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ROUNDTABLE

Bankruptcy & restructuring

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R O U N D T A B L E

BANKRUPTCY & RESTRUCTURING

Bankruptcy and restructuring is complex, full of twists and turns. Yet for all the expense, blame, negotiation, compromise and introspection involved, the process does provide an opportunity for distressed companies to get their businesses and finances back on track. For those companies that meet the challenges of bankruptcy and restructuring, there could well be a brighter future in store; for those that do not, a different outcome lies in wait.

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Robinson: Could you provide a brief overview of the global bankruptcy and restructuring landscape over the past 12 months? How much of the blame for the volume of bankruptcy and restructuring cases can be laid at the door of continuing economic difficulties, for example?

Hayek: The levels of large corporate bankruptcies have been relatively low for a number of reasons including highly liquid markets and low or even negative interest rates. Both serve to preserve existing structures. Consequently, there have been only few large bankruptcies such as the Brazilian telecoms company Oi or the Australian retailer Dick Smith. However, these large bankruptcies can be attributed to structural changes or failed individual business models and financing structures rather than prevailing economic difficulties. In contrast to this, on a local level we see smaller companies struggling in the current market environment. In Switzerland, the number of companies filing for bankruptcy has been on the rise in 2016. The continuing strength of the Swiss franc and corresponding difficulties for the exporting industry no doubt have been playing a role in this.

Durrer II: The second half of 2016 has seen a decrease in the number of US bankruptcy filings as compared to the first half of 2016. The decision by the Federal Reserve to continue deferring an arguably overdue interest rate increase has provided troubled companies with additional breathing room. Furthermore, the increasingly contentious bankruptcy litigation landscape continues to contribute to the reluctance of major players to undertake costly and uncertain bankruptcy and restructuring cases without a consensus among major constituencies and a well-established exit plan.

Feltman: The vast majority of significant filings in the last year are the direct result of sustained depression of commodity prices and a direct effect on industries including a range of energy companies, including coal, crude and natural gas on both the production and exploration sides. The downturn in commodity prices has also caused a slowdown for companies that process commodities, causing a ripple effect for ancillary goods and service providers impacted from this downturn. The slowdown in the Chinese economy, which is one of the world's largest draws on commodity products, has also had an impact on the number of filings. The depression of commodity prices should have caused an uptick in spending by consumers, but that has not happened either. The Hanjin filing is a classic example of the effect of the depressed commodity prices and the related ripple effect – fewer goods are being manufactured and shipped, resulting in less demand for shipping services and decreased revenue performance.

Liscio: The global bankruptcy and restructuring landscape over the last 12 months has been less about continuing economic difficulties and more about the impact of geopolitical forces on certain industries and the credit markets. Declining Chinese demand and the OPEC nations' responses to various nations' involvement in Middle Eastern conflicts, for example, have been particularly impactful. These factors, in turn, have had significantly negative impact on commodities and the price of oil. The collapse of oil prices has wreaked havoc on the entire energy sector in the US, but that collapse did not extend to other industries. However, the first three quarters of 2016 saw a tightening in the credit market across all asset classes and loan prices in the secondary markets were depressed.

The increasingly contentious bankruptcy litigation landscape continues to contribute to the reluctance of major players to undertake costly and uncertain bankruptcy and restructuring cases.

VAN C. DURRER II

Nolan: At the start of 2016, the oil price fell to an historic low of $28 per barrel. We have also seen Nordic High Yield Oil & Gas default rates rise to a record 34 percent in June 2016. Inevitably, this has forced North Sea operators to cut costs, refinance and restructure their portfolios. In the wake of the Brexit referendum, sterling has fallen to 31 year lows against the US dollar and faces a period of sustained weakness. Companies that are exposed to currency fluctuations will no doubt see an impact on their business. For example, UK airlines often purchase their fuel in dollars and pay ground handling fees in euros. Sterling in decline may well have a profound impact in increasing the major costs of certain businesses.

Golubow: United States bankruptcy filings for the 12-month period ending 30 September 2016 were the lowest for any 12-month period since December 2007, according to new statistics released on 26 October by the Administrative Office of the US Courts (AOUSC). The September 2016 annual bankruptcy filings totalled 805,580, compared with 860,182 cases filed in the previous year. A "national wave of bankruptcies that began in 2008" reached a peak in September 2010, when nearly 1.6 million bankruptcies were filed, the AOUSC report said. Bankruptcy filings fell by less than 10 percent for the third straight quarter, with filings falling by 6.3 percent for the 12-month period ending 30 September 2016 compared with the previous year. The three most recent reports follow a four-year period in which consecutive double-digit declines occurred in every reporting period since December 2011.

Chatz: Numerous factors have been impacting the restructuring landscape over the last 12 months, including the material reduction in oil prices, Brexit, continuing instability in the Middle East and other areas and the general impact of demography, which includes irreconcilable healthcare costs and the needs of our elder generations. The volume of bankruptcy and insolvency cases has not significantly increased in 2015 or 2016. What has occurred is that the nature of those cases continues to change and the businesses that are impacted thereby continue to suffer instability. There is a continuation of uncertainty in the markets which is leading to an ongoing fear of the future.

Central bankers cannot fix issues of demography. The costs of pension obligations and the additional needs of our elders will continue to sap the strength of the world economies for many years to come.

Robinson: Which sectors and industries are seeing the greatest number of distressed companies undergoing bankruptcy and restructuring procedures?

Golubow: Declining oil prices have already led to a number of bankruptcy filings for energy and natural resource companies. At least 58 oil and gas producers have sought bankruptcy court protection this year, representing about $50.4bn in debt, far above last year's $17.4bn debt accumulated from the 44 companies that filed for bankruptcy. And despite an uptick in oil prices from a 12-year low of $26 a barrel in January, the industry may be only halfway done, according to oil, gas and restructuring specialists. Brick and mortar retailers continue to struggle and are vulnerable and losing the battle against online retailers as consumers realise that the items they seek are less expensive and more easily accessible online.

Nolan: We are seeing a lot of distressed companies in the oil and gas sector with a particular focus on E&P and oilfield service providers. The sustained fall in the oil price over the last two years has resulted in an EBITDA reduction across a number of companies in the sector. Energy sector businesses have significantly cut back on capex, implemented disposal programmes and are focused on addressing operational inefficiencies. The retail sector is also under sustained pressure for the foreseeable future. This is primarily due to growing online competition. Imported clothing will also become more expensive due to the fall in sterling. The impact of Brexit on all of these sectors is yet to be fully determined but it is clear a long period of uncertainty over the outcome could harm consumer confidence.

Durrer II: Volatility in commodity pricing continues to negatively impact companies operating in a wide variety of industries. The United States in particular has seen a large number of restructurings, recapitalisations and bankruptcies in the retail, oil and gas, renewable energy and shipping sectors over the past 12 months and the trend is expected to endure for the near term.

Declining oil prices have already led to a number of bankruptcy filings for energy and natural resource companies.

RICHARD H. GOLUBOW

Although oil prices are showing signs of stabilising, the rebound may be coming too late to benefit deeply indebted companies with significant energy sector operations.

Hayek: With the oil price continuing on a historic low, the commodity sector has been under stress for some time. Difficulties have now also spread from companies engaging in exploration and production to companies engaging in supplies or other parts of the production chain. Other commodities such as gas as well as the energy and metal sector are increasingly feeling the pressure of falling prices too. In Switzerland, the high level of the Swiss franc has hit the retail sector and the tourism industry the most and companies in these sectors have been forced to undergo restructurings in order to cut down on costs and secure profitable continuation of their businesses.

Chatz: The energy sector, as well as retail sales and casual dining chain restaurants, appear to be the entities that are suffering the greatest distress in the marketplace. In addition, for-profit educational institutions are also suffering distress as their business models are under scrutiny from the US government thanks to the unclear benefit of some programmes and the concomitant material and seemingly unjustified student debt foisted upon young people based upon educational needs.

Liscio: Commodities and energy in particular have comprised the bulk of distressed activity, though August and September saw a decline in new cases as the capital markets seemed to solve a number of short-term problems for a number of distressed companies. Oil prices have remained flat and low with energy futures showing no sign of improvement. Creditors of companies that were hoping to outlast the decline in oil prices will be less willing to kick the can much further and are likely to take the pain and get a restructuring done at the trough. Media and communication companies that gorged on credit and are significantly overleveraged are beginning to show signs of distress.

Feltman: International restructurings are trending up, as reflected in the number of Chapter 15 filings in the energy, shipping, commodity-based or transportation based businesses.

Robinson: What, in your experience, are the main reasons or circumstances in which companies seek to undertake a financial or operational restructuring? How many see the warning signs too late?

Nolan: Companies are often forced to undertake a financial restructuring when overleveraged and unable to meet certain covenants in their financing agreements. Typically, negotiations commence with lenders or other stakeholders who may try to take the lead. The process clearly escalates if and when there is a liquidity crisis. On the operational side, a company may be exposed to key but burdensome contracts. This is particularly relevant if the group's contract prices rise above the market rate such as rents on premises or rates on asset or equipment hire. Existing stakeholders or new third-party investors will find further investment undesirable until the operational side of the business is addressed. Generally, sophisticated investors are adept at identifying early warning signs. However, it is not uncommon for some management teams to adopt a wait and see approach.

Liscio: The obvious reason companies seek to restructure is ▸▸

overleverage. The factors leading to overleverage are varied, but the more common ones are declining revenue due to systemic changes, for example, internet sales v. brick and mortar retail, and poor management and poor execution on business strategies. In middle market credits, poorly executed and ill-advised mergers often lead to restructurings as management teams routinely underestimate the cost and difficulty of integration and overestimate synergies. We also see restructurings occur where the entire asset class is impaired. A number of coal companies pursued aggressive restructurings in 2016 because the vendor, creditor and regulatory communities expected them to restructure, which provided cover.

Chatz: The failure of any business is often related to management's inability to forecast changes in the marketplace. This is far from a pejorative. Consumer demands, as well as business demands and the economic markets, are shifting with speed never before seen. The material drop in energy prices has impacted numerous entities throughout the global economy. Nobody, three years ago, would have expected the cost of oil to drop well below $50 per barrel. Consumer demand relating to how people spend their leisure time and monies appears to be changing as well. Casual dining appears to be on the wane and retail sales seem to be altogether disappearing. Younger professionals are not earning what they have in the past and are turning to the internet to find the best deal regardless of its place of manufacture.

Durrer II: Companies undertake restructurings for a wide variety of reasons, from right-sizing a debt-heavy balance sheet to jettisoning non-core assets in favour of strengthening the core businesses. Whatever the underlying reason, a company needs to engage with its key constituencies early and often. Developing and implementing a flexible strategy to communicate real-time developments is fundamental to managing the process, and that companies wait too long to initiate discussions with customers, vendors and other counterparties may jeopardise their ability to preserve or improve their operations as needed to ensure a successful restructuring.

Hayek: In my experience, companies mostly seek to undertake a restructuring when they are overleveraged and prospects for recovery do not look promising based on the company's business plan and model. Where the cash flow is insufficient and creditors do not see a clear prospect for improvement of the company's financial situation for the near or medium term, they may call their claims due immediately. This in turn is often the trigger for a company's bankruptcy. Such a situation can occur, in particular, if a company's financing arrangements do not adequately align the interests of all creditors, for example, where high yield bonds exist alongside a fully secured financing structure.

Feltman: We are in an unprecedented liquidity bubble where, by historical standards, the cost of capital has been extraordinarily low for much longer than expected. Even in this 'free money' environment, lenders have been reluctant to act against underperforming borrowers. The situation seems to be transforming into a more demanding lender environment, perhaps due to economic pressures, but regulations requiring greater transparency and accountability also play a factor. Earnings have not kept pace with expectations as the worldwide economy has been sluggish. Growth expectations have slowed, impacting valuations which, in turn, have affected the 'kick the can down the road' philosophy that has generally characterised lender attitudes over the last six to eight years. Now, defaults are increasing as a result of revenue and earnings falling, more event-driven issues, an increase in shareholder activism, and companies facing underperforming divisions.

Companies mostly seek to undertake a restructuring when they are overleveraged and prospects for recovery do not look promising based on the company's business plan and model.

DANIEL HAYEK

Golubow: There are various reasons why companies seek to undertake a financial or operational restructuring. Causes of financial distress include being overleveraged, experiencing decreased sales, increased operating expenses, macroeconomic forces such as the 'great recession' experienced by companies in 2008-2010, an inability to obtain financing or refinancing, management incompetence or disputes and non-recurring problems such as expensive litigation that drains financial resources or an adverse judgment. Most companies see the warning signs too late. Yet, an analysis of the precipitating factors for most distressed companies indicates they could have avoided severe losses and often the loss of the business itself by following some seemingly simple and elementary business principles. For example, preparing, updating and maintaining a proper business plan that includes plans for sales, marketing, operations, capital-expense budget and a cash-flow projection.

Robinson: Could you highlight any notable bankruptcy or restructuring cases in recent months? What insights can we gain from such cases?

Golubow: In the case of *U.S. Bank NA v. The Village at Lakeridge LLC*, the Ninth Circuit Court of Appeals held that a "person does not become a statutory insider solely by acquiring a claim from a statutory insider". Therefore, an insider can sell its claim to a friendly third party, whose vote fulfils or some would say circumvents Bankruptcy Code section 1129(a)(10)'s requirement that an impaired consenting class of creditors, excluding insiders, vote to accept a plan of reorganisation. Insiders can sell their claims for a nominal amount to friendly third parties that will vote in favour of the plan.

Chatz: The most notable case in the Chicago area is the Caesars bankruptcy. This case finally appears to be reaching resolution after many months of discord. Suffice it to say, the stakes are

much higher for creditors. Each potential loss creates a material impact upon a creditor's business operation. Therefore, the stakes for every interest holder are material and an orderly and efficient outcome is obviously the best result. Sadly, rancour is often the first and expensive reaction prior to resolution.

Hayek: A notable bankruptcy recently is Petroplus. This case exemplifies the importance of timing in bankruptcy proceedings. Creditors are interested in the swift conclusion of a bankruptcy and settlements can help accelerate the proceedings because they avoid potentially lengthy litigation. However, with interest rates in Switzerland currently being negative, the bankrupt estate's assets are charged with negative interest. This means that delaying distributions diminishes a creditor's returns. Therefore, settlements become even more important for creditors and they may try to exert influence over liquidators accordingly. In a large bankruptcy spanning multiple jurisdictions, such as Petroplus, concluding a settlement is, however, particularly challenging as it requires close cooperation between the liquidators and lawyers in different jurisdictions.

Feltman: The Caesars Casino bankruptcy case has been noteworthy, as it is a major player in an industry dominated by a few high-profile operators, and the amount of debt involved in the disputes is very significant. This particular filing was years in the making, so it will be instructive to see where valuations settle. The China Fisheries case is also interesting in that a global business with corporate structures and debts spanning multiple jurisdictions is attempting to reorganise itself. The dispersion of economic interests and the integrated nature of these businesses will make coordination between business and judicial processes something to observe and perhaps a learning tool for do's and don'ts going forward.

Durrer II: Lenders regularly consult with advisers and professionals to weigh the potential risks of executing tactics which a court may later view as overly aggressive; in extreme cases courts may equitably subordinate the lenders' claim or even recharacterise debt as equity. The recent New York opinion in the Aeropostale bankruptcy case provides welcome comfort to lenders seeking additional guidance regarding permissible actions in respect of borrowers which are, or who may shortly be, in default under applicable debt documents.

In practice, a company proposing a scheme will need to be prepared to present additional evidence at the scheme hearings.

ELAINE NOLAN

Liscio: There have been a plethora of energy cases over the last 12 months which have highlighted the complexities of property rights and competing claims in oil & gas reserves, resulting in a number of unpleasant surprises for creditors. Valuation has been in the spotlight, and like past cycles where there is insufficient value available for creditors – which has certainly been the story with energy, creditors have spared no expense to contest valuations if they are opposed to a particular reorganisation plan. The Sabine and Paragon cases are good examples of distressed creditors devoting considerable resources to opposing plans of reorganisation and other insolvency transactions which are based on valuations that are perceived by such creditors to be faulty.

Nolan: The Lehman Brothers cases continue to make their way through the English courts with the Waterfall I application recently being heard in the Supreme Court. Waterfall IIA and IIB will be heard in the Court of Appeal early next year. These cases will help to clarify and settle a number of areas including ranking of subordinated debt in the statutory waterfall, interpretation of ISDA Master Agreements and whether foreign currency conversion claims in administrations can be recognised. Another line of important case law has been the developments in creditor Schemes of Arrangement. The English judiciary has sought to apply a more rigorous standard when sanctioning schemes of foreign companies. The judgments in *Codere, VGG* and *Stemcor* indicate that the court may demonstrate greater rigour when applying the 'sufficient connection' test. In practice, a company proposing a scheme will need to be prepared to present additional evidence at the scheme hearings.

Robinson: How would you describe the appetite of creditors to assert their claims against insolvent debtors in the current market? What strategies are they using to improve the value of their recovery?

Chatz: Creditors are utilising committees to a much more efficient basis in the US Bankruptcy Courts, as well as in out-of-court workouts, in order to assure expedited returns and recoveries for their benefit. The stakes for every creditor are higher due to the potential impact upon any creditor's business operation due to a loss created by the insolvency of a debtor. Additionally, an increase in actions by creditors or trustees against insiders, relating to breaches of fiduciary duty and other nefarious actions, has been on the increase.

Hayek: Creditors will assert a claim in a bankruptcy if they consider that there are reasonable prospects for successfully enforcing the claim. The solutions and strategies adopted are thus mainly dictated by the legal analysis of such prospects. Accordingly, in a multijurisdictional bankruptcy which raises difficult legal questions and where the outcome of litigation cannot be predicted with certainty, settlements will present the most preferable solution. Sophisticated and well-advised creditors, in particular hedge funds, are then likely to hedge themselves and sell and buy claims strategically so that potential litigation between group companies does not impact on their recovery.

Feltman: Aeropostale is a good example of where a secured lender is willing to weigh in and take the lead in protecting its collateral interests. In cases where the dollar amounts are

significant, bondholders will to look to litigation as a principal recovery tool.

Liscio: The last 12 months have seen some changes in approach by creditors. The majority of activity, as has been widely reported, has been in the energy sector. At the early stages of the cycle, the asset-based financial institutions which lent based on reserve formulas were hesitant to take action against their troubled borrowers because market participants did not appreciate that energy and commodities prices would face such a severe and prolonged down cycle. Moreover, early entrants into the distressed energy market fared poorly as values continued to drop. As the cycle continued, the reserve lenders and bond market began to take more aggressive actions against the E&P and oil services companies resulting in a series of high-profile bankruptcy cases.

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MARK F. LISCIO

Nolan: The response of creditors really depends on a number of factors, which include how organised a group of creditors are, the number of creditors, whether a creditor or group has restructuring advisers, if they have an economic interest, or if they have significant leverage points. If creditors are sufficiently organised and communicative, are well advised and are part of the fulcrum credit, they may seek to drive the process.

Durrer II: Recent caselaw trends in the New York courts have significantly enhanced the negotiating leverage which 'holdout' bondholders may have against companies that seek to amend their indentures in ways that may impact the ability of bondholders to collect on their outstanding claims. These holdings may incentivise creditors to hold out and litigate for a better recovery, and we are seeing these motivations play out in the lengthy and expensive Caesars Entertainment Operating Corporation bankruptcy case pending in Illinois.

Golubow: Despite stagnant US macroeconomic growth, strong credit markets and low interest rates, many secured creditors' continue to display a willingness to amend and extend loans for healthy and viable businesses pursuant to out-of-court restructurings. Some secured creditors also continue to liquidate their claims through a sale of distressed debt to distressed debt purchasers. In the context of a bankruptcy proceeding, unsecured creditors have limited hope of recovery from the sale or forced liquidation of all or substantially all assets of a debtor, and are most likely to seek recovery through the pursuit of causes of actions ranging from asserting claims for breach of fiduciary duty, professional malpractice claims, or recovery of preferential or fraudulent transfers, by targeting potential deep pocket defendants and pursuing recovery of claims against insurance companies.

Robinson: What trends are you seeing in cross-border or multijurisdictional bankruptcies? What additional challenges do such engagements present?

Durrer II: Coordinating cross-border or multijurisdictional bankruptcies has always remained challenging, as courts often lack detailed knowledge regarding key substantive and procedural attributes of foreign insolvency regimes. However, the steady increase in international cases has helped to improve familiarity with foreign courts and regimes and we expect that the positive trend will continue. Counterparties are likewise becoming more sophisticated and knowledgeable about key similarities and differences between various international regimes, leading to new challenges as well as new opportunities for distressed companies with far-flung global counterparties.

Golubow: In foreign insolvency proceedings, foreign laws are applied in redefining property rights, creditors' rights, contracts, and more. Chapter 15 recognises the laws of most nations, notwithstanding how different they may be from those of the United States. Even foreign laws that provide less protection or cause different outcomes than US laws are imposed upon domestic creditors and other interested parties. Chapter 15 can also provide a way around often stringent jurisdictional requirements and foreign-judgment recognition laws applied by the US courts. Thus, depending on the law of the country in which the main proceeding is commenced, US domestic entities must be prepared for the impact on their rights in ways in which they would not be if US law controlled.

Nolan: 2016 has seen a record number – the total was 95 – of Chapter 15 recognitions of non-US bankruptcy filings since it was introduced in 2005. Such applications have originated from 47 different jurisdictions covering over 90 different forms of foreign proceedings. The recent upward trend has been triggered by the collapse in the oil price as well as difficulties in other commodity markets. Any cross-border court application will inevitably increase the risk of potential challenge by any disgruntled creditors in a public forum.

Hayek: There has been a trend to concentrate cross-border bankruptcies in England through the means of schemes of arrangement available under English law. They do not constitute formal bankruptcy proceedings and thus jurisdictional requirements are much lower. One main advantage is that they can be used to restructure a company's debts without the need for unanimity as required, for example, under the terms of New York law governed bond documentation. It remains to be seen what effects Brexit will have on this trend. It is also uncertain whether such schemes can be recognised in Switzerland. So far there are no decisions of Swiss courts.

Chatz: Multijurisdictional or cross-border bankruptcies do create multiple issues including material issues of jurisdiction. ▸▸

Bankruptcy courts have been circumspect of these cases given the less than clear jurisdictional rights over international assets. It is not clear what the future is with respect to these types of cases. However, it would seem to be logical that a uniform bankruptcy law commission should be undertaken to assure less disorder in a global restructuring marketplace. The current case of Hanjin Shipping is an excellent example of this; the debtor's assets are truly international with ships and containers in multiple jurisdictions often several times in a single day. The determination of what insolvency law controls in such a situation is, literally and figuratively, a fluid situation.

Robinson: To what extent is greater recourse to financing options – such as low interest rates and access to alternative lending – assisting companies to recover?

Feltman: Cheap cash has enabled companies in distress to extend their runway, which may or may not be beneficial to them in the long run. Recidivist weak borrowers end up transforming their debt capital into equity and losing control over their businesses. By having access to cheap cash, some companies are putting a band aid on the issues, instead of being forced to address their issues head on. The results are entirely predictable.

Durrer II: The continued availability of rescue financing has allowed distressed companies to postpone a more substantive restructuring. While in some instances rescue financing may provide an effective bridge to financial health, in others rescue financing may only delay a more substantial restructuring for a distressed company. Accordingly, ready financing options may buy more time, but may not provide a full road to recovery.

Nolan: Alterative investment is becoming popular with a number of funds being willing and able to provide rescue financing. This can be significant in stabilising cash flow when a debtor is struggling and there are no other funding providers.

Liscio: Low interest rates and a growing number of alternative financing solutions, coupled with historically low default rates, was the environment through mid-2015. The collapse in commodity prices in early 2015 brought on by, among other things, lowered demand from China, caused the markets to tap the brakes on providing financing for any credit facility with a looming maturity. Liquidity dried up for energy related companies, and the market got cautious. That in turn caused financial institutions and the par debt community to actively manage their distressed credits by retaining advisers and commencing restructurings. That state of affairs was reflected in the tougher credit markets through the end of summer 2016.

Hayek: Greater recourse to financing options is assisting companies whose business model is sound. However, where a company's business model is no longer viable it will also be difficult to secure alternative lending. In fact, low interest rates mean that borrowers are subject to increased scrutiny and credit checks from lenders because lenders' margins have been eroding. As a further consequence, lenders are focusing on large clients in order to justify the expense of credit checks. Therefore, access to financing options will heavily depend on the viability of a company's business model. Nevertheless, currently companies which exhibit structural weaknesses are often still surviving due to the abundant liquidity in the market.

Chatz: There are a greater number of financing alternatives in the restructuring forum. However, it is less than clear if the costs are in fact better than any given debtor's existing lending facilities. In fact, though a new facility may come with a lower interest rate, the upfront facility cost, monthly monitoring cost, auditing cost, and legal fee and other fee components, may in fact create an effective interest rate for the lending facility that is in fact well above fair distressed rates. Further, alternative lending has alternative consequences for debtors and, often, these alternative lenders are far less willing to work with companies when times are bad.

Golubow: Generally speaking, for companies with proven track records, distressed companies have been able to take advantage of an historically low interest rate environment to refinance, renegotiate their existing debt structures and amend covenants and extend maturities. In instances where traditional banks are fatigued with smaller distressed credit, investors in distressed credit facilities or specialty finance companies are willing to service these smaller credit facilities by either stepping in to acquire debt at an appropriate discount or provide refinancing capital.

By having access to cheap cash, some companies are putting a band aid on the issues, instead of being forced to address their issues head on.

JAMES FELTMAN

Robinson: Could you outline the main benefits of appointing a chief restructuring officer (CRO) to define, guide and execute a successful process?

Liscio: The benefits of hiring a CRO cannot be stressed enough. A good CRO can act as the architect of a restructuring or bankruptcy and act as the key point person among the various consultants, for example, equity, creditors, trade and employees. The appointment of a CRO is a strong signal to a company's creditors that the company is serious about addressing its current situation and generally gives the creditors comfort that the company is getting professional advice. From the company's perspective, a CRO can give the company's board and senior executives guidance on what is achievable, and can inform them of strategies that will be beneficial to the company, meaning a seasoned CRO will know how to exploit the lenders' weakness and potentially extract a better deal for the company.

Golubow: Objectivity is the most important benefit that a ▸▸

CRO brings to a financially distressed business enterprise as it helps the CRO earn the trust needed to gain consensus with key stakeholders. A financial restructuring is inherently contentious, since all stakeholders must to some degree reset and manage reasonable economic expectations. A seasoned CRO, one who has demonstrated financial, operational and management expertise, brings an unbiased view of the economic options available to the business and an objective assessment of these options that supports the process and implementation of a consensual solution of the financial or operational problems. When a business is experiencing financial distress such as decreasing revenue, weakened cash flow and liquidity, delays and missteps in reacting can create or exacerbate several operational issues, such as supply-chain problems and employee turnover that become life-threatening for the business.

Hayek: The benefits will vary depending on whether the CRO replaces the existing management or is appointed to act alongside it. As long as there are good prospects for successfully restructuring the company, the CRO will usually be appointed to act alongside the existing management. Here, the main benefits will be additional flexibility as well as experience, while allowing the existing management to concentrate on running the business. If the CRO replaces management, on the other hand, one of the main benefits will be the CRO's independence, which can help to eliminate long established but detrimental structures and to implement a new strategy necessary for a successful turnaround.

Durrer II: Bringing a chief restructuring officer on board during a restructuring process has two major advantages. First, the appointment of a CRO increases transparency and can boost market confidence in the management team during a tumultuous time. Second, during a bankruptcy case a CRO can focus on many of the specific 'bankruptcy-related' tasks, such as preparing to testify before a court, reporting to lenders and other key constituencies, driving negotiations with key creditor constituencies, and generally handling many of the day-to-day restructuring tasks in order to leave the core senior management team free to focus on broader operational and strategic issues.

Chatz: CROs often provide significant benefits to distressed entities. The CRO is often required by the debtor's existing lenders to provide the lenders with comfort in the restructuring process and clear and correct operational data going forward. Historical management may not be accustomed to the types of data required during the restructuring process, including weekly or daily cash flows and borrowing based certificates. Should a bankruptcy itself be required, the CRO often has been involved in the data gathering protocols needed for a Chapter 11 process which is a unique burden unto itself. The period of time leading up to and shortly after filing a Chapter 11 filing can be turbulent for businesses unprepared for the requirements and amount of information needed even for a bare-bones filing.

Nolan: A CRO's role is a difficult one but can be incredibly beneficial for stakeholders of a distressed company. A CRO has to fully integrate into the management structure of a company at a fraught time in the company's life. Experience plus a 'fresh set of eyes' on a company can be invaluable if he or she is brought in early enough. Appointing a CRO can give comfort to the creditors and avoids the need for changing the management structure of a company or group. A CRO can also be given

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a non-executive or 'light touch' role or be purely managerial while reporting to the board and creditors.

Feltman: A CRO is empowered by management to make decisions from an external point of view without internal politics and conflicts. This has obvious benefits in terms of the integrity of corporate decision-making. CROs also possess industry knowledge that allows them to be very well informed with the mechanics of the company, unlike a trustee which may not have the background necessary to make decisions that best benefit the company. CROs are usually granted the authority to negotiate with the creditors and, with board approval, significantly move the needle in discussions. There are limitations on CROs' authority, sometime set by contractual issues, such as the ability to fire senior management and the authority to file for bankruptcy.

Robinson: Could you outline some of the implications for boards and senior executives of troubled companies, in terms of related liabilities, potential litigation and personal risk?

Hayek: If a company experiences liquidity constraints and its balance sheet shows negative equity, according to Swiss law, the board has to notify the bankruptcy court unless there are tangible prospects for a prompt financial restructuring. The timeframe available to the board is considered to be four to six weeks. Thus, the board is required to act very swiftly. If the board does not start initiating and implementing the necessary restructuring measures quickly enough, its members may be held liable for wrongful trading if the company is declared bankrupt at a later stage. Timely reorganisation and equal treatment of creditors during the phase of restructuring are thus very important.

Liscio: There is a distinction between board members and senior executives, although there is often an overlap between the two. Board members have duties of care and duties of loyalty. In matters where a borrower is in the zone of insolvency, the board's duties extend to the company's creditors. Directors may incur liability should they breach those duties. One of the most common battlegrounds on director liability is where directors

pursue actions developed to benefit and protect equity holders at the expense of creditors. The Caesars case in Illinois is the best example of a board pursuing a series of complicated strategies and transactions which preserve value for the equity sponsor. Creditors have asserted that such actions are, among other things, breaches of duties and have contested the proposed restructuring.

Chatz: There are material risks for any board member and senior executives when a company becomes insolvent. The manner in which the board and executives treat all creditors needs to assure that no one is treated differently or with preference. Risks are much greater for the boards and executives of being subject to lawsuit, which may impact director and officer's coverage if such has been obtained by the company. Creditors may sue for breaches of fiduciary duty, aiding and abetting breaches of fiduciary duty, or in fact fraud, if the insiders of the company have acted in an improvident fashion. The board members and executives, especially in certain jurisdictions, need to be aware of their shifting duties and focus when their company approaches or enters the zone of insolvency.

Durrer II: Creditor constituencies are becoming more aggressive in seeking recoveries from alternative sources, which could include D&O insurance proceeds in the absence of other cash recovery opportunities. Furthermore, the continued uptick in cross-border insolvencies may put pressure on directors and senior management at downstream foreign operating companies which are not always effectively protected by the pending bankruptcy of an upstream holding company. Directors and officers should familiarise themselves with applicable law regarding D&O liability and personal liability in the jurisdiction where the parent company's restructuring is pending, as well as in their home jurisdictions. Personal risk can vary greatly from country to country depending on applicable law and local creditors could, in certain circumstances, seek to assert claims directly against the subsidiary entity – and its officers and directors – in local courts.

Nolan: Directors need to ensure that they are meeting regularly and taking professional restructuring advice to comply with their duties and to follow due process. If any potential conflicts emerge between directors and shareholders on the board, we would typically advise the company to form an independent restructuring subcommittee. Directors also need to be mindful of jurisdictional risks. In some European jurisdictions, directors may be required to file a petition to open insolvency proceedings under strict timeframes if the company is over indebted or cash-flow insolvent. It is critical for directors to take local advice where relevant.

Feltman: Common denominators in terms of implications for boards and senior executives include ignoring friction between activist shareholders and the board of directors or senior management, and waiting too long before seeking assistance from work-out professionals in dealing with lenders voicing concerns about debt repayment.

Golubow: Senior executives comprised of directors and officers still remain the target of post-bankruptcy litigation, particularly on the grounds that the management – or mismanagement – of the D&Os directly resulted in the bankruptcy filing or ultimate failure of the company. In the absence of a bankruptcy proceeding, such lawsuits would ordinarily be brought by shareholders. However, in a bankruptcy proceeding, new lawsuits may be asserted by a creditors' committee, a bankruptcy trustee or a liquidating trust and any pre-bankruptcy lawsuits brought by the shareholders remain pending. In such instances, creditors' committees or trustees assert claims, on behalf of the larger body of creditors of a debtor's bankruptcy estate, against D&Os for breach of their fiduciary duties, to the company and its shareholders. These additional lawsuits can lead to competing lawsuits being litigated simultaneously.

Robinson: What advice can you offer to companies that may require operational and financial restructuring? Are companies generally ill-prepared for such a scenario?

Liscio: The majority of companies are ill prepared for an operational or financial restructuring. Exceptions include situations where a sophisticated equity sponsor is directing the restructuring or where an entire industry is going through a restructuring, such as what the entire US coal industry had to undertake this past year. Our advice to companies in need of restructuring would be to retain professionals experienced in workouts and bankruptcies which can occur through an internal hire, for example, a new chief executive with prior restructuring experience, or to retain outside advisers. Secondly, we would recommend companies immediately review their liquidity and cash flow because once the distress starts in earnest, liquidity dries up very rapidly. An early start on this analysis will allow the company to be proactive and get ahead of problems. Thirdly, companies should approach their creditors with a solution rather than presenting a problem. In many cases, but not all, if a distressed company is forthcoming with its creditors a solution can be forged.

Chatz: The first piece of advice is to take a deep breath and relax. There are alternatives that may assure continuity of the business enterprise and an ability of the insiders to continue to earn a livelihood going forward. The stress created by restructuring or bankruptcy is of a type and nature that is not usually in a business person's nature. The demands created by lenders and other stakeholders are different as the parties' representatives may change and their character is often materially different. In general, a company requiring operational and financial restructuring used to only know positive balance sheets, distributable income to shareholders and mostly rosy outcomes. Restructuring changes this as life is more difficult and every action is reviewed or subject to review. The mundane becomes a priority.

Nolan: As soon as the company identifies any signs of distress, the board should meet regularly and engage, on at least a preliminary basis, with restructuring advisers to look at potential options. This will be a helpful starting point when commencing negotiations with stakeholders. The key is to be proactive but each situation will be different. Proposals for operational restructurings can also help secure financial assistance from stakeholders. Every case is different and some companies are much better prepared to address signs of distress than others.

Feltman: Companies should have their financial information and business plans refreshed, and rely on experienced advisers before undertaking a restructuring so that participants have access to the information they need from the start, thus minimising the risk of participants developing negative views about management. Prior to the restructuring, the development of an internal com-

munications plan with experienced advisers will greatly improve participants' ability to work well with company employees and other stakeholders if they know that senior management is supportive of the process.

Golubow: Companies are typically ill-prepared for an operational or financial restructuring. It is near impossible for businesses to track and understand the increasingly complex factors affecting corporate finances, marketing and virtually every other aspect of management. That is why seeking the advice and counsel of knowledgeable, experienced outside specialists such as a chief restructuring officer or counsel that specialises in financial restructuring is typically crucial to a company's survival. First and foremost advice to companies in distress is to be honest with yourself and others. The sooner management faces the reality of a challenging situation, the better prepared it will be to obtain a quick solution.

Hayek: The board needs to constantly monitor the company's financial conditions, in particular if business is declining, and recognise the need for a financial restructuring early on. In this context, it is particularly important that financial covenants are also monitored at board level so that potential future breaches of the financing terms can be detected as early as possible. Since such breaches often trigger a cross-default and bring down all financial arrangements, they can worsen the situation dramatically so that the company might not be able to complete the necessary restructuring in the relatively short timeframe available to the board under Swiss law. The consequence may be bankruptcy.

Robinson: What trends and developments do you expect to shape the bankruptcy and restructuring landscape over the next 12 months? Do you expect to see the number of such cases increase?

Durrer II: We expect to see continuing robust activity in the oil and gas sector as well as the retail sector. We would anticipate a likely interest rate increase in 2017, which could have a broad impact on companies that have thus far been able to delay major actions so long as lenders remain content to allow management teams significant time and flexibility to try and improve their balance sheet or streamline operations. A shift in interest rates, and a corresponding shift in lenders' appetites to hold such investments, could lead to an increased number of bankruptcy filings in 2017.

Chatz: I believe 2017 will reflect a year of deepening distress in the energy, retail and the for-profit educational markets. In addition, it is not clear, given the material burden of student debt and other obligations of our young citizens, whether housing and the auto markets will continue to grow during the 2017 period. The challenges raised by demography and the burdens of tax obligations created by pension and Medicare/Medicaid burdens upon the federal government and the states continues to impact the inability of markets to grow on an international basis. Fiscal policy cannot impact demography. The inability of our legislators to come to terms with the lack of availability of funds, no matter how much they seek to tax the populace, is materially impacting all sectors of the world's economies.

Nolan: As the oil and gas sector has been under pressure for some time, the future direction of the oil price will be critical. Nordic bonds are facing a 'wall of maturity' in 2018 with over $10bn of debt maturing. A large number of oilfield services vessels are currently laid up and so are unprofitable even if they have already been chartered. There are also substantial decommissioning costs in the UK Continental Shelf on the horizon which North Sea operators will need to factor into their business models. In the face of Brexit and the falling pound, there will likely be further pressure on the retail sector. Brexit may also lead to reforms in the English insolvency regime that will seek to make the UK the best place for doing business in Europe. These reforms essentially may include utilising some of the features of Chapter 11 of the US Bankruptcy Code, including broadening moratoriums, weakening contractual termination rights and widening recourse to rescue finance.

Feltman: Consumer spending has stalled for the moment and the direction consumer spending and business investment takes will be key factors on whether we will see more stagnated growth or other effects for the US economy. Continued fallout in the energy sector, with greater radiation towards complementary industries such as shipping, telecom and real estate, will most likely continue in the upcoming year. Depending on interest rates, the ability to take advantage of cheap cash and to refinance could dissipate, which would result in a great number of filings. Companies will continue to try to execute out of court restructurings for simplicity of process and control of expenses, as a prolonged chapter proceeding can be costly. Companies in 'stress' may have impetus to restructure underperforming divisions before their stock price or revenues begin taking substantial hits.

Hayek: We expect various factors to shape the bankruptcy and restructuring landscape over the next year. On the one hand, Brexit and corresponding exchange rate volatility as well as continuing pressure on the commodities and energy sectors may lead to an increase in the number of bankruptcies. On the other hand, low or negative interest rates as well as high liquidity are likely to persist. This will continue to keep companies with structural weaknesses up and running and might counterbalance any increase in bankruptcies post Brexit. In conclusion, we do not expect the number of bankruptcy cases to increase significantly.

Golubow: While oil & gas remains as one of the most distressed sectors, trouble is spilling over to other sectors including metals and mining, media, construction, durable consumer goods and retailers. Future restructuring and bankruptcy activity depends upon a combination of credit availability, interest rates and secured creditors' willingness to modify existing loans. Despite stagnant US macroeconomic growth, strong credit markets, low interest rates and secured creditors' willingness to amend and extend loans for healthy and viable businesses, should lead to more refinancings, out-of-court restructurings and distressed merger and acquisition activity, and fewer bankruptcy filings.

Liscio: Many parties have expected a second wave of energy insolvencies and restructuring in Q4 2016 and Q1 2017 due to the continued depression on oil prices. Lenders should expect to become reluctant owners of more insolvent energy companies in 2017. There is a developing trend of borrowers being advised by sophisticated advisers who are seeking to implement restructurings by swapping unsecured, junior bonds into secured or senior credit facilities using existing baskets or loosely written provisions in existing credit agreements. Companies are pursuing aggressive exchange offers or other amendments, and essentially forcing creditors to challenge these transactions. ■