the Model Law on International Commercial Conciliation[1] and expressed the conviction that the Model Law, together with the Conciliation Rules of the Commission[2] recommended in its resolution 35/52 of 4 December 1980, contributes significantly to the establishment of a harmonized legal framework for the fair and efficient settlement of disputes arising in international commercial relations,

Recognizing the value of mediation as a method of amicably settling disputes arising in the context of international commercial relations,

Convinced that the adoption of a convention on international settlement agreements resulting from mediation that is acceptable to States with different legal, social and economic systems would complement the existing legal framework on international mediation and contribute to the development of harmonious international economic relations,

Noting that the decision of the Commission to concurrently prepare a convention on international settlement agreements resulting

[1] Resolution 57/18, annex.

[2] *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17* (A/35/17), para. 106; see also *Yearbook of the United Nations Commission on International Trade Law*, vol. XI: 1980, part three, annex II.

from mediation and an amendment to the Model Law on International Commercial Conciliation was intended to accommodate the different levels of experience with mediation in different jurisdictions and to provide States with consistent standards on the cross-border enforcement of international settlement agreements resulting from mediation, without creating any expectation that interested States may adopt either instrument,[3]

Noting with satisfaction that the preparation of the draft convention was the subject of due deliberation and that the draft convention benefited from consultations with Governments as well as intergovernmental and non-governmental organizations,

Taking note of the decision of the Commission at its fifty-first session to submit the draft convention to the General Assembly for its consideration,[4]

Taking note with satisfaction of the draft convention approved by the Commission,[5]

Expressing its appreciation to the Government of Singapore for its offer to host a signing ceremony for the Convention in Singapore,

1. *Commends* the United Nations Commission on International Trade Law for preparing the draft convention on international settlement agreements resulting from mediation;

2. *Adopts* the United Nations Convention on International Settlement Agreements Resulting from Mediation, contained in the annex to the present resolution;

3. *Authorizes* a ceremony for the opening for signature of the Convention to be held in Singapore on 7 August 2019, and recommends that the Convention be known as the "Singapore Convention on Mediation";

4. *Calls upon* those Governments and regional economic integration organizations that wish to strengthen the legal framework on international dispute settlement to consider becoming a party to the Convention.

62nd plenary meeting
20 December 2018

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[3] *Official Records of the General Assembly, Seventy-second Session, Supplement No. 17* (A/72/17), paras. 238–239; see also A/CN.9/901, para. 52.

[4] *Official Records of the General Assembly, Seventy-third Session, Supplement No. 17* (A/73/17), para. 49.

[5] Ibid., annex I.

United Nations Convention on International Settlement Agreements Resulting from Mediation

Preamble

The Parties to this Convention,

Recognizing the value for international trade of mediation as a method for settling commercial disputes in which the parties in dispute request a third person or persons to assist them in their attempt to settle the dispute amicably,

Noting that mediation is increasingly used in international and domestic commercial practice as an alternative to litigation,

Considering that the use of mediation results in significant benefits, such as reducing the instances where a dispute leads to the termination of a commercial relationship, facilitating the administration of international transactions by commercial parties and producing savings in the administration of justice by States,

Convinced that the establishment of a framework for international settlement agreements resulting from mediation that is acceptable to States with different legal, social and economic systems would contribute to the development of harmonious international economic relations,

Have agreed as follows:

Article 1. Scope of application

1. This Convention applies to an agreement resulting from mediation and concluded in writing by parties to resolve a commercial dispute ("settlement agreement") which, at the time of its conclusion, is international in that:

(a) At least two parties to the settlement agreement have their places of business in different States; or

(b) The State in which the parties to the settlement agreement have their places of business is different from either:

(i) The State in which a substantial part of the obligations under the settlement agreement is performed; or

(ii) The State with which the subject matter of the settlement agreement is most closely connected.

2. This Convention does not apply to settlement agreements:

(a) Concluded to resolve a dispute arising from transactions engaged in by one of the parties (a consumer) for personal, family or household purposes;

(b) Relating to family, inheritance or employment law.

3. This Convention does not apply to:

(a) Settlement agreements:

(i) That have been approved by a court or concluded in the course of proceedings before a court; and

(ii) That are enforceable as a judgment in the State of that court;

(b) Settlement agreements that have been recorded and are enforceable as an arbitral award.

Article 2. Definitions

1. For the purposes of article 1, paragraph 1:

(a) If a party has more than one place of business, the relevant place of business is that which has the closest relationship to the dispute resolved by the settlement agreement, having regard to the circumstances known to, or contemplated by, the parties at the time of the conclusion of the settlement agreement;

(b) If a party does not have a place of business, reference is to be made to the party's habitual residence.

2. A settlement agreement is "in writing" if its content is recorded in any form. The requirement that a settlement agreement be in writing is met by an electronic communication if the information contained therein is accessible so as to be useable for subsequent reference.

3. "Mediation" means a process, irrespective of the expression used or the basis upon which the process is carried out, whereby parties attempt to reach an amicable settlement of their dispute with the assistance of a third person or persons ("the mediator") lacking the authority to impose a solution upon the parties to the dispute.

Article 3. General principles

1. Each Party to the Convention shall enforce a settlement agreement in accordance with its rules of procedure and under the conditions laid down in this Convention.

2. If a dispute arises concerning a matter that a party claims was already resolved by a settlement agreement, a Party to the Convention shall allow the party to invoke the settlement agreement in accordance with its rules of procedure and under the conditions laid down in this Convention, in order to prove that the matter has already been resolved.

Article 4. Requirements for reliance on settlement agreements

1. A party relying on a settlement agreement under this Convention shall supply to the competent authority of the Party to the Convention where relief is sought:

(a) The settlement agreement signed by the parties;

(b) Evidence that the settlement agreement resulted from mediation, such as:

(i) The mediator's signature on the settlement agreement;

(ii) A document signed by the mediator indicating that the mediation was carried out;

(iii) An attestation by the institution that administered the mediation; or

(iv) In the absence of (i), (ii) or (iii), any other evidence acceptable to the competent authority.

2. The requirement that a settlement agreement shall be signed by the parties or, where applicable, the mediator is met in relation to an electronic communication if:

(a) A method is used to identify the parties or the mediator and to indicate the parties' or mediator's intention in respect of the information contained in the electronic communication; and

(b) The method used is either:

(i) As reliable as appropriate for the purpose for which the electronic communication was generated or communicated, in the light of all the circumstances, including any relevant agreement; or

(ii) Proven in fact to have fulfilled the functions described in subparagraph *(a)* above, by itself or together with further evidence.

3. If the settlement agreement is not in an official language of the Party to the Convention where relief is sought, the competent authority may request a translation thereof into such language.

4. The competent authority may require any necessary document in order to verify that the requirements of the Convention have been complied with.

5. When considering the request for relief, the competent authority shall act expeditiously.

Article 5. Grounds for refusing to grant relief

1. The competent authority of the Party to the Convention where relief is sought under article 4 may refuse to grant relief at the request of the party against whom the relief is sought only if that party furnishes to the competent authority proof that:

(a) A party to the settlement agreement was under some incapacity;

(b) The settlement agreement sought to be relied upon:

(i) Is null and void, inoperative or incapable of being performed under the law to which the parties have validly subjected it or, failing any indication thereon, under the law deemed applicable by the competent authority of the Party to the Convention where relief is sought under article 4;

(ii) Is not binding, or is not final, according to its terms; or

(iii) Has been subsequently modified;

(c) The obligations in the settlement agreement:

(i) Have been performed; or

(ii) Are not clear or comprehensible;

(d) Granting relief would be contrary to the terms of the settlement agreement;

(e) There was a serious breach by the mediator of standards applicable to the mediator or the mediation without which breach that party would not have entered into the settlement agreement; or

(f) There was a failure by the mediator to disclose to the parties circumstances that raise justifiable doubts as to the mediator's impartiality or independence and such failure to disclose had a material impact or undue influence on a party without which failure that party would not have entered into the settlement agreement.

2. The competent authority of the Party to the Convention where relief is sought under article 4 may also refuse to grant relief if it finds that:

(a) Granting relief would be contrary to the public policy of that Party; or

(b) The subject matter of the dispute is not capable of settlement by mediation under the law of that Party.

Article 6. Parallel applications or claims

If an application or a claim relating to a settlement agreement has been made to a court, an arbitral tribunal or any other competent authority which may affect the relief being sought under article 4, the competent authority of the Party to the Convention where such relief is sought may, if it considers it proper, adjourn the decision and may also, on the request of a party, order the other party to give suitable security.

Article 7. Other laws or treaties

This Convention shall not deprive any interested party of any right it may have to avail itself of a settlement agreement in the manner and to the extent allowed by the law or the treaties of the Party to the Convention where such settlement agreement is sought to be relied upon.

Article 8. Reservations

1. A Party to the Convention may declare that:

(a) It shall not apply this Convention to settlement agreements to which it is a party, or to which any governmental agencies or any person acting on behalf of a governmental agency is a party, to the extent specified in the declaration;

(b) It shall apply this Convention only to the extent that the parties to the settlement agreement have agreed to the application of the Convention.

2. No reservations are permitted except those expressly authorized in this article.

3. Reservations may be made by a Party to the Convention at any time. Reservations made at the time of signature shall be subject to confirmation upon ratification, acceptance or approval. Such reservations shall take effect simultaneously with the entry into force

of this Convention in respect of the Party to the Convention concerned. Reservations made at the time of ratification, acceptance or approval of this Convention or accession thereto, or at the time of making a declaration under article 13 shall take effect simultaneously with the entry into force of this Convention in respect of the Party to the Convention concerned. Reservations deposited after the entry into force of the Convention for that Party to the Convention shall take effect six months after the date of the deposit.

4. Reservations and their confirmations shall be deposited with the depositary.

5. Any Party to the Convention that makes a reservation under this Convention may withdraw it at any time. Such withdrawals are to be deposited with the depositary, and shall take effect six months after deposit.

Article 9. Effect on settlement agreements

The Convention and any reservation or withdrawal thereof shall apply only to settlement agreements concluded after the date when the Convention, reservation or withdrawal thereof enters into force for the Party to the Convention concerned.

Article 10. Depositary

The Secretary-General of the United Nations is hereby designated as the depositary of this Convention.

Article 11. Signature, ratification, acceptance, approval, accession

1. This Convention is open for signature by all States in Singapore, on 7 August 2019, and thereafter at United Nations Headquarters in New York.

2. This Convention is subject to ratification, acceptance or approval by the signatories.

3. This Convention is open for accession by all States that are not signatories as from the date it is open for signature.

4. Instruments of ratification, acceptance, approval or accession are to be deposited with the depositary.

Article 12. Participation by regional economic integration organizations

1. A regional economic integration organization that is constituted by sovereign States and has competence over certain matters governed by this Convention may similarly sign, ratify, accept, approve or accede to this Convention. The regional economic integration organization shall in that case have the rights and obligations of a Party to the Convention, to the extent that that organization has competence over matters governed by this Convention. Where the number of Parties to the Convention is relevant in this Convention, the regional economic integration organization shall not count as a Party to the Convention in addition to its member States that are Parties to the Convention.

2. The regional economic integration organization shall, at the time of signature, ratification, acceptance, approval or accession, make a declaration to the depositary specifying the matters governed by this Convention in respect of which competence has been transferred to that organization by its member States. The regional economic integration organization shall promptly notify the depositary of any changes to the distribution of competence, including new transfers of competence, specified in the declaration under this paragraph.

3. Any reference to a "Party to the Convention", "Parties to the Convention", a "State" or "States" in this Convention applies equally to a regional economic integration organization where the context so requires.

4. This Convention shall not prevail over conflicting rules of a regional economic integration organization, whether such rules were adopted or entered into force before or after this Convention: *(a)* if, under article 4, relief is sought in a State that is member of such an organization and all the States relevant under article 1, paragraph 1, are members of such an organization; or *(b)* as concerns the recognition or enforcement of judgments between member States of such an organization.

Article 13. Non-unified legal systems

1. If a Party to the Convention has two or more territorial units in which different systems of law are applicable in relation to the matters dealt with in this Convention, it may, at the time of signature, ratification, acceptance, approval or accession, declare that this Convention is to extend to all its territorial units or only to one or more of them, and may amend its declaration by submitting another declaration at any time.

2. These declarations are to be notified to the depositary and are to state expressly the territorial units to which the Convention extends.

3. If a Party to the Convention has two or more territorial units in which different systems of law are applicable in relation to the matters dealt with in this Convention:

(a) Any reference to the law or rule of procedure of a State shall be construed as referring, where appropriate, to the law or rule of procedure in force in the relevant territorial unit;

(b) Any reference to the place of business in a State shall be construed as referring, where appropriate, to the place of business in the relevant territorial unit;

(c) Any reference to the competent authority of the State shall be construed as referring, where appropriate, to the competent authority in the relevant territorial unit.

4. If a Party to the Convention makes no declaration under paragraph 1 of this article, the Convention is to extend to all territorial units of that State.

Article 14. Entry into force

1. This Convention shall enter into force six months after deposit of the third instrument of ratification, acceptance, approval or accession.

2. When a State ratifies, accepts, approves or accedes to this Convention after the deposit of the third instrument of ratification, acceptance, approval or accession, this Convention shall enter into force in respect of that State six months after the date of the deposit of its instrument of ratification, acceptance, approval or accession. The Convention shall enter into force for a territorial unit to which this Convention has been extended in accordance with article 13 six months after the notification of the declaration referred to in that article.

Article 15. Amendment

1. Any Party to the Convention may propose an amendment to the present Convention by submitting it to the Secretary-General of the United Nations. The Secretary-General shall thereupon communicate the proposed amendment to the Parties to the Convention with a request that they indicate whether they favour a conference of Parties to the Convention for the purpose of considering and voting upon the proposal. In the event that within four months from the date of such communication at least one third

of the Parties to the Convention favour such a conference, the Secretary-General shall convene the conference under the auspices of the United Nations.

2. The conference of Parties to the Convention shall make every effort to achieve consensus on each amendment. If all efforts at consensus are exhausted and no consensus is reached, the amendment shall, as a last resort, require for its adoption a two-thirds majority vote of the Parties to the Convention present and voting at the conference.

3. An adopted amendment shall be submitted by the depositary to all the Parties to the Convention for ratification, acceptance or approval.

4. An adopted amendment shall enter into force six months after the date of deposit of the third instrument of ratification, acceptance or approval. When an amendment enters into force, it shall be binding on those Parties to the Convention that have expressed consent to be bound by it.

5. When a Party to the Convention ratifies, accepts or approves an amendment following the deposit of the third instrument of ratification, acceptance or approval, the amendment shall enter into force in respect of that Party to the Convention six months after the date of the deposit of its instrument of ratification, acceptance or approval.

Article 16. Denunciations

1. A Party to the Convention may denounce this Convention by a formal notification in writing addressed to the depositary. The denunciation may be limited to certain territorial units of a non-unified legal system to which this Convention applies.

2. The denunciation shall take effect 12 months after the notification is received by the depositary. Where a longer period for the denunciation to take effect is specified in the notification, the denunciation shall take effect upon the expiration of such longer period after the notification is received by the depositary. The Convention shall continue to apply to settlement agreements concluded before the denunciation takes effect.

DONE in a single original, of which the Arabic, Chinese, English, French, Russian and Spanish texts are equally authentic.

DECEMBER 8, 2017

New York Judge Bars Use of Chapter 15 to Disrupt a Foreign Bankruptcy

> ‘Bankruptcy tourism’ seems unaffected by an unusual cross-border insolvency.

Bankruptcy Judge Sean H. Lane declined an invitation for the bankruptcy court in New York to become a weapon designed to disrupt a reorganization in Brazil, where the U.S. court had already granted foreign main recognition under chapter 15.

Because the facts are so unique, Judge Lane’s Dec. 4 opinion probably does not undercut the ordinarily successful facet of so-called bankruptcy tourism, where a company located in a nation with unfavorable bankruptcy laws initiates insolvency proceedings in a more favorable forum where it is incorporated, such as Cayman Islands, and then obtains chapter 15 recognition in the U.S.

Judge Lane’s 120-page opinion is an exhaustive analysis of chapter 15 caselaw generally, with particular emphasis on the ability under Section 1517 to revoke or modify a previous ruling about a foreign company’s center of main interest, or COMI. If the opinion means anything, it means that a creditor must litigate the debtor’s COMI when the opportunity

anything, it means that a creditor must litigate the debtor's COMI when the opportunity first arises, because a U.S. court will be disinclined to alter a previous ruling on COMI when proceedings are underway in the court that first received foreign main recognition.

The Brazilian Debtors

The case involved one of Brazil's largest telecommunications providers, known as the Oi Group. The group included a wholly owned Dutch financing subsidiary whose sole business was to issue notes. In turn, the Dutch company would loan proceeds from the note issues to Brazilian affiliates to finance their activities. Of course, the Dutch company had receivables from the affiliates who received the proceeds, and the Brazilian parent guaranteed the notes.

Consequently, holders of the Dutch company's notes theoretically had two means of collection: from the Dutch issuer and through the parent's guarantee. Ultimately, however, the ability to recover on the Dutch-issued notes depends on the economic success of the Brazilian affiliates because the Dutch financing subsidiary has no substantial assets aside from the receivables owing by its affiliates.

Soon after four members of the Oi Group, including the Dutch financing subsidiary, initiated reorganization proceedings in Brazil, several holders of the Dutch-issued notes initiated an involuntary bankruptcy in the Netherlands against the Dutch financing subsidiary. As a defensive measure, Judge Lane said, the Dutch company commenced a suspension of proceedings in the Netherlands entailing a general moratorium on actions by unsecured creditors. The Dutch court appointed an independent individual to become the administrator.

Meanwhile, the four members of the group, including the Dutch financing subsidiary, sought recognition of the Brazilian proceedings as their foreign main proceeding.

Granting foreign main recognition to the four companies, Judge Lane had no difficulty finding that Brazil was the COMI for three of them. They were incorporated in Brazil and operated there. The Dutch company's COMI was more problematic because, unlike its corporate cousins, it was incorporated in the Netherlands and thus could not benefit from the presumption in Section 1516(c) that the place of incorporation was also the COMI.

In his recognition decision in July 2016, Judge Lane found that Brazil was also the COMI of the Dutch company under caselaw allowing a financing subsidiary to have its COMI at the group's nerve center in Brazil.

Although they were present in the recognition proceedings last year, U.S. hedge funds holding the Dutch-issued bonds did not object to the finding that the Dutch company's COMI was Brazil.

Meanwhile, the hedge funds persuaded the administrator in the Dutch proceedings to move for conversion to bankruptcy. Although the lower court did not convert, the Dutch appellate court reversed and switched the proceedings to bankruptcy. The same individual who had been the administrator continued as the insolvency trustee for the Dutch company.

With support and financing from the hedge funds, the Dutch trustee filed pleadings in New York to modify last year's recognition order by recognizing the Dutch bankruptcy as the foreign main proceeding for the Dutch subsidiary.

Writing an opinion that is must reading for anyone versed in cross-border insolvency law, Judge Lane refused to change last year's recognition order.

Section 1517(a) or (d)?

The hedge funds, as holders of the Dutch-issued notes, argued that Judge Lane should rule on recognition under Section 1517(a), which lays out the criteria for granting foreign recognition.

The Brazilian parent disagreed, contending that Section 1517(d) controls. That subsection deals with the modification or termination of previously granted recognition. In addition, the parent argued that the court must impose the standards in Rule 60(b) of the Federal Rules of Civil Procedure to alter the prior recognition order.

Judge Lane made short shrift of the bondholders' contention that Section 1517(a) governed. Were that the case, he said, it would read subsection (d) out of the statute.

However, Rule 60(b) does not apply, Judge Lane said, because Section 1517(d) contains a flexible discretionary standard that would be at odds with Rule 60(b).

Judicial Estoppel

Judicial Estoppel

The bondholders raised judicial estoppel arguments, contending that the Brazilian parent admitted that the Netherlands was the COMI for the Dutch subsidiary when initiating the Dutch suspension of proceedings.

The European Union regulations at play in the Dutch proceedings are not an implementation of the UNCITRAL Model Law from which chapter 15 was taken, Judge Lane said. Unlike the E.U. regulations, chapter 15 gives "limited weight" to the presumption of COMI as being the country of incorporation. For a variety of reasons, Judge Lane said that the Dutch court was not misled about the finance subsidiary's COMI, thus making judicial estoppel inapplicable.

Abstention and Comity

According to the hedge funds, the U.S. court should grant comity to the Dutch court's conclusion about the Dutch subsidiary's COMI.

Unlike the European regulations where one nation's decision on COMI is binding on other countries in the E.U., Judge Lane said that Section 1517 does not mention comity. He concluded that a U.S. court can "make its own determination on recognition in this case, rather than defer to the Dutch courts."

Applying Section 1517(d) to the Facts

Having decided that Section 1517(d) governs, Judge Lane applied the law to the facts, concluding that he would not exercise discretion to modify his prior recognition order and change the Dutch subsidiary's COMI to the Netherlands.

Section 1517(d) provides that chapter 15 does "not prevent modification or termination of recognition if it is shown that the grounds for granting it were fully or partially lacking or have ceased to exist . . . ." Analyzing an extensive trial record in detail, Judge Lane concluded there was no basis for exercising discretion to modify his COMI finding last year with regard to the Dutch subsidiary.

Then, Judge Lane announced another reason for declining to exercise discretion: the "behavior" of the hedge fund holders of the Dutch-issued bonds. He began by noting that the bondholders had not objected in the proceedings last year when he found that Brazil was the COMI of the Dutch subsidiary. He said that the bondholders' silence was part of a strategy aimed at derailing the reorganization that might emerge in Brazil.

strategy aimed at derailing the reorganization that might emerge in Brazil. According to Judge Lane, the holders of the Dutch bonds are hoping for a so-called double dip. They aim to recover once on their guarantee issued by the Brazilian parent and a second time, on the same debt, by a recovery from the Dutch subsidiary's claim against the parent. The bondholders are afraid, Judge Lane said, that the Brazilian proceeding would end with substantive consolidation, giving the bondholders only one dip.

If the Dutch proceedings were given foreign main recognition, Judge Lane said that the "credible evidence" indicated that the bondholders intended to use foreign main recognition of the Dutch proceedings "to block this court's recognition of the Oi Group's Brazilian plan."

He said that "the evidence here presents a disturbing picture: a creditor unhappy with Brazilian insolvency proceedings decided to strategically remain silent through a chapter 15 recognition of those proceedings . . . while planning . . . a strategy designed to reverse that recognition and block any restructuring in the Brazilian proceeding." The strategy, the judge said, is "at odds with many of the goals of chapter 15," such as "promoting cooperation between U.S. and foreign courts, greater legal certainty . . . [and] fair and efficient administration of cross-border insolvencies . . . ."

Near the end of the opinion, Judge Lane said that the bondholders' strategy "is a troubling one that the court refuses to countenance." That conclusion, he said, influenced the exercise of his discretion under Section 1517(d).

Although Judge Lane refused to modify his prior grant of foreign main recognition to the Brazilian bankruptcy, he did not forever slam the door shut on the bondholders. He said that the bondholders can come back to the U.S. court later "and challenge the recognition of any plan approved in" the Brazilian reorganization.

Opinion Link

http://www.nysb.uscourts.gov/sites/default/files/opinions/267397_174_opinion.pdf

Case Details

Judge Name Sean H. Lane

Case Citation	In re Oi Brasil Holdings Cooperatief UA, 16-11794 (Bankr. S.D.N.Y. Dec. 4, 2017)
Case Name	In re Oi Brasil Holdings Cooperatief UA
Case Type	Business
Court	2nd Circuit New York New York Southern District
Bankruptcy Tags	Bankruptcy Litigation Practice and Procedure Business Reorganization International Insolvency

[+] FEEDBACK

European Update

By Adam Gallagher, Toby Smyth and Madlyn Gleich Primoff

Is the New U.K. Restructuring Plan a Viable Alternative to Chapter 11?

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Editor's Note: *Transatlantic restructurings may have just gotten a little easier. Until now, transatlantic companies with New York law-governed debt looking to implement a balance-sheet restructuring enforceable against creditors in both the U.S. and Europe have primarily had two choices: a chapter 11 plan under the U.S. Bankruptcy Code, on the one hand, and on the other hand, a U.K. scheme of arrangement filed under Part 26 of the Companies Act 2006, coupled with recognition under chapter 15 of the U.S. Bankruptcy Code. At times, neither has been the perfect fit. Now, there is a new kid on the block.*

The U.K. government has enacted the Corporate Insolvency and Governance Act, which supplements the U.K.'s existing insolvency framework with new restructuring tools. One such tool is the new, but long-awaited, restructuring plan.[1] With certain characteristics that bring the position under the traditional scheme of arrangement more in line with that under chapter 11, the restructuring plan could be the versatile solution that transatlantic companies have been searching for under certain circumstances.

Is the Restructuring Plan Just a U.K. Chapter 11?

There certainly are many similarities. As is the case with a scheme of arrangement, both chapter 11 and the restructuring plan are (1) court-sanctioned processes that can be initiated by companies (including foreign companies with an appropriate connection to the U.S. or U.K., respectively); (2) recognized cross-border; (3) used to compromise secured creditors, unsecured creditors and shareholders; or (4) involve a high degree of public disclosure. However, they do not affect the directors' ordinary-course management powers.

The similarities do not stop there. Unlike a scheme of arrangement, both chapter 11 and the restructuring plan can be used to cram down dissenting classes of creditors and to implement a debt-for-equity swap without shareholder consent.

Both processes can be pre-planned and implemented relatively quickly by early negotiation and, where required, entering plan-support or lock-up agreements. As an indication, a chapter 11 could be implemented in approximately 45-90 days (although recent examples of a "speedy" pre-pack have required just 24 hours). A scheme of arrangement, which should be able to be used as a reasonable proxy for a restructuring plan, can be implemented in a similar time frame following commercial agreement.

In chapter 11, the company must place the claims of creditors into classes (based on their rights and interests, including the source of their debt and security in collateral). The company's chapter 11 plan requires the approval of at least one non-insider impaired class. The company will seek the bankruptcy court's approval of a disclosure statement and confirmation of its plan, and if approved, a confirmation order is issued by the court that binds all creditors.

For a U.K. restructuring plan, two court hearings will be held, and creditors (and/or shareholders) will be split into classes in a similar way. Creditors must be provided with sufficient information to make an informed decision (similar to an explanatory statement for a scheme of arrangement). Creditors or shareholders can challenge the class formation at the initial court hearing.

Once satisfied, the court will order that a vote of creditors and shareholders is taken, unless the applicant can convince the court that a class of creditors or shareholders has no genuine economic interest in the restructuring plan and therefore should be excluded. Subject to the voting threshold being passed, the court will consider whether to sanction the restructuring plan at a second court hearing. If sanctioned, the restructuring plan will bind all affected creditors.

How Are the Processes Different?

There remain several key differences between a chapter 11 and a restructuring plan. Different tools will be able to deliver different solutions. It is vital to assess at the outset what, in any given situation, is most important — and which tool is more likely to achieve this.

Voting Thresholds

A key factor when selecting the most appropriate implementation tool is the level of support required to approve the proposed restructuring. For

1 Companies Act 2020, Pt 26A.

a chapter 11, the company needs to secure, with respect to those creditors in the class that vote, (1) a majority in number, and (2) two-thirds in value of claims in a given class for that creditor class to accept a plan.

From a debtor's perspective, one disadvantage of a scheme of arrangement is that it requires a higher voting threshold. To obtain approval, the company must secure the votes of a majority in number and three-quarters in value of each class of creditors present and voting. These requirements have been relaxed under a restructuring plan, as the first test (majority in number) has been abolished.

So, a restructuring plan may be more attractive to a debtor than a chapter 11 where a dissenting minority of creditor claims of a necessary non-insider impaired class are held in a disproportionately large number of funds. However, a chapter 11 would be more attractive where the debtor cannot be certain of reaching the 75 percent in value threshold.

Cross-Class Cram Down and Debt-for-Equity Swaps

Closely linked to voting thresholds is whether the consent of all classes is required. Historically, a major advantage of chapter 11 has been the ability to cram down dissenting classes of creditors (known as a "cross-class cram down" in the U.K.) and to bind dissenting creditors within a class, so long as the voting thresholds are met.

In chapter 11, cross-class cram down is possible provided that (1) at least one impaired (non-insider) class votes in favor, (2) the plan does not discriminate unfairly toward each impaired class that has voted against it, and (3) the plan is fair and equitable to the non-consenting class, which will be the case if (a) secured creditors receive either deferred cash payments (and interest thereon) equal to at least the value of their collateral or the indubitable equivalent of their claims and collateral (cannot be equity in the reorganized debtor), and (b) unsecured creditors (which might be paid in any combination of cash, notes and/or equity in a cram-down) are paid in full before any more junior class of claims or interests receives any recovery (known as the "absolute-priority rule").

Cross-class cram down is not available in a scheme of arrangement, one of the major drawbacks of the process to date. However, under a restructuring plan, cross-class cram down will be permitted for the first time in the U.K. if the following conditions are met: (1) the U.K. court is satisfied that none of the members of the dissenting class would be any worse off than in the event of the most likely relevant alternative scenario, as determined by the court (known as "Condition A"); and (2) the restructuring plan has been agreed to by a class that would receive payment or has a genuine economic interest in the company in the event of the relevant alternative (known as "Condition B").

Crucially, for cross-class cram down under a restructuring plan there is no absolute-priority rule. Consequently, the authors can envisage arguments that equity in the restructured enterprise can be given to the existing shareholders where, for example, the efforts of shareholder management are required for the successful future operation of the restructured business, despite the impairment of junior creditors. On its face, this is a breach of the absolute-priority rule. This might be justified where the equity is gifted from what would otherwise have been the senior creditors' share, but the difficulty will be justifying an equity allocation to former shareholders in circumstances in which the senior creditors are not prepared to gift that value from what would otherwise have been their entitlement, and it is instead to be taken from value that might otherwise be enjoyed by junior creditors. Although this is conceptually possible, just how far the court will be prepared to go when asked to sanction a restructuring plan that does not respect the absolute-priority rule remains to be seen.

Novel for the U.K., the authors could also see a form of "cram up" whereby junior creditors seek to impose a haircut on more senior creditors, although this could be challenging in practice. For example, this could result in increased focus on whether the juniors have the right to participate in the prescribed part (*i.e.*, the £600/800k pot of floating charge realisations in a U.K. insolvency available for distribution to unsecured creditors) or if any unsecured assets could generate realizations. The court will ultimately assess these points and decide, in its absolute discretion, whether to sanction the restructuring plan. So both chapter 11 and the restructuring plan can be used to implement a debt-for-equity swap without shareholder consent, and both can be used to cram down dissenting classes.

Stay-of-Enforcement Efforts

Transatlantic trading companies will be keen to obtain protection from creditor enforcement to enable their businesses to continue to trade while a restructuring is implemented. A chapter 11 petition gives rise to a statutory injunction (known as an "automatic stay"), which automatically comes into effect immediately upon the commencement of a chapter 11 case. The automatic stay prohibits all actions against the company by creditors, wherever they are located (due to the wide reach of the U.S. bankruptcy courts).

In addition, subject to certain limited exceptions, the filing of a bankruptcy petition will prevent counterparties from terminating contracts with the debtor (called "*ipso facto* clauses"). The stay and restrictions on *ipso facto* clauses have proven to be valuable tools to allow a business to continue trading while implementing a rescue.

In contrast, the Corporate Insolvency and Governance Act does not include a stay during the restructuring-plan process. In rare situations, however, the court has ordered a short stay on enforcement for a scheme of arrangement (which again should be a reasonable proxy for a restructuring plan). Other reforms implemented by this legislation introduce a freestanding moratorium that could be used alongside a restructuring plan, if the company is eligible; there are broad categories of companies that are not, such as companies that are party to capital markets arrangements. Similarly, other reforms introduced in the legislation provide for a restriction on *ipso facto* clauses for

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the supply of goods and services contracts, and this will be triggered where the court summons a meeting under a restructuring plan.

Thus, a chapter 11 is likely to continue to be attractive if an automatic (and worldwide) stay and protection of contracts is key. The U.K. regime can now achieve this, too, in certain circumstances.

DIP Financing

Funding is critical to many companies going through a rescue process. The U.S. Bankruptcy Code permits a company to obtain debtor-in-possession (DIP) financing while in bankruptcy in order to operate the business in chapter 11 and pay the costs of the process. The Code also grants the lenders of such DIP financing super-priority status, so long as the court is satisfied that the company cannot obtain such financing on less-burdensome terms, and non-consenting pre-petition secured lenders that are primed are "adequately protected."

On the other hand, in the U.K. there are no provisions for higher-ranking financing (any such priority is a matter of contractual agreement). The courts have also held that a scheme of arrangement (which can be used as a useful proxy for the restructuring plan) cannot impose new obligations on creditors to advance money. The restructuring plan itself can, post-implementation, provide for existing contractual priorities to be changed to permit new money with higher-ranking priority. Chapter 11 continues to be the go-to where DIP financing is the key to funding the restructuring, rather than funding the company after the restructuring.

Group Guarantees

Another element a large transatlantic group might look at when assessing restructuring venues is whether the restructuring process can release guarantees provided by group companies for the borrowing of another member of the same group. Ahead of a chapter 11, given that a group guarantor would not normally receive the direct benefit of the automatic stay or the other advantages of a chapter 11 filing of the borrower (*e.g.*, DIP financing), the group will need to carefully consider whether each guarantor will also need to file for chapter 11 in order to obtain the protection required by the group as a going concern (which might necessitate additional time and costs).

By contrast, the restructuring plan (akin to a scheme of arrangement) should be able to release group guarantees where they are closely connected to the primary obligation being compromised under the restructuring plan (given that without such a release the restructuring plan would be of limited use, as the lenders could still pursue the group guarantors). It is unlikely that such a guarantor release would be effective if the debt was U.S.-law governed and the guarantors were in the U.S.

Expense

Any company will also look at the costs involved in the process. Is there a forum where the restructuring can be achieved for a lower cost?

Chapter 11 has often been criticized as being a costly tool. The widespread adoption of pre-packaged and pre-arranged chapter 11 cases has largely eliminated any distinction between the costs of chapter 11 and the costs of a scheme of arrangement. The costs of a free-fall chapter 11 case, however, continue to be substantial. This is largely due to the ongoing and frequent court involvement and the establishment of creditors' committees paid by debtors.

The restructuring plan is analogous to a pre-arranged case in the U.S. and thus would be less costly than a free-fall case. Although there are two court hearings (the convening and the sanction hearing), once the restructuring plan is approved and sanctioned by the court, there is no ongoing court involvement in the implementation of the restructuring plan.

Court Discretion

The restructuring plan involves, as a final step, the sanction of the U.K. court. For a scheme of arrangement, the court has made it very clear that this is not a rubber-stamping exercise and that even if the necessary voting majorities are met, the court retains absolute discretion on whether to sanction the scheme of arrangement. The restructuring plan also provides for court discretion, both where there is cross-class cram down and where there is not.

By contrast, in chapter 11, when the confirmation requirements (which include that the plan is proposed in good faith and complies with the applicable provisions of the U.S. Bankruptcy Code) have been met, the court will proceed to approve the plan. How much the U.K. court will make of its discretion will remain to be seen, and only case law will tell.

Conclusion: Has a Restructuring Plan Come Together?

The new restructuring plan is clearly a move by the U.K. in the direction of the U.S. chapter 11 and an improvement on the existing scheme of arrangement. The inclusion of cross-class cram down, along with the absence of the absolute-priority rule and numerosity test, may make the restructuring plan a flexible and attractive option for transatlantic companies in the right circumstances.

Nevertheless, it is hard not to think that this has been a missed opportunity. Without DIP financing, a broader moratorium and a stronger shield from *ipso facto* clauses, it is unlikely the restructuring plan will replace chapter 11 any time soon. What it does do, however, is provide transatlantic companies with more options, each to be considered on the merits of the individual case. abi

The International Scene

By Daniel M. Glosband[1]

Abstention and Chapter 15

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As chapter 15 cases proliferate, litigation in and related to those cases grows apace. Either the plaintiff or defendant may wish, for its particular reasons, to have the bankruptcy court abstain from the litigation. When abstention is statutorily mandated, the bankruptcy court can and must abstain. However, when abstention is permissive, the bankruptcy court's ability to abstain is uncertain because some courts have limited the applicability of permissive abstention in chapter 15 cases.

Bankruptcy jurisdiction in the U.S. derives from title 28 of the U.S. Code, Judiciary and Judicial Procedure (the "Judicial Code"). Specifically, 28 U.S.C. § 1334(a) grants "the district court ... original and exclusive jurisdiction of all cases under title 11," while 28 U.S.C. § 1334(b) provides that "the district courts shall have original but not exclusive jurisdiction of all civil proceedings arising under title 11, or arising in or related to cases under title 11."[2] That jurisdiction is limited by provisions dealing with permissive abstention under 28 U.S.C. § 1334(c)(1) and mandatory abstention under 28 U.S.C. § 1334(c)(2).

The introductory language of § 1334(c)(1) complicates the application of the abstention provisions to a chapter 15 case: "*Except with respect to a case under chapter 15 of title 11*, nothing in this section prevents a district court ... from abstaining from hearing a particular proceeding arising under title 11 or arising in or related to a case under title 11." This language has been held by some courts — incorrectly, in this author's opinion — to prohibit permissive abstention from any proceedings arising in or related to a chapter 15 case.

Conflicting Views on Permissive Abstention

When three Louisiana state pension funds sued Cayman Island hedge funds and others in Louisiana state court, the defendants removed the case to federal district court under 28 U.S.C. § 1452 as related to a chapter 11 case of a master fund to which the Cayman Islands funds were related.[3] The plaintiffs sought remand back to state court, where they presumably preferred their chances of success. The Fifth Circuit, in *Firefighters' Retirement System v. Citco Group Ltd.*, ruled that 28 U.S.C. § 1334(c)(1) bars abstention from any proceeding in a chapter 15 case and therefore bars remand:

> We have not previously addressed the extent to which this provision [28 U.S.C. § 1334(c)(1)] bars permissive abstention in Chapter 15 bankruptcy cases. There are two possible interpretations of the subsection. First, the phrase "[e]xcept with respect to a case under chapter 15 of title 11" could mean that § 1334(c)(1) only excepts the Chapter 15 bankruptcy itself. *See, e.g., Abrams v. Gen. Nutrition Cos.*, 2006 U.S. Dist. LEXIS 68574 (D.N.J. Sept. 25, 2006) (unpublished) (adopting this interpretation). Second, the phrase could mean that both the Chapter 15 case itself and cases "arising in or related to" Chapter 15 cases are excluded. *See, e.g., British Am. Ins. Co. v. Fullerton (In re British Am. Ins. Co.)*, 488 B.R. 205, 238-39 (Bankr. S.D. Fla. 2013) (adopting the latter interpretation); *Fairfield Sentry Ltd. v. Amsterdam (In re Fairfield Sentry Ltd.)*, 452 B.R. 64, 83 (Bankr. S.D.N.Y. 2011) (same), *rev'd on other grounds*, 458 B.R. 665 (S.D.N.Y. 2011).
>
> We hold that the latter interpretation is more consistent with the plain language and purpose of the statute. If one reads the rest of the subsection after the initial clause, the subsection clearly distinguishes between a "case" and a "proceeding."[4]

The "case" vs. "proceeding" distinction should have led to the opposite conclusion: abstention from a proceeding is permitted. By definition, a "petition" under § 1504 (as under §§ 301, 302 and 303) "commences a *case* under this title [11]."[5] Similarly, chapter 15 is titled, "Ancillary and Other Cross-Border *Cases*." It is the bankruptcy case itself — here, the chapter 15 ancillary case — that is the case.

Conversely, matters within or related to the case that may be litigated, as adversary proceedings or contested matters, are proceedings. Nothing in the exception to Judicial Code § 1334(c)(1) mentions "a particular proceeding arising under title 11 or arising in or related to a case under

1 The author is one of the two primary draftsmen of chapter 15 (with Prof. **Jay L. Westbrook** of the University of Texas School of Law) and the author of the chapter 15 sections of *Collier on Bankruptcy* (16th ed.). He wishes to thank his CBInsolvency colleague **Jacob A. Esher** for his review and assistance with the article.

2 28 U.S.C. § 157(a) provides that the district court may refer any or all cases under title 11 and any or all proceedings arising under title 11 or arising in or related to a case under title 11 to the bankruptcy court for the district.

3 The master fund in chapter 11 in the Southern District of New York (SDNY) was *Fletcher Int'l Ltd.*, Case No. 1:12-bk-12796; the defendant in the *Firefighters'* case, feeder fund FIA Leveraged Fund and its affiliated feeder fund, Fletcher Income Arbitrage Fund Ltd. were in liquidation in the Cayman Islands and their foreign representatives obtained chapter 15 recognition in the SDNY cases No. 14- 10093 and 14-10094.

4 796 F.3d 520, 526-27 (5th Cir. 2015).

5 11 U.S.C. § 101(42).

title 11" or limits post-recognition abstention or dismissal of proceedings in chapter 15 cases that arise under, in or are related to title 11.

The National Bankruptcy Conference (NBC) consists of approximately 60 judges, lawyers and academics who have consulted with Congress on bankruptcy legislation since the 1930s and whose conferees include the primary draftsmen of chapter 15. They view the Judicial Code exception to permissive abstention as limited to preventing abstention from hearing an application for recognition of a foreign proceeding (*i.e.*, from deciding the "case under chapter 15").[6]

Sections 305 and 1529 Allow Permissive Abstention in Chapter 15

Firefighters' neither noted nor discussed two other statutory provisions, §§ 305 and 1529 of the Bankruptcy Code, which support permissive abstention from proceedings in chapter 15 cases. Section 1529(a)(4), within chapter 15, states: "In achieving cooperation and coordination under sections 1528 and 1529, the court may grant any of the relief authorized under section 305."[7] In turn, § 305 provides:

> (a) The court, after notice and a hearing, may dismiss a case under this title, or may suspend all proceedings in a case under this title, at any time if— ...
>
> (2)(A) a petition under section 1515 for recognition of a foreign proceeding has been granted; and (B) the purposes of chapter 15 of this title would be best served by such dismissal or suspension.
>
> (b) A foreign representative may seek dismissal or suspension under subsection (a)(2) of this section.[8]

The *Firefighters'* interpretation of 28 U.S.C. § 1334(c)(1) results in rendering §§ 305(a)(2) and 1529(4) unworkable. This violates the basic rule of statutory construction that one part of a statute or of related statutes should not be read to negate other parts of the statute(s).[9]

Surprisingly, none of the *Firefighters'* or *British American* and *Fairfield Sentry* decisions it cited acknowledged the existence of § 1529(4), which authorizes the bankruptcy court to employ § 305. The *British American* court stated that "Congress required that if the district courts (and the bankruptcy courts by referral) have related-to jurisdiction, and the matter is not subject to mandatory abstention under section 1334(c)(2), then the court must hear the matter."[10] However, Congress said just the opposite in § 1529(4).

Mandatory Abstention Remains Clearly Applicable in Chapter 15

Unlike the confusion over permissive abstention, mandatory abstention is indisputably applicable to chapter 15 cases. Section 1334(c)(2) states:

> Upon timely motion of a party in a proceeding based upon a State law claim or State law cause of action, related to a case under title 11 but not arising under title 11 or arising in a case under title 11, with respect to which an action could not have been commenced in a court of the United States absent jurisdiction under this section, the district court shall abstain from hearing such proceeding if an action is commenced, and can be timely adjudicated, in a State forum of appropriate jurisdiction.[11]

[T]he combination of §§ 1529(4) and 305 permit a bankruptcy court to abstain from a proceeding arising in, arising under or related to a case under chapter 15.

In *Principal Growth Strategies LLC, et al. v. AGH Parent LLC*, the joint liquidators of Platinum Partners Value Arbitrage Fund LP (PPVA), and Principal Growth Strategies LLC (PGS), an entity formed by PPVA to hold a promissory note (together, the "plaintiffs"), claimed that parties stripped the note from PGS to the detriment of the plaintiffs.[12] The complaint included three counts under Delaware law and three under Cayman Islands law.[13] Filed in the Delaware Chancery Court, the suit was removed to the district court pursuant to 28 U.S.C. § 1452(a).[14]

The removing defendants argued that removal was appropriate because the district court had original bankruptcy jurisdiction under 28 U.S.C. § 1334(b), asserting that the chancery action arises under title 11 since the plaintiffs brought the action pursuant to powers granted under chapter 15. The plaintiffs moved to remand the case back to the chancery court, and several defendants objected on *Firefighters'* grounds. The plaintiffs asserted that the district court must abstain from hearing the case under 28 U.S.C. § 1334(c)(2) and must remand the case to the chancery court under 28 U.S.C. § 1452(b), which provides, "The court to which such

6 The NBC proposed that Congress revise 28 U.S.C. § 1334(c)(1) as follows: "(c)(1) Except with respect to a *determination of an application for recognition of a foreign proceeding in a* case under chapter 15 of title 11, nothing in this section prevents a district court in the interest of justice, or in the interest of comity with State courts or respect for State law, from abstaining from hearing a particular proceeding arising under title 11 or arising in or related to a case under title 11." *See* the NBC Letter of Nov. 13, 2019, *available at* nbconf.org/our-work (last visited Aug. 24, 2020).

7 Section 1528 applies to title 11 cases commenced after recognition under chapter 15 of a foreign main proceeding, while § 1529 applies to coordination of cases under other chapters of title 11 with foreign proceedings involving the same debtor.

8 11 U.S.C. § 305.

9 It is an "elementary canon of construction that a statute should be interpreted so as not to render one part inoperative." *Colautti v. Franklin*, 439 U.S. 379, 392, 99 S. Ct. 675, 684, 58 L. Ed. 2d 596 (1979). *See also United States v. Menasche*, 348 U.S. 528, 538-39, 75 S. Ct. 513, 520, 99 L. Ed. 615 (1955) ("It is our duty 'to give effect, if possible, to every clause and word of a statute,' *Montclair v. Ramsdell*, 107 U.S. 147, 152 [2 S. Ct. 391, 394, 27 L. Ed. 431], rather than to emasculate an entire section.").

10 488 B.R. 205, 240. The *British American* court did try to distinguish § 305 but ignored § 1529(4): "Section 305 is the sole statutory authority for abstention from a title 11 case. However, section 305 is not applicable in a case under chapter 15. 11 U.S.C. § 103(a). There is no provision in federal law allowing a federal court to abstain from an entire chapter 15 case." The NBC would also make a complementary change to § 103(a) to eliminate any possible doubt: 11 U.S.C. § 103. Applicability of chapters:

> (a) Except as provided in section 1161 of this title, chapters 1, 3, and 5 of this title apply in a case under chapter 7, 11, 12, or 13 of this title~~, and this~~. **This** chapter, **sections 305, 306,** 307, 362(o), 555, 556, ~~through~~ 557, and 559, **560, 561, and** ~~through~~ 562 of this title, **and any section of this title specifically made applicable by a section of chapter 15 apply in a case under chapter 15.**

11 *See In re Fairfield Sentry Ltd.*, 458 B.R. 665 (S.D.N.Y. 2011) (remanding removed claims to state court for determination of whether they could be timely adjudicated).

12 *Principal Growth Strategies LLC, et al. v. AGH Parent LLC, et al.*, 2020 WL 1677088 (D. Del. April 6, 2020). In November 2016, the joint liquidators had obtained recognition of PPVA's Cayman Islands liquidation proceeding in the Southern District of New York. *Id.* at *1.

13 *Principal Growth v. AGH*, Case No. 1:19-cv-01319, Doc. No. 10 (D. Del. Aug. 5, 2019).

14 *See supra* n.3.

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claim or cause of action is removed may remand such claim or cause of action on any equitable ground."

The defendants countered that remand on equitable grounds was prohibited by the *Firefighters'* decision because the chancery action was related to the PPVA chapter 15 case. The district court rejected that argument:

> I will not apply *Firefighters'* rationale or holding to this case for three reasons. First, as the Court acknowledged in *Firefighters'*, "§ 1452 does not explicitly exclude Chapter 15 cases." Second, *Firefighters'* addressed permissive abstention under § 1334(c)(1), but this case involves mandatory abstention under § 1334(c)(2) and there is no language in § 1334(c)(2) that suggests in any way that it does not apply to proceedings related to Chapter 15 cases. Third, the Third Circuit held in *Stoe* that "mandatory abstention [under § 1334(c)(2)] is not in conflict with 28 U.S.C. § 1452...." As the Court explained:
>
> > [S]ection 1334(c)(2) does not purport to interfere with a court's authority to remand under § 1452(b). Rather, § 1334(c)(2) governs only whether a district court must abstain from hearing a case. Once a district court determines that it ... must abstain from hearing a removed case pursuant to [§] 1334(c)(2) ... it can consider whether there is reason for the suit to proceed in state court. If so, there will be an equitable ground justifying remand under § 1452(b).[15]

Some Things Are Clear, Others Not So Much

Even absent the statutory fix suggested by the NBC,[16] the combination of §§ 1529(4) and 305 permit a bankruptcy court to abstain from a proceeding arising in, arising under or related to a case under chapter 15. Section 1334(c)(1) only prevents abstention from deciding the chapter 15 case (*i.e.*, the application for recognition). Nonetheless, there will likely be additional questionable decisions on permissive abstention in chapter 15 cases until the NBC's recommendation is actually adopted. Parties thwarted by a *Firefighters'* prohibition against permissive abstention might try an alternative approach in the appropriate cases, presenting a *forum non coveniens* argument or seeking modification or termination of recognition under § 1517(d).[17] As to mandatory abstention, the *Principal Growth*, *British American* and *Fairfield Sentry* courts agree that mandatory abstention under 28 U.S.C. § 1334(c)(2) applied regardless of the muddle over permissive abstention. abi

15 *Stoe v. Flaherty*, 436 F.3d 209, 214-15 (3d Cir. 2006) (internal citations omitted).

16 *See supra* n.7.

17 Concerning the *forum non coveniens* approach, *see In re Hellas Telecommunications (Luxembourg) II SCA*, 555 B.R. 323 (2016). Section 1517(d) provides: "The provisions of this subchapter do not prevent modification or termination of recognition if it is shown that the grounds for granting it were fully or partially lacking or have ceased to exist, but in considering such action the court shall give due weight to possible prejudice to parties that have relied upon the order granting recognition."

Feature

By Chip Ford and Ashley Edwards

Move Over, § 363: Why Buyers May Prefer Plan Sales in Subchapter V

Editor's Note: *To stay current on the effects of this legislation, bookmark ABI's SBRA Resources website at abi.org/sbra.*

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Although business assets can be bought and sold through the chapter 11 plan-confirmation process, § 363 of the Bankruptcy Code has, in many cases, been the preferred mechanism for buyers due to its relative speed, greater simplicity and lower transactional costs. However, Congress may have shifted the playing field for asset sales in smaller business bankruptcy cases through the enactment of the Small Business Debtor Reorganization Act (SBRA), known as subchapter V of chapter 11.

When subchapter V took effect on Feb. 19, 2020, it accelerated the process and reduced the costs of reorganization for small businesses. Congress recently expanded those eligible for relief under subchapter V by nearly tripling the debt limit (from $2.7 million to $7.5 million) as part of its response to the coronavirus pandemic.

The equation has not only changed for small business debtors. On the other side of the deal table, when a debtor qualifies for and elects treatment under subchapter V, opportunistic buyers might find that they can achieve the benefits of a sale pursuant to a confirmed plan while avoiding some of the more burdensome aspects of the traditional chapter 11 plan-confirmation process. However, because subchapter V is only a few months old, there are still outstanding questions about how business debtors, opportunistic buyers and bankruptcy practitioners can leverage its unique features.

The Old Equation: Chapter 11 Plan Sales vs. § 363 Sales

Before getting into subchapter V, it is useful to review the traditional ways that buyers have purchased assets out of a chapter 11 case: sales under a confirmed chapter 11 plan, and sales pursuant to § 363. A primary benefit of chapter 11 plan sales from a buyer's perspective is that they can allow for a private sale without an auction. Plan sales may also offer more robust statutory protections to a buyer, since assets dealt with by a confirmed plan are cleansed of "all claims and interests" under § 1141(c), whereas only an "interest in property" may be stripped under § 363(f).[1] A plan sale may also provide additional shields against liability through releases and injunctions included in the plan. Other benefits include exemption from transfer taxes under § 1146(a). At the end of the day, the sheer weight and inclusiveness of the plan-confirmation process provides a broad base of justification for this type of sale.

However, the plan-confirmation process can be painfully slow, costly, and fraught with uncertainty and complexity from a buyer's perspective. It is rare for a plan to be confirmed in less than six months; it is more common for the process to take a year or longer. Many of the issues addressed in a typical chapter 11 plan (even a liquidating plan) relate only tangentially to the sale of the debtor's assets, yet any of those issues could become the subject of a dispute that threatens to derail confirmation.

That is a major reason sales under § 363 have become the norm in chapter 11. A hearing on a § 363 sale motion only requires 21 days' notice, and the sale itself is often completed within two months. It is also less expensive for buyers in terms of transaction costs, which are limited to those directly tied to the sale.

In addition, § 363 sales tend to be simpler and more predictable for buyers because they do not involve the myriad other moving parts of a chapter 11 plan. There is no voting by creditors, and in many cases the thorny question of how the sale proceeds should be distributed among competing claimants can be shelved for another day. The primary areas of inquiry for the court are whether the debtor is receiving the highest and best price for the assets being sold, and whether the sale is proposed in good faith at an arm's length. By contrast, confirmation of chapter 11 plans requires navigating a much broader variety of competing interests and legal requirements.

There are downsides for buyers under § 363. Perhaps most problematic from a buyer's standpoint is the generally followed (if not statutorily mandated) practice of establishing competitive-bidding procedures, which expose a buyer to the risk

1 This advantage might be more theoretical than practical given the clear trend toward an expansive view of the kinds of "interests" assets that may be sold free and clear of under § 363(f), but the U.S. Bankruptcy Court for the Southern District of New York recognized as recently as August 2019 that "the 'free and clear' relief available to a debtor under section 363(f) is narrower than that afforded to a debtor under a confirmed plan because the relief is limited to 'interests' in property and only to the extent provided for under section 363(f)(1)-(5)." *In re Ditech Holding Corp.*, 606 B.R. 544, 581 (Bankr. S.D.N.Y. 2019).

of losing the deal after a substantial investment of time and money. This risk can be compensated to some extent through expense-reimbursement provisions and break-up fees for the initial or "stalking horse" bidder, but it is a substantial risk nonetheless. Judges may also view a sale of all or substantially all of the debtor's assets as an impermissible *sub rosa* plan: a proposed transaction that for all intents and purposes is (or effectively dictates the parameters of) a plan without providing creditors and other parties-in-interest with the procedural protections of the plan-confirmation process.

Buyers also have less post-closing protections under § 363. Some courts have ruled that even if the requirements of § 363(f) are satisfied in regard to the sale of assets free and clear of "interests" such as mortgages, Article 9 security interests, judgments and other types of liens, the purchased assets may remain subject to certain types of "claims" (such as successor-liability claims). Sales under § 363 are also generally subject to transfer taxes. Notwithstanding these potential drawbacks, the advantages tied to speed, cost and relative simplicity have caused § 363 to become the predominant method of selling all or substantially all of the assets of a debtor in chapter 11.

How Subchapter V Changes the Equation

Subchapter V may eliminate many of the downsides of purchasing assets through a plan. The plan-confirmation process is faster than in a traditional chapter 11 case, and the debtor has more control because of the absolute exclusivity given to debtors under § 1189(a).

A subchapter V plan must be filed within 90 days of the debtor's filing of the petition.[2] Thus, unlike a traditional chapter 11 case where debtors often obtain multiple extensions of the exclusivity period (with a concomitant delay in the actual filing of a plan), subchapter V plans could provide a confirmed sale within a comparable time frame as a § 363 sale. When selling a business, besides the parties' preference for a timely sale, a shorter time frame provides a buyer with a greater ability to ascertain the financial condition of a going-concern business at the time of the purchase.

From the perspective of a potential buyer or debtor alike, the aspect of control in a subchapter V plan might be attractive. In a § 363 sale, the debtor is generally required to hold an auction (or least solicit and entertain competing offers until the sale is approved) to ensure the highest and best price and recovery for creditors. Through a plan, a potential buyer might have more certainty that it will be the owner of the assets upon confirmation. Further, a plan sale may allow greater flexibility for creative payment terms for the assets. If the price paid is some combination of funds and alternate consideration (waiver of claims, etc.), this type of deal in the context of a plan is more easily understood by all and less likely to be disrupted by a higher bidder. Further, potential purchasers who are leery of being stalking-horse bidders — with the time and cost involved in that position — might prefer the certainty of a sale agreement incorporated into a subchapter V plan.

In addition, subchapter V does not allow for a creditors' committee, and the debtor has the exclusive right to file a plan.[3] Because a goal of subchapter V is to avoid drowning a small business in the procedural burdens and administrative costs of chapter 11, a subchapter V debtor — and, by proxy, its selected purchaser — should face less potential litigation with creditors. Subchapter V allows a judge to confirm a plan without any consenting creditors.[4] It specifically removes the absolute-priority rule in the required "fair and equitable" analysis for cramdown purposes.[5] As in a traditional chapter 11 case, a sale through a plan also does not require the consent of any junior lienholders.[6] These limitations on the ability of creditors (collectively or individually) to derail the process should greatly reduce the costs and delays often associated with chapter 11 plan sales.

Keys to Confirmation of a Liquidating Plan Under Subchapter V

A debtor seeking confirmation of a liquidation plan under subchapter V can avoid many of the usual hurdles to plan confirmation in a chapter 11 case, including having to negotiate (or litigate) with an unsecured creditors' committee and having to obtain the affirmative vote of an impaired class under § 1129(a)(10). As long as the court is satisfied that fair value is being paid for the assets and the plan otherwise satisfies the requirements of §§ 1190 and 1191 — including the "best interests of creditors" test of § 1129(a)(7) — there is no reason that a liquidation plan should not be approved by the creditors and the court (or the court over the objection of creditors in a cramdown scenario).[7] The keys to a smooth confirmation process will likely be (1) ensuring that the plan includes detailed information about the marketing efforts undertaken and/or valuation methods used to arrive at the proposed purchase price (which will be particularly important if the proposed sale is a private sale rather than an auction); and (2) gaining the support of the trustee, whose approval is not required but whose judgment is likely to be given a significant amount of deference by the court.

Furthermore, in a case where the only realistic source of a material recovery for unsecured creditors is the potential proceeds of avoidance actions, the plan could empower the trustee to pursue such claims post-confirmation in much the same manner as "liquidating trustees" are routinely empowered to do in traditional chapter 11 cases. Any recoveries might also provide an additional source of compensation for the trustee, adding to the potential appeal of this feature.

Wildcard: The Subchapter V Trustee

A unique feature of subchapter V is the appointment of a trustee to facilitate the negotiation and confirmation of a consensual plan.[8] The subchapter V trustee is appointed by the U.S. Trustee (or, with a nod to North Carolina and

2 11 U.S.C. § 1189(b).

3 *See* 11 U.S.C. § 1189(a).
4 *See* 11 U.S.C. § 1191(a) and (b).
5 *See* 11 U.S.C. § 1191(b).
6 *Id.*
7 The question may arise as to whether a debtor with no projected disposable income post-confirmation (having sold its income-generating assets) can satisfy the requirements of § 1191(c)(2) in a cramdown scenario, but if projected disposable income is $0, that should render § 1191(c)(2) moot as a practical matter.
8 11 U.S.C. § 1183(b)(7).

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Alabama, the Bankruptcy Administrator) from a panel of potential trustees.[9] While largely modeled after chapter 12 and 13 trustees, the obligations of the subchapter V trustee differ greatly in key functions.[10]

Naturally, the facilitator role of the trustee implies a strong business angle to the subchapter V role, and the governing code provisions provide for some duties akin to those of a financial consultant or chief restructuring officer (CRO).[11] For example, upon request, a subchapter V trustee may investigate the conduct and financial condition of the debtor and any other matter relevant to the case, and file a report.[12] Pursuant to §§ 1183 and 1185, a court may task the subchapter V trustee with running the debtor's business and filing all operating reports.[13] These are tasks often performed by a financial consultant or a CRO in chapter 11.

The point is that to have a successful subchapter V trustee panel, the bench should be stacked with experienced and savvy business finance experts. Such expertise could be leveraged by a debtor and/or potential purchaser to maximize consideration on both sides of the table and provide the financial evidence to the court of an optimal outcome in the sale for creditors.

Potential Policy Implications of a Liquidating Plan in Subchapter V

The policy behind the SBRA's formulation and enactment was to make it easier for small businesses to reorganize.[14] However, there is nothing in subchapter V that prohibits the sale of all or substantially all of a debtor's assets through a confirmed plan. To the extent that subchapter V enables a qualifying business to quickly and efficiently realize going-concern value for the benefit of all of its creditors through a court-approved sale — without the administrative costs and inefficiencies of a traditional chapter 11 case or the value-destroying fire-sale aspect of a chapter 7 liquidation — all creditors will benefit, including employees who stand to retain their jobs and vendors/customers who stand to retain an ongoing business relationship.

Addressing this policy issue in a different context, Chief Judge **Helen E. Burris** of the U.S. Bankruptcy Court for the District of South Carolina recently denied the U.S. Trustee's motion to strike an individual debtor's subchapter V designation on the grounds that the debtor was not "a person engaged in commercial or business activities" where the businesses owned and operated by the debtor had ceased operating and their assets had been liquidated.[15] Citing *Collier on Bankruptcy* for the proposition that "the definition of a 'small business debtor' is not restricted to a person who at the time of the filing of the petition is presently engaged in commercial or business activities *and who expects to continue in those same activities under a plan of reorganization*,"[16] Judge Burris held that the debtor's efforts to address residual business debt constituted engagement in commercial or business activities for purposes of § 101(51D).

Conclusion

Subchapter V might provide an ideal sweet spot for buyers who want the advantages of a chapter 11 plan sale combined with the speed and relative simplicity of a sale under § 363. Subchapter V likely gives buyers greater control, fewer potential headaches with dissenting creditors, and greater protection from successor-liability claims than § 363.

The authors say "likely" because the rubber is just beginning to meet the road with subchapter V. It was only implemented last February, so the earliest plans were due in late May. The expansion of eligibility tied to the pandemic began on March 27, so plans for those cases were due in late June. (This article was written in mid-June.) The case law is very much in its infancy but will expand quickly through the rest of this year. Bankruptcy professionals should keep tabs on that case law to see whether the theoretical benefits of subchapter V become practical benefits for their clients. abi

9 11 U.S.C. § 1183(a).
10 *See* 11 U.S.C. § 1183(b).
11 *Id.*
12 *See* 11 U.S.C. § 1106(a)(3), (4) and (7).
13 In the scenario pursuant to § 1185 when the subchapter V trustee is tasked with running the business, the only logical outcome (barring a change in career path by the trustee) is a sale of the business.
14 The Report from the House Committee on the Judiciary (Report No. 116-171) states that "[n]otwithstanding the 2005 Amendments, small business chapter 11 cases continue to encounter difficulty in successfully reorganizing" and that legislation was needed "to improve the reorganization process for small business chapter 11 debtors." The SBRA allows these debtors "to file [for] bankruptcy in a timely, cost-effective manner, and hopefully allows them to remain in business, which not only benefits the owners, but employees, suppliers, customers, and other who rely on that business."
15 *In re Charles Christopher Wright*, No. 20-01035-HB (Bankr. D.S.C. April 27, 2020).
16 *Id.* at *3 (emphasis added).

Sales Under Subchapter V of Chapter 11

Committees: Asset Sales

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A small business debtor who elects to proceed under subchapter V of chapter 11[1] has the same rights and powers to sell property under 11 U.S.C. § 363 as a trustee or a debtor in possession in a larger case.[2] But it remains to be seen whether subchapter V will be used by

debtors who intend to sell substantially all of their assets in a § 363 sale, or to confirm liquidating plans. A key benefit of subchapter V is that it allows a small business owner to retain its equity by eliminating the absolute priority rule, or a requirement that the owner contribute new value to retain its equity. Therefore, it seems more likely that subchapter V cases will be used by small business owners who prefer to reorganize with a three-to-five-year payment plan as an alternative to liquidation.

While it is too early to know for sure,[3] sales in subchapter V cases will more likely be used by debtors to "downsize," rather than liquidate, and therefore will involve discrete assets that the debtor finds burdensome or unnecessary. In this article, we will discuss the provisions of subchapter V that discourage all-asset sales and promote reorganization, the types of sales that are likely to occur in subchapter V cases, and issues that may arise from these sales.

Subchapter V Was Not Designed for All-Asset Sales

In creating subchapter V of chapter 11, the drafters of the Small Business Reorganization Act of 2019[4] followed many of the recommendations of the Commission to Study the Reform of Chapter 11.[5] Among the themes and concerns raised by the Commission were "a perceived increase in the number and speed of asset sales under section 363 of the Bankruptcy Code," a "perceived decrease in stand-alone reorganizations," and a general consensus that chapter 11 generally no longer works for small or medium-sized enterprises.[6] Of particular concern was the increase in all-asset sales, especially when expedited where it is difficult to know if the sales maximize value.[7] In addition, the commission noted that "the market for small companies is virtually nonexistent" because most small companies have no value without their owner-managers.[8] And even if a market existed, often the owner-managers of small businesses are intent on maintaining ownership of a business they may have built from the ground up.[9]

Subchapter V Promotes Reorganization over Going-Concern Sales

In order to address the commission's concerns, subchapter V includes provisions that facilitate reorganizations with existing ownership and management. First, subchapter V eliminates the absolute priority rule of 11 U.S.C. § 1129(b)(2).[10] As a result, pre-petition owners can retain their equity even if creditors are not paid in full, thus obviating the need to infuse new capital

to potentially satisfy the rule. Consequently, the owners have an incentive not to sell because of the potential profits after the subchapter V plan is completed.

Equally important, a subchapter V plan must include projections of future income and provide that all of the debtor's projected disposable income will be applied to payments under the plan for a three-to-five-year period.[11] In fact, 11 U.S.C. §§ 1190 and 1191 do not include options to pay creditors a lump sum from proceeds of an all-asset sale. Obviously, a three-to-five-year payment plan would require that the debtor retain sufficient assets to operate the business and generate disposable income. If a debtor in a case under subchapter V were to sell substantially all assets, the debtor almost certainly would not be able to satisfy the requirements for plan confirmation under 11 U.S.C. § 1191. In short, subchapter V is intended to be rehabilitative, not a means of orderly liquidation.

Sales Will Be of Discrete Assets

Because subchapter V is designed to promote rehabilitation rather than liquidation, a debtor intent on selling its business as a going-concern is unlikely to elect it. Still, sales of discrete assets may be important to reduce ongoing expenses for secured debt, eliminate burdensome assets, and generate cash to fund operations. For example, a debtor may be able to sell real estate and downsize its facilities to reduce future overhead costs. Or, a debtor may be able to sell excess equipment or inventory that is subject to a blanket lien, cram down the lender's secured claim to the fair market value of the remaining equipment and inventory, and thereby have lower monthly payments for the secured lender's claim. In many ways, such sales will conjure the early days of the Code when all-asset sales were circumspect and case law required stricter proof of exigency.[12]

Notably, sales of discrete assets often are less expensive and less complicated than a sale of a business as a going-concern, which usually requires the employment of investment bankers to analyze the value of the business and contact the limited universe of potential buyers with the appropriate industry experience. Real property and equipment, on the other hand, often can be sold with just an appraisal and a broker or an auctioneer. In other words, sales of assets in subchapter V cases will likely resemble sales in cases under chapter 7 or 12 (but without the option of discharging capital gains taxes under 11 U.S.C. § 1232).

If a subchapter V debtor does sell substantially all assets, it would likely be only after giving up on reorganization. Most small businesses, though, would not be able to afford dual-track

on reorganization. Most small businesses, though, would not be able to afford dual-track efforts to reorganize and sell substantially all assets. By the time a subchapter V debtor gives up on reorganization, it would likely be too late to engage investment bankers or to meaningfully market the business as a going-concern. There is also the risk that a subchapter V debtor would exhaust its cash collateral or DIP financing by the time that the debtor comes to the conclusion that reorganization is not possible, which would impair the debtor's ability to continue operating until a sale closes. Therefore, with the possible exception of sales of underperforming divisions that have stand-alone viability, such sales are likely to be liquidation sales of distinct real and personal property, rather than going-concern sales of an enterprise.

Conclusion

Although a subchapter V debtor has the same rights and powers to sell property as other chapter 11 debtors, subchapter V was designed for reorganization and was not designed to facilitate sales of substantially all assets. Therefore, sales under subchapter V of chapter 11 are likely to consist of discrete assets and will probably resemble sales that occur in cases under chapters 7 and 12, or in the early days of the Code.

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[1] 11 U.S.C. §§ 1181-95.

[2] 11 U.S.C. § 1184.

[3] As of the time of this writing, the authors are unaware of any subchapter V debtors who have sold substantially all assets.

[4] Pub. L. No. 116-54.

[5] http://commission.abi.org/full-report.

[6] *Id.* at 15-16.

[7] *Id.* at 84 ("[S]ales of all or substantially all of a debtor's assets on an expedited basis, particularly early in the chapter 11 case, can raise concerns about (a) the proper valuation and marketing of assets, (b) whether other restructuring alternatives were fully explored, and (c)

marketing of assets; (b) whether other restructuring alternatives were fully explored; and (c) whether the court, the U.S. Trustee, and stakeholders have sufficient information and time to review and comment on the proposed transaction.").

[8] *Id.* at 285, n.1034.

[9] *Id.* at 285, n.1034 ("[B]ecause of the absolute priority rule, the owner-managers common in small businesses may be reluctant to file a petition before the company is in dire condition because in bankruptcy, they risk losing their financial interests in the business.").

[10] 11 U.S.C. § 1181.

[11] 11 U.S.C. §§ 1190(a)(1)(C) and 1191(c).

[12] *See, e.g., In re Lionel Corp.*, 722 F.2d 1063 (2d Cir. 1983).

Bankruptcy by the Numbers

By Ed Flynn

Subchapter V's First 1,000 Cases

When the Small Business Reorganization Act of 2019 (SBRA) was enacted just over a year ago, no one had a clue of what 2020 had in store. At that time, the national unemployment rate was 3.7 percent, more than 20 Democrat candidates were running for President, and most economic indicators (except for the budget deficit) were positive.

The SBRA took effect on Feb. 19, 2020, just a few weeks before the national shutdown due to the COVID-19 pandemic. With the creation of subchapter V, the SBRA provided a streamlined path through chapter 11 for small business debtors.

This article presents a little statistical detail on what we know about the first 1,000 subchapter V cases that have been filed. It is not intended to cover the provisions of SBRA and subchapter V in detail. ABI has compiled a number of other resources regarding SBRA on its resource page,[1] and a very comprehensive e-publication authored by Hon. **Paul W. Bonapfel** (U.S. Bankruptcy Court (N.D. Ga.); Atlanta) is available for free from the ABI Store.[2] The following are the key dates regarding the SBRA and subchapter V:

Dec. 8, 2014: The ABI Commission to Study the Reform of Chapter 11 released its report. Chapter VII of the report included proposals regarding small and medium-sized enterprises.[3]

April 9, 2019: The SBRA was introduced in the Senate by Sen. Chuck Grassley (R-Iowa) and five other senators.

June 18, 2019: The SBRA was introduced in the House by Rep. Ben Cline (R-Va.).

June 25, 2019: The House Judiciary Subcommittee on Antitrust, Commercial and Administrative Law held a hearing on the SBRA and other bankruptcy-related proposals. Past ABI President **Robert J. Keach** (Bernstein Shur; Portland, Maine) testified in support of the bill. Mr. Keach served as co-chair of the ABI Commission to Study the Reform of Chapter 11.

July 23, 2019: The SBRA was approved by the House of Representatives.

Aug. 1, 2019: The SBRA was approved by the Senate.

Aug. 23, 2019: President Donald J. Trump signed the SBRA into law.

Feb. 19, 2020: The SBRA took effect; 16 subchapter V cases were filed in 13 judicial districts on the first day.

March 27, 2020: The Coronavirus Aid, Relief, and Economic Security (CARES) Act (P.L. 116-136) raised the debt ceiling for subchapter V eligibility from $2,725,625 to $7,500,000. (Absent further congressional action the threshold will return to $2,725,625 after one year.)

Oct. 9, 2020: The 1,000th subchapter V case was filed.

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Preparation for SBRA Effective Date

In a time when it often seems that government is dysfunctional, the SBRA has proven to be an exception, with each of the three branches of government having performed quite admirably. The bill was passed with widespread bipartisan support. By its effective date, the U.S. Trustee Program had appointed about 250 subchapter V trustees,[4] and had prepared a handbook for them to follow.[5] The Judicial Branch, through the Judicial Conference, had issued the interim rules and forms needed as a result of the SBRA.[6] When the pandemic hit shortly after the effective date, Congress included a very helpful increase to the small business debt ceiling in the CARES Act.[7]

Identification of Subchapter V Cases

No official (*e.g.*, government) figures on subchapter V cases have been released to date. In the absence of any official statistics, ABI has conducted a case-by-case review of PACER[8] records of all chapter 11 cases filed since Feb. 19, 2020, to identify subchapter V filings.[9]

The "Case Summary" report in PACER indicates whether a case is considered a small business

1 To stay current on the effects of this legislation, bookmark ABI's SBRA Resources website at abi.org/sbra.

2 *See* Bonapfel, *SBRA: A Guide to Subchapter V of the U.S. Bankruptcy Code*, *available at* store.abi.org/sbra-a-guide-to-subchapter-v-of-the-u-s-bankruptcy-code.html (unless otherwise specified, all links in this article were last visited on Oct. 12, 2020).

3 *See* "Proposed Recommendations: Small and Medium-Sized Enterprised (SME) Cases," *available at* abiworld.app.box.com/s/uzc6yo7dr8lt1g2m4uxs (excerpt of ABI Commission to Study the Reform of Chapter 11's Final Report published in 2014).

4 *See* "U.S. Trustee Program Ready to Implement the Small Business Reorganization Act of 2019," Dep't of Justice (Feb. 19, 2020), *available at* justice.gov/opa/pr/us-trustee-program-ready-implement-small-business-reorganization-act-2019. In addition, at least 20 other trustees are serving in the six judicial districts in North Carolina and Alabama, which are supervised by Bankruptcy Administrators.

5 *See* "Handbook for Small Business Chapter 11 Subchapter V Trustees," Executive Office for U.S. Trustees (February 2020), *available at* justice.gov/ust/file/subchapterv_trustee_handbook.pdf/download.

6 *See* "Interim Amendments to the Federal Rules of Bankruptcy Procedure," *available at* uscourts.gov/sites/default/files/2019_sbra_interim_rules_amendments_redline_0.pdf.

7 *See* CARES Act, *available at* congress.gov/116/bills/hr748/BILLS-116hr748enr.pdf.

8 PACER is the acronym for Public Access to Court Electronic Records (*see* pacer.uscourts.gov).

9 The "Case Summary" page for each case was reviewed to see whether there was any indication that it was subchapter V. All bankruptcy courts employ some sort of flag to identify these cases, although there is no uniformity on what the flag is (*e.g.*, Subchapter V, SmBusSubV, SubChV, SmBusV, SubV, etc.). In addition, there were a few cases that did not have any flag listed, but a review of the case docket showed that the case was subchapter V.

case and whether the debtor elected to proceed under subchapter V.[10] This review provides very limited information on the cases (*e.g.*, name of case, district, docket number, date filed and trustee name). ABI's website has posted this information on its SBRA Resources page.[11] Additional information on the cases will be available later this year when the Federal Judicial Center releases its FY 2020 update to the Integrated Data Base.[12]

However, official government statistics will be needed to truly assess the performance of subchapter V and to determine whether changes are in order. For example, in addition to an official count of the number of subchapter V cases filed, it would be helpful to know answers to the following questions:

- How many cases propose a consensual plan vs. how many propose a cramdown;
- How many plans are confirmed;
- What are the time intervals from filing to confirmation;
- What are the types of small businesses that are using subchapter V; and
- What are the amount of fees paid to subchapter V trustees?

Hopefully, the Administrative Office of the U.S. Courts will put in place statistical reporting systems to address these and other questions.

Filings by Month

Subchapter V case filings started out strong in February 2020. They dropped off during late March and April, likely due to the shutdowns as a result of the pandemic. However, filings have increased each month since April, and during each of the last four full months filings have set new records. Exhibit 1 provides a breakdown of these numbers.

10 This review probably missed a few cases. For example, PACER shows cases in their current chapter. The initial review conducted in June 2020 would have missed a few cases that had been converted out of chapter 11 prior to the PACER review. Cases that opted into subchapter V more than a few days after filing would not be identified. The review would also have missed cases filed prior to Feb. 19, 2020, that later opted into Subchapter V.

11 *See supra* n.1.

12 *See* Integrated Database, *available at* fjc.gov/research/idb. This database contains a record for each bankruptcy case filed, and it is updated with data as of Sept. 30 each year the case is still open. Although the Fiscal Year 2020 update will not have a subchapter V identifier, it will be possible to match docket numbers from the ABI list to the individual case records. This will give further information on assets, liabilities, county of residence, prior filings, *pro se* cases and related filings in the subchapter V cases. The additional data could be helpful to inform the discussion on whether the increased debt ceiling from the CARES Act should be extended. It will be too soon after the SBRA's effective date to obtain any meaningful information on case outcomes.

Exhibit 1: Subchapter V Cases Filed (Feb. 19 to Oct. 9, 2020)

Month	Total Filed
February (19-29)	82
March	122
April	68
May	114
June	133
July	138
August	140
September	160
October (1-9)	43
Total Cases	**1,000**

Cases by State and District

Three states have accounted for more than one-third of the subchapter V cases filed to date: Florida (127), Texas (126) and California (99). At least one subchapter V case has been filed in every state except Rhode Island (where no chapter 11 cases have been filed since Feb. 19, 2020).

In fact, 88 of the 93 judicial districts have now had a subchapter V filing. None of the five judicial districts without a subchapter V case (Eastern District of Oklahoma and the Districts of Rhode Island, Guam, Virgin Islands and Northern Mariana Islands) have had a business chapter 11 case filed since Feb. 19, 2020. Exhibit 2 on p. 42 shows a breakdown by state.

Just under 20 percent of the chapter 11 cases filed since Feb. 19, 2020, have been subchapter V cases. However, this figure is misleading because since the pandemic, chapter 11 filing figures have been skewed by the large number of related filings by subsidiaries in a corporate group. Most of the related filings occur in the largest chapter 11 cases, and most of these cases are filed in the Southern District of New York, the District of Delaware and the Southern District of Texas. If we exclude these three districts from the calculation of subchapter V frequency, about 36 percent of chapter 11 cases have been subchapter V. In 22 states and the District of Columbia, at least one-half of the chapter 11 cases filed have been subchapter V.

Professionals Serving in Subchapter V Cases

Three categories of professionals are involved in nearly every subchapter V case: the bankruptcy judge, the subchapter V trustee and the attorney for the debtor.[13] By this time, most of the more than 300 U.S. bankruptcy judges have been assigned at least a few subchapter V cases. The PACER records show that well over 500 individuals have served as lead attorney in one or more cases. The cases filed to date have been pretty well spread out among the subchapter V trustees. The PACER records indicate that more than 250 trustees have been assigned at least one case, but that only about a dozen trustees have been assigned 10 or more cases. So, in under eight months, about 1,000 bankruptcy professionals have served in a key role in a subchapter V case.

Types of Business

About 26 percent of the subchapter V cases were filed by individuals, who reported that a majority of their debt was business debt. Of these cases, 31 percent were joint filings, 18 percent were filed by female debtors and 51 percent were filed by male debtors.

The remaining subchapter V cases represent a wide range of business types. Based on the case name, case documents and online searches, it was possible to determine the type of business for most, but not all,[14] of the subchapter V cases.

13 Of course, there is a bankruptcy judge and a trustee assigned in every case. However, the PACER records did not indicate an attorney for the debtor in about 2 percent of the cases.

14 For about 6 percent of the cases, the type of business could not be determined. Some subchapter V debtors have rather generic names, no online presence and no informative press coverage of their filing.

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Bankruptcy by the Numbers: Subchapter V's First 1,000 Cases

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Clearly, many of these businesses were in industries that were most disrupted by the pandemic. The leading categories of businesses include medical, including health care professionals and facilities (75); restaurants and bars (75); business services (53); retail (51); construction and development (48); trucking and transport (39); real estate, including realtors, property managers and investors (36); home services (36); leisure and entertainment (30); manufacturing (23); energy production and services (21); health and fitness (19); hotels and motels (18); taxi and limousine services (15); farms and ranches (14); auto/truck sales and services (14); financial services, including insurance (12); and nonprofit businesses, including churches (10).

Comparison with Prior Years

Subchapter V is not mandatory for small business debtors. Since Feb. 19, 2020, there have been 1,260 small business cases filed, including 260 cases in which the debtor did not choose to use subchapter V. Exhibit 3 shows the number of small business cases filed this year and during the same period for the previous five years.

Exhibit 3: Small Business Cases Filed (Feb. 19 to Oct. 9, 2015-2020)

Year	Total Filed
2015	1,103
2016	1,032
2017	967
2018	880
2019	920
2020	1,260

Exhibit 2: Chapter 11 Cases Filed (Feb. 19 to Oct. 9, 2020)

	Chapter 11 Cases Filed	Subchapter V Cases	Percent Subchapter V		Chapter 11 Cases Filed	Subchapter V Cases	Percent Subchapter V
National	5,051	1,000	19.8%	National	5,051	1,000	19.8%
Alabama	48	13	27.1%	Nebraska	6	5	83.3%
Alaska	3	2	66.7%	Nevada	67	13	19.4%
Arizona	62	34	54.8%	New Hampshire	4	2	50.0%
Arkansas	19	8	42.1%	New Jersey	103	24	23.3%
California	335	99	29.6%	New Mexico	12	8	66.7%
Colorado	52	25	48.1%	New York	706	51	7.2%
Connecticut	5	3	60.0%	North Carolina	68	32	47.1%
Delaware	1,114	8	0.7%	North Dakota	2	2	100.0%
Florida	327	127	38.8%	Ohio	51	12	23.5%
Georgia	86	35	40.7%	Oklahoma	11	5	45.5%
Hawaii	3	1	33.3%	Oregon	13	6	46.2%
Idaho	15	11	73.3%	Pennsylvania	73	21	28.8%
Illinois	77	42	54.5%	Rhode Island	0	0	N/A
Indiana	20	10	50.0%	South Carolina	13	5	38.5%
Iowa	6	5	83.3%	South Dakota	3	1	33.3%
Kansas	13	6	46.2%	Tennessee	68	37	54.4%
Kentucky	32	18	56.3%	Texas	1,046	126	12.0%
Louisiana	34	23	67.6%	Utah	11	8	72.7%
Maine	13	12	92.3%	Vermont	3	3	100.0%
Maryland	42	16	38.1%	Virginia	157	13	8.3%
Massachusetts	31	11	35.5%	Washington	34	17	50.0%
Michigan	57	15	26.3%	West Virginia	17	9	52.9%
Minnesota	15	9	60.0%	Wisconsin	17	12	70.6%
Mississippi	42	20	47.6%	Wyoming	11	3	27.3%
Missouri	67	15	22.4%	Puerto Rico	21	9	42.9%
Montana	4	2	50.0%	Washington, D.C.	12	6	50.0%

Total small business filings have been higher since the SBRA took effect on Feb. 19, 2020, compared to previous years. However, this might be a result of the higher debt ceiling for small business eligibility, which went into effect on March 27, 2020, so the jury is still out on whether the SBRA has led to additional filings by small businesses.

Conclusion

It took less than eight months for the first 1,000 subchapter V cases to be filed. Subchapter V seems to have gained wide acceptance as nearly 80 percent of small business debtors have elected to use it, and nearly every bankruptcy court has already received cases. More than 1,000 bankruptcy professionals have already had a role in these cases, serving either as debtors' attorney, subchapter V trustee or the bankruptcy judge assigned to the case. A broad range of businesses have used subchapter V, including many in industries that have been particularly harmed by the COVID-19 pandemic. It is too early to determine whether subchapter V has met its goal of providing small business debtors a more streamlined path for restructuring their debt, but all in all, it seems to be off to a pretty good start. abi

On Our Watch

By Clifford J. White III[1]

Small Business Reorganization Act: Implementation and Trends

Editor's Note: *To stay current on the effects of this legislation, bookmark ABI's SBRA Resources website at abi.org/sbra.*

The Small Business Reorganization Act of 2019 (SBRA) ushered in substantial changes to bankruptcy law and practice when it became effective on Feb. 19, 2020. ABI Consultant **Ed Flynn** recently provided an excellent analysis of the first 1,000 cases filed under subchapter V.[2] Although he identified several questions to be answered as additional data becomes available, he concluded that subchapter V was "off to a pretty good start." We agree with Mr. Flynn that by all current measures, the SBRA is working as Congress intended, and we share in this article details about the U.S. Trustee Program's (USTP) implementation of SBRA and preliminary answers to some of the questions he posed.

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SBRA's Background and Implementation

Congress passed the SBRA with the goals of providing distressed small business owners the opportunity to reorganize their businesses more quickly and at a lower cost and allowing creditors to get paid sooner. Under the SBRA, small business debtors — defined as debtors with less than $2,725,625 in noncontingent liquidated debts[3] that also meet other criteria — may elect to have their cases administered under the new subchapter V of chapter 11 of the Bankruptcy Code, which proceeds under a tight timeline. To illustrate, within 24-48 hours after a small business debtor files and elects to proceed under subchapter V, the U.S. Trustee appoints a subchapter V trustee and schedules the § 341 meeting of creditors for a date as early as possible in accordance with applicable rules. The U.S. Trustee also conducts the initial debtor interview within 10 days of the filing. In addition, the court holds a status conference within 60 days of filing, and the debtor must file a plan within 90 days.[4]

A key component of the SBRA is the assistance of a subchapter V trustee to assess the viability of the business and facilitate the development of a consensual plan to reorganize the business. The U.S. Trustee appoints and supervises subchapter V trustees and oversees the administration of subchapter V cases. In implementing the SBRA, the USTP recruited, vetted and trained approximately 250 selectees from more than 3,000 applicants. The subchapter V trustees were selected for various pools from which they are appointed on a case-by-case basis. The selected trustees have a strong business acumen and include lawyers, CPAs, MBAs, restructuring consultants and financial advisors with diverse backgrounds in such areas as business, law, accounting, turnaround management and mediation.

The USTP developed a comprehensive handbook to guide subchapter V trustees in carrying out their SBRA responsibilities.[5] Immediately following appointment in a case, subchapter V trustees begin their primary pre-confirmation task of facilitating the development of a consensual reorganization plan by participating in both the USTP's initial debtor interview and the § 341 meeting of creditors. As anticipated, subchapter V trustees generally have not needed to hire professionals, which has helped to reduce the cost to debtors and increase recoveries to creditors.

Unlike compensation for chapter 7 panel trustees or standing chapter 12 and 13 trustees, subchapter V case trustee compensation is not based on case disbursements[6] or plan payments. Instead, subchapter V trustees must apply for fees and expenses pursuant to § 330 of the Bankruptcy Code. Accordingly, all fees must be reasonable and necessary under the circumstances of the case, and all expenses must be actual and necessary. Subchapter V trustees understand that they need to manage their time and control costs in the cases to which they are appointed. In fact, when appointed, they must file an affidavit with the court disclosing their proposed arrangement for compensation, so all parties are fully informed.

After completing their service in a case, subchapter V trustees file a final report stating whether

1 **Nancy J. Gargula**, U.S. Trustee for Regions 10 and 21, contributed to this article.

2 *See* Ed Flynn, "Subchapter V's First 1,000 Cases," XXXIX *ABI Journal* 11, 30-31, 42-43, November 2020, *available at* abi.org/abi-journal (unless otherwise specified, all links in this article were last visited on Dec. 1, 2020).

3 The Coronavirus Aid, Relief and Economic Security Act of 2020 (CARES Act) temporarily raised the debt ceiling to $7.5 million for cases filed between March 27, 2020, and March 26, 2021.

4 The court may extend this deadline when the "need for the extension is attributable to circumstances for which the debtor should not justly be held accountable." 11 U.S.C. § 1189.

5 *Handbook for Small Business Chapter 11 Subchapter V Trustees*, U.S. Dep't of Justice, *available at* justice.gov/ust/private-trustee-handbooks-reference-materials/chapter-11-subchapter-v-handbooks-reference-materials.

6 SBRA-conforming amendments specifically make 11 U.S.C. § 326(a) inapplicable to subchapter V cases, which precludes determining compensation based on disbursements.

they have administered assets (generally, the debtor remains in possession and the trustee will not administer assets, unless the court orders otherwise) or have served as the plan-disbursing agent. Typically, where a consensual plan is developed and confirmed, the trustee does not serve as the disbursing agent and will file the final report after substantial consummation of the confirmed plan. When a nonconsensual plan is confirmed, the trustee will usually act as the plan-disbursing agent and the final report will include an accounting for funds that the trustee handled and disbursed throughout the case. Subchapter V trustees also submit monthly reports to the USTP that provide detailed financial information on their assigned cases.

Preparing for any new law is a significant undertaking, especially one that brought as many changes as the SBRA. The USTP is fortunate to have been able to work cooperatively and collaboratively with key stakeholders and its partners in the bankruptcy community to meet this important mandate.

SBRA Trends

Once implementation was complete and the law became effective, two major questions remained: How many filers would use the new law, and would the SBRA work as Congress intended? We can say — without a doubt — that subchapter V has proven to be popular and is showing signs of success.

Overall Filing Trends

From Feb. 19 through Sept. 30, 2020, approximately 1,100 small business debtors in USTP districts elected to proceed under subchapter V. This total includes more than 100 cases — many originally filed prior to the SBRA's effective date — that amended into subchapter V. Over three-quarters of all small business chapter 11 debtors since the SBRA's enactment are proceeding under subchapter V, and this percentage has been fairly stable. Use of subchapter V has been widespread geographically, with subchapter V filings in every USTP region and all but one USTP field office. More than two-thirds of subchapter V filings have been by business entities, with the remainder filed by individuals who operate a business.

Indicia of SBRA's Success: Higher Plan Confirmation Rates, Speedier Plan Confirmation, More Consensual Plans and Improved Cost-Effectiveness

By analyzing the subchapter V trustees' monthly reports and information from other sources on a subset of the 625 cases that were filed under or amended into subchapter V through June 30, 2020, the USTP can begin to answer some of the questions posed in the recent *ABI Journal* article.[7] The indicia noted herein are based on the status of these cases as of September 2020, and the early results are promising.

One indicator that the SBRA is working as Congress intended is the percentage of cases with confirmed plans. More than 100 cases in the group, or nearly 20 percent, had confirmed plans. This is six times higher than the percentage of confirmed plans for small business cases that did not proceed under subchapter V during the same time frame. About 7 percent of the total cases amended out of subchapter V, often following a determination by the USTP that the debtor was ineligible to proceed under subchapter V. Of those that had not amended out of subchapter V, about 15 percent were converted or dismissed. Anecdotal reports suggest that some of these cases were successful because the subchapter V trustee facilitated a consensual resolution with parties who decided that they could resolve matters outside of bankruptcy court.

> **Preparing for any new law is a significant undertaking, especially one that brought as many changes as the SBRA.**

A closely related indicator of success is how long it takes from case filing to confirmation. Early indications are that subchapter V cases are confirming more quickly than other small business cases not proceeding under subchapter V. Although it is too early to determine an average time to confirmation, so far there are more subchapter V cases confirming in a short amount of time compared to similar small business cases that did not proceed under subchapter V. Already, around 40 of the subchapter V cases in the group (or 20, if factoring out a large group of related cases) had plans confirmed within 120 days. By comparison, none of the non-SBRA small business cases had a plan confirmed within 120 days during the same period, and only about 10 small business cases per year on average had plans confirmed within 120 days over the past three years.

Success also can be measured by how many reorganization plans are consensually confirmed. Thus far, the majority of the plans that were confirmed — more than 60 percent (or 80 percent, if factoring out a large group of related cases that had a nonconsensual plan confirmed) — were consensual. This is an encouraging statistic, because it suggests that the subchapter V trustees are successfully resolving confirmation disputes.

Finally, although there is not yet sufficient data to determine conclusively whether the law has affected fees, both anecdotally and from our own observations, the subchapter V trustees are resolving disputes prior to litigation, which should further reduce or eliminate unnecessary costs.

Conclusion

The SBRA was enacted to assist small business owners with a more efficient and economical path to reorganization. By all current measures, it appears that the SBRA is working as Congress intended. The USTP remains dedicated to supporting the SBRA and will continue to monitor its progress, analyze case data and make adjustments as appropriate to ensure that the mandates of the new law can continue to be carried out successfully. abi

7 Flynn, *supra* n.2.

DECEMBER 10, 2020

Subchapter V Trustees Are Entitled to 'Reasonable' Compensation Without a "Cap"

> Section 326(b) could have been (incorrectly) read to mean that non-standing subchapter V trustees are not entitled to compensation.

A trustee under subchapter V of chapter 11 who is not a standing trustee is entitled to "reasonable" compensation under Section 330(a)(1), not subject to the cap in Section 326(b), according to Chief Bankruptcy Judge Joseph M. Meier of Boise, Idaho.

The subchapter V case had been dismissed before confirmation. Having served six months, the trustee filed an application for about $2,000. The subchapter V trustee was not a standing trustee under 28 U.S.C. § 586(b) but had been appointed as a disinterested person under Section 1183(a).

Unlike chapter 13, where the statute is unclear about a trustee's compensation on dismissal before confirmation, Section 1194(a)(1)

specifically allows compensating the subchapter V trustee when dismissal occurs before confirmation.

Although Judge Meier said in his December 7 opinion that the requested compensation was reasonable, he addressed questions not raised by the parties: (1) What is the statutory authority fixing or capping the amount of a non-standing subchapter V trustee's fees; and (2) is the non-standing trustee entitled to any compensation at all as a result of faulty drafting in Section 326?

Judge Meier first looked at Section 326(a). It sets out sliding-scale compensation for trustees in chapters 7 and 11 but excludes trustees under subchapter V. Judge Meier therefore said that the subsection "specifically excludes" subchapter V trustees from receiving percentage compensation under Section 326(a).

Judge Meier's reading of Section 326(a) makes sense. In subchapter V, the services of a trustee are intended to be limited. Subchapter V is also designed to be comparatively inexpensive for debtors. If sliding-scale compensation were allowed, a subchapter V trustee might receive very large compensation for very little work.

Judge Meier then turned to Section 326(b), which provides that the court in a subchapter V case "may not allow compensation" for a U.S. Trustee or a standing trustee "but may allow reasonable compensation under Section 330 . . . of a trustee appointed under section 1202(a) or 1302(a) of" the Bankruptcy Code.

Judge Meier saw three possible interpretations of Section 326(b). First, he said it could be read to mean "that no compensation should be allowed under subsection 330 to subchapter V trustees," but only to trustees in chapters 12 and 13.

Judge Meier rejected the idea that Section 326(b) permits no compensation to a non-standing subchapter V trustee. He said that the subsection "does not present a bar to the Trustee to obtain compensation under Section 330(a)(1)."

The second possible reading of Section 326(b), Judge Meier said, is that "Congress only intended to place a percentage limitation on compensation to trustees who are not standing trustees in chapter 12 and chapter 13 and not to impose that cap on trustees in subchapter V."

The third interpretation of Section 326(b) would understand Congress as capping the fees of non-standing trustees in chapters 12 and 13 and subchapter V. Judge Meier saw it as "likely that the intent of Congress was to make trustee compensation in subchapter V mirror that in chapters 12 and 13."

"However," Judge Meier said, adopting the third interpretation would require rewriting the statute, a step he declined to take.

Judge Meier therefore decided to enforce the statute "as written" by holding that Section 326(b) does "not prevent an award of compensation to the Trustee under § 330(a)(1), nor does it place a cap [on] such compensation." He awarded the requested compensation as an administrative expense under Section 503(b)(2).

Observation

Section 330(a)(1) generally allows "reasonable compensation" to trustees, "subject to" Section 326. Standing alone, Section 330(a)(1) makes no distinction between standing and non-standing trustees. With regard to standing trustees, there are limitations on compensation elsewhere in the Bankruptcy Code and title 28.

As Judge Meier said, nothing in Section 326 or 28 U.S.C. § 586 applies to a non-standing trustee. Therefore, a non-standing trustee is entitled to compensation under the general provisions of Section 330(a)(1).

Opinion Link

PREVIEW

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https://abi-opinions.s3.amazonaws.com/Tri-State+Roofing.pdf

Case Details

Case Citation	In re Tri-State Roofing, 20-40188 (Bankr. D. Idaho Dec. 7, 2020)
Case Name	In re Tri-State Roofing
Case Type	Business
Court	9th Circuit Idaho
Bankruptcy Tags	Professional Compensation/Fees Business Reorganization Small Business

[+] FEEDBACK

Value & Cents

By Daniel R. Van Vleet

Bankruptcy and Business Valuation in the Current Environment

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Even in the best of times, the valuation of a company involved in a bankruptcy can present its own set of challenges. In the current environment, those challenges have been magnified. COVID-19 has fundamentally altered the social, financial and economic fabric of our society. Stay-at-home orders, social distancing, high unemployment, remote business operations, civil disorder, urban flight and the classification of essential vs. non-essential businesses has impacted different sectors of the economy in material and disparate ways. As one might expect, these changes have also affected the way that business valuations are conducted.

The income and market approaches are business-valuation approaches that are often used in bankruptcy matters to determine solvency/insolvency and plan feasibility. Given the current environment, the mechanical application of these approaches might produce indications of value that lack credibility and reliability. This article will address valuation issues associated with the current environment and provide suggested modifications to the traditional application of business-valuation approaches.

Income Approach

The income approach is based on projections of financial performance and the cost of capital of a subject company. From these projections, estimates of expected cash flows are developed and converted into an indication of value using a discount rate based on an appropriate cost of capital. One of the primary components of the income approach is the projected financial performance of the subject company.

Projected Financial Performance

When preparing the projections for the subject company, an assessment should be made to determine whether the current environment conditions will impact the subject company on a temporary or more permanent basis. If temporary, the following issues should be addressed in the analysis:

- the length of time of the temporary period and the cash-flow requirements for the subject company to return to normalized financial and operational performance;
- new cost structure of the business during the temporary period related to regulatory issues, financial performance and operational changes;
- temporary cash-flow impact of existing obligations, government loans, stimulus payments, the Payroll Protection Plan, debtor-in-possession financing, cash infusions and other forms of support; and
- the impact of depreciation, capital expenditures and incremental working capital on the projected cash-flow performance during the temporary period.

If the impact on the subject company is more permanent in nature, the projections should still reflect these aforementioned issues. However, the analysis should also reflect the reality that there will be no return to normalized business operations. When this is the case, the "new normal" conditions are projected to continue for the foreseeable future.

In addition to these issues, the current environment has created significant new challenges that must be addressed when estimating the discount rate used in the income approach. The discount rate can have a material impact on a company's valuation.

The Discount Rate

The discount rate is calculated based on the estimated costs of debt and equity capital for the subject company. The cost of equity capital is typically calculated by adding the market yield of U.S. Treasury securities to an equity risk premium derived from publicly traded companies. This calculation can become problematic when a "flight to quality" increases the demand for Treasuries during uncertain times. This increased demand can increase the price of Treasuries, which lowers their respective market yields. If an expert mechanically incorporates these lower Treasury market yields into a cost-of-equity-capital analysis in the current environment, the result can be a lower discount rate. This lower discount rate can imply that a company is less risky (and more valuable) than it was prior to the current environment.

When conducting valuations, experts should consider whether the current Treasury yield is the proper rate to use in the calculation of the cost of equity capital. It might be more appropriate to use a "normalized" or expected long-term Treasury yield if the valuation date occurs after mid-February 2020.

Yields on corporate debt are also changing due to the flight to quality. Accordingly, debt balances

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and interest rates reported on the financial statements of public companies may require further analysis. In addition, care should be exercised when estimating the components of debt and equity capital used in the calculation of the discount rate. Failure to do so could result in both an unreliable discount rate and indication of value.

In addition to the income approach, the market approach is a widely used business-valuation approach. The market approach is also susceptible to distortions attributable to the current environment.

Market Approach

The market approach is based on transactions involving the equity securities or business enterprises of publicly traded or privately held companies. When conducting the market approach, the expert will use market transactions to develop earnings multiples, which are then used to value the subject company.

Typically, the valuation methods used in the market approach are twofold: (1) merger-and-acquisition (M&A) method and (2) guideline-public-company (GPC) method. The current environment has had a substantial impact on the application of both of these methods for valuation dates occurring after mid-February 2020. Accordingly, modifications to the traditional application of these methods might be appropriate in order to conclude reliable indications of value.

M&A Method

M&A multiples are calculated by dividing the purchase price of the target company by its earnings. Prices paid in M&A transactions negotiated prior to mid-February 2020 likely do not reflect the impact of the current environment. In addition, the economic uncertainty, risk-aversion and tightening of corporate debt markets have reduced the flow of M&A transaction activity that would ordinarily serve as relevant data points for contemporaneous valuations.

If an expert is able to identify relevant M&A transactions, caution should be exercised when applying M&A multiples to the earnings of a subject company. Whether the earnings and purchase price of the target company are impacted by the current environment will be an important consideration in the analysis. Inconsistent measurements of the purchase price, earnings of the target company and earnings of the subject company may result in unreliable indications of value.

GPC Method

COVID-19 has had a substantial impact on public capital markets during 2020. From Feb. 19 to March 23, the major stock market indices experienced one of the most significant declines since the 1929 Great Depression. However, since March 23, these same capital markets have fully recovered and fueled speculation about a V-shape recovery.

GPC multiples are calculated by dividing the equity or enterprise values of public companies by their respective earnings. If these multiples are calculated based on stock prices occurring after mid-February 2020 and earnings that do not reflect the current environment (*e.g.*, financial statements dated Dec. 31, 2019), the application of these multiples to the earnings of a subject company, which are affected by the current environment, might be problematic. Given these potential issues, it is appropriate to consider what modifications to the M&A and GPC methods are appropriate in order to properly address the disruptions associated with the current environment.

Modifications to the Market Approach

It appears that the conditions associated with the current environment were not fully reflected in the capital markets until mid-February 2020. Accordingly, in situations where the valuation date occurs before mid-February 2020, no modifications to the traditional application of the market approach may be necessary. However, when the valuation date occurs after mid-February 2020, experts may wish to consider the following alternative valuation methods.

Alternative M&A Method 1

If the purchase price and earnings of the target company reflect the current environment, it might be appropriate to calculate and apply these multiple(s) to the affected earnings of the subject company. This can occur when the M&A transaction occurs after mid-February 2020 and the reported earnings of the target company also reflect the impact of the current environment.

If the purchase price of the target company reflects the current environment (the "affected purchase price") but its earnings do not (the "unaffected earnings"), the multiples derived from the transaction may not be appropriate to the earnings of a subject company affected by the current environment (the "affected earnings"). This can occur when the M&A transaction occurs after mid-February 2020, but the reported earnings of the target company are from an earlier, unaffected period (such as 2019). If this multiple is applied to the affected earnings of the subject company, the impact of the current environment might be double-counted, resulting in an unreliable indication of value. In order to correct this analysis, the following procedures may be appropriate: (1) Divide the affected purchase price of the target company by its unaffected earnings (this calculation will provide the "affected M&A multiples"); (2) the affected earnings of the subject company should then be adjusted to remove the impact of the current environment, resulting in its unaffected earnings; and (3) apply the affected M&A multiples to the unaffected earnings of the subject company to estimate the value of the subject company affected by the current environment (the "affected value").

Alternative M&A Method 2

If the current environment has not affected the purchase price of the target company (the "unaffected purchase price") and the unaffected earnings of the target company are used

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in the calculation of the multiples, the following procedures may be appropriate: (1) divide the unaffected purchase price by the unaffected earnings of the target company to calculate the "unaffected M&A multiples"; (2) if the earnings of the subject company are the affected earnings, adjust these earnings to quantify its unaffected earnings; (3) apply the unaffected M&A multiples to the unaffected earnings of the subject company to estimate the value of the subject company unaffected by the current environment (the "unaffected value"); and (4) conduct an income-approach analysis to estimate the value detriment attributable to the current environment for the subject company, which should provide an estimate of damages attributable to the current environment for a discrete time period, then subtract this damage estimate from the unaffected value of the subject company to estimate its affected value.

Alternative GPC Method 1

If the stock price and reported earnings of the public companies reflect the impact of the current environment (*i.e.*, after mid-February 2020), no modifications to the traditional application of the GPC method might be necessary. However, if the valuation date stock price reflects the impact of the current environment (the "affected stock price"), but the reported earnings used in the calculation of the GPC multiples are the unaffected earnings (*e.g.*, derived from Dec. 31, 2019, financial statements), the multiples derived from this analysis might not be appropriate for application to the affected earnings of the subject company.

This is due to the fact that the multiples are calculated by dividing the affected stock price by the unaffected earnings of the GPC. If this multiple is then applied to the affected earnings of the subject company, the impact of the current environment might be double-counted, resulting in an unreliable indication of value. In order to correct this analysis, the following procedures may be appropriate: (1) divide the affected stock price by the unaffected earnings of the GPC to calculate the "affected GPC multiples"; (2) if the earnings of the subject company are the affected earnings, adjust these earnings to quantify its unaffected earnings; or (3) apply the affected GPC multiples to the unaffected earnings of the subject company to estimate the affected value of the subject company.

Alternative GPC Method 2

An alternative to GPC Method 1 is conducted using the following procedures: (1) divide the GPC stock price unaffected by the current environment (the "unaffected stock price") by the unaffected earnings of the GPC to calculate the "unaffected GPC multiples"; (2) in order to quantify the unaffected GPC multiples, it is necessary to identify a date for the unaffected stock price to use in the analysis (this date will likely be different than the valuation date because the stock price as of the valuation date presumably reflects the impact of the current environment; potential dates may include (a) the unaffected stock price date closest to the valuation date, (b) the date of the financial statements of the GPCs used in the calculation of multiples (under the assumption that the financial information is known or knowable); or (c) the first trading day after the financial statements are publicly disclosed by the SEC); (3) if the earnings of the subject company are the affected earnings, adjust these earnings to quantify its unaffected earnings; (4) apply the unaffected GPC multiples to the unaffected earnings of the subject company to estimate the unaffected value of the subject company; and (5) conduct an income approach to estimate the value detriment attributable to the current environment for the subject company, which should provide an estimate of damages attributable to the current environment for a discrete time period, then subtract this damage estimate from the unaffected value of the subject company to estimate its affected value.

Conclusion

The current environment is reshaping the valuation landscape. Accordingly, the mechanical application of traditional valuation methods may produce values that lack credibility and reliability. It is important for valuation experts and bankruptcy lawyers to consider whether modifications to traditional valuation methods are appropriate for any given engagement. If modifications are conducted, the expert should be prepared to provide supportable reasoning for those changes. abi

News at 11

By David Dormont, Edward L. Schnitzer and Joseph E. Samuel, Jr.

Rebutting the Presumption of Insolvency During a Pandemic

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Editor's Note: *To stay up to date on the COVID-19 pandemic, be sure to bookmark ABI's Coronavirus Resources for Bankruptcy Professionals website (abi.org/covid19).*

As the COVID-19 pandemic continues to cause harsh economic conditions throughout the U.S., many companies face the difficult prospect of bankruptcy. Smaller businesses in particular have had to endure significant pain as a result of state-mandated closures, stay-at-home orders, public fears about the virus and tighter lending conditions. Certain industries, such as leisure, dining and travel, have been hit especially hard by the pandemic.[1]

Recent studies suggest that 2 percent of small businesses — numbering more than 100,000 — and 3 percent of restaurant operators have already gone out of business.[2] Larger companies are not exempt from the devastation caused by COVID-19, either: One commentator predicted a record number of bankruptcies by companies with $1 billion or more in debt, and bankruptcies filed with more than $100 million in debt may approach the record set by the 2008 financial crisis.[3] According to Bloomberg, more than 100 companies that declared bankruptcy this year have expressly cited COVID-19, at least in part, as the cause.[4]

Many of these businesses will file for bankruptcy despite having sound finances at the beginning of March. These "sudden collapse" bankruptcy cases might call into question one of the key elements when analyzing a preferential transfer claim — the debtor's insolvency at the time of the transfer —as they could rebut the Bankruptcy Code's presumption, under § 547(f), that a debtor was insolvent 90 days before filing for bankruptcy. This article analyzes the presumption of insolvency and how it will apply to bankruptcies brought on by the rapid onset of the COVID-19 pandemic.

Background on Preferential Transfers

Section 547 of the Bankruptcy Code allows a trustee or debtor in bankruptcy to recover, or "avoid," certain payments made by the debtor in the 90 days (or in the case of a payment to an insider within one year) prior to the filing of a bankruptcy petition. For example, a trustee might be able to avoid an end-of-year distribution to a business owner or a payment to a restaurant supplier for goods.

Known as "preferences," a trustee or debtor is entitled to recover these payments so that the transferred funds may be returned to the bankruptcy estate for equal distributions to all similarly situated creditors. Often, creditors who received payments during the applicable look-back period become angered to learn that they may have to return to the debtor's estate the money they were paid. Adding insult to injury, a distressed company will often fall behind in paying its vendors, so it is common for preference payees to be owed significant sums by the debtor. However, § 547's preference provisions serve an important purpose in the bankruptcy scheme. It prevents the preferential treatment — hence, the name — of some creditors over others in the weeks and months leading up to the filing of a bankruptcy petition.

Five requirements must be met to constitute an avoidable preference under § 547(b). One such requirement, that the transfer be made while the debtor was insolvent, is generally a rebuttable presumption.[5] In light of the difficult economic conditions caused by COVID-19, this rebuttable presumption is especially relevant, as the pandemic presents the rare case where a debtor might have become insolvent only a short time before the bankruptcy filing.

The insolvency presumption usually prevents the debtor or trustee from having to present evidence of insolvency. This makes sense because, in almost all cases, a company does not transition from solvency to filing for bankruptcy during the look-back period. Usually, a company will attempt to ride out tough times — often for months or longer — before taking the extraordinary step of filing for bankruptcy. However, the typical presumptions might not be the case for businesses hit so hard and so suddenly by COVID-19.

1 Brad Moon, "24 Bankruptcy Filings Chalked Up to COVID-19," *Kiplinger* (Sept. 11, 2020), *available at* kiplinger.com/investing/601342/bankruptcy-filings-chalked-up-covid-19-coronavirus (unless otherwise specified, all links in this article were last visited on Sept. 24, 2020).

2 Heather Long, "Small Business Used to Define America's Economy. The Pandemic Could Change That Forever," *Washington Post* (May 12, 2020), *available at* washingtonpost.com/business/2020/05/12/small-business-used-define-americas-economy-pandemic-could-end-that-forever.

3 Mary Williams Walsh, "A Tidal Wave of Bankruptcies Is Coming," *New York Times* (June 18, 2020), *available at* nytimes.com/2020/06/18/business/corporate-bankruptcy-coronavirus.html.

4 Davide Scigliuzzo, Josh Saul, Shannon D. Harrington, Claire Boston & Demetrios Pogkas, "COVID-19 Is Bankrupting American Companies at a Relentless Pace," Bloomberg (July 9, 2020), *available at* bloomberg.com/graphics/2020-us-bankruptcies-coronavirus.

5 11 U.S.C. § 547(f) states, "The debtor is presumed to have been insolvent on and during the 90 days immediately preceding the date of the filing of the petition."

Defining "Insolvency" Under the Code

Insolvency is a question of fact decided by the bankruptcy judge.[6] Thus, "the Bankruptcy Court has broad discretion when considering evidence to support a finding of insolvency."[7] To determine whether a debtor was insolvent, courts look to the statutory definition of this term. Under the Bankruptcy Code, a debtor is insolvent if "the sum of such entity's debts is greater than all of such entity's property, at fair valuation."[8] Thus, "In determining a 'fair valuation' of the entity's assets, an initial decision to be made is whether to value the assets on a going concern basis or a liquidation basis."[9] Finally, "If liquidation in bankruptcy was not clearly imminent on the transfer date, then the entity should be valued as a going concern."[10]

Evidence of the debtor's book value is generally only a "starting point" to the court's determination of insolvency, as "fair valuation" is the test under the definition set forth in § 101(32).[11] Even financial statements prepared in accordance with Generally Accepted Accounting Principles (GAAP) are not viewed by the bankruptcy court as evidence of insolvency, as these statements record assets at historical cost rather than fair value.[12] Instead, courts have long held that "'fair valuation,' as used in the Bankruptcy Act, means the fair cash value or the fair market value of the property as between one who wants to purchase and one who wants to sell the property."[13]

In the context of an avoidance action, the relevant date of insolvency is the date of a given transfer that the debtor seeks to avoid — not the date on which the bankruptcy petition was filed.[14] Sometimes, it is difficult to ascertain whether a debtor was insolvent on a particular date. In such circumstances, courts have approved of the "retrojection" principle,[15] which provides that "when a debtor was insolvent on the first known date and insolvent on the last relevant date, and the trustee demonstrates the absence of any substantial or radical changes in the assets or liabilities of the bankrupt between the retrojection dates, the debtor is deemed to have been insolvent at all intermediate times."[16]

Rebutting the Presumption of Insolvency

The debtor/trustee bears the ultimate burden of proof and must prove insolvency by a preponderance of the evidence.[17] While § 547(f) provides a presumption that the debtor is insolvent during the look-back period, this presumption might be rebutted by the creditor. Thus, "To rebut a presumption of insolvency, a creditor must introduce some evidence that the debtor was not in fact insolvent at the time of the transfer."[18] In addition, "If the creditor introduces such evidence, then the trustee must satisfy its burden of proof of insolvency by a preponderance of the evidence."[19]

Generally, creditors attempt to present evidence from a valuation expert in order to show that the debtor's assets exceeded its liabilities at the time of the transfer, but the expert's methodology must be sufficiently reliable.[20] One of those methods, the discounted-cash-flow method of valuation, has been approved by bankruptcy courts for purposes of determining solvency.[21]

The insolvency presumption does not apply in actions to avoid transfers to insiders made more than 90 days but less than one year before the filing of the bankruptcy petition. In that case, the burden is on the trustee by default to demonstrate insolvency at the time of the insider preference payment.[22]

The Insolvency Presumption and Other Concerns in the Time of COVID-19

The insolvency requirement under § 547(b)(3), together with its presumption under § 547(f), present important issues for both debtors and creditors as companies declare bankruptcy as a result of the economic conditions imposed by the COVID-19 pandemic. Following government orders across the nation closing many brick-and-mortar, non-life-sustaining businesses, a number of companies, both large and small, have filed for bankruptcy in the past several months.

The date-of-insolvency question is crucial for businesses, their owners and their creditors, as prior to COVID-19 many businesses were profitable with no knowledge that bankruptcy was imminent. Indeed, but for the outbreak of COVID-19 and the resulting shutdown orders, many of these businesses would not have been insolvent. Unlike the typical bankruptcy case, in which a company that files for bankruptcy has been in a difficult financial situation for many months or even years prior to the filing of a petition, pandemic-related shutdowns are causing companies that might not have been insolvent to find themselves in need of initiating bankruptcy proceedings. In such circumstances, affected creditors might seek to rebut the presumption of insolvency, or use such a threat to negotiate a more favorable settlement of the dispute.

The rapid onset of bankruptcies due to COVID-19 is not entirely without precedent. Regrettably, the situation resembles the struggle faced by some businesses in the wake of the Sept. 11, 2001, terrorist attacks. These cases provide guidance as to how the insolvency presumption might be rebutted in bankruptcy cases stemming from the pandemic.

For example, take the bankruptcy filed by the domestic cruise ship company American Classic Voyages on Oct. 19, 2001.[23] In that case, American Classic sought to avoid a $29 million payment made to various banks on Aug. 14, 2001.[24] The banks presented expert testimony analyzing American Classic's financial statements in the months leading up to the Sept. 11, 2001, attacks, and the court found this evidence sufficient to rebut the insolvency presumption.[25]

6 *In re Ames Dep't Stores Inc.*, 506 Fed. App'x 70, 72 (2d Cir. 2012).
7 *Id.*
8 11 U.S.C. § 101(32).
9 *In re Am. Classic Voyages Co.*, 367 B.R. 500, 508 (Bankr. D. Del. 2007).
10 *Id.*
11 *See In re Waccamaw's Homeplace*, 325 B.R. 524, 529 (Bankr. D. Del. 2005).
12 *Id.*
13 *Grandison v. Nat'l Bank of Commerce of Rochester*, 231 F. 800, 804 (2d Cir. 1918); *see also In re F & S Cent. Mfg. Corp.*, 53 B.R. 842, 849 ("Fair value is determined by estimating what the debtor's assets would realize if sold in a prudent manner in current market conditions.") (citing 2 *Collier on Bankruptcy* ¶ 101.26, p. 101-56 (15th ed. 1985)).
14 *In re Parker Steel Co.*, 149 B.R. 834 (Bankr. N.D. Ohio 1992).
15 *See, e.g., Briden v. Foley*, 776 F.2d 379, 382-83 (1st Cir. 1985).
16 *In re Terrific Seafoods Inc.*, 197 B.R. 724, 731 (Bankr. D. Mass. 1996).
17 *See In re Roblin Indus. Inc.*, 78 F.3d 30, 34 (2d Cir. 1996).
18 *Ames*, 506 Fed. App'x at 72 (citing *Roblin*, 78 F.3d at 34).
19 *Roblin*, 78 F.3d at 34.
20 *See, e.g., In re Lids Corp.*, 281 B.R. 535, 546 (Bankr. D. Del. 2002).
21 *See, e.g., In re Energy Co-Op. Inc.*, 109 B.R. 822 (Bankr. N.D. Ill. 1989).
22 *In re Perry*, 158 B.R. 694 (Bankr. N.D. Ohio 1993).
23 *See Am. Classic*, 367 B.R. at 502.
24 *Id.*
25 *Id.* at 509-14.

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As will likely be the case in bankruptcies stemming from COVID-19, the court considered the rapid onset of cancellations and closures experienced by American Classic and concluded that, despite any financial challenges before Sept. 11, 2001, it was the attacks themselves that struck the "fatal blow to their business."[26] Thus, the $29 million in payments were not avoidable as preferences because American Classic was not insolvent on Aug. 14, 2001, the date of the transfer.[27]

A similar issue was addressed in the *Irving Tanning Co.* bankruptcy. In adjudicating a $23.6 million fraudulent-transfer action, the U.S. Bankruptcy Court for the District of Maine addressed a similar insolvency fact pattern. Although the defendants prevailed for other reasons, the court noted that the plaintiff would not have been "able to convincingly link [the debtor's 2009 inability to pay its bills] with the 2007 payments to the Shareholder Defendants. A more likely culprit was the unforeseen, intervening, and devastating impact of the recession of late 2007 through 2009, about which several Defendants testified and of which I can take judicial notice."[28] This suggests that bankruptcy courts could similarly be willing to take judicial notice of the harsh impact that pandemic-related closures have had on American businesses.[29]

26 *Id.* at 513.

27 *Id.* at 516.

28 *Dev. Specialists Inc. v. Kaplan (In re Irving Tanning Co.)*, 555 B.R. 70, 85 n.11 (Bankr. D. Me. 2016) (citing *W. Coast Hotel Co. v. Parrish*, 300 U.S. 379, 399 (1937) (court may take judicial notice of well-known, widespread economic conditions)).

Conclusion

Courts might need to perform this same analysis in bankruptcies stemming from COVID-19 to determine whether a company was already insolvent before the pandemic. The rapid onset of closures and other difficult economic conditions as a result of the pandemic — especially in or around March 2020 — will present challenging issues for creditors and debtors as they seek to resolve the insolvency question. Many companies across the U.S. likely suffered steep financial losses from solvency in February to insolvency by April. The recipients of payments from such companies presumably had little reason to believe that such payments could eventually be deemed preferences in bankruptcy. Now, they could find themselves defendants to a preference avoidance action. Both creditors and debtors will have to deal with the presumption of insolvency as more and more bankruptcies are filed in COVID-19's wake. abi

29 This article does not cover the ordinary-course defense being relevant in this aspect as it would take away from the focus of this discussion, which is solely on the insolvency presumption and COVID-19. That focus relates to § 547(b) (the requirement of insolvency) and (f) (the 90-day insolvency presumption). Under § 547(c), there are nine affirmative defenses, including the ordinary-course defense. Each of those defenses could apply in a COVID-caused bankruptcy the same as they could in a non-COVID-caused bankruptcy. As there have been numerous ABI articles written on the ordinary-course defense, as well as the new value defense and other § 547(c) affirmative defenses, the authors did not want to grow this article and have it cover any of those § 547(c) affirmative defenses.

Valuation Will Drive the Next Wave of Chapter 11 Cases

Committees: Business Reorganization

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Many professionals anticipate that valuation will be the fulcrum issue in the upcoming wave of chapter 11 cases, and creative advocacy will be at a premium.

Traditional Valuation Approaches and the Bankruptcy Code

The two tried-and-true, traditional methods of business valuation — "the income approach" and "the market approach" — are regularly utilized and recognized in bankruptcy courts. With many businesses experiencing no or diminished cash flow and the future of the economy uncertain, the traditional valuation approaches become less reliable and meaningful.

Valuation is central to the chapter 11 process. It affects the (1) use of cash collateral during a chapter 11 case, (2) rights of secured creditors with regard to claim amounts and interest, (3) rights of creditors when a § 363 sale of assets is proposed, and (4) rights of creditors to challenge confirmation of a chapter 11 plan. The Bankruptcy Code is almost silent on the

challenge confirmation of a chapter 11 plan. The Bankruptcy Code is almost silent on the definition of "value," however. Section 506(a) is one of the only provisions that discusses valuation, and it states that "value shall be determined in light of the purpose of the valuation and of the proposed disposition or use of such property...."[1]

In many cases, valuation is the single most important issue affecting a reorganization's success. When a company files for chapter 11 protection, it ordinarily reassesses the entire business structure, looking at operations, possible sales of assets, management, personnel, debt structures and every other aspect of the company. Included in this review is the valuation of the business and its assets. It is not only helpful to re-examine the company, but it is required to confirm a chapter 11 plan. This is normally done with the help of valuation experts. Without a pandemic, the methods of valuation are familiar, predictable and steady.

Valuation in Pandemic-Era Chapter 11 Cases

The pandemic has wiped out many companies' abilities to project future performance. For the worst-affected companies, financial data such as revenues and expenses, cash flow and net income are at best skewed and at worst unknowable. How can there be a baseline paradigm for valuation without these normal markers? There really is no predictable model for valuation in an economic pandemic. This means that a "battle of the experts" will feature prominently in many chapter 11 cases, and creative advocacy will be at a premium. It also means that parties are going to have to lay the valuation issue at the feet of bankruptcy judges and ask those legal experts (not business valuation experts) to value businesses with no predictable cash flow, revenue or expense numbers. All the uncertainty makes valuing a business even more speculative.

Some of the changes brought on by COVID-19 will be visible in the testimony of expert witnesses. For example, a mechanical market approach analysis might not be appropriate, because COVID-19 likely impacted other similar businesses on different scales. It may not be an apples-to-apples comparison. The most crucial factor for any valuation will be the company's balance sheet. After that, an expert will need to factor in such things as customer loyalties, goodwill, brand value and other considerations, such the effect of *force majeure* contract provisions. Experts will need to examine existing or future commitments, cancelled business, and whether contracts or leases can be re-priced. The availability of government financial rescue opportunities, and the tax implications of any government programs, will also be critical.

Likewise, experts will have to rethink valuations in the context of (1) available capital; (2) COVID-19's effect on human resources, supply chains and the need for physical office space; (3) a COVID-19 discount rate under various market conditions, perhaps forecasting the rate for years of pandemic conditions; and (4) whether a business can refinance its debt in the short term if cash flow is a problem. In addition to proving feasibility at confirmation, all of the unknown valuation factors affect the best-interest-of-creditors test,[2] insolvency analyses, chapter 11 voting, claim disputes, sale of assets and myriad common chapter 11 issues. These valuation unknowns are like discovering a new planet: We just don't know what is out there or ahead.

Valuation of a business during this time is likely to yield some unpredictable results. At least if valuation is occurring within the confines of chapter 11, there is a familiar process and statutory guideposts to lend some predictability. All businesses should be aware that valuation is the target that most unhappy creditors aim for to either force a company to liquidate or to exert control over a company's reorganization. For many companies, the strength of its balance sheet is going to be a primary valuation factor in these uncertain pandemic conditions. It is important for companies to get their financial houses in order.

Conclusion

Valuation is a critical component of every chapter 11 case. In the coming wave of pandemic-driven business reorganizations and orderly wind-downs, companies should seize the opportunity created by market uncertainty to push valuations favorable to their desired outcomes.

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[1] 11 U.S.C. § 506(a).

[2] 11 U.S.C. § 1129(a)(7).

The International Scene

BY RAFAEL X. ZAHRALDDIN-ARAVENA, ANTOINE LEDUC AND OLYA ANTLE

COVID-19: A Catalyst of Modernization Across Jurisdictions

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Editor's Note: *To stay up to date on the COVID-19 pandemic, be sure to bookmark ABI's Coronavirus Resources for Bankruptcy Professionals website (abi.org/covid19). Mr. Zahralddin-Aravena also leads ABI's COVID-19 Global Economic Response Project (globalinsolvency.com/covid19).*

The novel coronavirus disease has altered the way that legal professionals practice law across the globe, as courts in both the common law and civil law traditions[1] have had to modify the administration of law to do their part to enforce health restrictions. Courts closed, then reopened, primarily virtually, as their services are deemed "essential" functions in many jurisdictions.

In some courts, there has been a ban on paper deliveries of any kind due to health concerns.[2] The magnitude of the effects on legal systems around the world and their duration is yet undetermined but merits a close review, as common law jurisdictions (such as the U.S.) and civil law jurisdictions (such as Québec and France) are forced to accelerate the move toward electronic signatures, electronic filings and remote notarizations.[3]

Pre-COVID-19 Efforts to Modernize the Administration of Justice

Global Proliferation of Electronic Transactions

The United Nations Conference on Trade and Development (UNCTAD) reports that 145 countries across the globe have adopted laws to facilitate electronic transactions. It sees such laws as essential, stating that "to have e-transaction laws that recognize the legal equivalence between paper-based and electronic forms of exchange" is a "prerequisite for conducting commercial transactions online."[4] Eighty-one percent of the world's nations have such legislation in place, 6 percent have drafted legislation, 4 percent have no legislation, and the remaining 9 percent have not reported data to UNCTAD.[5]

Movement Toward Digitized Records, Electronic Filings and e-Signatures

In 1998, the Uniform Law Conference of Canada adopted the Uniform Electronic Commerce Act.[6] It proposed the use of "functional equivalents" to paper in a "technology neutral" way to make the law "media neutral" (*i.e.*, equally applicable to paper-based and electronic communications).[7] Legislation based on these principles was thereafter adopted throughout Canada, including in Québec,[8] and is "generally permissive in relation to the use of [an] e-signature so long as the e-signature technology used is reliable and meets the basic characteristics of an enforceable e-signature."[9]

The U.S.'s federal law has recognized electronic transactions, including smart contracts and electronic signatures, through the U.S. Electronic Signatures in Global and National Commerce (ESIGN) Act passed in 2000, as well as through the adoption of the Uniform Electronic Transactions Act (UETA) released in 1999.[10] The UETA provides that when a law requires either a writing or a signature, an electronic record or an electronic signature can satisfy that requirement when the parties to the transaction have agreed to proceed electronically.[11] The UETA and ESIGN ensure that electronic records and signatures have the same legal effect as traditional paper documents and wet-ink signatures.[12]

1 On the various legal traditions of the world in general, *see* H. Patrick Glenn, *Legal Traditions of the World, 2d Ed.* (Oxford University Press 2004).

2 For example, by order of March 16, 2020, the Supreme Court of Delaware ordered that as a precautionary measure, lawyers shall not submit any copies of electronically submitted documents. Order (March 16, 2020), *available at* courts.delaware.gov/rules/pdf/March162020COVIDPaperFilingsSuspended.pdf (unless otherwise specified, all links in this article were last visited on May 28, 2020).

3 The Council of Europe has an informative webpage, "Management of the Judiciary — Compilation of Comments and Comments by Country," which provides a good survey of measures across Europe; *available at* coe.int/en/web/cepej/compilation-comments.

4 U.N. Conference on Trade and Development, E-Transactions Legislation Worldwide, *available at* unctad.org/en/Pages/DTL/STI_and_ICTs/ICT4D-Legislation/eCom-Transactions-Laws.aspx.

5 *Id.*

6 Uniform Law Conference of Canada, Uniform Electronic Commerce Act (Annotated 1999), *available at* ulcc.ca/en/1999-winnipeg-mb/359-civil-section-documents/1138-1999-electronic-commerce-act-annotated.

7 *Id.*

8 "Act to Establish a Legal Framework for Information Technology," C.Q.L.R. c C-1.1, *available at* legisquebec.gouv.qc.ca/en/ShowDoc/cs/C-1.1 (updated Feb. 1, 2020).

9 Tracy Springer & Kiriakoula Hatzikiriakos, "What's Ink Got to Do with It ? Enforceability of E-Signature in Commercial Lending Documentation," *ABA Business Law Today* (April 9, 2020), *available at* businesslawtoday.org/2020/04/whats-ink-got-enforceability-e-signature-commercial-lending-documentation.

10 Electronic Transactions Act, Uniform Law Comm'n, *available at* uniformlaws.org/committees/community-home?CommunityKey=2c04b76c-2b7d-4399-977e-d5876ba7e034.

11 *Id.*

12 Several U.S. states, including Arizona and Tennessee, have also passed measures related to ESIGN and EUTA to encourage the proliferation of electronic transactions. Delaware has passed legislation and initiated a study to use technology to modernize securities and Uniform Commercial Code filings and record maintenance. For an excellent survey of areas where Delaware is positioned to push such innovation forward, *see* My Say, "Why the Delaware Blockchain Initiative Matters to All Dealmakers," *Forbes* (Sept. 20, 2017), *available at* forbes.com/sites/groupthink/2017/09/20/why-the-delaware-blockchain-initiative-matters-to-all-dealmakers/#ab9b8fa75508; Blockchain Consulting LLC, Open Letter to Delaware (Sept. 14, 2017), *available at* blockchainconsulting.net/open-letter-to-delaware.

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In September 1998, the Judicial Conference of the U.S. adopted electronic record-keeping, opening up access to legal information to the public through the Public Access to Court Electronic Records (PACER).[13] In the late 1990s, federal courts in the U.S. also adopted the electronic case-management system known as the Case Management/Electronic Case Files (CM/ECF), which allowed electronic filings of documents with electronic signatures (in lieu of wet signatures). While the movement toward digitization has not weaned the legal industry away from paper, it modernized the administration of justice in the U.S. and Québec, and created a platform from which their judicial systems can transition into the post-COVID-19 era.

Electronic Notarizations and Remote Online Notarizations

Pre-COVID-19 modernization efforts did not escape the realm of notarizations. In the U.S., even before the pandemic, a number of states permitted electronic notarizations or e-notarizations, which involve the notarization of electronic signatures on documents in electronic format in the presence of a notary.[14] A number of states also permitted remote notarizations performed through the remote online notarization systems (RONs), whereby the notary and signer appear remotely and use audio/video technology to notarize documents.[15] By the end of 2019, 22 U.S. states allowed RONs, with Virginia being the first state to lead this charge in 2010.[16]

However, prior to COVID-19, similar efforts were not implemented in civil law jurisdictions, likely due to the conceptual and substantive differences between a common law notary and a civil law notary. In common law jurisdictions, such as the U.S. and Great Britain, the notary public is a public officer with a more narrowly defined role centered on the identification of document signers, taking of signers' acknowledgments, and administering oaths and affirmations.[17] Notaries in these systems are not responsible for the accuracy, contents or legality of the underlying documents they notarize.

On the other hand, the civil law notary is subject to ethical standards, with considerable responsibility and discretion in the performance of such legal functions as drafting and authenticating legal instruments (which conclusively establishes that the instruments themselves are genuine and that what they recite accurately represents what the parties said).[18] An action authenticated by a civil law notary is given great probative value in the civil law system, a legal regime dominated by the need for authenticity of a written record, where notaries are trained in law school and perform tasks similar to those of a solicitor or attorney.[19] The responsibility of a Latin American *Notario Publico* is an excellent example of the gravity of the civil law notary's duties, which extend to the incorporation of every company, buying and selling of real estate, establishment of deeds and wills, and the creation of mortgages.[20] *Notarios Publico* will "labor over the document and make sure it is in conformance with the law."[21] The Mexican *Notario Publico* has the words "Doy Fe" next to the signature on a document, which translates into "I give faith," as the civil law notary's role is more akin to that of a jurist than a lawyer.[22]

The difference in the degree of formality and evidentiary effect of the notarial act accounts for the relative ease with which certain common law traditions, such as in the U.S., have moved toward the implementation of RONs, even prior to the pandemic. However, it is clear that the pandemic has augmented the pace at which these changes must be made across all traditions, forcing both the civil law and common law jurisdictions to expedite the process of adopting the relevant regulations to modernize the traditional processes now challenged by the stay-at-home orders and social-distancing mandates.

Acceleration of Modernization Efforts in Light of the Pandemic

Measures in the U.S.

In response to the global emergency caused by the outbreak of COVID-19, courts and legal professionals in the U.S. have implemented a number of measures to address the pandemic.[23] Such measures include the use of videoconferencing facilities to conduct remote court hearings, mediations, depositions and other functions that normally require extensive personal contact.[24]

In bankruptcy (and other federal) courts across the U.S., "wet signatures" have been eliminated for most filings under the CM/ECF system; however, the majority of the U.S. bankruptcy courts have now gone a step further by temporarily suspending the requirement to obtain "wet signatures" on documents for which such signatures were

13 *See* "25 Years Later, PACER, Electronic Filing Continue to Change Courts," *Judiciary News* (Dec. 9, 2013), *available at* uscourts.gov/news/2013/12/09/25-years-later-pacer-electronic-filing-continue-change-courts.

14 *See* Michael Lewis, "Remote Notarization: What You Need to Know," *Notary Bulletin* (June 27, 2018), *available at* nationalnotary.org/notary-bulletin/blog/2018/06/remote-notarization-what-you-need-to-know.

15 Notary performing the notarization services remotely must verify the identity of the signer through knowledge-based authentication (KBA) methods, credential analysis and remote presentation of the identification documents (via a webcam). To start a remote notarization, both the signer and notary must access a RON platform. Documents used must be in an electronic format, such as a PDF. Once the notary verifies the signer's identity and is confident that the signer is willing and mentally competent, the signer and notary both sign the document electronically, and the notary affixes an electronic seal to the same. When finished, the document can be retrieved from the RON platform. In addition to keeping a journal of the remote online notarization, notaries are also required to create an audiovisual recording of each remote notarization. *See* David Thun, "The State of Remote Online Notarization," *Nat'l Notary Magazine* (November 2019), *available at* nationalnotary.org/notary-bulletin/blog/2019/11/the-state-of-remote-online-notarization.

16 Bob Jawarowski, "Remote Online Notarization: More States, Including New Jersey, Join the Crowd," Holland & Knight Alerts (April 17, 2020), *available at* hklaw.com/en/insights/publications/2020/04/remote-online-notarization-more-states-including-new-jersey.

17 *See generally* Pedro A. Malavet, "Counsel for the Situation: The Latin Notary, a Historical and Comparative Model," 19 *Hastings Int'l & Comp. L. Rev.* 389 (Spring 1996).

18 *See* John Henry Merryman, *The Civil Law Tradition* 113-115 (1969). Civil law notaries are at work in more than 88 countries around the world and are collectively grouped in the International Union of Notaries, "a non-governmental organization that aims to promote, co-ordinate and develop the function and activities of notaries throughout the world." *See* the Union's mission statement at uinl.org/mission.

19 J.-F. Sagaut, "The Notary," 4 *Henri Capitant L. Rev.* 130 (2012), *available at* henricapitant.org/revue/en/n4.

20 Jonathan A. Pikoff & Charles J. Crimmins, "Lost in Translation: *Texas Notary Public v. Mexico* Notario Publico," *available at* sos.state.tx.us/statdoc/notariopublicoarticle.shtml.

21 *Id.* (quoting personal interview with Franciso Visoso, *Notario Publico* No. 145 for Mexico City, Feb. 15, 2005).

22 *Id.*

23 *See* "Global Responses to Limit the Economic Impact of Covid-19 Pandemic," Global Insolvency, *available at* globalinsolvency.com/covid19/usa.

24 *Id.*

required, including the debtors' voluntary petitions for bankruptcy relief.[25]

More than 20 other states have adopted emergency legislation allowing remote online notarization.[26] In those states where RON services are permitted (either on a temporary or permanent basis), there might be certain limitations concerning the audio/video platforms used, as well as certifications that notaries must obtain from the states' regulatory authorities.[27]

Measures in Québec[28]

The modernization of the Québec judiciary system is still at an early stage; however, the pandemic is accelerating it.[29] In 2018, the government of Québec had already announced a plan to modernize the justice system and invest CAD $500 million between 2018-23, including a sum of CAD $289 million dedicated to bringing the justice system in line with the latest technology.[30] In addition, since 2016 the newly enacted Code of Civil Procedure (Québec) adopted several provisions to foster the use of appropriate technology.[31]

In Québec, since March 16, 2020, courthouse services have been reduced and hearings limited to urgent matters. On March 26, 2020, a judge of the Superior Court of Trois-Rivières (Québec) presided over Québec's first virtual trial.[32] All Québec Superior Court judges have received special training on videoconference facilities and have formed a judicial IT Committee. The use of technology for all hearings that remain scheduled is favored, including virtual hearings, but lawyers are encouraged to try to amicably settle their cases. The Montréal Commercial Chamber (*i.e.*, the bankruptcy court) was only available for urgent or priority matters by telephone on a case-by-case basis during the pandemic until June 1, 2020, when it somewhat resumed its hearings and added virtual hearings as a possibility.

There is no e-filing system, and new urgent applications must still be filed at the court registry on paper with court fees paid at the registry,[33] but this is about to change in the forthcoming weeks.[34] However, the Digital Office of the Québec Court of Appeal, launched on April 7, 2020, allows lawyers and citizens across Québec to file electronic notices of appeal in *de plano* appeals in civil matters, and court fees for these filings are payable online.[35] Some matters may be heard by videoconference before the court of appeals.[36]

As previously mentioned, e-signatures in Québec were generally accepted after the adoption of legislation based on the Uniform Electronic Commerce Act,[37] but not for notarial deeds.[38] On March 28, 2020, the government of Québec announced a temporary measure allowing notaries to close notarial deeds remotely.[39] Notarial deeds can be closed remotely if (1) the notary can see and hear each party; (2) all parties and intervenors can see and hear the notary; (3) where the context requires, witnesses can see and hear the parties and the notary; (4) the signatories and the notary can see the act; (5) the signatories other than the notary affix their signature by a technological means that enables their identification and the acknowledgment of their consent; and (6) the notary affixes his/her official digital signature.[40]

A notary must ensure the integrity and confidentiality of the documents shared and the signature process. This notary must also maintain the integrity of the act throughout its lifecycle, including to ensure its preservation.[41] As a side note, similar measures have also been adopted in France.[42]

Conclusion

The virus has not respected borders, significantly affecting how lawyers provide legal services and courts administer justice in both common law and civil law jurisdictions. Katherine Mangu-Ward, editor-in-chief of *Reason* magazine, recently stated:

> COVID-19 will sweep away many of the artificial barriers to moving more of our lives online. Not everything can become virtual, of course. But in many areas of our lives, uptake on genuinely useful online tools has been slowed by powerful legacy players, often working in collaboration with overcautious bureaucrats.[43]

Current changes have occurred on a truncated timeline, accelerating trends that were already underway. As legal systems throughout the world are propelled into the digital age, they will emerge from the current crisis dramatically transformed post-pandemic. abi

25 For a list of bankruptcy courts that have adopted such orders and to obtain copies of the orders, *see* uscourts.gov/about-federal-courts/court-website-links/court-orders-and-updates-during-covid19-pandemic#bankruptcy.

26 For notary law updates by state, *see* nationalnotary.org/notary-bulletin/blog/2020/03/answers-urgent-questions-notaries-ron.

27 *Id.*

28 On Québec's legal traditions, *see* Antoine Leduc, *Mondialisation et Harmonisation Du Droit Des Sûretés* (Les Éditions Thémis 2012), at 315-20. Québec is a mixed jurisdiction, with its private law system belonging to the civil law tradition and its public law system inspired by the British common law institutions. *Id.*

29 Emmanuelle Gril, "La Justice à Distance: Des Enjeux Pour L'avenir de la Profession Juridique," National | ABC National (April 14, 2020), *available at* nationalmagazine.ca/fr-ca/articles/law/hot-topics-in-law/2020/la-justice-a-distance.

30 Minister of Justice and Attorney General of Québec, Budget 2018-2019/Justice, "A Plan to Modernize the Justice System" (March 27, 2018), *available at* justice.gouv.qc.ca/fileadmin/user_upload/contenu/documents/En__Anglais_/centredoc/publications/ministere/dossiers/Justice_1819.pdf.

31 Code of Civil Procedure, C.Q.L.R. c C-25.01, Art. 26, *available at* legisquebec.gouv.qc.ca/en/ShowDoc/cs/C-25.01. *See also* Jean-François De Rico & Patrick Gingras, "Les Premiers Pas de la Procédure Technologique: Regard Technologique sur le Nouveau Code de Procédure Civile," 21 *Lex Electronica* 1 (2016), *available at* lex-electronica.org/articles/volume-21/les-premiers-regards-de-la-procedure-technologique-regard-technologique-sur-le-nouveau-code-de-procedure-civile.

32 Éric Thibault, "Le Système Judiciaire Arrivera Enfin au 21e Siècle: La Crise Forcera Nos Tribunaux à Moderniser Leurs Pratiques," *Le Journal de Montréal* (April 11, 2020) at 20, *available at* journaldemontreal.com/2020/04/11/le-systeme-judiciaire-arrivera-enfin-au-21e-siecle.

33 "Expanded Operations of the Superior Court – Civil and Family Matters (District of Montreal)," Superior Court of Québec (April 17, 2020), *available at* tribunaux.qc.ca/c-superieure/avis/index_avis.html.

34 "A stronger Justice System Emerges as Québec Courthouses Gradually Resume Activities," Minister of Justice and Attorney General of Québec (May 28, 2020), *available at* justice.gouv.qc.ca/en/press-releases/a-stronger-justice-system-emerges-as-quebec-courthouses-gradually-resume-activities.

35 *See* Québec Court of Appeal Digital Office website, *available at* https://courdappelduquebec.ca/en/digital-office.

36 *See* "Virtual Courtrooms," Court of Appeal of Quebec, *available at* courdappelduquebec.ca/en/virtual-courtrooms.

37 Vincent Gautrais, "Signature," LCCJTI.CA, *available at* lccjti.ca/definitions/signature.

38 Mark Philips, "Électronique Juridique et Juridisme Électronique," *Les Cahiers de Propriété Intellectuelle* 155 (2008), at 161, 165, *available at* lccjti.ca/doctrine/electronique-juridique-et-juridisme-electronique. *See also* Notaries Act, C.Q.L.R. c N-3, Art. 45-61, *available at* legisquebec.gouv.qc.ca/en/ShowDoc/cs/N-3.

39 "Temporary Measures Authorizing Notaries to Close Acts Remotely and Bailiffs to Serve Pleadings by Technological Means," Minister of Justice and Attorney General of Québec (March 28, 2020), *available at* justice.gouv.qc.ca/en/press-releases/temporary-measures-authorizing-notaries-to-close-acts-remotely-and-bailiffs-to-serve-pleadings-by-te; *but see* "Management of the Judiciary: Compilation of Comments and Comments by Country," Council of Europe, *available at* coe.int/en/web/cepej/compilation-comments (reflecting that notarial cases in civil jurisdictions across Europe have been treated in other ways in light of pandemic: prioritized by courts in Denmark, suspended in Portugal utilizing judicial holiday procedure, allowed in Serbia with discrete social distancing measures in place, and suspended in Italy).

40 "Regulation Respecting the Digital Official Signature of a Notary," C.Q.L.R. c N-3, r.13.1, Art. 2, *available at* legisquebec.gouv.qc.ca/en/ShowDoc/cr/N-3,%20r.%2013.1.

41 *See* Cristina N. Armella, "The Exercise of the Notarial Activity in Times of Pandemic: New Technologies at the Service of the Notarial Function," Int'l Union of Notaries (April 28, 2020), *available at* www.uinl.org/en_GB/-/the-exercise-of-the-notarial-activity-in-times-of-pandemic-new-technologies-at-the-service-of-the-notarial-function.

42 Notaires du Grand Paris, "Signature d'un Acte Chez le Notaire: Quelle Situation Pendant le Confinement?," Votre Notaire Vous Informe (April 2020), *available at* fr.calameo.com/read/003616144b21750e7f304.

43 "Coronavirus Will Change the World Permanently. Here's How," *Politico* (March 19, 2020), *available at* politico.com/news/magazine/2020/03/19/coronavirus-effect-economy-life-society-analysis-covid-135579.

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Andrew M. Golanowski
Geraci Law LLC | Milwaukee

Hon. John E. Hoffman, Jr.
U.S. Bankruptcy Court (S.D. Ohio) | Columbus

Jeana K. Reinbold
Jeana Kim Reinbold, P.C. | Springfield, Ill.

M. Gretchen Silver
Office of the U.S. Trustee | Chicago

CONCURRENT SESSION

2020

VIRTUAL MEETINGS – BEST PRACTICES

I. Attorney/Client Meetings/Consultations

a. Issues with verification of ID and Social Security Number

b. Be sure that you are in an area that is quiet enough for your microphone not to pick up stray conversations

c. Be patient, and speak slowly. The opportunity for misunderstandings is greater via videoconference than in person.

II. Hearings with the Court/Trustee by telephone

a. Use the mute button. Until your hearing is called, mute your telephone.

b. Do not place the call on hold. The hold music/message will be piped through to the courtroom/hearing room.

c. Do not interrupt. There is a tendency when on the telephone to start talking just a bit too early. Remember, this is still a hearing, not just a phone call.

d. Make sure your client has the telephone number and access code in advance of the hearing.

e. Look through your court's procedures ahead of time.

III. Hearings with the Court/Trustee by video

a. Most courts do have procedures for remote hearings. Learn and know them.

b. Test out the video conferencing with your client before the hearing. Make sure they are comfortable and familiar with, most likely,

Zoom, prior to the hearing. You do not want to have someone who can't unmute themselves, and be dealing with that at the hearing. Straighten it out ahead of time.

c. Speak slowly and clearly, and do not interrupt. Sometimes a hiccup in the connection can cause one to believe a person is done speaking. Wait a second before you go ahead.

Attached are sample general orders from different courts regarding court proceedings during the COVID-19 pandemic, sample orders establishing procedures for virtual hearings in a specific case, examples of procedures, notices and informational sheets for debtors generated by Trustees, some examples of Judges' videoconference rules and tips, and a sample of a short Zoom guide for debtors.

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF ILLINOIS

THIRD AMENDED GENERAL ORDER NO. 20-03

Court Proceedings During COVID-19 Public Emergency

Because a state of emergency has been declared in response to the spread of COVID-19, and because the Centers for Disease Control and Prevention have urged reduced contact among people to slow the spread of the disease, the U.S. Bankruptcy Court for the Northern District of Illinois issues this order, *effective October 13, 2020*, to protect public health.

1. Court hours. The Bankruptcy Court will remain open during normal business hours, pending further order of court. Because some deadlines under the Bankruptcy Code and Federal Rules of Bankruptcy Procedure cannot be changed, the Bankruptcy Court will remain open as long as possible.

2. All court calls to be heard electronically. All court calls will be held remotely by electronic means. No personal appearances in court will be necessary or permitted, unless the judge orders otherwise. Attorneys must direct their clients *not* to appear in person at the courthouse.

3. Motions. Local Rule 9013-1(E)(1) governing presentment of motions in court is suspended. All motions will be heard remotely by electronic means, without personal appearances. Movants *must* use one of the two attached Notice of Motion forms.

4. Court appearances by Zoom for Government or AT&T Teleconference. At the discretion of the individual judge, the bankruptcy court will use either Zoom for Government or AT&T Teleconference for court appearances. There is no charge for using these services (other

than the usual toll charges for Zoom for Government). Attorneys and parties in interest should consult the individual judge's page on the court's web site to see which service the judge uses.

a. Zoom for Government. Attorneys and parties may connect through Zoom for Government by computer or by telephone. To connect by audio only, a telephone or a computer with a microphone and speakers (or headphones) is necessary. To connect by video, a computer with a webcam and microphone or a smartphone with audio-visual capability is necessary.

To appear by video, use the following link: https://www.zoomgov.com/ Then enter the meeting ID and password. The applicable meeting ID and password can be found on the judge's page on the court's web site: https://www.ilnb.uscourts.gov.

To appear by telephone, call Zoom for Government at 1-669-254-5252 or 1-646-828-7666. The meeting ID and password will differ for each court call. The applicable meeting ID and password can be found on the judge's page on the court's web site: https://www.ilnb.uscourts.gov.

b. AT&T Teleconference. Attorneys and parties may connect through AT&T Teleconference only by telephone. To do so, dial the toll-free number and enter the access code followed by the pound (#) sign. The toll-free number and access code will differ for each judge and can be found on the judge's page on the court's web site: https://www.ilnb.uscourts.gov.

5. Protocols for electronic court appearances.

a. Your computer or telephone must be on "mute" except when your case is called.

b. Each time you speak, identify yourself for the record. Remember to speak slowly and distinctly. Do not interrupt others.

c. Do not use a speaker phone or call from a public place. Disruptions or background noise may cause the judge to mute you or terminate your participation.

d. No one except the assigned court reporter or another person that the court directs may record the audio or video.

e. Though held remotely by electronic means, each court call is a judicial proceeding. Formalities of a courtroom will be observed. Participants must conduct themselves in a suitable manner and if appearing by video must dress appropriately.

6. Dates and times of individual judges' court calls. To avoid simultaneous electronic court calls, the judges will hear matters on the following schedule rather than as originally scheduled, noticed, or (unless otherwise indicated) shown on the court's web site. Attorneys must check the court's docket to ensure that a matter has not been rescheduled.

a. Outlying county court calls (Joliet, Kane County, Lake County): All outlying county court calls will be held on the same dates and at the same times as previously scheduled but will be held electronically.

b. Chapter 7 and Chapter 11 calls: Each judge's chapter 7 and chapter 11 call will be held on a single day as follows.

- Chief Judge Goldgar: Monday, original motions at 9:30 a.m., set matters at 10 a.m.
- Judge Baer: Wednesday, original motions at 1:00 p.m., set matters at 1:30 p.m.
- Judge Barnes: Monday, original motions at 1:00 p.m., set matters at 1:30 p.m.
- Judge Cassling: Tuesday, original motions at 9:30 a.m., set matters at 10:00 a.m.
- Judge Cleary: Wednesday, original motions at 10 a.m., set matters at 10:30 a.m.
- Judge Cox: Tuesday, original motions at 1:00 p.m., set matters at 1:30 p.m.
- Judge Doyle: Thursday, original motions at 10 a.m., set matters at 10:30 a.m.
- Judge Hunt: Thursday, all matters at 11 a.m.
- Judge Lynch: Wednesday, all matters at 11 a.m.

- Judge Schmetterer: Tuesday, original motions at 10 a.m., set matters at 10:30 a.m.

- Judge Thorne: Thursday, original motions at 9 a.m., set matters at 9:30 a.m.

c. Chapter 13 calls and Western Division Chapter 12 calls:

- Chief Judge Goldgar: Tuesday afternoon

  1:15 p.m. trustee motions
  1:30 p.m. original motions
  2:00 p.m. set matters
  2:30 p.m. confirmations

- Judge Barnes: Thursday afternoon

  1:00 p.m. trustee motions
  1:30 p.m. original motions
  2:00 p.m. set matters
  2:30 p.m. confirmations

- Judge Cassling: Thursday morning, at times currently shown on the court's web site

- Judge Cleary: Monday afternoon

  1:00 p.m. trustee motions
  1:30 p.m. original motions
  2:00 p.m. set matters
  2:30 p.m. confirmations

- Judge Cox: Monday morning, at times currently shown on the court's web site

- Judge Doyle: Tuesday morning, at times currently shown on the court's web site

- Judge Lynch: Thursday morning

  8:45 a.m. trustee motions
  9:00 a.m. original motions
  10:00 a.m. confirmations
  11:00 a.m. chapter 12 matters

- Judge Schmetterer: Wednesday morning, at times currently shown on the court's web site

• Judge Thorne: Wednesday afternoon

1:00 p.m. trustee motions
1:30 p.m. original motions
2:00 p.m. set matters
2:30 p.m. confirmations

7. **Motions; Objection procedure; Service.** The following procedures apply to all motions noticed for presentment on or after October 13, 2020.

a. Every motion must be filed using the applicable attached Notice of Motion form. If a motion noticed for presentment on or after October 13, 2020, has already been filed, the movant must file and serve an amended notice of motion using the applicable Notice of Motion form.

b. A party who objects to a motion and wants it called must file a Notice of Objection no later than two (2) business days before the presentment date.

c. A Notice of Objection need only say that the respondent objects to the motion. No reasons need be given for the objection.[1/]

d. If a Notice of Objection is timely filed, the motion will be called on the presentment date.

e. If no Notice of Objection is timely filed, the court may grant the motion without a hearing before the date of presentment.

f. Local Rule 9013-1(D) governing service of motions is suspended in part. All motions must be served at least seven (7) days before the date of presentment, regardless of the method of service.

1/ For example, a trustee's objection to a chapter 13 debtor's motion to modify the plan post-confirmation need only say: "The trustee objects to the motion to modify the plan."

g. Any matter not subject to a deadline in the Bankruptcy Code or Bankruptcy Rules may be continued to another date by agreement of the parties. To obtain a continuance, the parties should contact chambers.

8. Trials and evidentiary hearings. All trials and evidentiary hearings will be held by video using the Zoom for Government platform. No trials and evidentiary hearings will be held in the courthouse. *See* General Order No. 20-05.

9. Original Non-Attorney Signatures. Section II.C.1 of the Administrative Procedures for the Case Management/Electronic Case Filing System is suspended. Electronic signatures using a method like DocuSign will be accepted.

10. Deadlines in Bankruptcy Code and Bankruptcy Rules unchanged. Nothing in this order alters in any respect deadlines under the Bankruptcy Code or Bankruptcy Rules.

11. Authority of judges to enter orders unaffected. This order does not affect the authority of judges to enter orders in any bankruptcy case or proceeding.

12. Local Rules remain in effect. Except as provided in this order, the Local Rules of the Bankruptcy Court and the court's Administrative Procedures for the Case Management/ Electronic Case Filing System remain in effect, including Local Rule 9013-2 concerning emergency motions.

13. Effective date; Superseding effect of this order. This order is effective October 13, 2020. On the effective date, this order supersedes all other orders and all notices from individual judges concerning court proceedings during the current emergency.

Dated: September 28, 2020

ENTERED FOR THE COURT:

A. Benjamin Goldgar
Chief Judge

1. Notice of Motion form for Zoom for Government

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

[caption]

NOTICE OF MOTION

TO: See attached list

PLEASE TAKE NOTICE that on _____, 20__, at _____ a.m./p.m., I will appear before the Honorable _____, or any judge sitting in that judge's place, and present the motion of _____ [to/ for] _____, a copy of which is attached.

This motion will be presented and heard electronically using Zoom for Government. No personal appearance in court is necessary or permitted. To appear and be heard on the motion, you must do the following:

To appear by video, use this link: https://www.zoomgov.com/. Then enter the meeting ID and password.

To appear by telephone, call Zoom for Government at 1-669-254-5252 or 1-646-828-7666. Then enter the meeting ID and password.

Meeting ID and password. The meeting ID for this hearing is _____ and the password is _____. The meeting ID and password can also be found on the judge's page on the court's web site.

If you object to this motion and want it called on the presentment date above, you must file a Notice of Objection no later than two (2) business days before that date. If a Notice of Objection is timely filed, the motion will be called on the presentment date. If no Notice of Objection is timely filed, the court may grant the motion in advance without a hearing.

[Name of movant]
By: _____

[Name, address, telephone number,
and email address of counsel]

CERTIFICATE OF SERVICE

I, _____, certify [if an attorney]/declare under penalty of perjury under the laws of the United States of America [if a non-attorney] that I served a copy of this notice and the attached motion on each entity shown on the attached list at the address shown and by the method indicated on the list on _____, 20__, at _____ a.m./p.m.

2. Notice of Motion form for AT&T Teleconference

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

[caption]

NOTICE OF MOTION

TO: See attached list

PLEASE TAKE NOTICE that on _____, 20__, at _____ a.m./p.m., I will appear before the Honorable _____, or any judge sitting in that judge's place, and present the motion of _____ [to/ for] _____, a copy of which is attached.

This motion will be presented and heard electronically using AT&T Teleconference. No personal appearance in court is necessary or permitted. To appear and be heard on the motion, you must call this toll-free number: _____. Then enter access code _____ followed by the pound (#) sign.

If you object to this motion and want it called on the presentment date above, you must file a Notice of Objection no later than two (2) business days before that date. If a Notice of Objection is timely filed, the motion will be called on the presentment date. If no Notice of Objection is timely filed, the court may grant the motion in advance without a hearing.

[Name of movant]
By: _____

[Name, address, telephone number,
and email address of counsel]

CERTIFICATE OF SERVICE

I, _____, certify [if an attorney]/declare under penalty of perjury under the laws of the United States of America [if a non-attorney] that I served a copy of this notice and the attached motion on each entity shown on the attached list at the address shown and by the method indicated on the list on _____, 20__, at _____ a.m./p.m.

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF OHIO

In re:

ORDER REGARDING VIRTUAL HEARINGS

General Order No. 44-1

The Court issues this General Order in response to the COVID-19 public health emergency and the continuing recommendations from the Centers for Disease Control and Prevention, the Ohio Department of Health, and the Administrative Office of the United States Courts to exercise caution during the pandemic. With General Order 35-1 and its subsequent amendments, the Court has adopted procedures to conduct non-evidentiary hearings telephonically. This General Order is intended to supplement General Order 35 and to provide notice of the general requirements and expectations for all virtual hearings in the Bankruptcy Court for the Southern District of Ohio.

Carefully monitor the presiding judge's individual page on the Court's website (https://www.ohsb.uscourts.gov/) to be aware of his or her specific procedures.

The following is applicable to all virtual hearings:

1. **Platforms**

   a. The presiding judge maintains the discretion to conduct any hearing—whether evidentiary or non-evidentiary—telephonically, through videoconferencing technology, or using a combination of both (all a "Virtual Hearing").

   b. For any Virtual Hearing, the presiding judge reserves the right to choose the platform employed for audio (the "Audio Platform") (e.g., AT&T conference line, CourtCall, CourtSolutions) and/or video (the "Video Platform") (e.g., Skype, Zoom for Government, Microsoft Teams, GoToMeeting).

2. **Required Equipment**

   a. For any Virtual Hearing using an Audio Platform, each attorney and each Remote Witness (defined below) must have access to a telephone. If possible, parties appearing telephonically should use a landline rather than a cell phone. If a cell phone is used, parties shall ensure that they have a strong cellular phone system or use the Wi-Fi calling option on their phones. Parties shall not use cell phones while in public spaces or while driving or riding in an automobile.

(44-1)

b. For any Virtual Hearing using a Video Platform, each attorney and each Remote Witness must have access to a computer, tablet, phone, or other device equipped with (i) a camera, (ii) an internet connection sufficient to support the applicable Video Platform, and (iii) a microphone. In lieu of a microphone, many Video Platforms also have the option of using a telephone for audio.

c. For any Virtual Hearing, each attorney and Remote Witness must be able to access exhibits in Portable Document Format ("PDF") through the use of a PDF reader (e.g., Adobe Acrobat Reader, Apple Books). If a Remote Witness does not have access to a program for viewing PDF files, the party sponsoring the Remote Witness shall ensure the Remote Witness has a printed copy of all exhibits.

3. Exhibits and Testimony

a. In advance of any Virtual Hearing, parties will be expected to provide to each other and to the Court electronic copies of exhibits in PDF format. A party's exhibits should be combined into a single PDF file and each individual exhibit should be labeled and, to the extent possible, bookmarked to ensure easy navigation.

   i. Some judges may require that exhibits be filed on the docket; others may require that exhibits be emailed. Parties should familiarize themselves with the presiding judge's policies and procedures on the provision of exhibits.

b. In accordance with Federal Rule of Civil Procedure 43(a) (made applicable by Federal Rule of Bankruptcy Procedure 9017), for good cause and in compelling circumstances a witness may be permitted to testify by contemporaneous transmission from a location other than the courtroom. Based on the foregoing, unless ordered otherwise in a particular case, any witness called to testify or subject to cross-examination in relation to a Virtual Hearing shall be permitted to testify by contemporaneous transmission from a different location ("Remote Witness").

c. All Remote Witnesses shall be sworn in virtually by the presiding judge or other court employee, and such testimony will have the same effect as if such Remote Witness was sworn in person in open court at the courthouse.

d. As an additional safeguard for the allowance of a Remote Witness, the presiding judge may require the Remote Witness or the party sponsoring the Remote Witness to provide certain information. The Remote Witness and/or the sponsoring party should be prepared to provide the information such as: (i) the location of the Remote Witness (city, state, country); (ii) the place from which the Remote Witness will testify (e.g., home, office); (iii) whether anyone is or will be in the room with the Remote Witness during the testimony, and if so, who and for what purpose; and (iv) whether the Remote Witness will have access to any documents other than exhibits provided to the Court and the parties, and if so, what documents.

e. The party sponsoring a Remote Witness shall be responsible for ensuring that any applicable dial-in information, any applicable link for the Video Platform, and all exhibits are supplied to the Remote Witness before the Virtual Hearing.

4. **Recordings**

   a. Other than official court reporters and official electronic recorders employed by the Court, no party shall be permitted to record any Virtual Hearing. Local Bankruptcy Rule 5073-1, which prohibits the use of cameras or other recording devices where judicial proceedings are being conducted, applies to Virtual Hearings.

5. **General Recommendations**

   a. Parties should carefully review the presiding judge's webpage and any scheduling orders or other orders entered in the particular case for specific policies and procedures. After such review, parties may contact the presiding judge's courtroom deputy with any procedural questions or concerns.

   b. Parties should carefully monitor their email in advance of hearings to ensure receipt of any necessary instructions, dial-in information, or links for Video Platforms.

   c. Parties should mute their phones when not addressing the Court to prevent background noise, which is distracting to participants and interferes with the record.

   d. Parties should, where possible, avoid speaker phone, Bluetooth, and other hands-free features when addressing the Court, as these features can cause interference.

   e. Successful Virtual Hearings require the cooperation of all participants. Parties should continue to exercise patience and care in the course of their participation in Virtual Hearings to maximize the swift and orderly administration of justice during this public health emergency. To that end, every party should: (i) wait until called upon to speak; (ii) announce his or her name for the record each time the party speaks; (iii) make an effort to speak slowly, clearly, and concisely; and (iv) pause before speaking and avoid speaking over or interrupting other parties and the Court.

IT IS SO ORDERED.

Dated: August 21, 2020

FOR THE COURT

Chief Judge Jeffery P. Hopkins
United States Bankruptcy Court
Southern District of Ohio

IT IS SO ORDERED.

Dated: April 11, 2020

John E. Hoffman, Jr.
United States Bankruptcy Judge

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF OHIO
WESTERN DIVISION

In re:	)	Chapter 11
MURRAY METALLURGICAL COAL HOLDINGS, LLC, *et al.*,[1]	)	Case No. 20-10390 (JEH)
	)	Judge John E. Hoffman, Jr.
Debtors.	)	(Jointly Administered)

AGREED ORDER ESTABLISHING PROCEDURES FOR TELEPHONIC AND/OR VIRTUAL HEARING SCHEDULED FOR APRIL 14, 2020, AS A RESULT OF THE COVID-19 PANDEMIC [RELATED TO DOCKET NO. 361]

The above-captioned debtors and debtors in possession (collectively, the "Debtors"), the Official Committee of Unsecured Creditors (the "UCC"), the Ad Hoc Group of Prepetition Term Loan Lenders (the "Ad Hoc Group"), Murray Energy Holdings Co. and its affiliated debtors (the "Murray Energy Debtors", and collectively with the Debtors, the UCC, the Ad Hoc Group, the

[1] The Debtors in these Chapter 11 cases, along with the last four (4) digits of each Debtor's federal tax identification number, if applicable, are: Murray Metallurgical Coal Holdings, LLC (4633); Murray Eagle Mining, LLC (4268); Murray Alabama Minerals, LLC (4047); Murray Alabama Coal, LLC (3838); Murray Maple Eagle Coal, LLC (4435); and Murray Oak Grove Coal, LLC (4878). The Debtors' primary business address is 46226 National Road, St. Clairsville, OH 43950.

Murray Energy Debtors, the "Parties", or, each individually, a "Party"), each by and through counsel, having agreed that pursuant to Federal Rule of Civil Procedure 43(a) (made applicable by Federal Rule of Bankruptcy Procedure 9017), the current COVID-19 pandemic provides for good cause and constitutes compelling circumstances, and as a result thereof, the Parties having further agreed to certain telephonic and virtual hearing procedures which shall provide appropriate safeguards in relation to the hearing on the *Motion of the Official Committee of Unsecured Creditors for Entry of an Order Granting it Standing and Authorizing it to Prosecute and Settle Certain Claims on Behalf of the Debtors' Estates* [Docket No. 361] (the "UCC Standing Motion"), and the Court having reviewed the record and being fully advised,

IT IS HEREBY AGREED AND ORDERED that:

1. **Telephonic and Video Conferencing Solutions**. The hearing scheduled for Tuesday, April 14, 2020 at 10:00 a.m. prevailing Eastern Time shall take place virtually. The Court will be utilizing both CourtSolutions (for audio purposes) and Skype (for video purposes). CourtSolutions can be accessed by calling (917) 746-7476 or visiting the website www.court-solutions.com and the Skype link shall be provided to those Parties who have submitted a notice of intent to participate via Skype to the Court in accordance with Section 3 below. All counsel and witnesses shall conduct a pre-hearing test of Skype and, if possible, CourtSolutions, using the same equipment that they will be using during the hearing.

2. **Limit on Video Conferencing**. Due to video conferencing limitations, the optimal number of Skype participants is ten (10), as opposed to CourtSolutions, which allows for unlimited participants. In an effort not to overburden the Skype platform, video conference participants shall be limited to the witnesses, those parties that anticipate questioning or cross-examining witnesses and, when possible, should be limited to one attorney per firm. Parties

participating via Skype who wish to address a witness shall simultaneously be connected to CourtSolutions for audio purposes. Parties attending via Skype shall utilize the Skype link only during the matter for which they wish to be heard. Upon the conclusion of such matter, the party shall disconnect from the Skype link and may continue participation in the hearing through CourtSolutions. Similarly, witnesses shall utilize the Skype link only during the matters on which they are called to testify. Upon completion of their testimony and all cross-examination, the witness shall disconnect from the Skype link and may continue participation in the hearing through CourtSolutions. In order to limit the number of Skype participants to ten persons, if necessary, the Court will take a recess between matters in order to add or subtract individuals participating via Skype.

3. **Prior Notice of Intent to Skype**. All Parties wishing to attend the hearing via Skype shall provide notice to Hoffman282@ohsb.uscourts.gov via electronic mail no later than 4:00 p.m. prevailing Eastern Time on Saturday, April 11, 2020. The Court will circulate the Skype link to all Parties participating via Skype prior to the hearing.

4. **Submission of Exhibits to Court**. Parties submitting exhibits related to the UCC Standing Motion shall send all exhibits to Hoffman282@ohsb.uscourts.gov via electronic mail in .pdf format no later than 4:00 p.m. prevailing Eastern Time on Saturday, April 11, 2020. Such information shall be submitted to the Court separately from (and in addition to) the Exhibit Lists required to be filed with the court three-business days prior to the hearing pursuant to Section 52 of that certain *Supplemental Order Implementing Certain Notice and Case Management Procedures* [Docket No. 317] (the "Case Management Order").

5. **Form of Exhibits**. Each Party shall combine all of its exhibits into one .pdf document and each individual exhibit shall be bookmarked for easy review by the Court. All parties shall submit their exhibits to the Court separately.

6. **Filing and Service of Exhibits**. Parties submitting exhibits are excused from (i) filing exhibits on the court docket, and (ii) serving the exhibits on the Master Service List. Parties submitting exhibits need only email the exhibits to the other Parties to this Order and the Court.

7. **Remote Witness Testimony**. In accordance with Federal Rule of Civil Procedure 43(a) (made applicable by Federal Rule of Bankruptcy Procedure 9017), for good cause and in compelling circumstances a witness may be permitted to testify by contemporaneous transmission from a location other than the courtroom. Based on the foregoing, any witness called to testify or subject to cross-examination in relation to the UCC Standing Motion shall be permitted to testify by contemporaneous transmission from a different location ("Remote Witness").

8. **Requirements for Allowance of Remote Testimony; Additional Information**. As additional safeguards for the allowance of a Remote Witness, the Party sponsoring said Remote Witness shall file with the Court, no later than 4:00 p.m. prevailing Eastern Time on Saturday, April 11, 2020, a document containing the following information:

a. The name and title of the Remote Witness.

b. The matter on which the Remote Witness will provide testimony.

c. The location of the Remote Witness (city, state, country).

d. The place from which the Remote Witness will testify (e.g. home, office – ***no addresses are required***).

e. Whether anyone will be in the room with the Remote Witness during the testimony, and if so, who (name, title, relationship to the Remote Witness), and for what purpose.

f. Whether the Remote Witness will have access to any documents other than exhibits that have been emailed to the Court and the parties, and if so, what documents.

Such information may be filed with the Court separately from (or incorporated within) the Witness Lists required to be filed with the Court no later than 4:00 p.m. prevailing Eastern Time on Saturday, April 11, 2020.

9. **Swearing In of Remote Witnesses**. All Remote Witnesses shall be sworn in over the telephone, Skype, or other video conferencing solution, as applicable, and such testimony will have the same effect and be binding upon the Remote Witness in the same manner as if such Remote Witness was sworn in by the Court deputy in person in open court. To the extent there is an error or malfunction with Skype or other video conferencing solution, the Remote Witness may be sworn in and testify via telephone only.

10. **Responsibility for Remote Witnesses**. The Party sponsoring the witness shall be responsible for ensuring that the CourtSolutions dial-in, Skype link, and all exhibits are supplied to the Remote Witness prior to the hearing and that the Remote Witness has been registered with CourtSolutions and Skype, as applicable.

SO ORDERED.

Copies to Default List.

AGREED TO AND SUBMITTED BY:

/s/ *Thomas R. Allen*
Thomas R. Allen (0017513)
Richard K. Stovall (0029978)
James A. Coutinho (0082430)
Matthew M. Zofchak (0096279)
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- and -

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Counsel to the Debtors and Debtors in Possession

-and-

/s/ *Christopher W. Peer*
(*Per email authorization on April 11, 2020)*
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John A. Polinko (No. 0073967)
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(973) 597-2400 (Fax)

Proposed Counsel to the UCC

/s/ *Joseph C. Pickens*
(*Per email authorization on April 11, 2020)*
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Counsel to the Ad Hoc Group

-and-

/s/ *Kim Martin Lewis*
(Per email authorization on April 11, 2020)
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Counsel to the Murray Energy Debtors

UNITED STATES BANKRUPTCY COURT
CENTRAL DISTRICT OF ILLINOIS

In re:

CLAYTON HAMILTON WEISENBORN
BRENDA S. WEISENBORN
Debtor

Chapter 7

Case No. 20-80900

NOTICE OF VIDEO CONFERENCE FOR 341 MEETING OF CREDITORS AND PROCEDURES REGARDING SAME

PLEASE TAKE NOTICE that in addition to the telephonic 341 Meeting of Creditors provided for under 11 U.S.C. § 341 previously noticed for **November 20, 2020 at 1:00 p.m.** the Trustee has scheduled a video conference for participation in the Meeting of Creditors. Participation by video is **required** for the Debtors and is optional for any other parties.

PLEASE TAKE FURTHER NOTICE that to connect to the 341 Meeting of Creditors, at the time and date set for your meeting, follow the instructions below:

1. **From a telephone,** call the Trustee's telephonic conference line 877-396-3767
   Enter Passcode 4747452

To connect to the video conference:

2. **From a separate device (computer, laptop, ipad, another phone) connected to the Internet with a camera,** click:
   Join Zoom Meeting
   https://us02web.zoom.us/j/89050674712?pwd=akNaUFdlUnoydGZETmNFWm9RamN5dz09

   Meeting ID: 890 5067 4712
   Passcode: 101754

After you connect, you will be placed into the Trustee's waiting room, and be admitted to the video conference when your case is called. Please do not be late to your scheduled meeting time, or your case may be rescheduled.

PLEASE TAKE FURTHER NOTICE that a separate device connected to the internet with a camera, other than the telephone you are using to call into the conference, is necessary to be able to connect to the video conference. Only the audio of the 341 Meeting of Creditors will be electronically recorded. To ensure the quality of the record, please be sure to limit any background noise. Participants must be able to hear all parties for the entirety of the 341 Meeting of Creditors.

PLEASE TAKE FURTHER NOTICE that the Debtor(s) must timely submit to the Trustee documents requested at the Section 341 meeting of creditors on October 6, 2020 and any missing documents from the Trustee's standing Section 341 Meeting letter, a copy of which is available at: https://reinboldlawfirm.com/wp-content/uploads/2020/05/341requirements-5-1-20.pdf. Debtor(s)' counsel are required to use the Trustee's Document Delivery Portal for submitting identification documents and other required documents, unless alternate arrangements are made

PLEASE TAKE FURTHER NOTICE that failure to comply with the above procedures may be deemed a failure to appear at the 341 Meeting of Creditors, result in a continuance or a request for dismissal of the case.

/s/ Jeana K. Reinbold
Jeana K. Reinbold
Chapter 7 Trustee
P.O. Box 7315
Springfield, IL 62791
Telephone: (217) 241-5629
Email: trustee@jeanareinboldlaw.com

CC: Debtor's counsel of record and parties who have filed an electronic appearance in the case

INFORMATION FOR SECTION 341 MEETING OF CREDITORS CENTRAL AND SOUTHERN DISTRICTS OF ILLINOIS

Bankruptcy Code section 343 requires each debtor to appear and submit to examination under oath at the meeting of creditors convened pursuant to section 341(a). Because of developing issues with the COVID-19 virus and the national declaration of emergency by the President of the United States, meetings of creditors will be conducted by telephone conference call. The dial-in number and participant code for the telephone conference line appear on the notice of meeting of creditors. The conference line is only for meetings of creditors. The trustee's contact information is listed elsewhere on the notice.

Bankruptcy Information Sheet

Prior to the meeting, the debtor must read the Bankruptcy Information Sheet, provided by their attorney or available at https://www.justice.gov/ust/bankruptcy-information-sheet-0.

Identification Materials & Tax Return

At least seven days prior to the meeting, the debtor (through counsel) must provide the trustee with a copy of (1) the most recently filed federal income tax return or a transcript thereof; (2) government-issued photo ID; and (3) evidence of complete Social Security Number. Contact the trustee to obtain instructions for submitting these materials (collectively, the "Identification Documents"). Failure to timely submit these materials may result in the meeting being rescheduled or the case being dismissed.

Acceptable forms of picture identification (ID) include: driver's license, U.S. government ID, state ID, student ID, passport (or current visa, if not a U.S. citizen), military ID, resident alien card, and identity card issued by a national government authority. Acceptable forms of proof of social security number include: social security card, medical insurance card, pay stub, W-2 form, IRS Form 1099, and Social Security Administration (SSA) Statement.

Debtors and their counsel should be prepared to indicate on the record at the 341 meeting that the name and social security number on the documents filed in the bankruptcy case match the name and number on the Identification Documents provided to the trustee. Trustees will also take appropriate measures (1) to secure the Identification Documents, both to protect the debtors' privacy and to prevent their unauthorized disclosure, and (2) to destroy or return the Identification Documents when they are no longer needed.

Dial-In Instructions

(1) Type of Phone. You must use a touch-tone telephone to participate. If you have a choice, use a landline phone rather than a cell phone.

(2) Limit Distractions and Background Noise. Make the call from a quiet area where there is as little background noise as possible. Do not use a speaker phone.

(3) One Phone Per Caller. Persons attending the meeting from the same location (e.g., joint debtors) should each use a separate touch-tone telephone to participate.

(4) Call at Appointed Time. Dial the telephone conference line number and then enter the participant code (7 numerals followed by a # sign). Do not call in advance; call at your appointed meeting time. Once connected, place your phone on mute, remain on the line, and wait until your case is called prior to speaking, as another meeting may be underway.

(5) Connection. Do not put the call on hold at any time after the call is connected. If your call is disconnected before the meeting is completed, you must immediately call back.

(6) Tardiness. Meetings are scheduled either individually or in small blocks. Trustees will commence and end meetings as scheduled. If the debtor is tardy, the trustee may assign a call back time later that day or reschedule the meeting to another date.

Conference Call Instructions

(1) Listen for Call of Case. At the appointed time, the trustee will announce the case name and number. When your case is called, unmute your phone and identify yourself.

(2) Each Debtor Must Testify. For joint cases, each debtor must clearly and audibly answer every question.

(3) Recording. The trustee or United States Trustee will electronically record the meeting. Other recordings are prohibited. Debtors and other parties must speak clearly and loudly to ensure a clear record.

(4) Bankruptcy Papers. Debtors must have their bankruptcy papers (including the petition, schedules, statement of financial affairs, means test, and tax returns, as well as any document the trustee has indicated in advance that the debtors should have) available to review and respond to questions.

(5) Additional Time. Trustees will commence and end meetings as scheduled. If additional time is needed, the trustee may assign a call back time later that day or continue the meeting to another date.

(6) Terminating the Call. Please hang up promptly at the end of your meeting.

Special Services

(1) Foreign Language Interpretation. The United States Trustee Program provides telephonic foreign language interpreter services for participation at section 341 meetings by debtors and creditors. Although the provider does not require prior notice, it will be helpful to alert the trustee prior to the meeting. There is no charge for this service.

(2) Assistance for Hearing Impaired Parties. The United States Trustee Program offers the services of a sign language interpreter for debtors and creditors at meetings of creditors. Prior notice is required to enable the United States Trustee to make necessary arrangements. Under the current circumstances, the meeting may be rescheduled until appropriate arrangements can be made. There is no charge for this service.

SCOTT LIESKE, CHAPTER 13 TRUSTEE
MEETINGS OF CREDITORS
VIDEO PROTOCOL

Given recent health concerns, my office will be conducting Meetings of Creditors via videoconference (Zoom.us) until further notice. The audio of the Meetings will be recorded and the audio recordings will be available from the US Trustee.

Debtors and their attorneys do not have to be in the same location as long as each of them has access to the Zoom videoconference portal (can be accessed via a free app on a smartphone/tablet or on a PC with video/microphone). A video appearance via the Zoom portal is preferable. However, if a debtor is unable to appear via the Zoom videoconference portal, they can appear telephonically by following the instructions on the Notice of 11 U.S.C. § 341(a) Meeting To Be Held By Telephone that was mailed to them by the Bankruptcy Court.

1. Approximately one-week prior to the scheduled meeting, my office will send an email to the debtor's attorney with a link to the Meeting ID. The attorney will be responsible for forwarding this information to the debtor(s).

2. The debtor(s) will need to download the free ZOOM Cloud Meetings app to their smartphone/tablet from the Apple App Store or Google Play Store and set-up their free account.

    a. Once the app is downloaded, click the 'Sign Up' button
    b. Enter your Email Address, First Name, and Last Name; click the button agreeing to the Terms of Service; and then click the 'Sign Up' button in the upper right corner
    c. A pop-up box will inform you that a confirmation email has been sent to the Email Address that you have provided; Click 'OK'
    d. Go to your email inbox and check for the activation email from Zoom and click on the 'Activate Account' button in the email (if you have not received the activation email, check your Spam folder)
    e. You will be directed to the Zoom website to create a password; enter a password and confirm the password and then click the 'Continue' button
    f. Return to the Zoom app on your phone and click the 'Sign In' button
    g. Enter your Email Address and the Password you just created
    h. Test the connection by clicking the 'Join' button at the top of the screen; Enter the Meeting ID provided in Step 1 and click the 'Join' button (Note: you MUST make sure the Personal Link Name is your full First & Last name so the Trustee can identify the participant)
    i. If everything was set up correctly, the next screen should show the Meeting ID, the Time and Date of the scheduled Meeting of Creditors (the time shown will be the 8:30am morning start time for the entire day regardless of what time the debtor's actual meeting is scheduled for); you should also see a spinning wheel notifying you that the app is waiting for

the host to start the meeting (now that you have successfully tested your connection and confirmed the Meeting information, you may click the 'Leave' button in the upper right corner of the screen)

Note: This process is relatively simple, but can take a little bit of time so debtors should NOT wait until the day of their hearing to complete this step. The Trustee requests that attorneys test the Zoom video connection with their clients prior to the Meeting of Creditors.

3. Approximately 10 minutes prior to the scheduled start of the Meeting, the debtor should extract their Picture ID and Social Security verification from their wallets/purses and find a private distraction-free location with good Wi-Fi or a strong cellular signal to participate in the videoconference Meeting.

4. Approximately 5 minutes prior to the scheduled start of the Meeting, the debtor should log in to the Zoom app.
   a. Return to the Zoom app on your phone and click the 'Sign In' button
   b. Enter your login Email Address and Password
   c. Click the 'Join' button at the top of the screen; Enter the Meeting ID provided in Step 1 and click the 'Join' button (Note: you MUST make sure the Personal Link Name is your full First & Last name so the Trustee can identify the participant; if the Trustee cannot identify you, you may not be admitted to the Meeting)
   d. A Video Preview window will open on your phone; click the blue 'Join with Video' button and you will receive a message indicating that the meeting host will let you in soon (there are 4 cases scheduled in each half-hour block, so you could be the first case called right away or you could be the 2nd, 3rd, or 4th case called; be patient)
   e. Once the Host (Trustee) is ready for your case and admits you into the Meeting, you will receive a pop-up message instructing you to join the audio in order to hear the other participants; click the 'Call using Internet Audio' button (you must click this button in order for the other meeting participants to hear you)

5. The Trustee will swear you in and conduct the Meeting of Creditors. You will be asked to hold up your Picture ID and Social Security verification in front of your camera phone so the Trustee can verify your identity.

6. Once the Host (Trustee) has disconnected you from the Meeting, you may close the app. Your attorney will contact you if there any further instructions.

Updated 4/2/20

9/11/2020

Judge Baer's Zoom Trial Rules and Tips

General Matters

1. "Listening in" on the proceedings. The trial is a "public proceeding." Thus, any party interested in the case may "listen in" to the Zoom trial. Parties to the case may share the Zoom ID and passcode with interested parties who wish to "listen in." The information will also be posted on the Court Calendar which is located on Judge Baer's website. Parties who "listen in" must have their cameras off and their microphones muted at all times.

2. Video/audio on. Only parties who are expected to call witnesses or pose objections at the trial and the witnesses who are testifying should have their cameras and microphones turned on during the trial. All others should turn their cameras off and mute their microphones. The video feed will show only the parties who will actually be participating—the Judge, the witness, the lawyer asking the questions, and any parties entitled to object. Other attorneys assisting in the case must have their cameras off and their microphones muted.

3. Slow down and do not interrupt. It is vital that everyone slow down when speaking and not interrupt each other. This is even more key now than when proceedings are held in the courtroom. Generally, when two people speak at the same time, nothing is heard from either. Thus, anything that is said will have to be repeated, making the trial even longer.

4. Regular breaks. If people want to take breaks during the trial, they should just ask for a break or raise their hand if someone else is speaking. If it is just a simple break, participants should turn off their video and audio during the break and then turn them back on when the trial commences again.

5. Breakout rooms. If any party wants to be placed in a breakout room so that he or she may speak separately to another participant, the party should ask the Court, and, if appropriate, the courtroom deputy will arrange for the breakout and place the parties in the correct breakout room. Breakout rooms will be set up in advance for the plaintiff and the defendant. Court personnel will also have a chambers breakout room.

6. Technical information. The Court must be provided with a list of cell phone numbers of all parties expected to participate in the trial and descriptions of the types of technology (e.g., Mac, PC, I-pad) that each party will be using at trial. Such a list will allow Court personnel to immediately contact and provide appropriate technical assistance to any party experiencing technical issues during the trial.

7. Courtroom behavior. Although this will be a virtual trial, parties are expected to conduct themselves in the same way that they would if we were in person in the courtroom. This includes appropriate formality and attire. While I love cats and babies, please try to avoid their participation in the trial if at all possible. In addition, if you are having trouble with the video or audio or other technical difficulties, please speak up immediately. Though glitches are expected,

they do not always occur on the Court's end, so we will not necessarily know if your Internet goes down until you tell us.

8. Photos/recordings. No photographs or recordings of the proceedings are permitted. You may have your cell phones or similar devices with you during the trial, but they must be muted, and you may not use them to take photographs or record any part of the proceedings. A court reporter will be present, and she will be preparing the only official record of the proceedings. While the Zoom bot will be engaged as a backup for the court reporter, you will not be provided access to that recording.

Witnesses

9. Witness protocol. When a party is called to testify, the witness must generally be in a room by himself or herself with no papers in front of the witness other than the filed exhibits. The witness will be sworn in by the courtroom deputy via Zoom video and audio. Then, while under oath, the witness will be asked to testify as to where the witness is located, who is in the room with the witness, and whether the witness has any papers in front of him or her. The witness will also be asked to tell the Court if, at any time, someone who was not initially there enters the room. If witnesses wish to have counsel with them in person, that fact must be disclosed to the Court, and the parties must maintain social distance in the room.

10. Violation of witness rules. If, during the course of a witness's testimony or otherwise, it is discovered that (a) the witness is being coached or otherwise communicated to, (b) there is an undisclosed person in the room with the witness, or (c) the witness has notes in front of him or her that have not been disclosed, the Court may disqualify the witness from testifying, enter sanctions, or take other appropriate action within the Court's discretion.

11. Excluding witnesses. At the start of the trial, the parties must inform the Court if they wish to have testifying witnesses excluded from the courtroom. If so, the Court will decide whether the request is appropriate pursuant to the applicable federal rules. Either excluded witnesses will be placed in a Zoom waiting room until it is time for them to testify, or they should be directed not to dial in to the Zoom trial until they are expected to testify.

12. Objections. If parties wish to object to questions during examination, they should simply state "objection" orally and physically raise their hand. When the word "objection" is stated and/or the hand is raised, all parties must stop talking. At that point, the Court will invite the objecting party to state the legal basis for his or her objection; may, at its discretion, solicit a response from the other party; and then rule.

13. Sidebar. If a lawyer needs a sidebar with the Court and opposing counsel during a witness's testimony, the lawyer should just ask. We can arrange for the witness to be placed in the waiting room while the sidebar takes place.

Exhibits

14. Filing and sharing exhibits. Exhibits must all be filed on the Court's docket. The courtroom deputy will serve as host for the trial and thus be the only person who has the right to

"screen share." If a party wishes to have an exhibit shared on the screen, the deputy will be the one who will retrieve the document from the docket and share the document with the trial participants. Exhibits must be marked with page numbers that will allow the deputy to readily and quickly find the appropriate pages in each exhibit.

15. Hardcopy exhibits. In addition to filing exhibits electronically, the parties may provide hard copies of the exhibits to each other and the witnesses. One full hardcopy set of the exhibits must be delivered to the Judge via the Bankruptcy Court mailroom, 219 S. Dearborn Street, Room 717, on the date required in the Court's pretrial order.

16. Confidential exhibits. If the parties designate as exhibits documents that are marked as confidential, a redacted set of the confidential documents should be filed on the public docket, and a separate, unredacted version of the documents should be filed under seal with the Court pursuant to Local Rule 5005-4. The courtroom deputy will be directed to "screen share" only the redacted version of confidential exhibits. The Court does not need hard copies of the redacted exhibits. In the hardcopy set of exhibits to be delivered to the Court, the confidential documents should be provided in separate sealed envelopes marked as confidential. Whenever witnesses are expected to testify on the record about confidential information, counsel must provide advanced notice so that the Court can determine whether arrangements need to be made to protect that information from anyone listening in during the trial.

17. Impeachment/rebuttal documents. If a lawyer wants to use a document that is not a marked exhibit for impeachment or rebuttal, he or she must send the relevant document via email to the courtroom deputy who will then share the document on the screen as directed by the lawyer.

18. Deposition transcripts. If a lawyer anticipates using a deposition transcript for impeachment, he or she may either designate the transcript as an exhibit and file it with the other exhibits ahead of the trial or have the transcript downloaded and readily available to provide to the courtroom deputy to be shared during the trial.

Judge Cassling's Zoom Rules and Tips

1. These rules and tips apply to all court proceedings, including the motion calls. There are additional procedures and rules which must be followed for Zoom trials. Those procedures and rules are contained in the pretrial order which will be issued approximately a week before the trial is scheduled to start. They can also be found on the Court's website.

2. Ability of the public to observe the proceedings. A court hearing/trial is a public proceeding. Thus, any party interested in the case may attend or observe the Zoom hearing. Parties to the case may share the Zoom ID and passcode with any interested persons who wish to listen in. The information will also be posted on the Court Calendar which is located on Judge Cassling's website. Persons who are only observing must turn their cameras and microphones off at all times.

3. Use of video/audio. Turn your video/audio on only if you are participating in the hearing at issue. Only attorneys who are appearing in order to represent parties, pro se parties, and witnesses who are testifying may turn on their cameras and microphones during a court hearing. The video feed will display only the parties who will actually be participating—the Judge, the witness, the lawyer asking the questions, and any parties entitled to appear or object. Other attorneys assisting in the case must have their cameras off and their microphones muted.

4. Use of headsets. We strongly recommend that you use a headset or earbuds *with a microphone* for all Zoom hearings. Using a separate headset microphone instead of a built-in computer microphone reduces distortion, eliminates background noise, and ensures that

everything you say will be picked up. The result will be a more accurate record of the proceeding.

5. Avoid cross-talk where possible. Slow down and do not interrupt. It is vital that everyone slow down when speaking and not interrupt each other. Cross-talk will prevent the Court from understanding what is being said and will prevent the Court Reporter from making an accurate transcript. If repeated, willful, violations of this rule occur, the Court may sanction the offending party.

6. Early opening of the virtual courtroom. Zoom meeting rooms will be opened to the public thirty minutes prior to the scheduled court hearing. Attorneys may use the virtual courtroom during this time to conduct business (i.e, discussion with the trustee's office or opposing counsel) just as they would if appearing in person. Parties engaged in such discussions should be aware that, as soon as the court reporter enters a meeting room, the audio will be recorded.

7. Courtroom dress and decorum. You are reminded that, even though your matter will be heard in a virtual courtroom, parties and their attorneys are expected to conduct themselves with the same formality and decorum as they would if the matter were being heard in the Court's regular courtroom. This requirement includes the obligation, particularly for attorneys, to dress with the same formality and attire as they would if the proceedings were conducted in the Court's regular courtroom. If you are having trouble with the video or audio or other technical difficulties, please speak up immediately if possible. Otherwise, contact the courtroom deputy by email or

phone as soon as possible. Though glitches are expected, they do not always occur on the Court's end, so we will not necessarily know if your Internet goes down unless you tell us.

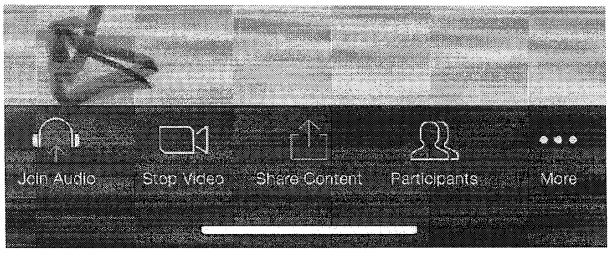
8. Photos/recordings. No photographs or recordings of the proceedings are permitted. During your presentation or testimony, cell phones must be turned off. More specific rules governing witnesses' access to cellphones during their testimony may be found in the Court's pretrial order for Zoom trials. The court reporter who is present for the hearing will be preparing the only official record of the proceedings.

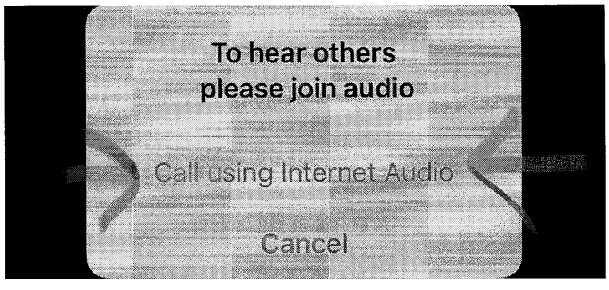
9. Breaks during the course of a trial. If people want to take breaks during the trial, they should just ask for a break or raise their hand if someone else is speaking. If it is just a simple break, participants should turn off their video and audio during the break and then turn them back on when the trial commences again.

10. Breakout rooms for trials. If any party wants to be placed in a breakout room so that he or she may speak separately to another participant, the party should ask the Court, and, if appropriate, the courtroom deputy will arrange for the breakout and place the parties in the correct breakout room. For scheduled trials, breakout rooms will be set up in advance for the participating parties. Court personnel will also have a chambers breakout room.

ZOOM GUIDE

1. Download the app to your smartphone or tablet
2. Set up an account using your FULL name
3. Click "JOIN"
4. Enter the Meeting ID and verify your full name is used
5. When you enter the meeting, you will be placed in a waiting room. Your screen will say "Please wait" until the Trustee is ready for you. There are 4 hearings every 30 minutes so your meeting may not start immediately!
    a. For example, if you have a 9:00 AM hearing, the Trustee will call your case sometime between 9:00 AM and 9:30 AM. Please wait by your phone.
6. Your meeting will have 4 people in it that Trustee will admit in from the waiting room: You, the Trustee, our attorney, and the Trustee's assistant.
7. When admitted to the meeting, turn on your audio and your video right away!!





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By Hon. Mark X. Mullin and Michael Berthiaume

Virtual Hearings Might Be New, but Your Evidence Must Still Be Correct

Editor's Note: *To stay up to date on the COVID-19 pandemic, be sure to bookmark ABI's Coronavirus Resources for Bankruptcy Professionals website (abi.org/covid19).*

Hon. Mark X. Mullin
U.S. Bankruptcy Court (N.D. Tex.); Fort Worth

Michael Berthiaume
U.S. Bankruptcy Court (N.D. Tex.); Fort Worth

Hon. Mark Mullin is a bankruptcy judge with the U.S. Bankruptcy Court for the Northern District of Texas in Fort Worth. Michael Berthiaume is a term clerk to Judge Mullin.

COVID-19 has forced a rethinking in the way we conduct business, and those in the bankruptcy world are no exception. We are doing our best to respect social-distancing protocols while trying to keep our cases moving forward. Just as attorneys and other professionals are discovering new ways to work effectively in a virtual world, judges, law clerks and clerks' office personnel are also implementing creative new rules and procedures to ensure that cases proceed in a virtual setting.

But to say that things feel different via WebEx or Zoom would be an understatement, and several aspects of these new virtual courtrooms have taken some "getting used to." Foremost in the struggles to adapt has been the virtual presentation of tangible evidence. Most judges understand that, by its very nature, appearing in a virtual courtroom feels more relaxed and less formal than appearing in a traditional courtroom. However, while the "feel" of the hearings and trials might seem more relaxed, the evidentiary requirements and the Federal Rules of Evidence (FRE) are not so forgiving.

Counsel must be prepared for the unique challenge of satisfying their evidentiary burden in a virtual courtroom, notwithstanding being separated from witnesses and the court by, at times, thousands of miles. Counsel must remember: It is your job to ensure the record contains the admissible evidence required to satisfy your clients' burden of proof. Although this article will only scratch the surface of unique evidentiary issues that may arise in virtual courtrooms, the following are a few tips to consider prior to trial and certainly before the court says, "Counsel, you may call your first witness."

Review and Comply with the Court's Local Rules, and Know Your Judge

Courts and judges across the nation have been quickly (sometimes hurriedly) implementing new, creative local rules and procedures to facilitate the virtual courtroom experience. Therefore, it is imperative that counsel review and comply with the court's latest virtual courtroom rules, procedures and technology requirements. A word of advice: Do not be shy. Feel free to contact the clerk's office or the judge's courtroom deputy to confirm that you have the latest policies to ensure a smooth evidentiary presentation on game day.

Witnesses: An Exposé of the Technologically Challenged

There is no way around it: Presentation of witnesses in a virtual courtroom is challenging,[1] and preparing a witness to testify virtually requires more thought, attention and preparation than it does in person. To reiterate the first point, be aware that several courts have identified specific procedures for the allowance of remote testimony, such as disclosure of a witness and its location, whether anyone will be in the room with a witness, and whether a witness will have access to any documents.[2] Again, knowing the local rules and procedures is paramount. Here are some witness-related considerations to consider.

Impress Upon Your Witness the Formality of the Proceeding

There is no need to belabor that attorneys should treat virtual court proceedings with the same formalities of a traditional courtroom. By now, most have experienced attorneys appearing in casual wear (to put it kindly), and we still do not know the culprit behind the now-infamous U.S. Supreme Court toilet flush.[3]

However, suffice it to say, witnesses are often even less formal. While our new virtual format is unavoidably less formal than a trip to your local WPA-era federal courthouse, counsel should impress upon his/her witnesses the inherent formalities of appearing in federal court. If the witness would have worn a suit and sat at the witness stand to testify in a traditional courtroom, why would tes-

1 "At trial, the witnesses' testimony must be taken in open court.... For good cause in compelling circumstances and with appropriate safeguards, the court may permit testimony in open court by contemporaneous transmission from a different location." Fed. R. Civ. P. 43(a). Courts in the federal judiciary have expressly approved the use of video and teleconferencing due to the pandemic. *See* "Judiciary Authorizes Video/Audio Access During COVID-19 Pandemic," U.S. Courts (March 31, 2020), *available at* uscourts.gov/news/2020/03/31/judiciary-authorizes-videoaudio-access-during-covid-19-pandemic (unless otherwise specified, all links in this article were last visited on Sept. 22, 2020).

2 *In re Rubie's Costume Co. Inc.*, No. 20-71970 (AST) (Bankr. E.D.N.Y. June 8, 2020), Order Setting Evidentiary Hearing by Videoconference and Establishing Related Deadlines, Case No. 20-71970, ECF No. 109, at 4.

3 Ariane de Vogue, "Supreme Embarrassment: The Flush Heard Around the Country," CNN (May 6, 2020), *available at* cnn.com/2020/05/06/politics/toilet-flush-supreme-court-oral-arguments.

tifying in a fishing shirt while riding (hopefully not driving)[4] in a car be acceptable? Always remember that even in a virtual courtroom, your witness's presentation and credibility might be a critical component to your client's case.

Test Your Witness's Technology Before Game Time

By now, many attorneys and other professionals have had sufficient experience honing their virtual presentation skills, but for many witnesses, this might be their first foray into testifying or participating in a virtual courtroom. Technical glitches happen, and most judges are patient souls who will allow the parties every opportunity to fix the glitch, but in some instances, the "fix" never comes. When that happens, the hearing might be continued, or worse, your client might not be able to testify, which could be devastating to your client's case.[5] Before the hearing, conduct a dry run with the witness to ensure that his/her internet connects properly, that his/her computer has the capability of running videoconferencing (this means having a computer with a camera), and that your witness chooses a place at home, the office or wherever with sufficient lighting and as few distractions as possible. The key is to enhance the witness's effectiveness and to improve the judge's ability to hear and properly assess the witness's testimony and credibility.

Invoking "the Rule": FRE 615[6]

Another witness issue that might sneak up on the unprepared is an attempt to invoke "the Rule": "At a party's request, the court must order witnesses excluded so that they cannot hear other witnesses' testimony...."[7] Traditionally, excluding a witness by requiring them to sit outside of the courtroom required little thought, but in a virtual courtroom, application and enforcement of "the Rule" requires more forethought and preparation. Many times, virtual hearings are packed with parties listening in who do not intend to make a formal appearance. After all, courts are a public forum, and all creditors, parties-in-interest and the public at large are invited to listen in or watch most hearings.

To complicate matters, witnesses might participate remotely from across the nation, while other witnesses might be sitting together in the same room. Depending on the location of witnesses and technology systems used by the court, enforcement of "the Rule" might be simple in some cases, but not so simple in others. In any event, if counsel intends to invoke "the Rule," pre-hearing preparation and arrangements might be necessary to ensure compliance.

Calling Witnesses to the Virtual Witness Stand

Typically, a witness's whereabouts are not an issue, as the witness might be corralled in the courtroom gallery or just outside of the courtroom. In a virtual setting, on the other hand, we have seen that witnesses sometimes wander off and go about their day as usual. When counsel is ready to call the witness to the virtual witness stand, the witness might be away from his/her computer, or while the witness was patiently waiting to be called to testify, the witness's smartphone, tablet or computer battery may have died with no available charging station or back-up available. To avoid the problem of the missing witness, additional prehearing planning and attention is required. Simply put, the typical instruction of "See you at the courthouse at 9 a.m." might not be sufficient.

Proffers and Stipulations Are Your Friend

No matter how thoroughly you prepare your witness and no matter how advanced everyone's technology might be, technology hiccups and glitches are inevitable. We have all lived the nightmare: The video feed is skipping in and out, someone's video is not working, or that awful feedback is coming from who knows where, yet direct testimony is pressing on. With the court's permission, one way to avoid an unwelcome hiccup is to proffer your witness's direct testimony.[8] Of course, your witness must still be available *on video* for any cross-examination,[9] but getting the key facts into evidence as smoothly and glitch-free as possible might avoid your key evidence being overshadowed by technology gremlins.

Electronic Exhibits: Who Knew They Were So Convenient?

Perhaps one of the more beneficial consequences of a virtual courtroom experience is the expanded use of electronic exhibits. Of course, many tech-savvy attorneys have been using electronic exhibits for years, but now even those attorneys who are not so tech-savvy (or maybe who just like hauling around large binders) have been forced to succumb to 21st-century technology.

Preparing electronic exhibits for virtual courtroom contested matters and trials takes a bit more planning and coordination than simply serving your exhibits on opposing counsel and showing up in court with a thumb drive or paper exhibit binders. To adapt to the virtual courtroom, many courts have developed specific rules governing the admissibility and required availability of your electronic exhibits to the court, opposing counsel and witnesses. Therefore, as previously noted, study and follow your court's local rules and procedures, which might vary widely. Again, most judges are patient and will work with the attorneys as we all learn how best to try a case in a virtual courtroom, but critical to any case is developing your record with admissible evidence, so it is up to you to be prepared.

Impeachment Documents and Exhibits

Although electronic exhibits have proven convenient in virtual courtrooms, some attorneys have struggled when

4 Some courts have been forced to go so far as expressly forbidding testimony while driving. *See Rubie's Costume* at 3 ("[C]ounsel and witnesses are directed to refrain from participating either by audio or video while operating a vehicle.").

5 *See Rubie's Costume* at 4 ("The party sponsoring each witness shall be responsible for ensuring that the remote witness has obtained the password-protected link to the videoconference, has obtained all exhibits prior to the Hearing, has registered via the Cisco WebEx link provided for the Hearing, and has equipment and internet service sufficient to permit participation in the hearing.").

6 "At a party's request, the court must order witnesses excluded so that they cannot hear other witnesses' testimony...." Fed. R. Evid. 615.

7 Fed. R. Evid. 615. Excluding witnesses from a trial serves two purposes: "It exercises a restraint on witnesses 'tailoring' their testimony to that of earlier witnesses; and it aids in detecting testimony that is less than candid." *Geders v. U.S.*, 425 U.S. 80, 87 (1976).

8 For a thorough discussion, *see* Hon. Craig A. Gargotta, "The Effective Use of Proffers in Bankruptcy Court," XXXVI *ABI Journal* 6, 26-27, 66-67, June 2017, *available at* abi.org/abi-journal.

9 While an attorney need only read into the record a potential witness's testimony, the witness must still be present on video to take an oath, affirm the testimony and be available for cross-examination. *See U.S. v. Bernardine*, 73 F.3d 1078, 1082 (11th Cir. 1996).

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Dicta: Virtual Hearings Might Be New, but Your Evidence Must Still Be Correct

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attempting to use documents for impeachment purposes.[10] Some courts have established specific rules and procedures for impeachment documents, but many have not. In a traditional courtroom, counsel could stash impeachment documents in a briefcase and present them in a flurry of drama when necessary. In the virtual courtroom, however, the ability to seamlessly whip out and use impeachment documents might be a challenge. For example, counsel must ensure that he/she has the ability to show the impeachment documents to the witness, the court and opposing counsel. Before the hearing, additional thought and planning is needed to distribute and effectively use impeachment documents over the virtual platform.

Evidentiary Objections

In the traditional courtroom, it is common for attorneys to object to questions, witness responses and the admission of evidence, but in a virtual courtroom, voicing those objections is not as seamless. Many times, for example, attorneys forget that their line is muted, or the judge may have muted all lines other than those speaking to prevent feedback and background noise. Feed delays and other technical issues might also prevent counsel from timely raising an evidentiary objection.

To ensure that all counsel are provided a fair opportunity to raise objections and create as clear and clean of a record as possible, perhaps a brief, pre-hearing discussion on the record with the court might be appropriate to establish clear and fair ground rules for evidentiary objections. A fair opportunity to raise objections and to create a clear record is always the goal.

Background Bingo

This final tidbit applies to everyone appearing on video in any virtual hearing. Most everyone in your virtual courtroom hearing will not only see you, they will also peek around at your room, whether it is an office, a dining room, and even in some instances — well, no need to go there; you get the idea. It is just too tempting! Judges are people, too, and many are doing the same thing. Some call it "background bingo," and law clerks of a younger generation call it "Room Raiding."[11]

With that said, we should all pay more attention to our backgrounds, as it really is easy to get distracted by things that stand out. But do not take this too literally! On the other side of the coin, you should also avoid putting yourself into what appears to be an "interrogation room," as blank walls can be just as distracting. Bottom line: You do not need to hire an interior designer, but you probably do not want to be a finalist in a game of background bingo, either.

On second thought, forget everything we just wrote about background bingo. Some fun and levity in our COVID-19 world is good. You may call your next witness. abi

10 Some courts distinguish between impeachment documents, which need not be served upon opposing parties, unanticipated-rebuttal exhibits, and good, old-fashioned rebuttal exhibits, which must be listed on an exhibit list and served upon other parties.

11 Based on an old MTV show that apparently aired well after MTV stopped actually playing music.

Lien on Me

By Kathleen L. DiSanto

When Less Is Not More

Sufficient Identification of Collateral in Financing Statements

Editor's Note: *For additional perspective on the* I80 Equipment *case, see the article on p. 34.*

Skimping on collateral descriptions might come at a cost, depending on the jurisdiction, as evidenced by recent decisions from two courts of appeals that reached very different conclusions in analyzing the issue. In January 2019, the First Circuit Court of Appeals held that a financing statement, which made reference to "pledged property" as defined in the security agreement, was insufficient under Puerto Rico's version of the Uniform Commercial Code (UCC).[1] However, just nine months later, the Seventh Circuit Court of Appeals reached the exact opposite conclusion, finding that a financing statement that merely referenced the collateral description in the security agreement sufficiently described the collateral under Illinois law, which adopts the UCC.[2] Surprisingly, the Seventh Circuit's opinion failed to acknowledge the circuit split or even mention, let alone discuss, the First Circuit's ruling in the *Puerto Rico* decision.

The First and Seventh Circuit's analyses turn on several provisions of the UCC, which govern the sufficiency of collateral descriptions in financing agreements. Pursuant to § 9-502 of the UCC, a financing statement is sufficient if it "(1) provides the name of the debtor; (2) provides the name of the secured party or a representative of the secured party; and (3) indicates the collateral covered by the financing statement."

Section 9-504 also addresses the sufficiency of a financing statement. Under § 9-504 of the UCC, the financing statement must provide "a description of the collateral pursuant to Section 9-108" or "an indication that the financing statement covers all assets or all personal property." In turn, § 9-108(a) provides that a description of collateral is sufficient "whether or not it is specific, if it reasonably identifies what is described." Pursuant to § 9-108(b), a description reasonably identifies the collateral if it identifies the collateral in one of six ways: (1) specific listing; (2) category; (3) type of collateral defined in the UCC; (4) quantity; (5) computational or allocational formula or procedure; and (6) "any other method, if the identity of collateral is objectively determinable."

1 *In re Fin. Oversight & Mgmt. Bd. for Puerto Rico*, 914 F.3d 694 (1st Cir. 2019) (hereinafter the "Puerto Rico decision" or "Puerto Rico case").
2 *First Midwest Bank v. Reinbold (In re I80 Equip. LLC)*, 938 F.3d 866 (7th Cir. 2019).

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The *Puerto Rico* Decision

The *Puerto Rico* case involved bonds issued in 2008 by the employee retirement system of the Puerto Rican government and efforts by the Commonwealth of Puerto Rico to avoid the bondholders' interests in the retirement system's property under the Puerto Rico Oversight, Management and Economic Stability Act (PROMESA), which incorporated various provisions of the Bankruptcy Code, including § 544.[3] The bondholders asserted security interests in property owned by the retirement system, including certain employer contributions to the system, and contended that their interests were properly perfected in accordance with Puerto Rico's UCC.[4] The security agreement made reference to a pension funding bond resolution, which identified the property subject to the bondholders' security interest.[5] However, the resolution was not attached to the security agreement, which did not specify the collateral, incorporate the description of the collateral set forth in the resolution, or otherwise describe the pledged property.[6] The financing statement, which was filed with the Puerto Rico Department of State in 2008, described the collateral as "[t]he pledged property described in the Security Agreement attached as Exhibit A hereto and by reference made a part thereof."[7] The security agreement was attached to the financing statement, but the resolution was not.[8] Thus, the financing statement did not define the "pledged property," nor was the "pledged property" defined in the documents attached to the financing statement.

Amendments to the financing statement were filed in 2015 and 2016.[9] Similar to the initial financing statement, the amendments described the collateral as "[t]he Pledged Property and all proceeds thereof and all after-acquired property as described more fully in Exhibit A attached hereto and incorporated by reference."[10] However, unlike the initial financing statement, the definition of "pledged property" excerpted from the resolution was attached as Exhibit A.[11]

3 *Puerto Rico*, 914 F.3d at 703.
4 *Id.*
5 *Id.* at 704-05.
6 *Id.*
7 *Id.* at 705.
8 *Id.*
9 *Id.*
10 *Id.*
11 *Id.*

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Lien on Me: Sufficient Identification of Collateral in Financing Statements

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In addition to the collateral description, there was also a question as to whether the amendments to the financing statements sufficiently named the debtor due to a change in Puerto Rican law. After the filing of the initial financing statement in 2008, but before the filing of the amendment in 2015, Puerto Rico amended the act establishing the employee retirement system in 2014.[12] Among other things, the 2014 amendments did not exclusively refer to the employee retirement system as the "Employees Retirement System of the Government of the Commonwealth of Puerto Rico" and interchangeably referred to the system as either the "Employees Retirement System of the Government of the Commonwealth of Puerto Rico" or the "Retirement System for Employees of the Government of the Commonwealth of Puerto Rico."[13] However, notwithstanding the changes to Puerto Rican laws, the amendments to the financing statement continued to identify the debtor as the "Employees Retirement System of the Government of the Commonwealth of Puerto Rico."[14]

Under these facts, the First Circuit concluded that the 2008 financing statements satisfied the requirements of Article 9, with one critical exception: They failed to sufficiently describe the collateral.[15] In so holding, the First Circuit rejected the bondholders' invitation to adopt a more relaxed understanding of the collateral description requirement.[16] The First Circuit noted that the 2008 financing statements "do not describe even the type(s) of collateral, much less the items at issue," and that the resolution describing the collateral was not attached.[17] Thus, the First Circuit concluded that the "total combination of facts undercuts several key goals of the UCC and its filing system," including "fair notice to other creditors and the public of a security interest" and "facilitat[ing] the expansion of commercial practices."[18] However, the case had a happy ending for the bondholders on the perfection issue, as the First Circuit determined that the amendments to the financing statements cured the defects created by the 2008 filings and that the debtor was properly named in the 2015 and 2016 amendments.[19] Although the bondholders did not meet the requirements for perfection until December 2015, their interest was properly perfected prior to the enactment of the PROMESA legislation, which provided the basis for the attempted avoidance of the bondholders' liens.[20]

I80 Equipment LLC

Faced with an issue of first impression in an interlocutory appeal of the bankruptcy court's order, the issue before the Seventh Circuit was whether a financing statement sufficiently "indicates" the collateral by making reference to an unattached security agreement. The debtor, I80 Equipment, purchased and refurbished trucks and obtained a commercial loan from First Midwest Bank.[21] The security agreement granted the lender a security interest in 26 categories of collateral, and First Midwest Bank timely filed its financing statement, which described the collateral as "all collateral described in the security agreement."[22] However, when the borrower defaulted on the loan and filed a chapter 7 case two years later, the lender sued the trustee and sought declaratory relief that its security interest was properly perfected and senior in priority to all other claimants.[23]

> **While a financing statement must describe the collateral, the threshold for adequacy of a collateral description in a financing statement is much lower than in a security agreement.**

The chapter 7 trustee took the position that the security interest was unenforceable, arguing that the financing statement lacked a sufficient description of the collateral, and asserted a counterclaim to avoid the lien.[24] The trustee argued that based on the principles of *ejusdem generis*, the meaning of "any other method" as used in § 9-108(b)(6) of the Illinois Code should be interpreted narrowly to mean "of a like kind" or "similar to" the specifically enumerated classes of things.[25]

The bankruptcy court concluded that the security interest was voidable because the financing statement, on its face, failed to include a description of the collateral. In so holding, the court analyzed the Illinois Code Comment to Article 9, which provides that "[t]he security agreement and the financing statement are double screens through which the secured party's rights to collateral are viewed, and his rights are measured by the narrower of the two."[26] The bankruptcy court also cited two bankruptcy court opinions that addressed the sufficiency of a collateral description, both of which concluded that the collateral descriptions were insufficient.[27] The Seventh Circuit accepted the lender's request for a direct appeal.[28]

In reversing the bankruptcy court's judgment, the Seventh Circuit held that the financing statement was sufficient by applying the "plain and ordinary meaning" of Illinois's version of the UCC.[29] Hon. Michael B. Brennan, who authored

12 *Id.* at 706.
13 *Id.* at 706-07. The changes to the statute summarized herein are based on the official translation of the Puerto Rican Laws from Spanish to English.
14 *Id.* at 706.
15 *Id.* at 710.
16 *Id.*
17 *Id.*
18 *Id.* at 711.
19 *Id.* at 713.
20 *Id.* at 721.
21 *I80 Equip. LLC*, 938 F.3d at 869.
22 *Id.*
23 *Id.*
24 *Id.*
25 *First Midwest Bank v. Reinbold (In re I80 Equip. LLC)*, 591 B.R. 353, 358 (Bankr. C.D. Ill. 2018).
26 *Id.* at 359 (citing Ill. Ann. Stat. ch. 26, § 9-110, Illinois Code Comment at p. 85 (Smith-Hurd 1974)).
27 *Id.* at 360. (citing *In re Lynch*, 313 B.R. 798 (Bankr. W.D. Wis. 2004) (mere filing of financing statement is insufficient and collateral must be identified or described); *In re Lexington Hospitality Grp. LLC*, 2017 WL 5035081 (Bankr. E.D. Ky. Nov. 1, 2017) (reference to security agreement that fully described collateral but was not attached was insufficient description of collateral)).
28 *I80 Equip. LLC*, 938 F.3d at 869.
29 *Id.* at 868.

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the court's opinion, focused on the 2001 revisions to the UCC and the difference between including a "description of the collateral" versus "indicating the collateral."[30] Based on the reduced requirement to "indicate" rather than "describe" the collateral, the lender's description of the collateral in the financing statement was adequate under the Seventh Circuit's analysis and application of the Illinois UCC.[31] The Seventh Circuit's interpretation is consistent with the UCC's notice function recognized by other courts and "the goal of the filing system … to make known to the public whatever outstanding security interests exist in the property of debtors."[32]

The court also noted the different functions served by a security agreement and a financing statement: "[T]he security agreement defines and limits the collateral, while the financing statement puts third parties on notice that a creditor may have an existing security interest in the property and further inquiry may be necessary."[33] While a financing statement must describe the collateral, the threshold for adequacy of a collateral description in a financing statement is much lower than in a security agreement.[34] Essentially, the Seventh Circuit puts the onus on creditors to request a copy of the security agreement if they need to resolve questions regarding the collateral description indicated in a financing statement. The takeaway from the Seventh Circuit's ruling is that a financing statement is sufficient if it "puts third parties on notice that a creditor may have an existing security interest."[35]

Given the circuit split (the U.S. Supreme Court denied *certiorari* of the *I80 Equipment LLC* appeal and provides some clarity on the issue),[36] a savvy professional will err on the side of caution. Ideally, even if arguably not required by the UCC, practitioners should continue to include more robust descriptions of collateral in financing statements or attach the security agreement to the financing statement in order to avoid challenges to their security interests based on the adequacy of the "indication" of collateral. abi

30 *Id.* at 871.
31 *Id.*
32 *Id.* at 872 (citing and quoting *In re Blanchard*, 819 F.3d 981, 986, 988 (7th Cir. 2016)).
33 *Id.*; *see also In re Grabowski*, 277 B.R. 388, 391 (Bankr. S.D. Ill. 2002).
34 *Id.* at 873.
35 *Id.* at 872.
36 The trustee docketed a petition for *certiorari* on Jan. 14, 2020; *cert. denied, Reinbold v. First Midwest Bank*, No. 19-870, 2020 WL 871954 (U.S. Feb. 24, 2020).

JUNE 1, 2020

Supreme Court Finds No Appointment Clause Violation in Puerto Rico's Oversight Board

> The Supreme Court reversed the First Circuit, which had held that the Oversight Board violated the Appointments Clause because the members were not appointed by the President and confirmed by the Senate.

Although the members of the Financial Oversight and Management Board of Puerto Rico were not nominated by the President nor confirmed by the Senate, the Supreme Court ruled today that the appointment of the Board did not violate the Appointments Clause of the Constitution because they exercise "primarily local duties."

All of the justices agreed in the judgment reversing the First Circuit, which had held that the Board's appointment violated the Appointments Clause. The decision by the high court means there will be no lingering doubt about the validity of Puerto Rico's debt arrangement.

Justice Stephen G. Breyer wrote the opinion of the court.

Justices Clarence Thomas and Sonia Sotomayor concurred in the judgment, which means they agreed with the result but for different reasons. In her opinion, Justice Sotomayor raised but did not answer questions about the ability of Congress to set aside Puerto Rico's democratically elected government by appointing a federal board to take over the island commonwealth's fiscal powers and responsibilities.

The Creation and Appointment of the Oversight Board

The Supreme Court ruled in June 2016 that Puerto Rico was ineligible for chapter 9 municipal bankruptcy. To allow the island commonwealth to restructure its unsupportable debt, Congress almost immediately adopted the Puerto Rico Oversight, Management, and Economic Stability Act, or PROMESA (48 U.S.C. §§ 2161 *et. seq.*).

The members of the Oversight Board were not nominated by the President nor were they confirmed by the Senate. Rather, PROMESA allowed the President to appoint one member of the Oversight Board. The President selected six more from a list of candidates provided by leaders of Congress. If any members appointed by the President were not on the congressional list, Senate confirmation would have been required. Since the six were all on the list, there was no Senate confirmation.

The Oversight Board commenced debt-adjustment proceedings for the commonwealth and its instrumentalities beginning on May 3, 2017, in district court in Puerto Rico. Aurelius Investment LLC and its affiliates filed a motion in August 2017 seeking dismissal of Puerto Rico's debt-arrangement proceedings, arguing that the filing of the petition on behalf of the Commonwealth of Puerto Rico by the Board under Title III of PROMESA violated the Appointments Clause. The Oversight Board, the official unsecured creditors' committee and COFINA bondholders, among others, opposed Aurelius.

Designated by the Chief Justice and sitting in the District of Puerto Rico to preside over the PROMESA proceedings, District Judge Laura Taylor Swain of New York handed down an opinion in July 2018 holding the Board was properly constituted under the Territories Clause of the Constitution, Article IV, Section 3, Clause 2. *In re Financial Oversight and Management Board for Puerto Rico*, 318 F. Supp. 3d 537 (D.P.R. July 13, 2018). To read ABI's discussion of the district court opinion, **click here**.

The First Circuit Reversal

On appeal, the First Circuit reversed, holding that the appointment of the members of the Oversight Board violated the Appointments Clause because they were not nominated by the President and confirmed by the Senate. Relying on the *de facto* officer doctrine, the appeals court went on to rule that its opinion would "not eliminate any otherwise valid actions of the Board prior to the issuance of our mandate in this case." *Aurelius Investment LLC v. Commonwealth of Puerto Rico*, 915 F.3d 838 (1st Cir. Feb. 15, 2019). For ABI's report on the First Circuit opinion, **click here**.

The appeals court entered an order that operated as a stay to remain in effect until the Supreme Court ruled on the case.

The Oversight Board filed a petition for *certiorari* in April 2019. Four other petitions followed, by the U.S. Solicitor General, Aurelius, the official creditors' committee and a labor union in Puerto Rico.

The Supreme Court granted *certiorari* on June 20 to decide two questions: (1) Should the members of the Oversight Board have been nominated by the President and confirmed by the Senate; and (2) if the appointment was unconstitutional, does the *de facto* officer doctrine validate actions already taken by the Oversight Board?

Oral argument took place on October 15. To read ABI's report on oral argument, **click here**.

In retrospect, two issues raised by the justices at oral argument presaged the result: (1) Were they to uphold the First Circuit, some justices were concerned

result: (1) were they to uphold the First Circuit, some justices were concerned that the precedent would undermine the governance of the District of Columbia and the territories; and (2) Counsel for the Oversight Board and the bondholders agreed that the case turned on whether the Board acted primarily locally or primarily nationally.

Counsel for the Board argued that its members were performing primarily local functions because they were supplanting Puerto Rico's legislature and governor. The bondholders contended that the Board's functions were national in scope because the proceedings would affect billions of dollars of investments and investors throughout the country who held the debt.

The Opinion for the Court by Justice Breyer

The Appointments Clause of the Constitution, Art. II, §2, cl. 2, provides that the President "shall nominate, and by and with the Advice and Consent of the Senate, shall appoint Ambassadors, other public Ministers and Consuls, Judges of the supreme Court, and all other Officers of the United States . . . ."

To decide whether Board members are Officers of the U.S., Justice Breyer — like Justice Thomas — leaned heavily on eighteenth century history and actions taken by Congress in dealing with territories immediately after adoption of the Constitution.

Justice Breyer quickly made a distinction between "ordinary" officers of the U.S. to whom the Appointments Clause applies and officers of the District of Columbia and the territories to whom the clause may nor may not apply in view of Article I, §8, cl. 17, pertaining to the District, and Article IV, §3, cl. 2, applicable to territories.

Justice Breyer did not leave the reader wondering about the result.

On the first page of his 22-page decision, he said that the "Board's statutory responsibilities consist of primarily local duties, namely, representing Puerto Rico in bankruptcy proceedings and supervising aspects of Puerto Rico's fiscal and budgetary policies." He held "that the Board members are not 'Officers of the United States.' For that reason, the Appointments Clause does not dictate how the Board's members must be selected."

Justice Breyer did not disagree entirely with the First Circuit. He agreed with the Boston-based appeals court to the extent that "Appointments Clause restricts the appointment of all officers of the United States, including those who carry out their powers and duties in or in relation to Puerto Rico."

In other words, he held that the clause applies to "*all* 'Officers of the U.S,' . . . even when those officers exercise power in or related to Puerto Rico." [Emphasis in original.] Although the Appointments Clause applies to officers of the District of Columbia and the territories, he limited the holding by saying that the clause "*does not* restrict the appointment of local officers that Congress vests with primarily local duties under Article IV, §3, or Article I, §8, cl. 17." [Emphasis in original.]

Justice Breyer then turned to the question of whether the Board's powers and duties were primarily local. Parsing PROMESA, he concluded that "the Board's members have primarily local duties, such that their selection is not subject to the constraints of the Appointments Clause."

Rejecting the bondholders' reliance on the nationwide effect of the Board's decisions, Judge Breyer said that "[t]aking actions with nationwide consequences does not automatically transform a local official into an 'Officer of the U.S.'" The "same might be said of any major municipal, or even corporate bankruptcy."

Basing the ruling on the Appointments Clause, Justice Breyer avoided having to overrule the so-called Insular Cases from the very early twentieth century, which have been criticized for justifying colonialism. He was also not required to opine on the *de facto* officer doctrine.

The Concurrence by Justice Thomas

In his 11-page opinion, Justice Thomas agreed there was no violation of the Appointments Clause. However, he could not agree with the majority's "dichotomy between officers with 'primarily local versus primarily federal' duties," which he called an "amorphous test."

Instead, Justice Thomas relied on his understanding of the "original meaning" of the Appointments Clause. In his view, Board members are territorial officers performing duties under Article IV of the Constitution and "are not federal officers within the original meaning of that phrase . . . ."

Justice Thomas would also reverse the First Circuit, because the Board's members perform duties under Article IV and thus "do not qualify as 'Officers of the U.S.'" In his view, the majority's "primarily local" test would enable Congress to evade the Appointments Clause
"by supplementing an officer's federal duties with sufficient territorial duties, such that they become 'primarily local,' whatever that means."

The Concurrence by Justice Sotomayor

The opinion by Justice Sotomayor is required reading for anyone concerned about depriving residents of Puerto Rico of their constitutional rights. She focused on the 1950 compact with Puerto Rico, enacted by Congress as Public Law 600, where residents of the island were given the right of self-governance.

In her 24-page opinion, Justice Sotomayor repeatedly asked whether Congress had the right to take away Puerto Rico's self-governance once residents of the island had been ability to elect their own officials. At a minimum, she questioned whether taking away rights of self-governance turned the Board members into federal officials.

The board members "exist in a twilight zone of accountability," Justice Sotomayor said, because they were "neither selected by Puerto Rico itself nor subject to the strictures of the Appointments Clause. I am skeptical that the Constitution countenances this freewheeling exercise of control over a population that the Federal Government has explicitly agreed to recognize as operating under a government of their own choosing, pursuant to a constitution of their own choosing."

Justice Sotomayor "reluctantly" concurred in the judgment because, in her view, the most important issues were not presented in the case. She saw the

case as raising a "serious questions about when, if ever, the Federal Government may constitutionally exercise authority to establish territorial officers in a Territory like Puerto Rico, where Congress seemingly ceded that authority long ago to Puerto Rico itself."

Opinion Link

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Case Details

Case Citation	Financial Oversight and Management Board for Puerto Rico v. Aurelius Investment LLC, 18-1334 (Sup. Ct. June 1, 2020)
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NOVEMBER 30, 2020

Court of Claims Rebuffs Puerto Rico Bondholders' Claims of Unconstitutional Takings

> Cutting off post-petition liens under PROMESA did not violate the Takings Clause.

Holders of secured Puerto Rico retirement system bonds lost in their latest effort at squeezing blood out of a rock.

Building on decisions by the Supreme Court and the First Circuit, Judge Richard A. Hertling of the U.S. Court of Claims ruled on November 23 that the federal government was not liable for a Takings Clause violation when bondholders lost their security interest in employer contributions as a consequence of the enactment of the Puerto Rico Oversight, Management, and Economic Stability Act, or PROMESA (48 U.S.C. §§ 2161 *et. seq.*).

Bondholders Lose Their Post-Petition Liens

After the Supreme Court ruled that Puerto Rico was ineligible for chapter 9 municipal bankruptcy, Congress quickly adopted PROMESA. Large swaths of chapter 9, governing municipal bankruptcy, are incorporated into PROMESA, including Section 552. With the exception in Section 552(b), Section 552(a) cuts off a prepetition security interest in property acquired after filing.

Including the retirement system, Puerto Rico and many of its instrumentalities sought relief under PROMESA in 2017. In the debt-adjustment proceedings, Puerto Rico's federally appointed Financial Oversight and Management Board effectively represented the retirement system.

At the Oversight Board's behest, the Puerto Rico legislature passed legislation requiring the retirement system to transfer its assets to the commonwealth's general fund. In return, Puerto Rico's government assumed responsibility for paying retirement benefits. The transfer meant that employer contributions went to the general fund, not to bondholders. The Oversight Board took the position that Section 552 cut off the retirement system bondholders' security interest in employer contributions made after filing.

The retirement system bondholders mounted several lawsuits, so far unsuccessfully. At the end of January, the First Circuit upheld the district court and ruled that Section 552 cut off the security interest held by bondholders in contributions made to Puerto Rico's retirement system by employers after filing. *In re Fin. Oversight & Mgmt. Bd. for P.R.*, 948 F.3d 457, 462 (1st Cir. 2020) ("Section 552 Decision"), *cert. denied sub nom. Andalusian Glob. Designated Activity Co. v. Fin. Oversight & Mgmt. Bd. for P.R.*, No. 20-126 (Nov. 16, 2020). To read ABI's report on the January opinion, **click here**.

In the lawsuit before Judge Hertling, the bondholders raised three claims under the Takings Clause of the Fifth Amendment. They contended there had been unconstitutional takings of (1) their liens and their contractual right to timely payment on the bonds; (2) their liens on post-petition employer contributions, and (3) their contractual right to timely payment from post-petition employer contributions.

In addition to the January First Circuit opinion, Judge Hertling's decision was informed by the Supreme Court's holding on June 1 that the appointment of the Oversight Board did not violate the Appointments Clause of the Constitution because the members were exercising "primarily local duties." *Fin. Oversight & Mgmt. Bd. for P.R. v. Aurelius Inv., LLC*, 140 S. Ct. 1649 (2020). To read ABI's report, **click here**.

The opinion by Judge Hertling is a *tour de force* on the law of takings. Had he not dismissed the bondholders' claims, federal legislation would often hit a tripwire making the government liable for the impairment of contracts.

The First Claim Fails

The Supreme Court's decision in June led to the demise of the bondholders' first claim, based on the notion that PROMESA effected an unconstitutional taking of their liens. The result turned on whether the Oversight Board was a federal entity.

If the Oversight Board was not a federal entity, the Court of Claims would lack subject matter jurisdiction under the Tucker Act, 28 U.S.C. § 149.

In *Aurelius*, the Supreme Court held that the Oversight Board exercised primarily local duties. Judge Hertling said that "*Aurelius* is dispositive; it speaks to the precise issue the Court needs to address in order to determine its jurisdiction."

The Oversight Board "is an instrumentality of Puerto Rico, not the federal government," Judge Hertling said. Consequently, the bondholders' "first claim therefore is not against the United States as required under the Tucker Act."

Judge Hertling dismissed the first claim after also ruling that the Oversight Board's actions could not be attributed to the U.S.

The Second and Third Claims Fail

The second and third claims were doomed by the First Circuit's decision this year that the bondholders had no enforceable security interest in post-petition contributions. On both claims, the bondholders argued that Section

552 effected a taking of their security interests in post-petition employer contributions.

Unlike the First Circuit, Judge Hertling was looking at the question in terms of an unconstitutional taking, not the operation of Section 552 alone. He reached the same result as the First Circuit because he ruled that the bondholders only held an "expectancy" in post-petition contributions. In a constitutional sense, there could be no taking of property, because the property did not exist on the filing date.

Judge Hertling said that the First Circuit opinion collaterally estopped those bondholders who were parties to the appeal in Boston.

For bondholders not parties to the Boston appeal as to whom collateral estoppel did not apply, Judge Hertling agreed with the First Circuit. He dismissed the second claim, holding that the bondholders "did not have a property interest in their purported liens on post-petition employer contributions. Accordingly, the plaintiffs cannot establish a taking and have failed to state a claim upon which relief can be granted."

The bondholders' third claim likewise failed. He ruled that "Section 552 impaired the plaintiffs' contractual right to post-petition employer contributions, but this impairment does not constitute a taking under the Fifth Amendment. Accordingly, the plaintiffs fail to state a claim upon which relief can be granted."

Judge Hertling explained that the bonds themselves were not "taken." Rather, he said, they were "impaired," and an impairment "is insufficient to support a claim for a taking."

Opinion Link

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Case Details

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Feature

By Luke A. Barefoot and Daniel J. Soltman

Are Special Revenues as Special as They Once Were?

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Two years ago, municipal bond markets were roiled when a Puerto Rico district court held that chapter 9 of the Bankruptcy Code *authorizes*, but does not *require*, municipal debtors to make timely interest payments on special revenue bonds during the pendency of a chapter 9 proceeding (the "district court opinion").[1] This opinion was affirmed by the U.S. Court of Appeals for the First Circuit in 2019 (the "First Circuit opinion").[2] Thereafter, credit-rating agencies undertook a review and downgraded certain outstanding special revenue bonds so as to bring the special revenue bond rating closer to the rating assigned to a city's (or in some cases, a state's)[3] general obligation bonds. In January 2020, the U.S. Supreme Court declined to review the First Circuit opinion,[4] which will remain in place.

Accordingly, investors should recalibrate their expectations with respect to special revenue bonds, particularly insofar as they relate to the expectations on timing and assurance of continued interest payments during a chapter 9 proceeding. Investors should be careful to separate assuring continued payments during the pendency of a proceeding from the ultimate prospects for recovery through an adjustment plan, which the First Circuit opinion does not directly implicate. To aid in that process, this article discusses (1) a brief history of special revenue bonds, (2) the district court and First Circuit opinions, (3) subsequent analysis from credit-rating agencies and (4) additional considerations for municipal investors.

A Brief History of Special Revenues

Although the concept of "special revenue" bonds is unique to municipal finance, it is not new. Municipalities have historically issued two broad categories of bonds: (1) general obligation bonds; and (2) special revenue bonds. The key difference is that while general obligation bonds are payable from the applicable municipality's general treasury, special revenue bonds are payable only from a specific pledged revenue stream.[5] Since special revenue bonds are nonrecourse, they are typically issued at a higher interest rate than general obligation bonds and do not count against constitutional debt limits.[6]

Holders of special revenue bonds strike a different bargain than general obligation bondholders, and in 1988, chapter 9 was amended to more accurately reflect that bargain in a chapter 9 proceeding. Although the 1988 amendments included a number of aspects,[7] the two most critical are the addition of (1) § 922(d),[8] which places *some* limitation on the application of the automatic stay to post-petition payments of special revenues; and (2) § 928, which allows for pre-petition liens on special revenue streams to continue after a chapter 9 filing.[9]

Procedural Background

The PRHTA, which oversaw Puerto Rico's highway development, issued special revenue bonds secured by revenue streams such as toll revenues and vehicle license fees (the "PRHTA SR bonds") and special revenues (the "PRHTA SRs").[10] Following the filing of PRHTA's PROMESA proceeding, the fiscal agent for the Commonwealth and its instrumentalities gave an instruction to "refrain from making the scheduled July 1, 2017 payment" to the holders of the PRHTA SR bonds.[11] Following the subsequent default on a $219 million payment, insurers on the PRHTA SR bonds, subrogated to the rights of bondholders after having paid their claims,[12] sought to compel periodic payments during PRHTA's PROMESA proceeding pursuant to the schedule in the governing documents. Specifically, the insurers sought (1) a declaratory judgment that the automatic stay did not apply and that failure to

1 *In re The Fin. Oversight and Mgmt. Bd. for Puerto Rico*, 582 B.R. 579 (D.P.R. 2018). Although the district court's opinion arose from the Puerto Rico Highway and Transportation Authority's (PRHTA) Title III proceeding under the Puerto Rico Oversight, Management and Economic Stability Act (PROMESA), PROMESA incorporates the applicable provisions from chapter 9 of the Bankruptcy Code such that the opinions at issue should represent persuasive authority in the chapter 9 context (or arguably binding authority within the First Circuit).

2 *In re The Fin. Oversight and Mgmt. Bd. for Puerto Rico*, 931 F.3d 121 (1st Cir. 2019).

3 Under the Bankruptcy Code, a "municipality" is a "political subdivision or public agency or instrumentality of a State." 11 U.S.C. § 101(40). Although states are not eligible for chapter 9, state instrumentalities are. Accordingly, in some cases, the ratings analysis for an issuer potentially eligible for chapter 9 focused on its relationship to a state rather than a municipality.

4 *See* Order Denying Petition for *Certiorari*, *Assured Guaranty Corp. v. Fin. Oversight Bd.*, 140 S. Ct. 855 (2020) (No. 19-391), 2020 WL 129573.

5 There are other municipal finance mechanisms, but this article focuses on these for illustrative purposes.

6 *See* H.R. Rep. No. 100-1011 (1988), 1988 WL 169907, at *4.

7 The 1988 amendments also added a definition of "special revenues" in 11 U.S.C. § 902(2).

8 Section 922(d) reads in full: "Notwithstanding section 362 of this title and subsection (a) of this section, a petition filed under this chapter does not operate as a stay of application of pledged special revenues in a manner consistent with section 92[8] of this title to payment of indebtedness secured by such revenues."

9 Absent the addition of § 928, liens on after-acquired revenues would have been extinguished by the application of § 552 of the Bankruptcy Code.

10 District Court Opinion at 586. The parties did not dispute that the revenues were "special revenues."

11 *Id.* at 587 (quoting the instruction).

12 *Id.*

pay the PRHTA SRs would violate §§ 922(d) and 928(a) of the Bankruptcy Code, (2) an order enjoining future violations, and (3) an order that the PRHTA SRs be remitted.[13]

The district court relied on a plain-text reading of §§ 922(d) and 928(a) to determine that neither required any specific action on the part of a municipal debtor, nor did those sections exempt bondholder enforcement actions from the automatic stay. The district court found that § 928(a) "includes no language that could be construed to implicate the payment of special revenues or the timing thereof."[14] Similarly, the district court found that § 922(d) has only a "limited purpose," but that it did "not address actions to enforce liens on special revenues, [nor did it] sanction nonconsensual interference with governmental properties or revenues." The district court held that § 922(d) imposed no obligation on the debtor, but rather merely established that "the automatic stay is not an impediment to continued payment, whether by the debtor or by another party in possession of pledged special revenues, if other relevant circumstances permit or require such payments."[15]

The First Circuit, finding the language of both §§ 922(d) and 928 unambiguous, affirmed the district court's opinion. Agreeing with the district court's analysis, the First Circuit explained what behavior § 922(d) *did* exempt from the automatic stay — namely, the voluntary payment of funds from a debtor or the application of collateralized funds already in the creditor's possession (which would have been violations of the automatic stay prior to the 1988 amendments).[16] After denying a petition for rehearing and rehearing *en banc*,[17] the insurers sought *certiorari*, which the Supreme Court denied without analysis in January 2020.[18]

Credit-Rating Agency Analysis

For context, it is important to appreciate what appears to have been a shared market assumption that special revenue bond service payments would be made on time in chapter 9 proceedings, which came largely from historical experience and case law arising from Jefferson County, Ala.,'s chapter 9 proceeding.

The dispute in Jefferson County revolved around what was meant by the phrase "pledged special revenues" in § 922(d) and whether it was intended to capture only revenues actually held by the indenture trustee or receiver as of the petition date, or whether it included revenues not yet remitted. Examining both the text and legislative history after finding the word "pledged" to be ambiguous, the court broadly determined that "pledged special revenues" in § 922(d) applied broadly to revenues that were not yet in the possession of the indenture trustee or receiver.[19] Although the dispute centered around the scope of which revenues were covered by § 922(d)'s "pledged special revenues," there was no dispute as to whether the applicable special revenues would be remitted once a determination was made.[20]

Having relied on the expectation that periodic special revenue debt service payments would be paid on time in a chapter 9 proceeding, ratings agencies began to reevaluate its guidance following the First Circuit opinion.[21] In doing so, the agencies closely examined the potential for diversion of revenues away from a chapter 9 debtor, and expressed concerns where the rating on the special revenue bonds was significantly higher than the rating of the underlying municipality or state's general obligation bonds. Downgrades came shortly thereafter. For example, in July 2019 Moody's downgraded Cleveland's water revenue bonds, noting that "[t]he downgrade of the [bonds] reflects a closer alignment of the rating to Cleveland's general obligation (GO) rating ... because of the water system's strong legal and governance linkages as a department of the city," noting that "[t]he risks to bondholders of the strong interrelatedness between the city and its utility are highlighted by the [First Circuit opinion]," and "[i]n the event of serious fiscal stress of the city, there is greater risk for system creditors that the city could impair pledged special revenue than if the system were legally independent of the city."[22]

Considerations for Investors

Notwithstanding the review undertaken by ratings agencies, investors should not assume that further downgrades on special revenue debt are forthcoming. The analysis undertaken by the ratings agencies focused on re-examining the totality of circumstances, and considering whether and to what extent the special revenue debt was entangled with a municipality (or state) such that there was an increased risk of nonpayment in a chapter 9 proceeding.

It is also important to keep in mind that any ratings adjustments are corrections for how debt-service payments on special revenue bonds might be treated in a chapter 9 proceeding, and are not generally reflections of any imminent change. In addition, investors should separate an analysis of the timely receipt of interest obligations during the pendency of a chapter 9 proceeding from ultimate treatment and recovery in a chapter 9 plan. Finally, investors must remain conscious that in addition to treatment in a hypothetical chapter 9 proceeding, the ratings analysis is even more attenuated where the potential debtor is in a state that has not authorized its municipalities to file for chapter 9 or has placed limitations on filings.[23]

Moreover, even assuming that the First Circuit opinion is adopted by other courts, holders of special revenue bonds

13 *Id.* at 592.
14 *Id.* at 593.
15 *Id.* at 594-98. In discussing each of §§ 928 and 922(d), although relying on a plain-language analysis, the district court noted that its analysis was consistent with the legislative history and purpose of chapter 9 and these two sections in particular.
16 First Circuit Opinion at 132.
17 *In re Fin. Oversight and Mgmt. Bd. for Puerto Rico*, 931 F.3d 111 (1st Cir. 2019) (the "*En Banc* Denial Opinion"). This opinion, joined by four judges of the First Circuit, acknowledged that there might be some ambiguity in § 922 (*e.g.*, who is exempted from the automatic stay and the meaning of "application"), but there was no ambiguity as to whether § 922 allowed bondholder-enforcement actions, emphatically finding that it did not. *See id.* at 114. A single dissenting judge found the text of § 922(d) to be ambiguous and found that the legislative history supported the insurers' position. *Id.* at 119 (Lynch, C.J) (dissenting).
18 *See* Order Denying Petition for *Certiorari, Assured Guaranty Corp. v. Fin. Oversight Bd.*, 140 S. Ct. 855 (2020) (No. 19-391), 2020 WL 129573.
19 *In re Jefferson Cty., Ala.*, 474 B.R. 228, 262-75 (Bankr. N.D. Ala. 2012).
20 *Id.* The district court and First Circuit opinions each found *Jefferson County* inapposite as to whether the applicable payment required to be made was not at issue. *See* District Court Opinion at 595-96; First Circuit Opinion at 132. Although the majority in the *En Banc* Denial Opinion did not discuss it, the dissent focused on the *Jefferson County* court's statement that "the structure and intent of what Congress enacted by its 1988 amendments to chapter 9 was to provide a mechanism whereby the pledged special revenues would continue to be paid uninterrupted to those to which/whom payment of the sewer system's indebtedness is secured by a lien on special revenues." *En Banc* Denial Opinion at 120 (Lynch, C.J) (dissenting).
21 *See, e.g.*, "Kroll Reviewing Special Revenue Bond Implications of Court Ruling," Kroll Bond Rating Agency (March 27, 2019).
22 "Moody's Downgrades Cleveland, OH's Senior Lien Water Revenue Bonds to Aa2, Outlook Stable," Moody's Investor Service (July 29, 2019). As noted in the insurers' petition for *certiorari*, similar downgrades have also occurred.
23 Section 109(c) of the Bankruptcy Code places eligibility requirements on chapter 9 filings, including that the municipality must be authorized by state law to file. Nearly half of U.S. states do not permit chapter 9 filings in any form, with the remaining states either providing blanket or conditional authorizations.
24 *See* S. Rep. No. 100-506 at 6 (1988).

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are not without remedy in chapter 9 proceedings — even if debt service is not timely paid. First, even if not required, a chapter 9 debtor may choose to timely service debt for other reasons. For example, as noted in the Senate Report, in the San Jose Unified School District's chapter 9 case, the district continued paying bondholders throughout the proceeding in order to ensure continued access to credit markets and comply with applicable state law.[24]

Second, a holder of a secured claim can always bring a motion to lift the stay and enforce its rights, and these opinions do not disturb the rights of bondholders to do so. The Bankruptcy Code provides that the automatic stay may be lifted for "cause," and lift-stay motions typically argue that the secured creditor's collateral is not adequately protected from diminution in value.[25] However, creditors should be aware that this process might be expensive, will often be disfavored by bankruptcy courts (particularly at the early stages of the proceeding), and may include complicated valuation issues on a potentially indefinite future revenue stream.

Third, even where not receiving regular payments over the course of a chapter 9 proceeding, holders of special revenue bonds are still well-positioned to influence the restructuring because of the special protections provided to them on ultimate treatment in an adjustment plan. To nonconsensually confirm an adjustment plan over the objection of a class of secured creditors, the secured creditor class must either retain their existing liens, or receive a future payment stream with a present value equal to the value of their claim (or alternatively, if their collateral is sold with the liens attaching to the proceeds or they receive the "indubitable equivalent" of their claim).[26] Accordingly, subject to the aforementioned valuation issues, municipalities are limited in cramming down a plan on special revenue bondholders.

Finally, the Code provides that to confirm an adjustment plan, the plan must provide that, *inter alia*, "the debtor is not prohibited by law from taking any action necessary to carry out the plan," and that it "is in the best interests of creditors and is feasible."[27] Accordingly, where state law is inconsistent with proposed treatments under a plan, a court may refuse to confirm the plan on the grounds that the municipal debtor will not be able to carry out the plan and thus it is not feasible.[28]

Conclusion

Although it is likely that any downgrades resulting from the district court and First Circuit opinions have already occurred, the recent COVID-19-driven downturn means that pressure will increase, including in the public sector, which is expected to suffer disruptions and decreases in revenue collections. At present, the scope of the downturn and timeline for market recovery remain uncertain, and investors should be focused on evaluating just how "safe" timely periodic payment obligations on special revenue bonds might be in a true downside scenario. abi

25 *See* 11 U.S.C. § 362(d).
26 11 U.S.C. § 1129(b)(2)(A)(iii).
27 11 U.S.C. § 943(b)(4), (7).
28 *See, e.g., Matter of Sanitary & Improvement Dist. No. 7*, 98 B.R. 970 (Bankr. D. Neb. 1989) (denying confirmation where plan was inconsistent with Nebraska law).

Faculty

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Hon. Marvin Isgur is a U.S. Bankruptcy Judge for the Southern District of Texas in Houston, appointed Feb. 1, 2004, and also served as Chief Judge. His first bankruptcy experience was as an expert witness before the bankruptcy court and then as a principal of a number of real estate partnerships that became chapter 11 debtors. From 1978-1990, Judge Isgur was an executive with a large real estate development company in Houston. Between 1990 and 2004, he represented trustees and debtors in chapter 11 and chapter 7 cases, as well as various parties in 14 separate chapter 9 bankruptcy cases. Judge Isgur has written over 500 memorandum opinions and was one of the first judges to issue opinions interpreting the 2005 Bankruptcy Abuse Prevention and Consumer Protection Act. He is one of the principal organizers of the annual University of Texas Consumer Bankruptcy Conference in Galveston, Texas, and is a frequent speaker at continuing education programs. Judge Isgur is a member of the Judicial Conference Committee on Court Administration and Case Management, appointed by Chief Justice John Roberts, and active participant in national bankruptcy rules process; he also led a national compromise effort on chapter 13 plans. He received his bachelor's degree from the University of Houston in 1974, his M.B.A. with honors from Stanford University in 1978, and his J.D. with high honors from the University of Houston in 1990.

Hon. Laurel Myerson Isicoff is Chief Judge for the U.S. Bankruptcy Court for the Southern District of Florida in Miami, initially appointed on Feb. 13, 2006, and named chief judge on Oct. 1, 2016. She is the president of the National Conference of Bankruptcy Judges, and is also a member of ABI's Board of Directors. Judge Isicoff is a member of the *Pro Bono* Committee of the American College of Bankruptcy, as well as chair of its Judicial Outreach Committee. She also currently serves as judicial chair of the *Pro Bono* Committee of the Florida Bar's Business Law Section and is a member of the Florida Bar's Standing Committee on *Pro Bono*. Prior to becoming a judge, Judge Isicoff specialized in commercial bankruptcy, foreclosure and workout matters both as a transactional attorney and litigator for 14 years with the law firm of Kozyak Tropin & Throckmorton, after practicing for eightyears with Squire, Sanders & Dempsey, now known as Squire Patton Boggs. In private practice, she also developed a specialty in SEC receiverships involving Ponzi schemes. Following law school, Judge Isicoff clerked for Hon. Daniel S. Pearson at the Florida Third District Court of Appeals before entering private practice. She is a past president of the Bankruptcy Bar Association (BBA) of the Southern District of Florida, and, until she took the bench, chaired its *Pro Bono* Task Force. Judge

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Hon. Enrique S. Lamoutte is a U.S. Bankruptcy Judge for the District of Puerto Rico in San Juan, initially appointed in November 1986 and having served as Chief Judge. He is also a judge for the U.S. Bankruptcy Appellate Panel for the First Circuit, for which he served as Chief Judge. Judge Lamoutte previously clerked for U.S. District Judge Hernan G. Pesquera of the U.S. Bankruptcy Court for the District of Puerto Rico and was chief of the Civil Division of the U.S. Attorney's Office. He is also a retired colonel of the Puerto Rico Air National Guard. Judge Lamoutte graduated from Boston College and the University of Puerto Rico Law School.

Hon. Robert A. Mark was appointed a Bankruptcy Judge for the U.S. Bankruptcy Court for the Southern District of Florida in 1990 in Miami and served as Chief Judge from 1999-2006. Prior to his appointment to the bench, Judge Mark served as head of the bankruptcy department of the Miami firm of Stearns, Weaver, Miller, Weissler, Alhadeff & Sitterson, PA. He has served on the National Conference of Bankruptcy Judges Endowment for Education and frequently lectures at continuing education seminars, including the National Conference of Bankruptcy Judges and the Federal Judicial Center's educational programs for bankruptcy judges. Judge Mark is a Fellow of the American College of Bankruptcy and is an author for *Collier on Bankruptcy*. His community activities include participation in a program that offers internships to minority law students, and participation in financial education programs for high school students through the Bankruptcy Bar Association's CARE program, which teaches students about the dangers of credit card abuse. Judge Mark is a Fellow of the American College of Bankruptcy and an author for *Collier on Bankruptcy*. He is a graduate of Boalt Hall School of Law, University of California at Berkeley.