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2022 International Insolvency & Restructuring Symposium

Shall We Dance?

Presented by ABI

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Bankruptcy and Other Methods for the Resolution of Mass Claims

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American Bankruptcy Institute

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Presenters

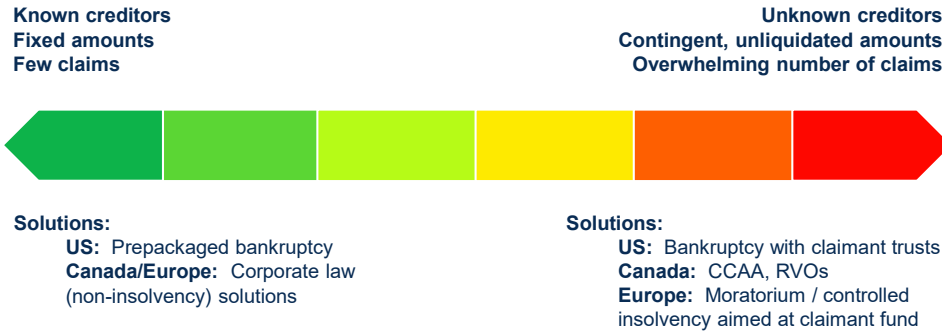
- **Paul H. Zumbro, Moderator**
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The Claim Continuum



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Mass Claim Issues

- Fair and equitable treatment of similarly situated claimants
- Present claims vs. future claims
- Preservation of value
- Resolution of claims against multiple entities (debtors and non-debtors)

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Mass Claim Solutions in the United States

- **Class Action**
 - Commonality requirement

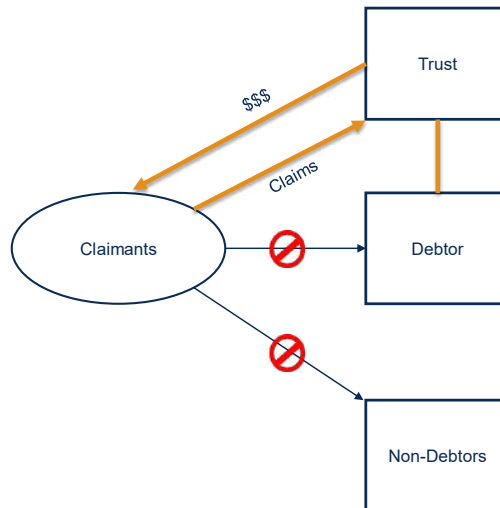
- **Multi-District Litigation (“MDLs”)**
 - Only consolidates pre-trial proceedings
 - Trials result in disparate outcomes for similarly situated claimants
 - Attempts at global settlements suffer from holdout problem

- **Bankruptcy**
 - Collective forum for resolution of all claims against the debtor
 - Requirement of equal treatment for similarly situated claimants (present and future)
 - Ability to bind the minority

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Mass Claim Solutions in the United States: 524(g) Trusts

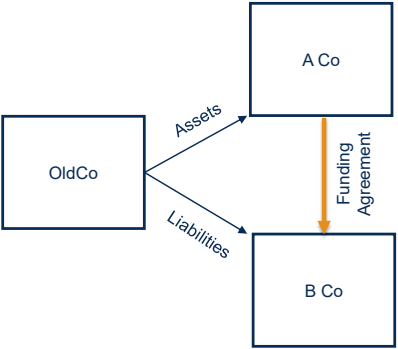
- Trust owns the reorganized debtor
- All claims channeled to the trust
- Streamlined process through agreed-upon trust distribution procedures (“TDPs”)
- 75% of voting claimants must approve the plan
- Explicitly applicable to asbestos context; courts split on non-debtor releases in other contexts



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Mass Claim Solutions in the United States: Texas Two-Step

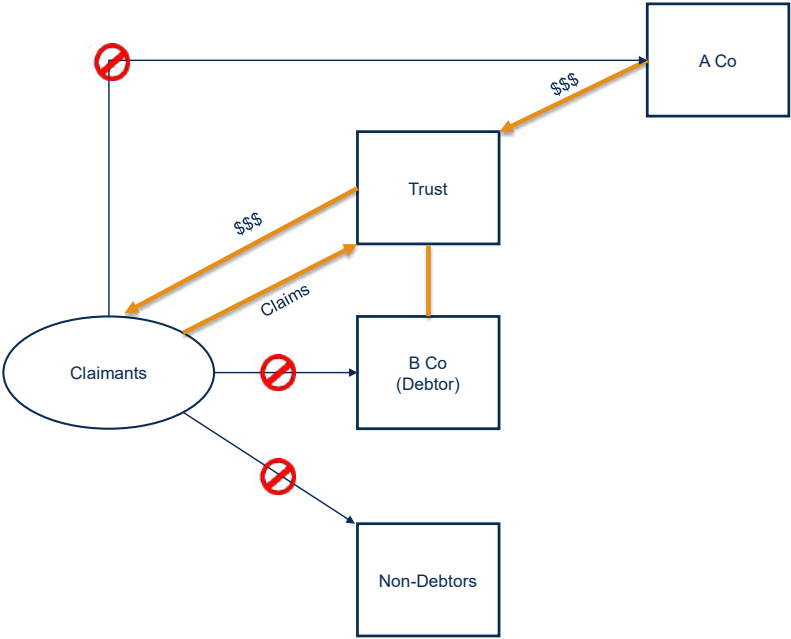
▪ Step 1: Divisional Merger



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Mass Claim Solutions in the United States: Texas Two-Step

▪ Step 2: B Co files chapter 11, establishes 524(g) trust to be funded by A Co



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Canada: Reverse Vesting Order

▪ Vesting Order

- Court-authorized sale of assets free and clear of any security, charge or other restriction.
- Existed prior to being codified.
- Now used in CCAA, BIA proceedings and receiverships.

▪ Reverse Vesting Order

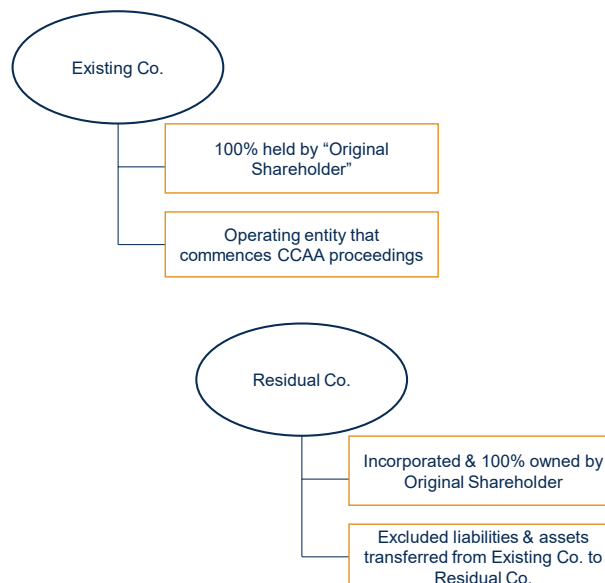
- Court-authorized purchase of debtor's shares and "vesting out" from the debtor to a new company, of *unwanted* assets, obligations and liabilities.
- Not dealt with specifically under CCAA or BIA, however, issuance of RVO jurisprudentially considered a valid exercise of Court's discretion to achieve CCAA objectives (*Nemaska Lithium Inc., Re*).

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Canada: Reverse Vesting Order

▪ Typical Structure of RVO

- New corporation is incorporated: "ResidualCo."
- ResidualCo is added as a debtor in CCAA proceedings.
- Unwanted liabilities, assets and contracts are transferred to ResidualCo.
- Shares of the original debtor are sold to purchaser free and clear of liabilities.

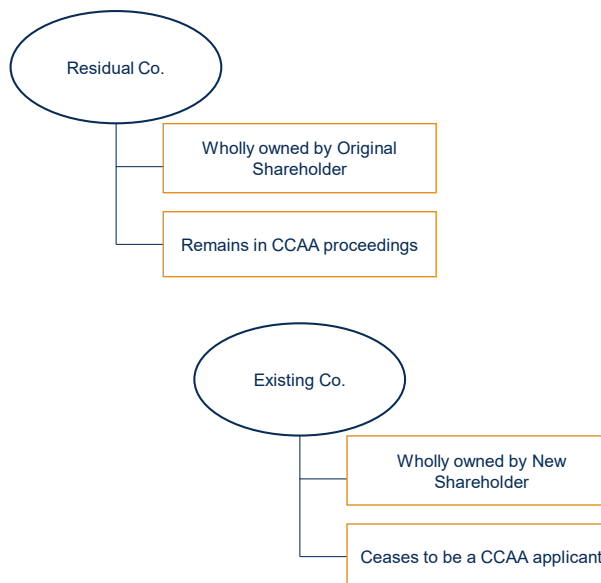


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Canada: Reverse Vesting Order

▪ Result of RVO

- Original debtor emerges from CCAA
- Creditors of the original debtor now have claims against ResidualCo within CCAA
- ResidualCo is placed in bankruptcy or files a plan of arrangement



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Canada: Reverse Vesting Order

▪ An RVO shares the typical advantages of a share deal over an asset purchase:

- Non-transferable licences and permits may be maintained.
- Tax attributes may be preserved.
- Complex corporate structures may be maintained.
- Contracts need not be assigned.
- Employees will continue to be employed – no requirement for employment letters / offers.

▪ An RVO has advantages over a plan of arrangement under the CCAA:

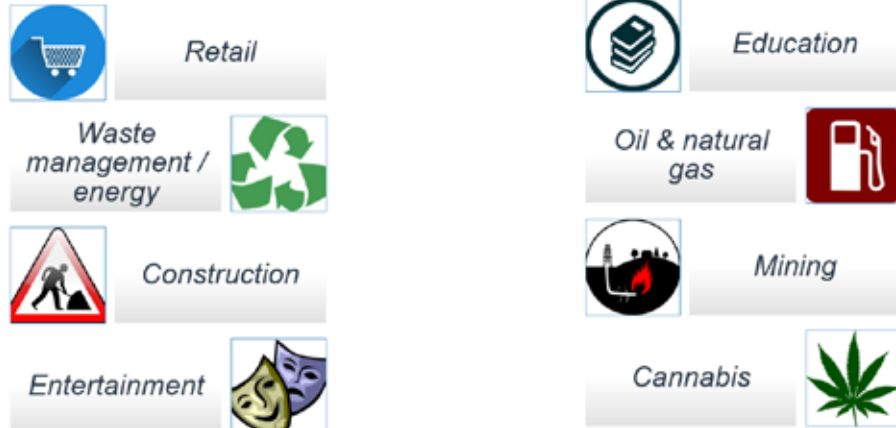
- Speed – no need to conduct a claims process or file a plan of arrangement.
- No creditor vote is required.
- Can be achieved even when there is no residual value for unsecured creditors, i.e., where no plan of arrangement could be filed.

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Canada: Reverse Vesting Order

▪ RVO: History

- RVOs have been granted in a variety of sectors mentioned below, with the majority being in the cannabis and mining sector:



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Canada: Reverse Vesting Order

▪ Legal Test for RVOs

- In *Harte Gold Corp. Re*, the Ontario Superior Court of Justice laid down the framework of questions to be addressed by the debtor, purchaser and the court-appointed Monitor:



Why is the RVO necessary in this case?



Does the RVO structure produce an economic result at least as favorable as any other viable alternative?



Is any stakeholder worse off under the RVO structure than they would have been under any other viable alternative?



Does the consideration being paid for the debtor's business reflect the importance and value being preserved under the RVO structure?

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Canada: Reverse Vesting Order

Legal Test for RVOs

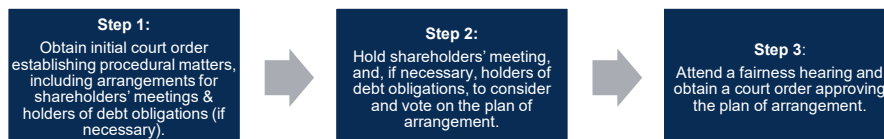
- There are additional considerations that Courts examine while granting an RVO (*Harte Gold Corp. Re*):



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Canada: Plans of Arrangement: CBCA

- Plans of arrangement have increasingly attracted the attention of corporations seeking to restructure debt, usually in connection with a more comprehensive balance sheet restructuring.
- CBCA permits reorganization of both debt and equity, hence, it can assist corporations in restructuring their debt outside of insolvency statutes such as the CCAA.
- Less expensive as compared to a CCAA restructuring and is likely to involve fewer stakeholders and professionals.
- Under s. 192 of the CBCA an arrangement typically proceeds in three steps:



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Mass Claim Solutions in Canada

- Canada's approach to mass tort insolvencies is mainly driven by needs and realities of individual cases.
 - Non-debtor third party releases: Commonly used tool by courts as a part of global resolution of all suits and claims under CCAA insolvency proceedings.
 - The Canadian system for handling large insolvencies, including mass tort cases, remains far less codified than its American contemporary in Chapter 11 of the Bankruptcy Code.
 - CCAA's flexibility has provided appropriate means to tackle exceptional situations, especially in mass tort litigations.
 - Recognition provisions in the CCAA promote deference to orders issued by foreign courts, provided those orders are consistent with the CCAA's purposes.
 - RVOs are yet to be issued in cases involving mass tort claims.
- **Red Cross - Canada's first mass tort insolvency case**
 - Canadian Red Cross Society faced with tainted blood scandal in the late 90s.
 - First CCAA case involving appointment of representative counsel for tort claimants.
 - Legitimized use of a CCAA insolvency process to resolve mass tort & class litigation.
 - Canada's blood system was successfully transferred to new authorities.

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Mass Claim Solutions in Europe

- **Class Action**
 - Commonality requirement
 - Collective Redress Directive (EU) 2020/1828: *consumer claims* in ALL EU Member States
 - Aims at consumers recovering monetary damage, not punitive. Other environment
 - Claims vehicle tried and tested (Neth)
 - No individual action if represented
 - Opt-out or opt-in – but very effective nevertheless
 - Netherlands already forum of choice with Collective Redress Schemes (WAMCA 2020)
 - Scope includes privacy infringements, human rights violations, other
 - Stay on individual action. Also *future* claimants in Neth. with time bar on opt-out
 - Jurisdiction Dutch courts over EU defendants, and judgment recognized in EU
- **Bankruptcy as liability management instrument**
 - Not typically used
 - Background: Chapter 11-like restructuring schemes fairly recent in most EU countries
 - However: key features helpful in US are similarly helpful in EU:
 - Efficiency – Collective forum for resolution of all claims against the debtor
 - Equality – not first come, first serve, but mandatory coordinated resolution
 - Finality – ability to bind minority, no opt out, so no hold out
 - Equality & finality – equal treatment for future claimants

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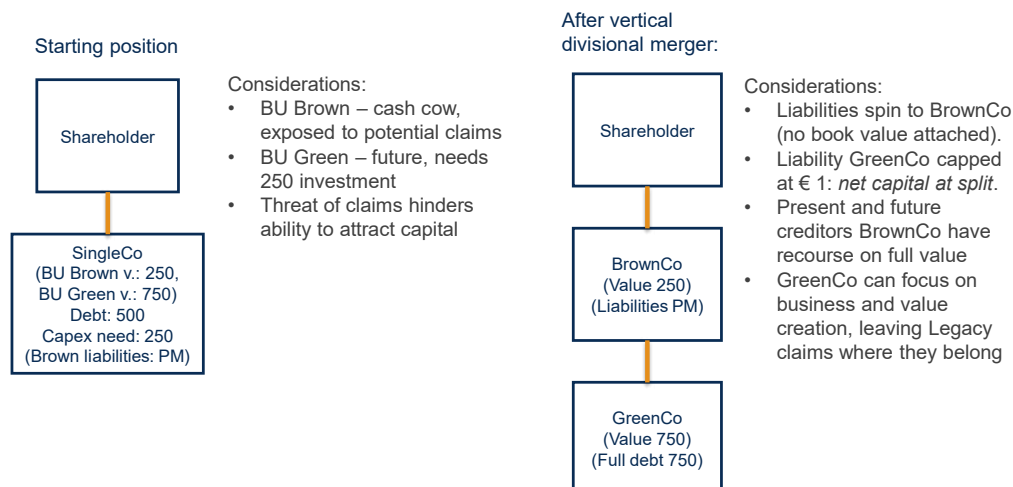
Mass Claim Solutions in Europe: Parallel to the Trust?

- **Tort claims irreconcilable with using bankruptcy as an instrument?**
 - No. Legitimacy to mitigate impact on business continuity
 - Balancing act between creditor interest and value creation for all
- **40+ years of pushing boundaries in Chapter 11 helps:** Channeling injunction and NDRs not in EU
- **But trust structure not alien to EU:**
 - Single forum exists in EU collective redress schemes
 - Release debtor and replace with a new instrument issued by a newco ('trust')
 - Testing of structure in court (not always in tort context) comes down to same considerations:
 - are all affected debts in scope / ancillary to restructuring (i.e. recovery on debtor unpaid debts)
 - necessary to ensure effectiveness
 - instrument reflecting economic value
 - sufficient information to assess position
 - Helpful precedents both in continental Europe and in UK
 - Overall: fair (legitimate interest / avoiding temporal disparity), equitable, fits statutory framework
- **We need more time on NDRs**
 - Legitimacy? No standing, unless for same loss.
 - No insolvency non-debtor, due process?
 - Will likely start only as process, if not artificial.
 - Guarantees, D&O, buyer/financier probably ok. Others "contributing to the plan" not.
- **Added flexibility in divisive merger: EU may well be ahead of US on the first step of the 'dance'**

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Mass Claim Solutions in Europe: Example of a 3M or LTL

- **Long way from insolvency, but need to start thinking in scenarios**



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Mass Claim Solutions in Europe: Example of a 3M or LTL

▪ When reasonable prospect of insolvency BrownCo (if ever)

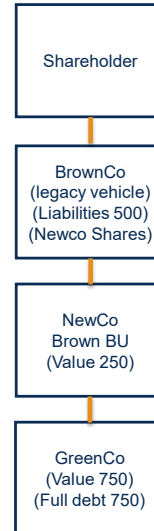
- Dutch Scheme or classical insolvency moratorium with stay on enforcement and litigation
- Negotiate Restructuring plan with claimants representatives and others, incl pay-out mechanism
- Maybe put claimants in a separate class, also if not needed, to add voice and standing

• Plan:

- The BrownCo business is put aside in a separate newco
- Management moves with business, debtor becomes ring-fenced settlement vehicle
- Creditors retain recourse on business value, but liabilities and ongoing litigation do not bring down business value (only impact shareholder value)
- Pay-out regime established on all claims (equitable, not necessarily one size fits all)
- Financing can be raised against shares if cash needed.
- Claimants get full value of the business, including future earnings
- Residual value, if any, flows to shareholders

• Test by the court (briefly put):

- 2/3 majority in one class: can also be banks, financiers, claimants.
- Best interest of creditors test: should be easy if full value flows to claimants.
- Absolute Priority Rule: in cross-class cram down or up
- Has the light insolvency test been met?
- Is the outcome of the plan reasonable and fair?



• NB: also significant potential for (listed) shareholder claims in a debt restructuring setting

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Faculty

Hon. Robert D. Drain is a retired U.S. Bankruptcy Judge for the Southern District of New York in White Plains, currently serving on recall as a mediator in the Puerto Rico Electric Power Authority PROMESA case. At the time of his appointment in 2002, he was a partner in the Bankruptcy Department of the New York law firm of Paul, Weiss, Rifkind, Wharton & Garrison, where he represented debtors, trustees, secured and unsecured creditors, official and unofficial creditors committees, and buyers of distressed businesses and distressed debt in chapter 11 cases, out-of-court restructurings and bankruptcy-related litigation and also was actively involved in several transnational insolvency matters. Judge Drain is a Fellow of the American College of Bankruptcy and an ABI Board member. He also is a member of the International Insolvency Institute, a member and former Secretary of the National Conference of Bankruptcy Judges, and a founding member and chair of the Judicial Insolvency Network. For several years, Judge Drain chaired the Bankruptcy Judges Advisory Group established through the Administrative Office of the U.S. Courts and was appointed to the FDIC's Systemic Resolution Advisory Committee through Dec. 31, 2024. He also was an adjunct professor for several years at St. John's University School of Law's LL.M. in Bankruptcy Program and currently is an adjunct professor at Pace University School of Law, and he has lectured and written on numerous bankruptcy-related topics. Judge Drain presided over such chapter 11 cases as *Loral*, *RCN*, *Cornerstone*, *Refco*, *Allegiance Telecom*, *Delphi*, *Coudert Brothers*, *Frontier Airlines*, *Star Tribune*, *Reader's Digest*, *A&P*, *Hostess Brands*, *Christian Brothers*, *Momentive*, *Cenveo*, *21st Century Oncology*, *Tops*, *G A&T*, *Sears*, *Standard Amusements (Playland)*, *Full Beauty Brands*, *Sungard*, *Windstream*, *Purdue Pharma*, *Jason Industries*, *OneWeb* and *Frontier Communications*, as well as many mid-sized and small chapter 11 cases and an active consumer docket. He also has presided over the ancillary or plenary cases of *Corporacion Durango*, *Satellites Mexicanas*, *Par-malat S. p. A.* and its affiliated United States debtors, *Varig S.A.*, *Yukos (II)*, *SphinX*, *Galvex Steel*, *TBS Shipping*, *Excel Maritime*, *Nautilus*, *Landsbanki Islands*, *Roust* and *Ultrapetrol*. Judge Drain has served as the court-appointed mediator in a number of chapter 11 cases, including *New Page*, *Cengage*, *Quicksilver*, *Advanta*, *LightSquared*, *Molycorp*, *Breitbart Energy* and *China Fishery*. He also authored a novel, *The Great Work in the United States of America*. Judge Drain received his B.A. *cum laude* from Yale University and his J.D. from Columbia University School of Law, where he was a Harlan Fiske Stone Scholar for three years.

Ferdinand Hengst is a corporate partner with De Brauw Blackstone Westbroek N.V. in Amsterdam, The Netherlands, and specialises in international debt restructuring, corporate recovery and special situations financing deals. His broad practice encompasses both tailor-made finance deals and insolvency-sensitive transactions or litigation, always in a cross-border context. Mr. Hengst advises boards of directors on their corporate governance, fiduciary duties and liability considerations around funding and scenario planning in a more stressed environment. He is a Fellow of INSOL International, a member of INSOLAD, and regularly publishes on restructuring and insolvency, leveraged financing and corporate recovery. In addition, he is a member of De Brauw's Diversity committee and heads De Brauw's Africa practice. Mr. Hengst was educated at the University of Groningen, London Business School, Tufts University and Chinese University of Hong Kong.

Natasha MacParland is a partner in the Toronto office of Davies Ward Phillips & Vineberg LLP, where she provides clients with solutions for their high-end insolvency and restructuring challenges. She advises on a broad variety of debt-restructuring, bankruptcy and insolvency, corporate debtor/creditor rights enforcement, turnarounds, workouts, and plans of arrangement under the Companies' Creditors Arrangement Act. Ms. MacParland has advised on many significant and groundbreaking restructurings and insolvencies. She is frequently consulted for strategic advice and risk analysis on deal-structuring and lending, and she regularly acts for a number of North America's best-known private-equity firms in their acquisitions of distressed entities and participation in distressed sales and investor solicitation processes. Ms. MacParland is a longstanding board member of the Insolvency Institute of Canada. She is a member of ABI, the Insolvency Institute of Canada, INSOL International, the International Insolvency Association, the International Women's Insolvency & Restructuring Confederation, the Ontario Bar Association and the Turnaround Management Association. Ms. MacParland has been listed in *Chambers Global*, *Chambers Canada* and the *IFLR1000*, among others, and she received the Turnaround Management Association's Women of Excellence Award, Today's Leader in 2019. She received her B.A. in political science and commerce in 1994 from Memorial University of Newfoundland and her LL.B. in 1997 from Dalhousie University.

Paul H. Zumbro is a partner in Cravath, Swaine & Moore LLP's Corporate Department in New York and heads the firm's Financial Restructuring & Reorganization practice. His practice focuses on restructuring transactions and related financings, both in and out of court, as well as on bankruptcy M&A transactions. Mr. Zumbro recently represented PG&E in one of the largest and most complex bankruptcy cases in U.S. history to fairly and efficiently resolve liabilities resulting from the 2017 and 2018 Northern California wildfires. He also represented The Weinstein Co. (TWC) in its voluntary petition for chapter 11 bankruptcy. Under Mr. Zumbro's leadership, Cravath's FR&R practice was named a 2020 and 2019 Practice Group of the Year by *Law360*, and Cravath was named the 2019 "Restructuring Advisory Firm of the Year" by *The Deal*. Mr. Zumbro received his B.A. *cum laude* and with distinction from Yale College in 1992 and his J.D. from Columbia Law School in 1997, where he was a Harlan Fiske Stone Scholar.