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Crossing Borders: International Reorganizations

By James H.M. Sprayregen and David A. Agay

Surveying the landscape evolving from the most recent credit cycle, we have noted in recent commentary that increasingly complex and overleveraged capital structures, with their multiple layers of secured debt, have had unexpected implications for Chapter 11 reorganizations.

For example, though rarely drawing much attention prior to 2007, credit bidding under section 363(k) of the Bankruptcy Code and "cramming up" secured creditors through the "indubitably equivalent" prong of section 1129(b)(2)(A) have surfaced as newly popular tools to implement restructurings [see "Credit (Bid) Where Credit's Due," *The Bankruptcy Strategist*, January & February 2010]. Similarly, the debt balloon appears to have generated tricky issues around cross-border reorganizations.

As a business extends globally, likewise its capital providers consider value and sources of recovery in multiple jurisdictions. If the enterprise then encounters difficulties or requires de-leveraging, it may need to undertake a transaction that compromises debt claims as to U.S. and non-U.S. operations.

In this regard, Chapter 11 can present opportunities and challenges to accomplishing the reorganization. In particular, out of legal, business, or other concerns, a global enterprise may file Chapter 11 petitions for its U.S. legal entities while its non-U.S. legal entities continue to operate outside of Chapter 11. In such scenarios, questions quickly arise regarding protecting the non-U.S. legal entities from creditor action and discharging funded debt claims against an entity that did not file a Chapter 11 petition. Akin to the developing approaches in credit bidding and indubitable equivalent cases, bankruptcy judges and lawyers have started to consider a combination of contractual and bankruptcy rights and remedies to effect cross-border reorganizations through Chapter 11 plans.

In certain respects, the Chapter 11 cases of LyondellBasell Industries and its subsidiaries present an early case study for these issues. LyondellBasell is the product of the 2007 leveraged buyout of Lyondell Chemical Company by Basell AF S.C.A. The combination created LyondellBasell Industries AF S.C.A, one the world's largest petrochemical companies.

As of the commencement of the Chapter 11 cases, LyondellBasell owed over $20 billion in secured and unsecured debt, a portion secured by junior liens. The initial Lyondell Chapter 11 filings on Jan. 6, 2009, excluded certain of the non-U.S. funded debt obligors. Thereafter, in response to actions taken against certain non-debtor affiliates, including the parent entity (organized under the laws of the Grand Duchy of Luxemburg), the debtors obtained a temporary injunction pursuant to Section 105 of the Bankruptcy Code enjoining such actions. Subsequently, on April 24, 2009, the parent entity filed for Chapter 11, obtaining the automatic stay and the other rights and protections under the Bankruptcy Code.

For their Chapter 11 plan of reorganization, the Lyondell debtors have proposed, among other things, largely standard-fare injunctions and discharges as to the debtor entities. For the non-U.S., non-debtor Lyondell obligors, the plan contemplates releasing liens and guarantees through a combination of contractual and bankruptcy measures.

First, through the aggregated majority vote of the senior secured classes (Class 3- DIP Roll-Up and Class 4 - Senior Secured), the plan provides for a release of guarantees and liens against non-U.S. Lyondell obligors pursuant to the terms of the prepetition senior secured credit agreement.

Second, through an "Enforcement Sale" transaction under the prepetition intercreditor agreement, done as part of the other restructuring transactions under the plan, the plan will release liens and guarantees held by certain junior secured and unsecured parties (i.e., the Bridge Loan and the 2015 Notes). Finally, the plan has a bankruptcy injunction against post-effective date enforcement of the liens and guarantees against the non-U.S. Lyondell obligors.

In effect, the LyondellBasell plan channels acceptance of the plan by the senior secured classes into a lender directive to the agent under the prepetition loan documents. Such direction would empower the agent to act to release liens and guarantees against non-debtors, with non-debtors further shielded by the plan and confirmation order injunction. Even though not yet confirmed,

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on these issues, the LyondellBasell plan likely presages future cross-border recapitalizations, whether implemented through Chapter 11 or outside of it.

Strategies to implement balance-sheet restructurings vary. Absent 100% lender consent, it can be difficult to accomplish the reorganization on an out-of-court basis. Sponsors typically explore different options, including a debt exchange scenario whereby less than 100% of lenders may tender and compromise their claims and, post-closing, the company may continue to service a nominal "stub" of the existing debt. Companies may also consider amending the credit documents to overcome dissenting lenders; although credit arrangements typically preclude compromising debt claims without consent from affected lenders.

Chapter 11 solves the "hold out" problem through Section 1129 and other provisions of the Bankruptcy Code. Assuming a debtor can obtain the requisite class majorities (at least two-thirds in amount and more than one-half in number of those voting), and/or meets the other tests for confirmation under Chapter 11, a recapitalization is achievable despite non-acceptance by dissenting lenders. However, if lenders can still seek recourse against non-U.S. affiliates that remain outside the bankruptcy process, notwithstanding confirmation of a Chapter 11 plan, Chapter 11 may not provide full closure or a fresh start. For this reason, where possible, much planning often goes into addressing funded debt liabilities of the non-U.S. entities.

One option often considered is filing U.S. bankruptcy petitions for the non-U.S. entities. This may not be feasible, for example, because of the lack of a sufficient U.S. nexus under section 109 of the Bankruptcy Code, or because in foreign jurisdictions, where bankruptcy has a stronger cultural taint, a Chapter 11 filing may harm operations. Where a U.S. bankruptcy filing appears viable, the company still needs to consider enforcement in non-U.S. jurisdictions. While U.S. law generally views the automatic stay as extending beyond U.S. borders, the law or a judge outside the U.S. may take a different view. In solving recognition and enforcement problems, adoption of the Model Law on Cross-Border Insolvency in the U.S. and across several non-U.S. jurisdictions certainly has provided a new means of enforcement, but it may not be a complete answer. Countries may adopt their own variation on the Model Law and, where a jurisdiction has not adopted the Model Law, preexisting local law and precedent on foreign recognition must be evaluated. In any event, the advice and counsel of local, non-U.S. counsel will play a critical role in the planning process.

In the planning phase, parties may also consider rights and remedies under the relevant loan agreements. The Lyondell plan construes lender acceptance in a bankruptcy solicitation as a concurrent direction to release non-U.S. liens and guarantees under prepetition credit agreements. Similarly, at the outset of a case, lenders may consent to a forbearance, waiver, or amendment relating to enforcement actions under the prepetition credit agreements, which consent or direction would then bind the loan agent. With the loan agent not pursuing remedies, this may protect affiliates not subject to the automatic stay from independent lender action. Likewise, as to junior creditors, the debtor and/or senior lenders may seek to rely on standstill periods often contained in intercreditor agreements. Furthermore, as in Lyondell, a direction from the accepting lenders for the agent to act under the loan documents, as channeled through a Chapter 11 plan or otherwise, may cause a release of liens, guarantees, or other obligations.

However, in "free fall" situations, often it may not be feasible to seek cooperation from lenders. In addition, in either a "free fall" or preplanned bankruptcy, resort to the credit documents may not suffice. For example, in Lyondell, the debtors had to obtain a temporary injunction against collection actions against non-debtor, non-U.S. guarantors under section 105 of the Bankruptcy Code. We believe that other Chapter 11 debtors likely will follow Lyondell's lead by invoking sections 105 or 362 of the Bankruptcy Code to extend the automatic stay or enjoin actions as to non-debtor, non-U.S. affiliates. Precedent exists for enjoining actions against non-debtor guarantors or other co-liable parties, but U.S. courts appear to have not fully considered the issue as it pertains specifically to non-U.S. affiliates. In considering funded debt claims against non-debtor, non-U.S. entities, we also believe that courts will consider existing precedent on non-debtor plan releases under sections 105 and 1123(b)(6) of the Bankruptcy Code.

Where neither U.S. bankruptcy nor contractual remedies provide a complete solution, parties may consider parallel non-U.S. processes for the foreign affiliates to discharge debt claims. Jurisdictions outside the U.S., for example in the U.K. and Canada, have developed their own mecha-

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nisms for implementing recapitalizations on a preplanned, fast-track basis, similar to prepackaged bankruptcies in the U.S. Also, where a U.S. debtor obtains bankruptcy court or contractual protections against enforcement outside the U.S., parties may consider recognition and enforcement proceedings in the foreign jurisdiction under the Model Law (as enacted there) or existing local precedent on granting comity to non-domestic reorganizations. Depending on the jurisdiction, we expect that parties will be working closely with local counsel to evaluate the feasibility of such measures in the context of a broader restructuring strategy.

As is evident, we have not endeavored in this note to fully treat and evaluate the many complex issues arising in cross-border reorganizations, any one of which may merit its own, much lengthier discussion. For now, we note simply that, as the liability column of U.S. balance sheets has developed a more international hue, bankruptcy practitioners in the U.S. have started to engineer creative solutions to implement restructurings that draw from existing precedent and transactional mechanisms. We look forward to the further development and interesting challenges in this area in the coming years.

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