

EUROPEAN RESTRUCTURING AND DISTRESSED TRENDS

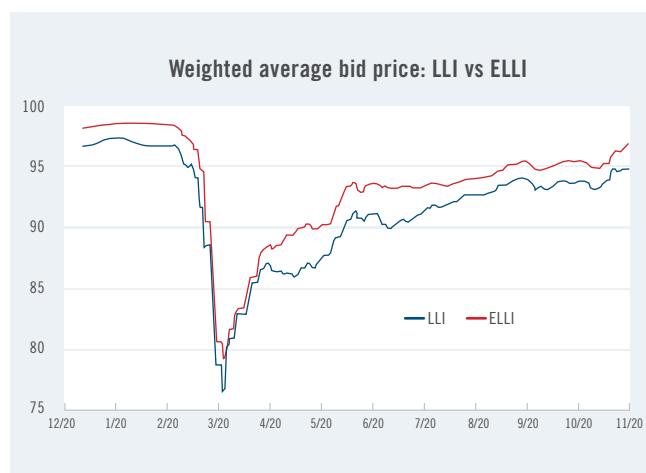
What Just
Happened?
What Lies Ahead?



ROPES & GRAY

2020: WHAT JUST HAPPENED?

- **Jan. 29:** first COVID-19 case in UK
- **Feb. 14:** first COVID-19 death in Europe
- **Feb. 23:** Italy placed in lockdown
- **Mar:** LLI / ELLI dropped to lowest point (see diagram)
- **Mar. 11:** pandemic declared by WHO. UK budget statement, including £12 billion emergency support package
- **Mar. 17:** France placed in lockdown. UK announced £330 billion government-backed loans, £20 billion tax cuts/grants
- **Mar. 19:** GBP to USD fell to 1.14
- **Mar. 20:** UK furlough scheme (80% wages) announced
- **Mar. 23:** UK placed in lockdown
- **Mar. 25:** US announced \$2 trillion rescue package
- **Mar. 27:** TUI received €1.8 billion KfW loan commitment
- **Apr. 10:** US Federal Reserve announced \$2.3 billion support package
- **Apr. 20:** US oil price fell below zero
- **May 18:** €500 billion German-French scheme announced to aid European recovery
- **Jun. 1:** lockdown eased in UK. Lufthansa accepted €9 billion German state aid package
- **Jun. 9:** French €15 billion aerospace aid package announced
- **Jun. 18:** £100 billion Bank of England stimulus announced
- **Jun. 22:** Cineworld agreed new \$250m secured debt facility
- **Jun. 26:** Corporate Insolvency and Governance Act (CIGA) entered into force
- **Jul. 5:** £1.57 billion UK arts industry support announced
- **Jul. 8:** £30 billion UK plan announced to support employment, including £1,000 employee retention bonus and 'eat out to help out'
- **Jul. 21:** €750 billion EU pandemic recovery fund announced
- **Jul. 30:** parts of northern England placed in local lockdowns
- **Aug. 4:** £1.3 billion UK green economic recovery funding
- **Aug. 5:** Gold price broke \$2,000/oz
- **Aug. 12:** TUI received €1.2 billion KfW financing package
- **Aug. 24:** Hema B.V. scheme of arrangement sanctioned
- **Sept. 2:** Virgin Atlantic Airways Part 26A Restructuring Plan sanctioned
- **Sept. 3:** €100 billion recovery package announced in France
- **Sept. 11:** Hema B.V. debt-for-equity swap approved by Dutch court
- **Sept. 21:** English pubs ordered to close at 10pm. Fear of second lockdown triggered £50 billion loss from FTSE 100



S&P Global Market Intelligence, Leveraged Finance & High Yield, "European distressed debt opportunities underwhelm in 2020" (25 Nov, 2020), Isabell Witt (accessed at <https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/european-distressed-debt-opportunities-underwhelm-in-2020-61439909>)

- **Oct. 23:** New Look scheme of arrangement sanctioned
- **Oct. 25:** Italy placed under second lockdown restrictions. Spain declared nationwide state of emergency
- **Oct. 27:** Selecta Group scheme of arrangement sanctioned
- **Oct. 28:** France and Germany placed under month-long lockdowns
- **Oct. 29:** Pizza Express Part 26A Restructuring Plan sanctioned
- **Oct. 30:** WHO declared Europe as epicentre of pandemic
- **Oct. 31:** England placed under month-long lockdown
- **Nov. 3:** US presidential election
- **Nov. 5:** UK furlough scheme extended to March 2021. KCA Deutag scheme of arrangement sanctioned
- **Nov. 16:** Moderna vaccine announced
- **Nov. 18:** Pfizer vaccine announced
- **Nov. 23:** Cineworld agreed new \$450m debt facility
- **Dec. 2:** UK approved Pfizer vaccine. TUI received €1.8 billion KfW financing package
- **Dec. 8:** UK administered first dose of Pfizer vaccine
- **Dec. 11:** Swissport scheme of arrangement sanctioned
- **Dec. 19:** London and South East England placed under tier 4 (local lockdown) restrictions
- **Dec. 20:** France closed borders to freight from the UK, and various countries worldwide announced travel restrictions to and from the UK
- **Dec. 24:** UK-EU agreed Trade and Cooperation Agreement
- **Dec. 27:** \$900 billion US coronavirus pandemic aid package announced
- **Dec. 30:** UK approved Oxford vaccine

2020: ENGLISH INSOLVENCY LAW REFORM

The Corporate Insolvency and Governance Act (CIGA), which came into force on 26 June 2020, introduced the most significant changes to English insolvency law in a generation. It introduced three permanent changes and implemented temporary measures to support businesses affected by the COVID-19 pandemic.

- The permanent changes provided welcome additions to the English pre-insolvency framework. We expect to see the increased use of these tools in 2021 and the courts to work through uncertainties in application (e.g., judicial views on the as-yet-untested cross-class cram-down feature in the Part 26A Restructuring Plan).
- For companies facing difficulties arising from the COVID-19 pandemic, the temporary changes have created much-needed breathing space, buying time for companies to get through the worst of the pandemic. However, with the pandemic—and economic recovery—lasting longer than initial projections, many companies have now accumulated debt in excess of their going concern value. Once the temporary measures expire, and if no further support is provided to these companies, we expect to see increased use of restructuring and insolvency processes, including the new Part 26A Restructuring Plan and the new Dutch and German Schemes (see page 7).

Permanent changes

'Free-standing' moratorium

- Provides formal **breathing space** for a company to pursue a rescue plan: applies for 20 business days (extendable for 20 business days; court and creditor consent required for further extensions up to max. 1 year).
- **Payment holiday** from *some* pre-moratorium debts and **protection from enforcement actions**.
 - Bank and most bond debt is excluded.
- **Debtor-in-possession process**, supervised by a monitor (licensed insolvency practitioner) who must assess whether rescue of the company as a going concern is likely.

New Part 26A Restructuring Plan

- **Similar to existing English scheme**, with three key differences:
 - '**Cross-class cram-down**', provided that dissenting creditors are no worse off than in the alternative scenario and that the plan is fair and reasonable;
 - **No numerosity** requirement: approval of a plan requires only the support of 75% by value within each class; and
 - Requires that a company **has experienced, or is likely to experience, financial difficulties** that affect or will or may affect its ability to continue operations as a going concern.
- **No DIP financing ability**: although new financing could be proposed pursuant to the terms of the restructuring plan itself.

Prohibition on enforcing ipso facto clauses

- Preserves insolvent company's supply contracts to aid rescue plan: suppliers of goods and services **barred from enforcing ipso facto (termination) clauses**.
- Prohibits suppliers from increasing pricing or introducing new payment terms.

Temporary changes

Suspension of the application of certain **wrongful trading provisions** from 26 November 2020 until 30 April 2021 (previous suspension from 1 March 2020 expired on 30 September 2020 and was reintroduced).

Suspension of winding-up proceedings commenced on basis of **statutory demands** until 31 March 2021.

Suspension of **winding-up proceedings** triggered by cash-flow insolvency, where pandemic has caused relevant financial difficulties, until 31 March 2021.

Deferrals to certain **company filings** until the earlier of 30 September 2020 and 12 months from the end of the company's accounting period.

Relaxations to **company law framework**: certain general meetings may be convened electronically and on an extended time frame, until 30 March 2021.

2020: INSOLVENCY LAW IN FRANCE AND GERMANY

Many countries have implemented their own temporary relief measures in response to the COVID-19 pandemic, suspending directors' duties and filing obligations and/or suspending company law requirements relating to reporting and general meetings.

Germany

The German Parliament proposed a bill in late 2020, which was then passed and came into force on 1 January 2021. The bill brought significant changes to the German restructuring and insolvency landscape. The bill (called by its acronym "SanInsFoG") implemented certain COVID-19 related mitigation measures (including extending the suspension of the obligation to file for insolvency) and introduced for the first time in Germany a pre-insolvency procedure ("StaRUG-Scheme," see further on page 7).

- Strict filing obligation (on basis of illiquidity¹ or overindebtedness²) suspended until 31 January 2021, if a company has applied for, or was eligible for, state aid between 1 November 2020 and 31 December 2020. Eligibility for state aid is assumed by law, unless it is evident that the state aid criteria could not be met by the company, or the state aid available for the company is evidently insufficient to overcome a company's illiquidity or overindebtedness.
- Overindebtedness test has been amended:
 - Business forecast period now set at 12 months.
 - Between 1 January 2021 and 31 December 2021, the overindebtedness forecast period has been reduced from 12 months to 4 months, provided that the overindebtedness resulted from the COVID-19 pandemic (assumed by law if (i) by 31 December 2019 the company was not illiquid, (ii) in the financial year ending prior to 1 January 2020 the company was cash-flow positive, and (iii) revenues declined in 2020 by more than 30%).
- If the above criteria could not be met, and after 31 January 2021, the obligation to file for insolvency (re-)applies.

France

- No suspension of wrongful trading or other directors' duties in response to the COVID-19 pandemic, subject to the modified insolvency test (see below).
- 45-day filing obligation for insolvency was suspended between 12 March 2020 and 23 August 2020 (suspension now expired).
- Amendments to certain insolvency proceedings, including:
 - For conciliation proceedings, (i) coercive tools to force standstill on creditors, available until 31 December 2020; and (ii) extension of max. duration by 10 months for proceedings opened between 24 August 2020 and 31 December 2021.
 - For expedited safeguard and expedited financial safeguard, a waiver of threshold conditions for opening proceedings until 31 December 2021.
- Temporary company law measures were also introduced to permit:
 - deferrals of certain company filing obligations; and
 - convening of shareholders' and board meetings by telephone, video-conference or written consultation, until 1 April 2021.

¹ Company is unable to make payments as they become due.

² Company's assets no longer cover existing liabilities.

2020: COVID-19 SUPPORT MEASURES

- Governments have provided unprecedented support to companies through financial and operational measures during the COVID-19 pandemic (key measures that remain available are summarised below). However, certain businesses have struggled to access the support available. For example, certain companies without strong working relationships with eligible banks have reportedly been unable to obtain CLBILS loans.
- The economic and operational support measures have provided relief to many companies, enabling them to continue operating and retaining employees. The consequence of these measures, together with certain stakeholders injecting new capital to address liquidity concerns, is that many businesses have continued to trade and are likely to find that they are over-levered in 2021. Addressing these leverage issues, especially once the temporary changes mentioned on page 3 and below expire, will be a common theme of 2021. Government-backed loans will also add a new dynamic to certain restructurings with government entities as new stakeholders.

Economic stimulus measures

Germany

- Entrepreneur loan of up to €100 million per company group. Loan amount limited to the higher of: max. 25% annual turnover in 2019; double wage costs in 2019; current financing arrangements for next 12 months (18 months for SMEs); or 50% of company's total debt / 30% of the balance sheet total of the group in case of loans exceeding €25 million. KfW assumes 80% risk for large companies (90% for SMEs). Loans must be used for business purposes only, e.g. working capital financing or investments (acquisition of assets including shareholdings). Re-financing and dividend distribution, among others, is not permitted during the term of the loan.³
- KfW also directly participates in syndicate financing (term up to six years): assume 80% risk up to 50% total debt or 30% of balance sheet total. KfW portion of loan amount (min. €25 million) limited on same basis as entrepreneur loan (excl. 50% total debt / 30% of balance sheet total criteria). Purpose of loan and non-permitted actions similar to entrepreneur loan.
- Schemes available until 30 June 2021.

France

- €300 billion state guarantee scheme on new loans (70% for large companies with >€5 billion of turnover / 90% for SMEs). No principal repayment for at least a 12-month period (option to amortise over additional 1 to 5 years).
- Main terms of eligible loans: (i) max. amount limited to 3 months turnover; (ii) no other security or guarantee securing the loan; and (iii) drawn until 30 June 2021.

UK

- CLBILS 80% guarantee on loans up to £200 million for companies with >£250 million turnover (£25 million for companies with >£45 million turnover).
- Scheme available until 31 March 2021.

EU has

temporarily loosened state aid rules until 30 June 2021.

Operational measures: assistance for employees

UK

- Lower of £2,500 or 80% of salary per month.
- Extended to end April 2021.

France

- *Chômage partiel* ('partial employment'):
 - For employees: 70% gross salary (84% net salary) until 31 January 2021 / 60% gross salary (employer top-up to 100%) until end of 2021.
 - For employers: partial refund of indemnity paid to employees equal to 70% of employee's gross salary until 31 January 2021 / 36% of employee's gross salary until end of 2021, up to 4.5x minimum wage.

Germany

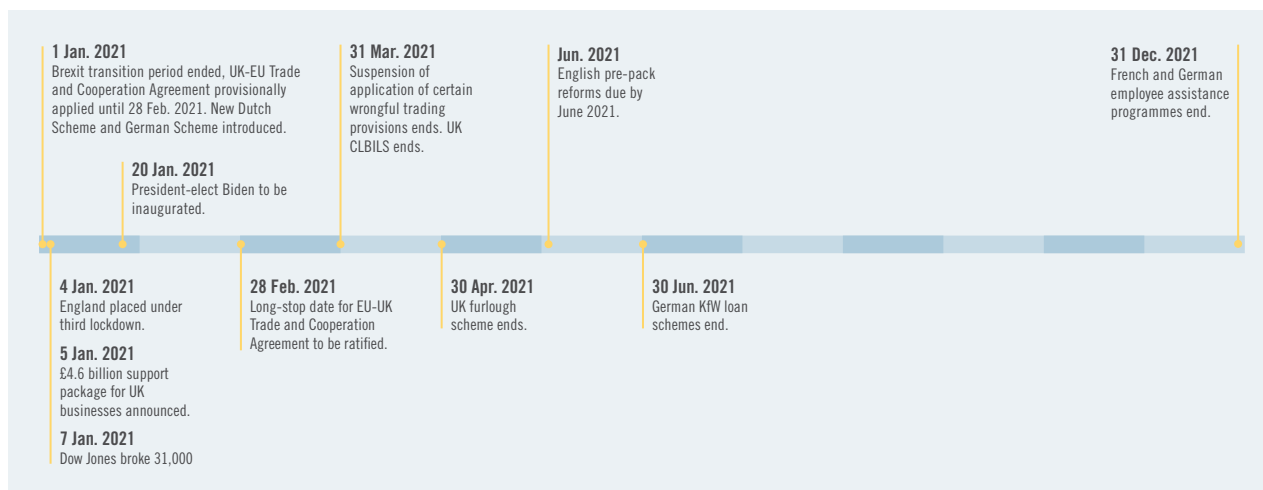
- *Kurzarbeit* ('part-time work'): 60% of net salary shortfall (67% if a child lives in the employee's household; rises after four months to 70% / 77% if an employee is working 50% or less of previous hours and up to 80% / 87% after first six months).
- Extended to end 2021.

³ KfW also assumes 100% risk for loans of smaller companies that existed at January 2019: loan amount up to 25% annual turnover in 2019, max. €300,000 for companies with up to 10 employees (€500,000 / max. 50 employees; €800,000 / over 50 employees). Loan purpose similar to entrepreneur loan; company required to made a profit on average from 2017 to 2019 or in 2019.

2021: UK

Key dates for 2021

(as at 11 Jan. 2021)



UK: pre-pack reform

- A **'pre-pack'** is a prepackaged sale of the whole or part of a company's business or its assets by an administrator to a NewCo. It can also be combined with an English scheme of arrangement or Part 26A Restructuring Plan.
- Pre-packs have become **increasingly popular** in recent years due to the ability to execute the pre-pack quickly once a deal has been agreed. This enables business operations to continue and also limits the process's impact on the brand and operations.
- Pre-packs have historically faced criticism due to **lack of transparency** and **lack of inclusivity**. Under certain circumstances, they can **prejudice certain creditor groups**, especially unsecured creditors.
- **New laws** are due by June 2021 that will increase scrutiny in relation to connected party transactions.
 - Sale to a connected party will require mandatory independent scrutiny or advanced creditor approval.
- We expect that the popularity of pre-packs will remain after the proposed pre-pack reforms, but in a more **robust and transparent** form. The increased scrutiny will, however, add a layer of **complexity**, with preparation for a pre-pack likely taking longer than under the existing regime.

UK: Brexit impact on insolvency law

- The UK-EU Trade and Cooperation Agreement does not include provisions in relation to cross-border insolvency law. We expect the consequences of Brexit on restructuring and insolvency to become clearer over the coming months, and further guidance or legislation may materialize, but the current situation is that:
 - *Coordination of proceedings*: the Recast Insolvency Regulation, which provided for the coordination of proceedings in cross-border insolvencies in the EU (including the UK), will no longer apply.
 - *Cross-border recognition of judgments*: automatic recognition of judgments between the EU and the UK is no longer available. Instead, companies using an English restructuring or insolvency process will need to seek recognition in relevant EU jurisdictions, or even open parallel proceedings in relevant EU jurisdictions, adding cost and complexity to the process.

2021: DUTCH AND GERMAN SCHEMES AND THE RISE OF EU FORUM SHOPPING?

The Netherlands and Germany introduced new pre-insolvency tools on 1 January 2021, frequently referred to as the Dutch scheme and the German scheme. Taking inspiration from Chapter 11 and the English scheme of arrangement, these tools enable companies to address financial difficulties without filing for formal insolvency.

In England and Wales, the Part 26A Restructuring Plan was introduced in June 2020 to ensure that English courts would continue to have a competitive edge in restructurings, providing a cross-class cram-down mechanism for companies to utilise. We expect that, in 2021, forum shopping will be a key theme, with companies having more options for completing their restructuring and being able to choose between the Netherlands, Germany, other EU jurisdictions and England and Wales. It is likely that differences in interpretation across jurisdictions of certain new features such as cross-class cram-down and/or valuation will be determinative for companies in choosing which forum to use. In the short term, another determinative factor may be that the English judiciary interprets the English Part 26A Restructuring Plan by reference to existing English scheme law precedent. This means that the English Part 26A Restructuring Plan will provide more certainty to debtors as to whether the restructuring plan will be approved than may be the case in the Dutch and German schemes, which will initially have no precedent to refer to.

	Chapter 11	Part 26A Restructuring Plan	Dutch Scheme	German Scheme
Basis for jurisdiction	Asset in the United States	Sufficient connection	COMI (public); sufficient connection (non-public)	COMI
Debtor-in-possession	Yes	Yes	Yes	Yes
Court involvement	Heavy	Medium	Light	Light (level optional)
Required majority in class	2/3 in value or majority in number of allowed claims	75% in value	2/3 in value	75% in value
Cross-class cram-down	Yes	Yes	Yes	Yes
Absolute priority rule⁴	Yes	No	Yes (Dutch twist ⁵)	Relaxed
Moratorium	Yes	Limited	Yes	Yes (max. 8 months)
Threshold for commencement: (likely to) experience financial difficulties	No; option for DIP financing only if company does face difficulties	Yes	Yes	Yes (imminent illiquidity, i.e., overwhelming risk of becoming illiquid within 24 months)
Effect of process on contracts	May terminate contracts; prohibition on enforcing ipso facto ⁶ clause	CIGA has introduced prohibition on enforcing ipso facto clauses in supply contracts	May amend or terminate contracts; prohibition on enforcing ipso facto clauses	Prohibition on enforcing ipso facto clauses
Cross-border recognition	No; foreign subsidiaries of a company typically file concurrent proceedings	Private International Law / US Chapter 15	Insolvency Regulation (public); Private International Law / US Chapter 15 (non-public)	Insolvency Regulation (public); Private International Law / US Chapter 15 (non-public)

⁴ Absolute priority rule governs order of payment. Senior classes must be paid in full ahead of junior classes and/or shareholders.

⁵ Dutch Twist: may depart from Absolute Priority Rule provided that (1) at least one in the money class accepts the plan; (2) there are reasonable grounds for deviation, and the plan is fair and reasonable and not detrimental to rejecting class; and (3) the rejecting class that would have been in the money on liquidation offered cash-out (secured creditors and / or creditors providing new money are not eligible for the cash-out option).

⁶ Ipso facto clauses are provisions in an agreement that permit its termination due to the bankruptcy, insolvency or financial condition of a party.

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