INSOL INTERNATIONAL

# ESG IN RESTRUCTURING

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**ISBN: 978-1-907764-36-3**

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# PRESIDENT'S INTRODUCTION

Environmental, social and governance (ESG) issues are rapidly changing the way that business is conducted across the world. We are witnessing new regulations on climate change, biodiversity and environmental conservation, modern slavery and workers' rights and board accountability, conflicts and stakeholder engagement.

More broadly, we are also seeing a change in social attitudes, and a growing expectation from financiers, insurers, investors and customers that the businesses they deal with must behave in a responsible and ethical manner.

These dynamic regulatory, social and economic changes will inevitably drive future restructuring activity, as companies seek to align their operational structures and business models with improved governance, labour protection, social justice goals and the reality of a net zero emissions economy and the necessity of a greener footprint.

At the same time, however, the evolution of social and economic settings – and the dominant focus on ESG – raises the question as to whether existing restructuring and insolvency laws adequately protect and uphold environmental obligations, employee entitlements and workplace health and safety obligations, and hold directors and other officers to account in relation to their responsibilities to the company and its stakeholders.

There is a delicate balancing act between the protection of these interests and the underlying assumption that restructuring and insolvency processes ought to maximise value for the collective body of creditors – and in some cases, the respective policy concerns of ESG issues and restructuring and insolvency law and practice may conflict.

This has been apparent in the controversial "Texas Two-Step" option canvassed in recent United States case law (under which it has been proposed for tort liabilities to be spun off to a new corporate entity that undergoes a restructure), as well as non-consensual third party releases and, in some jurisdictions, the potential for an insolvent entity to disclaim or otherwise evade liability for its environmental obligations.

This new publication from INSOL International – *ESG in Restructuring* – therefore comes at an important time. Project Leaders Clayton Chong and Smitha Menon, from WongPartnership, canvass the policy motivations of ESG and insolvency and restructuring law and practice, and consider the regulatory standards, soft law frameworks and practices concerning key ESG issues outlined by esteemed practitioners and academics in 31 jurisdictions.

The Project Leaders consider the manner in which restructuring law and practice may be shaped to deal with incredibly complex and emerging ESG issues – particularly environmental responsibilities, labour protection and board accountability – that can have far-reaching impacts on vulnerable claimants and broader society. They provide a "roadmap" of issues that regulators and policy makers may consider in shaping future law reform.

This book is an invaluable contribution to law reform and regulatory and policy development as we strive to ensure that restructuring and insolvency laws are modern, progressive and "fit for purpose" in relation to the underlying economic and social circumstances in which they operate.

# PRESIDENT'S INTRODUCTION cont.

The book also highlights important practical issues for our members to be aware of in addressing a multitude of ESG issues in the course of an insolvency appointment. Uniquely, the book also analyses recent market developments and trends in the ESG refinancing sphere, with the aim of serving as a useful "one stop" resource for financial institutions considering the provision of finance to entities (in good times and in the event of financial distress) in the context of complex and evolving ESG obligations and liabilities.

I express my sincere thank you to the Project Leaders, and each of the jurisdictional contributors, for their significant expertise, time and commitment in completing this project over the last 12 months, as well as to our team of INSOL International technical and administrative staff for their efforts in bringing the project to fruition.

I hope you enjoy reading this publication and will find it useful in your future pursuits.

**Scott Atkins**
President & INSOL Fellow
INSOL International

September 2023

## 1. Introduction

Environmental, social and governance (ESG) issues are becoming increasingly important in the restructuring world.

In recent years, restructuring proceedings have been used to resolve a wide spectrum of ESG-related liabilities, including claims arising from wildfires,[1] carcinogenic baby powder,[2] opioid addiction and overdose,[3] sexual abuse[4] and the mis-selling of loans.[5] These types of restructurings call for special consideration by policymakers. The claimants involved are often involuntary creditors. Unlike, say, a bank or supplier that can assess the insolvency risk of a company before extending credit (and safeguard itself against such risk), a tort claimant has no choice in the matter. Because ESG-related liabilities do not have priority or preference under most jurisdictions' laws, many ESG claimants are left severely disadvantaged in a restructuring or insolvency of a company.

Even when a restructuring does not involve ESG-related liabilities, a host of other ESG-related matters, such as labour issues and conflicts of interests, are bound to arise.

Policymakers and practitioners should think about how to better deal with ESG matters in restructurings.

From a policymaker's perspective, this is crucial because restructuring laws have an upstream effect on the way that companies behave while they are solvent. Indeed, we discuss below insightful empirical research which identifies that companies have decreased their pollution activities as a consequence of environmentally friendly court rulings. In that sense, restructuring laws can be shaped to make companies more ESG-conscious.

There is also an economic incentive for policymakers to think about ESG, as stronger ESG performance is correlated with stronger corporate financial performance, lower credit risk, better credit ratings and lower cost of capital.[6]

From a practitioner's perspective, ESG is important because institutional investors and creditors are increasingly attuned to ESG concerns. ESG risks (financial and reputational) affect financiers' appetites for injecting fresh capital and restructuring existing debt in distressed businesses. Credit ratings agencies such as Moody's and Standard and Poor's also now directly integrate ESG risk assessment in their credit ratings,[7] which ultimately makes capital costlier for companies with greater ESG risk. These factors will influence whether a restructuring succeeds or not – and they also influence whether a company becomes a candidate for restructuring in the first place as companies with greater ESG risk will increasingly face higher operating costs, more expensive capital and lower profit margins.

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1 *In re PG&E Corporation*, Bankruptcy Case No. 19-30088 (DM) (US Bankruptcy Court for the Northern District of California, San Francisco Division).

2 *In re LTL Management, LLC,* 58 F.4th 738 (US Court of Appeals, Third Circuit).

3 *In re Purdue Pharma, LP,* 635 BR 26 (US District Court, Southern District of New York).

4 *In re Boy Scouts of America*, No. 20-10343 (US Bankruptcy Court for the District of Delaware); *In re USA Gymnastics*, No. 18-09108-RLM-11 (US Bankruptcy Court for the Southern District of Indiana).

5 *Re All Scheme Limited* [2021] EWHC 1401, [2022] EWHC 1318, [2022] EWHC 549 (England and Wales, High Court of Justice).

6 G Friede, T Busch and A Bassen, "ESG and Financial Performance: Aggregated Evidence from More than 2000 Empirical Studies" (2015) 5(4) *Journal of Sustainable Finance & Investment* 210-233; G Inderst and F Stewart, "Incorporating Environmental, Social and Governance Factors into Fixed Income Investment" World Bank (2018); W Henisz and J McGlinch, "ESG, Material Credit Events and Credit Risk" (2019) 31(2) *Journal of Applied Corporate Finance* 105-117; I Oikonomou, C Brooks and S Pavelin, "The Effects of Corporate Social Performance on the Cost of Corporate Debt and Credit Ratings", *Financial Review*, 49-75.

7 Moody's, ESG Credit and Sustainable Finance, accessible at https://www.moodys.com/newsandevents/topics/ESG-Credit-00702C (last viewed on 14 April 2023); S&P Global, ESG in Credit Ratings, accessible at https://www.spglobal.com/ratings/en/research-insights/special-reports/esg-in-credit-ratings (last viewed on 14 April 2023).

This report aims to serve both policymakers and practitioners. We have undertaken a cross-jurisdictional survey on key ESG issues that intersect with restructuring law. In doing so, we have compiled a series of jurisdictional reports authored by esteemed and experienced academics and practitioners relating to the selected issues. These reports provide the foundation for analysing the practices and standards across jurisdictions. Based on these reports, we provide a "roadmap" of issues which policymakers can consider if they are undertaking policy reviews. The jurisdictional reports also synthesise market developments and trends in the ESG-financing sphere to serve as a useful "one-stop" resource for financial institutions in the restructuring space.

## 2. Scope of research and impetus

In this study, we have selected some of the more pressing issues in which the fields of ESG and restructuring intersect. The questions are grouped (horizontally in the table below) according to each of the following themes:

- the restructuring of liabilities (broadly with a focus on the limitations or conditions imposed in relation to the restructuring of ESG-related liabilities);
- the protection of stakeholder interests (relating to advocacy of environmental and social interests and managing governance conflicts of interest in a restructuring); and
- "soft law" frameworks (relating to non-legally binding instruments such as industry guidelines and best practices that serve to guide or influence conduct on ESG-related matters in a restructuring).

A mix of "hard" and "soft" law issues were selected to encourage a more holistic consideration of the ways that ESG issues can be addressed in a restructuring. Non-binding "soft law" instruments can be a useful precursor to formal legislation by shaping restructuring practice and instilling among entities what is expected of them in the market – including from their customers and other stakeholders.

The ESG questions selected for this project are summarised in the table below.

| Topic | Environmental | Social | Governance |
|---|---|---|---|
| **Restructuring of liabilities** | Can environmental liabilities be restructured and, if so, what restrictions or conditions apply? | Can health and safety-related liabilities be restructured and, if so, what restrictions or conditions apply? | Can a restructuring plan provide for third party releases in favour of directors and officers of the company and, if so, what restrictions or conditions apply? |
| **Protection of stakeholder interests** | Do environmental protection authorities or environmental advocacy groups have standing to air their views / concerns in a restructuring, and to what extent can the courts or the relevant approving bodies consider environmental issues in deciding whether to approve a restructuring plan? | Do labour authorities, unions or employee / worker advocacy groups have standing to air their views / concerns in a restructuring, and to what extent can the courts or the relevant approving bodies consider labour issues in deciding whether to approve a restructuring plan? | How are board / management conflicts addressed in a restructuring, e.g. in situations where board / management receive benefits under a restructuring plan (such as shares under a management incentive plan)? |

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| **"Soft law" framework** | What industry guidelines and/or best practices are prescribed for the protection of the environment in a restructuring? | What industry guidelines and/or best practices are prescribed for the protection of employee rights in a restructuring? | What industry guidelines or codes of conduct are restructuring professionals (including formal officeholders and financial advisers) subject to? |
| **ESG in financing** | What market developments, trends, or experiences in the ESG-financing space have you observed in your jurisdiction (either generally or specific to the restructuring context)? | | |

The impetus for some of these questions arises from controversial restructurings which have caught the wider public's attention.

For example, the question on the restructuring of health and safety liabilities[8] was spurred by the attempted restructuring by Johnson & Johnson (J&J) of its talc-related liabilities.[9] J&J was alleged to have caused ovarian and lung cancer due to the presence of asbestos in its talc-based baby powder. J&J faced over 38,000 lawsuits relating to these claims. With mounting payouts and litigation costs, J&J attempted to restructure under Chapter 11 of the United States Bankruptcy Code, invoking a controversial technique called the "Texas Two-Step" process. This involved J&J spinning off its talc liabilities into a new entity through a divisional merger (i.e. splitting the business) under Texas law and then restructuring the new entity bearing the talc liabilities. The stated goal of this approach was to isolate the talc liabilities in a new subsidiary so that it did not have to subject the entire operating enterprise to bankruptcy proceedings.

The move drew strong criticism, even leading a group of law professors to file an *amicus curiae* brief objecting to the restructuring and labelling the strategy "a novel and dangerous tactic that represents a significant departure from the use of Chapter 11 to validly reorganise financially troubled businesses", as they perceived J&J to be "us[ing] Chapter 11 as a tool to shield assets from the claims of their victims."[10]

The Chapter 11 proceedings were eventually dismissed in January 2023 by an appellate court.[11] Somewhat ironically,[12] the basis for the dismissal was that the restructuring entity, LTL Management LLC (LTL), was not considered to be in financial distress. This was on the basis that LTL was backstopped by a funding agreement with its J&J parent which it could draw on to pay its talc liabilities. The court held that financial distress was a necessary pre-requisite for Chapter 11 proceedings as it ensured the claimants' pre-bankruptcy remedies (particularly the right to a jury trial to prove their claims) were disrupted only when necessary. Absent financial distress, the Chapter 11 proceedings did not serve a valid bankruptcy purpose and failed for lack of good faith. Paradoxically, this ruling might have created perverse incentives for those attempting the "Texas

8 See in the table above – i.e. "can health and safety-related liabilities be restructured and, if so, what restrictions or conditions apply?"

9 *In re LTL Management, LLC*, 58 F.4th 738 (2023) (US Court of Appeals, Third Circuit).

10 See e.g. *In re LTL Management, LLC*, Case No. 21-30589 (MBK), *Memorandum of Law of Amici Curiae by Certain Law Professors in Support of Motion of the Official Committee of Talc Claimants to Dismiss Debtor's Chapter 11 Case*.

11 *In re LTL Management, LLC*, 58 F.4th 738 (2023) (US Court of Appeals, Third Circuit). At the time of writing, J&J has said that it intends to appeal to the US Supreme Court to overturn the Third Circuit's ruling: see D Knauth, "J&J to Seek US Supreme Court Review on Unit's Bankruptcy", *Reuters*, 23 March 2023, accessible at: https://www.reuters.com/legal/jj-seek-us-supreme-court-review-units-bankruptcy-2023-03-22/ (last viewed on 19 May 2023).

12 The court observed: "We do not duck an apparent irony: that J&J's triple A-rated payment obligation for LTL's liabilities, which it views as a generous protection it was never required to provide to claimants, weakened LTL's case to be in bankruptcy. Put another way, the bigger a backstop a parent company provides a subsidiary, the less fit that subsidiary is to file. But when the backstop provides ample financial support to a debtor who then seeks shelter in a system designed to protect those without it, we see this perceived incongruity dispelled" – see *In re LTL Management, LLC*, 58 F.4th 738 (2023) (US Court of Appeals, Third Circuit).

Two-Step" to provide *less* financial support to a spun-off entity in order to meet the financial distress requirement, opening the door to the potential for abuse of vulnerable claimants since there might be fewer assets to meet their claims.

In fact, some of these concerns may have already materialised. J&J launched a second attempt at restructuring in April 2023, with new, less robust financing arrangements aimed at putting LTL in a position of financial distress. Instead of the ultimate J&J parent providing the funding for LTL's talc liabilities, the new backstop funder is LTL's immediate holding company (an entity with a much weaker balance sheet than J&J). To support its position that it is financially distressed, LTL pointed to the fact that its immediate holding company had transferred its consumer health business (which represented a substantial portion of its assets) prior to its second Chapter 11 filing.[13] One commentator has called J&J's revived restructuring attempt "a rather audacious ploy" and said that "such cynical strategic machinations to manufacture self-inflicted financial distress hardly bolster the case for a legitimate, good faith resort to bankruptcy relief".[14] J&J / LTL's second attempt at a Chapter 11 restructuring has since been dismissed by the US Bankruptcy Court, which found that LTL was not sufficiently financially distressed to avail itself of bankruptcy as the revised funding backstop agreement was still more than adequate to cover the projected near term and aggregate talc liabilities of LTL.[15] At the time of writing, J&J / LTL have announced that they will appeal the court's ruling.[16]

Purdue Pharma's Chapter 11 restructuring[17] was another high-profile matter that provided the impetus for one of the questions for this research report, namely whether third party releases in favour of directors or officers of a company are allowed under a restructuring plan.[18] Purdue Pharma has been widely blamed for playing a major role in the opioid addiction crisis in the United States through its aggressive marketing of its painkiller, OxyContin. It was alleged to have downplayed the addictive potential of OxyContin and to have encouraged the prescription of the drug to a broader range of patients than appropriate. Purdue Pharma faced thousands of lawsuits by claimants who had become addicted to OxyContin and by the estates of addicts who had overdosed on OxyContin.

One of the controversial aspects of Purdue Pharma's Chapter 11 restructuring plan was the provision of third party releases (also known as "non-debtor releases") in favour of various members of the Sackler family, who were the owners of Purdue Pharma, and several of whom also served as officers, directors and managers of the company. The Sackler family faced personal liability for their role in Purdue Pharma's marketing of OxyContin.

Prior to Purdue Pharma's bankruptcy, the Sackler family upstreamed some US $10.4 billion out of the company, significant portions of which were invested in offshore companies or deposited into trusts that could not be reached in bankruptcy. Under Purdue Pharma's Chapter 11 plan, the Sackler family agreed to contribute approximately US $4.3 billion to a fund that would be used to resolve public and private civil claims, as well as civil and criminal settlements with the Federal Government. In exchange, the Sackler family required broad releases under the plan that would release them from a wide range of claims (including breaches of fiduciary duties, fraudulent

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13 *In re LTL Management, LLC*, Case No. 23-12825 (MBK), *Declaration of John K. Kim in Support of First Day Pleadings* at paragraphs 78 to 85.

14 D C Weiss, "Johnson & Johnson Tries Once Again to Settle Talc Claims Through 'Texas Two-Step' Bankruptcy", *ABA Journal* (online), 7 April 2023, accessible at https://www.abajournal.com/news/article/jj-tries-once-again-to-settle-talc-claims-through-texas-two-step-bankruptcy (last viewed on 19 May 2023).

15 *In re LTL Management, LLC,* 2023 Bankr. LEXIS 1884 (US Bankruptcy Court for the District of New Jersey) at page 25.

16 LTL Management LLC press release, "Johnson & Johnson Subsidiary to Appeal Bankruptcy Court Ruling that Deprived Talc Claimants of an Equitable and Efficient Resolution", accessible at https://ltlmanagementinformation.com/wp-content/uploads/2023/07/Johnson-Johnson-Subsidiary-to-Appeal-Bankruptcy-Court-Ruling-that-Deprived-Talc-Claimants-of-an-Equitable-and-Efficient-Resolution.pdf (last viewed on 7 August 2023).

17 *In re Purdue Pharma, LP*, 635 BR 26 (US District Court, Southern District of New York).

18 See in the table above – i.e. "can a restructuring plan provide for third party releases in favour of directors and officers of the company and, if so, what restrictions or conditions apply?"

conveyances, breaches of state laws relating to unfair trade practices and consumer protection laws).

The plan was overwhelmingly supported by Purdue Pharma's creditors, with some 120,000 votes cast on the plan and over 95% of those voting in the aggregate supporting the plan. The plan was also confirmed (albeit reluctantly) by the Honourable Judge Drain of the United States Bankruptcy Court for the Southern District of New York, with Judge Drain lamenting that the outcome was a "bitter result" and how it was "frustrating … that it is so difficult to hold board members and controlling shareholders liable for their corporation's conduct."

However, that was not the end of the matter, as various parties appealed to the United States District Court for the Southern District of New York against the confirmation of the plan, with the main objection being the broad releases granted to the Sackler family under the plan. The appellants included the United States Trustee in Bankruptcy (the government official who supervises the administration of bankruptcy cases) and several states which brought civil claims against Purdue Pharma for breaches of consumer protection laws. After extensive consideration of the statutory and case law, the appellate court in a "blockbuster ruling"[19] decided that there was no statutory authority under the Bankruptcy Code that permitted the non-consensual releases of third-party claims against non-debtors (apart from asbestos cases where the statute expressly authorises non-debtor releases). The court accordingly vacated the order confirming the plan.

Subsequently, there was yet another appeal to the United States Court of Appeals for the Second Circuit. In another twist of events, the District Court's ruling was overturned and the original confirmation of the reorganisation plan by the Bankruptcy Court was upheld. While the appeal was pending, eight states – California, Connecticut, Delaware, Maryland, Oregon, Rhode Island, Vermont, and Washington – and the District of Columbia that had appealed the confirmation of the original settlement, entered into a new settlement agreement with Purdue Pharma and the Sackler family that provided for an additional US $1.175 to $1.675 billion in contributions from the Sackler family (resulting in an aggregate US $5.5 to $6 billion contribution to the plan). As part of the revised settlement agreement, they agreed to withdraw their opposition to the plan.[20]

The Second Circuit held that the imposition of non-debtor releases was permissible as the Bankruptcy Code[21] gives bankruptcy courts broad equitable power to carry out the objectives of the Code and to include appropriate provisions in a plan, so long as those provisions are not inconsistent with other sections of the Bankruptcy Code. Nevertheless, the court acknowledged that there is a heightened potential for abuse posed by non-debtor releases, and it accordingly set out a list of factors that bankruptcy courts should consider before endorsing releases, including: (i) whether the scope of the releases sought is appropriate; (ii) whether the non-debtor contributes substantial assets to the reorganisation; (iii) whether the impacted class of creditors overwhelmingly support the plan; and (iv) whether the plan provides for the fair payment of enjoined claims. The Second Circuit ultimately decided that the Bankruptcy Court's detailed findings supported approval of the plan under the factors laid out.

The Purdue Pharma and J&J cases show how – in the context of rapidly evolving social and economic changes and developments – restructuring law and practice is itself now facing deeply complex problems which can have far-reaching implications on society. As the Second Circuit's opinion in Purdue Pharma astutely observes in its opening paragraph:

> Bankruptcy is inherently a creature of competing interests, compromises, and less-than-perfect outcomes. Because of these defining characteristics, total satisfaction of all that is owed – whether in money or in justice – rarely occurs. When a bankruptcy is the result of mass tort litigation against the debtor, the complexities are magnified because the debts owed are wide-ranging and the harm caused goes beyond the financial. That is the circumstance here.

19 L Simon, "Bankruptcy Grifters" (2022) 131 *Yale Law Journal* 1154.
20 *In re Purdue Pharma, LP*, Case no. 22-110-bk (L) (US Court of Appeals, Second Circuit).
21 Specifically, § 105(a) read with § 1123(b)(6).

There are difficult policy choices involved in deciding how restructuring laws can be shaped to better deal with these problems.

For example, how would allowing third party releases affect the behaviour and decision-making of companies, boards, management and shareholders in the future? Echoing Judge Drain's remarks in the Purdue Pharma case, would it make it even more difficult to hold board members and controlling shareholders liable for their corporation's conduct? In particular, where the corporation's conduct implicates wider societal concerns such as health and safety of the community, should stricter rules apply to deter unwanted corporate behaviour? On the other hand, perhaps the overwhelming support for the plan reflects the claimants' begrudging acceptance of the reality of the situation – that having a plan (which sees the owners returning substantial sums of money) might be better than having no plan at all (and facing the prospect of years long litigation that may not prove fruitful).

The balancing of these competing policy considerations requires careful deliberation by policymakers. By studying the selected research topics, it is hoped that this book can provide some impetus and direction to policymakers considering ESG reforms in the sphere of restructuring law.

## 3. Key policy considerations

Before analysing the findings from the jurisdictional reports, it is helpful to provide a brief overview of some key policy considerations when balancing ESG and restructuring interests. These policy themes apply to many of the research questions considered in this project.

The benefits of an effective restructuring framework are well understood and accepted in the current era. The restructuring of economically viable businesses helps to maximise the value of the debtor and improve the returns for creditors, compared to the alternative of liquidating the debtor's assets. Restructuring viable businesses protects employment and preserves technical know-how, skills, goodwill and business relations of the debtor that might otherwise be lost in a liquidation.[22]

Some ESG matters, such as the protection of employees' rights and ensuring good corporative governance of the debtor-in-possession, are generally consistent and aligned with the policy objectives of restructuring law.

However, in other cases, there are added layers of complexity, where a choice has to be made between giving primacy to ESG interests or to the interests of ordinary creditors. A clear example where this problem can arise is when an insolvent company owes significant environmental liabilities, such as fines or clean-up costs. If these liabilities have priority over other debts under the law, it will likely reduce the recovery which other creditors would expect to receive in a restructuring. In essence, the policy issue is how the value of the restructured business should be allocated or divided among the creditors of the company.

The "polluter pays" principle in environmental law is the notion that the party responsible for causing pollution should be the one that pays the costs to remediate the effects of the pollution.[23] However, when the polluter is insolvent, the burden lies on the *creditors* of the polluter, as any costs spent to clean up the pollution will correspondingly reduce the assets that are available to the creditors. The real question in insolvency situations is not whether "polluter pays", but rather whether "creditors pay".

One view is that the burden should not be placed on creditors, and that it should be left to the State to bear any shortfall in environmental costs that cannot be recovered from the estate. The State has greater financial resources at its disposal than the creditors of the company and is better

22 See, for example, the EU Restructuring Directive (Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks, on discharge of debt and disqualifications, and on measures to increase the efficiency of procedures concerning restructuring, insolvency and discharge of debt, and amending directive (EU) 2017/1132).

23 A Keay and P de Prez, "Insolvency and Environmental Principles: A Case Study in a Conflict of Public Interests" (2001) 3(2) *Environmental Law Review* 90-112.

able to absorb the losses suffered.[24] From a moral perspective, it might also be thought to be unfair to impose the burden on creditors who might not have played any role in causing the pollution.

However, a "creditors pay" principle might better serve the protection of the environment. If creditors are potentially adversely affected by the environmental costs incurred by a debtor, they would be more hesitant to extend credit to a heavy-polluting borrower or might impose stricter monitoring conditions on the debtor. This in turn disincentivises borrowers from engaging in environmentally unfriendly behaviour and encourages capital to flow to borrowers that are more environmentally responsible. The concept of using the financial system (and, necessarily, the restructuring and insolvency system) as a lever for enabling environmental change[25] is no longer novel and underlies global efforts like the Network for Greening the Financial System and the United Nations Environment Programme's Net-Zero Banking Alliance.

Real world examples show how restructuring laws can have an effect on reducing pollution levels. Two studies have investigated the impact of the pro-environment 2009 United States court ruling in *United States v Apex Oil Company Inc*[26] (*Apex Oil*) by the Seventh Circuit Court of Appeals, and they reveal interesting insights.[27]

In *Apex Oil*, a company was ordered to clean up a contaminated site that was causing groundwater and air pollution as a result of past oil refinement activities. The company (more precisely, the predecessor of the company) had undergone Chapter 11 reorganisation proceedings prior to the clean-up order. The company argued that the Chapter 11 proceedings discharged the government's claim to seek a clean-up order against the company. The court dismissed the arguments, as the clean-up order was not a "claim" within the meaning of the United States Bankruptcy Code and could not be discharged through the restructuring. In order to constitute a "claim" under the Code, it was necessary for the claim to give rise to a right to payment. However, the environmental statute under which the clean-up order was issued, the Resource Conservation and Recovery Act (RCRA), did not authorise any form of monetary relief. Hence, the court ultimately ruled that the clean-up order was not discharged in the reorganisation and the company had to comply with the clean-up order post-reorganisation. Effectively, it gave the environmental obligations of the company *de facto* priority in the reorganisation.

After *Apex Oil*, it was observed that many companies and lenders changed their behaviour in response to the ruling. The *de facto* priority of RCRA environmental obligations meant that creditors of companies with RCRA-covered liabilities would have less assets available to meet their claims if the companies entered bankruptcy, and hence there was greater credit risk for the creditors. Empirical studies found that there was a significant decrease in the bond returns and a significant increase in the interest rates of bonds issued by heavy RCRA-polluters that were at greater risk of default. The loan spreads for heavy RCRA-polluters closer to bankruptcy widened appreciably following *Apex Oil*. Lenders imposed loan provisions giving them the right to inspect borrowers' facilities specifically for the purpose of assessing chemical safety handling. Most crucially, there was a decrease in the levels of pollutants released by companies affected by the ruling, with one study estimating a 12-30% reduction. In totality, these findings suggest that *Apex*

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24 See, for example, Report of the Review Committee on Insolvency Law and Practice (Cmnd 8558, 1982) (Cork Report). In recommending the abolition of Crown preference for unpaid tax, the Committee opined at paragraph 1410 that "a bad debt owed to the State is likely to be insignificant in terms of total Government receipts; the loss of a similar sum by a private creditor may cause substantial hardship and bring further insolvencies in its train."

25 Opening address by Mr Ravi Menon, Managing Director of the Monetary Authority of Singapore and Chair of the Network for Greening the Financial System, at the Green Swan Conference 2022, 31 May 2022, accessible at https://www.bis.org/review/r220602e.htm (last viewed on 14 April 2023).

26 *U.S. v. Apex Oil Co., Inc.*, 579 F.3d 734 (2009) (US Court of Appeals, Seventh Circuit).

27 M Ohlrogge, "Bankruptcy Claim Dischargeability and Public Externalities: Evidence from a Natural Experiment" (24 May 2022), available via SSRN at https://ssrn.com/abstract=3273486 or http://dx.doi.org/10.2139/ssrn.3273486; J Chen et al, "Environmental Liabilities, Borrowing Costs and Pollution Prevention Activities: The Nationwide Impact of the Apex Oil Ruling" (February 2022), NBER Working Paper No. w29740, available via SSRN at https://ssrn.com/abstract=4037010 or http://dx.doi.org/10.2139/ssrn.4037010.

*Oil* created financial incentives for lenders to pressure their borrowers to reduce emissions of pollutants, particularly for borrowers that were closer to bankruptcy.[28]

The key takeaway from the discussion above is that there is often a close interplay between ESG and restructuring policy interests. ESG and restructuring should not be viewed as separate silos. Rather, restructuring law can be shaped in order to promote ESG interests. Balancing the policy interests can be very difficult and might require trade-offs or compromises when those interests are in tension with one another. For example, a strong pro-environment stance under restructuring laws may make it more difficult for businesses to restructure,[29] may inhibit a company's access to finance (in good times and in bad) and may fail to adequately protect vulnerable creditors such as employees or small suppliers who are more at risk of suffering financial hardship if the debtor's assets have to be used to meet environmental obligations.[30]

With these considerations in mind, this book does not aim to prescribe a "one-size-fits-all" framework for addressing ESG issues in a restructuring. Rather, the book aims to analyse the practices and standards across jurisdictions and to provide a "roadmap" of issues which policymakers *may* elect to consider if they are undertaking policy reviews. Jurisdictions with unique models for addressing particular ESG issues are highlighted to provide policymakers with ready comparisons and options for their own law reform processes.

## 4. The restructuring of ESG-related liabilities

### 4.1 Environment (E): the restructuring of environmental liabilities

The first issue covered in this book is whether environmental liabilities, such as clean-up or remediation costs imposed by environmental regulations, can be restructured in the same way as ordinary debt claims, or if there are any special restrictions or conditions which apply when restructuring such liabilities.

Generally, most of the jurisdictions surveyed do not have any special restrictions or conditions for restructuring environmental liabilities *per se*. There are, however, several ways through which environmental liabilities *indirectly* receive protection in a restructuring.

Some jurisdictions give preferential treatment to government fines or statutory liabilities, which could encompass fines or statutory liabilities under environmental regulations. The effect is that any such types of environmental liabilities either cannot be restructured non-consensually or would be classified separately together with other preferential creditors for the purposes of a restructuring plan. In practice, this often leads to these environmental liabilities having priority over unsecured debts. Table 1 below summarises the laws in the relevant jurisdictions.

[28] M Ohlrogge, "Bankruptcy Claim Dischargeability and Public Externalities: Evidence from a Natural Experiment" (24 May 2022), available via SSRN at https://ssrn.com/abstract=3273486 or http://dx.doi.org/10.2139/ssrn.3273486; J Chen et al, "Environmental Liabilities, Borrowing Costs and Pollution Prevention Activities: The Nationwide Impact of the Apex Oil Ruling" (February 2022), NBER Working Paper No. w29740, available via SSRN at https://ssrn.com/abstract=4037010 or http://dx.doi.org/10.2139/ssrn.4037010.

[29] In *Apex Oil*, for example, the company argued that had it known when it declared bankruptcy that it might be liable for US $150 million in clean-up costs, it would have had to liquidate and could not have reorganised with such a huge debt overhanging it.

[30] E Vaccari, "A Modular Approach to Restructuring and Insolvency Law: Executory Contracts and Onerous Property in England and Italy" (2022) 31(5) *Norton Journal of Bankruptcy Law and Practice (West)*, article 3.

*Table 1: Restructuring environmental liabilities (preferential treatment to fines and statutory liabilities)*

| Jurisdiction | Summary |
|---|---|
| **Canada** | Orders and penalties issued by environmental regulators in the nature of fines, restitution orders or similar are not affected by a restructuring unless the proposal or plan explicitly provides for their compromise and the creditor in relation to that debt or liability votes in favour of the compromise.[31] |
| **Germany** | Certain debts, such as claims arising from tort and fines, are excluded from being restructured under a restructuring plan.[32] |
| **Hong Kong** | Statutory debts, which are debts of which the liability and the amount are determined by or under any provision in any Ordinance, are treated as preferential debts,[33] and may have to be classified separately for the purpose of a scheme of arrangement.[34] |
| **India** | India follows the principle of "absolute liability" when dealing with extremely hazardous waste or "inherently dangerous" activity, and it is quite likely that a court will find that such "absolute liability" (whether presently due or contingent in nature) cannot be restructured under a resolution plan.[35] |
| **Japan** | A restructuring plan may not provide for the reduction or release of administrative and criminal fines that arose prior to the commencement of a restructuring procedure.[36] |
| **Mexico** | Environmental liabilities caused before the bankruptcy proceeding will have the priority of tax claims, which means they will be paid after: (i) labour claims for wages and employee benefits for a period of two years preceding the date of the insolvency judgment; and (ii) secured claims. Tax claims cannot be restructured through a reorganisation agreement entered between the debtor and creditors – hence the debtor must request the authorities' remission of the debt if they are unable to pay it.[37] |
| **Spain** | Regulatory sanctions and penalties constitute public claims, which can only be subject to a restructuring plan if certain requirements are met. The Spanish Bankruptcy Law expressly bans the possibility of affecting public claims under a restructuring plan by: (i) reductions; (ii) a change of debtor; (iii) a modification or extinction of security; or (iv) debt for equity swaps or conversion of debt into profit participating loans or into any instruments of characteristics or rank other than those of the original one.<br><br>Consequently, a restructuring plan can only seek to stay a public claim. Such a stay is limited to a six month term (if a deferment on the affected public claims had been already granted prior to the approval of the plan) or to a 12 month term (if the affected public claims had not previously been deferred). Furthermore, a stay on public claims may only be proposed under a restructuring plan if the debtor certifies that it is up to date in the payment of tax and social security obligations. In practice, this means that only public |

31 Canada report, section 2.2.3.
32 German report, section 1.2.
33 Hong Kong report, section 2.1.2.
34 Hong Kong report, section 1.1.
35 India report, section 2.1.
36 Japan report, section 2.1.
37 Mexico report, section 2.1.

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| | claims that have not reached their maturity date or those that have been deferred (and not over two years) may be subject to a plan.[38] |
| **The Netherlands** | Certain environmental liabilities may qualify as estate claims in a bankruptcy procedure. In Dutch legal literature, there had been debate on the question whether environmental claims rank as estate claims. This debate has been settled largely in case law in recent years, as a result of which the general view is that environmental claims qualify as estate claims in a bankruptcy procedure, given that the bankruptcy trustee has to comply with environmental obligations. According to Dutch Supreme Court (*Hoge Raad*) case law, a bankruptcy trustee should comply with environmental requirements, regardless of the circumstances of the bankruptcy. If the bankruptcy trustee does not comply with these requirements, the failure is directly attributable to the bankruptcy trustee. Such claims then qualify as estate claims and will have priority over other claims. This reasoning is also followed by the Administrative Jurisdiction Division of the Council of State (*Afdeling bestuursrechtspraak van de Raad van State*) from an administrative law perspective and the Trade and Industry Appeals Tribunal (*College van Beroep voor het bedrijfsleven*).[39] |
| **United Arab Emirates** | Liabilities owed to government authorities (such as environmental fines) would constitute a preferred liability and would not be capable of being restructured without the approval of the relevant government authority.[40] |

Another way in which some jurisdictions protect environmental liabilities is by conferring security interests over a debtor's property to cover any clean-up costs incurred by governmental authorities to remedy the pollution or contamination caused by the debtor. The effect in these jurisdictions is that these environmental liabilities are treated as secured debts and would be classified separately under a restructuring plan, and would typically be given *de facto* priority under such a plan. This alternative is summarised in Table 2 below.

*Table 2: Restructuring environmental liabilities (security for clean-up costs)*

| Jurisdiction | Summary |
|---|---|
| **Australia** | Environmental legislation in Australia enables the environmental regulator to obtain financial assurances to cover clean-up costs. For example, the Protection of the Environment Operations Act 1997 (NSW) section 250(1)(h) enables a court to order an offender to provide to the Environment Protection Authority "a financial assurance, of a form and amount specified by the court … if the court orders the offender to carry out a specified work or programme for the restoration or enhancement of the environment." As a further example, Part 8.4 of the Environment Protection Act 2017 (Vic) allows the Environment Protection Authority to require a person undertaking a particular activity regulated by that Act to provide a financial assurance if the Authority is satisfied the assurance "is necessary as security for the costs and expenses of remediation or clean-up in connection with the particular activity."[41]<br><br>These provisions potentially allow the regulator to have a security interest over the company's property to secure the performance of its |

38 Spain report, section 2.1.3.
39 The Netherlands report, section 2.1.
40 United Arab Emirates report, section 2.1.
41 Australia report, section 2.1.2.

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| | environmental obligations. The regulator in whose favour the security has been given will have the rights of a secured creditor.[42]<br><br>Under a deed of company arrangement (one of the restructuring procedures in Australia), the rights of secured creditors to enforce their securities are not affected unless the deed says so and the creditor voted in favour of it. However, the court retains the power to limit the rights of secured creditors and owners and lessors of property if the court is satisfied that the enforcement of those rights would have a material adverse effect on the achievement of the purposes of the deed.[43] |
| **Canada** | Restructuring and insolvency legislation in Canada includes provisions addressing claims made by the federal and provincial governments for the costs associated with remedying environmental conditions or damage affecting real or immovable property of the debtor. The legislation provides security for those costs by conferring a charge on the affected real property and any contiguous real property that is related to the activity that caused the environmental condition or damage, which security ranks in priority ahead of any other security against the property in question.[44] |
| **Singapore** | Remediation or clean-up costs incurred by the environmental regulator are secured by a first charge on the premises in respect of which the costs and expenses were incurred, if the owner of the premises is liable to pay such costs and expenses.[45] Secured debts typically receive *de facto* priority under a restructuring plan in Singapore.[46] |

In some jurisdictions, certain types of environmental obligations, such as regulatory orders to clean up a contaminated site, cannot be restructured (i.e. they cannot be discharged or modified) under a restructuring plan as they are classified as non-monetary obligations. The *Apex Oil* ruling discussed above is an example of this, although it should be noted that the position in the United States differs from circuit to circuit.[47] Table 3 below summarises this alternative.

*Table 3: Restructuring environmental liabilities (non-dischargeability of non-monetary environmental obligations)*

| Jurisdiction | Summary |
|---|---|
| **Canada** | The Supreme Court of Canada ruled in *Orphan Well Association v Grant Thornton Ltd* that regulatory orders to reclaim abandoned oil wells[48] were not "provable claims" and therefore could not be compromised under a plan of arrangement under the Companies' Creditors Arrangement Act.[49] The regulatory orders were non-monetary obligations that were binding on the bankrupt estate and had to be complied with notwithstanding the consequences doing so might have for the bankrupt's secured creditors.[50] |

42 Australia report, section 2.1.2.
43 Australia report, section 1.2.1.
44 Canada report, section 2.2.2.
45 Singapore report, section 2.1.2.
46 Singapore report, section 1.1.
47 See above, n 27. See also Appendix B.4 for detailed discussion on cases from other circuits.
48 Reclamation involves plugging and capping oil wells to prevent leaks, dismantling surface structures and restoring the surface to its previous condition.
49 Canada report, sections 2.2.2 and 2.2.3; T Cumming, C Hanert and J Oliver, "The Intersection of Regulatory and Insolvency Law: Redwater's Final Chapter and the Aftermath" (2019) *Annual Review of Insolvency Law* 5, 34.
50 *Orphan Well Association v Grant Thornton Ltd* 2019 SCC 5, [160].

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| **Poland** | Non-monetary environmental claims, such as those resulting from an administrative decision imposing on the debtor an obligation to conduct remediation of the land or cease infringement, are not capable of being modified by a restructuring arrangement. Any modification of such environmental obligations will result in the court's refusal to approve the arrangement on the ground that it violates the law.[51] |

In jurisdictions where it is possible to disclaim (i.e. abandon) onerous property, [52] an additional issue for consideration is the extent to which environmental obligations can be disclaimed in a restructuring. The power of disclaimer allows an insolvency practitioner (usually a liquidator) to abandon property which is a substantial drain on the resources of the company. Traditionally, the main aim of disclaimer is to enable the insolvency practitioner to realise or dispose of onerous property without needlessly protracting a liquidation and diminishing the assets available for distribution to creditors.[53] Although disclaimer is a power that is usually limited to liquidation,[54] it can be deployed as part of an overall restructuring strategy. For example, it has been observed in the United Kingdom that some companies undergo administration proceedings to sell the profitable parts of a business before entering liquidation to enable the liquidators to disclaim onerous environmental liabilities.[55]

There is significant uncertainty among the jurisdictions surveyed regarding the extent to which property of a company which is subject to environmental clean-up obligations may be disclaimed, as summarised in the table below.

*Table 4: Restructuring environmental liabilities (disclaimer of environmental obligations)*

| Jurisdiction | Summary |
|---|---|
| **Canada** | The decision of the Supreme Court of Canada in *Orphan Well Association v Grant Thornton Ltd* has created significant uncertainty regarding the ability of a court officer to effectively disclaim contaminated property. The court concluded that the disclaimer power conferred upon the trustee by the Bankruptcy and Insolvency Act is only related to the personal liability of the trustee, and "says nothing about the liability of the 'bankrupt' or the 'estate'".[56] The result of a trustee's disclaimer of property where an environmental order has been made in relation to that property is that the trustee is protected from personal liability, while the ongoing liability of the bankrupt estate is unaffected.[57] |
| **Hong Kong** | The extent to which the disclaimer of onerous property may be used to relieve a company of its statutory environmental obligations is uncertain, given that there are no Hong Kong case authorities on this issue. The likely issues are whether environmental licences are treated as property of a company, and the tension between the polluter pays principle in |

51 Poland report, section 2.1.
52 BVI report, section 2.1.3; Canada report, section 2.2.3; Guernsey report, section 2.1.3; Hong Kong report, section 2.1.3; Nigeria report, section 2.1.3; Thailand report, section 2.1.3; United Arab Emirates report, section 2.1; Uganda report, section 2.1.3; India report, section 2.1.3; New Zealand report, section 2.1.1; Singapore report, section 2.1.3.
53 A Keay and P de Prez, "Insolvency and Environmental Principles: A Case Study in a Conflict of Public Interests" (2001) 3(2) *Environmental Law Review* 90-112; P Omar, "Disclaiming Onerous Property in Insolvency: A Comparative Study" (2010) 19 *International Insolvency Review* 41, 47.
54 However, in Singapore, it is also available in judicial management, which can be deployed as a restructuring procedure.
55 B Mamutse, "Environmental Liabilities in Insolvency – An Area Ripe for Reform?" (2016) 8(3) *International Journal of the Law in the Built Environment* 243.
56 Canada report, section 2.2.3.
57 *Orphan Well Association v Grant Thornton Ltd* 2019 SCC 5, [75].

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| | environmental law and the interests of creditors in an insolvency proceeding.[58] |
| **India** | Disclaimer under a corporate insolvency resolution process under the Insolvency and Bankruptcy Code 2016 is untested. The Code, in the first instance, requires that the corporate debtor must be restructured as a going concern. This means together with *all* its property. Therefore, in principle, the corporate insolvency resolution process does not allow disclaimer of a particular property. That said, recently a new provision has been added under which the resolution professional can sell assets of the debtor rather than sell the entire debtor but only if no bidder comes forth for the entire debtor. In such an instance, it is possible that bids are received for non-polluted assets, and the polluted assets are effectively disclaimed and left to liquidation.[59] |
| **Singapore** | Under a judicial management process, a judicial manager has the power to disclaim onerous property. In principle, onerous property could include property such as a plant or a factory which is subject to continuing and onerous environmental obligations that are to be performed over a substantial period of time and which will involve expenditure that may not be recovered. Where a judicial manager wishes to disclaim property that is subject to certain environmental laws, the judicial manager is required to notify the relevant regulator before issuing a notice of disclaimer. This ensures that the relevant regulatory authority has the opportunity to address any issues relating to the property under the relevant environmental legislation.<br><br>The extent to which the power of disclaimer may be used to relieve a company of its statutory environmental obligations is uncertain, as there are no reported decisions in Singapore relating to the issue. The Singapore disclaimer provisions are adopted from the United Kingdom, where there are conflicting decisions relating to the application of the disclaimer regime to environmental licences, centred around the issue of whether the interest in protecting the environment should take precedence over the interest in ensuring a fair and orderly insolvency proceeding.[60] |
| **Uganda** | Contracts may be disclaimed within a bankruptcy process with the approval of the court. To approve this, the court would need to be satisfied that this is necessary to enable the debtor to continue its business, or if disclaiming the contract would fulfil the interests of all the creditors of the debtor company and would not materially affect the interests of the counterparty concerned. Counterparties to disclaimed contracts would be entitled to prove in the process as an unsecured creditor.<br><br>In theory, the right to disclaim could be used in relation to an ESG related liability provided that such liability arose pursuant to a contract (as opposed to the liability arising as a matter of law or pursuant to a government imposed fine / order).[61] |

### 4.2 Social (S): restructuring of health and safety-related liabilities

The second issue studied in this project is whether there are any special restrictions or conditions which apply when restructuring health and safety-related liabilities.

58 Hong Kong report, section 2.1.3.
59 India report, section 2.1.3.
60 Singapore report, section 2.1.3.
61 Uganda report, section 2.1.3.

As with environmental liabilities, most jurisdictions surveyed do not impose special restrictions on health and safety-related liabilities. Generally, only employee-related health and safety liabilities, such as work injury compensation, receive preferential treatment under insolvency law. Such preferential employee-related health and safety liabilities either cannot be restructured non-consensually, or would be classified separately together with the debts of other preferential creditors for the purpose of a restructuring plan. This often leads to such health and safety-related liabilities having priority over unsecured debts. In the People's Republic of China and Russia, personal injury claims (not limited to the employment context) have priority under insolvency law as well. A summary is provided in Table 5 below.

*Table 5: Restructuring of health and safety-related liabilities (preferential treatment for health and safety liabilities)*

| Jurisdiction | Summary |
|---|---|
| **Argentina** | Health and safety-related liabilities that arise out of a labour relationship (occupational diseases and accidents at work) are given priority and considered secured claims in an insolvency proceeding. In addition, such labour creditors are entitled to collect their credits with a fast-track procedure named "*pronto pago*" in a restructuring proceeding.<br><br>The Argentine Supreme Court (in *re Pinturas y Revestimientos S.A. s/quiebra*) decided that the priorities regime under the Argentine Bankruptcy Law shall be integrated with the provisions of international treaties, and therefore general preferred labour claims shall have priority over any other general secured claim – in particular, over tax and social security claims.<br><br>Municipal fees imposed by competent authorities are considered secured claims and thus, probably, not included in the restructuring plan. Such creditors are entitled to file or continue any legal action seeking enforcement of their credit after judicial endorsement of the restructuring plan.[62] |
| **Australia** | With two exceptions, health and safety liabilities attract no specific priority under Australia's statutory restructuring regimes. First, amounts due in relation to injury compensation where the liability arose before the administration attract priority ahead of debts relating to leave, debts arising from employee retrenchment and unsecured creditors. Secondly, where a company was insured in relation to a liability to third parties (for example, liability insurance to cover employee injuries), the proceeds of any such policy must be paid to the third party in respect of whom the liability was incurred.[63] Creditors who are owed these preferential liabilities would likely be classified separately under a scheme of arrangement or a deed of company arrangement and have priority over unsecured creditors in a restructuring.[64] |
| **Brazil** | Labour-related claims (safety-related liabilities being one of them) are considered basic maintenance amounts, and the Brazilian Bankruptcy Law establishes that they must be paid within one year. This deadline may be extended for up to two years if the restructuring plan complies with the following requirements, cumulatively: (i) it provides sufficient guarantees in the court's opinion; (ii) it is approved by labour creditors at the creditors meeting; and (iii) it guarantees payment of all labour claims in full.[65] |

62 Argentina report, section 2.2.2.
63 Australia report, section 2.2.2.
64 Australia report, sections 1.1 and 1.2.1.
65 Brazil report, section 2.2.2.

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| **Canada** | Any award of damages concerning bodily harm intentionally inflicted or wrongful death and orders and penalties relating to health and safety matters in the nature of fines, restitution orders or similar are not compromised by a restructuring unless the compromise is expressly provided for in the plan or proposal and the creditor in respect the relevant debt or liability votes in favour.[66] |
| **Germany** | Certain debts, such as claims arising from torts and fines, are excluded from being restructured under a restructuring plan.[67] |
| **Hong Kong** | Health and safety-related liabilities may possibly be classified as secured for priority debts where: (i) the amounts are due in relation to work injury compensation under the Employees' Compensation Ordinance (Cap 282);[68] or (ii) the liabilities fall within the scope of statutory debts, which are debts of which the liability and the amount are determined by or under any provision in any Ordinance.[69] |
| **Japan** | A restructuring plan may not provide for the reduction or release of administrative and criminal fines that arose prior to the commencement of a restructuring procedure.[70] Hence, insofar as any administrative and criminal fines relate to health and safety regulations, they would not be capable of being reduced or released under a restructuring plan. |
| **Malaysia** | Employees' compensation under any written law, as well as remuneration payable in the event of death of employees, are given priority over all other unsecured debts. These debts that are given priority could include those arising from health and safety-related liabilities.[71] |
| **Mexico** | Compensation owed to employees deriving from health and safety liabilities is given absolute priority under the Constitution of the Mexican United States, the Commercial Insolvency Law and the Federal Labour Law.[72] |
| **Nigeria** | Contributions and obligations of the company under the Employees' Compensation Act are treated as preferential payments ranking in priority to all other debts (subject to certain exceptions such as debts owed to secured creditors and liquidation expenses). To this extent, in an administration, any health and safety-related liabilities pursuant to the Employees' Compensation Act may be treated as preferential (priority) payments.[73] |
| **People's Republic of China** | Pursuant to the hierarchies provided by the Enterprise Bankruptcy Law, subsequent to the repayment of bankruptcy expenses and debts incurred for common benefits, priorities are granted to employee wages, medical and disability subsidies, compensation expenses and pension insurance and basic medical insurance expenses that should be borne by individual employees, as well as the compensation that should be paid to employees legally.<br><br>For those liabilities that have not been covered by legislation, the court may reasonably decide the payment sequence on a principle that requires |

66 Canada report, sections 2.3.2 and section 2.4.
67 German report, section 1.2.
68 Which is a preferential debt in a winding up pursuant to ss 265(1)(cb) and 265(1)(ce) of the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap 32).
69 Hong Kong report, section 2.2.2.
70 Japan report, section 2.2.2.
71 Malaysia report, section 2.2.2.
72 Mexico report, section 2.2.2.
73 Nigeria report, section 2.2.2.

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| | compensation for personal injuries to be treated better than compensation for property, claims incurred under private laws to be treated better than those incurred under public laws, and compensatory claims to be treated better than punitive claims.<br><br>Compensation for personal injuries arising from a debtor's tortious acts may obtain the same preferential treatment as labour and pension claims under section 113 of the Enterprise Bankruptcy Law, unless the claims are punitive. Punitive damages can only be paid when all claims provided by section 113 of the Enterprise Bankruptcy Law are cleared.[74] |
| **Russia** | Claims connected with bodily injuries and other injuries to health have priority under insolvency law, ranking after the monetary obligations that arise after the commencement of the insolvency proceedings (e.g. the insolvency practitioner's remuneration and expenses and salaries).[75] |
| **South Africa** | The Insolvency Act provides for a preference in respect of certain statutory health and safety-related obligations under liquidation proceedings. In particular:<br><br>▪ all amounts which were owed by the insolvent company to the Compensation Commissioner under the Compensation for Occupational Injuries and Diseases Act immediately prior to the liquidation of the company. This includes fines and assessments imposed by the Compensation Commissioner; and<br><br>▪ all amounts owed by the insolvent company to the Mines and Works Compensation Fund, established in terms of the Occupational Diseases in Mines and Works Act.<br><br>Under insolvency proceedings, the above liabilities rank behind a portion of employees' claims. Although not required to do so, a restructuring proposal may also provide for the above preferences, or at least provide that the above creditors receive a dividend that is equal to or better than the expected outcome in a liquidation.[76] |
| **Spain** | An arrangement with creditors may not affect certain claims that are related to particular health and safety-based liabilities, namely:<br><br>▪ claims that correspond to the percentages of the social security contributions to be paid by the employer for common contingencies and for professional contingencies; and<br><br>▪ claims that correspond to the percentages of the workers' quota, which relates to common contingencies or accidents at work and occupational disease.[77] |
| **Switzerland** | All amounts due in relation to work injury compensation under the Federal Law on Accident Insurance are preferential debts in a winding up pursuant to art 219 para 4, 1st Class b Swiss Federal Code on Debt Enforcement and Bankruptcy. Such liabilities may be given priority treatment under a proposed composition agreement.[78] |

74 People's Republic of China report, section 2.2.2.
75 Russia report, section 2.1.2.
76 South Africa report, section 2.2.2.
77 Spain report, section 2.2.2.
78 Switzerland report, section 2.2.2.

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| **United Arab Emirates** | Under the Bankruptcy Law, amounts owing to employees are afforded preferential status but this is capped at the equivalent of three months' salary. Any incremental amounts would be regarded as unsecured claims. While the preferential portion cannot be compromised without the approval of the relevant employee, in theory it should be possible to compromise incremental amounts owing to employees (which may include health and safety liabilities which the company owes direct to the employee).[79] |

Some jurisdictions provide even greater safeguards for certain employment-related health and safety liabilities by conferring security interests over the employer's property to secure the payment of claims (which might include work injury compensation claims). The security interests are created over property which is used in connection with or produced as a result of the activity that caused the claims to arise. For example, plant or machinery that was used for manufacturing activity which caused a worker to suffer injury could be attached with a security interest to secure payment of compensation to the worker. This alternative is outlined in Table 6 below.

*Table 6: Restructuring of health and safety-related liabilities (security for workers' compensation liabilities)*

| Jurisdiction | Summary |
|---|---|
| **Canada** | Certain health and safety-related statutes concerning workers' compensation create liens to secure the payment of obligations to health and safety regulators.[80] Under these statutes, amounts owing by an employer to the relevant regulatory authorities (such as work injury compensation) are secured by the property of the employer used in connection with or produced by the activity with respect to which the employer was ordered to pay the compensation. |
| **Nigeria** | Where an employer becomes insolvent, any amount due or required by an employer to be paid to the Employees' Compensation Fund on an assessment or on a judgment for it, shall constitute a lien in favour of the Fund payable in priority over all liens, charges or mortgages of every person, wherever created or to be created, with respect to the property or proceeds of property, real, personal or mixed, used in or in connection with or produced in or by the industry with respect to which the employer was assessed or the amount became payable, except liens for wages due to employees by their employers.[81] |

## 4.3 Governance (G): third party releases in favour of directors and officers

In relation to the restructuring of liabilities, the third issue which this book aims to investigate is whether a restructuring plan can provide for third party releases in favour of directors and officers of the company and, if so, the restrictions or conditions which apply to the releases.

Across the jurisdictions surveyed, there are broadly three ways in which third party releases are treated:

- some jurisdictions do not permit third party releases (Brazil, India, Japan, Russia and Thailand);
- some jurisdictions allow for third party releases of guarantee liabilities, but it is uncertain whether and to what extent third party releases may be granted in favour of directors and

79 United Arab Emirates report, section 2.2.
80 Canada report, section 2.3.2.
81 Nigeria report, section 2.2.2.

officers for non-guarantee liabilities (Bermuda, Hong Kong, Malaysia, Singapore, South Africa and the Netherlands); and

- some jurisdictions permit third party releases in favour of directors and officers but with constraints and only if it is fair and reasonable in the circumstances (Canada, Germany and the United Kingdom).

In relation to the second category above (third party releases of guarantee liabilities), the rationale for permitting third party releases in those circumstances is to facilitate an effective restructuring. If guarantors are not released from liability under a restructuring plan, the creditors would claim against the guarantors, and in turn, the guarantors would then claim against the primary debtor (i.e. the company undergoing restructuring) to be indemnified. In other words, the claims "ricochet" back to the debtor company and potentially undermine the effectiveness of the restructuring. As explained by the Singapore Court of Appeal in *Pathfinder Strategic Credit LP v Empire Capital Resources Pte Ltd* [2019] 2 SLR 77 at [81], the third party releases of other group co-debtors were necessary "since otherwise liability and enforcement risks would merely be shifted between members of the corporate group and the overall restructuring objective would be entirely unmet."

However, in relation to the third category above (third party releases of directors and officers for non-guarantee liabilities), the concern relating to "ricochet" claims does not necessarily apply as the directors and officers may not have a right to be indemnified by the debtor company for their personal liabilities owed to creditors. Furthermore, as seen in the *Purdue Pharma* case discussed earlier, there are contentious policy issues surrounding the grant of third-party releases in favour of directors and officers of the company, particularly where the claims relate to alleged wrongdoing committed by the directors and officers.

At the same time, however, the absence of a release for guarantees could deter directors / officers from placing a company in a restructuring process to begin with, given the commercial reality that the guarantors are often shareholders and directors who are the main players in seeking an arrangement with creditors by offering their own assets in return for the release of their guarantees.[82]

In jurisdictions where third party releases of directors and officers are permitted, there are various factors the courts consider in deciding whether to allow those releases under a restructuring plan, such as whether the parties to be released were necessary and essential to the restructuring of the debtor, whether they provided financial contributions for the plan or valuable services for the restructuring, and whether the claims to be released were rationally connected to the purpose of the proposal or plan and were necessary for it to proceed.
Additionally, in Canada, legislation expressly prohibits the compromise of certain claims against directors, such as those based on allegations of misrepresentation made by directors to creditors or of wrongful or oppressive conduct by directors. These various forms of dealing with third party releases are outlined in Table 7 below.

*Table 7: Third party releases in favour of directors and officers*

| Jurisdiction | Summary |
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| **Argentina** | From a theoretical standpoint, a restructuring plan may provide a release to directors and officers, and the court shall analyse the fairness of the plan and whether or not the terms are deemed abusive. Nevertheless, third party releases in Argentina are unlikely to be effective in releasing any liability of the directors and officers of the company for fraudulently causing, facilitating, permitting or aggravating the financial status or the insolvency of |

82 *Re CEL Tractors Pte Ltd* [2001] 1 SLR(R) 700 at [27] (affirmed on appeal in *Daewoo Singapore Pte Ltd v CEL Tractors Pte Ltd* [2001] 2 SLR(R) 791); *Re Lydian International Limited*, 2020 ONSC 4006 at para 55.

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| | the company, or any liability for negligence or breach of their fiduciary duties.[83] |
| **Australia** | Schemes of arrangement can be used to effect the release of third parties from debts owed to, and claims by, creditors without the express consent of the releasing creditors (provided the relevant scheme voting thresholds are met), but neither deeds of company arrangement nor restructuring plans can do so.[84] |
| **Bermuda** | In some instances, a scheme of arrangement may release third parties from liability. However, this will be determined by the nature of the underlying obligation and the surrounding circumstances. *In re Markel CATCo Reinsurance Fund Ltd, et al*, Nos. 307 and 309, the court found that the release of certain third parties from potential liability *vis a vis* contingent creditor claims (as part of the proposal) was necessary to avoid ricochet claims which fell outside of the relevant indemnities and to secure additional funding from the shareholder of the scheme companies which was conditional upon obtaining the releases.<br><br>Following this judgment and given the substantial similarities in provisions relating to schemes of arrangements to those under Singapore law, the Bermuda court would likely consider and follow the position in Singapore in future when determining jurisdiction. This may include the "sufficient nexus" test – that is, whether there is a sufficient nexus or connection between the release of the third party liability and the relationship between the company and the scheme creditors.[85] |
| **Brazil** | Brazilian Bankruptcy Law expressly provides that third party guarantees shall remain in place. The restructuring plan, however, under the assumption that creditors may waive the guarantee, may provide for release of third party guarantees. This has sparked controversy in Brazilian courts, and such a provision is usually considered by courts to be binding only on those creditors who voted in favour of the plan of reorganisation without any reserve to the release – this is the overall rule in Brazilian restructuring cases.<br><br>Additionally, restructuring or insolvency proceedings do not have the effect of releasing directors and other stakeholders from liability for previous actions and decisions.[86] |
| **Canada** | Canadian courts regularly sanction releases in favour of directors and officers (and other third parties) in the context of restructuring proceedings under the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act. In doing so, they consider the following factors (with no single factor being determinative or necessarily applicable in each case):<br><br>▪ whether the parties to be released were necessary and essential to the restructuring of the debtor (e.g. because they provide monetary contributions under the restructuring plan or, in the case of directors or officers being released, because they would never have brought forward a proposal for a restructuring plan in the first place in the absence of the release);<br><br>▪ whether the claims to be released were rationally connected to the purpose of the proposal or plan and are necessary for it (in the sense that |

83 Argentina report, section 2.3.
84 Australia report, section 2.3.
85 Bermuda report, section 2.4.
86 Brazil report, section 2.3.

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| | they are not overly broad and do not extend to liabilities unrelated to the operation of the relevant company being restructured);<br>▪ whether the proposal or plan could succeed without the releases;<br>▪ whether the parties being released contributed to the proposal or plan; and<br>▪ whether the releases benefit the debtor as well as the creditors generally.<br><br>Both the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act contemplate the compromise of certain pre-filing claims against directors and officers in proposals and plans. However, both statutes do not permit the compromise of the following claims against directors: (i) claims that relate to contractual rights of one or more creditors arising from contracts with one or more directors; and (ii) those based on allegations of misrepresentation made by directors to creditors or of wrongful or oppressive conduct by directors.[87] |
| **Germany** | Third parties can receive releases of liability under a restructuring plan. However, the releases are subject to certain limitations and requirements. For example, releases must be fair and reasonable, must not prejudice the interests of creditors and must be approved by the court overseeing the restructuring proceeding. The releases can be granted in exchange for financial contributions to the restructuring plan, or in recognition of other valuable services provided to the restructuring effort. It is important to note that releases are only possible in the context of a restructuring or insolvency plan and cannot be granted as part of a formal insolvency proceeding.[88] |
| **Hong Kong** | It is possible for a scheme to provide for third party releases. The release of third party rights is permissible where necessary in order to give a scheme efficacy. For example, where two companies are jointly liable as co-obligors for the same debt, a third party release in favour of one of the co-obligors may be necessary to give the scheme efficacy. Without such a third party release, the co-obligor would remain liable for the debt and may be entitled to claim a contribution from the scheme company, thereby resulting in a ricochet claim against the scheme company that would defeat the purpose of the scheme.<br><br>Third party releases have been allowed to release guarantees of the debt sought to be compromised in the scheme given by associated companies of a debtor company. The release of a principal obligor's liability where the debt compromised in the scheme is that of a guarantor has also been allowed.<br><br>There are no reported decisions in Hong Kong directly on third party releases granted in favour of directors and officers of the company. However, it has been explained in *obiter* that a scheme may also release any claims or purported claims by the scheme creditors against other third parties including directors, legal advisors, financial advisers and various other intermediaries. As the release of a third party right is only permissible if it is required to give efficacy to the scheme, it would not be permissible for a company to include releases that are not necessary and to allow third parties associated with the company to escape from unrelated liabilities.[89] |

87 Canada report, section 2.4.
88 Germany report, section 2.3.
89 Hong Kong report, section 2.3.

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| **India** | Indian insolvency law does not provide releases to third parties (such as directors) for past breaches committed by them.[90] |
| **Japan** | There is no provision that expressly allows third party releases in favour of directors or officers of a company under restructuring procedures. Restructuring procedures under Japanese law proceed only for the entity or individual who filed the procedures, not for other associated entities or individuals (such as a director of the debtor company). |
| **Malaysia** | There are no statutory provisions in Malaysia which expressly prohibit the release of third party liabilities *vis-à-vis* directors and officers of the scheme company. However, there are also no reported cases in Malaysia to date which directly address the issue of whether a third party release can be granted in favour of directors and officers of the scheme company.<br><br>While the High Court has held that it is permissible for a scheme to provide for a third party arrangement involving the company's guarantor who is not a party to the scheme of arrangement (*Re Khondker Yarad Ahmed; ex p MIDF Amanah Ventures Sdn Bhd* [2016] 3 CLJ 637), the court did not provide guidance on the factors to be taken into consideration when determining whether the release of third party liabilities would be allowed.<br><br>In another case, the High Court was of the view that a restraining order (granted in a scheme of arrangement) could extend to the guarantor company, if the guarantor was an integral component of the scheme and the scheme would not be workable without the guarantor company (*Sentoria Bina Sdn Bhd v Impak Kejora Sdn Bhd & Ors* [2021] 12 MLJ 690). Although the court was not directly concerned with the issue of whether a third party release *vis-à-vis* a guarantor is allowed in a scheme of arrangement, based on the court's reasoning on the issue concerning the restraining order, it is arguable by analogy that the court in *Sentoria* would have similarly allowed a scheme of arrangement which also seeks to release the liability of the guarantor company. |
| **Russia** | There are no statutory provisions to authorise third party releases in favour of directors and officers of the company. Debt rescheduling (applied to individuals) can be used in a separate case to release the directors and officers from liability.[91] |
| **Singapore** | It is possible for a scheme to provide for third party releases. There are two aspects that govern whether a third party release will be allowed by the court:<br><br>▪ whether there is a sufficient nexus or connection between the release of the third party liability and the relationship between the company and the scheme creditors; and<br><br>▪ whether the third party release sought is fair and reasonable in the circumstances.<br><br>Third party releases have been allowed in circumstances where the relevant third parties were related companies of the debtor within the same corporate group, and the debts of the scheme company and the third parties arose under the same issuance of notes. The rationale in permitting third party releases of debts, at least where related companies are concerned, is to allow a holistic group restructuring to be effective. In |

90 India report, section 2.3.
91 Russia report, section 2.3.

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| | *Pathfinder Strategic Credit LP v Empire Capital Resources Pte Ltd* [2019] 2 SLR 77, the Singapore Court of Appeal explained that the third party releases sought in that case were necessary "since otherwise liability and enforcement risks would merely be shifted between members of the corporate group and the overall restructuring objective would be entirely unmet."<br><br>There have been no reported decisions in Singapore regarding whether third party releases can be granted in favour of directors and officers of the company and the principles applicable to the granting of such releases. In principle, the "sufficient nexus" test might be met for a proposed third party release, even if the third parties are not members within the same corporate group. For example, in the Federal Court of Australia decision of *Re Opes Prime Stockbroking Ltd* [2009] FCA 813, which was cited with approval by the Singapore Court of Appeal in *Pathfinder*, the third party releases were granted in favour of not just another company in the corporate group, but also certain banks, liquidators and receivers. However, the precise extent to which third party releases are allowed in favour of directors and officers of the company is not clear in Singapore. |
| **South Africa** | Whether a business rescue plan may provide for the release of directors' and officers' liability for non-contractual claims such as claims for negligence, claims for the breach of directors' fiduciary duties and claims for trading under insolvent circumstances has not been decided in reported judgments.<br><br>There is nothing in the legislation expressly preventing a business rescue plan from allowing the restructuring of potential non-contractual obligations of directors towards creditors, but one may conceive of circumstances in which an aggrieved creditor may successfully apply to have a business rescue plan set aside even if it is adopted by the requisite majority of creditors in value where it is contrary to public policy or the South African Constitution.[92]<br><br>In a similar vein, the court retains the discretion to sanction or refuse to sanction a section 155 arrangement and its decision may be guided not only by whether the requisite majorities of creditors voted for the arrangement, but also by considerations of public policy. In *Mahomed v Kazi's Agencies (Pty) Ltd* 1949 (1) SA 1162 (N), the court went as far as to state that "the court ought not to sanction a compromise where the probable result of such a course will be to allow evil-doers to go unpunished."<br><br>This indicates that although in principle a section 155 arrangement may provide for third party releases, the court retains a broad discretion to refuse to sanction the arrangement and the release of third parties should the court find that it is not just and equitable in the circumstances.[93] |
| **Thailand** | A business rehabilitation plan can only govern the debts owed by the debtor to its creditors and cannot alter or release liabilities any third party might have with the same creditors, for example in their capacity as a guarantor or joint debtor.[94] |
| **The Netherlands** | Dutch law does not specifically allow nor restrict third party releases of liability under a restructuring plan, other than for group guarantees under the WHOA (*Wet homologatie onderhands akkoord*, or Act on Confirmation of Composition Plan) procedure. However, it is uncertain if third party |

92 South Africa report, section 2.3.1.
93 South Africa report, section 2.3.2.
94 Thailand report, section 2.3.

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| | releases of obligations of directors, shareholders and other parties which were involved with the debtor before the opening of the relevant insolvency procedure are possible in composition plans in the Netherlands (regardless of whether that is a bankruptcy procedure, suspension of payment or a WHOA procedure).<br><br>According to Dutch legal literature, most authors believe the release of third party debtors will only apply against the parties who voted in favour of the plan, rather than to all parties who are bound to it. However, from Dutch case law, there have been composition plans in the past which contained third party releases and which have been confirmed by the courts. The third party releases in those plans were, however, effectively not challenged, so it remains uncertain what the outcome would have been if third party releases were challenged by a dissenting creditor.[95] |
| **United Kingdom** | Releases of third party liabilities are common in English restructurings, in particular schemes and restructuring plans. A typical example is the release of liabilities owed by a guarantor of the principal debtor which has proposed a scheme or restructuring plan. If the guarantee liability was not released, this would jeopardise the implementation of the debtor company's restructuring, given that the guarantor would have a cross-claim against the debtor company if a demand was subsequently made by a creditor under the guarantee.<br><br>It is also common for directors, officers and advisers of a company launching a scheme or a restructuring plan to obtain a release of liabilities in relation to the preparation and negotiation of the scheme or a restructuring plan and the wider restructuring implemented by the scheme or plan. It would be unusual for those releases to extend to liabilities unrelated to the restructuring and, even if included, the release would only be binding on those stakeholders which were bound by the scheme or a restructuring plan (which may not necessarily include all such stakeholders).[96] |

## 5. The protection of stakeholder interests

This section explores the ways that ESG stakeholder interests are protected or addressed in a restructuring. Ordinarily, a restructuring plan only requires the approval of the creditors and / or the court. This section aims to investigate whether jurisdictions have procedures or rules which protect the interests of ESG stakeholders who are not creditors of the company. Connected with this issue is whether courts have the discretion to consider wider public interest issues when deciding whether to approve a restructuring plan.

### 5.1 Environment (E): the influence of environmental protection authorities or environmental advocacy groups in a restructuring

The first issue considered in this section is whether environmental protection authorities or environmental advocacy groups have standing to air their views / concerns in a restructuring, and the extent to which the courts or the relevant approving bodies consider environmental issues in deciding whether to approve a restructuring plan.

In all the jurisdictions surveyed, a restructuring plan does not require the approval of environmental protection authorities. There are also typically no express statutory provisions granting standing to environmental protection authorities or environmental advocacy groups to air their views in a restructuring. In jurisdictions where court approval of a restructuring plan is required, the courts also usually primarily focus on the interests of the creditors and do not typically take into account broader environmental issues in deciding whether to approve a restructuring plan.

95 The Netherlands report, section 2.3.
96 United Kingdom report, section 2.3.

Any influence of environmental protection authorities on a restructuring is usually indirect. For example, such authorities may decide to suspend or terminate licences if there is uncertainty about the debtor company's ability to meet its environmental obligations, which can have a material impact on whether the restructuring of a company is viable. The approval of environmental protection authorities may also be required where licences have to be transferred to a new buyer under a sale of the debtor's business.

It is noteworthy that in Japan, if a reorganisation plan involves matters that require the permission, authorisation or a licence by an administrative agency, the reorganisation plan can only be approved if it is not in conflict with the opinions of the administrative agency (see further below). There is arguably merit in this approach, as it avoids a restructuring plan being approved in vain. A restructuring could be rendered unviable if, for example, a material licence of the company is subsequently revoked by the authorities. By addressing such issues at the plan approval stage, it may give greater certainty that the restructuring can be properly implemented.

The approaches to these issues among the jurisdictions surveyed in this project are summarised in Table 8 below.

*Table 8: Protection of stakeholder interests (influence by environmental protection authorities or environmental advocacy groups in a restructuring)*

| Jurisdiction | Summary |
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| **Australia** | While environmental authorities and advocacy groups might seek to influence a scheme of arrangement on public policy grounds, the only public policy concerns relevant to a court's authorisation of creditors' meetings and scheme documents are those relating to the interests of members, creditors, future counterparties and future investors. Accordingly, it is unlikely that an environmental regulator or advocacy group would have standing to oppose a scheme for a regulatory or public interest purpose.<br><br>There is also no public interest basis on which to challenge a deed of company arrangement or restructuring plan. While the courts have jurisdiction to terminate a deed of company arrangement on the ground that effect cannot be given to it without injustice or undue delay, an environmental regulator or advocacy group would not have the necessary standing to apply for such an order, as standing is restricted to the company, creditors, the corporate regulator (ASIC) and persons whose material rights or economic interests are or might be substantially affected by the deed.<br><br>Standing is even more restricted in relation to applications to terminate restructuring plans, with the effect that environmental regulators and advocacy groups would have no capacity to move the court to terminate such a plan (other than as affected creditors).[97] |
| **Brazil** | There is no express rule in the Brazilian Bankruptcy Law which determines that the plan should be approved by any regulatory body other than the court. The Public Prosecution Officer, because it has the power / obligation to defend the public interest, may file petitions at any time, and / or appeals against the ratification of the plan, if it understands that one or more clauses of the restructuring plan are illegal.<br><br>However, "illegality" is a narrow ground, and there is no general requirement for a restructuring plan to be approved by environmental protection authorities or environmental advocacy groups.[98] |

97 Australia report, section 3.1.
98 Brazil report, section 3.1.

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| **Canada** | While courts may consider the impact of their decisions on the public interest, the proposal provisions of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act are still primarily focused on addressing the relationship between insolvent entities and their creditors, with the purpose of preventing the social and economic costs of a liquidation. Therefore, the interests of creditors are given considerable weight and deference, both in the provisions of the statutes and by the courts in exercising their jurisdiction under the Acts.<br><br>There is no statutory requirement under the Acts for environmental protection authorities or advocacy groups to approve a proposal or plan. However, where the claims of environmental regulators are afforded super priority, those obligations may have a significant practical impact on the course of the restructuring proceedings. If environmental obligations have to be paid out in priority to other creditors, with the result that subsequent creditors will see little or no recovery, debtors may find it difficult to secure the debtor-in-possession financing they require to fund a restructuring proceeding. In some cases, this may result in debtors not being able to pursue a restructuring at all.[99] |
| **France** | Environmental protection authorities may have an indirect influence on a restructuring. French environmental law remains fully applicable in the context of insolvency proceedings. Therefore, if the draft restructuring plan purports to have an impact on activities or facilities subject to environmental law, the environmental protection authorities may be consulted via a process that is independent of the plan adoption process.<br><br>For example, if a sale plan adopted by the court includes a FCEP (Facilities Classified as Environmental Protection) that is subject to the authorisation scheme under the French Environmental Code, the buyer must obtain the authorisation of the prefect to change operator before continuing the business. Otherwise, it will not be authorised to operate the site.[100] |
| **India** | There is no requirement for a resolution plan under the Insolvency and Bankruptcy Code 2016 to be approved by any environmental authority or environmental advocacy group.<br><br>The Code is essentially a creditor restructuring tool and tries to restrict the discretion of the National Company Law Tribunal. The National Company Law Tribunal can only reject a resolution plan if it is in violation of any applicable law (including environmental laws) or does not conform to the payment principles prescribed under the Code. To this end, an advocacy group could intervene in the resolution plan hearings stating that the business and revival plan envisaged in the resolution does not conform to environmental laws. However, practically, we have not seen this occur since it is the duty of the resolution professional as well to ensure the resolution plan complies with environmental laws – as a result, a plan that would not comply with those laws is unlikely to be put to creditors and to proceed to resolution plan hearings in the first place.[101] |
| **Japan** | A restructuring plan under in-court insolvency proceedings is subject only to the approval (i.e. an order of confirmation) of the creditors and the courts, not the approval of any other regulatory bodies, such as environmental protection authorities. However, it is possible that regulatory bodies may be able to indirectly influence the relevant court's plan confirmation process. |

99 Canada report, section 3.1.
100 France report, section 3.1.
101 India report, section 3.1.

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| | That is because, if a reorganisation plan provides for matters that require permission, authorisation, a licence, or any other disposition by an administrative agency, the reorganisation plan can only be approved if it is not in conflict with the opinions on important points heard from the administrative agency.[102] |
| **Kenya** | There is no express requirement that restructuring proposals be submitted to and approved by environmental protection authorities, but from a plain reading of the environmental laws, it is arguable that proposals should adhere to any environmental standards set by law in case they involve environmental protection issues.<br><br>As an illustration, if a restructuring proposal includes projects that have some impact on the environment, Kenya law requires the relevant projects to be submitted to the environmental protection authority for verification and analysis on whether they may have a negative impact on the environment (commonly referred to as an environmental impact assessment, after which, if approval is granted, the projects receive a licence to go ahead).[103] |
| **South Africa** | The Companies Act aims to "provide for the efficient rescue and recovery of financially distressed companies, in a manner that balances the rights and interests of all relevant stakeholders". In certain instances, it could be argued that relevant stakeholders would include environmental authorities. Ultimately, however, it is up to the creditors to adopt or reject a business rescue plan and, as long as the plan sufficiently provides for their interests, it is likely that environmental concerns will not be a determining factor. It is conceivable that an environmental authority could successfully apply to the court to set aside a business rescue plan if the plan does not sufficiently provide for the fulfilment of a company's obligations under environmental legislation, although this has not been done before.<br><br>When deciding whether to sanction a section 155 arrangement, a court does have the discretion to consider wider public interest concerns and retains a broad discretion to refuse to sanction an arrangement if, in the particular circumstances, it is not just and equitable to do so. Although no precedent exists where a court has refused to sanction an arrangement based on environmental concerns, there is nothing preventing a court from taking environmental concerns into account when considering whether to sanction an arrangement.<br><br>In instances where mining rights or licences are owned by a company undergoing a business rescue, the Minister's consent is required in order to alienate any mining right or licence. In this way, the Minister may indirectly influence the proposals contained in a business rescue plan or under a section 155 arrangement should the arrangement contemplate the disposal of mining rights.[104] |
| **Thailand** | Although the Bankruptcy Act prescribes the conditions for the court to consider and, if these conditions are met, the court usually approves the plan, the court still has the discretion to take into consideration other significant issues, for example fairness in general or the adverse effects approval or non-approval of the plan may cause to other interested parties. Despite the fact the Supreme Court has not to date considered environmental public concerns as one of these issues, there may be scope |

102 Japan report, section 3.1.1.
103 Kenya report, section 3.1.
104 South Africa report, section 3.1.

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| | for it to do so in future as the importance of these issues continues to increase in coming years.[105] |

## 5.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

The second issue considered in this section is whether labour authorities, unions or employee / worker advocacy groups have standing to air their views and concerns in a restructuring, and the extent to which the courts or the relevant approving bodies consider labour issues in deciding whether to approve a restructuring plan.

As a preliminary point, most of the jurisdictions surveyed protect employees' interests in a restructuring by giving preferential treatment to employee claims, with some jurisdictions even requiring that *all* employee claims be paid in full under a restructuring plan (such as Argentina,[106] Brazil,[107] Germany[108] and Russia).[109]

This section focuses not on the treatment of employee claims, but instead on how employees' other interests or concerns in relation to a restructuring can be taken into account. This may be important as employees have a role to play in the future of the restructured business and will want to ensure that their interests are not being harmed in a restructuring.

Many jurisdictions surveyed have rules or practices which help to give employees a voice in a restructuring and enable them to participate the formulation of a restructuring plan. There are broadly three ways in which jurisdictions achieve this:

- some jurisdictions require a representative of the employees to be appointed on a creditors' committee (Argentina, the People's Republic of China and Malaysia). The creditors' committee might have various rights and powers depending on the jurisdiction, such as the right to request information from the debtor or approve certain acts of the debtor;

- some jurisdictions give rights to trade unions or other employee representative bodies, such as a works council, to represent employees in a restructuring (Australia, France, Malaysia, Singapore, South Africa and the Netherlands), thereby providing a coordinated platform for employees to act, seek advice, and advocate for the protection of their interests. For example, in Singapore, a trade union may apply to the court to seek orders to protect the interests of its union members if the company's affairs, business and property are being or have been managed by in a manner that is unfairly prejudicial to their interests.[110] In France, the works council (a body that represents employees in the company) must be informed and consulted on the draft restructuring plan and on all envisaged decisions that may have an impact on employment (e.g. staff reductions and changes in working conditions) and must be heard by the court before the adoption of the reorganisation or sale plan; and

- in some jurisdictions, the court may have the power to establish committees for employees and / or to appoint representative counsel for employees (Canada, South Africa and the United Arab Emirates). For example, in Canada, the courts can exercise their discretion to appoint representative counsel to act on behalf of employees in proceedings under the Companies' Creditors Arrangement Act, the costs of which may be paid out of the debtor company's estate. Depending on the circumstances, representative counsel may assist employees and former employees by providing a reliable resource of information and by litigating claims on behalf of individuals who, on their own, would have little means of pursuing their claims in relation to pension, termination, severance, retirement and other payments.

105 Thailand report, section 3.1.
106 Argentina report, section 3.2.3.
107 Brazil report, section 2.2.2.
108 Germany report, section 3.2.3.
109 Russia report, section 3.2.3.
110 This applies only to judicial management proceedings and not scheme of arrangement proceedings.

The approaches taken by the jurisdictions surveyed are considered in further detail in Table 9 below.

*Table 9: Protection of stakeholder interests (influence by labour authorities, unions or employee / worker advocacy groups in a restructuring)*

| Jurisdiction | Summary |
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| **Argentina** | In a reorganisation proceeding (*concurso preventivo*), a creditors' committee is appointed to act, in addition to the trustee, as an information and advisory body. As the creditors' committee must include representatives of the debtors' employees, workers of the company will have standing to air their views or concerns in a restructuring. The creditors' committee shall be heard when the debtor requests judicial authorisation for performing certain acts and has powers to request information from the trustee and the debtor, require the exhibition of books and records, propose measures for the custody and conservation of the debtor's assets, request hearings before the judge and propose other measures considered to be appropriate.<br><br>In addition to the individual rights afforded to workers, if employees of a company undergoing a restructuring proceeding are members of a trade union, the union may be entitled to submit motions to the court seeking to protect the interests of its members.[111] |
| **Australia** | In voluntary administration, particularly in large administrations, it is not uncommon for unions (usually with the cooperation of the relevant voluntary administrator) to obtain court orders allowing them to vote on behalf of employee creditors during the administration process, effectively "dealing them in" to the negotiation of any deed of company arrangement.[112] |
| **Canada** | Canadian courts have exercised their discretion to appoint representative counsel to act on behalf of employees in proceedings under the Companies' Creditors Arrangement Act, the costs of which may be paid out of the debtor company's estate. Depending on the circumstances, representative counsel may assist employees and former employees by providing a reliable source of information and by litigating claims on behalf of individuals who, on their own, would have little means of pursuing their claims in respect of pension, termination, severance, retirement and other payments.[113] |
| **France** | The works council is the body that represents employees in the company. It must be set up in companies with more than 11 employees. The members of the works council are elected by the employees of the company for a maximum period of four years. The powers, composition and functioning of the works council depend on the size of the company.<br><br>The works council may have an influence (variable, according to the situation) on the approval of the debtor's restructuring plan.<br><br>During out of court restructuring proceedings, if the debtor requests the approval of a conciliation agreement by the court, it is required to inform the works council of the content of the conciliation agreement and representatives of the works council are called to the attend the court hearing that will hear the request for approval of the conciliation agreement. |

111 Argentina report, section 3.2.3.
112 Australia report, section 3.2.
113 Canada report, section 3.2.3.

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| | During court proceedings, the works council must be: (i) informed and consulted on the draft plan (repayment plan or sale plan) and on all envisaged decisions that may have an impact on employment (e.g. staff reductions and changes in working conditions); and (ii) heard by the court before the adoption of the reorganisation or sale plan.[114] |
| **Kenya** | Unionised employees are represented by their unions, which advocate for their rights. In a restructuring, given the need for approval by employees as preferential creditors, it would be expected that restructuring plans would involve proposals that address any health, safety or other concerns that employees would have. Otherwise, the proposal would risk failure because employees may decline to vote for it.[115] |
| **Malaysia** | In the context of judicial management, the committee of creditors must consist of at least one employee or the trade union, provided the employees are members of the trade union and the employer recognises the union. This indicates that a trade union is entitled to represent any members at a meeting of creditors summoned to consider the judicial manager's proposals.<br><br>The trade union representing the employees has a right to attend the meetings of the committee of creditors as non-voting delegates but cannot preside over the meetings of the committee of creditors.[116] |
| **People's Republic of China** | A representative of the employees or the labour union of the debtor is entitled to attend creditors' meetings and express opinions over matters relating to labour rights. If a creditors' committee is established during the proceeding, the representative of the debtor's labour union will become a member participating in the operation of the committee.[117] |
| **Singapore** | In the context of judicial management, where employees of a company are members of a trade union that is recognised by the company under the Industrial Relations Act 1960, the trade union functions as an intermediary for the employees. The trade union is entitled to represent any of its members at a meeting of creditors summoned to consider the judicial manager's statement of proposals. The trade union may also, with the permission of the court, apply to the court to seek orders to protect the interests of its members if the company's affairs, business and property are being or have been managed by the judicial manager or interim judicial manager in a manner that is or was unfairly prejudicial to their interests. The trade union may also make representations to the judicial manager on behalf of those employees in respect of any matter connected with their employment contracts.[118] |
| **South Africa** | During the business rescue process, employees and trade unions representing employees have the right to, *inter alia*:<br><br>▪ participate in any court proceedings arising during the business rescue proceedings;<br><br>▪ form a committee of employees' representatives, which may consult with the business rescue practitioner about matters relating to the business |

114 France report, section 3.2.1.
115 Kenya report, section 3.2.
116 Malaysia report, section 3.2.3.
117 People's Republic of China report, section 3.2.3.
118 Singapore report, section 3.2.3.

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| | rescue proceedings and may, on behalf of employees, receive and consider reports relating to the business rescue proceedings;<br>▪ be consulted by the business rescue practitioner during the development of the business rescue plan; and<br>▪ make submissions at the meeting where the business rescue plan is to be considered and voted on by creditors.[119] |
| **Spain** | Under Spanish law, the labour force has relevance under certain insolvency solutions. For example:<br>▪ in the event the insolvency proceedings result in the sale of a production unit or the business as a whole, the offer will need to set out the impact it will have on the labour force;<br>▪ where the sale of a production unit or the business as a whole is proposed, the Commercial Court will grant a 15 day period for objections to be filed against on the sale;<br>▪ in the event the sale of a production unit or the business as a whole takes place by public auction, the Commercial Court may authorise a sale of less than 15% in price compared to the best economic offer if it considers that this option will better guarantee the sale of the productive unit and will save more jobs;<br>▪ under an accelerated sale scenario, workers may establish a cooperative or labour company to make an offer for the business unit. If the workers' offer is equal or higher in value to the alternative acquisition proposals, the Commercial Court will give priority to the workers' offer; and<br>▪ if an arrangement with creditors envisages the acquisition by a third party either of all the assets and rights assigned to the professional or business activity of the insolvent debtor, or of certain production units, it may not be permitted by the Commercial Court without the prior hearing of the workers' representatives.[120] |
| **The Netherlands** | Dutch labour law contains the requirement for each company that has 50 or more employees to establish a works council (*ondernemingsraad*) in which the employees of the company are represented. Under certain circumstances, a works council can also be established for companies with less than 50 employees.<br>The works council must be requested for its advice on the following topics (among others):<br>▪ transfer of control over the company or part thereof;<br>▪ vesting, taking or disposing of control over another company as well as entering into, making material amendments in or cancelling a sustainable cooperation (*duurzame samenwerking*) with another company, including the entry into, materially amending or cancelling an important financial participation due to or for the benefit of such company;<br>▪ cancellation of the business of the company or an important part thereof; |

[119] South Africa report, section 3.2.3.
[120] Spain report, section 3.2.1.

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| | ▪ important reductions, increases or other amendments of the business of the company; and<br>▪ an important amendment in the organisation of the company or in the allocation of tasks within the company.<br><br>Throughout the WHOA (*Wet homologatie onderhands akkoord*, or Act on Confirmation of Composition Plan) procedure, the debtor is in a debtor-in-possession proceeding. All its obligations remain in force, including its obligation to comply with the relevant provisions in law applicable on the works council.[121] |
| **United Arab Emirates** | In the context of a court-controlled restructuring, the court has the power to approve the formation of creditor committees to represent the interests of different categories of creditors. In a situation where the rights of employees are to be compromised (or otherwise affected) pursuant to the plan, it is possible that the court may sanction an employee-focused committee to ensure the interests of employees are taken into account in formulating the plan.[122] |

### 5.3 Governance (G): board / management conflicts addressed in a restructuring

The third issue in this section relates to how board / management conflicts are addressed in a restructuring. This question is mostly relevant to debtor-in-possession restructurings where the existing directors or management remain in control of the company and have the power to control or influence the formulation of a restructuring plan. In some situations, the board / management may seek to negotiate for post-restructuring shares or options (e.g. under a management incentive plan or options scheme) in return for committing to continuing their service for the company post-restructuring.

Most jurisdictions address board / management conflicts primarily by barring directors and / or managers from voting on a restructuring plan (Argentina, Brazil and Singapore) and / or by requiring the disclosure of any benefits the directors and / or managers receive in a restructuring (Australia, Hong Kong, Malaysia, Singapore and Switzerland). In Canada, the courts consider a variety of factors when deciding whether to approve a management incentive plan, including the reasonableness of the terms, whether the employment of the personnel under the plan is critical to the successful restructuring of the debtor company and whether the proposal trustee or monitor (as independent parties) support the plan.

In the United Kingdom, in the case of a conflict, a practical solution sometimes employed is for the board to form a sub-committee of independent directors and delegate the negotiation of the terms of the restructuring with the company's stakeholders to that sub-committee.

The approaches taken by the jurisdictions surveyed are summarised in Table 10 below.

*Table 10: Protection of stakeholder interests (addressing board / management conflicts in a restructuring)*

| Jurisdiction | Summary |
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| **Argentina** | One of the usual conflicts in restructuring matters arises when managers or directors or other administrators have pre-petition claims and are creditors of the insolvent company. The Argentine Bankruptcy Law solves that situation, providing that controlling shareholders, managers, directors or their assignees (appointed within one year prior to the filing date) do not |

121 The Netherlands report, section 3.2.
122 United Arab Emirates report, section 3.2.

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| | have voting rights over the restructuring plan as they are related creditors and are to be discounted from the majorities required to support the plan.<br><br>If the directors or managers are receiving shares or options under a management incentive plan or options scheme as part of the restructuring plan, in return for committing to continuing their service for the company post-restructuring, all such terms and conditions shall be set out in the plan. The fairness and reasonableness of the restructuring plan shall be analysed by the court provided the majorities and formalities have been met.[123] |
| **Australia** | In a scheme of arrangement, the explanatory statement must disclose "any material interests of the directors of the body, whether as directors, as members or creditors of the body or otherwise, and the effect on those interests of the proposed compromise or arrangement in so far as that effect is different from the effect on the like interests of other persons."<br><br>There is a divergence of views at trial level, so far unresolved by any appellate court, as to whether it is appropriate for a director who will receive a substantial benefit by reason of the scheme participating in any recommendation to creditors or members. One view is that such a director should not participate in making the recommendation, whereas the contrary (and increasingly predominant) view is that such a director may participate so long as the benefit is disclosed "fully and prominently" in the scheme booklet.[124] |
| **Brazil** | To avoid conflict of interests, as many times the board / management may control or influence the formulation of a restructuring plan, the Brazilian Bankruptcy Law provides that the debtor's partners, as well as affiliate companies, controllers, controlled entities or those which have a shareholder with equity in the company greater than 10% of the debtor's capital or in which the debtor or any of its partners own stake in more than 10% of the share capital, may participate in the general creditors' meeting, but are not entitled to vote and will not be considered for the purposes of verification of the quorum of installation and deliberation. |
| **Canada** | In certain circumstances, where management and other employees of a debtor company are deemed critical to restructuring efforts, courts may approve a key employee retention plan (KERP) and / or a key employee incentive plan (KEIP). KERPs typically provide for payments to employees at specified times in the future, on the condition that the employees remain with the debtor company when those specified times arrive. KEIPs typically provide for payments tied to the debtor company successfully achieving certain milestones. Both plans are aimed at retaining those essential employees during the period in which they are likely to seek other opportunities as a result of the financial state of the debtor company.<br><br>KERPs and KEIPs are developed in conjunction with a proposal trustee or a monitor and are subject to court approval. Courts have considered the following non-exhaustive list of factors in deciding whether to approve these plans:<br><br>▪ whether the proposal trustee or monitor (as the case may be) supports the plan;<br><br>▪ whether the key employees who are the subject of the plan are likely to pursue other employment opportunities absent the approval of the plan; |

123 Argentina report, section 3.3.
124 Australia report, section 3.3.

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| | ▪ whether the employees who are the subject of the retention plan are truly "key employees" whose continued employment is critical to the successful restructuring of the debtor company;<br><br>▪ whether the quantum of the proposed retention payments is reasonable; and<br><br>▪ the business judgment of the board of directors regarding the necessity of the retention payments.<br><br>KERPs and KEIPs may create conflicts between the interests of management and those of the debtor company. For example, where management negotiates debtor-in-possession financing, management may use their strategic position to, for example, negotiate for a higher amount of financing than would otherwise be necessary in order to fund payments to themselves pursuant to a KERP or KEIP. This conflict is mitigated to a degree by the oversight of the court in approving both debtor-in-possession financing and KERPs / KEIPs, and the deference given by the court to the opinion of the proposal trustee or the monitor (who has participated in the formulation of the relevant plan) as to whether it should approve the retention / incentive plan.<br><br>Potential conflicts of interest between management and the debtor company are also addressed by the restriction on voting rights of "related parties" (which may include directors). Under both the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act, a "related person" may vote *against* but not for the acceptance of the proposal or plan.[125] |
| **France** | In the context of in-court proceedings, the French Commercial Code provides for some rules intended to prevent or avoid board / management conflict, including a prohibition against management bidding for the business or the assets of the debtor company during insolvency proceedings. Exceptionally, the court may authorise a sale in favour of managers at the public prosecutor's request.[126] |
| **Hong Kong** | Material interests of the company's directors (whether in their capacity as directors or members or creditors of the company or otherwise) are required to be disclosed in the explanatory statement.<br><br>If the directors or management personnel are receiving shares or options pursuant to a management incentive plan or options scheme, these matters would very likely have to be disclosed in the explanatory statement such that the creditors can form a reasonable judgment on whether the scheme is in their best interests or not.[127] |
| **Malaysia** | Board / management conflicts are generally addressed via the disclosure requirements. In this regard, section 369(1) of the Companies Act 2016 imposes an obligation on the party who summons the court-convened meetings to send to the scheme creditors and / or scheme members a statement explaining the effect of the proposed scheme and in particular, stating any material interests of the directors, whether as directors or as members of the company or otherwise, and the effect of the proposed scheme so far as it is different from the effect on the similar interests of other persons. |

125 Canada report, section 3.3.
126 France report, section 3.3.
127 Hong Kong report, section 3.3.

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| **Singapore** | Board / management conflicts are largely addressed in a restructuring through the disclosure requirements under the scheme regime, as well as the fairness and reasonableness requirements imposed by the court when deciding whether to approve the scheme. If the directors or management personnel are receiving shares or options pursuant to an incentive plan as part of the restructuring, such matters would likely have to be disclosed in the scheme explanatory statement in order to enable creditors to assess whether the allocation of loss and the division of benefits is fair and in their commercial interests.<br><br>Furthermore, if the directors or management personnel are also scheme creditors, their votes on the scheme might be disregarded in the vote count on the basis that they are related creditors.[128] |
| **Switzerland** | Board / management conflicts are largely addressed in a restructuring through the disclosure requirements under the moratorium regime, as well as the conditions for deciding whether to confirm the composition agreement in the confirmation stage. If the directors or management personnel are receiving shares or options pursuant to an incentive plan as part of the restructuring, such matters would likely have to be disclosed in the explanations regarding the draft agreement in order to enable the creditors to assess whether they are in their commercial interests.[129] |
| **United Kingdom** | In a restructuring of a private equity portfolio company, conflicts can sometimes arise where the sponsor of an operational company being restructured has appointed directors on that company to represent its interests. Often sponsors only appoint directors of holding companies at the top of the corporate structure and executive management team members are appointed directors of the operational companies.<br><br>However, where there are shareholder appointees at the level in the corporate structure where the restructuring is being implemented, there is a risk of conflict (for example, where the sponsor is considering injecting additional funding into the group in exchange for a debt write-off). In the case of conflict, the practical solution is sometimes for the board to form a sub-committee of independent directors and delegate the negotiation of the terms of the restructuring with the company's stakeholders to that sub-committee.<br><br>Conflicts can also arise where management incentive plans (MIPs) are proposed as part of a restructuring. In a restructuring, it is commonplace for directors of the relevant company to benefit from MIPs and creditors are often willing to agree to MIPs where they are perceived to assist in achieving successful performance of the company post-restructuring. The management would typically be separately advised and would negotiate terms of the MIP directly with the creditors (assuming the shareholders had no economic interest in the company post-restructuring).[130] |

## 6. "Soft law" framework

The last section of this synopsis investigates three topics relating to non-legally binding instruments such as industry guidelines and best practices that serve to guide or influence conduct on ESG-related matters in a restructuring. Understanding the soft law instruments employed in other jurisdictions can be a useful stepping-stone or middle ground for policymakers that prefer to develop laws in a more conservative and incremental manner. Even if they are not legally binding,

128 Singapore report, section 3.3.
129 Switzerland report, section 3.3.
130 United Kingdom report, section 3.3

they can offer guidance to encourage responsible corporate behaviour by recommending best practices to follow.

### 6.1 Environment (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

There is a dearth of soft law instruments for the protection of the environment in a restructuring across jurisdictions, with one notable exception being France, which has published a guide for insolvency practitioners on best practices for addressing environmental issues under various French insolvency and restructuring proceedings. This is discussed in further detail in Table 11 below.

*Table 11: Soft law framework (industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring)*

| Jurisdiction | Summary |
|---|---|
| **France** | Various government agencies, including the Ministry in Charge of the Environment, the Ministry of Justice and the National Council of Judicial Administrators and Judicial Liquidators have published a joint guide (*Guide à l'attention des administrateurs judiciaires, mandataires judiciaires et de l'inspection des installations classées*) for insolvency practitioners which provides guidance on the environmental obligations of court-appointed administrators and liquidators under safeguard, reorganisation and liquidation proceedings.<br><br>The guide sets out, among other things:<br><br>▪ the national strategy for the management of polluted sites and soils and the missions of the inspection of classified installations;<br><br>▪ the various collective procedures and the missions of judicial administrators and judicial liquidators;<br><br>▪ the environmental obligations of judicial administrators and judicial representatives from the opening of collective proceedings;<br><br>▪ how claims relating to installations subject to environmental regulations should be treated; and<br><br>▪ the restrictions and conditions for assignments and sales in judicial safeguard, reorganisation and liquidation proceedings.<br><br>The guide provides practical guidance on the steps that an insolvency practitioner should take after assuming control of a company which owns or operates sites that are subject to environmental regulation. A template questionnaire is a provided in the guide which lists various items of information and documents which the insolvency practitioner should request from the debtor immediately after the commencement of proceedings. The questionnaire covers issues such as the potential pollutants on site, the surrounding environment, whether the site is being occupied by people, monitoring measures and emergency measures taken to contain hazards.<br><br>Insolvency practitioners are also directed to provide the information collected to the relevant governmental agencies and to obtain their observations on the situation of the sites, and are recommended to consider an on-site inspection by the relevant authorities for complex or large installations. |

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| | The guide also directs judicial administrators (who are appointed to supervise and manage the debtor's business under safeguard or reorganisation proceedings) to request the preparation of an environmental assessment report by the debtor or by an expert appointed by the court. The environmental report (similar to the questionnaire above) covers various issues such as the existence of potential pollution, emergency safety measures taken or planned to be taken, and monitoring measures.<br><br>Guidance is also provided on the classification of environmental claims under various restructuring and insolvency procedures, as well as measures which insolvency practitioners can undertake in the event there are insufficient funds to meet the environmental obligations of the debtor. |

## 6.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

In relation to the protection of employee rights, there are a number of jurisdictions which have guidelines for how a company should develop and carry out retrenchment plans if necessary. While these guidelines apply generally, and not specifically to restructuring scenarios, they can be useful as many of the practices recommended are equally applicable in a restructuring.

These guidelines cover various matters such as:

- considering alternatives to retrenchment (such as salary reductions, shorter work week and no-pay leave);
- communicating and engaging with unions and employees to discuss possible retrenchment measures before implementing them;
- the use of fair and objective criteria in the selection of employees for retrenchment;
- notifying employees of retrenchment in a respectful manner;
- providing retrenchment benefits to enable the affected employees to move on to new employment opportunities; and
- providing assistance to employees to find new employment opportunities.

In Australia, the Australian Restructuring Insolvency and Turnaround Association (ARITA) – the leading industry body for restructuring professionals – has also published practice statements which encourage both employee-specific communication plans to be developed in restructuring and the inclusion of employee-specific provisions in the statutory reports to creditors under voluntary administration.

These issues are outlined in further detail in Table 12 below.

*Table 12: Soft law framework (industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring)*

| Jurisdiction | Summary |
|---|---|
| **Australia** | There are no soft law instruments which apply specifically in a restructuring context for the purpose of directly protecting employee interests, but practice statements published by ARITA encourage both employee-specific communication plans to be developed in a restructuring and the inclusion of |

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| | employee-specific provisions in the statutory reports to creditors under voluntary administration.[131] |
| **Germany** | The "*Verband Insolvenzverwalter und Sachwalter Deutschlands e. V.*" (VID) (Registered Association of Insolvency Administrators), as Germany's professional association of insolvency administrators, has published its guidelines on insolvency and debtor-in-possession proceedings. These guidelines stipulate that the employees of the company have to be informed immediately and continuously about the proceedings and emphasise the employees' interest especially concerning the receipt of insolvency payments.[132] |
| **Guernsey** | The States of Guernsey provide an employment relations portal of documents which governs many aspects of employment, and the responsibility of employers. Within the guide, there is a specific section for "handling redundancy", which details inadmissible reasons for redundancy as well as practical guidance to employers, employees, trade unions and employee representatives. The guide prescribes a checklist of procedures for communicating and consulting with employees and unions before finalising redundancy plans.[133] |
| **Hong Kong** | The Labour Department has issued "Guidelines on What to Do if Wage Reductions and Retrenchments are Unavoidable". The Guidelines set out the recommended practice of employers and what employees can do when wages, reductions or retrenchments are unavoidable.[134] |
| **Malaysia** | The Code of Conduct for Industrial Harmony was introduced as guidelines for employers and employees on the practice of industrial relations for achieving greater industrial harmony. The Code provides for matters concerning redundancy and the retrenchment of workers. The Code identifies the appropriate measures to be adopted before retrenching employees in a restructuring exercise. In the context of the Code, "restructuring" refers to a restructuring of workforce requirements, but the Code would apply equally where a corporate restructuring gives rise to the collective termination of employment.[135] |
| **Mexico** | In Mexico, there are several guidelines or best practices that should be observed to take actions or decisions to protect employees' interests in a restructuring context, such as:<br><br>▪ the C173 - Protection of Workers' Claims (Employer's Insolvency) Convention, 1992 (No. 173);<br><br>▪ the R180 - Protection of Workers' Claims (Employer's Insolvency) Recommendation, 1992 (No. 180); and<br><br>▪ the Criteria issued by the Federal Institute of Insolvency Experts regarding the protection of employees' interests and claims.[136] |
| **Singapore** | The Tripartite Advisory on Managing Excess Manpower and Responsible Retrenchment is a set of guidelines jointly promulgated by the Ministry of Manpower, the National Trades Union Congress and the Singapore National Employers Federation. The Advisory sets out guidelines relating to how |

131 Australia report, section 4.2.
132 Germany report, section 4.2.
133 Guernsey report, section 4.2.
134 Hong Kong report, section 4.2.
135 Malaysia report, section 4.2.
136 Mexico report, section 4.2.

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| | Singapore businesses should seek to retrench employees in a responsible manner.[137] |
| **South Africa** | The Code of Good Practice: Dismissal Based on Operational Requirements provides guidelines to employers for the correct procedural and substantive requirements in order to carry out dismissals based on operational requirements (i.e. retrenchments).[138] |

### 6.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

Many jurisdictions impose statutory duties on restructuring practitioners to avoid conflicts of interest. Nevertheless, industry guidelines or codes of conduct remain relevant and useful as they can help to provide practical guidance on how to identify and address potential conflicts of interest. Table 13 below summarises the various industry codes promulgated across the jurisdictions surveyed.

These codes prescribe, among other things, measures to identify potential conflicts of interests, safeguards to apply in the event of potential conflicts (such as disclosing the potential conflicts and obtaining the consent of the interested parties) and circumstances in which conflicts of interests are unavoidable and a practitioner should decline an appointment.

*Table 13: Soft law framework (Industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to)*

| Jurisdiction | Summary |
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| **Australia** | ARITA has published a Code of Practice, which imposes a detailed set of rules that bind ARITA members and operate additionally to the legal duties. Among other things, those rules restrict the appointments which practitioners take, and prescribe certain disclosures which must be made in reports to creditors. Further, ARITA members, their firms and their firms' partners and employees must not derive any profit or advantage from an administration (including by buying property from, or selling property to, an entity in administration) without legislative or judicial approval.[139] |
| **British Virgin Islands** | Insolvency practitioners are governed by the Insolvency Code of Practice (issued under section 487 of the Insolvency Act). Chapter IV sets out the ethical principle that a licensee must conduct all insolvency work. It notes that the greatest threat to an insolvency practitioner's objectivity is likely to be a conflict of interest. An insolvency practitioner must be aware of actual or potential conflicts of interest in the form of self-review threats and self-interest threats.<br><br>A self-review threat to objectivity may arise where an insolvency practitioner, or his or her firm, has or had a material professional relationship with the company or individual in relation to which or whom insolvency work is performed. The threat that lies behind a material professional relationship is that the licensee, who is the custodian of what are often competing interests in the prosecution of insolvency work, may improperly and inappropriately favour one or more of these interests. In that way, an insolvency practitioner's objectivity would be lost. Any such relationship would usually require the insolvency practitioner to decline insolvency work.[140] |

137 Singapore report, section 4.2.
138 South Africa report, section 4.2.
139 Australia report, section 4.3.
140 British Virgin Islands report, section 4.3.

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| | A self-interest threat is one that could affect the reasoning an insolvency practitioner applies because it is, or might be, affected by considerations that either favour or are prejudicial or disadvantageous to the insolvency practitioner.[141] |
| **Canada** | The Canadian Association of Insolvency and Restructuring Professionals (CAIRP) has both rules and standards of professional conduct applicable to its members and candidates registered in their qualification programme. Each of these regulatory schemes include provisions requiring that applicable professionals take reasonable steps to identify circumstances that could pose a conflict of interest, apply necessary safeguards in situations of conflict, such as notifying the client of the circumstances giving rise to the conflict and obtaining their consent to act in such circumstances, and decline to accept an engagement or resign from an engagement if a conflict of interest cannot be appropriately resolved with the application of safeguards.[142] |
| **Hong Kong** | The Hong Kong Institute of Certified Public Accountants (HKICPA) has issued a Code of Ethics for Professional Accountants in the HKICPA Members' Handbook. Part E Section 500 of the HKICPA Members' Handbook specifically deals with professional ethics in liquidation and insolvency (HKICPA Ethics Code). The HKICPA Ethics Code expressly covers insolvency practitioners acting as "administrator, manager, adjudicator or any other similar role, however described in respect of a scheme of arrangement between a company and its creditors".<br><br>The HKICPA Ethics Code provides a framework which insolvency practitioners can use to identify actual or potential threats to compliance with the fundamental principles and determine whether there are any safeguards that may be available to mitigate them.[143] |
| **India** | The Insolvency and Bankruptcy Board of India (IBBI) has established a code of conduct for insolvency professionals undertaking assignments under the Insolvency and Bankruptcy Code 2016 and it has the force of law. The following measures have been provided under this code of conduct to avoid any potential conflict of interest:<br><br>▪ insolvency professionals are bound to act with objectivity in their professional dealings by ensuring that their decisions are made without any conflict of interest, whether directly connected to the insolvency proceedings or not;<br><br>▪ insolvency professionals are also required to disclose the details of any conflict of interests to stakeholders whenever they come across any relevant conflict during an assignment;<br><br>▪ insolvency professionals are restricted from acquiring any of the assets of the debtor, whether directly or indirectly;<br><br>▪ in cases where insolvency professionals are dealing with a debtor's assets during liquidation or a bankruptcy process, they are also required to ensure that they and their relatives do not knowingly acquire any such assets, unless it is shown that there was no impairment of objectivity, independence or impartiality in the liquidation or bankruptcy process and the IBBI's approval was obtained; and |

141 *Ibid*.
142 Canada report, section 4.3.
143 Hong Kong report, section 4.3.

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| | ▪ insolvency professionals are required to disclose their relationship, if any, with the corporate debtor, other professionals engaged by them, financial creditors, interim finance providers, and prospective resolution applicants to the respective insolvency professional agency of which they are a member.[144] |
| **Malaysia** | Restructuring professionals are guided by the Insolvency Guidance Notes (Guidance Notes) provided by the Malaysian Institute of Accountants (MIA). The Guidance Notes outlines the means for identifying and addressing conflicts of interest involving an insolvency practitioner. The Guidance Notes also provide examples of certain situations (e.g. involving material professional relationships between an insolvency practitioner and a company) in which an insolvency practitioner should decline to act.[145] |
| **People's Republic of China** | The Supreme People's Court of the PRC has formulated the Provisions on the Appointment of Administrators in the Trial of Insolvency Cases (PAATIC), which prescribe guidelines in relation to avoiding conflicts of interest for restructuring professionals. The PAATIC list various scenarios under which a professional institution or a member of such an institution may be deemed to have an interest in the case, such as:<br><br>▪ having provided long-term services to the debtor within three years before commencement of the proceeding;<br><br>▪ acting as the controlling shareholder or actual controller of the debtor or creditor within three years before commencement of the proceeding; and<br><br>▪ acting as financial and / or legal counsel of the debtor or creditor within three years before commencement of the proceeding.[146] |
| **Singapore** | The Insolvency Practitioners Association of Singapore's (IPAS) Code of Professional Conduct and Ethics (IPAS Code) prescribes general guidelines as to how insolvency professionals who are members of IPAS should deal with potential conflicts of interest, without specific reference to restructuring scenarios. The IPAS Code states that insolvency professionals should:<br><br>▪ take reasonable steps to identify circumstances that could pose a conflict of interest;<br><br>▪ apply necessary safeguards in situations of conflict, such as notifying the client of the circumstances giving rise to the conflict and obtaining their consent to act in such circumstances;<br><br>▪ apply additional safeguards such as using separate teams, implementing procedures to prevent access to information and to maintain security and confidentiality, and regularly reviewing the application of safeguards by a senior individual not involved with the relevant client engagements; and<br><br>▪ decline to accept an engagement or resign from one or more conflicting engagements if a conflict of interest creates a threat to one or more of the fundamental principles, including objectivity, confidentiality or professional behaviour, that cannot be eliminated or reduced to an acceptable level through the application of safeguards.[147] |

144 India report, section 4.3.
145 Malaysia report, section 4.3.
146 People's Republic of China report, section 4.3.
147 Singapore report, section 4.3.

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| **South Africa** | The South African Restructuring and Insolvency Practitioners Association's (SARIPA) Code of Ethics, which applies only to members of SARIPA, is specifically tailored for restructuring professionals, being liquidators and trustees of insolvent estates and business rescue practitioners. Some relevant provisions in the SARIPA Code include the following:<br><br>▪ practitioners must be honest, truthful and conscientious in the performance of their services and must avoid all relationships and direct or indirect interests that will adversely influence, impair, or threaten their integrity or in any manner create the impression of doing so;<br><br>▪ practitioners must render and perform their services free from any improper influence or pressure and in an impartial and independent manner;<br><br>▪ practitioners owe a fiduciary responsibility to creditors and affected persons and generally all parties involved and have a duty to be fair and act without bias in assessing the competing interests of stakeholders; and<br><br>▪ practitioners may not accept any appointment if they will be unable to render and perform their services in respect of an estate impartially or independently by reason of relationships or direct or indirect interests or for whatever other reasons. Practitioners may not by means of any misrepresentation or reward or offer of any reward, whether direct or indirect, induce or attempt to induce any person to vote for their appointment.[148] |
| **The Netherlands** | The Dutch Association for Insolvency Practitioners (INSOLAD) published practice rules for bankruptcy trustees in April 2019 with the aim of laying down the best practice processes for bankruptcy trustees in writing. The practice rules aim to fill gaps where neither the law / statute nor case law provides clarity for bankruptcy trustees as to how to act and follow the best practice that most bankruptcy trustees believe to be valid. The practice rules solely intend to provide guidance and are not intended to be enforceable or binding in any way.[149] |

## 7. ESG in financing

Before concluding this synopsis with a roadmap for policymakers, we synthesise some of the emerging market developments and trends in the ESG financing space that may have an impact on the restructuring sphere in the years to come. The shift towards ESG-friendly policies in financial markets is happening slowly but surely. As financial institutions, spurred on by central banks, imbed ESG factors into the construction and management of their investment and loan portfolios, less ESG-friendly industries and sectors may see less capital available for deployment. Companies exposed to greater ESG risk may experience an increase in their cost of capital,[150] as well as added costs of complying with ESG requirements, threatening their profitability and ability to reliably service their debt.

A common trend observed in many of the jurisdictions surveyed is the significant rise in financial institutions participating in international efforts to achieve ESG targets in their lending and investment portfolios or to apply ESG-risk management policies in their investment decisions. These efforts include:

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148 South Africa report, section 4.3.
149 The Netherlands report, section 4.3.
150 As discussed in the introduction, credit ratings agencies such as Moody's and Standard and Poor's now directly integrate ESG risk assessment in their credit ratings, which ultimately makes capital costlier for companies with greater ESG risk.

- the United Nations Environment Programme Finance Initiative (UNEPFI) Net-Zero Banking Alliance, which is an international consortium of 130 banks from 41 countries representing US $74 trillion in assets (over 40% of global banking assets). Banks in the Net-Zero Banking Alliance have committed to reduce the greenhouse gas emissions attributable to their lending and investment portfolios, with the aim of achieving net-zero emissions by 2050. They have also committed to setting emissions targets for 2030 (or sooner), publishing emissions data in line with best practice, and within a year of setting targets, disclosing progress on their transition strategy and setting out proposed actions and climate-related sectoral policies. The banks' first 2030 targets will focus on priority sectors which are the most greenhouse gas-intensive sectors within their portfolios;[151]

- the UNEPFI's Principles for Responsible Banking, which commit signatories to aligning their business strategy with the UN Sustainable Development Goals and the Paris Climate Agreement. There are currently 324 signatories to the Principles, representing US $89.4 trillion in assets (around 50% of global banking assets). Banks who commit to the Principles are required to undertake a three-step process of: (i) identifying the most significant impacts of products and services on the societies, economies and environments the bank operates in; (ii) setting and achieving measurable targets in the bank's areas of most significant impact; and (iii) publicly reporting on progress on implementing the Principles;[152] and

- the Equator Principles, which prescribe a set of principles for the assessment, management and monitoring of environmental and social risks when financing large infrastructure and industrial projects. The Equator Principles have been adopted by 138 financial institutions in 38 countries. The Principles require participating financial institutions to ensure that borrowers or investees conduct environmental and social assessment, develop management systems to ensure compliance with the applicable environmental and social standards, engage with affected communities, workers and other stakeholders, and develop grievance mechanisms to facilitate resolution with these affected stakeholders. Participating financial institutions are also required to ensure that an independent environment and social consultant is engaged to review, monitor and report on a project's compliance with the Equator Principles.[153]

Relatedly, another major trend which has been observed is the increased issuance of bonds and loans with an ESG dimension to them. These include:

- sustainability-linked bonds and loans, in which the commercial terms, such as interest rates or drawdown limits, could be tied to the borrower's performance on pre-determined ESG metrics or targets (without any restrictions on what the bond / loan proceeds can be used to fund);

- green bonds and loans, in which the financing proceeds are used exclusively for green initiatives – such as renewable energy and green infrastructure projects, pollution prevention, procuring low carbon transport solutions and climate change adaptation; and

[151] United Nations Environment Programme Finance Initiative, Net-Zero Banking Alliance website, accessible at: https://www.unepfi.org/net-zero-banking (last viewed on 26 May 2023). Among the jurisdictions surveyed for this book, Australia, Brazil, Canada, Hong Kong, Japan, Mexico, Singapore, South Africa, Spain, Switzerland, the Netherlands, the United Kingdom and the United States have banks which are members of the Net-Zero Banking Alliance: see section 5.2 of the respective country reports.

[152] United Nations Environment Programme Finance Initiative, Principles for Responsible Banking website, accessible at: https://www.unepfi.org/banking/more-about-the-principles/ (last viewed on 26 May 2023). The Principles for Responsible Banking Guidance Document is accessible at: https://www.unepfi.org/wordpress/wp-content/uploads/2022/04/PRB-Guidance-Document-Jan-2022-D3.pdf (last viewed on 26 May 2023). The Key Steps to be Implemented by Signatories is accessible at: https://www.unepfi.org/wordpress/wp-content/uploads/2022/09/13-Key-Steps-to-be-Implemented-by-Signatories.pdf (last viewed on 26 May 2023).

[153] Equator Principles EP4 (July 2020), accessible at: https://equator-principles.com/app/uploads/The-Equator-Principles_EP4_July2020.pdf (last viewed on 26 May 2023). Among the jurisdictions surveyed for this book, Argentina, Australia, Brazil, Canada, Hong Kong, Japan, Mexico, China, Singapore, South Africa, the Netherlands, the United Kingdom and the United States have financial institutions which are members of the Equator Principles Association: see section 5.2 of the respective country reports.

- social bonds and loans to support various social endeavours – such as affordable infrastructure, access to health and nutrition, affordable housing, employment generation, food security and access to essential services.

These ESG-linked bonds and loans have been observed in Australia,[154] Bermuda,[155] Canada,[156] France,[157] Germany,[158] Guernsey,[159] Hong Kong,[160] India,[161] Indonesia,[162] Japan,[163] Kenya,[164] Malaysia,[165] Mexico,[166] New Zealand,[167] Nigeria,[168] Poland,[169] the PRC,[170] Russia,[171] Singapore,[172] South Africa,[173] Spain,[174] Switzerland,[175] Thailand,[176] the Netherlands,[177] Uganda,[178] the United Kingdom[179] and the United States.[180]

In conjunction with developments in the private sector, many central banks and regulators across the jurisdictions surveyed have launched various initiatives to boost ESG-friendly investments. For example:

- in Australia, the Clean Energy Finance Corporation (CEFC), a Commonwealth Government corporation, was established by statute in 2012 with the intention of facilitating increased flows of finance into the clean energy sector. The CEFC was granted seed capital of AU $10 billion, and operates under executive government mandates to invest those Commonwealth funds in clean energy projects;[181]

- Hong Kong has administered a three-year pilot scheme known as the "Pilot Green and Sustainable Finance Capacity Building Support Scheme" to provide subsidies for the training and acquisition of relevant professional qualifications in sustainable finance as part of a collaborative effort to build capability for the industry;[182]

- the Monetary Authority of Singapore, which is the central bank of Singapore, has launched two grant schemes to encourage sustainable bonds and loans: (i) the Sustainable Bond Grant Scheme, which provides grants to issuers of sustainability-linked bonds to offset the costs of conducting external reviews or ratings done for the purpose of demonstrating alignment with any internationally-recognised green, social, sustainability and sustainability-linked principles or standards; and (ii) the Green and Sustainability-Linked Loan Grant Scheme, which provides grants to defray the expenses of engaging independent service providers to validate the

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154 Australia report, section 5.1.
155 Bermuda report, section 5.2.
156 Canada report, section 5.1.
157 France report, section 5.1.
158 Germany report, section 5.1.
159 Guernsey report, section 5.1.
160 Hong Kong report, section 5.1.
161 India report, section 5.1.
162 Indonesia report, section 5.1.
163 Japan report, section 5.1.
164 Kenya report, section 5.1.
165 Malaysia report, section 5.1.
166 Mexico report, section 5.1.
167 New Zealand report, section 5.1.
168 Nigeria report, section 5.2.
169 Poland report, section 5.1.
170 PRC report, section 5.1.
171 Russia report, section 5.2.
172 Singapore report, section 5.1.
173 South Africa report, section 5.1.
174 Spain report, section 5.1.
175 Switzerland report, section 5.1.
176 Thailand report, section 5.1.
177 The Netherlands report, section 5.1.
178 Uganda report, section 5.1.
179 United Kingdom report, sections 5.1.1 to 5.1.5.
180 United States report, section 5.1.
181 Australia report, section 5.3.
182 Hong Kong report, section 5.3.

green and sustainability credentials of qualifying loans, as well as grants to encourage banks to develop green and sustainability-linked loan frameworks;[183] and

- in Malaysia, the Securities Commission Malaysia has launched the Sustainable Responsible Investment Sukuk (Islamic bonds)[184] and Bond Grant Scheme, which covers up to 90% of the actual costs incurred by issuers on external assessments conducted to ensure their compliance with the Sustainable Responsible Investment Sukuk Framework.[185]

Additionally, in many jurisdictions surveyed, financial regulators are now requiring financial institutions such as banks and insurance companies to incorporate climate and social risk assessment and management into their existing risk management frameworks.[186] Financial regulators in Australia, Canada and Hong Kong have also conducted climate risk assessments to assess the potential impact of climate change on their respective financial sectors. Notably, the Australian Prudential Regulation Authority (APRA) in Australia has observed that climate risk impacts are likely to be concentrated in specific industries that are more exposed to transition risks, such as mining, manufacturing and transport. In response to the potential losses, the Australian banks that underwent the climate risk assessments predicted that they would adjust their risk appetites and lending practices, such as cutting back on high loan-to-valuation lending and reducing their exposure to higher risk regions and industries.[187]

The various trends discussed above are still in their nascent stages. However, as momentum builds on these developments, tectonic shifts will occur within the financial landscape. Ultimately, the diversion of capital towards more ESG-friendly businesses and away from less ESG-friendly ones might pose challenges to certain industries that are exposed to greater ESG risk (such as the fossil fuels sector and connected support services like exploration, extraction, refining and transportation). There is a danger of a “perfect storm” brewing, as the companies that are most exposed to ESG risk could also be the most susceptible to facing the ESG problems discussed in this book. Cases such as *Apex Oil* (discussed in section 3) and *Orphan Well* (discussed in section 4.1) involving oil companies illustrate how serious environmental issues can arise in the wake of insolvency. It is critical for policymakers to look ahead to address these risks pre-emptively.

## 8. Roadmap ahead

Despite the wide differences in restructuring and insolvency regimes across the globe, this synopsis (informed by the accompanying jurisdictional reports) has highlighted some broad commonalities in how ESG issues can be addressed under restructuring law. There are targeted ways of protecting ESG interests within the restructuring space which do not require a wholesale reworking of restructuring laws.

To aid policymakers that are considering ESG reform under their restructuring laws, the Annex below synthesises the key issues that should be considered under the various topics analysed in this book. The aim of the Annex is to provide a roadmap to guide policymakers on the specific areas that can be considered in their reform agenda. The roadmap is not intended to be prescriptive in nature, as the right balance of the competing policy considerations will necessarily be different for each jurisdiction, depending on local social, economic and other issues. Nevertheless, policymakers can take guidance from the approach adopted by other jurisdictions where relevant to aid their reform efforts.

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183 Singapore report, section 5.3.
184 Sukuk refers to Islamic bonds.
185 Malaysia report, section 5.3.
186 Australia, Brazil, Canada, Germany, Hong Kong, Kenya, Malaysia, Nigeria, Singapore, South Africa, Uganda and the United Kingdom: see section 5.3 of the respective country reports.
187 Australia report, section 5.3.

**Annex: policy roadmap for ESG issues in restructuring matters**

| Topic | Issues to consider |
|---|---|
| **Restructuring of liabilities** | ***Environmental liabilities***<br>▪ Should certain types of environmental liabilities such as fines or statutory liabilities (e.g. clean-up costs) be granted preferential treatment over unsecured debts? (see Table 1)<br>▪ Should clean-up costs incurred by government regulators be secured over the property on which environmental clean-up action was performed? (see Table 2)<br>▪ Should certain types of environmental orders issued by regulators be non-dischargeable in a restructuring? (see Table 3)<br>▪ For jurisdictions with disclaimer regimes, should environmental obligations be capable of being disclaimed and under what conditions? (see Table 4) |
| | ***Health and safety-related liabilities***<br>▪ Should certain types of health and safety-related liabilities (such as work injury compensation or personal injury claims) be granted preferential treatment over unsecured debts? (see Table 5)<br>▪ Should certain types of health and safety liabilities (particularly employment-related liabilities) be secured over the employer's property? (see Table 6) |
| | ***Third party releases in favour of directors and officers***<br>▪ Should third party releases in favour of directors and officers (particularly relating to non-guarantee claims) be permitted, and, if so, under what conditions? (see Table 7) |
| **Protection of stakeholder interests** | ***Environmental interests***<br>▪ Should environmental protection authorities be granted standing to object to a restructuring, for example if there is uncertainty about the debtor's ability to meet its environmental obligations? (see Table 8)<br>▪ If a restructuring plan involves matters that require the permission, authorisation, or a licence by an environmental regulator, should it be a condition for the court's approval of the restructuring plan that the environmental regulator does not object to the restructuring? (see Table 8) |
| | ***Labour interests***<br>▪ Should employees be entitled to appoint at least one representative on the creditors' committee (if any) in a restructuring? (see Table 9)<br>▪ Should trade unions or other employee representative bodies be given rights to represent employees in any negotiations or court proceedings in a restructuring? (see Table 9) |

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|---|---|
| | ▪ Should courts be empowered to establish committees for employees and / or to appoint representative counsel for employees where necessary to protect the employees' interests? (see Table 9) |
| | ***Board / management conflicts***<br><br>▪ In debtor-in-possession restructurings, if the directors and / or managers are receiving any benefits under the restructuring (such as shares under a management incentive plan), what measures should they be required to take to minimise conflicts of interests and what factors should a court consider in determining whether to permit such arrangements? (see Table 10). |
| **"Soft law" framework** | ***Environmental protection***<br><br>▪ What guidelines or best practices should be followed in relation to dealing with environmental matters in a restructuring (such as environmental assessments, communication with environmental regulators and addressing situations where there is insufficient funding to comply with environmental obligations)? (see Table 11) |
| | ***Protection of employee rights***<br><br>▪ What guidelines or best practices should be followed in relation to dealing with the retrenchment of employees in a restructuring (such as considering potential alternatives to retrenchment, communication with unions and employees and the use of fair and objective criteria for retrenchment)? (see Table 12) |
| | ***Avoidance of conflicts of interests for restructuring professionals***<br><br>▪ What guidelines or best practices should be followed by restructuring professionals in identifying potential conflicts of interests, applying safeguards in the event of such potential conflicts and determining circumstances in which conflicts of interests are unavoidable and a professional should decline an appointment? (see Table 13) |

# ARGENTINA

# 1. General overview of the restructuring regime

Law Nr 24522 (as amended, the Argentine Bankruptcy Law or ABL) provides the general regime for reorganisations and bankruptcy proceedings in Argentina. The formal procedures in the ABL for companies in financial distress are the reorganisation proceeding (*concurso preventivo*), the bankruptcy proceeding (*quiebra*) – the aim of which in principle is the liquidation of the assets of the insolvent person or entity – and an out of court restructuring (*acuerdo preventivo extrajudicial* or APE).

There are special legal frameworks for certain insolvency cases, such as those of financial entities[1] and insurance companies.[2] In addition, Law Nr 25284 provides a particular insolvency framework for the restructuring of certain sports organisations. Under this regime, when a non-profit sports organisation is declared bankrupt, an administration trust is created with all the assets of the debtor and managed by a fiduciary body, judicially monitored. The fiduciary body is entrusted with the liquidation of the assets and distribution of the proceeds with the admitted creditors, as per the priorities set out in the ABL.

## 1.1 Formal restructuring procedures

The ABL provides for two statutory restructuring proceedings that may only be commenced by the debtor: the reorganisation proceeding (*concurso preventivo*) and an out of court restructuring proceeding (the APE).

### *1.1.1 Reorganisation proceeding*

The main formal restructuring proceeding is the *concurso preventivo,* a voluntary insolvency proceeding through which the debtor attempts to continue its activities by restructuring its obligations. The goals of this proceeding are to permit the reorganisation of a debtor's business in order to avoid liquidation *(quiebra*), to develop a plan for the payment of creditors' claims, and to allow the continuation of the debtor's activities as a viable entity. The proceeding has certain similarities to the United States Chapter 11 proceeding. Certain entities are not eligible for a *concurso preventivo* (e.g. financial entities and insurance companies, among others).

With the commencement of the *concurso preventivo*, the court appoints a provisional creditors' committee comprised of the three unsecured creditors with the largest claims as declared by the debtor and a representative of the debtors' employees. Members of the committee are then replaced when categories of creditors are established and the creditors with the largest claims in each category and two representatives of the debtors' employees are appointed to the committee. The final creditors' committee is proposed by the debtor in the restructuring plan and continues to function in the event of a subsequent bankruptcy proceeding (e.g. if the voluntary restructuring fails). The creditors' committee acts as an information and advisory body and the final committee (proposed in the plan) monitors the performance and execution of the approved restructuring plan.

In addition to the creditors' committee, the trustee *(síndico*) plays a key role in a *concurso preventivo*, protecting creditors' interests and providing information and advice. The trustee supervises the management and administration of the company and advises the court about the

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1 Law Nr 21526 (Financial Entities Law) provides the rules for the insolvency of banks or financial entities and sets out a special procedure to be followed before the Central Bank of Argentina, which may exclude and transfer certain assets and liabilities to a trust, as allowed under section 35-bis of the Financial Entities Law. The list of secured creditors with priority over the trust's assets includes the credits of depositors, labour claims and the Central Bank of Argentina. Assets not transferred to the trust shall be sold and the liquidator, appointed by the court, shall distribute the proceeds between the creditors whose proof of claim has been accepted, following priorities set out in the Financial Entities Law.

2 The insolvency of insurance companies is covered by Law Nr 20091. Liquidation proceedings require the intervention of the Insurance Commission (*Superintendencia de Seguros de la Nacion*). Beneficiaries of life insurances and insurance claims credits are afforded general priority over unsecured claims. Liquidation shall be carried out by the liquidator, acting as trustee, appointed by the Insurance Commission.

claims submitted and the debtor's restructuring plan, as well as preparing and rendering special reports about the claims and the evolution of the company's business.

The court order instituting the *concurso preventivo* triggers the automatic stay of new monetary claims whose cause or title pre-dates the filing of the *concurso preventivo.* These claims can then only be submitted to the appointed trustee under a system whereby the creditors file their proofs of claim *(verificación de créditos).* This order also suspends any enforcement of pre-petition claims not secured by pledge or mortgage. However, there are some exceptions, such as certain types of judicial procedures filed before that date, which may continue their proceedings at their original courts, and labour claims, among others. The commencement of the *concurso preventivo* also causes the accrual of interest on claims (except for certain labour claims) not secured by pledge or mortgage to be suspended.

During a *concurso preventivo*, the debtor conserves possession and administration of its assets in the ordinary course of business, subject to certain restrictions. The debtor will be under the supervision of the trustee, who will have full access to the company's business records and will report any breach or violation to the court. For performing certain acts regarding registrable assets (such as real estate, airplanes and vehicles), disposal or lease of going concerns, granting of pledges and any other matters outside the ordinary course of business, the debtor shall request the court's authorisation.

In the initial order opening the proceedings, the court prescribes a timeframe for the pre-petition creditors (secured and unsecured) to submit their proofs of claim before the trustee. At the end of that period, the trustee issues a report with its recommendation as to whether to accept or reject (totally or partially) the claims submitted and the court then issues a ruling about the claims filed (*resolución verificatoria*). Only creditors who are verified and recognised in the ruling will have voting rights regarding the debtor's restructuring plan.

Any claim against a company may be restructured under a *concurso preventivo*, including contingent, unproven or unliquidated claims. There are no restrictions on the types of debt which may be restructured under a reorganisation proceeding. Non-monetary claims *(obligaciones de hacer o de no hacer)* shall be converted into a monetary claim for all purposes of the proceeding.[3]

If the court does not admit a claim in the *resolución verificatoria*, the creditor can request a review of the decision before the same court but in a special ancillary proceeding where the creditor shall offer more evidence to support its claim. When an interested party does not file a review motion against the first decision and does not file an appeal against an unfavourable decision, those decisions have the effect of *res judicata*. Creditors who do not present the proof of claim in due time can present a late filing (*verificación tardía*), but they shall not be entitled to vote or consent to the plan.

The debtor shall present its restructuring plan aimed, at least, towards unsecured creditors. The debtor may include, at its discretion, secured creditors in the plan but in that case it must obtain the unanimous consent of secured creditors with special preference. The debtor enjoys an exclusivity period (of 90 to 120 business days) to offer a restructuring plan and obtain the consent of the majority of creditors representing more than one half in number (headcount majority) and at least two thirds of the principal amount of the claims (principal majority) subject to the plan. Controlling shareholders, managers, directors or their assignees (appointed within one year prior to the filing date) do not have voting rights.

Creditors are separated into classes and a distinction is made between secured, unsecured, unsecured labour and contractually subordinated claims. The debtor may propose, based on reasonable grounds, to divide the creditors further into subcategories, such as financial creditors, service providers and tax authorities. However, the debtor must obtain at least the legal majorities (headcount and principal) for the restructuring plan in each class of unsecured creditors. Therefore, depending on the composition of the unsecured creditors' category, the debtor may easily negotiate and gather consents in a general category of unsecured claims, without dividing creditors into subcategories.

3 ABL, s 19.

If, at the end of the exclusivity period, the debtor does not obtain consent to the plan reaching the legal majorities, the court can exercise its cram down power and impose the plan over the non-consenting creditors where:

- the debtor has obtained the majorities in at least one category of creditors;
- the collective creditors' consents represent at least three quarters of the aggregate principal amount of unsecured claims;
- the plan does not discriminate between the dissident categories of creditors (such as banning the creditors from electing an available alternative restructuring option, if any); and
- payment received under the plan is not less than the dividend the dissident creditors would receive in a bankruptcy proceeding, liquidating the debtor's assets.

Provided the debtor has obtained the legal majorities (headcount and principal majority), the court shall issue a resolution stating that the debtor has obtained the necessary majorities for approval of the restructuring plan. Within a specific timeframe of five days after the resolution, the plan may be challenged by dissenting creditors involved in the restructuring. There may be challenges to the calculation of the required majorities or alleging concealment or exaggeration of the assets or liabilities, among others. The court shall analyse any challenge submitted and adjudicate bankruptcy if the challenge is admitted, except in the case of certain companies (limited liability companies and corporations) that follow a different procedure called "*salvataje*".[4]

If no challenges are filed, the court shall examine the terms offered in the debtor's plan. Even if the debtor has achieved the legal majorities, the court is entitled to reject endorsement of the plan if it does not comply with the rules of the ABL, or if the terms are deemed abusive. The ABL does not provide significant criteria for assessing whether a restructuring plan may be deemed fair or abusive. Several guidelines have been provided by case law and scholars, whose aim is to distinguish between fair and abusive restructuring plans, for example through comparison of the dividend derived from liquidation *vis-à-vis* the amount to be paid under the plan, verification that all creditors are equally treated within each category and that no unfair discrimination prevails, and confirmation that there are no excessive sacrifices imposed on dissident creditors. In certain major cases based on the number of workers of the company, the magnitude of the company in the market and the macroeconomic context of the country, the courts have granted the debtor a new opportunity to improve the terms of the plan (what has been called the third way).

If the restructuring plan is endorsed and approved by the court, it becomes binding on all pre-petition unsecured creditors, whether or not they have consented to the plan.

### 1.1.2 *Out of court restructuring*

The ABL provides a framework for the *acuerdo preventivo extrajudicial*, that is basically an agreement entered into by a debtor and a certain majority of its creditors that may be binding on all the creditors involved in the agreement if the court endorses the plan, whether the creditors have expressly accepted the plan or not. It has certain similarities with the pre-packaged proceeding under the United States Bankruptcy Code.

A debtor that suspends its payments or is undergoing economic or financial difficulties of a general nature may reach an agreement with its creditors and then submit the agreement for judicial endorsement. The debtor starts negotiating a plan proposal with its main creditors with the aim of obtaining the required creditors' consents to meet the headcount and the principal

[4] If the debtor is a limited liability company, corporation, cooperative or company with state participation, before declaring the debtor bankrupt, the court shall initiate a bidding process opened with a five-day period for the registration of the creditors, workers' cooperative or other third parties interested in acquiring the debtor's equity and submitting alternative competing reorganisation plans. The debtor may also file a new competing restructuring plan or continue gathering consents for the previously submitted plan. If there is no alternative reorganisation plan or no plan is agreed to by the requisite majority of creditors, the court will declare the debtor bankrupt.

majorities and then requesting the judicial endorsement of the APE. The plan may contain precedent conditions that need to be complied with to become effective, such as a specific deadline or a certain minimum of consenting creditors. The debtor seeking endorsement of an out of court restructuring agreement keeps possession of its assets and full administration of its property without limitations, other than those expressly assumed by the debtor in the agreement covenants.

In order to request judicial endorsement, the debtor must meet minimum formal requisites (similar to those required for a *concurso preventivo*, related to assets and liabilities) and substantive requisites, such as consents granted by creditors representing the legal majorities. The APE is not applicable to debtors that do not qualify for bankruptcy proceedings or that have special insolvency proceedings (such as financial entities or insurance companies).

When the company files for judicial endorsement of the plan, the court analyses the equal treatment of all the creditors, whether or not the restructuring plan can reasonably be achieved and if the terms are abusive (such as offering less than creditors will collect in a bankruptcy proceeding). If the restructured debts include publicly offered notes, negotiable obligations or other securities, the debtor will generally carry out an exchange of its outstanding notes for new notes reflecting the terms of the restructuring. In addition, the APE allows the debtor to direct the restructuring towards certain groups of creditors (such as financial creditors), setting aside other kinds of liabilities (such as tax authorities or providers).

The debtor may propose to classify creditors into subcategories, as in the *concurso preventivo*, but shall gather consents in all categories, as described above.

The restructuring plan is governed by contract law and may contain whatever provisions the debtor and the participating creditors deem convenient. A judicially endorsed plan shall have the same effect as a restructuring plan obtained in a formal judicial reorganisation proceeding (a *concurso preventivo*).

An APE is a simplified procedure (much faster than a *concurso preventivo*), it entails minor costs (the court tax is lower, and the procedure does not require a trustee appointed by the court) and failure to obtain court approval of the plan does not imply adjudication of bankruptcy.

### 1.2 Informal restructuring procedures

Informal restructurings are conducted primarily on a consensual basis and are governed by non-statutory frameworks.

A consensual restructuring frequently starts with the appointment of legal and financial advisers, and in scheduling meetings with the main creditors to analyse the current financial status and possible restructuring schemes. From a debtor's perspective, standstill agreements or default waivers form part of initial conversations; while creditors, on the other hand, frequently form a steering committee as a supervisory body to monitor financial status and approve some relevant acts (such as the transfer of assets, material disbursements, new indebtedness and the granting of securities). A controller may be appointed by the creditors' steering committee for inside supervision of the company.

Negotiations with certain creditors, as members of an ad hoc steering committee, may evolve in the launching of a proposal. If the proposal receives the support of a significant majority of creditors, the restructuring of the indebtedness could be managed through a voluntary exchange agreement and, should consenting creditors reach a certain legal threshold, the debtor may reserve the right to convert this voluntary exchange into an *acuerdo preventivo extrajudicial* and request court approval, as described above.

## 2. Restructuring of ESG-related liabilities

### 2.1 Environmental (E): restructuring environmental liabilities

Environmental liabilities may be restructured in the same way as ordinary claims under a restructuring proceeding (*concurso preventivo*) or an out of court restructuring (APE).

The Argentine Bankruptcy Law does not provide for particular solutions concerning the treatment of environmental liabilities. There are no special restrictions or conditions that apply when restructuring environmental liabilities.

#### *2.1.1 Types of environmental liabilities*

In a federal country such as Argentina, environmental rights and the protection of the environment in general are contemplated in the National Constitution since the 1994 Amendment. The Argentine system is one in which three levels or tiers of authorities may exercise concurrent (and sometimes overlapping) jurisdiction. Aside from the national level, the country's 23 provinces and the Autonomous City of Buenos Aires have their own environmental laws and regulations. Further, the several municipalities comprising a province may also have ordinances and enforcing agencies of their own.

At the national (federal) level, the basic statute is the so-called General Environmental Law Nr 25,675, which – according to the Constitution – sets up the minimum environmental policy standards to be observed by all jurisdictions within the country. Provinces may establish standards which are more stringent than those set forth by the General Environmental Law. The provinces (and the City of Buenos Aires) cannot, on the other hand, establish standards which are less demanding than those fixed at the federal level. Finally, even at the federal level, a number of other laws and regulations may apply.[5]

As a general overview, of the broad spectrum of issues related to the protection of the environment, a company in Argentina may face the following environmental liabilities:

- prevention and remediation – in general terms, preventive and / or remedial actions may be brought as claims before a court handling insolvency proceedings such as a *concurso preventivo*. As discussed above, monetary claims may be filed under the ABL, while proceedings aimed at the specific performance of an obligation (to engage in or to abstain from certain action, in this case one of an environmental nature), shall be converted into monetary claims and subject to the restructuring proceeding;

- civil claims such as claims in tort and claims in contract – according to the General Environmental Law, whenever restitution of the environment to its prior condition becomes technically impossible, or non-feasible, the party responsible for the environmental damage may be ordered to pay monetary compensation to a special Compensation Fund, which at the federal level has not become fully operative as of this date. The compensation would be

[5] Law Nr 13,273 on the Defence, Improvement and Expansion of Forests; Law Nr 17,319 on Hydrocarbons; Law Nr 20,284 on the prevention of critical situations of atmospheric pollution; Law Nr 22,351 on National Parks, National Reserves and Natural Monuments; Law Nr 22,421 on Wildlife Conservation; Law Nr 22,428 on the promotion of private and public action aimed at the conservation and recovery of the productive capacity of soils; Law Nr 24,051 on Hazardous Waste; Law Nr 24,585 on Environmental Protection for Mining Activity; Law Nr 25,018 on Radioactive Waste Management; Law Nr 25,612 on Integral Management of Industrial Waste and Service Activities; Law Nr 25,670 on Minimum Budgets for the Management and Elimination of PCBs; Law Nr 25,688 on Environmental Water Management; Law Nr 25,831 on Free Access to Public Environmental Information; Law Nr 25,916 on Household Waste Management; Law Nr 26,168 on creation of the Cuenca Matanza Riachuelo Authority as an interjurisdictional public law entity; Law Nr 26,331 on Minimum Budgets for Environmental Protection of Native Forests; Law Nr 26,562 on Minimum Budgets for Control of Burning Activities; Law Nr 26,639 on Minimum Budgets for the Preservation of Glaciers and the Periglacial Environment; Law Nr 26,815 on Fire Management; Law Nr 27,037 on Protected Marine Areas; Law Nr 27,279 on Minimum Budgets for Environmental Protection for the Management of Phytosanitary products Empty Containers; Law Nr 27.520 on Minimum Budgets for Adaptation and Mitigation of Global Climate Change; among others.

determined by a judge. In theory at least, monetary compensation determined in this way (in lieu of actual remediation) could be subject to the rules of the ABL if the obligation to be payable to the Fund originates prior to the debtor's filing for protection under the ABL. In such a hypothetical event, the Fund, which is expected to be set up as a Public Trust, would be in a position to file a proof of claim as any other unsecured creditor.

Aside from the above (which deals with damages to the environment itself), in the case of an individual loss derived from damage to the environment (such as loss of property or personal injuries), the person directly harmed by the event will be entitled to file a claim in a restructuring proceeding.

In addition, the Ombudsman, environmental associations, national, provincial or municipal states are entitled to submit claims, including class actions in case of environmental damage; and

- fines imposed by governmental authorities – state agencies[6] have sanctioning powers to apply fines for breaches of environmental duties. Agencies are empowered to issue debt determinations and specify their amounts. Other provincial or municipal agencies may also have local powers to monitor and sanction companies for breach of environmental duties.

### *2.1.2 Priority given to environmental liabilities*

As a general rule, environmental liabilities are unsecured claims in a restructuring proceeding. Only claims of providers for any work performed on specific assets that remain in the power of the debtor may be deemed as secured claims.[7]

In case the company is declared bankrupt, some environmental claims originating after adjudication of bankruptcy arising from the maintenance, management and liquidation of the assets of the debtor may be considered as maintenance and court expenses and paid immediately.[8]

### *2.1.3 Disclaimer of environmental obligations*

Environmental liabilities existing prior to the filing may be restructured under the restructuring process. However, a company will maintain its statutory or contractual obligations under the proceeding and post-restructuring process. The restructuring process does not entail, in Argentina, any change in its post-restructuring environmental obligations, and thus, the company may incur new environmental liabilities.

In a restructuring proceeding, as the company is not empowered to perform gratuitous acts, it shall not be able to disclaim onerous property. Under a restructuring process, a debtor may transfer any property provided it has obtained prior judicial approval. When the restructuring plan is judicially endorsed, the transfer of real estate may be subject to the restrictions agreed on the plan.

## 2.2 Social (S): restructuring health or safety-related liabilities

Health and safety-related liabilities (such as product liability tort claims, civil liability tort claims, occupational diseases and accidents at work) can be restructured in the same way as ordinary liabilities of a company.

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6 Such as the Secretariat of Environment and Sustainable Development (under the Ministry of Environment and Sustainable Development), the main agency empowered to exercise the sanctioning police power at the national level in environmental matters, or the Authority of the "Cuenca Matanza Riachuelo – ACUMAR", a public interjurisdictional entity (National state, province of Buenos Aires and CABA) whose objective is to address the environmental situation of the Matanza Riachuelo river and its surroundings, backed by sanctioning powers (Resolution No. 12/2019).

7 ABL, s 241, 1°.

8 *Idem*, s 240.

In addition, as per the priority afforded to the claim (whether it is secured or unsecured), liabilities will have different treatment in the restructuring, as secured creditors are not frequently involved in a restructuring plan (as it is only mandatory for unsecured creditors). Therefore, secured creditors excluded from the plan will be entitled to file or continue any legal action seeking enforcement of their credit.

### *2.2.1 Types of health and safety-related liabilities*

Health and safety-related liabilities may arise from:

- civil claims, such as claims in tort and claims in contract (including consumers). A company may be liable under the tort of negligence for the negligent manufacture, distribution or supply of goods or for breach of contractual duties. In addition, as per the Consumer Law Nr 24,240, breach of duty of information and / or duty of care, in particular with respect to dangerous goods, or liability for defective products, may result in claims filed by consumers;

- occupational diseases and accidents at work. Work accidents and occupational diseases are mainly regulated by laws Nr 24,557, 26,773 and 27,348. These regulations set forth a compensation system in the event the employee loses part of his / her working capacity as a result of an accident at work or an occupational disease. Employers with workers under a labour contract must provide their workers with a compulsory occupational risk insurance with a private occupational risk insurer (ART). The compensation payment is the responsibility of the occupational risk insurer, but the employer may be liable if the compensation is insufficient to cover the damages suffered by the worker. The creditor of these claims is always the worker; and

- municipal fees imposed by competent authorities. The employer is obliged to comply with the legal rules on hygiene and safety at work. Law Nr 19,587 and complementary regulations set forth certain standards that are intended to prevent occupational risks. The Ministry of Labor controls and supervises the compliance with these laws and is empowered to impose sanctions (fines)[9] on employers that do not comply. The creditor of this claim is the national or provincial authority (as appropriate).

### *2.2.2 Treatment of health and safety-related liabilities*

Health and safety-related liabilities that arise out from a labour relationship (occupational diseases and accidents at work) are afforded with priority and considered secured claims in an insolvency proceeding. In addition, such labour creditors are entitled to collect their credits with a fast-track procedure named "*pronto pago*"[10] in a restructuring proceeding.

The Argentine Supreme Court (in *re Pinturas y Revestimientos S.A. s/quiebra*)[11] decided that the priorities regime provided for in Law Nr 24,522 shall be integrated with the provisions of international treaties – in the case at hand, ILO Convention Nr 173. Therefore, general preferred labour claims shall have priority over any other general secured claim, in particular over tax and social security claims.

Municipal fees imposed by competent authorities shall be considered a secured claim and thus unlikely to be included in the restructuring plan. Such creditors are entitled to file or continue any legal action seeking enforcement of their credit after judicial endorsement of the restructuring plan.

Other health and safety-related liabilities (claims in tort and claims in contract, including consumers such as product liability claims) are considered unsecured claims and subject to the restructuring plan to be submitted in the proceeding. Class actions that may have been started prior to the filing of the reorganisation proceeding may continue while the restructuring is ongoing

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9 Law Nr 25,212 sets forth the legal framework of the corresponding sanctions.

10 ABL, s 16.

11 Fallos: 337:315.

and then, when obtaining the condemnatory ruling, creditors shall file the correspondent proof of claim to be admitted by the insolvency court and subject to the plan.
There has been an intense debate in Argentina in relation to involuntary creditors,[12] holders of unsecured claims.

The Argentine Supreme Court was called upon to make a ruling in a tort claim based on medical malpractice suffered by a child at the time of his birth in *re Asociación Francesa Filantrópica y de Beneficencia s/ quiebra s/ incidente de verificación de crédito por L.A.R. y otros*.[13] The Supreme Court, in confirming the ruling of the Commercial Court of Appeals, supported the priorities set forth in the ABL and considered that the recognition of a specific right in an insolvency proceeding cannot be derived directly from international treaties.

A few months later and with a different composition (one judge retired from the court), in a similar claim in tort (malpractice suffered by a child at birth), the Supreme Court in *re Institutos Médicos Antártida s/ quiebra s/ inc. de verificación (R.A.F. y L.R.H. de F*[14] changed its understanding and declared unconstitutional and inapplicable certain sections of the priority regime of the ABL and granted the creditor with a super priority privilege over any other secured claim. The Supreme Court noted that the child that suffered the malpractice was 28 years old and that the vulnerability of the family and the lack of sufficient economic resources to face the appropriate medical treatments significantly aggravated the health of the victim. Furthermore, the Supreme Court pointed out that human rights established both by Argentina's Federal Constitution and by many international conventions (such as the Convention on the Rights of the Child, the Convention on the Rights of Persons with Disabilities, the International Convention on Economic, Social and Cultural Rights, the American Convention on Human Rights and the Universal Declaration of Human Rights) led to the conclusion that the claim must be protected with a priority to guarantee the victim the enjoyment of their right to the highest possible level of health and a full and decent life. Therefore, the Supreme Court granted the creditor a super priority privilege over any other secured claim.

In December 2021, Panel F of the Commercial Court of Appeals ruled in an aberrant case (a claim in tort suffered by a child, a victim of sexual abuse when she was two years old) in *re Fundacion Educar s/ Concurso Preventivo* case Nr 23177/2016, that the human rights established by Argentina's Federal Constitution, many international conventions[15] and some Federal laws (Law Nr 26,061 of Comprehensive Protection of the Rights of Children and Adolescents and Law Nr 26,485 of Comprehensive Protection of Women) demand an effective protection to girl victims of gender violence via the recognition of their rights as irrevocable and intangible. Therefore, the Court declared inapplicable to the claim the restructuring plan which entailed a haircut and a payment deferral and ordered the full payment of the credit to the victim.

### 2.3 Governance (G): third party releases in favour of directors and officers of the company

We have not identified cases in Argentina addressing this issue in a reorganisation proceeding.

As a general rule, the reorganisation plan is binding only upon the debtor and the prepetition creditors comprehended by the plan. The ABL expressly states that guarantors and co-debtors are not released by the novation that entails endorsement of the plan.

A release to directors and officers in a reorganisation plan shall be deemed a provision in favour of a third party.

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[12] Claims in tort in aberrant cases, suffered by a child seriously injured with a permanent disability or a victim of sexual abuse.

[13] Fallos: 341:1511.

[14] *Idem*, 342:459.

[15] Convention on the Rights of the Child; Convention on the Elimination of all Forms of Discrimination against Women; the Inter-American Convention on the Prevention, Punishment, and Eradication of Violence against Women, known as the Convention of Belém do Pará; Convention on the Rights of Persons with Disabilities; American Convention on Human Rights; Universal Declaration of Human Rights.

The court shall analyse the fairness of the plan and whether the terms are deemed abusive. Our interpretation is that the fairness of a release needs to be analysed with increased scrutiny and only be approved if it is critical or "necessary" to the reorganisation – for example, if the third party benefiting from the release is funding the company to enable it to fulfil the plan.

Notwithstanding the foregoing, third party releases in Argentina are unlikely to be granted or shall be ineffective because, if the company is declared bankrupt, the release provided to directors and officers of the company does not affect the abilities and powers of the trustee or any other creditor of the insolvent company to file a bankruptcy liability action[16] for having fraudulently caused, facilitated, permitted or aggravated the financial status or the insolvency, or a corporate liability action for negligence or breach of their fiduciary duties.[17] A similar analysis applies to shareholders and related companies of the debtor, as bankruptcy liability action and the extension of bankruptcy petitions will not be affected by a release granted in the plan.

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by the environmental protection authorities or environmental advocacy groups in a restructuring

#### *3.1.1 Approving a restructuring plan*

As noted, a restructuring plan is subject to the approval of the court and creditors. A restructuring plan is not subject to the approval of any regulatory body or environmental agency or authority.

#### *3.1.2 Discretion to consider wider public interest concerns*

We have not identified cases in which a court has considered environmental issues in deciding whether to approve a restructuring plan.

#### *3.1.3 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

As a general rule, there are no statutory provisions which grant environmental protection authorities or environmental advocacy groups standing to air their views or concerns in a restructuring proceeding. However, certain government agencies empowered to impose sanctions or fines for environmental breaches are entitled to file a proof of claim and participate as an unsecured creditor in the restructuring proceeding.

In addition, considering that the protection of the environment is in the public interest, public or private organisations may have the right to file motions in a restructuring proceeding, seeking to protect the environment from continued harmful activities.

### 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

#### *3.2.1 Approving a restructuring plan*

A restructuring plan is not subject to the approval of any labour authorities, unions or advocacy groups.

#### *3.2.2 Discretion to consider wider public interest concerns*

When the court is called upon to analyse the restructuring plan, it shall consider the equal treatment of all the creditors, whether the restructuring plan can reasonably be achieved and if the terms are deemed abusive (such as offering less than creditors will collect in a bankruptcy proceeding).

[16] ABL, s 173.
[17] Law Nr 19,550, s 275.

As one of the main goals of the reorganisation proceeding is to allow the continuation of the company as a viable entity, the court may consider the number of workers of the company, the magnitude of the company in the market and other key features when deciding whether to endorse the restructuring plan or grant the debtor a new opportunity to improve the terms of the plan (the third way referred to above). There is case law in Argentina in that regard.[18]

### 3.2.3 *Protection of employee rights*

The ABL grants several rights to workers in a restructuring proceeding, as follows:

- fast-track payment (*pronto pago*): in a *concurso preventivo*, certain labour claims[19] are entitled to special treatment, and immediate payment of their debts may be requested. The debts will be paid in full, if there are liquid funds available. Otherwise, and until their existence is detected by the trustee, 3% per month of the debtor's gross income must be reserved to cover such claims. The judge may exceptionally authorise the payment of the claims which, due to their nature or particular circumstances of the creditors, must be applied to cover health, alimentary expenses or other contingencies that do not allow any delay;

- participation in the creditors' committee: in a reorganisation proceeding (*concurso preventivo*), a creditors' committee is appointed to act, in addition to the trustee, as an information and advisory body. As the creditors' committee shall be composed of representatives of the debtors' employees,[20] workers of the company will have standing to air their views or concerns in a restructuring. As a matter of fact, the creditors' committee shall be heard when the debtor requests judicial authorisation for performing certain acts (section 16 of the ABL) and has broad powers of information and advice (section 260 of the ABL) as it is empowered to: request information from the trustee and the debtor; require the exhibition of books and records; propose measures for the custody and conservation of the debtor's assets; and request hearings before the judge; and

- individual control: debtors' employees are entitled to request information from the trustee about the creditors (secured and unsecured) that submitted a proof of claim.[21]

In addition to the individual rights afforded to workers, if employees of a company undergoing a restructuring proceeding are members of a trade union,[22] the union may be entitled to submit motions to the court seeking to protect the interests of its members.

## 3.3 Governance (G): board / management conflicts addressed in a restructuring

One of the usual conflicts in a restructuring arises when managers or directors or other administrators have pre-petition claims and are creditors of the insolvent company. The ABL resolves that situation, setting forth that controlling shareholders, managers, directors or their

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18 See "Argenfruit S.A. en Pedro López e Hijos SACIA p/conc. s/inc. cas" (Supreme Court of Mendoza); Commercial Court of Appeals: Sociedad Comercial del Plata S.A y otros s/ Concurso preventive"; "Editorial Perfil S.A. s/ Concurso Preventivo"; "Hebos S.A. s/conc. prev."; "Romario SRL s/ concurso preventivo" (First Instance Commercial Court Nr 14), among others.

19 Salaries owed to workers, compensation for occupational diseases and accidents at work and those provided for in arts 132 bis, 212, 232, 233 and 245 to 254, 178, 180 and 182 of the Labour Contract Regime approved by Law Nr. 20,744; the compensation provided for in Law Nr. 25,877, in arts 1 and 2 of Law Nr. 25,323; in arts 8, 9, 10, 11 and 15 of Law Nr. 24,013; in arts 44 and 45 of Law Nr. 25,345; in art 52 of Law Nr. 23,551; and those provided for in the special statutes, collective agreements or individual contracts, that enjoy general or special privilege.

20 With the commencement of the *concurso preventivo*, the court appoints a provisional creditors' committee comprised of the three unsecured creditors with the largest claims declared by the debtor, and a representative of the debtors' employees. Members of the committee are then replaced when categories of creditors are established, and the creditors with the largest claims in each category and two representatives of the debtors' employees are appointed to the committee. The final creditors' committee is proposed by the debtor in the restructuring plan, with the representatives of the debtors' employees that continue in their functions and shall monitor the performance and execution of the approved plan.

21 ABL, s 34.

22 Governed by Law Nr 23,551.

assignees (appointed within one year prior to the filing date) do not have voting rights in relation to the restructuring plan, as they are related creditors and are to be discounted from the majorities required to support the plan.[23]

If the directors or managers are receiving shares or options under a management incentive plan or options scheme as part of the restructuring plan, in return for committing to continuing their service for the company post-restructuring, all such terms and conditions shall be set out in the plan. The fairness and reasonableness of the restructuring plan shall be analysed by the court provided the majorities and formalities have been met.

Outside the restructuring context, the Argentine Companies Law Nr 19,550 sets forth that managers and directors that have a conflict of interest with the company shall, in light of their duty of loyalty, refrain from intervening in the transaction and must inform the board of directors and the corporate statutory auditor (*síndico societario*) of the conflict.[24] The Civil and Commercial Code provides a similar provision applicable to the rest of the legal private entities and recommends that private legal entities implement preventive systems for mitigating the risk of conflicts of interest in their relations with the legal entity.[25]

In relation to listed companies, the Argentine Capital Market Law Nr 26,831 expands the duty of loyalty of directors, setting forth, in section 78, that the following acts are comprehended by the duty:

- the prohibition on making use of company assets and the prohibition on making use of any confidential information for private purposes;
- the prohibition on taking advantage of or allowing another to take advantage, either by action or by omission, of the company's business opportunities;
- the obligation to exercise their powers only for the purposes for which the law, the statute, the assembly or the board of directors have granted them; and
- the obligation to scrupulously ensure that their actions never result in a direct or indirect conflict of interest with those of the company.

In addition, the National Securities Commission (CNV or *Comisión Nacional de Valores*), to adapt governance practices and standards to the Corporate Governance Principles issued by the Organisation for Economic Cooperation and Development (OECD), amended the Corporate Governance Code by General Resolution No. 797/19. The current Corporate Governance Code sets forth 29 principles dealing with transparency issues, conflicts of interest with directors' remuneration, the interests of shareholders and stakeholders and various other topics.

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

We have not identified any industry guidelines and / or best practices prescribed for the protection of the environment in a restructuring.

Notwithstanding the foregoing, outside a restructuring proceeding, regulation ISO 14001 is an internationally accepted standard that establishes how to implement an efficient environmental management system. The regulation seeks a balance between profitability and the reduction of environmental impact.

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23 ABL, s 45.
24 Law Nr 19,550, s 272.
25 Civil and Commercial Code, s 159.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

We have not identified any industry guidelines and / or best practices prescribed for the protection of employee rights in a restructuring.

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

We have not identified specific guidelines or codes of conduct for restructuring professionals. Nevertheless, legal professionals are governed by general rules about the duty of loyalty.

The legal profession is ruled by local laws – therefore, the precise content of the duty may vary depending on the corresponding venue. In the City of Buenos Aires, Law Nr 23,187 provides several duties, such as loyalty to the client, information to be provided, and the avoidance of conflict of interests, among others.

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

ESG financing has consistently been growing in Argentina in recent years. The growth of socially responsible investment has promoted the creation, by the National Securities Commission (*CNV* or *Comisión Nacional de Valores*), of financial products and regulations aimed at increasing the finance of projects with environmental and social impact in the capital market.

In accordance with internationally recognised standards, such as the Green Bond Principles, the Social Bond Principles and the Sustainable Bonds Guidelines prepared by the International Capital Market Association (ICMA), and the International Climate Bonds Standard created by the Climate Bonds Initiative, the National Securities Commission issued General Resolution Nr 788/2019 approving the "Guidelines for the Issuance of Social, Green and Sustainable Securities in Argentina".

In 2021, the National Securities Commission issued General Resolution Nr 896 approving three Sustainable Guidelines that are relevant for Socially Responsible Investment (SRI):

- Guide for Socially Responsible Investment in the Argentine Capital Market;
- Guide for the Issuance of Social, Green and Sustainable Bonds; and
- Guide for External Reviews of Social, Green, and Sustainable Bonds.

These guides are not mandatory, but their objective is to create an orientation and consultative framework, in order to transmit and raise awareness about the different aspects that encompass sustainable finance. This will allow the development of a theoretical framework and a common language to provide clarity to the concepts related to ESG principles in the Argentine capital market.

Within the framework of General Resolution Nr 885/2021, a special regime aimed at promoting investment in ESG marketable securities, the National Securities Commission authorised different types of ESG investment funds (*Fondos Comunes de Inversión Abiertos ASG*). Recently, the National Securities Commission issued General Resolution Nr 940/2022 setting forth a simplified framework for issuing guaranteed bonds with social impact applicable to entities intending to finance eligible social projects.

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

Financial institutions in Argentina have adopted many guidelines and standards that address the impact of climate change in the financial services markets, such as the Paris Agreement (the instrument under the United Nations Framework Convention on Climate Change adopted on 12

December 2015), the Sustainable Development Goals (SDGs) of the 2030 Agenda for the Sustainable Development, the Principles for Responsible Investment (PRI), the Principles for Banking Responsible of the Financial Initiative of the United Nations Environment Programme (UNEP FI), the Equator Principles, and the standards prescribed by the Financial Stability Board (FSB) within the G20 group, among others.

In 2019, with the support of IDB Invest (a private arm of the Inter-American Development Bank) and Fundación Vida Silvestre Argentina, the most important public and private banks of Argentina executed the Sustainable Finance Protocol for promoting a unified sustainability strategy in the Argentine banking system. The initiative established a framework on four key points:

- develop internal policies to implement sustainability strategies;
- create financial products and services to support the financing of projects with a positive environmental and social impact;
- optimise current risk analysis systems with an environmental and social focus; and
- promote a culture of sustainability.

### 5.3 Promoting ESG by the central bank and regulators

Fostered by the Technical Committee for Sustainable Finance,[26] the main regulatory entities of the banking, insurance and capital market sector – the Ministry of Economy, the Argentinian Central Bank, the National Securities Commission and the Insurance Superintendency – entered into an agreement in September 2021, aiming to create the conditions for the financial sector to attract public and private investments that contribute to achieving ESG objectives, within the framework of the Sustainable Development Goals.

Regulators in the agreement stated their commitment to the following policies:

- promote the development of sustainable financing in the country and promote adequate incorporation, management, regulation and supervision of risks associated with ESG criteria, in order to design policies that contribute to the strengthening, development and stability of the Argentine financial system;
- prepare a joint long-term agenda for incorporating ESG criteria into their business strategies;
- advance in the evaluation and mitigation of the potential risks, linked to ESG factors, such as financial risks associated with the climate and towards a low carbon economy;
- promote communication channels, joint work mechanisms and coordination spaces between the public and private sectors, for incorporating sustainable finance criteria; and
- contribute, within the framework of the Technical Committee for Sustainable Finance, in designing a national strategy for the development of sustainable finance in Argentina.

Argentina also participates in the Financial Stability Board, an international body that monitors and makes recommendations about the global financial system, and the International Platform on Sustainable Finance, a forum for dialogue between policymakers, with the aim of increasing the amount of private capital being invested in ESG investments.

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26 *Mesa Técnica de Finanzas Sostenibles (MTFS),* a permanent group for exchanging information, discussion, coordination and evaluation of public policy actions, strategies and activities, with the objective of developing and strengthening sustainable finance in Argentina. It is composed by the Ministry of Economy, the Argentinian Central Bank, the National Securities Commission, the Insurance Superintendency, the National Argentinian Bank (Banco de la Nación Argentina), the Investment and Foreign Trade Bank (BICE), the Ministry of Productive Development, the Ministry of Environment and Sustainable Development, among others.

# AUSTRALIA

## 1. General overview of the restructuring regime

A proper understanding of the Australian corporate restructuring regime and its interaction with ESG matters must begin with a broad overview of the Australian legal system.

The Commonwealth of Australia is a federation of six states. The Commonwealth also contains two self-governing internal territories. Each of the Commonwealth, the states and the territories has its own law-making powers.

Australia has a common law legal system which inherited many characteristics from English law. There is a single common law of Australia.[1]

Most of the laws regarding corporate insolvency and restructuring are found in the Commonwealth Corporations Act 2001. Laws regarding corporate governance are largely created by the Corporations Act and the common law, but laws regarding environmental standards and employee rights originate in Commonwealth, state and territory statutes as well as the common law.

### 1.1 Formal restructuring procedures

Australia has only one in-court restructuring procedure: the scheme of arrangement. It is a court-supervised procedure which is capable of compromising the rights of a company's creditors and members and is frequently used for the reorganisation of both debt and share capital. A scheme of arrangement can be commenced inside or outside liquidation.[2] The existing management remains in place, although if the scheme occurs within liquidation, the powers of management are attenuated by the liquidation and are subject to the powers of the liquidator.

There are five stages in the scheme of arrangement process.

First, the terms of the scheme must be determined, and an "explanatory statement" (or scheme booklet) prepared.

Second, the company (or less commonly, its liquidator, a creditor or a shareholder) must make an application to a court for the convening of a scheme meeting (or scheme meetings) and the approval of the explanatory statement. That application must be served on the corporate regulator (the Australian Securities and Investments Commission or ASIC), which must be given the opportunity to examine the proposed terms of the scheme and the explanatory statement, and to make submissions to the court.

One of the most important matters considered by the court in determining whether to approve the convening of meetings is the division of the creditors and members into "classes". Such a division occurs whenever the rights and entitlements of a particular group, considered in the context of the proposed scheme, are so dissimilar from those of the remainder "as to make it impossible for them to consult together with a view to their common interest."[3]

Third, if the court approves the holding of meetings and the explanatory statement, the meetings are convened and the explanatory statement is sent to members and creditors. A separate meeting is held for each identified class.

Fourth, the scheme meetings are held, and members of each class are asked to vote on the question of whether the scheme should be approved. A class is only taken to approve of the scheme if the resolution to approve it is passed by a majority of voting creditors by number, and

1 That is, the states, the Commonwealth, and its territories all share a single common law: *Lipohar v R* (1999) 200 CLR 485, 505-509 (Gaudron, Gummow and Hayne JJ).

2 Corporations Act, s 411(1).

3 *Sovereign Life Assurance Co v Dodd* [1892] 2 QB 573 at 583 (Bowen LJ); *Re Hills Motorway Ltd* (2002) 43 ACSR 101, [12] (Barrett J); *First Pacific Advisors LLC v Boart Longyear Ltd* (2017) 320 FLR 78, 93-94 [81] (Bathurst CJ, Beazley P and Leeming JA).

the aggregate value of those creditors' debts is 75% or more of the total value of all voting creditors' debts.[4]

Fifth, if each class approves the scheme, a second court hearing is held at which the court is asked to approve the scheme. The court can approve the scheme subject to alterations or conditions.[5] A series of frequently recited principles concerning approval have emerged.[6] Approval is within the court's discretion, regardless of the outcome of the first hearing and the class meetings. The court will usually not attempt to assess the commerciality of the scheme, leaving it to creditors to determine their own commercial interests. The matters which the court considers in exercising its discretion include: whether the creditors have voted in good faith and not for an improper purpose; whether the proposal is so fair and reasonable that an intelligent, honest and properly-informed member of each class, acting alone, could have approved it; whether all relevant matters were fully disclosed to the court and fairly disclosed to class members; the existence of any oppression to minorities; and matters of public policy.

Once approved by the court, a scheme binds every class of creditors or members that has approved it at the relevant meeting.[7] A scheme can be used to bind creditors in relation to their rights against third parties (for example, guarantors).[8] And it can depart from some aspects of the insolvency process that would apply in liquidation – for example, *pari passu* distribution among unsecured creditors.[9] But the power of the scheme to alter members' and creditors' rights cannot be used to avoid the operation of any "special and exclusive procedure" laid down by statute.[10] Procedures which have been held to be unavoidable include the statutory requirement that the rights attached to certain classes of shares can only be varied in compliance with the company's constitution,[11] the statutory prohibition on the assets of an insurer in liquidation being applied to the discharge of non-Australian liabilities[12] and the statutory requirement that reinsurance recoveries of an insurer in liquidation be used to satisfy the insurance liabilities in relation to which that reinsurance relates.[13]

Typically, a scheme of arrangement must be administered by an independent registered liquidator[14] known as a "scheme administrator". The appointment of a scheme administrator does not displace the powers of the company's directors (save to the extent that the scheme documents so provide).

## 1.2 Out of court restructuring procedures

There are two forms of statutory out of court corporate restructuring procedure under Australian law: voluntary administration and small business restructuring. Restructuring by private arrangement with creditors is also possible.

### *1.2.1 Voluntary administration*

The object of voluntary administration is to maximise the chance of the company's business (or as much as possible of it) continuing in existence, and if that is not possible, to achieve a higher return to creditors and shareholders than would result from an immediate liquidation.[15]

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4 Corporations Act, s 411(4).
5 *Idem*, s 411(6).
6 See e.g. *Absolute Equity Performance Fund Ltd, in the matter of Absolute Equity Performance Fund Ltd (No 2)* [2022] FCA 1135, [7]-[11] (Halley J), from which the principles recited here have been extracted.
7 Corporations Act, s 411(4).
8 *Fowler v Lindholm* (2009) 178 FCR 563, 578 [67]-[69] (Emmett, Gordon and Jagot JJ).
9 *Re HIH Casualty and General Insurance Ltd* (2005) 215 ALR 562, 594 [121], [127] (Barrett J).
10 *Australian Securities and Investments Commission v Marlborough Gold Mines Ltd* (1993) 177 CLR 485, 501 (HCA).
11 *Re White Horses Pty Ltd (No 2)* [2017] 2 Qd R 422, 438 [47] (Bond J).
12 *Re HIH Casualty & General Insurance Ltd* (2005) 215 ALR 562 (Barrett J).
13 *Ibid*.
14 Corporations Act, s 411(7).
15 *Idem*, s 435A.

Under voluntary administration, the company's directors remain in place but cede all control of the company to a "voluntary administrator",[16] who must be an independent natural person who is also a registered liquidator.[17]

The voluntary administrator can be appointed by the company's directors (if they have resolved that the company is or is likely to become insolvent)[18] or by an existing liquidator of the company (if he or she is of the view that the company is or is likely to become insolvent),[19] or by a creditor holding an enforceable security interest over all or substantially all of the company's property.[20]

During the administration, the company has the benefit of a moratorium which protects its property, stays court proceedings and restricts the exercise of the rights of most secured creditors and other third parties.[21]

The administrator holds a first meeting of creditors within eight days of his or her appointment.[22] At that meeting, creditors can vote to appoint a "committee of inspection" and to replace the administrator.

The administrator investigates the company's affairs, and for that purpose has a right to its books.[23] The directors are obliged to allow the administrator access to the company's records, and to provide him or her with a report as to the company's business and affairs.[24]

The administrator must publish a report to the company's creditors, and then convene a second meeting of those creditors,[25] at which he or she must recommend one of three courses of action:

- that the administration should end, and the company be handed back to its directors;
- that the company should be wound up; or
- that the company should execute a deed of company arrangement.[26]

The creditors may resolve that the company take one of those three actions.[27]

A resolution is passed only if it is supported by a majority of voting creditors by number, and the aggregate value of those creditors' debts is more than half of the total value of all voting creditors' debts.[28] If only one of those two criteria is satisfied, the chair of the meeting (which will usually be the voluntary administrator) has the casting vote.

Any deed of company arrangement must propose a "deed administrator" responsible for the administration of the deed. The voluntary administrator typically becomes the deed administrator, but the creditors may appoint an alternative deed administrator by resolution at the meeting.[29]

Where the creditors resolve that a deed of company arrangement be executed, the company and the deed administrator must execute it within 15 business days following the meeting (or such later date as a court may order).[30]

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16 *Idem*, s 437A-437D.
17 *Idem*, ss 448B, 448C.
18 *Idem*, s 436A.
19 *Idem*, s 436B.
20 *Idem*, s 436C.
21 *Idem*, ss 440A - 441J.
22 *Idem*, ss 436A.
23 *Idem*, ss 438A, 438C
24 *Idem*, s 438B.
25 The meeting must be convened within 20 or 25 business days (dependent of the time of year) after the commencement of the administration, subject to extension by a court: ss 439A(5)-439A(8).
26 *Idem*, s 439A.
27 *Idem*, s 439C.
28 Insolvency Practice Regulations (Corporations) 2001 (Cth), r 75-115.
29 Corporations Act, s 444A(2).
30 *Idem*, s 444B.

The deed administrator then administers the deed and (subject to the terms of the deed) the company is usually returned to the hands of its directors while the deed operates.

The deed must identify (among other things) what property of the company is to be available to pay creditors' claims, the nature and duration of any moratorium under the deed, the extent to which the company is to be released from its debts, the order in which the proceeds of property are to be distributed among creditors, and the circumstances in which the deed terminates.[31]

All creditors are bound by the terms of a deed of company arrangement, although the rights of secured creditors to enforce their securities are not affected unless the deed says so and the creditor voted in favour of it.[32] The court retains a power to limit the rights of secured creditors and owners and lessors of property if the court is satisfied that the enforcement of those rights would have a material adverse effect on the achievement of the purposes of the deed.[33] While the deed remains on foot, the company also enjoys an ongoing moratorium against liquidation applications and other litigation brought by any person bound by the deed.[34]

A deed can release or compromise claims against the company,[35] but where the deed provides for the business to continue, it is common for debts owed to those creditors who will continue to deal with the company to be preserved or to be paid in full.

During the administration period (i.e. until the company enters a deed of company arrangement or administration is otherwise terminated), guarantees given by the company's directors and their relatives may not be enforced without leave of the court.[36] But a deed of company arrangement cannot bind a creditor in relation to its rights against a party other than the debtor company (for example, guarantors).[37]

The Corporations Act allows great flexibility in terms of the compromise of debts and the distribution of property under a deed of company arrangement, but there are two important exceptions. First, a deed of company arrangement must provide eligible employee creditors with priority at least equal to that which they would be entitled if the company were in liquidation[38] (although that rule can be avoided by court order or by a resolution of a meeting of the eligible creditors held before the second creditors' meeting).[39] Secondly, where a deed departs from the statutory scheme of priorities or *pari passu* distribution between unsecured and non-priority creditors that would apply in a winding up, it may be vulnerable to being set aside by a court on grounds of injustice or unfair prejudice.[40]

A deed can provide for the transfer of shares in the company, although consent of the affected shareholders or leave of a court is required to effect the transfer.[41]

A deed comes to an end when: it has satisfied the criteria prescribed by the deed itself; the deed administrator executes a notice of termination having fulfilled the deed; a court makes an order terminating the deed; or the company's creditors resolve that it be terminated.[42]

No court order is required at any stage of the voluntary administration process, and it is common for a company to complete the entire process from appointment through to deed termination without the involvement of a court. Nevertheless, the Supreme Courts of the various states and territories and the Federal Court of Australia have concurrent jurisdiction to hear various applications concerning the administration and deed administration procedure, the rights and

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31 *Idem*, s 444A.
32 *Idem*, s 444C.
33 *Idem*, s 444F.
34 *Idem*, s 444E.
35 *Idem*, s 444H.
36 *Idem*, s 400J.
37 *Lehman Brothers Holdings Inc v City of Swan* (2010) 240 CLR 509.
38 Corporations Act, s 444DA(1).
39 *Idem*, s 444DA(2), (5).
40 *Idem*, s 445D(1).
41 *Idem*, s 444GA.
42 *Idem*, ss 445C, 445A.

obligations of the voluntary administrator and the deed administrator and the content, operation and potential termination of a deed of company arrangement.

### *1.2.2 Small business restructuring*

The object of the small business restructuring provisions is to allow an eligible company to retain control of its business, property and affairs while developing a restructuring plan with the assistance of a "small business restructuring practitioner" and to enter into a restructuring plan with creditors.[43]

A company which has total liabilities no greater than AU $1 million, and which is not already the subject of another statutory insolvency process[44] may appoint a small business restructuring practitioner to commence a restructuring if the directors resolve that the company is insolvent or is likely to become insolvent at some future time.[45] The restructuring practitioner must be an independent registered liquidator.[46]

The company's directors remain in place during the restructuring process, but are obliged to attend on, provide information to, and allow access to the company's books by, the restructuring practitioner.[47] However, the directors may not cause the company to enter a transaction or dealing affecting the company's property, nor approve such a transaction, unless it is in the ordinary course of the company's business or has the approval of the restructuring practitioner or a court.[48]

During the restructuring, the company has the benefit of a moratorium which protects its property, stays court proceedings and restricts the exercise of the rights of most secured creditors and other third parties.[49]

Within the period of 20 business days following the commencement of the restructuring period (which may be extended by the restructuring practitioner and by court order),[50] the company may propose a restructuring plan.[51] A plan may only be proposed if the company is in substantial compliance with its obligation to pay employee entitlements and its income tax filing obligations.[52]

The restructuring plan must, among other things, identify the company's property that is to be dealt with, and how it is to be dealt with. It may (among other things, and subject to the standard terms discussed below) authorise the restructuring practitioner for the plan to deal with the identified property in a specified way, and provide for any other matter relating to the company's affairs. It may not provide for the transfer of property other than money to a creditor or provide for the company to make payments under the plan more than three years after the day the plan is made.[53]

The restructuring plan must include standard terms which are prescribed by regulations. Those terms include a requirement that all admissible debts and claims rank equally and are to be paid proportionately if the amount available under the plan is inadequate to pay them in full.[54] A restructuring plan may not provide for the transfer of property other than money to a creditor.[55]

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43 *Idem*, s 452A.
44 There are other eligibility criteria prescribed by Corporations Act s 453C and Corporations Regulations 2001 (Cth) reg 5.3B.03, which it is not necessary to explain here.
45 Corporations Act, s 453B.
46 *Idem*, ss 456B-456C.
47 *Idem*, ss 453F, 453K.
48 *Idem*, s 453L.
49 *Idem*, ss 453Q-453T, 454A-454M.
50 Corporations Regulations 2001 (Cth), reg 5.3B.17.
51 Corporations Act, s 455A.
52 Corporations Regulations 2001 (Cth), reg 5.3B.14, 5.3B.24.
53 *Idem*, reg 5.3B.15(4)(b).
54 *Idem*, reg 5.3B.27.
55 *Idem*, reg 5.3B.15(4)(a).

As soon as possible after the restructuring plan is made, the restructuring practitioner must:

- make a declaration concerning his or her opinion regarding the company's eligibility criteria for restructuring, its capacity to discharge the obligations under the plan, and its compliance with its disclosure obligations, and explaining the relationship between any affected creditor and the restructuring practitioner;[56]

- give the declaration to as many of the company's affected creditors as possible, together with a copy of the restructuring plan, the restructuring plan standard terms and the restructuring proposal statement; and

- ask each affected creditor to give a written statement which states whether or not that creditor accepts the restructuring plan and verifies or disputes the amount of that creditor's debts.

A proposal to make a restructuring plan lapses if the plan is not accepted within an "acceptance period" of 15 business days after the plan and other documents are provided to creditors.[57] The restructuring practitioner may cancel the proposal if he or she becomes aware that: the plan is incomplete in a way which is likely to affect the company's ability to comply with it; one or more creditors were not disclosed in the proposal; the proposal was incorrect in a material way or omitted a material particular; or certain material changes in circumstances have occurred.[58]

The plan is accepted if, at the end of the last day of the acceptance period, creditors whose debts constitute a majority of the value of those debts the subject of responses to the restructuring practitioner have stated that the plan should be accepted.[59] The restructuring plan is taken to have been made at the time of acceptance.[60]

A restructuring plan binds the company, its officers and members, the restructuring practitioner for the plan, unsecured creditors, and secured creditors (to the extent their debts are unsecured or they consented to the plan).[61] While the plan remains on foot, those persons bound by the plan may not commence or continue a winding up application against the company, or any proceeding against the company or in relation to its property, or any enforcement process in relation to property of the company (to recover an admissible debt or claim) without the leave of the court.[62]

As with voluntary administration, during the restructuring period (i.e. until the company makes a restructuring plan or the restructuring is otherwise terminated), guarantees given by the company's directors and their relatives may not be enforced without leave of the court.[63] But a restructuring plan cannot bind a creditor insofar as it has rights against a party other than the debtor company (for example, a guarantor).[64]

A restructuring plan comes to an end when: all of the obligations under the plan have been fulfilled and all debts and claims dealt with in accordance with the plan; the court makes an order terminating the plan; a contravention of the plan has occurred and 30 days have passed without it being rectified; or an administrator or liquidator is appointed.[65] If the plan terminates successfully, the company is released from all admissible debts and claims, and becomes entitled to any property that was not required to be distributed to creditors.[66]

As with voluntary administration, no court order is required at any stage of the restructuring process, but the courts have many powers to deal with disputes that arise, including powers to

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56 *Idem*, reg 5.3B.18.
57 *Idem*, reg 5.3B.20, 5.3B.25.
58 *Idem*, reg 5.3B.20.
59 *Idem*, reg 5.3B.25.
60 *Idem*, reg 5.3B.26.
61 *Idem*, reg 5.3B.28, 5.3B.29.
62 *Idem*, reg 5.3B.30.
63 Corporations Act, s 453W.
64 Corporations Regulations 2001 (Cth), reg 5.3B.29(2) and, by analogy, *Lehman Brothers Holdings Inc v City of Swan* (2010) 240 CLR 509.
65 Corporations Regulations 2001 (Cth), reg 5.3B.31(1).
66 *Idem*, reg 5.3B.31(2).

adjudicate on disputed debts,[67] to vary, void, validate or terminate the restructuring plan,[68] and to limit the rights of secured creditors and owners.[69]

There is presently little case law on available on the operation of the small business restructuring provisions, as they only took effect in January 2021 and statistics suggest that take-up of the new process has been very limited.[70]

#### *1.2.3 Informal restructuring*

A company may reach a voluntary arrangement with one or more of its creditors to restructure its debt, but such an arrangement cannot bind any creditor without agreement, nor vary any obligation imposed by law. Consequently, there is no need to deal with such informal arrangements further in this chapter.

## 2. Restructuring of ESG-related liabilities

### 2.1 Environmental (E): restructuring environmental liabilities

Liabilities that arise out of environmental responsibilities may be restructured in the same way as any other liabilities.[71] However, where a restructuring results in the company continuing to operate, and the company is subject to ongoing positive statutory or contractual obligations, the restructuring will not relieve the company of those obligations.

#### *2.1.1 Types of environmental liabilities*

There is a vast range of laws in Australia that may create environmental liabilities. The common law torts of nuisance and negligence may create civil liabilities for causing environmental harm, and the Commonwealth and every state and territory have promulgated extensive legislation which creates potential liabilities arising out of matters including pollution, dangerous goods and hazardous waste, waste disposal and biodiversity. Liabilities can be of a civil or criminal nature.

#### *2.1.2 Priority given to environmental liabilities*

With one potential exception, environmental liabilities are not given any specific priority under Australia's statutory restructuring regimes. However, where the discharge of an environmental obligation is secured over the company's property,[72] the regulatory authority in whose favour the security has been given will have the rights of a secured creditor. Similarly, a liability might attract a *de facto* priority if it is paid in the course of the administration process, because provisions giving priority to the costs of administration are commonplace in deeds of company arrangement.

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67 *Idem*, reg 5.3B.60.
68 *Idem*, reg 5.3B.62, reg 5.3B.63.
69 *Idem*, reg 5.3B.64.
70 See M Murray and J Harris, *Keay's Insolvency: Personal and Corporate Law and Practice* (11th ed, 2022) 986 [21.170].
71 The Corporations Act provides at s 553 that "all debts payable by, and all claims against, the company (present or future, certain or contingent, ascertained or sounding only in damages), being debts or claims the circumstances giving rise to which occurred before the relevant date, are admissible to proof against the company" in liquidation. In *BE Australia WD Pty Ltd (subject to a deed of company arrangement) v Sutton* (2011) 82 NSWLR 336, Campbell JA (McColl and Young JJA agreeing) held at [120]-[144] that the meaning of "creditor" for the purposes of voluntary administration had no wider meaning than that arising from s 553.
72 See e.g. Protection of the Environment Operations Act 1997 (NSW), s 250(1)(h), which enables a court to order an offender to provide to the Environment Protection Authority "a financial assurance, of a form and amount specified by the court … if the court orders the offender to carry out a specified work or programme for the restoration or enhancement of the environment." As a further example, Part 8.4 of the Environment Protection Act 2017 (Vic) allows the Environment Protection Authority to require a person undertaking a particular activity regulated by that Act to provide a financial assurance if the Authority is satisfied that assurance "is necessary as security for the costs and expenses of remediation or clean up in connection with the particular activity."

The exception is found in environmental protection legislation recently enacted by the State of Victoria, which purports to enable the Victorian Environment Protection Authority to recover from a company reasonable costs incurred by the Authority in exercising its regulatory powers,[73] regardless of the operation of the restructuring provisions of the Corporations Act.[74] However, that provision is yet to be considered in any reported judgment, and it remains to be seen whether it will prevent such costs being compromised under a restructuring, or (in effect) provide them with a super-priority, and whether other states will follow suit and enact cognate provisions.

#### *2.1.3 Disclaimer of environmental obligations*

Unlike the situation in liquidation, none of the corporate restructuring mechanisms available under Australian law provides for the disclaimer of onerous property.

### 2.2 Social (S): restructuring health or safety-related liabilities

The general situation regarding the restructuring of health or safety-related liabilities is the same as that regarding environmental liabilities, set out in section 2.1 above.

#### *2.2.1 Types of health and safety-related liabilities*

As with environmental obligations, laws regarding health and safety are many and varied, and have their source in both common law and statutes, the latter at both Commonwealth and state and territory level.

For example, tort creates liabilities in (among others) the manufacturers of products, the occupiers of property and the operators of vehicles and machinery. Contracts can impose express and implied safety requirements. Statutes impose liabilities on employers to ensure the safety of employees and their workplaces.

#### *2.2.2 Treatment of health and safety-related liabilities*

With two exceptions, as with environmental liabilities, health and safety liabilities attract no specific priority under Australia's statutory restructuring regimes. Secured debts and debts discharged by a voluntary administrator might attract liability by reason of the fact that they bear those characteristics.

The two exceptions arise by reason of the inclusion of the employee entitlement priorities in the order of payment under the voluntary administration process.[75] Under the Corporations Act, amounts due in relation to injury compensation where the liability arose before the administration attract priority ahead of debts in respect of leave, debts in respect of employee retrenchment, and unsecured creditors.[76] Secondly, where a company was insured in respect of a liability to third parties (for example, liability insurance to cover employee injuries), the proceeds of any such policy must be paid to the third party in respect of whom the liability was incurred.[77]

### 2.3 Governance (G): third party releases in favour of directors and officers of the company

As a general rule, third parties can be released from liabilities under any of the statutory or informal restructuring arrangements if the releasing party agrees to the release (for example, by voting in favour of the restructuring).

73 Environment Protection Act 2017 (Vic), s 297(1).
74 *Idem*, ss 297(5), 297A.
75 See above, n 38.
76 Corporations Act, s 556(1).
77 *Idem*, s 561.

Additionally, schemes of arrangement can be used to effect the release of third parties from debts to, and claims by, creditors without the express consent of the releasing creditors,[78] but neither deeds of company arrangement[79] nor restructuring plans[80] can do so.

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

Environmental protection authorities and environmental advocacy groups have no particular rights to intervene in the process of making or overseeing deeds of company arrangement or restructuring plans, save to the degree that such an authority or group might be a creditor of the company in question (for example, where a regulator has imposed a penalty or compensation order under environmental legislation prior to the commencement of the proceeding).

It remains the case that a company undergoing restructuring may be required to comply with obligations under environmental legislation, though, and plaintiffs in court proceedings to enforce such obligations might be granted leave to continue despite the moratorium created by the voluntary administration and small business restructuring regimes.

While environmental authorities and advocacy groups might seek to influence a scheme of arrangement on public policy grounds,[81] the only public policy which is relevant to a court's authorisation of creditors' meetings and scheme documents is that relevant to the interests of members, creditors, future counterparties and future investors,[82] and so it is unlikely that an environmental regulator or advocacy group would have standing to oppose a scheme for a regulatory or public interest purpose.

There is no public interest basis on which to challenge a deed of company arrangement or restructuring plan. While the courts have jurisdiction to terminate a deed of company arrangement on the ground that effect cannot be given to it without injustice or undue delay, an environmental regulator or advocacy group would not have the necessary standing to apply for such an order, as standing is restricted to the company, creditors, ASIC and persons whose material rights or economic interests are or might be substantially affected by the deed.[83] Standing is even more restricted in relation to applications to terminate restructuring plans,[84] with the effect that environmental regulators and advocacy groups would have no capacity to move the court to terminate such a plan (other than as affected creditors).

#### *3.1.1 Approving a restructuring plan*

This is addressed above.

#### *3.1.2 Discretion to consider wider public interest concerns*

This is addressed above.

#### *3.1.3 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

To the extent that a scheme, deed of company arrangement or restructuring plan might involve the ongoing operation of a business or ownership of property, environmental protection authorities and environmental advocacy groups might have relevant input into the formulation of the relevant proposal. Any such input results not from legal prescription, but as a practical

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78 See above, n 8.
79 See above, n 37.
80 See above, n 64.
81 For which see above, n 6.
82 *Re CSR Ltd* (2010) 183 FCR 358, 375 [54] (Keane CJ and Jacobsen J), 381 [82] (Finkelstein J).
83 *In the matter of Antqip Hire Pty Limited* [2020] NSWSC 487, [84] (Rees J).
84 Corporations Regulations 2001 (Cth), reg 5.3B.63.

function of the fact that the prospect of the business successfully operating under the scheme, deed or plan might be dependent on regulatory authorisation (such as ongoing licences) or (practically speaking) the absence of challenges from advocacy groups.

## 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

Generally speaking, in all restructuring proceedings, labour unions and worker advocacy groups are in the same position as environmental advocacy groups, described in section 3.1 above.

However, where a large proportion of a company's employees are members of a labour union, that union is likely to have greater say at the bargaining table in the preparation of any scheme or deed.

Further, in voluntary administration, particularly in large administrations, it is not uncommon for unions (usually with the cooperation of the relevant voluntary administrator) to obtain court orders allowing them to vote on behalf of employee creditors during the administration process, effectively "dealing them in" to the negotiation of any deed of company arrangement.[85]

### *3.2.1 Approving a restructuring plan*

This is addressed in section 3.1 above.

### *3.2.2 Discretion to consider wider public interest concerns*

This is addressed in section 3.1 above.

### *3.2.3 Protection of employee rights*

This is addressed in section 3.1 above.

## 3.3 Governance (G): board / management conflicts addressed in a restructuring

In a scheme of arrangement, the explanatory statement must disclose "any material interests of the directors of the body, whether as directors, as members or creditors of the body or otherwise, and the effect on those interests of the proposed compromise or arrangement in so far as that effect is different from the effect on the like interests of other persons."[86]

There is a divergence of views at trial level, so far unresolved by any appellate court, as to whether it is appropriate for a director who will receive a substantial benefit by reason of the scheme participating in any recommendation to creditors or members. One view is that such a director should not participate in making the recommendation, whereas the contrary (and increasingly predominant) view is that such a director may participate so long as the benefit is disclosed "fully and prominently" in the scheme booklet.[87]

In voluntary administration, failure to disclose the directors' interests in a deed of company arrangement may lead to the deed being overturned by a court.[88] For example, in *Re Recycling Holdings Pty Ltd*,[89] a director had an interest in the approval of a deed because it would potentially avoid the investigation by a liquidator of transactions under which the director had received money. The director also had a personal interest in litigation which a company associated with him intended to fund under the deed. Neither interest was disclosed to creditors by the voluntary administrator before the meeting at which the creditors voted in favour of the deed. On an

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85 See *Transport Workers' Union of Australia, in the matter of Virgin Australia Holdings Ltd* [2020] FCA 1218 (Middleton J) and the cases cited therein at [16].

86 Corporations Act, s 411(3).

87 The views are summarised, by reference to the supporting authorities, in *Re Japara Healthcare Ltd* (2021) 156 ACSR 695, [2021] FCA 1150, [71] (Moshinsky J).

88 Under the Corporations Act, s 445D.

89 (2015) 107 ACSR 406, [2015] NSWSC 1016 (Brereton J).

application to set aside the deed, the judge held that those omissions were material, but found that inclusion of the omitted matters would not have altered the outcome of the second meeting (and that under that particular deed, the creditors would in any event retain the ability to liquidate the company should they not receive a 100% return) and so declined to set aside the deed.[90]

The courts' powers to terminate restructuring plans are similar to the powers to terminate deeds of company arrangement,[91] and so the expectations regarding the disclosure of directors' interests are likely to match the voluntary administration requirements closely. However, given the mandatory nature of the standard terms for restructuring plans[92] and the consequently limited scope for involvement by directors in the terms of a plan, a need to disclose might arise less often than under schemes and deeds.

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

There are no environment-specific soft law instruments which apply directly in a restructuring context.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

There are no soft law instruments which apply specifically in a restructuring context for the purpose of directly protecting employee interests, but practice statements published by the leading industry body for restructuring professionals (the Australian Restructuring Insolvency and Turnaround Association, or ARITA) encourage both employee-specific communication plans to be developed in restructuring[93] and the inclusion of employee-specific provisions in the statutory reports to creditors under voluntary administration.[94]

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

Company directors, other company officers and certain employees are subject to statutory and equitable duties to avoid conflicts of interest. The Corporations Act applies the same statutory duties that apply to other officers of the company to voluntary administrators, deed administrators and restructuring practitioners.[95]

Further, ARITA's Code of Practice imposes a detailed set of rules which bind ARITA members and operate additionally to the legal duties. Among other things, those rules restrict the appointments which practitioners take, and prescribe certain disclosures which must be made in reports to creditors.[96] Further, ARITA members, their firms and their firms' partners and employees must not derive any profit or advantage from an administration (including by buying property from, or selling property to, an entity in administration) without legislative or judicial approval.[97]

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

ESG-linked bonds are issued by government, corporate and other non-government issuers in Australia. Australia's largest state, New South Wales, had AUD $7.2 billion in "sustainable bonds" on

90 *Re Recycling Holdings Pty Ltd* (2015) 107 ACSR 406, [48], [56]-[57], [110]-[112] (Brereton J).
91 See Corporations Act, s 445D; cf Corporations Regulations 2001 (Cth), reg 5.3B.63.
92 See above, n 53 to n 55.
93 ARITA, *Practice Statement Insolvency 6: Communication with Creditors*, para 6.5.
94 ARITA, *Practice Statement Insolvency 4: Voluntary Administrator's Report*, para 4.4.5.
95 Corporations Act, s 9 (definition of "officer") and Part 2D.1.
96 ARITA, *Code of Professional Practice (4th edition)*, 16 September 2019, s 3.
97 *Idem*, cl 6.11.

issue by 30 June 2022,[98] and other states have issued billions of dollars in bonds as well. The Commonwealth Government announced in December 2022 that it would consider issuing its own sustainable bonds.[99] Outside of government, bonds have been issued by banks, private companies and public institutions such as universities. According to the Climate Bonds Initiative (CBI), at the end of the first half of 2022, Australian issuers had issued US $25.3 billion in "green bonds', US $2 billion in "social bonds" and US $9.2 billion in "sustainability bonds".[100]

Australian banks and their borrowers have also shown a significant appetite for sustainability-linked loans (SLLs). Typical characteristics of SLLs include pricing linked to the achievement of environmental goals, and covenants limiting the use of loan proceeds to particular sustainable purposes.[101] A CBI report dated April 2021 summarised hundreds of millions of dollars of SLLs issued in the Australian market to that date,[102] as well as several classes of asset-backed securities underpinned by green loans.[103] Even major loans have been refinanced, with reports of SLL-conforming club loans in excess of AU $2 billion.[104]

## 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

Of Australia's "big four" banks,[105] only NAB is a signatory to the UNEP Commitment to Climate Action.

However, all four have introduced targets for financed emissions,[106] have adopted the Equator Principles,[107] and are members of the Net Zero Banking Alliance. All of them (together with many other large Australian organisations) have declared their support for the recommendations of the Task Force on Climate-Related Financial Disclosures (TCFD).[108] Additionally, all four banks

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98 New South Wales Treasury Corporation, *NSW Sustainability Bond Programme Annual Report 2022*, <https://www.tcorp.nsw.gov.au/resource/NSW_Sustainability_Bond_Programme_Annual_Report_2022.pdf>, accessed 12 January 2023, 3.

99 Jacob Greber, *Chalmers Takes Aim at Climate "Greenwashing" in Disclosure Shakeup*, Australian Financial Review, 11 December 2022 <https://www.afr.com/politics/federal/chalmers-takes-aim-at-climate-greenwashing-in-disclosure-shakeup-20221211-p5c5eh>, accessed 12 January 2023.

100 <https://www.climatebonds.net/market/data/>, accessed 12 January 2023.

101 See e.g. Martin Kelly, *Green Financing Takes Off in Commercial Property*, Australian Financial Review, 8 June 2022, https://www.afr.com/property/commercial/green-financing-takes-off-in-commercial-property-20220607-p5arpp, accessed 12 January 2023. For a broader discussion of potential clauses that might be included in SLLs or green bonds in an Australian context, see Ryan Chan, "Endorsing Impactful Performance in Green Bonds and Sustainability-Linked Loans" (2021) 42(1) *Adelaide Law Review* 221, 242-251.

102 CBI, *Green Loans Australia & New Zealand* <https://www.climatebonds.net/files/reports/cbi-green-loans-aus-nz-final-14102020.pdf>, accessed 12 January 2023, 5.

103 CBI, *Green Loans Australia & New Zealand* <https://www.climatebonds.net/files/reports/cbi-green-loans-aus-nz-final-14102020.pdf>, accessed 12 January 2023, 6.

104 See e.g. Allens Linklaters, *Allens Advises on Australia's Largest Sustainability-Linked Loan*, <https://www.allens.com.au/insights-news/news/2021/05/allens-advises-on-australias-largest-sustainability-linked-loan/>, accessed 13 January 2023.

105 Commonwealth Bank of Australia (CBA), National Australia Bank Limited (NAB), Westpac Banking Corporation (WBC), Australia and New Zealand Banking Group Limited (ANZ).

106 See <https://www.commbank.com.au/content/dam/commbank/about-us/shareholders/pdfs/results/fy20/cba-fy20-tcfd-report.pdf> (CBA); <https://www.nab.com.au/about-us/social-impact/environment/climate-change> (NAB); <https://www.westpac.com.au/content/dam/public/wbc/documents/pdf/aw/sustainability/Net-Zero_2030_Targets_and_Financed_Emissions-our_methodology_and_approach.pdf> (WBC), and <https://www.anz.com/content/dam/anzcom/shareholder/2022-anz-esg-supplement.pdf> (ANZ) all accessed 12 January 2023.

107 <https://equator-principles.com/members-reporting/>, accessed 12 January 2023.

108 As at the time of writing, TCFD records indicated that 168 organisations including CBA, NAB, WBC and ANZ had declared their support: <https://www.fsb-tcfd.org/supporters/>, accessed 13 January 2023. In 2021, 86% of the largest 50 companies listed on the Australian Securities Exchange (ASX) reported (fully or partially) under the TCFD recommendations, or disclosed that they were in the process of aligning their reporting with those guidelines, and 40% of the largest 200 ASX-listed companies aligned (or partially aligned) their disclosure to those recommendations: letter from the Council of Financial Regulators to the International Sustainability Standards Board dated 27 July 2022, <

consider ESG factors in their credit decisions.[109] Many other banks and financial organisations have their own climate and sustainability goals.

### 5.3 Promoting ESG by the central bank and regulators

The Financial Stability Board (FSB)[110] is an international organisation established by the heads of state and government of the G20.[111] In November 2015, at the request of the G20, the FSB established the TCFD.[112]

The TCFD published its final report in June 2017.[113] The report contains four recommendations for disclosure, "applicable to organisations across sectors and jurisdictions", and related to governance, strategy, risk management, and metrics and targets.[114]

One commentator has noted:[115]

> The TCFD report was greatly influential in Australia, with many regulators and governing bodies signalling their commitment towards monitoring entities' management of climate change risk, and also endorsing the report's recommendations as a preferred disclosure framework.

Two such regulators are the Australian Prudential Regulation Authority (APRA) and ASIC. APRA is responsible for the supervision of banks, insurance and superannuation companies. ASIC regulates corporations, financial markets and financial services.

Together with Commonwealth Treasury and the Reserve Bank of Australia (the RBA, Australia's central bank), APRA and ASIC are members of a coordinating body known as the Council of Financial Regulators (CFR). CFR members are members of the FSB, the G20 Sustainable Finance Working Group, and the Network for Greening the Financial System.

The CFR established a climate working group in 2017, and its member organisations have been engaged in several major ESG-related activities in recent years.

In 2019, ASIC updated its regulatory guide regarding disclosures in prospectuses and its regulatory guide regarding disclosure in operating and financial reviews to include climate-related risks within the kinds of risks that might need to be disclosed in fundraising documents. Both updates made reference to the risks referred to by the TCFD.[116]

At the request of the CFR, in 2020, APRA commenced a series of climate vulnerability assessments (CVAs) of major Australian banks, insurers and superannuation companies. The first

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https://www.ifrs.org/content/dam/ifrs/project/climate-related-disclosures/exposure-draft-comment-letters/a/australian-securities-and-investments-commission-7f6db4a7-bf19-47b1-bf45-b45906e3418f/final-cfr-submission---draft-issb-standards-27-07-2022.pdf>, accessed 13 January 2023.

109 See above, n 106.

110 <https://www.fsb.org/about/organisation-and-governance/members-of-the-financial-stability-board/>, accessed 13 January 2023.

111 <https://www.fsb.org/about/history-of-the-fsb/>, accessed 13 January 2023.

112 Financial Stability Board, *Press Release: FSB to establish Task Force on Climate-related Financial Disclosures*, 4 December 2015, <https://assets.bbhub.io/company/sites/60/2015/12/12-4-2015-Climate-change-task-force-press-release.pdf>, accessed 13 January 2023.

113 TCFD, *Final Report: Recommendations of the Task Force on Climate-related Financial Disclosures*, June 2017, <https://assets.bbhub.io/company/sites/60/2021/10/FINAL-2017-TCFD-Report.pdf>, accessed 13 January 2023.

114 *Idem*, 13-14.

115 See above, n 101, 240.

116 ASIC, 19-208MR ASIC Updates Guidance on Climate Change Related Disclosure, 12 August 2019, <https://asic.gov.au/about-asic/news-centre/find-a-media-release/2019-releases/19-208mr-asic-updates-guidance-on-climate-change-related-disclosure/>, accessed 15 January 2023.

five CVAs concerned the big four banks, together with another large bank, Macquarie Group Limited. Reporting on those CVAs in November 2022, APRA remarked:[117]

> The CVA results suggest that climate risk impacts are likely to be concentrated in specific regions and industries. For example, mortgage lending losses were higher in northern Australia, while bank losses were higher from lending to business sectors that are more exposed to transition risks, such as mining, manufacturing and transport.
>
> In response to these potential losses, the banks predicted that they would adjust their risk appetites and lending practices, such as cutting back on high loan-to-valuation lending and reducing their exposure to higher risk regions and industries.

In November 2021, APRA released Prudential Practice Guide (PPG) CPG 229 Climate Change Financial Risks.[118] APRA's PPGs do not set enforceable requirements but provide guidance on APRA's view of sound practice. The risks considered in the PPG include physical climate risks, transition climate risks and liability risks, and it encourages institutions to understand the interaction between those risks and the other risks created by the institutions' respective businesses. The PPG concerns matters of governance, risk management, scenario analysis and disclosure.

Also in November 2021, CFR members conducted consultations regarding potential Australian approaches to sustainable finance taxonomies. The CFR subsequently reported that it supports the work of the Australian Sustainable Finance Initiative (ASFI) in developing an Australian set of taxonomies.[119] The ASFI's work includes efforts to ensure that international rules are suitable for application to Australia's resource-intensive economy.[120]

In early 2022, the chair of ASIC announced that ASIC had commenced a review of the managed investment and superannuation sector focussed on "greenwashing": the practice where an entity "overrepresent[s] the extent to which its practices are environmentally friendly, sustainable, or ethical."[121] ASIC subsequently issued an information sheet to assist in the avoidance of greenwashing.[122]

Following a series of industry consultations, in June 2022, the CFR wrote to the International Sustainability Standards Board, supporting the development of a "climate first" set of sustainability-related disclosure standards.[123]

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117 APRA, APRA Releases Results of Inaugural Climate Vulnerability Assessment, 30 November 2022, <https://www.apra.gov.au/news-and-publications/apra-releases-results-of-inaugural-climate-vulnerability-assessment>, accessed 13 January 2023.

118 <https://www.apra.gov.au/sites/default/files/2021-11/Final%20Prudential%20Practice%20Guide%20CPG%20229%20Climate%20Change%20Financial%20Risks_0.pdf>, accessed 13 January 2023.

119 CFR, Council of Financial Regulators Climate Change Activity Stocktake 2022, < https://www.cfr.gov.au/publications/policy-statements-and-other-reports/2022/council-of-financial-regulators-climate-change-activity-stocktake-2022/>, accessed 13 January 2023.

120 Ayesha de Kretser, *Transition Rules Sped up as Emissions Target Set,* Australian Financial Review, 8 August 2022, <https://www.afr.com/companies/financial-services/transition-rules-sped-up-as-emissions-target-set-20220731-p5b603>, accessed 13 January 2023.

121 Joe Longo, Speech to the AICF Australian Governance Summit, *ASIC's Corporate Governance Priorities and the Year Ahead*, 3 March 2022, < https://asic.gov.au/about-asic/news-centre/speeches/asic-s-corporate-governance-priorities-and-the-year-ahead/>, accessed 14 January 2023.

122 ASIC, Information Sheet 271: How to Avoid Greenwashing when Offering or Promoting Sustainability-Related Products, June 2022, < https://asic.gov.au/regulatory-resources/financial-services/how-to-avoid-greenwashing-when-offering-or-promoting-sustainability-related-products/>, accessed 13 January 2023.

123 Letter from the CFR to the ISSB dated 27 July 2022, <https://www.ifrs.org/content/dam/ifrs/project/climate-related-disclosures/exposure-draft-comment-letters/a/australian-securities-and-investments-commission-7f6db4a7-bf19-47b1-bf45-b45906e3418f/final-cfr-submission---draft-issb-standards-27-07-2022.pdf>, accessed 13 January 2023. The ISSB had been established by the trustees of the International Financial Reporting Standards

The CFR's priorities for 2023 include further analysis of the outcomes of the CVAs and consideration of the next steps which they reveal as being appropriate; development and supervision of disclosure standards regarding sustainable finance; and continual engagement with industry in relation to the development of sustainable finance taxonomies.[124]

In addition to the work of the members of the CFR, it is important to note the activities of the Clean Energy Finance Corporation (CEFC), a Commonwealth Government corporation established by statute in 2012 with the intention of facilitating increased flows of finance into the clean energy sector.[125] The CEFC was given seed capital of AU $10 billion,[126] and operates under executive government mandates to invest those Commonwealth funds in clean energy projects.[127]

Foundation in 2021 to produce standards for ESG reporting: < https://www.ifrs.org/groups/international-sustainability-standards-board/>, accessed 13 January 2023.

124 Council of Financial Regulators Climate Change Activity Stocktake 2022, <https://www.cfr.gov.au/publications/policy-statements-and-other-reports/2022/council-of-financial-regulators-climate-change-activity-stocktake-2022/>, accessed 12 January 2023.

125 Clean Energy Finance Corporation Act 2012 (Cth), ss 3, 58.

126 *Idem*, s 46.

127 Most recently, the Clean Energy Finance Corporation Investment Mandate Direction 2020, dated 1 May 2020.

# BERMUDA

# 1. General overview of the restructuring regime

## 1.1 Formal restructuring procedures

### *1.1.1 Scheme of arrangement*

Bermuda's corporate insolvency and restructuring regime is governed by Part XIII of the Companies Act 1981 (Companies Act), as read together with the Companies (Winding up) Rules 1982. These statutes are based on the United Kingdom's Companies Act of 1948, and the United Kingdom's Companies (Winding Up) Rules 1949.

The scheme of arrangement is the primary tool used for restructuring debts in Bermuda. A scheme of arrangement is a formal procedure set out in section 99 of the Companies Act, which may be used to reorganise the debtor's business – that is, to reach a compromise or arrangement with its members and / or creditors, with a view to its continued trading. A scheme of arrangement is available to both solvent and insolvent companies.

Once a scheme of arrangement is approved by the requisite majority of creditors and sanctioned by the court, it becomes binding on all creditors subject to the scheme.

The result of a scheme of arrangement may, among other things, include the following:

- the adjustment or compromise of all or a class of the debt of the company;
- the cram-down of minority dissenting creditors;
- the transfer of rights, property and liabilities of the company to another; or
- the reorganisation of the company's capital.

Implementing a scheme of arrangement is generally the same whether it is proposed under a debtor-in-possession or a judicial management process.

A scheme of arrangement may be initiated by an application to the court by a creditor, a member, the company itself or a liquidator. The application is filed seeking leave to convene a meeting of the creditors, or the applicable class of creditors, at which they can vote on the proposed scheme. If the court so directs (which will almost always be the case), creditors must be summoned by notice and advertisement of the meeting in the local newspaper, The Royal Gazette.[1]

Where, because of differences in their respective rights, two or more creditors are unable to align their interests, it is necessary to separate creditors into classes to vote on the scheme proposal. A binding scheme of arrangement requires the approval of a majority within each class of creditors present and voting, representing 75% in value of that class. If the proposed solution is not approved by the requisite majority of the affected creditors or members in each class, the entire plan shall be void.

There are no restrictions on the types of debt which may be restructured. Any pecuniary claims against a company may be restructured under a scheme of arrangement, including contingent, unproven or unliquidated claims.[2]

Following approval through voting, a scheme must be sanctioned by the court. The court must be content that the statutory requirements are met, including the holding of requisite class meetings and approval by the necessary majorities, and that each class has been fairly represented. In addition, the court must be satisfied that the scheme is fair to the general body of creditors – specifically, that the majority has not taken unfair advantage of its position.

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1 The first hearing at the court is guided by Practice Direction No. 18 of 2017 "Guidelines Applicable to Schemes of arrangement under Section 99 of the Companies Act 1981", accessible at: https://www.gov.bm/sites/default/files/2007guidelines-applicable_schemes_of_arrangements.pdf.

2 See *re Markel CATCo Reinsurance Fund Ltd, et al,* Nos.307 and 309 (2022).

The final step is to deliver a copy of the order sanctioning the scheme to the Registrar of Companies, after which the scheme becomes effective and binding.

If the scheme of arrangement is conducted outside a liquidation, the company's board of directors and any managers control the process, although a scheme administrator is usually appointed to administer the scheme once it is implemented. The liquidator controls the process if the scheme of arrangement is conducted within a liquidation. As discussed below, there is a hybrid option, which is common, under which the scheme of arrangement is conducted by management under the supervision of a provisional liquidator.

### *1.1.2 Provisional liquidation*

The Supreme Court has developed an insolvency practice, through the appointment of provisional liquidators or "soft-touch" provisional liquidators with specific powers to implement a restructuring. This practice is designed to support formal and informal restructuring plans that have credible prospects of success and the support of the majority of creditors.

The compulsory liquidation process is initiated by petition to the Supreme Court of Bermuda by any one of the following:

- a creditor, including any contingent or prospective creditor;[3]
- a contributory;[4]
- the company itself (by a shareholders' resolution if it is solvent and / or by a directors' resolution if it is insolvent);
- the Registrar of Companies or the Supervisor of Insurance (being the Bermuda Monetary Authority); or
- in exceptional circumstances, receivers of segregated accounts within a segregated accounts company.

A company may be compulsorily wound up by the Supreme Court of Bermuda in any of the following circumstances:[5]

- if the company has, by resolution, resolved to wind up the company by the court;
- if the company is unable to pay its debts;[6]
- if the company fails to comply with specific statutory provisions;[7] or
- if the court opines that it is just and equitable that the company be wound up.[8]

3 Also including, in the case of insurance companies, pursuant to s 34 of the Insurance Act 1978, the petition of 10 or more policyholder creditors owed an aggregate value of not less than BMD 50,000.

4 That is, any person liable to contribute to the assets of the company in the event of its liquidation, i.e. a shareholder or member.

5 Companies Act, s 161.

6 For the purpose of s 161, a company is deemed to be unable to pay its debts, pursuant to s 162, if a creditor serves a statutory demand on the company's registered office which has been neglected or unsatisfied for a period of three weeks thereafter, or if a judgment in favour of a creditor remains unsatisfied, or if it is proved to the satisfaction of the court that the company is unable to pay its debts.

7 This includes if there is a default in holding the company's statutory meeting; if the company does not commence its business within a year of its incorporation or suspends its business for a whole year; if the company carries on any restricted business activity; if the company engages in a prohibited business activity; or if the company's ministerial consents were obtained as a result of a material misstatement in the application for consent.

8 There are a wide range of circumstances in which a court may conclude that it is just and equitable to wind up a company, including, for example, exclusion from management of a quasi-partnership,

Section 170(2) of the Companies Act allows the court to appoint provisional liquidators between the presentation of a winding up petition and its final hearing. There are a variety of circumstances in which the appointment of provisional liquidators or "soft-touch" provisional liquidators can be appropriate and in the best interests of creditors – for example, where there is an immediate risk of the dissipation of assets or there is a case for restructuring the company under the supervision of an independent court officer and with the benefit of a stay of legal proceedings.

Provisional liquidation operates similarly to Chapter 11 in the United States or administration in the United Kingdom, but with greater flexibility. The distinguishing feature of a Bermuda "soft-touch" provisional liquidation is that the board of directors retains some control over the company to effect a workout under the supervision of the provisional liquidators and the court.

The function, roles and powers of a provisional liquidator are set out in the order appointing the provisional liquidator. The powers can be tailored to suit the particular situation but typically include, as a minimum, unrestricted access to the company's books and records, oversight of the board and significant input on decisions made or transactions entered and the ability, if, necessary to seek a full-powers provisional liquidation wherein the board's powers are removed.[9] Likewise, the appointment order will set out any responsibilities or restrictions on the board deemed necessary.

This management-led, hybrid process offers a rich menu of choices for businesses weighing their restructuring alternatives, whether on a consensual basis or coupled with the scheme of the arrangement.

Under such a process, the key benefit is the operation of an automatic moratorium, which ensures the interests of the entire body of creditors are protected.[10] When a winding up order has been made or a provisional liquidator has been appointed, no action or proceeding shall continue or commence against the company except by leave of the court and subject to such terms as the court may impose.[11]

The other benefit is that the restructuring can be guided by the expertise of the provisional liquidators or "soft-touch" provisional liquidators, who act as officers of the court as its eyes and ears during the process.

## 1.2 Informal restructuring procedures

Informal, out of court restructurings are entirely possible. These restructurings are not explicitly governed by any legislation, but are conducted consensually, with no mechanism to "cram down" creditors.

Pre-packaged sales, while not entirely uncommon, are not easily facilitated under the current Bermuda regime. Winding up proceedings anticipate the company's death and the distribution of its assets, while the scheme of arrangement process is very creditor-centric in nature. Neither allows the discretion necessary for the negotiation and pre-agreement of a company's business disposal typical in a pre-packaged sale.

In some scenarios, a receiver and manager appointed by a secured creditor could potentially execute something akin to a pre-packaged sale. Similarly, a Bermudian-exempt company with its main interests or assets and liabilities in England might seek the support of both Bermudian and English courts for a pre-packaged sale under the supervision of a court-appointed administrator. However, there is some uncertainty in the case law regarding the scope of the power of courts in this respect.

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irretrievable breakdown of business relationships, failure of substratum, and lack of probity on the part of the company's directors.

9 Companies Act, s 175.

10 *Idem*, s 167(4).

11 Additionally, s 165 of the Companies Act provides that, at any time after the presentation of a winding up petition and before a winding up order has been made, the company or any creditor or contributory may apply to the court for a stay of any proceedings pending against the company.

In the case of an insolvent insurance company, another restructuring tool is available whereby the court can reduce the amount of the insurance contracts of the insurer on such terms and subject to such conditions as the court considers appropriate.[12] Although the procedure and case law in this area is not fully developed in Bermuda, the court would likely require that a meeting of policyholders be convened to canvass their views, and one relevant consideration for the court would be the effect of any reduction order on the insurance company's ability to make recoveries against its reinsurers. Depending on the circumstances, a formal scheme of arrangement may be required in any event.

## 2. Restructuring of ESG-related liabilities

### 2.1 Environmental (E): restructuring environmental liabilities

There exists a lacuna regarding the status of ESG claims, including environmental liabilities, under Bermuda's insolvency and restructuring laws. Such claims have not been distinguished from ordinary claims in any way, and there are no statutory protections, rules or general principles concerning the same.

Generally, then, ESG-related liabilities can be restructured under a scheme of arrangement in the same way as the ordinary liabilities of a company.

#### *2.1.1 Types of environmental liabilities*

The following are examples of environmental liabilities that can be or have been imposed in Bermuda:[13]

- Fines for air pollution

  Under the Bermuda Clean Air Act 1991 and the Clean Air Regulations 1993, entities can face environmental liabilities for non-compliance with air pollution control regulations. The Act mandates the licensing of polluting plants and establishes an Environmental Authority to oversee the issuance of these licenses. Violations of the terms and conditions related to the emission of air contaminants, as stipulated by the licenses, can result in significant penalties, including fines of up to BMD $50,000. The Act also provides for the issuance of Emission Control Orders and Stop Orders, non-compliance with which could potentially lead to further penalties. Furthermore, the forthcoming Clean Air Amendment Bill is set to update the existing legislation, setting stricter emission limits and making new provisions for odour control, thereby potentially expanding the scope of environmental liabilities related to air pollution in Bermuda.

- Enacted legal policies for the conservation of marine species

  Being an island, many fisheries provide a nourishing source of food for locals in Bermuda. There are a number of associated potential penalties which fall under the umbrella of environmental liabilities. Under the Fisheries Protected Species Order 1978, no company or individual is allowed to capture, injure, kill or destroy marine species in an exclusive economic zone (EEZ). Those breaking the law shall be liable to pay a sum of BMD $25,000 or serve two years as a punishment in jail.

- Clean-up costs for environmental contamination

  Bermuda has developed a monitoring system for repeatedly inspecting the impact of organisational activities on the environment. According to the guidelines set by the

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12 Insurance Act 1978, ss 37(5), 39.

13 Other environmental liabilities in Bermuda include penalties under the Protection of Birds Act 1975, the Protected Species Act 2003, and various Agriculture Acts, with fines ranging up to BMD $25,000 for violations. Additionally, non-compliance with pollution control laws such as the Water Resources Act 1975, and animal care and management regulations, such as the Dogs Act 2008, can result in significant fines and penalties. A comprehensive list of the relevant legislation, policies and plans can be found at https://environment.bm/legislation-and-policy/.

Department of Environmental and Natural Resources,[14] any company responsible for the discharge or release of petroleum or hazardous substances shall be liable to pay for the cleanup costs and follow the remedial action plan that incorporates all the necessary actions in this regard.

#### 2.1.2 *Priority given to environmental liabilities*

In Bermuda's insolvency or reorganisation processes, environmental claims are not given any special priority. There are no specific provisions that contemplate the controlling and remediation of environmental damage. This suggests that such claims would be treated as ordinary unsecured claims.

#### 2.1.3 *Disclaimer of environmental obligations*

Section 240 of the Companies Act provides that the liquidator of a company can, with the court's permission, disclaim any property belonging to the company or any rights under any contracts which the liquidator considers to be onerous for the company to hold, unprofitable or unsaleable.

The same provision can also apply in provisional liquidation. In Bermuda, the powers of a provisional liquidator are outlined in the order appointing them. This means that the ability of a provisional liquidator to disclaim property during a provisional liquidation would be determined on a case-by-case basis, depending on the specific powers granted to him / her in the court order.

As to whether the property can be disclaimed in a scheme of arrangement outside of a liquidation process, Bermuda law does not contain specific provisions as in the case of liquidation. However, it is generally understood that a scheme of arrangement allows for a wide range of restructuring possibilities and could potentially include some form of disclaimer arrangement. This would be subject to the specific terms of the scheme and the approval of the court.

This provides an avenue through which property that may give rise to continuing ESG-related obligations can be disclaimed. While there are no provisions or precedents in Bermuda specific to ESG liabilities, Bermuda recognises English common law, as well as United Kingdom legislation expressly made applicable to the jurisdiction.[15]

Section 178 of the United Kingdom’s Insolvency Act 1986 allows for the disclaimer of onerous property, which severs a company's rights, interests or obligations in relation to the property. The case of *Re UK Coal Operations Ltd* (2013) EWHC 2581 provides a precedent that may apply in Bermuda. In that case, UK Coal Operations Ltd commenced administration proceedings in mid-2013 and restructured prior to liquidation to enable its liquidators to disclaim onerous property, specifically a colliery destroyed by fire immediately following their appointment, which would otherwise incur continuing costs exceeding £100,000 per week.

### 2.2 Social (S): restructuring health or safety-related liabilities

#### 2.2.1 *Types of health and safety-related liabilities*

A company may be subject to the following health and safety-related liabilities regarding its operations in Bermuda:

- Food-related liabilities

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14 https://www.gov.bm/sites/default/files/Bermuda%20RBCA%20Guidelines%20March%202011%20Rev.4.pdf.

15 Decisions of the High Court and the Court of Appeal in England and Wales are persuasive on matters of English law applicable in Bermuda and such decisions are in practice often followed. Decisions of the Supreme Court (or its predecessor the House of Lords) are almost always followed in Bermuda in common law matters unless the case concerns a field of common law where circumstances in Bermuda make it inappropriate to develop that field in the same way in Bermuda as it has developed in England and Wales.

Bermuda has shown a commitment to the cleaner production and quality of food that is beneficial for human health and carries no harm to the body. According to the Public Food Health Regulations 1950, any act that incorporates food imported in Bermuda by any company for human consumption shall be liable to a certificate that the Chief Environmental Officer issues with a payment of a fee that comes in accordance with the Government Fees Act 1965. Authorities can cancel the licenses of any company if they fail to follow the standards.

- Liability in tort

  Any claims regarding safety and damage recovery are treated in the manner prescribed by the Law Reform (Liability in Tort) Act 1951. According to the Act, any tortfeasor liable in respect of that damage may recover a contribution from any other tortfeasor who is liable, or would if sued have been liable, in respect of the same damage, whether as a joint tortfeasor or otherwise. However, no person can recover contribution from any person entitled to be indemnified in relation to the liability for which the contribution is sought.[16]

### *2.2.2 Treatment of health and safety-related liabilities*

As with environmental claims, health and safety-related liabilities are not accorded any special priority during insolvency or reorganisation processes in Bermuda. This suggests that such claims are likely treated as ordinary unsecured claims. In the event of restructuring, the management and mitigation of potential health and safety issues, such as workplace accidents or food safety violations, typically fall to the entity undergoing the process.

## 2.3 Governance (G): third party releases in favour of directors and officers of the company

A restructuring proceeding can release claims against non-debtor parties where the company would otherwise have the power to do so. A release may be given either through a scheme of arrangement or by agreement of the liquidator or provisional liquidator on behalf of the company.

In some instances, a scheme of arrangement may release third parties from liability. However, this will be determined by the nature of the underlying obligation and the surrounding circumstances. In *re Markel CATCo Reinsurance Fund Ltd et al*, Nos. 307 and 309,[17] the court found that the release of certain third parties from potential liability *vis a vis* contingent creditor claims (as part of the proposal) was necessary to avoid ricochet claims which fell outside of the relevant indemnities and to secure additional funding from the shareholder of the scheme companies which was conditional upon obtaining the releases.

Given the substantial similarities in provisions relating to schemes of arrangements to those under Singapore law, the Bermuda court could consider and follow the position in Singapore in future when determining jurisdiction. This may include the "sufficient nexus" test – that is, whether there is a sufficient nexus or connection between the release of the third party liability and the relationship between the company and the scheme creditors.[18]

No restrictions or conditions apply when third party releases are sought in favour of directors and officers of a company concerning potential claims against them personally.[19]

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16 Civil proceedings in the Supreme Court are commenced by issuing a writ of summons (writ), originating summons, and a motion or petition in the Supreme Court Registry pursuant to order 5 of the Rules of the Supreme Court 1985.

17 See *re Markel CATCo Reinsurance Fund Ltd, Re CATCo Reinsurance Opportunities Fund Ltd* [2022] SC (Bda) 12 Com, Case 2021: Nos. 307 and 309.

18 See *Re Pathfinder Strategic Credit LP v Empire Capital Resources Pte Ltd* [2019] SGCA 29.

19 Additionally, a person who has knowingly assisted a director to commit a breach of his / her fiduciary duties to the company can be held liable for the loss to the company caused by the breach of the director's duties (see *Royal Brunei Airlines Sdn Bhd v Tan* [1995] 2 AC 378, a Privy Council decision cited as binding on the Supreme Court of Bermuda in *Mexico Infrastructure Finance LLC v Par-la-Ville Hotel and Residences Ltd* [2015] SC (Bda) 35 Com).

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

As set out in section 1.1 above, a binding scheme of arrangement requires the approval of a requisite majority within each class of creditors.

There is no requirement for a scheme of arrangement to be approved by environmental protection authorities or environmental advocacy groups. Likewise, there are no statutes or precedents which grant environmental protection authorities or ecological advocacy groups standing to air their views or concerns in a restructuring.

There is no case law in Bermuda concerning the extent to which the court may consider environmental issues in deciding whether to approve a scheme of arrangement.

On the matter of disclaiming onerous property, *Re Mineral Resources Ltd*[20] highlights possible tension between the application of section 178 of the United Kingdom's Insolvency Act 1986 *vis a vis* the polluter pays principle. The principle revolves around a public interest in maintaining a conducive and healthy environment. In contrast, powers under section 178 lean towards facilitating the orderly and prompt winding up of a company.

In *Re Celtic Extraction Ltd*,[21] the Court of Appeal was moved to answer the question of whether a license for waste management granted under the Environmental Protection Act of 2020 to a company can be disclaimed by a liquidator. The court opined that a waste management licence may be disclaimed as onerous property. The court further stated that the polluter pays principle does not extend to cases where a polluter is unable to pay as this would shift the costs to its unsecured creditors. This serves to affirm that it is unlikely that ESG-related liabilities, nor public interest concerns regarding ESG issues such as clean-up costs for environmental protection, would be given any form of precedence over or enjoy priority over the other debts owed by a company in a Bermuda liquidation.

### 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

As noted above, a scheme of arrangement must be approved by each class of creditors and the court. Employees, to the extent they are, or maybe, creditors, and any properly authorised representatives of employees, expressly have a standing to air their concerns in a restructuring.

Besides this, there is no requirement for a scheme of arrangement to be approved by labour authorities, unions or employee / worker advocacy groups. Likewise, there are no statutes or precedents which grant labour authorities, associations or employee / worker advocacy groups standing to air their views or concerns in a restructuring.

There is no case law in Bermuda concerning the extent to which the court may consider labour issues in deciding whether to approve a scheme of arrangement.

### 3.3 Governance (G): board / management conflicts addressed in a restructuring

Directors' and officers' duties are principally owed to the company itself. To the extent the company is solvent, those duties are ordinarily owed to the company for the benefit of its present and future shareholders. Directors may be held civilly or criminally liable if they fail to provide full disclosure to the court or a liquidator, fraudulently remove or conceal assets of the company, falsify accounts of the company or have been dealing with assets of a company with the intent to defraud creditors.[22]

20 (1999) 1 All ER 746.
21 [2001] Ch 475.
22 Companies Act, s 97.

Following approval of a scheme of arrangement through voting, it must be sanctioned by the court. Generally, in deciding whether to approve a restructuring plan, the court must be satisfied that:

- the statutory requirements have been satisfied;
- each class of members or creditors is represented fairly; and
- the scheme of arrangement passes the reasonable person test.[23]

In the absence of a challenge to the scheme, the court will typically be guided, but not bound, by the views of the creditors and will be reluctant to differ from those views. In some instances, the court may refuse to sanction a scheme of arrangement – for example, if the court finds it is being used as a mechanism to oppress minority shareholders, that the scheme itself is fraudulent, or that creditor classes have not been adequately established.

When winding up proceedings are commenced, directors must act in the best interests of the company's creditors. A director may be held personally liable if it is proven to the court that the director:

- knew of the carrying on of a company and had the intent to defraud creditors;[24]
- misapplied company property or resources;[25] or
- is guilty of breach of trust in relation to the company.[26]

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and best practices prescribed for the protection of the environment in a restructuring

There have yet to be any industry guidelines or best practices prescribed for protecting the environment in a restructuring.

Though ESG has yet to be incorporated into law in Bermuda, some corporate and financial services firms in Bermuda are following the lead of their global counterparts by creating their own ESG policies[27] and reporting standards, and beginning to increase service offerings in the space, reflecting growing awareness and changing tastes among clients.

### 4.2 Social (S): industry guidelines and best practices prescribed for the protection of employee rights in a restructuring

There are no Bermuda-specific industry guidelines or best practices prescribed for dealing with employees in a restructuring. Restructuring professionals abide by the local labour laws, and generally beyond, through the incorporation of hard and soft laws in other jurisdictions.

Section 33 of the Employment Act 2000 states that employment contracts are automatically terminated one month after the winding up unless the business continues to operate and

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[23] The reasonable person test generally describes the benchmark that would need to be met for an intelligent and honest person to approve. See *Re National Bank plc* (1966) 1 WLR 819; *Re English, Scottish and Australian Chartered Bank* (1893) 3 Ch 385, 409; *Re Alabama, New Orleans, Texas and Pacific Junction Railways Company* [1891] 1 Ch 213; and *Re Dorman, Long and Company Limited* [1934] Ch 635.

[24] Companies Act, ss 246-247.

[25] *Idem*, s 54.

[26] *Idem*, ss 243-248.

[27] Examples include corporate services firm Ocorian (https://www.ocorian.com/environmental-social-and-governance-esg-responsibility).

employees are retained. Upon termination, employees are entitled to apply for the recovery of various accrued entitlements in priority to the unsecured creditors.[28]

### 4.3 Governance (G): industry guidelines or codes of conduct prescribed for restructuring professionals

There are no specific qualification requirements or licenses for restructuring professionals in Bermuda, but they are generally qualified accountants with particular expertise in insolvency or restructuring.[29]

Restructuring professionals are typically members of international communities which promote best practices and the formulation of legislation, such as the Restructuring and Insolvency Specialists Association of Bermuda.

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

As a significant international financial hub, Bermuda actively supports the creation and management of ESG-linked bonds, loans and investments. This is achieved through an array of services and structures that can be custom-tailored to meet specific ESG goals. These services range from developing and listing insurance-linked securities (ILS) to establishing investment funds and trust structures[30] for both institutional investors and high-net-worth individuals.[31]

The commitment to ESG initiatives extends to participation in regional promotional activities, as illustrated by Bermuda's representation at events such as the Caribbean ESG & Climate Financing Summit.[32] Furthermore, the Bermuda Business Development Agency (BDA)[33] has spearheaded the launch of Climate Hub. This Hub is a cross-agency partnership with Bermuda's Ministry of Home Affairs, Regulatory Authority and the Bermuda Ocean Prosperity Programme. Its primary goal is to stimulate climate-centric initiatives and attract related investments.[34]

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

Financial institutions in Bermuda are moving toward the adoption of ESG-friendly initiatives and opportunities and carbon neutrality, driven by a combination of rising awareness of ESG issues, changes in underlying investor demand and perceptions of reputational risks from the failure to meet the prevailing climate of public opinion.[35]

The collective aim of these institutions is to achieve carbon neutrality by designing and implementing comprehensive strategies to reduce their carbon emissions. Moreover, the

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28 The Workmen's Compensation Act 1965 provides that employees may also claim redundancy payments under unsecured preferential payments in liquidation. Unless an express clause in a contract of employment says otherwise, employees who bring a claim for redundancy payment will be limited to a maximum of BMD $2,500 each. Employees may also recover severance pay not exceeding their annual salary and benefits for 26 weeks.

29 Since November 2020, at least one office holder must be resident in Bermuda, which ensures that provisional liquidators are familiar with local practices and legal requirements.

30 For example, as the first offshore jurisdiction to permit the establishment of non-charitable purpose trusts with the Trusts (Special Provisions) Act 1989 (as amended). Such trusts have no ascertainable individual beneficiaries and instead have specific purposes which need not be charitable, and so can be, and today are widely used to manage ESG investments.

31 Such as The Atlantic Philanthropies which was founded in Bermuda in 1982.

32 The country was represented at the 2nd Caribbean ESG & Climate Financing Summit, an event aimed at accelerating the adoption of a new operating and financing ecosystem for the Caribbean Region. This event brings together borrowers, lenders, and investors to normalize the use of ESG and climate finance region wide.

33 The Bermuda Business Development Agency (BDA) is an industry advocacy group that uses targeted marketing, events and networking strategies to facilitate growth in the Bermuda economy.

34 Such as Bermuda's first Climate Summit, hosted in May 2022.

35 Bermuda's HSBC recently joined the Net Zero Banking Alliance (NZBA), alongside 42 other monetary institutions worldwide designed to accelerate the global transition to net zero.

importance of ESG issues is increasingly acknowledged in the insurance sector, particularly in aspects such as underwriting risk, investment decision-making, corporate governance and the structuring of their businesses. To arrive at their net-zero goals, local institutions are beginning to build out their net-zero pathways through current portfolio emanations, using data modelling to estimate carbon emissions and developing holistic transition strategies to reduce carbon emissions through incremental goals.

Banks also offer "green loans," which can be used to finance environmentally friendly projects such as the cost of solar panels, electric cars, solar water heaters and other energy-saving enhancements at lower interest rates than personal loans.[36]

### 5.3 Promoting ESG by the central bank and regulators

The Bermuda Monetary Authority (BMA), as the central bank and main financial regulator of Bermuda, plays a vital role in promoting ESG principles. The BMA has demonstrated this commitment by revising the Insurance Code of Conduct to place a greater emphasis on good governance and effective management of risk, particularly in the context of ESG issues. It has also issued a series of guidelines that outline its expectations regarding climate risk management for insurance companies. In addition, the BMA is proactive in its efforts to refine its regulatory regime, with a particular focus on integrating good practice methodologies related to ESG.

The Bermuda Government and regulatory authorities frequently interact with industry advocacy groups to help Bermuda's markets identify and capitalise on new openings within a resilient regulatory framework.[37]

Bermuda plans to replace 85% of its fossil fuel consumption with renewable energy sources by 2035.[38] It aims to achieve this through a variety of public sector programmes such as investing in solar power, cultivation and protection of the local ecosystem from pollution and invasive species and investment in infrastructure for electric vehicles.[39]

In line with this goal, the Regulatory Authority has developed an innovative track under Bermuda's Economic Recovery Plan, which provides a platform for new renewable energy developers to test their products.[40]

In a similar vein, the Bermuda Stock Exchange has taken steps to promote responsible investment strategies. This commitment was demonstrated in 2019 when it launched an ESG campaign that promoted sustainability principles developed by the World Federation of Exchanges.[41]

36 https://www.hsbc.bm/loans/products/green-loan/ and https://clarienbank.com/besolar/.
37 The Bermuda Institute of Ocean Sciences (BIOS) partners with the Government's Department of Environment and Natural Resources, the Department of Education and the Marine Resources Board.
38 https://www.gov.bm/articles/government-bermuda-%E2%80%93-protecting-environment.
39 https://www.bda.bm/conservation-central/.
40 Following the success of the Bermuda Monetary Authority's Sandbox for Digital Assets and Insurtech.
41 https://iclg.com/briefing/13620-esg-investing-in-bermuda.

# BRAZIL

## 1. General overview of the restructuring regime

Federal Law No. 11,101/2005 (Brazilian Bankruptcy Law), amended by Law 14.112/2020, establishes three insolvency proceedings in Brazil: judicial reorganisation, extrajudicial reorganisation and liquidation.

The liquidation proceeding shall apply when the company is no longer viable. In this case, the debtor is removed from the company's management, activities and control of its assets. The existing assets are gathered, appraised and sold by a judicial administrator appointed by the court, who will use the proceeds to pay the creditors of the bankruptcy.

### 1.1 Formal restructuring procedures

A judicial reorganisation proceeding starts with the filing of a petition by the debtor with the court, and may only be voluntary, insofar as creditors cannot request a debtor's judicial reorganisation, and neither can the court include *ex officio* a company that was not included by the debtor in its request.

To be eligible to file the request, the debtor cannot:

- be bankrupt;
- have had another judicial reorganisation request granted within the past five years; or
- have been convicted for a bankruptcy crime.

The judicial reorganisation request must be filed before a court with competent jurisdiction, which is the court where the company's centre of main interests is located (being the place where the debtor conducts the administration of its interests).

The judicial reorganisation binds all the existing claims against the debtor at the time of the request (pre-petition claims), even those undetermined or not yet matured or disputed, contingent or unliquidated at the time of the filing, except for:

- tax and social security-related claims;
- claims related to forward foreign exchange agreements; and
- claims arising from financial leases, claims secured by a fiduciary lien (*alienação fiduciária*), claims of owners or committed sellers of real estate where the underlying agreements include an irrevocable and / or irreversible provision, and claims arising under purchase agreements containing a title retention provision.

For ease of reference, the above claims are referred to in this chapter as Exempted Claims, and the creditors of such Exempted Claims are referred to as Exempted Creditors.

Regarding tax claims, the Brazilian Bankruptcy Law expressly demands a debt clearance certificate from the debtor for the ratification of the restructuring plan. However, the Law enables companies under judicial reorganisation to negotiate and enter into agreements with the Office of the General Counsel for the National Treasury from the date of the processing order until the moment immediately before the ratification of the plan by the court.

Once the debtor files for judicial reorganisation, and provided all legal requirements are met, the court will appoint a judicial administrator and authorise the commencement of the proceeding (Processing Order), which triggers a stay period of 180 calendar days, extendable once for the same period, provided the debtor did not contribute to the necessity of the extension (Stay Period). During the Stay Period, most of the lawsuits filed against the debtor, including all foreclosure proceedings, will be stayed. Although Exempted Claims are not subject to the proceeding, assets deemed by the reorganisation judge to be essential for debtor's activities cannot be sold or removed from the debtor's place of business during the Stay Period.

As a rule, the debtor remains in possession of the assets and management of its activities. After the filing, the debtor cannot sell its non-current assets without prior authorisation of the court or of the plan approved at the creditors' meeting foreseeing the sale of the assets.

The role of the judicial administrator is limited to the supervision of the proceeding, verification of claims and organisation of the creditors' meeting.

After the publication of the list of creditors in the Official Gazette, creditors may file a proof of claim with the judicial administrator challenging the list (its own claim or other creditors' claims) within 15 days. After 45 days, the judicial administrator shall submit a new list, considering the proof of claims filed. After the publication of the new list, creditors may file a proof of claim before the court within 10 days. The court will then render a final decision on the credit claim.

The debtor must submit its reorganisation plan with the court within 60 days of the date of publication of the Processing Order in the Official Gazette, under penalty of a bankruptcy decree.

After the publication of a notice informing the creditors about the filing of the plan, creditors may file objections to the plan within 30 days. If there is no objection, which is unusual, the plan will be automatically approved. However, in case of an objection to the plan filed by any creditor, the court must convene a creditors' meeting to discuss and vote on the plan. The debtor may modify or amend the plan even during the creditors' meeting.

There are four classes of creditors in judicial reorganisation proceedings that vote at the creditors' meeting:

- class I – labour creditors;
- class II – secured creditors;
- class III – unsecured creditors; and
- class IV – micro and small businesses companies.

As a rule, the four classes of creditors must approve the plan by a majority of the votes of creditors attending the meeting. Labour and micro-enterprises or small businesses must approve the plan on a headcount basis, while secured and unsecured creditors must approve it both on a headcount and amount of claims basis.

The shareholders, affiliated companies, controllers, companies under control of the debtor, companies holding more than 10% of the debtor's shares or companies in which the debtor holds more than 10% of the shares cannot vote at the creditors' meeting.

The court may approve the plan by the "cram down" mechanism if it is approved by:

- three out of the four classes of creditors;
- at least 50% of the creditors attending the meeting, by number of claims; and
- a third of the creditors in the dissenting class.

If the plan is approved, the court will analyse the legality of the plan and, afterwards, homologate it, causing the novation of all the claims subject to the judicial reorganisation.

In case of rejection of the plan, the judicial administrator will give creditors a deadline of 30 days to file an alternative judicial reorganisation plan (Alternative Plan). To be voted on, the Alternative Plan presented by the creditors must include a written statement of support from creditors representing more than 25% of all claims subject to the proceeding or at least 35% of the creditors that were present at the creditors' meeting in which it was decided to submit the Alternative Plan.

If the Alternative Plan is rejected, the court will decree the debtor's liquidation.

After ratification of the approved plan by the court, the debtor remains under judicial reorganisation for a period of up to two years under the supervision of the judicial administrator and the court. Such a period shall be defined by the court.

In case of failure by the debtor to comply with the provisions of the plan during the supervision period, the court will decree the debtor's liquidation. After the supervision period, the judicial reorganisation proceeding is terminated, and in case of default by the debtor, creditors may either request the debtor's liquidation, or file an enforcement proceeding against the debtor seeking the payment pursuant to the conditions of the approved reorganisation plan.

### 1.2 Informal restructuring procedures

During the extrajudicial or out of court reorganisation proceeding, the debtor remains in possession and shareholders, officers and directors appointed by the shareholders keep control and management of the debtor company's business, under the supervision of a creditors' committee if applicable and of the judicial administrator.

Out of court reorganisation allows the debtor to restructure its debts with specific groups of creditors, for example, only financial institutions or secured creditors. In the extrajudicial reorganisation proceeding, the debtor negotiates a plan with its creditors (pre-package restructuring) and may request the homologation of the plan before the court to become binding on other creditors included in the extrajudicial reorganisation.

The debtor negotiates the terms of the plan, and which companies are going to be part of the restructuring, prior to the filing of the request before the court.

Brazilian Bankruptcy Law provides that the debtor may request the homologation of its extrajudicial reorganisation plan that has the previous adhesion of the creditors representing the majority of claims (amount of claims basis) in each class subject to the plan.

Afterwards, if the legal requirements are met and the court homologates the extrajudicial plan, the non-adherent creditors will also be subject to the conditions agreed by the majority of creditors.

As the plan is previously negotiated between the debtor or debtors of the same economic group and its creditors, the court cannot include, *ex officio*, another company in the extrajudicial reorganisation.

As is the case in a judicial reorganisation, an out of court reorganisation binds all the existing claims against the debtor at the time of the request (pre-petition claims), except for the Exempted Claims referred to above.

Exempted Claims are not subject to extrajudicial reorganisation, and the inclusion of labour and occupational accident claims requires collective bargaining with the labour union of the respective professional category.

The debtor must obtain the approval of creditors representing more than 50% of the claims, in amount, in each affected group or class of claims. If that is obtained then, pursuant to the applicable law, the plan shall be confirmed by the court and become binding on holders of all impaired claims, including those who disagreed with it.

The request for confirmation of the extrajudicial reorganisation plan will also trigger the Stay Period, but only in relation to the claims included in the reorganisation. The ratification of the plan does not prevent the Exempted Creditors or creditors that were not included in the extrajudicial reorganisation from requesting the debtor's bankruptcy liquidation.

## 2. Restructuring of ESG-related liabilities

### 2.1 Environment (E): restructuring environmental liabilities

#### *2.1.1 Types of environmental liabilities*

Under the Brazilian Federal Constitution, environmental liabilities may occur at administrative, civil and criminal levels. Each type of liability is independent and may be cumulative, depending on the environmental violation.

Administrative liabilities are verified when the environmental legislation is violated and may result in the imposition of administrative sanctions by the environmental protection agencies, such as warnings, fines, suspension of activities, demolition of facilities, loss of tax benefits and prohibition of contracting with public authorities.

At the civil level, liabilities arise from damages caused to the environment and / or to third parties by means of environmental damage and give rise to repairing measures (recovery, compensation and / or indemnification).

The liability may be claimed in court by any injured party or, with respect to matters of public interest, by the Public Prosecutor, the Federal, State and / or Municipal Governments, or by organisations created to defend the environment, such as Non-Governmental Organisations (NGOs).

Although it does not require the evidence of fault, civil liability requires proof of the actual damage and of the causal link between such damage and the activity (acts / omissions) undertaken by the applicable party. In other words, the party will only be held liable if the damage, its extent and the link between the damage and the activity are evidenced.

In certain situations, Brazilian law allows, pursuant to the Environmental Crimes Act, the assignment of personal liability to the shareholders of a company in connection with environmental damages.

At the criminal level, the Environmental Crimes Act allows for the assignment of criminal liability to individuals and legal entities. Pursuant to the Brazilian Supreme Court's current understanding, companies can be criminally prosecuted for environmental crimes regardless of the concomitant prosecution of a representative or employee, and vice-versa. Regarding all other criminal offenses, including typical "white collar" crimes (such as fraud, bribery, money laundering, tax evasion and embezzlement), criminal liability only applies to individuals, not to companies.

Under Brazilian law, there is no strict liability in relation to criminal matters, because criminal liability cannot be passed on and Brazilian law does not provide for joint and several liability in criminal matters. In order to be criminally liable, the perpetrator must act with *mens rea* (knowledge and intention of wrongdoing) or fault (when the requirement of intent is expressly dispensed by law) and given this requirement of a subjective bond between the perpetrator and the criminal result, Brazilian law does not authorise the attribution of criminal liability based only on someone's role within a company.

#### *2.1.2 Priority given to environmental liabilities*

As a rule, environmental liabilities are considered unsecured credits, subject to the judicial reorganisation proceeding, and they ought to be restructured in a judicial reorganisation plan.

However, article 6 of the Brazilian Bankruptcy Law, amended by Law 14.112/2020, determines that the Stay Period does not apply to tax foreclosures. Hence, as environmental liabilities are enforced by tax foreclosures, there is a legal possibility that environmental fines are not subject to the judicial restructuring proceeding. However, this issue has not yet been finally settled by Brazilian courts.

Brazilian Bankruptcy Law states, after the amendment by Law 14.112/2020, that there is no succession to environmental liabilities of the purchaser of an asset of the restructuring company provided that it is acquired through an Isolated Productive Unit (UPI), through a competitive process and in accordance with the judicial restructuring plan approved in the general creditors' meeting duly ratified by the court.

However, as the Law is very new and there are no court decisions on this matter to date, it is possible that, if a third party (such as the Public Prosecutor's Office, environmental authorities, and others) challenges this "no succession rule" when it comes to the civil sphere (reparation of environmental damages), the entity acquiring the asset is held liable for environmental obligations and / or damages arising therefrom.

Furthermore, even if no challenges are raised by third parties, it is possible that, from a practical perspective, the entity acquiring or renting assets may need to adopt environmental recovery measures in order to be able to use the property. Depending on the existing environmental liabilities, restrictions may apply for the occupation and use of the assets while there are outstanding liabilities.

When it comes to the administrative sphere, it is likely that the acquirer will not be held liable for violations arising from activities developed by the company under reorganisation, given that administrative liability is personal and could not be transferred to third parties. Nevertheless, there are no court decisions on this matter to date either.

#### *2.1.3 Disclaimer of environmental obligations*

There is no concept of disclaimer under the Brazilian Bankruptcy Law.

### 2.2 Social (S): restructuring health or safety-related liabilities

#### *2.2.1 Types of health and safety-related liabilities*

Employers are responsible for providing a healthy and safe workplace for their employees. Besides several aspects established by the Labour Code (known as the CLT) related to the matter, there are 37 regulatory norms issued by the Ministry of Labour related to several distinct aspects of health and safety in the workplace.

The main provisions regarding health and safety set forth by Labour Code and regulatory norms are:

- election of an Internal Commission for Accident Prevention (CIPA);
- hiring of a specialised Safety Engineering and Occupational Medicine team (SESMT);
- providing free of charge personal protective equipment;
- providing medical examinations upon hiring, during the relationship and at the termination; and
- rules related to work environment conditions – including light, ventilation, fire protection, safety signs, buildings structures, machinery and equipment (safety shut off switches), unhealthy work conditions, risky work conditions, work at heights and ergonomic regulations.

If employers do not comply with measures related to health and safety in the workplace, employees may file labour claims requesting indemnifications, including damages relating to work-related accidents and illness and compensation for a reduction in capacity or death.

There may also be health and safety-related liabilities linked to social security contributions. For instance, the social security agency is responsible for the payment of retirement allowances.

Employees that work in unhealthy environments are entitled to special retirement, which means that they are allowed to retire before other employees (with the result that their length of contribution to the social security agency is reduced when compared to employees that do not face unhealthy conditions in their workplace). Because of that, employers that have unhealthy workplaces must pay higher social security contributions to the social security agency. Moreover, the fact that there are work-related accidents and illness at the workplace increases the social security contribution rate that the employer must pay. If the employer does not pay the proper social security contribution, the social security agency may claim it from the company.

#### *2.2.2 Treatment of health and safety-related liabilities*

According to the principle of "*par condition creditorum*", there are no payment priorities among claims.

However, as labour-related claims (safety-related liabilities being one of them) are considered basic maintenance amounts, the Brazilian Bankruptcy Law establishes that they must be paid within one year. This deadline may be extended to up to two years if the restructuring plan complies with the following requirements, cumulatively:

- it provides sufficient guarantees in the court's opinion;
- it is approved by labour creditors at the creditors' meeting; and
- it guarantees payment of all labour claims in full.

Moreover, according to Brazilian Bankruptcy Law, the claims in the nature of salary payments that are overdue for at least three months before the judicial reorganisation request date (limited to the amount of five minimum wages per employee – approximately BRL 7,000) must be paid within 30 days.

In the event of liquidation, claims are paid according to a priority list, in which labour creditors are the first to be paid.

### 2.3 Governance (G): third party releases in favour of directors and officers of the company

The Brazilian Bankruptcy Law expressly provides that third party guarantees shall remain in place. In theory, the restructuring plan, under the assumption that creditors may waive the guarantee, may provide for the release of third party guarantees. However, this issue has sparked considerable controversy in Brazilian courts.

Such a provision is usually considered by courts to be binding only on those creditors who voted in favour of the plan of reorganisation without any reserve to the release – this is the overall rule in Brazilian restructuring cases.

As per Brazilian law, restructuring or insolvency proceedings do not have the effect of releasing directors and other stakeholders from liability for previous actions and decisions, but it shall be analysed as per applicable law, as the Bankruptcy Law does not impose any changes in directors' and officers' duties.

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

#### *3.1.1 Approving a restructuring plan*

As previously mentioned, as a rule, the four classes of creditors must approve the plan by majority of the votes of creditors attending the meeting. The creditors' meeting has the sole jurisdiction to vote on the restructuring plan.

After the restructuring plan is approved at the creditors' meeting, the court must ratify it.

Creditors, the debtor itself, the judicial administrator and / or the Public Prosecution Officer might file appeals to the Court of Appeals to challenge the decision that ratified or did not ratify the plan.

There is no express rule in the Bankruptcy Law that determines the plan should be approved by any regulatory body other than the court. The Public Prosecution Officer, because it has the power / obligation to defend the public interest, may file petitions at any time, and / or appeals against the ratification of the plan, if it understands that one or more clauses of the restructuring plan are illegal.

However, there is no requirement for a restructuring plan to be approved by environmental protection authorities or environmental advocacy groups.

### *3.1.2 Discretion to consider wider public interest concerns*

In Brazil, insolvency proceedings are governed by the principles of the preservation and recovery of the company, maintenance of its social purpose and the incentive to economic activities. According to the Bankruptcy Law, the preservation of viable companies helps maintain employees' jobs, the interests of creditors and the maintenance of a production source.

These are the ultimate and wider public interest concerns of the judicial administrator, the Prosecution Office and the court.

However, as the approving body is constituted by the creditors that are seeking to recover their outstanding claims, the focus tends to be on creditors' own interests, ignoring wider issues such as environmental rights.

### *3.1.3 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

As mentioned previously, there is no express rule in the Brazilian Bankruptcy Law that determines that the plan should be approved by any regulatory body other than the restructuring court. It may happen, however, that a specific restructuring plan contains provisions regarding the fulfilment of environmental obligations. In such a case, the legality of such a provision will be analysed by the restructuring court.

## 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

Regarding the judicial reorganisation proceeding, its request binds all existing claims against the debtor at the time of the request (pre-petition claims), even those undetermined or not yet matured or disputed. It is not mandatory that unions of employees negotiate the restructuring plan. On the other hand, it is not unusual that the unions of employees have powers of attorney to represent creditors in the negotiations and during the creditors' meetings.

Regarding out of court reorganisation, the subjection of labour and occupational accident claims requires collective bargaining with the labour union of the respective professional category.

As mentioned, the court must exercise legal control of the restructuring plan and analyse its provisions – including those regarding the payment of labour claims – to verify if there is any illegality.

Therefore, if the restructuring plan does not follow the requirements mentioned in section *2.2.2* above or has any provision that is inconsistent with the Brazilian Bankruptcy Law and / or any other labour related laws (for example, by providing for a four-year payment plan), the court shall not ratify it.

### *3.2.1 Approving a restructuring plan*

As mentioned in section 1.1 above, the restructuring plan shall be voted on by the creditors at the creditors' meeting. Once it is approved, the court must analyse the legality of it and, afterwards, ratify it, causing the novation of all the claims subject to the judicial reorganisation.

It is important to mention that the court must not analyse the commerciality of the plan, but rather only verifies if there are any illegalities.

#### *3.2.2 Discretion to consider wider public interest concerns*

When deciding whether to approve a restructuring plan, the restructuring court is bound only by the result of the creditors' voting / deliberation. This means that the restructuring court's role is to analyse the legality of the restructuring plan provisions regardless of broader social concerns.

#### *3.2.3 Protection of employee rights*

As mentioned previously, if there are any illegalities regarding the requirements for employees' payment, the court shall not ratify the restructuring plan.

However, if the plan provides for haircuts not prohibited by the Brazilian Bankruptcy Law, the court does not have jurisdiction to rule on the negotiation held with creditors.

### 3.3 Governance (G): board / management conflicts addressed in a restructuring

Once the Processing Order is granted, the company under judicial reorganisation shall not encumber nor sell assets or rights of its non-concurrent assets, unless authorised by the court, after the creditors' committee is heard, or if authorised by the restructuring plan approved at the creditors' meeting.

In addition, to avoid conflicts of interests – given that the board / management will often control or influence the formulation of a restructuring plan – the Brazilian Bankruptcy Law provides that the debtor's partners, as well as affiliate companies, controllers, controlled entities or those which have a shareholder with equity in the company greater than 10% of the debtor's capital or in which the debtor or any of its partners own stake in more than 10% of the share capital, may participate in the general creditors' meeting, but are not entitled to vote and will not be considered for the purposes of verification of the quorum of installation and deliberation.

This restriction also applies to a spouse or relative, an administrator, a controlling partner, a member of the advisory, tax or similar boards of the debtor company, and any company in which any of these people perform those functions.

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

We have not identified any industry guidelines and / or best practices prescribed for the protection of the environment in a restructuring.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

We have not identified any industry guidelines and / or best practices prescribed for the protection of labour claims in a restructuring.

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

We have not identified any industry guidelines and / or best practices prescribed for the protection of the governance in a restructuring.

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

The theme of "investing with sustainability" is something that is growing every year in Brazil, with the implementation of efficient measures for greater investment in this area, through regulations and tax benefits for companies.

As an example, there are so-called "green bonds", whose focus is on sustainable projects that are beneficial to the climate and the environment. A green bond can be issued by any company, if it is able to demonstrate the destination of the resources and the positive impact on the environment.

In 2016, Brazil started showing its concern with "green investments" by issuing the Decree 8.874/2016, which seeks to provide incentives to finance projects with environmental or social benefits, thereby boosting the issuance of green bonds in the country.

As for tax incentives, since 2020, with the regulation of Law 12.431, there is the possibility of a tax exemption for investment in infrastructure debentures related to projects that provide relevant environmental or social benefits.

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

According to research by Morningstar and Capital Reset, in Brazil, ESG funds raised BRL 2.5 billion in 2020 – and more than half of this came from funds created in the previous 12 months.

The Brazilian Federation of Banks – Febraban – has indicated that more than 15 Brazilian banks have already adhered to the UN Net Zero Banking Alliance initiative, which envisions being carbon neutral by 2050.

Furthermore, almost all major Brazilian banks have adhered to the Equator Principles, including Banco do Brasil, Banco de Desenvolvimento Econômico Social, Banco Bradesco, Caixa Econômica, Bradesco and Votorantim, Itaú and BTG Pactual.

Only Bradesco, Itaú and Santander are part of the pilot project of the UNEP Initiative.

### 5.3 Promoting ESG by the central bank and regulators

The Central Bank of Brazil became a member of the Network for Greening the Financial System in March 2020.

The Central Bank's participation in the Network for Greening the Financial System is important because of the national and international influence, as well as the attention that the Central Bank provides to issues that affect the environment, governance and social practices – items that encompass the ESG concept.

On 1 July 2022, the Brazilian Monetary Council's Resolution 4,945/2021 became effective, which provides for the creation of the Social, Environmental and Climatic Responsibility Policy (PRSAC) and its effectiveness. This Resolution determines that financial institutions and other institutions authorised to operate by the Brazilian Central Bank must establish and implement policies with principles and guidelines of a social, environmental and climate nature in the conduct of their business and activities.

The PRSAC redefines the concepts of social risk and environmental risk, the former being related to practices of violation of fundamental rights or collective interests, while the latter is associated with acts of environmental degradation. Also, in relation to climate risks, differentiations were introduced between the transition climate risk, related to the transition process of a low carbon economy, and the physical climate risk, related to the occurrence of extreme environmental conditions.

Other rules and resolutions from the Brazilian Central Bank and the Brazilian Monetary Council were issued in 2021 to regulate ESG risks as follows:

- BCB Normative Instruction n° 153/2021 – establishes the standardised tables for the purpose of disclosure of the Report on Social, Environmental and Climatic Risks and Opportunities (GRSAC Report);

- BCB Resolution No. 140/2021 – provides for the creation of section 9 (Social, Environmental and Climatic Impediments) in Chapter 2 (Basic Conditions) of the Rural Credit Manual (MCR);

- Resolution BCB n° 139/2021 – provides for the disclosure of the GRSAC Report by the institutions authorised to operate by the Brazilian Central Bank that fit into segments 1, 2, 3 and 4. The report must cover the governance of risk management, the actual and potential impacts of risks on the strategies adopted by the institution in business and risk and capital management and the environmental, social and corporate governance risk management processes;

- CMN Resolution No. 4,944/2021 – amends Resolution No. 4,606/2017, which provides for the simplified optional methodology for calculation of the minimum Simplified Reference Equity requirement (PRS5), the requirements for opting for this methodology and the additional requirements for the simplified continuous risk management structure. This is a rule intended for institutions classified in segment 5, being less demanding and with a longer period for entry into force.

  This Resolution deals with:

  - criteria to identify risks as significant sources of risk (including, social and environmental risks);

  - mechanisms to identify and monitor the risks incurred by the institution as a result of its own processes or those of counterparties;

  - identification, evaluation, classification and measurement of risks; and

  - procedures for the adequacy of management to political, legal, regulatory, technological or market changes that may impact the institution in a relevant manner; and

- CMN Resolution No. 4,943/2021 – amends Resolution No. 4,557/2017, which provides for the risk management structure, the capital management structure and the disclosure policy and is intended for financial institutions authorised to operate by the BCB that fit into segments 1, 2, 3 or 4. Among the changes are the requirement for the identification, evaluation, measurement and monitoring of risks, as well as the establishment of mechanisms for identifying and monitoring risks and the establishment of a management structure and minimum prudential requirements to be observed for each type of risk. Now, environmental and social risks will be treated separately, and the observance of climate risks has been included, all of them exemplified in an express, but not exhaustive, list.

Under this regulatory framework, it has been determined that financial institutions must implement corporate governance practices with the objective of managing socio-environmental risks linked to their businesses, services, and products.

Finally, each year the Central Bank sets measurable goals for the inclusion of a more responsible culture that is more attentive to ESG issues.

The Brazilian Securities Commission (CVM) has also taken steps to implement ESG measures for public companies. Signed in November 2021 and scheduled to come into effect on 2 January 2023, CVM Resolution 59/21 aims to expand the disclosure requirements on ESG aspects of businesses.

Among the main changes in Resolution 59/21 is the requirement to maintain basic information, periodically, on the company's official website for a period of three years.

The resolution also provides that the information on the Brazilian Code of Corporate Governance must be delivered, which will now apply to those who:

- are registered in category A;
- have securities admitted to trading on the stock exchange; and
- have shares or share certificates in circulation.

This is, therefore, yet another demonstration of the importance that environmental, social and governance issues have for corporations today, and that the trend is that these requirements will be increasingly demanded of all companies.

# BRITISH VIRGIN ISLANDS

# 1. General overview of the restructuring regime

## 1.1 Formal restructuring procedures

The BVI Business Companies Act 2004 (BVI BCA) provides the statutory framework for a BVI company to undertake a restructuring. The BVI BCA allows a BVI company to approve a plan of arrangement to restructure the company's affairs or enter into a compromise or arrangement with any class of its creditors or any class of its members. There are no statutory restrictions on the types of debts, liabilities or claims against the company that can be restructured under the BVI BCA.

### *1.1.1 Plan of arrangement*

Under section 177 of the BVI BCA, the board of directors of a BVI company is permitted to approve a plan of arrangement to restructure the company's affairs, which might involve:

- a reorganisation or reconstruction of a company;
- a merger or consolidation of one or more companies with one or more other companies, if the surviving company or the consolidated company is a company incorporated under the BCA;
- a separation of two or more businesses carried on by a company;
- any sale, transfer, exchange or other disposition of any part of the assets or business of a company to any person in exchange for shares, debt obligations or other securities of that other person, or money or other assets, or a combination thereof;
- any sale, transfer, exchange or other disposition of shares, debt obligations or other securities in a company held by the holders thereof for shares, debt obligations or other securities in the company or money or other property, or a combination thereof;
- a dissolution of a company; or
- any combination of any of the above.

Once directors have resolved to approve a plan of arrangement, they must then make an application to the BVI court for approval of the proposed arrangement. At the hearing (which is normally referred to as the first hearing), the court has the power to:

- determine what notice, if any, of the proposed arrangement is to be given to any person;
- determine whether approval of the proposed arrangement by any person should be obtained and the manner of obtaining the approval;
- determine whether any holder of shares, debt obligations or other securities in the company may dissent from the proposed arrangement and receive payment of the fair value of their shares, debt obligations or other securities;
- conduct a hearing and permit any interested person to appear; and
- approve or reject the plan of arrangement as proposed or with such amendments as it may direct.

Once the court has approved the plan of arrangement, the directors may, if they still wish to proceed, confirm the plan as approved by the court and then give notice of the plan to each person who the court requires notice to be given, and obtain the consent of each person whose consent the court has indicated is required. Once all relevant consents and approvals are in place, the directors should prepare the articles of arrangement (which include the plan of arrangement and the relevant court order) and file them with the BVI Registrar of Companies. The Registrar will issue a certificate in approved form and the arrangement has effect from the date of registration (or on such later date, up to 30 days later, as may be specified in the articles).

In practice, the court will usually prescribe which persons must be given notice and which persons must give their consent at the first hearing and will then fix a subsequent hearing date (the second hearing) at which all of the relevant persons would normally be expected to attend and comment on the plan of arrangement. In the normal course of things, the court will usually require the widest possible notice of the proposed arrangement to be given and will expect any person who might dissent or be adversely affected to be given the fullest opportunity to make their objections known. The plan is fully approved at the second hearing after the court is satisfied that all of the relevant parties have either received the necessary notice or given consent.

Many of the plans of arrangement in the BVI are entirely consensual and the relevant parties have all agreed to the relevant plan in advance. Plans of arrangements are often used to take advantage of extreme flexibility of BVI company law to reorganise groups in a single stroke in a way which might be time consuming, expensive or otherwise undesirable if done in a series of individual steps. They simply provide an expedited system for taking a series of steps and can be used to sidestep "chicken-and-egg" problems which can bedevil complicated reorganisations.

Where plans of arrangement are contested, the court will be particularly mindful of the risk of imposing an arrangement that may unfairly prejudice the rights of a particular stakeholder. Inevitably, where there is disagreement, one party is going to be disappointed with the outcome, but the presupposition is that maintaining an uncomfortable status quo is preferable to stripping a party unwillingly of its rights. However, unlike a scheme of arrangement or a creditor's arrangement, there are no specific approval thresholds which must be met. The court will specify the approvals and the requisite majority required and will normally follow any requirements specified in the memorandum and articles of association of the company.

In the event there are dissenters, the BVI BCA[1] provides that on an application to approve a plan of arrangement, the court may determine whether any holder of shares, debt obligations or other securities in the company may dissent from the proposed arrangement and receive payment of the fair value of the relevant shares, debt obligations or other securities held. The court may also permit any interested person to appear at a court hearing. If the court makes such a determination, its order should structure the method by which dissenters raise their objections and be bought out at fair value. The BVI BCA[2] entitles members of a company who dissent to a plan of arrangement to receive payment of the fair value of their shares and gives the process for the member to exercise this right to payment. Section 179 of the BVI BCA outlines the process for a shareholder to dissent but the section does not refer to holders of shares, debts or other securities. The expectation would be that the valuation mechanisms given in section 179(9) of the BVI BCA would apply to both shareholders as well as the holders of debt and other securities.

### *1.1.2 Scheme of arrangement*

A compromise or scheme of arrangement commences when the company devises, and the company's creditors agree, to a proposal by the company. A proposal must include an explanatory statement, a restructuring framework agreement, a term sheet and a practice statement letter.

When the company and its stakeholders have reached a compromise, the formal process commences with an application to the court for directions on the convening of a meeting of scheme creditors as the parties to the compromise or scheme. The BVI BCA allows a range of persons to make the application – the company, a member of the company or an administrator, voluntary liquidator or liquidator (as applicable).

Administration and insolvency are governed by the Insolvency Act 2004 (Insolvency Act). However, the statutory provisions relating to administration are not in force in the BVI.

[1] BVI BCA, ss 177(4)(c), 177(4)(d).
[2] *Idem*, s 179.

The existing management of a company remains in control of the company during its restructuring under a scheme.

A court-sanctioned scheme of arrangement follows the following process:

- the company makes an application to the court by way of a claim form, usually *ex parte*, seeking leave to convene a meeting of creditors. The application usually gives details of the location and time for a scheme meeting, the name of the proposed person to act as chairperson for the scheme meeting and if necessary, the appointment of a foreign representative. The application usually requests a hearing date for the court to sanction the scheme subject to approval by creditors. The company's supporting affidavit will exhibit for the court the company's scheme supporting documents such as the restructuring support agreement and practice statement letter;

- the BVI BCA requires the approval of 75% in value of the creditors or class of creditors or members or class of members present in person or by proxy of any compromise, if sanctioned by the court. Any application to the court to convene a scheme meeting must confirm to the court that the statutory quorum is attained. At the sanction hearing, therefore, the court is not considering the merits or fairness of the scheme.[3] To determine whether to grant leave to convene a scheme meeting, the court considers:

  - whether it has jurisdiction to make the order for the company to convene a meeting of creditors under the relevant BVI BCA provision;

  - whether the scheme has a reasonable prospect of success;

  - the classes of creditors proposed by the scheme;

  - the notice, timing and conduct of the scheme meeting; and

  - the documentation to be approved at the scheme meeting;

- following a scheme meeting, the company is required to obtain the court's sanction of the scheme. The company must therefore file further supporting evidence of the steps taken to advertise the scheme meeting and report on the outcome of the scheme meeting. The evidence should specify the documents supplied by the company to creditors, confirm whether the requisite majority of creditors approved the scheme and enclose the chairperson's report of the scheme meeting. At the hearing to sanction the scheme, the court seeks to be satisfied that:

  - the statute was complied with;

  - the class of creditors affected were fairly represented by those who attended the scheme meeting so that the statutory majority are acting bona fide and not coercing the minority in order to promote interests adverse to the class they purport to represent; and

  - the scheme as approved is one that an intelligent and honest person, as a member of the affected class acting in the person's best interests, might reasonably approve.[4] A scheme sanctioned by the court is binding on all creditors or class of creditors or members or class of members and on every person liable to contribute to the company's assets in the event of its liquidation.

There is no provision for dissenters' rights. There is also no requirement for any form of official supervision of the scheme of arrangement (beyond the requirement of court sanction).

A court order sanctioning a successful scheme has no effect until the company files a copy of the court's order with the Registrar of the BVI Registry of Corporate Affairs.

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3 BVIHC(COM) 2022/0008 *In the Matter of Rongxingda Development (BVI) Ltd*, Judgment 1, 13 April 2022.

4 *Ibid*.

#### *1.1.3 Soft touch liquidation*

The traditional appointment of a provisional liquidator under the Insolvency Act occurs where an application to appoint a liquidator is pending determination and it is necessary to make the appointment. The court needs to be satisfied the appointment is necessary for the purpose of maintaining the value of the assets owned or managed by the company or it is in the public interest. The provisional liquidator has all the rights and powers of a liquidator as is necessary to preserve the company's assets.

Significantly, however, the BVI court for the very first time in the *Constellation* matter in February 2019 appointed provisional liquidators in aid of restructuring over six BVI companies[5] and stayed proceedings against the companies. As explained in *Constellation*, the essence of a "soft touch" provisional liquidation is that a company remains under the day-to-day control of the directors but is protected against actions by individual creditors. The purpose is to give the company and its group the opportunity to restructure its debts, or otherwise achieve a better outcome for creditors than would be achieved by liquidation. The court described this option as potentially appropriate where there is no alleged wrongdoing of the directors. The application was described as a protective measure serving the primary purpose of warding off predatory creditors who could commence satellite *ex parte* actions against the BVI subsidiaries in an attempt to gain an advantage over creditors generally.

In *Constellation*, the holding company was insolvent being unable to pay its debts as they fell due. Therefore, the holding company, along with its subsidiary companies, embarked on a major cross-border restructuring involving a Brazilian judicial reorganisation and a United States Chapter 15 recognition application. The group had a complex, integrated, multi-national corporate structure and debt structure, thereby requiring relief from the BVI and United States courts. The company applied to the BVI court to support and facilitate the restructuring through the Brazilian process, already supported by the Chapter 15 proceedings. The company's largest unsecured creditor, being owed US $1 billion out of a US $1.5 billion debt, also supported the company's application for the appointment of provisional liquidators. The decision made it clear that the application did not seek the recognition of an international insolvency or foreign representative under the Insolvency Act. Therefore, the principles of modified universalism as discussed in *Rubin v Eurofinance*[6] and *Cambridge Gas*[7] did not arise. Likewise, the issue of legislation impliedly excluding the use of common law powers as arose in *Singularis*[8] did not apply.

The *Constellation* decision has established that when seeking the appointment of soft touch liquidators, the court need not be satisfied that a restructuring will occur. From the English authorities followed by the court, the only requirement is to show "some prospect" of promoting a restructuring. Historically, a distinction has been drawn between applications for provisional liquidator appointments made by the company as opposed to its creditors. If the company itself makes the application or consents to it, "the appointment is almost a matter of course."[9]

### 1.2 Informal restructuring procedures

There are two main informal restructuring options available in the BVI, both prescribed by the Insolvency Act: the out of court appointment of a liquidator by a members' qualifying resolution and a creditors' arrangement (an agreement between the company and its creditors to restructure the company's debt).

5 BVIHCM 2018/0206, 0207, 0208, 0210, 0212 *In the Matter of Constellation Overseas Ltd and five others*, Adderley, J, 5 February 2019.

6 [2013] 1 AC 236.

7 *Cambridge Gas Transportation Corporation v Official Committee of Unsecured Creditors of Navigation Holdings Plc* [2006] UKPC 26.

8 *Singularis Holdings Ltd v Pricewaterhouse Coopers* [2014] UKPC 36.

9 *Palmer's Company Law*, referred to in *Re Union Accident Insurance Co Ltd* [1972] All ER 1105.

### *1.2.1 Member appointed liquidator*

The Insolvency Act allows members of a company to pass a qualifying resolution to appoint an eligible insolvency practitioner as a liquidator of the company. The court's approval is not necessary for a member appointed liquidation to be valid. The resolution appointing the liquidator marks the date of the commencement of liquidation of the company. A qualifying resolution is defined in section 159 of the Insolvency Act as one that is passed at a properly constituted meeting of the company by a majority of 75%, or any higher majority that the company's memorandum or articles of association requires, who are present at a meeting and entitled to vote on the resolution. The proposed liquidator must provide his / her consent to act. The Insolvency Act bars members of a foreign company from passing a resolution to appoint a liquidator. Similarly, members of a regulated company must first give five days' written notice to the Financial Services Commission of a resolution to appoint a liquidator. Members of a company cannot appoint a liquidator if there is a pending application to the court for a liquidator to be appointed, or a liquidator has been appointed by the court or the proposed liquidator has not consented to being appointed.

The liquidator on appointment has restricted functions until 14 days has elapsed, at which time the liquidator is required to convene a meeting of the company's creditors. The liquidator's restricted activities include:

- taking the company's assets into his / her custody and control;
- disposing of perishable goods and other assets that will diminish in value if they are not disposed of immediately; and
- doing everything necessary to protect the company's assets. If the liquidator desires to engage wider powers given to a liquidator prior to the meeting of creditors, he / she must obtain the court's sanction. The objective of the creditors' meeting is to allow the liquidator to give an account of the steps he / she has taken, to appoint a creditors' committee and, if the creditors determine, to replace the member appointed liquidator. If the parties dispute the replacement of the liquidator, they have liberty to apply to the court to resolve the appointment.

### *1.2.2 Creditors' arrangement*

Section 14 of the Insolvency Act allows a company to enter into a compromise with its creditors. The compromise is then implemented with the supervision of an insolvency practitioner appointed as a trustee or otherwise. The arrangement may cancel or vary all or any part of a liability of the debtor, vary the rights of the debtor's creditors or the terms of a debt and include any other provision that may be prescribed. The arrangement cannot affect the rights of the company's secured creditors to enforce their security interest or vary the liability secured by the security interest or result in a preferential creditor receiving less than it would receive in a liquidation if liquidation were commenced at the time of the arrangement. Sureties or co-debtors of a company remain liable to the company unless the terms of the arrangement expressly provide otherwise. Regulated companies entering into a creditor's arrangement are required to give notice to the BVI Financial Services Commission.

For a creditors' arrangement, the board of the company remains in place. The Insolvency Act provides that if the company is not in liquidation or administration, the company's board may propose an arrangement and nominate an interim supervisor to act in relation to the proposed arrangement if it believes on reasonable grounds that the company is insolvent or is likely to become insolvent, and it has passed a resolution stating its belief that the company is insolvent or is likely to become insolvent.

The resolution should approve a written proposal containing the information prescribed and nominate an eligible insolvency practitioner to act as interim supervisor. It becomes an offence if a director signs such a resolution without having reasonable grounds for believing the company is insolvent or likely to become insolvent. The company passing such a resolution is then required to provide the nominated insolvency practitioner with a copy of the resolution passed, a copy of the board-approved proposal, the company's statement of affairs no older than two weeks before the date of the appointing resolution and a notice of intention to appoint the nominated insolvency practitioner as interim supervisor.

The proposed insolvency practitioner is required, if he / she accepts the appointment, to deliver notice to the company's board within five days from the date of the resolution. The interim supervisor's appointment takes effect from the date the endorsed notice is delivered to the board. Any appointment of an interim supervisor by a company in liquidation has to occur via the liquidator. The interim supervisor's appointment takes effect when he / she returns the endorsed notice to the liquidator. Where a liquidator intends to make a proposal, he / she may act as the interim supervisor himself / herself or can appoint someone else. There are no restrictions on the types of debts, liabilities or claims that parties can agree to restructure in the BVI.

If a company is a regulated entity, it will be subject to the restriction in the Insolvency Act that it must first notify the Financial Services Commission of an intention to restructure and / or the terms of the restructuring. Similarly, the liquidation of a foreign company that is deemed to be connected to the British Virgin Islands will require the court's involvement. A foreign company is a body corporate incorporated, registered or formed outside the British Virgin Islands. Under the Insolvency Act, a foreign company is deemed to have a connection with the British Virgin Islands if it has assets, or appears to have assets, in the Virgin Islands, it is carrying on or has carried on business in the Virgin Islands, or there is reasonable prospect that the appointment of a liquidator of the company will benefit the creditors of the company. Where an arrangement is approved, the company is to take steps to put the appointed supervisor into possession of the company's assets.

## 2. Restructuring of ESG-related liabilities

### 2.1 Environmental (E): restructuring environmental liabilities

The liability for environmental obligations is not contained in one statute in the BVI but is imposed by multiple statutes. The Ministry of Natural Health & Resources has confirmed that it now has a draft of a comprehensive environmental law to be presented to the House of Assembly shortly. The obligations imposed under BVI law include the following:

- the Ports Authority Act;
- the Radioactive Minerals Ordinance, Cap 152;
- the Prevention of Oil Pollution Act 1971 (Overseas Territories) Order 1982;
- the Merchant Shipping (Prevention of Oil Pollution) Order 1983;
- the Merchant Shipping Act 2001;
- the BVI Electricity Corporation Ordinance with the BVI Electricity Corporation (Renewable Energy) Regulations 2018;
- the United Kingdom Food and Environment Protection Act (1985);[10]
- the Food Security and Sustainability Act; and
- the Environmental Protection and Tourism Improvement Fund Act 2017 (the Environmental Protection Fund Act).

#### *2.1.1 Types of environmental liabilities*

The Ports Authority Act imposes liability on the owner or master of a vessel which causes any damage, pollution or injury to the marine environment, or the marine life of the BVI. The sums payable for any damage caused will be recoverable in civil proceedings as a debt to the Port

[10] Extended to the BVI by section 26 of the Environment Protection (Overseas Territories) Order 1988 No 1084.

Authority or the Crown. Vessels involved in pollution or damage may be seized and detained until the estimated cost of repairing the damage or clearing the pollution has been fully paid or the Crown or a security has been given to the Port Authority.

The Radioactive Minerals Ordinance prohibits mining within the BVI for radioactive minerals without a licence. Liability for offences under the Act, upon summary conviction or on conviction on indictment, consists of imprisonment with hard labour for 12 months or a fine of US $25,000 or both.

The United Kingdom Food and Environmental Protection Act 1985 imposes the requirement to obtain a licence for the deposit of substances and articles into the sea or incineration at sea. It is an offence to do anything requiring a licence without a licence and a person shall be liable on summary conviction to a fine not exceeding £50,000. On conviction on indictment, a person is liable to a fine or to imprisonment for a term of not more than two years or to both.

The Prevention of Oil Pollution Act 1971 (Overseas Territories) Order[11] enables taking measures to prevent, mitigate or eliminate grave and imminent danger to the coastline or related interests from pollution or threat of pollution of the sea by oil, following a maritime casualty. Such measures may include those permitted under the International Convention Relating to Intervention on the High Seas in Cases of Oil Pollution Casualties, opened for signature in Brussels on 29 November 1969.

The BVI Electricity Corporation (Renewable Energy) Regulations 2018 govern the process for the creation and use of renewable energy generation systems. The Regulations stipulate that persons setting up renewable energy systems must obtain the relevant authorisation, grant or permit called a "green energy licence". Failure to obtain a permit is an offence liable on summary conviction to a fine not exceeding US $5,000 or an imprisonment term not exceeding three months or both. For each day the offence continues, the fine is US $500 per day. For a corporate entity, the fine is US $10,000 on summary conviction. For each day the offence continues, the fine is US $1,000 per day.

The Environmental Protection Fund Act regulates the collection of funding to be used for the protection and improvement of the environment, the tourism product and for incidental matters. It imposes a US $10 charge to non-residents arriving by sea or air collected by Financial Secretary to be paid to the Environmental Protection and Tourism Improvement Fund.

#### *2.1.2 Priority given to environmental liabilities*

There are no priorities given to environmental liabilities under the insolvency laws of the BVI.

#### *2.1.3 Disclaimer of environmental obligations*

Section 217 of the Insolvency Act defines onerous property as an unprofitable contract or assets of the company which are unsaleable or not readily saleable, or which may give rise to a liability to pay money or perform an onerous act. The liquidator of a company may file a notice of disclaimer with the court, thereby disclaiming onerous property of the company even though the liquidator has taken possession of it, has tried to sell or assign it or otherwise exercises rights of ownership in relation to the property.

In the absence of any special provisions governing the disclaiming of environmental obligations, section 217 of the Insolvency Act applies.

### 2.2 Social (S): restructuring health or safety-related liabilities

In the absence of any statutory provisions to the contrary, health and safety related liabilities are restructured in the same way as ordinary debt claims. There are no special restrictions or conditions applicable when restructuring such liabilities.

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[11] Extends to the BVI with the exceptions and modifications specified in Schedule 2.

#### *2.2.1 Types of health and safety-related liabilities*

Under the Public Health Act, the Minister for Health is responsible for promoting and preserving the health of the inhabitants of the BVI. Premises serving the public are liable to inspection by the Minister and his / her agents. If an owner receives a notice to carry out remedial works, if those works are not undertaken, the Minister may obtain an order for the premises to be closed. Similarly, where there is a communicable disease in the territory, the Minister may restrict the assembling of persons together. Any person who is present at, promotes or aids the promotion of a prohibited assembling may be convicted by summary process and liable to a fine of US $1,000 and to imprisonment for 12 months.

#### *2.2.2 Treatment of health and safety-related liabilities*

Health and safety-related liabilities do not have specific priority under the Insolvency Act.

Schedule 2 of the Insolvency Rules outlines the preferential claims and their maximum amounts that will be regarded as preferential. They include:

- sums due to a person as a present or past employee of the debtor that represent, *inter alia,* wages and salary due six months prior to the liquidation date or accrued holiday pay incurred before liquidation to the maximum of US $10,000;
- without limit, any sums payable to the BVI Social Security Board in respect of employee contributions deducted from the employee and in respect of an employer's contributions payable for the six months immediately before liquidation;
- sums due for pension contributions in respect of medical insurance payable within 12 months immediately before the liquidation of the debtor to the maximum of US $5,000 in respect of each employee;
- sums due to the BVI Government for any tax, duty, licence fee or permit to the maximum of US $50,000 and
- sums due to the BVI Financial Services Commission in respect of any fees or penalty to the maximum sum of US $20,000.

### 2.3 Governance (G): third party releases in favour of directors and officers of the company

The BVI BCA is silent on the power of the court to allow third parties to receive releases of liability under a restructuring plan whether or not it relates to liabilities of a director or officer in relation to potential claims against them personally.

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

The involvement of the court in approving a restructuring plan and the relevant considerations are outlined in section 1 above. The court is therefore not concerned with wider public interest considerations and there are no other regulatory bodies involved in the approval of a restructuring plan in the BVI.

#### *3.1.1 Approving a restructuring plan*

The relevant factors the court will consider when approving a plan of arrangement or a scheme of arrangement are considered in section 1 above and do not include the views of other regulatory bodies, including environmental protection authorities.

#### *3.1.2 Discretion to consider wider public interest concerns*

The court, being the only approving body for a plan or scheme of arrangement, is not concerned with wider public interest considerations.

#### *3.1.3 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

Environmental protection authorities and advocacy groups do not have standing to air their views or concerns in a restructuring. Most BVI companies that will be subject to restructurings or rescue procedures are generally holding or finance companies with operations elsewhere in the world. Environmental matters will therefore be subject to the legislation of the countries in which the operations are based.

### 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

In the BVI, there are no provisions giving labour authorities, unions or employee / worker advocacy groups standing to air their views in a restructuring.

The courts may consider employment issues in terms of any employees who meet the criteria for a preferential creditor as determined by the Insolvency Act in the event of liquidation proceedings.

#### *3.2.1 Approving a restructuring plan*

As noted, labour authorities play no role in the approval of a restructuring plan.

#### *3.2.2 Discretion to consider wider public interest concerns*

The BVI court, as the sole approving body for a restructuring plan, does not have discretion to consider the wider public interest concerns.

#### *3.2.3 Protection of employee rights*

Most BVI companies that are subject to restructuring or rescue procedures are holding or finance companies with operations elsewhere in the world. Most often, these companies will have no local BVI employees. Employment contracts and environmental matters will therefore be subject to those other countries' legislation where that company's operations are based.

### 3.3 Governance (G): board / management conflicts addressed in a restructuring

As a matter of general law, where a company becomes insolvent, the directors' duties switch from considering the best interests of the company's shareholders, to prioritising interests of the company's creditors. Directors are expected to exercise their powers in the best interests of the company's creditors until such times as solvency is restored, or the company goes into liquidation. The BVI court treats decisions of the English Supreme Court as highly persuasive. The BVI court is therefore likely to follow the principles of the court outlined in the recent Supreme Court decision in *BTI 2014 LLC v Sequana SA,*[12] and as articulated in *West Mercia Safetywear Ltd v Dodd.*[13]

The "interests of the company's creditors" means the interests of its creditors as a general body, not the interests of particular creditors.

The BVI BCA deals with the potential conflict that directors may encounter when performing their duties. A director of a BVI company is required, forthwith after becoming aware of the fact that he or she is interested in a transaction entered into or to be entered into by the company, to disclose his or her interest to the full board of the company and / or to the shareholders of the company. Directors are also subject to the common law duty to avoid actual or potential conflicts of interest.

12 [2022] UKSC 25.
13 [1988] BCLC 250.

Where a company, in formulating its restructuring plan, offers an instruction fee, this is usually offered to creditors. We have guidance from the BVI court that a payment of a 1.5% instruction fee to creditors committed to supporting a scheme would not create a separate class. Further English authority supports the position that a fee of up to 2.5% would not fracture a class of creditors.[14] There is no authority on payments to board members or management.

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

As previously highlighted, many BVI companies are by nature holding or finance companies with operations outside of the BVI. Nevertheless, there are no soft law instructions available to guide or influence a BVI company to take environmentally responsible actions or decisions in a restructuring context.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

The BVI has no soft law instruments that guide or influence a company to take actions or decisions that protect an employee's interests especially in a restructuring context.

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

Insolvency practitioners are governed by the Insolvency Code of Practice (issued under section 487 of the Insolvency Act). Chapter IV sets out the ethical principles that a licensee must comply with in conducting all insolvency work. The principles are integrity, objectivity, competence, due skill and courtesy. The Code notes that the greatest threat to an insolvency practitioner's objectivity is likely to be a conflict of interest. An insolvency practitioner must be aware of actual or potential conflicts of interest in the form of self-review threats and self-interest threats.

A self-review threat to objectivity may arise where an insolvency practitioner, or his or her firm, has or had a material professional relationship with the company or individual in relation to which or whom insolvency work is performed. The threat that lies behind a material professional relationship is that the licensee, who is the custodian of what are often competing interests in the prosecution of insolvency work, may improperly and inappropriately favour one or more of these interests. In that way, an insolvency practitioner's objectivity would be lost. Any such relationship would usually require the insolvency practitioner to decline insolvency work.

A self-interest threat is one that could affect the reasoning an insolvency practitioner applies because it is, or might be, affected by considerations that either favour or are prejudicial or disadvantageous to the insolvency practitioner.

In particular, the Code states that it is improper for an insolvency practitioner to be influenced by a significant financial or other benefit accruing, or which might accrue, or the avoidance of disadvantage, to himself or herself or to anyone with whom he or she is associated or connected.

The special nature of insolvency appointments makes it inappropriate to pay or offer any valuable consideration for the introduction of insolvency appointments. This does not, however, preclude an arrangement between an insolvency practitioner and a bona fide employee whereby the employee's remuneration is based in whole or in part on introductions obtained for the insolvency practitioner through the effort of the employee.

[14] *In Re RongXingDa Development (BVI) Ltd* (Judgment No 1) BVIH (COM) 8 of 2022 (13 April 2022).

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

There are no specific ESG-linked loans or bonds observed in the BVI. Nevertheless, the BVI Government and banks are alert to the need for green financing. The BVI Government promotes the adoption of measures and projects that are environmentally friendly. Local banks also state their own commitment to protect and preserve the BVI's natural resources and to sustainable development. There are, however, no such loans available as "green loans."

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

The BVI has seven entities that are licenced to provide banking services in the BVI. There are no legal requirements for financial institutions to sign onto commitments to achieve ESG targets in their lending and investment portfolios or to apply ESG risk management policies such as the United Nations Environment Programme Net-Zero Banking Alliance. Individual banks nevertheless adopt strategies as they consider appropriate. For example, one bank is included in the new sustainability indices launched by SIX Swiss Exchange – which are guided by the three internationally recognised standards comprising the UN Global Compact, the UN Guiding Principles for Business and Human Rights and the International Labour Organisation Labour Standards, together with the controversies identified by MSCI.[15] Another bank became an official signatory to the Global Principles for Responsible Banking in September 2020 and has aired its commitment to align with the Paris Agreement. This bank has pledged to lend, invest and arrange US $200 million by 2025 and has expressed its intention to achieve a net-zero greenhouse-gas emissions in its financing activities by 2050.[16]

### 5.3 Promoting ESG by the central bank and regulators

The BVI Financial Services Commission acts as the regulatory body for banks in the BVI. There are no known policies promulgated by the FSC to promote ESG in financing. Banks are therefore free to adopt the policies they deem appropriate for ESG funding.

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15 VP Bank (BVI) Limited, https://vg.vpbank.com/en/about-us/responsibility/group-sustainability.

16 The Republic Bank, https://www.republictt.com/republic-journal/sustainable-development-goals-our-commitment-you-environment-clean-energy.

# CANADA

## 1. General overview of the restructuring regime

### 1.1 Formal restructuring procedures

The Canadian Constitution divides the power to legislate between federal and provincial governments according to subject matter,[1] with bankruptcy and insolvency being matters within federal jurisdiction.[2] Most Canadian restructuring and insolvency proceedings are governed by two federal statutes: the Companies' Creditors Arrangement Act (CCAA)[3] and the Bankruptcy and Insolvency Act (BIA).[4] These statutes contain mechanisms for corporate reorganisation and liquidation proceedings and are applicable in all provinces. However, even in the context of proceedings under these federal statutes, the provinces retain jurisdiction over property and civil rights.[5] Thus, in the absence of a conflict with the CCAA or the BIA (as the case may be),[6] provincial legislation pertaining to property and civil rights continues to apply in insolvency / restructuring proceedings.[7]

At a high-level:

- restructuring under the BIA is available to most debtors and provides a structured set of rules and regulations;
- the CCAA provides greater flexibility in restructuring proceedings and applies to corporate debtors with total debts of over CAD $5 million. It is Canada's primary reorganisation statute for large companies; and
- both the BIA and the CCAA provide for:
  - a broad stay of creditors' rights and remedies;
  - the filing of a plan (or proposal) to compromise the debtor's debts;
  - the sale of some or all of the debtor's assets (either in conjunction with or instead of a plan or proposal);
  - meeting(s) of affected classes of creditors for voting on the debtor's plan or proposal;

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1 Territorial governments exercise province-like powers and responsibilities delegated from the federal government pursuant to devolution agreements between each respective territory and the federal government: see Government of Canada, "Federal, Provincial and Territorial Overview" online: <www.canada.ca/en/environment-climate-change/corporate/transparency/briefing-materials/corporate-book/federal-provincial-territorial-overview.html>. Accordingly, for the purpose of this chapter, references to "province" will include "territory".

2 Constitution Act 1867 (UK), 30 & 31 Vict, c 3 (UK), reprinted in RSC 1985, App II, No 5, s 91(21).

3 Companies' Creditors Arrangement Act, RSC, 1985, c C-36.

4 Bankruptcy and Insolvency Act, RSC 1985, c B-3 and, specifically, Part III (Proposals). Several other statutes govern specific situations, including: the Winding-Up and Restructuring Act, RSC, 1985, c W-11 (banks, trust companies, loan companies and insurance companies), sections 106-110 of the Canada Transportation Act, RSC 1996, c 10 (railway companies incorporated by a special act of the federal or provincial legislature), and the Farm Debt Mediation Act, SC 1997, c 21 (in certain situations involving farmers).

5 Constitution Act 1867, s 92(13).

6 Where federal and provincial legislation conflict, either by operational conflict (where it is impossible to comply with both statutes) or frustration of purpose (where the operation of the provincial statute would frustrate the legislative purpose behind the federal statute), the Canadian constitutional doctrine of federal paramountcy dictates that the provincial legislation is inoperative to the extent of the conflict: see, for example, *Rothmans, Benson & Hedges Inc v Saskatchewan*, 2005 SCC 13 at para 11; see also *Orphan Well Association v Grant Thornton Ltd*, 2019 SCC 5, discussed later in this chapter in relation to environmental liabilities, in which the Supreme Court of Canada addressed the relationship among provincial environmental orders and legislation and the federal BIA.

7 *Orphan Well Association v Grant Thornton Ltd*, 2019 SCC 5 at para 64; *Husky Oil Operations Ltd v Minister of National Revenue*, [1995] 3 SCR 453, 1995 CanLII 69 at para 87; *Sun Indalex Finance, LLC v United Steelworkers*, 2013 SCC 6 at paras 51, 52; *Crystalline Investments Ltd v Domgroup Ltd*, 2004 SCC 3 at para 43.

- court sanction of the plan or proposal; and
- the appointment of a court-appointed officer to monitor the proceedings and report to the court and creditors.

Restructuring proceedings under the BIA and the CCAA are court-supervised, and an important feature of Canada's insolvency regime is the role played by licensed insolvency trustees (LITs), who function as the "eyes and ears of the court."[8] LITs have different roles depending on the type of restructuring proceeding: as a "monitor" in a CCAA proceeding or as a "proposal trustee" in a BIA proposal proceeding.[9] Although there may be nuances between the two roles, whether as monitor or proposal trustee, LITs are required to act neutrally and to assist the court's supervision of the restructuring process by providing periodic, objective reports to the court and stakeholders with information that may otherwise be unavailable to the competing interested parties.[10]

### *1.1.1 Application*

Debtors must meet certain threshold requirements before they can access either restructuring regime. In this respect, the BIA's proposal provisions only apply to a:

- "bankrupt";
- "insolvent person"; or
- receiver, liquidator or trustee on behalf of a bankrupt or an insolvent person.

The terms "bankrupt" and "insolvent person" are defined in the BIA as follows:

- "bankrupt" is an individual or company "who has made an assignment or against whom a bankruptcy order has been made".[11] It is a legal status; and
- "insolvent person" is an individual or company "who is not bankrupt and who resides, carries on business or has property in Canada, whose liabilities to creditors provable as claims under [the BIA] amount to one thousand dollars" and who meets one or more of the following three tests:[12]
  - they are unable to "meet [their] obligations generally as they become due";
  - they have ceased paying their "obligations in the ordinary course of business"; or
  - if their total assets, at "a fair valuation", or "disposed of at a fairly conducted sale under legal process", would "not be sufficient to enable payment of all obligations, due and accruing due".[13]

The first two tests are each known as the "cash flow test" and the third test is known as "the balance sheet test".

8 See, for example, *Walter Energy Canada Holdings, Inc (Re)*, 2017 BCSC 53 at para 26.

9 In these roles, the LIT acts as a court officer with statutory and other duties as set out by the court. LITs also act as bankruptcy trustees in bankruptcy proceedings and as receivers in receivership proceedings, which are sometimes commenced in respect of insolvent persons or bankrupts under s 243 of the BIA.

10 *Walter Energy* at para 26; *Mutual Trust Co v Scott, Pichelli & Graci Ltd* (1999), 11 CBR (4th) 62 at para 5 (Ont Gen Div); BIA, ss 50(10), 59(1); CCAA, s 23(1).

11 BIA, s 2(1), "bankrupt".

12 The use of the disjunctive "or" in the paragraph that follows indicates that only one of the criteria is necessary to meet the definition: John Honsberger and Vern DaRe, *Honsberger's Bankruptcy in Canada* (Thomson Reuters, 5th ed, 2017) at 6; *Royal Bank of Canada v Eastern Infrastructure Inc*, 2019 NSSC 243 at para 45; *Stelco Inc, Re* (2004), 48 CBR (4th) 299, 2004 CanLII 24933 at para 28 (ONSC).

13 BIA, s 2(1). The courts have interpreted "due and accruing due" restrictively, in that obligations are excluded which are not yet due or are not chargeable to the accounting period in which the test is applied.

The CCAA has a different set of threshold requirements, applying to a "debtor company" or a group of "affiliated debtor companies" whose total claims against them exceed CAD $5 million.[14] The term "debtor company" is defined in the CCAA as a company that:

- is bankrupt or insolvent;
- has committed an act of bankruptcy under the BIA or is deemed insolvent under the Winding up and Restructuring Act (WURA);
- has made an authorised assignment into bankruptcy or a bankruptcy order has been made against it under the BIA; or
- is in the course of being wound up under the WURA.[15]

The CCAA does not define "insolvent" or "insolvency". As a result, Canadian jurisprudence has adopted the definition of an "insolvent person" under the BIA, but with one modification: it has expanded the first test described above such that "a financially troubled corporation is insolvent if it is reasonably expected to run out of liquidity within reasonable proximity of time as compared with the time reasonably required to implement a restructuring".[16]

Finally, the CCAA only applies to bankrupt or insolvent companies that are either incorporated under the laws of Canada or a province, have assets in Canada, or do business in Canada.[17]

### *1.1.2 Reorganisation*

The CCAA and the BIA restructuring regimes contain similar provisions. For example, each statute generally provides for:

- the approval of debtor in possession financing (commonly referred to as DIP financing);
- the granting of certain priority charges to secure, among other things, administration costs, DIP financing and certain directors' liabilities;
- the disclaimer or repudiation of agreements;
- prohibitions on the sale of assets outside the ordinary course of business without court approval;
- the postponement of equity claims;
- the preservation of intellectual property licenses; and
- voting thresholds for the approval of any plan or proposal put to creditors.[18]

In addition, the BIA and the CCAA contain provisions which permit certain claims against directors to be stayed during restructuring proceedings as well as compromised in a proposal or plan.[19]

While there is significant overlap between the two regimes, there are also significant differences. For instance, the BIA proposal provisions are generally seen as more prescriptive, which in turn may result in reduced flexibility in the workout process with creditors.[20] The CCAA, by contrast, is a

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14 CCAA, s 3(1).
15 *Idem*, s 2(1), "debtor company".
16 *Stelco ONSC* at para 26.
17 CCAA, ss 2, 3.
18 See, for example, BIA, ss 50.6, 54, 65.11, 65.13 65.2, 104.1; CCAA, ss 6, 11.2, 32, 36.
19 In addition, as discussed later in this chapter, in order to encourage directors to remain in a restructuring proceeding, both statutes provide the court with the ability to order that the debtor company indemnify the directors for certain obligations which they may incur following initiation of the proceedings and grant a charge over the debtor company's assets as security for such indemnity in priority to other creditors.
20 Sarra, *Rescue!* at 44; *Century Services Inc v Canada (Attorney General)*, 2010 SCC 60 at para 15.

flexible statute that is skeletal in nature,[21] resulting in a more court-driven process, which may increase the cost of the process.[22]

That said, as the BIA and the CCAA are both federal legislation dealing with substantively similar subject matter (i.e. insolvency), Canadian courts have held that they are to be interpreted, "to the greatest extent possible",[23] in a harmonious manner to prevent "statute shopping".[24]

*CCAA reorganisation*

A CCAA proceeding must be commenced by way of an initial application to the court in the province where the debtor company's head office or principal place of business is located or, if the company has no place of business in Canada, in any province within which any of the company's assets are situated.[25] The initial application typically is made by the debtor company, but the legislation permits an application to be made by any person interested in the matter,[26] including a creditor,[27] in what are sometimes referred to as "creditor-driven CCAAs".[28] The initial application must be accompanied by substantial evidence to support the relief sought, including evidence to satisfy the threshold requirements (discussed above), as well as information regarding the assets and liabilities of the debtor company and the cause(s) of the company's financial difficulties.[29]

If satisfied the requirements under the CCAA have been met, the court will pronounce an initial order. Typically, these initial orders contain provisions:

- declaring that a corporation is entitled to protection under the CCAA;
- appointing a monitor to supervise the restructuring of the debtor company;
- granting an initial stay of proceedings against the company, for a maximum period of 10 days;[30] and
- granting certain priority charges in favour of administrative professionals, interim lenders and directors and officers (among others).

On the initial application, the court may only grant relief that is reasonably necessary for the continued operations of the debtor company in the ordinary course during that initial period.

The debtor company will return to court before the expiry of the initial stay period (at what is referred to as the comeback hearing) to apply for an extension of the stay. While the initial stay period is limited by statute to 10 days, there is no limit on the duration of subsequent stay extensions, provided the court finds they are "necessary" in the circumstances.[31] Debtor companies

21 *Nortel Networks Corp, Re*, 2010 ONSC 1708 at para 67 (*Nortel 2010*); see also *Stelco Inc (Bankruptcy), Re* (2005) 75 OR (3d) 5, 2005 CanLII 8671 at para 36 (CA) (*Stelco ONCA*).

22 *Nortel 2010* at para 67; see also *Stelco ONCA* at para 36; Canada, Office of the Superintendent of Bankruptcy, Insolv Bull 98809435001, "Report on the Operation and Administration of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act" (Ottawa: Industry Canada, 2002).

23 *Kitchener Frame Limited (Re)*, 2012 ONSC 234, at para 47.

24 *Century Services Inc v Canada (Attorney General)* 2010 SCC 60, at para 47.

25 CCAA, s 9(1). This gives debtor companies some flexibility to select their preferred provincial jurisdiction. For example, in *1057863 BC Ltd (Re)* 2020 BCSC 1359, the debtor companies filed in British Columbia where their head office was located, despite the fact that the main asset and business in the restructuring proceedings was a pulp mill located in Nova Scotia.

26 CCAA, s 11.

27 *Idem*, s 11.

28 See, for example, Luc Morin and Arad Mojtahedi, "In Search of a Purpose: The Rise of Super Monitors & Creditor-Driven CCAAs" in Jill Corraini and the Honourable D Blair Nixon, *Annual Review of Insolvency Law 2019* (Thomson Reuters, 17th ed, 2020).

29 Specifically, the CCAA requires that a weekly cash flow projection be filed with the court along with all the financial statements (audited and unaudited) prepared in the last year, or if none were prepared in that time period, the most recent financial statements: CCAA, s 10(2).

30 CCAA, s 11.7(1).

31 *Idem*, s 11.02(2). However, despite this lack of time limit on further extensions, courts have made it clear that they expect an expeditious process: Sarra, *Rescue!* at 37.

will often use the comeback hearing as an opportunity to seek an amended and restated initial order (commonly referred to as an ARIO), which will contain additional substantive relief and extend the relief previously granted in the initial order to cover the extension of the stay period.

While the CCAA itself contains no detailed claims process, Canadian courts have recognised that to meet the fundamental objective of the statute (i.e. to facilitate compromises and arrangements between debtor companies and their creditors), "it is necessary to determine what are the true claims of the creditors as these might be compromised or arranged".[32] Accordingly, courts have exercised their broad jurisdiction under the CCAA to make such orders as are "appropriate", to grant orders establishing a process for calling for claims, adjudicating claims, and barring claims not filed before the specified claims deadline.[33] These orders are typically referred to as "claims process orders".

Following the completion of a claims process, the debtor company, with the assistance of the monitor, may put forward a plan of compromise or arrangement to the court.[34] Plans may involve creditors accepting various forms of compromise to the immediate payment of their claim, including a reduced payment, payment over time, a debt for equity conversion or some other form of compromise / compensation. A plan does not need to deal with all creditors and if a creditor is not dealt with in a plan, their claim is unaffected by it.

Before a plan can be put to creditors, the supervising CCAA court must first be satisfied that the proposed plan has a reasonable chance of success.[35] If it does not, courts will seek to avoid the unnecessary costs being expended in calling and conducting a vote by refusing to permit the plan to be filed.[36] A court order accepting a plan for filing typically establishes rules regarding the calling of a meeting for creditors to vote on the plan.

A plan may be put to one or more classes of creditors, both secured and unsecured.

Section 22 of the CCAA permits the debtor company to divide its creditors into classes and requires the debtor to apply for court approval of the classification before the meeting(s) of the creditors. Creditors "may be included in the same class if their interests or rights are sufficiently similar to give them a commonality of interest", and the CCAA sets out a list of factors the court will consider.[37]

Each class of creditors must vote separately on the plan. To be accepted by the creditors of a class (and for the plan to be binding on the creditors in a class), the plan must be approved by more than 50% of the creditors voting on the plan (in person or by proxy), who represent 2/3 in monetary value of the claims of those creditors voting.[38]

Following the approval of the plan by the creditors, the plan is then brought to the court for sanction. Before a supervising CCAA court will sanction a plan, it must be satisfied that:

- there has been strict compliance with the statutory requirements and adherence to previous orders of the court;

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32 *Bul River Mineral Corporation (Re)* 2014 BCSC 1732 at para 36. For a general review of the policy objectives of the CCAA, see Sarra, *Rescue!* at 13-17.

33 CCAA, s 11; see also *Bul River* at para 43.

34 There are certain required payments which must be provided for in the plan (i.e., certain wages, benefit payments and tax payments): CCAA, ss 6(3)-6(6). Subject to certain statutory restrictions, the plan may contain any provision that a legal contract may contain. There is no requirement in the CCAA regarding who may develop the plan. However, in some cases the initial order will contain a provision that gives the debtor the exclusive right to prepare and file the plan.

35 See, for example, *Royal Bank v Fracmaster Ltd* 1999 ABCA 178 at para 13.

36 Sarra, *Rescue!* at 524-525; see also *Re Fracmaster Ltd* 1999 ABQB 379 (aff'd 1999 ABCA 178).

37 These factors are: "(a) the nature of the debts, liabilities or obligations giving rise to their claims; (b) the nature and rank of any security in respect of their claims; (c) the remedies available to the creditors in the absence of the compromise or arrangement being sanctioned, and the extent to which the creditors would recover their claims by exercising those remedies; and (d) any further criteria, consistent with those set out in paragraphs (a) to (c), that are prescribed": CCAA, s 22(2).

38 A creditor related to the debtor company may vote against, but not for, a plan.

- nothing has been done or purported to be done that is not authorised by the CCAA; and
- the plan is fair and reasonable.[39]

If the court approves the plan, it is binding on all members of those classes of creditors who voted in favour of the plan (even those creditors in each class who may have voted against the plan).[40]

*BIA reorganisation*

Unlike a proceeding under the CCAA, a BIA proposal proceeding is not initiated with a court application. Instead, these proceedings are typically commenced through the filing of a proposal or a notice of intention to make a proposal (NOI) by the proposed proposal trustee with the Office of the Superintendent of Bankruptcy. The filing of an NOI or proposal triggers an automatic stay of proceedings against the debtor corporation.[41] However, the stay does not apply to a secured creditor who, more than 10 days prior to the filing of the NOI or proposal, served the debtor company notice of its intention to enforce its security.[42]

Subject to the filing of certain documents (including a cash flow statement which must be filed within 10 days after the filing of the NOI), the BIA provides for an initial stay period of 30 days.[43] This stay may be extended by the court, on application of the debtor company, in increments of up to 45 days at time, to a maximum stay period of six months from the date of filing the proposal or the NOI.[44]

If the debtor company fails to file a proposal within the maximum six month period (or such shorter period if not all possible stay extensions are granted by the court), the company will automatically be deemed to have made an assignment in bankruptcy.[45] Similarly, if the debtor company fails to file certain prescribed documents (including the cash flow statement mentioned above), it is deemed to have made an assignment in bankruptcy.[46]

As with a CCAA plan, the BIA contains provisions mandating certain payments that must be included in a proposal.[47] In addition, a proposal must contain certain provisions, including that:

- it be made to the creditors generally, either as a mass or segregated into classes;[48]
- all funds payable under it must be paid to the proposal trustee to be distributed to the creditors;[49] and
- it must provide for the ratable payment of all claims, subject to certain provisions in the BIA.[50]

Other than the provisions prescribed in the BIA, there are few limits on the terms of a proposal.[51]

Once a proposal has been filed, the proposal trustee is required to send the proposal to all known creditors along with a report on the proposal and notice of the meeting of creditors at which a vote will be held on the proposal.[52]

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39 *Northland Properties Ltd, Re* (1989) 73 CBR 195 at paras 23-26; see also *Global Light Telecommunications Inc, Re* 2004 BCSC 745 at para 19.
40 BIA, s 54(2)(d).
41 *Idem*, s 69(1).
42 This is the formal notice (Notice of Intention to Enforce Security) required by s 244 of the BIA.
43 BIA, ss 50.4(1), 50.4(8).
44 *Idem*, s 50.4(9).
45 If no proposal has been filed, s 11.6 of the CCAA allows a BIA proposal proceeding to be continued under the CCAA if the debtor company has more than CAD $5 million in liabilities.
46 BIA, s 50.4(8).
47 *Idem*, s 60.
48 *Idem*, s 50(1.2).
49 *Idem,* s 60(2).
50 *Idem,* s 141.
51 *Honsberger's* at 183.
52 BIA, s 51(1).

Creditors vote on BIA proposals by class, according to the class of their respective claims. The BIA provides that all unsecured claims constitute one class (unless the proposal provides for more than one class of unsecured claims), and the classes of secured creditors (if any) are determined by considering factors set out in the BIA. These factors include:

- the nature of the debts giving rise to the claims;
- the nature and rank of the security in respect of the claims;
- the remedies available to the creditors in the absence of the proposal, and the extent to which the creditors would recover their claims by exercising those remedies;
- the treatment of the claims under the proposal, and the extent to which the claims would be paid under the proposal; and
- such further criteria, consistent with those set out above.[53]

To be approved by a class of creditors, the proposal must be approved by creditors holding a majority in number and more than 2/3 of the value of the claims voted in that class.[54]

As discussed above, once creditors have voted as a class to accept or reject a proposal, the court must then approve it. Once the proposal is approved by a class of creditors, it binds all parties in that class, regardless of whether a particular creditor in that class voted in favour of the proposal or not.[55]

If approved by the required majorities of voting creditors, a proposal must then be submitted to the court for approval.[56] In deciding whether to approve a particular plan, the court must consider:

- the interests of the debtor in making a settlement with its creditors;
- the interests of creditors in obtaining a settlement that is reasonable and does not prejudice their rights; and
- the interests of the public in a settlement that preserves the integrity of the bankruptcy process and complies with the requirements of commercial morality.[57]

The court typically will not approve a proposal where it is not satisfied that the terms of the proposal are reasonable or calculated to benefit the general body of creditors.[58]

If the proposal is not approved by both the creditors and the court, the debtor company is automatically deemed bankrupt.[59]

### *1.1.3 Reorganising pursuant to corporate statutes*

While a comprehensive review of restructurings under corporate legislation (at both the federal and provincial level) is beyond the scope of this chapter, we note that the arrangement provisions of the Canada Business Corporations Act (CBCA), as well as the equivalent provincial legislation, can be used in conjunction with the CCAA or the commercial proposal provisions of the BIA to reorganise the capital structure of a corporation.[60]

53 *Idem*, ss 50(1.4), 54(2).
54 Creditors who are related to the debtor corporation are only entitled to vote against, but not for, the proposal: BIA, s 54(3).
55 *Idem*, s 62(2).
56 *Idem*, s 58(a).
57 *Re Gardner* (1921) 21 CBR 424, 59 DLR 555.
58 BIA, s 59(2).
59 In contrast, under a CCAA proceeding there is no deemed bankruptcy.
60 See also the corporations statutes issued under provincial jurisdiction, including the Business Corporations Act, RSA 2000, c B-9, ss 192-193 (ABCA); *Business Corporations Act*, R.S.O. 1990, c B-16, ss 182, 186 (OBCA).

Section 192 of the CBCA (and similar provisions of provincial statutes)[61] has also been employed as a mechanism for corporate financial restructuring.[62] While there are certain advantages to proceeding under the CBCA (corporate reorganisation proceedings can be faster, less costly, and less dependent on court supervision than CCAA proceedings),[63] the CBCA is not an insolvency statute and therefore has certain limitations. These limitations include, among others, no express authority to:

- grant a stay of proceedings;
- authorise DIP financing; or
- grant priority charges in favour of administrative professionals.[64]

The CBCA also does not contemplate or otherwise provide for the appointment of a court officer to supervise the restructuring, and courts have held that the jurisdiction to grant releases to third parties is more limited than the jurisdiction available under the CCAA and the BIA.[65]

### *1.1.4 Cross-border restructurings and insolvencies*

Canada has incorporated a modified version of the United Nations Commission on International Trade Law (UNCITRAL) Model Law on Cross-Border Insolvency into both the CCAA and the BIA.[66] An authorised foreign representative in a foreign insolvency proceeding may thus bring an application to the Canadian court for recognition of the foreign proceeding. On such an application, the Canadian court must determine if the foreign proceeding is a foreign main proceeding or a foreign non-main proceeding.[67]

If the debtor company's centre of main interests (COMI) is located in the jurisdiction of the foreign proceeding, the proceeding will be referred to as a foreign main proceeding.[68] Both the CCAA and the BIA provide that for the purpose of the applicable recognition provisions of each Act, a debtor company's registered office is deemed to be its COMI in the absence of proof / evidence to the contrary.[69] The courts will consider the following factors to determine COMI:

- whether the location is readily ascertainable by creditors;
- whether the location is one which the debtor's principal assets or operations are found; and
- whether the location is where the management of the debtor takes place.[70]

Where courts are assessing the COMI of a Canadian entity operating as part of a larger corporate group, courts will consider additional factors, including:

- the location where corporate decisions are made;
- the location of employee administration, including human resource functions;

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[61] See, for example, OBCA, s 182; BCBCA, s 288.

[62] Martin McGregor and Paul Casey, "CBCA Section 192 Restructurings: A Streamlined Restructuring Tool or a Statutory Loophole?", online: <https://www.insolvency.ca/en/iicresources/resources/CBCA-Section-192_Canadas-Next-Insolvency-Regime_Myles-Davis.pdf> at 20; see also *Yellow Media Inc, Re* 2012 QCCS 4180.

[63] Roderick Wood, *Bankruptcy and Insolvency Law* (Irwin Law, 2nd ed, 2015) at 593.

[64] Mitch Grossell, "The Clash Between Corporate & Insolvency Law; CBCA Restructurings" online: <https://www.insolvency.ca/en/whatwedo/resources/TheClashBetweenCorporateLawandInsolvencyLawbyMitchGrossell.pdf>

[65] See, for example, *Re iAnthus Capital Holdings, Inc* 2020 BCSC 1442.

[66] BIA, Part XIII; CCAA, Part IV.

[67] CCAA, s 47; BIA, s 270.

[68] CCAA, s 45(1); BIA, s 268(1).

[69] CCAA, s 45(2); BIA, s 268(2).

[70] *Lightsquared LP, Re* 2012 ONSC 2994 at para 25.

- the location of the company's marketing and communication functions;
- whether the enterprise is managed on a consolidated basis;
- the extent of integration of an enterprise's international operations;
- the centre of an enterprise's corporate, banking, strategic and management functions;
- the existence of shared management within entities and in an organisation;
- the location where cash management and accounting functions are overseen;
- the location where pricing decisions and new business development initiatives are created; and
- the location of an enterprise's treasury management functions, including management of accounts receivable and accounts payable.[71]

The court may also consider the connection between the debtor and foreign jurisdiction to give effect to the legitimate expectations of a debtor’s constituents as to which laws will apply.[72]

As noted above, the BIA and the CCAA are, to the extent possible, to be interpreted harmoniously.[73] Thus, in recognition proceedings under the BIA, Canadian courts have considered and utilised the factors articulated in CCAA cases.[74]

Once a foreign proceeding is recognised as a foreign main proceeding, the Canadian court is required to grant a limited stay of proceedings in relation to the debtor company.[75] If the foreign proceeding is recognised as a foreign non-main proceeding, there is no automatic stay; rather, the relief granted is in the discretion of the Canadian court.[76]

The principle of comity requires that Canadian courts recognise and enforce judicial acts of foreign jurisdictions provided that the other foreign jurisdiction has assumed jurisdiction that is consistent with principles of order, predictability and fairness. Canadian courts have stressed the importance of comity and cooperation in cross-border insolvency proceedings to avoid multiple proceedings, inconsistent judgments and uncertainty.[77] However, where foreign judicial acts would be contrary to Canadian public policy, the CCAA and BIA do not limit Canadian courts’ discretion to refuse to recognise such foreign judicial acts.[78]

### 1.2 Informal restructuring procedures

In Canada, informal out of court restructurings are not governed by any legislation, but rather are conducted on a consensual basis.[79] Informal restructurings usually involve a combination of the following:

- making arrangements directly with vendors / suppliers / landlords;[80]

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71 *In the Matter of Voyager Digital Ltd* 2022 ONSC 4553 at para 21 [*Voyager*]; see *Hollander Sleep Products, LLC (Re)* 2019 ONSC 3238 at para 33 *[Hollander]*; *CHC Group Ltd (Re)* 2016 BCSC 2623 at para 11.

72 *Wolfridge Farm Ltd, Re* 2015 NSSC 168 at para 30.

73 *Century Services* at para 45.

74 *Wolfridge* at paras 30, 32.

75 CCAA, s 47(2); BIA, s 270(2).

76 Additionally, upon the recognition of a foreign proceeding, the CCAA and the BIA require the foreign representative to take on certain obligations, including the posting of notices related to the foreign proceeding. As well, although not required by the statute, it is typical that a court will require the appointment of an information officer to monitor and report to the court on the status of the proceedings.

77 CCAA, s 44; BIA, s 267; see also *Voyager* at para 9; *Hollander* at paras 41, 42.

78 CCAA, s 61(2); BIA, s 284(2).

79 These are sometimes referred to as “private workouts”.

80 For example, reducing payments or any associated interest rates or penalties, as well as payment plans.

- making changes internally to the business;[81]
- asset sales;[82] and / or
- securing additional financing or investment.

Two of the more common informal restructuring tools that debtors utilise as part of informal restructurings are forbearance agreements and bridge financing.

Forbearance agreements are agreements whereby a lender agrees to delay in (or forbear from) enforcing its security and other remedies for a period of time. These agreements can be mutually beneficial for both the debtor and the lender, as they can: (i) obviate the need for a debtor to commence formal restructuring proceedings; and (ii) provide the debtor "breathing space" to rehabilitate itself and take other informal restructuring steps, such as securing take-out or bridging financing. A well-drafted forbearance agreement can also be an opportunity for a lender to receive a fee or increased interest as consideration for the forbearance, correct any gaps or inconsistencies in its security, obtain an acknowledgement of the amount outstanding from the debtor, and set out terms for the enforcement of that security if the debtor cannot rehabilitate itself.

Meanwhile, bridge financing is a type of short-term financing utilised by debtor companies to take out an operating lender or replace their secured financing. This type of financing is generally short-term in nature and comes at a higher borrowing cost. In addition, bridge lenders typically require some form of security, which may be over unencumbered assets or in second priority to a current lender. By replacing or supplementing its existing secured debt with bridge financing, the debtor may "buy time" to find more suitable long-term and operating financing for its business.

## 2. Restructuring of ESG-related liabilities

While Canada currently has no restructuring specific ESG legislation or guidelines,[83] it appears to be a receptive framework for ESG considerations, given that:

- natural resources (mining, oil and gas, forestry) play a significant role in Canada's economy, and companies operating in these areas are regular participants in Canada's insolvency regime;
- ESG considerations and the public interest already play an informal role in the restructuring process.[84] In particular, when courts are asked to exercise their discretion, "the broader public interest" may be engaged "and may be a factor against which the decision of whether to allow a particular action will be weighed".[85] In deciding whether to approve plans of arrangement, for example, courts have considered the impacts that such plans will have on local communities, including their effect on jobs, the continuation of humanitarian work, and the supply of key

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81 For example, changes in management or downsizing, including reducing inventory, staff and other fixed costs.

82 Due to the time-sensitive nature of most restructuring situations, this often will be at discounted prices.

83 The Canadian Securities Administrators (CSA) mandate corporate governance related disclosure in Disclosure of Corporate Governance Practices, NI 58-101 (17 June 2005). The CSA provides further guidelines in Corporate Governance Guidelines, NP 58-201 (15 April 2005), which does not prescribe or restrict specific governance matters but does reflect best practices for governance. More specifically, in January 2022, CSA published guidance for investment funds on their disclosure of ESG practices. In Ontario, the Capital Markets Modernisation Task Force has recommended disclosure of material ESG information and specifically climate-change related disclosure. Likewise, as discussed in section 5.3 below, the Federal Government is seeking to mandate the adoption of the Task Force on Climate-Related Financial Disclosure standards for large corporations. These existing (and potential) ESG regulations expose non-compliant corporations to regulatory enforcement, including monetary sanctions.

84 The role of "social stakeholders" such as the government, environmental stakeholders, First Nations, and the local community in business restructuring proceedings have been recognised since the evolution of the modern CCAA, as has the role of the public interest.

85 *Century Services* at para 60.

community services.[86] Courts have considered similar factors in deciding whether to exercise their discretion to grant stays of proceedings.[87] That being said, ESG considerations are not definitive factors. They tend to be given less weight in the face of creditor opposition or in circumstances where they are not tied directly to the immediate demands of the debtor's restructuring;[88]

- Canadian corporate law provides that directors of a company may consider, when acting in the interests of the company, "the interests of shareholders, employees, suppliers, creditors, consumers, governments, and the environment";[89] and

- evidence suggests that there is a correlation between ESG performance and profitability.[90] Additionally, growing customer and investor advocacy on ESG issues may cause lenders and investors to tighten access to funds for companies that do not meet or exceed ESG requirements, while companies with higher levels of ESG performance may appeal to a broader spectrum of lenders and investors and be viewed as less of a credit risk.

Despite the above, there are some structural limits and practical hurdles that limit the role of ESG considerations in Canadian insolvency proceedings, including:

- the BIA and the CCAA are both commercial statutes. The primary purpose of both statutes is clear: to permit the debtor to continue to carry on business and, where possible, avoid the social and economic costs of liquidating its assets.[91] Therefore, unless addressing ESG issues will positively contribute to meeting that purpose, court officers and debtors may not be able to prioritise those matters;[92]

86 In *Re Canadian Red Cross Society / Société Canadienne de la Croix Rouge* (2000) 19 CBR (4th) 158, 99 ACWS (3d) 732 (ONSC) [*Canadian Red Cross*], for example, the court approved a plan of arrangement in CCAA proceedings because, among other things, the Red Cross employed approximately 7,000 Canadians in other aspects of its humanitarian work and "makes valuable contributions to society through these humanitarian efforts": para 28. Similarly, in *Re Canwest Global Communications Corp* 2010 ONSC 4209, the court approved a plan of arrangement for a television broadcasting company because, among other things, it would "ensure the continuation of employment for substantially all of the employees" and would "maintain for the general public broad access to and choice of news, public and other information and entertainment programming" which was "an important public service": para 26.

87 For example, in *Re JTI-Macdonald Corp* 2019 ONSC 1625, JTI-Macdonald, a tobacco company, argued that they required a stay of proceedings to stop the enforcement of a judgment to preserve, among other things, the jobs of 500 employees, the work of 1,300 suppliers, and approximately CAD $1.3 billion in continued payments in respect of federal and provincial taxes and duties. Considering this, the court granted the stay of proceedings as "[a]ny steps to enforce the judgment could cause serious harm to JTIM's business to the detriment of all of its stakeholders": paras 4, 13.

88 In *Re 1057863 BC Ltd* 2020 BCSC 1359, for example, the debtor sought permission to pay pre-filing unsecured employee amounts, arguing that it was necessary to, among other things: (i) "mitigate the adverse effects of the Pulp Mill's closure in the communities in which the Petitioners operate"; and (ii) "preserve their relationships with the employees who are no longer working, many of whom are expected to be called upon to return to employment at the Pulp Mill in the future": para 75. The Province of Nova Scotia, the major secured creditor of the debtor, opposed these payments. The court declined to approve the payments, despite noting that it "appreciate[d] that this vulnerable group of stakeholders will suffer arising from my decision". However, the court also noted that "[i]n the absence of any objection by Nova Scotia, and with the general support of the Petitioners and the stakeholders appearing on this application, I might have come to a different conclusion": para 87. In contrast, the court approved the payment of pre-filing obligations to employees in *Re Cinram International Inc* 2012 ONSC 3767 because these payments were necessary to keep employees working at the company and their services were "critical to the ongoing operations": para 67.

89 *BCE Inc v 1976 Debenture holders*, 2008 SCC 69.

90 ISS EVA, "ESG Matters" online: < https://www.issgovernance.com/library/esg-matters/>.

91 *Century Services* at para 15.

92 Indeed, "[the CCAA] is, after all, commercial legislation. Public interest is not the primary focus of the legislation and generally social stakeholders play a secondary role to that of creditors": Virginia Torrie and Vern DaRe, *The Participation of Social Stakeholders in* CCAA *Proceedings* 2019 AnnRevInsolv9 at 1.

- non-creditors cannot vote on plans and proposals.[93] Therefore, unless ESG stakeholders have a claim that is monetary in nature, such that they have the standing of a creditor, they cannot exert influence on the terms of a plan or proposal via the creditor approval process; and

- even if they do have the right to vote, ESG stakeholders can face challenges to participating in the restructuring process.[94] Canadian courts have granted orders appointing representative counsel for large stakeholder groups that collectively have a significant interest, but whose members individually lack the resources to secure "a seat at the table".[95] However, such appointments are not commonplace, likely because of the resources and coordination required to seek such an appointment.

## 2.1 Environmental (E): restructuring environmental liabilities

Canada is subject to both provincial and federal environmental laws. Most of these laws provide for various enforcement remedies, including orders and administrative penalties.

The primary federal law is the Canadian Environmental Protection Act,[96] which focuses on national and international environmental issues and establishes the federal regulatory authority. There are also federal laws and regulations related to water, fisheries, animals, and forestry that may be relevant to a company's environmental obligations.

In addition, every province has its own environmental protection laws. Provincial laws typically impose obligations to clean up contaminated land, which obligations are enforced by the provincial environmental regulator.[97] The majority of environmental enforcement orders are governed by provincial law.

### *2.1.1 Types of environmental liabilities*

The costs associated with remediation or clean-up of affected property (otherwise known as reclamation and abandonment liabilities) are the most common type of environmental liability faced by insolvent corporations. A company may also be subject to fines and penalties issued by environmental regulators.

### *2.1.2 Priority given to environmental liabilities*

Both the BIA and the CCAA include provisions addressing claims made by the federal and provincial governments for the costs associated with remedying environmental conditions or damage affecting real or immovable property of the debtor.[98] These sections provide for security for those costs by a charge on the affected real property[99] and any contiguous real property that is related to the activity that caused the environmental condition or damage, which security ranks in priority ahead of any other security against the property in question.[100] However, this charge does not apply to all environmental obligations a government seeks to enforce. This is illustrated in *Orphan Well Association v Grant Thornton Ltd* (*Redwater*),[101] discussed in greater detail below, where the majority of the Supreme Court of Canada (SCC) found that the regulator did not have a provable claim because it was not seeking a financial benefit and was acting in its capacity as regulator rather than creditor.[102] The statutory charge only applies to claims provable in

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93 These stakeholders can only express their displeasure if granted standing at the court approval stage.

94 ESG stakeholders may have limited funds, may be spread across large geographic areas, and may find it difficult to organise themselves into cohesive groups.

95 See, for example, *League Assets Corp (Re)* 2013 BCSC 2043 at para 63.

96 Canadian Environmental Protection Act, SC 1999, c 33.

97 The provincial regulator can order the assessment and clean-up of contaminated land.

98 BIA, ss 14.06(6)-14.06(8); CCAA, ss 11.8 (7)-11.8(9).

99 However, this charge is limited to the real property itself and does not attach to interests therein: *Yukon (Government of) v Yukon Zinc Corporation* 2021 YKCA 2 at para 98.

100 BIA, s 14.06(7); CCAA, s 11.8(8).

101 *Orphan Well Association v Grant Thornton Ltd* 2019 SCC 5 [*Redwater*].

102 *Redwater* at para 128.

bankruptcy, meaning there must be a debt, liability or obligation owing to the government / regulator and to which it must be possible to attach a monetary value.[103]

### *2.1.3 Disclaimer of environmental obligations*

The decision of the SCC in *Redwater* has created significant uncertainty regarding the ability of a court officer to effectively disclaim contaminated property.[104] The SCC concluded that the disclaimer power conferred upon the trustee by the *BIA* is only related to the personal liability of the trustee, and "says nothing about the liability of the 'bankrupt' or the 'estate'".[105]

Orders and penalties issued by environmental regulators in the nature of fines, restitution orders or similar are not affected by a restructuring unless the proposal or plan explicitly provides for their compromise and the creditor in relation to that debt or liability votes in favour of such compromise.[106]

Both the BIA and the CCAA include provisions that give proposal trustees and monitors, respectively, protection in relation to specified environmental liabilities, provided the court officer acts in accordance with those provisions.[107] The court officer has no personal liability for any environmental condition or damage that pre-dates the court officer's appointment, or that arises or occurs post-appointment unless it is established that the issue was a result of the court officer's gross negligence or wilful misconduct.[108] However, proposal trustees and monitors are still required to comply with any applicable duty to report or make disclosure under applicable environmental laws.[109]

## 2.2 Social (S): restructuring health or safety-related liabilities

There are no provisions in the BIA or CCAA that relate specifically to the restructuring of health or safety-related liabilities.

### *2.2.1 Types of health and safety-related liabilities*

In Canada, health and safety-related liabilities include amounts owing under the provincial workplace health and safety statutes and legislation relating to hazardous materials.[110] Another category of health and safety-related liabilities are those arising from products liability litigation – whether pursuant to class action proceedings or by way of "mass tort" claims. For example, in Canada there have been restructurings implemented to manage litigation (and the associated liabilities) regarding pharmaceuticals, transport, tobacco and tainted blood.[111]

### *2.2.2 Treatment of health and safety-related liabilities*

Certain health and safety-related statutes create liens to secure the payment of obligations to health and safety regulators.[112]

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103 *Idem* at para 119. These may also include contingent claims, provided they are not too remote or speculative: *Redwater* at para 138 and may include claims for costs incurred after the commencement of proceedings: CCAA, s 11.8(9); BIA, s 14.06(8).

104 A comprehensive discussion of *Redwater*, including this issue, can be found in T Cumming, CE Hanert and J Oliver, "The Intersection of Regulatory and Insolvency Law: Redwater's Final Chapter and the Aftermath", 2019 AnnRevInsolv 5.

105 *Redwater* at para 74.

106 BIA, ss 62(2.1), 178(1)(a); CCAA, s 19(2)(a).

107 BIA, s 14.06(7); CCAA, s 11.8(5).

108 BIA, s 14.06(2); CCAA, s 11.8(3).

109 BIA, s 14.06 (which applies to proposal trustees by virtue of s 66.4(1)); CCAA, s 11.8.

110 Workplace Safety and Insurance Act, 1997, SO, c16, ss 144, 145; Workers' Compensation Act, RSA 2000, c W-15, s 127; Workers Compensation Act, RSBC 2019, c 1, s 264.

111 For a discussion on the settlement of mass tort claims via the CCAA, see Vern W DaRe, "Risks Inherent in the Settlement of Tort Claims: Recent Direction from the Red Cross Case", 2008 AnnRevInsolv 10.

112 The Workers Compensation Act, RSM 1987, c W200, s 104; Workers' Compensation Act, RSA 2000, c W-15, s 129; Workers' Safety and Compensation Act, SY 2021, c 11, s 185; Workers Compensation Act,

Under both the BIA and the CCAA, claims of the federal or provincial governments and workers' compensation bodies are treated as unsecured claims unless they are secured by certain types of security or charges, which have been registered in accordance with the applicable personal property securities legislation.[113]

As is the case with those issued by environmental regulators, orders and penalties relating to health and safety matters in the nature of fines, restitution orders or similar, are not compromised by a restructuring unless such compromise is expressly provided for in the plan or proposal and the creditor in respect of such debt or liability votes in favour.[114] Otherwise, there are no specific restrictions or limitations on the compromise or restructuring of health and safety-related liabilities.

Tort claimants and judgment creditors whose claims arise from health and safety-related matters are treated as unsecured creditors for the purposes of insolvency and restructuring proceedings.

### 2.3 Governance (G): third party releases in favour of directors and officers of the company

Canadian courts regularly sanction releases in favour of directors and officers (and other third parties) in the context of restructuring proceedings under the BIA and the CCAA.[115] In doing so, they consider the following factors (with no single factor being determinative or necessarily applicable in each case):

- whether the parties to be released were necessary and essential to the restructuring of the debtor;
- whether the claims to be released were rationally connected to the purpose of the proposal or plan and necessary for it;
- whether the proposal or plan could succeed without the releases;
- whether the parties being released contributed to the proposal or plan; and
- whether the releases benefit the debtors as well as the creditors generally.[116]

The broad jurisdiction of the court in a CCAA proceeding can be exercised to grant releases to directors and officers in the absence of a plan.[117] If no proposal is filed in a proposal proceeding under the BIA and the stay thereunder expires without the proposal proceeding being converted into a CCAA proceeding, the company will be deemed bankrupt, and no release will be available to directors.[118]

Both the BIA and the CCAA contemplate the compromise of certain pre-filing claims against directors and officers in proposals and plans.[119] However, both statutes also include limits on the

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RSBC 2019, c 1, s 265; Workers' Compensation Act, SNS 1994-95, c 10, s 148; Workers' Compensation Act, RSNB 1973, c W-13, s 73; Workers' Compensation Act, SNWT 2007, c 21, s 143; Workers Compensation Act, SPEI 1994, c 67, s 78; The Workers' Compensation Act, SS 2013, c W-17.11, s 160; Workers' Compensation Act, SNU 2007, c 15, s 143; Workplace Health, Safety and Compensation Act, RSN 1990, c W-11, s 122; Workplace Safety and Insurance Act, 1997 SO, c 16, s 145.

113 BIA, ss 86, 87; CCAA, ss 38, 39.

114 BIA, ss 62(2.1), 178(1)(a); CCAA s 19(2)(a).

115 CCAA, s 5.1; BIA, s 50(13).

116 *Re Lydian International Limited*, 2020 ONSC 4006 at para 54. Third party releases generally in the context of restructuring proceedings were considered in *ATB Financial v Metcalfe & Mansfield Alternative Investments II Corp* 2008 ONCA 587.

117 Under the CCAA, the court can – in exceptional circumstances – utilise the broad jurisdiction conferred by s 11 (to "make any order that it considers appropriate in the circumstances") to release third party claims against directors and officers where a plan is not approved upon termination of the CCAA proceedings. To receive such an order, the applicant must demonstrate that the order is appropriate in the circumstances and that the parties to be released have acted in good faith and with due diligence: see for example, *Re ENTRETEC Corporation*, 2020 ABQB 751, where Justice Romaine granted such an order, subject to the exclusion of specified claims.

118 BIA, s 50.4 (8).

119 BIA, s 50(13); CCAA, s 5.1.

nature of claims that can be compromised, namely: (i) claims that relate to contractual rights of one or more creditors arising from contracts with one or more directors; and (ii) those based on allegations of misrepresentation made by directors to creditors or of wrongful or oppressive conduct by directors.[120] Further, under both statutes claims such as fines, penalties or award of damages in respect of bodily harm or wrongful death cannot be compromised unless the plan or proposal explicitly provides for the compromise of that debt or liability, and the creditor in relation to that debt or liability voted in favour of the acceptance of the plan or proposal.[121]

The BIA and CCAA both authorise the court to grant a priority charge over all or part of the property of the debtor company in favour of the directors and officers as security for the indemnification of directors and officers in respect of liabilities that they may incur in such capacities after the commencement of proceedings.[122] These charges are intended to keep management in place during restructuring so that the debtor company may benefit from their experience and institutional knowledge.[123]

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

#### *3.1.1 Approving a restructuring plan*

As noted above, any proposal or plan is subject first to approval by the affected creditors – a majority in number holding at least two thirds by value of the claims voted in a class. While there is no requirement for approval of a proposal or plan by environmental regulators, environmental liabilities can be very significant, with the result that environmental stakeholders may have an effective "veto" of any plan if those liabilities represent more than one third of the value of claims voting in a particular class.

#### *3.1.2 Discretion to consider wider public interest concerns*

As discussed above, after the requisite majorities have voted to approve a proposal or plan, the court will consider whether to exercise its discretion to approve it. In doing so, the court will weigh various factors, including whether the proposal or plan is in "the interests of the public".[124] Such interests include the preservation of jobs,[125] the provision of important services to communities[126] and ensuring that debtors comply with their tax obligations.[127]

However, while courts may consider the impacts of their decisions on the public interest, the proposal provisions of the BIA and CCAA are still primarily focused on addressing the relationship between insolvent entities and their creditors with the purpose of preventing the social and economic costs of a liquidation.[128] Therefore, the interests of creditors are given considerable

120 CCAA, s 5.1(2); BIA, s 50(14).
121 BIA, ss 62(2.1), 178(1); CCAA, s 19(2).
122 BIA, s 64(1); CCAA, s 11.51.
123 *Northstar Aerospace Inc, Re,* 2013 ONSC 1780 at para 29.
124 *Canwest* at paras 19-21; *Silbernagel, Re* (2006), 81 OR (3d) 152, 2006 CanLII 13427 at paras 9, 10. See BIA, ss 50.6, 54, 65.11, 65.13 65.2, 104.1; CCAA, ss 6, 11.2, 32, 36.
125 *Canadian Red Cross* at para 28.
126 *Canwest* at para 26.
127 *Silbernagel* (2006), 81 OR (3d) 152, 2006 CanLII 13427 (SC) at para 14.
128 See, for example, *Century Services* at para 15. In addition, the long form title of the CCAA is "[a]n act to facilitate compromises and arrangements between companies and their creditors", which also provides insight into its intended purpose: see, for example, *Stelco ONCA* at para 7; For BIA example, see *Kitchener Frame Ltd., Re,* 2012 ONSC 234 at para 53. While courts have recognised that the public interest includes, for example, the enforcement of environmental regulations, it has found that insolvency legislation has balanced this with the public interest of "third-party creditors in being treated equitably": *AbitibiBowater Inc, Re*, 2012 SCC 67 at para. 32; see also *Yukon (Government of) v Yukon Zinc Corporation*, 2021 YKCA 2 at para 91.

weight and deference, both in the provisions of the statutes and by the courts in exercising their jurisdiction under the Acts.[129]

### *3.1.3 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

There is no statutory requirement under the BIA or the CCAA for environmental protection authorities or advocacy groups to approve a proposal or plan. However, creditors holding claims in respect of environmental liabilities that will be affected by a proposal or plan can vote on that proposal or plan. Accordingly, if those stakeholders have large monetary claims, they may exert significant influence on the course of restructuring proceedings. Moreover, where the claims of environmental regulators are afforded super-priority, those obligations may have a significant practical impact on the course of the restructuring proceedings.[130]

Additionally, if environmental obligations have to be paid out in priority to other creditors, with the result that subsequent creditors will see little or no recovery, debtors may find it difficult to secure the DIP financing that they require to fund a restructuring proceeding. In some cases, this may result in debtors not being able to pursue restructuring at all.

## 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

### *3.2.1 Approving a restructuring plan*

There is no statutory "veto" given to government regulators, unions, or employee advocacy groups under either the BIA or the CCAA.

As noted above, proposals and plans are subject to creditor approval. To the extent that employees and former employees are creditors of a debtor company, they are entitled to vote on the proposal or plan. Depending on the circumstances, employee creditors may be classified separately from other creditors.[131]

No proposal or plan can be approved by the court if it does not make provision for certain prescribed payments to and for the benefit of employees.[132]

### *3.2.2 Discretion to consider wider public interest concerns*

As noted above, the court has the discretion to consider the public interest in proceedings under the BIA and the CCAA. This includes the interests of employees.

### *3.2.3 Protection of employee rights*

Canadian Courts have exercised their discretion to appoint representative counsel to act on behalf of employees in CCAA proceedings, the costs of which may be paid out of the debtor company's estate.[133] Depending on the circumstances, representative counsel may assist employees and former employees by providing a reliable resource of information and by litigating claims on

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[129] For an example in BIA proposal proceedings, see *Wiivv Wearables Inc (Re),* 2021 BCSC 511 at paras 50, 52; see also *Magnus One Energy Corp, Re,* 2009 ABQB 200 at para 11; *Re Abou-Rached,* 2002 BCSC 1022 at para 65; For an example in CCAA proceedings, see *Olympia & York Developments Ltd v Royal Trust Co* (1993), 12 OR (3d) 500, 17 CBR (3d) 1 at para 42.

[130] See, for example, the discussion of *Redwater* in section *2.1.2* above.

[131] *Re Invictus MD Strategies Corp et al*, [2020] (BCSC), Vancouver Registry No S-201708 [*Invictus*].

[132] BIA, s 60(1.1), (1.3), (1.5) and CCAA, s 6(3), (4), (5), (6). A bill (Bill C-228) is currently before the Senate of Canada. If enacted, the proposed legislation would amend BIA, s 60(1.5) and CCAA s 6(6) by adding amounts in respect of certain pension obligations that must be provided for in any proposal or plan.

[133] *Sears Canada Inc et al (Re),* Toronto CV-17-11846-00CL (Ontario Superior Court of Justice [Commercial List]); *Nortel Networks Corp, Re* (2009), 53 CBR (5th) 196, 2009 CanLII 26603 at para 12 (*Nortel 2009*). For an example of representative counsel being appointed in BIA proposal proceedings, see *Kitchener Frame Ltd, Re* 2012 ONSC 234.

behalf of individuals who, on their own, would have little means of pursuing their claims in respect of pension, termination, severance, retirement, and other payments.[134]

Collective agreements entered into by the debtor remain in force during CCAA and BIA proceedings and may not be altered except as expressly authorised.[135] Collective agreements are expressly excluded from the operation of the contractual disclaimer provisions.[136]

Employees who are owed "eligible wages"[137] when their employer commences a proceeding pursuant to the CCAA or the proposal provisions of the BIA are eligible for payments pursuant to the Wage Earner Protection Programme (WEPP),[138] which provides for payments to employees of up to an amount equal to seven times the maximum weekly insurable earnings under the Employment Insurance Act by the federal government.[139] The government is subrogated to any rights that employees who receive payments may have against the insolvent employer, or the directors of the insolvent employer, to recoup amounts paid under the WEPP.[140] The balance of employee claims is unsecured.

### 3.3 Governance (G): board / management conflicts addressed in a restructuring plan)?

In certain circumstances, where management and other employees of a debtor company are deemed critical to restructuring efforts, courts may approve a key employee retention plan (KERP) and / or a key employee incentive plan (KEIP).[141] KERPs typically provide for payments to employees at specified times in the future, on the condition that the employees remain with the debtor company when those specified times arrive. KEIPs typically provide for payments tied to the debtor company successfully achieving certain milestones. Both plans are aimed at retaining those essential employees during the period in which they are likely to seek other opportunities as a result of the financial state of the debtor company.[142] Although neither the BIA nor the CCAA specifically contemplate priority charges over the debtor company's assets to secure KERPs and KEIPs, such charges have been granted in both types of proceedings.[143]

KERPs and KEIPs are developed in conjunction with a proposal trustee or a monitor and are subject to court approval. Courts have considered the following non-exhaustive list of factors in deciding whether or not to approve these plans:

- whether the proposal trustee or a monitor (as the case may be) supports the plan;
- whether the key employees who are the subject of the plan are likely to pursue other employment opportunities absent the approval of the plan;
- whether the employees who are the subject of the retention plan are truly "key employees" whose continued employment is critical to the successful restructuring of the debtor company;
- whether the quantum of the proposed retention payments is reasonable; and

134 *Nortel 2009* at para 13.
135 See *Honsberger's* at 222; see also Sarra, *Rescue!* at 389.
136 CCAA, ss 32(9), 33(1); BIA, ss 65.12(6), 65.11(10).
137 See Wage Earner Protection Programme Act, SC 2005, C. 47, s 2(1) [WEPPA].
138 WEPPA, s 5(1)(b)(iv).
139 WEPPA, s 7(1). The prescribed maximum amount payable to a single employee at the time of writing is CAD $7,578.83 (for proceedings commenced between November 20,2021 and December 31, 2021), and CAD $8,117.34 for those commenced in 2022. See Practical Law, "Wage Earner Protection Programme Act (WEPPA): Overview" online: < https://ca.practicallaw.thomsonreuters.com/Document/I8f9dd0a88e2511ea80afece799150095/View/FullText.html?transitionType=Default&contextData=(sc.Default)&clientid=910138-00001>.
140 WEPPA, s 36(1).
141 *Danier Leather Inc (Re)*, 2016 ONSC 1044 at para 75.
142 Sarra, *Rescue!* at 346.
143 *Danier Leather* at para 78. For CCAA examples, see *Cinram* at para 91 and *Grant Forest Products Inc, Re,* 2009 OJ No 3344 at para 4. For a BIA example, see *Ontario Securities Commission v Bridging Finance Inc,* 2021 ONSC 4347 at para 14.

- the business judgment of the board of directors regarding the necessity of the retention payments.[144]

KERPs and KEIPs may create conflicts between the interests of management and those of the debtor company. For example, where management negotiates DIP financing, management may use their strategic position to, for example, negotiate for a higher amount financing than would otherwise be necessary in order to fund payments to themselves pursuant to a KERP or KEIP.[145] This conflict is mitigated to a degree by the oversight of the court in approving both debtor-in-possession financing and KERPs / KEIPs, and the deference given by the court to the opinion of the proposal trustee or the monitor (who has participated in the formulation of the relevant plan) as to whether it should approve the retention / incentive plan.

Potential conflicts of interest between management and the debtor company are also addressed by the restriction on voting rights of "related parties" (which may include directors). Under both the BIA and the CCAA a "related person" may vote against but not for the acceptance of the proposal or plan.[146]

The provisions of federal and provincial corporate law continue to apply to the directors and officers of companies that are undergoing restructuring pursuant to the CCAA or the BIA. These include a duty of care and a fiduciary duty of loyalty on the part of directors and officers.[147] Further, companies listed on Canadian stock exchanges are also subject to additional disclosure obligations and other regulations targeted at reducing the risk of conflicts of interest with respect to management compensation. For example, companies listed on the TSX must publicly disclose in an information circular whether there are restrictions on insiders participating in security-based compensation arrangements. Companies listed on the TSX Venture Exchange are subject to additional restrictions, including requirements that disinterested shareholders approve insider participation in security-based compensation arrangements exceeding certain thresholds as well as for any amendment to security-based compensation that results in a benefit to an insider.[148]

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

We have not identified any industry guidelines and / or best practices prescribed for the protection of the environment in a restructuring.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

We have not identified any industry guidelines and / or best practices prescribed for the protection of employee rights in a restructuring.

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

Lawyers, accountants and LITs are all subject to legally binding ethical obligations imposed by their respective governing bodies. The Canadian Association of Insolvency and Restructuring

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144 *Danier Leather* at para 76; see also *Grant Forest Products Inc (Re)* (2009) 57 CBR (5th) 128, 2009 CanLII 42046 (ONSC).

145 Sarra, *Rescue!* at 347.

146 BIA, ss 4(2), 54(3); CCAA, ss 2(2), 22(3).

147 See, for example: CBCA, s 122; Business Corporations Act, SBC 2002, c 57, s 142; ABCA, s 122, Business Corporations Act, RSO 1990, c B 16, s 115, Business Corporations Act, SNB 1981, c B 9.1, s 79, Business Corporations Act, SNWT 1996, c 19, s 102, Business Corporations Act, SPEI 2018, c 22, s 77, Business Corporations Act, CQLR, c S-31.1, s 119, The Business Corporations Act, SS 2021, c 6, s 9-1t, Business Corporations Act, RSY 2002, c 20, s 102, 123, The Corporations Act, RSM 1987, c C225, s 97, 116, Corporations Act, RSN 1989, c. C-36, s 203.

148 TSXV, Policy 4.4: Security Based Compensation (24 November 2021) online: <https://www.tsx.com/resource/en/2761>, s 5.3.

Professionals (CAIRP) has both rules and standards of professional conduct applicable to its members and candidates registered in their qualification programme.[149]

Each of these regulatory schemes include provisions requiring that applicable professionals:

- take reasonable steps to identify circumstances that could pose a conflict of interest;
- apply necessary safeguards in situations of conflict, such as notifying the client of the circumstances giving rise to the conflict and obtaining their consent to act in such circumstances; and
- decline to accept an engagement or resign from an engagement if a conflict of interest cannot be appropriately resolved with the application of safeguards.[150]

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

Responsible investment is a growing trend in Canada. A 2020 report prepared by the Responsible Investment Association shows that "responsible investing" accounts for 61.8% of the country's professionally managed assets, with 45% of that amount being public equities.[151]

A number of financial institutions in Canada have established ESG / sustainable financing programmes. Several examples of financial products offered by these institutions include: "green bonds" to support initiatives related to among other things, renewable energy and green infrastructure; "social bonds" to support affordable infrastructure, access to health and nutrition, and businesses owned or led by equity seeking groups; and "transition bonds" that provide loans related to activities that significantly reduce emissions.[152]

In addition, at the time of writing this chapter, six Canadian financial institutions have adopted the Equator Principles.[153] The Equator Principles were formulated in 2003 and last updated in October 2020, and are intended to serve as a common baseline and risk management framework for financial institutions to identify, assess and manage environmental and social risks when financing projects.[154] By adopting the Equator Principles, these Canadian financial institutions have agreed

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149 See CAIRP, "Rules of Professional Conduct and Interpretation" (August 2018) online: <https://cairp.ca/rules-prof-conduct.html> r 4, which provides that "[m]embers shall with respect to any professional engagement be free of any influence, interest or relationship which impairs their professional judgment or objectivity or which, in the view of a reasonable and informed observer, has that effect".

150 See, for example, BC, Law Society of British Columbia, Code of Conduct, r 3.4 and Ontario, Law Society of Ontario, Code of Conduct, r 3.4; Alberta, Law Society of Alberta, Code of Conduct, r 3.4; BC, Chartered Professional Accountants of British Columbia, Code of Professional Conduct, r 210; Ontario, Chartered Professional Accountants of Ontario, CPA Code of Professional Conduct, r 210; Alberta, Chartered Professional Accountants of Alberta, Rules of Professional Conduct with Guidance, r 210; Bankruptcy and Insolvency General Rules, CRC, c 368, ss 34, 42-44, 47.

151 See Responsible Investment Association, "2020 Canadian Responsible Investment Trends Report" (Responsible Investment Association, November 2020) online: <https://www.riacanada.ca/research/2020-canadian-ri-trends-report/> at 4, 9, 10.

152 See, for example, Export Development Canada, "Sustainable Finance: Enabling a Sustainable, Equitable Economy", online: <www.edc.ca/en/about-us/esg/sustainable-finance.html>; see also, Royal Bank of Canada, Capital Markets, "Sustainable Finance", online: <www.rbccm.com/en/expertise/sustainable-finance.page>.

153 Including Bank of Montreal, the Bank of Nova Scotia, Canadian Imperial Bank of Commerce (CIBC), Export Development Canada, Royal Bank of Canada, and TD Bank Financial Group: Equator Principles, Members & Reporting: "Equator Principles Financial Institutions (EPFIs) and their annual reporting on EP-related activities", online: <equator-principles.com/members-reporting/>.

154 Carla Potter et al, "The Equator Principles – EP4: Impacts and Considerations for Project Financings" (December 1, 2021), American Bar Association, online: <www.americanbar.org/groups/business_law/publications/blt/2021/12/equator-principles/>; Equator Principles, "About the Equator Principles: A financial industry benchmark for determining, assessing and managing environmental and social risk in projects", online: <equator-principles.com/about-the-equator-principles/>.

they will not finance projects that do not comply with the requirements of the Principles. Accordingly, in considering financing, these institutions may, for example, require that prospective borrowers:

- develop and maintain environmental and social management systems that will identify, assess and manage ESG risks in their projects;
- develop plans to minimise or offset the potential risks of their projects; and / or
- show ongoing engagement with local communities that may be affected by their projects.[155]

## 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

Six of the largest Canadian banks[156] have committed to achieving a net-zero banking economy by 2050, as outlined in the Paris Agreement on climate change.[157] They are also members of the Net-Zero Banking Alliance.[158]

Several Canadian banks are working on implementing the climate-related disclosures developed by the International Task Force on Climate-Related Financial Disclosures[159] which, as discussed in the section below, will be mandated by the Canadian Federal Government in 2024. In addition, many of Canada's largest banks also have committed to increasing the issuance of green bonds to finance new and existing green projects and developing new metrics to link ESG factors with bank group performance and executive pay.[160]

## 5.3 Promoting ESG by the central bank and regulators

Climate change is an area of focus for both Canada's central bank, the Bank of Canada,[161] and the Office of the Superintendent of Financial Institutions (OSFI). In January 2022, the Bank of Canada and OSFI released the results of a pilot project on climate scenario analysis, and the development of certain scenarios (developed in conjunction with six[162] federally regulated financial institutions) designed to help the Canadian financial sector identify, measure, and disclose climate-related risks.[163]

In May 2022, OSFI issued a draft guideline addressing the impact of climate change on managing risk, and introducing mandatory financial disclosures aligned with the International Task Force on Climate-Related Financial Disclosures framework.[164]

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155 *Ibid*.

156 These include: (i) Bank of Montreal; (ii) Canadian Imperial Bank of Commerce; (iii) National Bank of Canada; (iv) Royal Bank of Canada; (v) Scotiabank; and (vi) TD Bank Group.

157 National Bank, "Six of Canada's Largest Banks Join United-Nations-convened Net-Zero Banking Alliance" (October 15, 2021), online: <www.nbc.ca/about-us/news-media/press-release/2021/20211015-Six-des-grandes-banques-canadiennes-se-joignent-a-lalliance-bancaire-Net-Zero-des-Nations-Unies.html>.

158 This is an industry led, UN convened global group of banks committed to aligning their lending and investment portfolios with net-zero emissions by 2050: UN Environment Programme, Finance Initiative, "Net-Zero Banking Alliance", online: <www.unepfi.org/net-zero-banking/>.

159 Canadian Bankers Association, "Focus: Banks in Canada Committed to a Net-Zero Economy by 2050", online: <cba.ca/Assets/CBA/Documents/Files/Article%20Category/PDF/bkg_netZeroCommitments_en_Nov.pdf.>

160 *Ibid*.

161 The Bank of Canada is a member of the Central Banks' and Supervisors' Network for Greening the Financial System.

162 These include: (i) Co-operators Group Limited; (ii) Intact Financial Corporation; (iii) Manulife Financial Corporation; (iv) Royal Bank of Canada; (v) Sun Life Financial; and (vi) TD Bank Group.

163 Bank of Canada, "Bank of Canada / OSFI pilot helps Canadian financial sector assess climate change risks" (January 14, 2022), online: <https://www.bankofcanada.ca/2022/01/bank-canada-osfi-pilot-helps-canadian-financial-sector-assess-climate-change-risks/>.

164 OSFI has stated that it plans to issue the final version of the guideline by early 2023, disclosure starting in 2024, which "aligns with a commitment made by the federal government to require financial institutions to publish climate disclosures starting in 2024": OSFI, "OSFI consults on expectations to advance climate risk management" (May 26, 2022), online: <www.osfi-bsif.gc.ca/Eng/osfi-bsif/med/Pages/b15-dft_nr.aspx>.

# FRANCE

## 1. General overview of the restructuring regime

The French Commercial Code provides for two categories of insolvency proceedings (in court and out of court proceedings), the main differences of which are:

- confidentiality – out of court proceedings are strictly confidential, whereas in court proceedings are public;
- the constraint of creditors – out of court proceedings are based on negotiations and are subject to creditors' agreement on an amicable agreement, whereas in court proceedings provide for a collective proceeding against creditors and can lead to a plan imposed on creditors; and
- the outcomes of the proceedings:
  - subject to creditors' agreement, out of court proceedings usually lead to an agreement that provides for a restructuring of the debtor, including usually the staggering of the debtor's debts, possible write-off and new money or asset sales. More rarely, these proceedings can result in organising the sale of the debtor's company / business; and
  - depending on the proceedings, in court proceedings can lead to a repayment plan (debt staggering over a maximum of 10 years), a global or partial sale plan of the debtor's activities (see below for further details) or the cessation of the debtor's business activities and a piecemeal sale of its assets.

### 1.1 Formal restructuring procedures

The French Commercial Code provides for four in court proceedings: safeguard proceedings, accelerated safeguard proceedings, reorganisation proceedings and judicial liquidation.

These proceedings are public and take place under the supervision of the court.

The diversity of these proceedings aims to respond to the different needs of the debtor depending on its financial situation. Thus, each in court proceeding is governed by its own opening conditions, is graduated according to the debtor's situation and leads to restructuring solution(s) depending on the analysis of the business of the debtor and possible ways to restore profitability.

#### *1.1.1 Presentation of in court proceedings*

In court proceedings are graduated according to the debtor's situation, the key point of which is the concept of cash flow insolvency. Whether the debtor is cash flow insolvent or not determines the following:

- whether it is eligible for a safeguard proceeding (if not cash flow insolvent) or a reorganisation proceeding / judicial liquidation (if it is cash flow insolvent);
- whether it remains in control of the restructuring (i.e. debtor in possession). In practice, this impacts on whether the debtor is the only one who can request the opening of an in court proceeding and whether there may be an outcome that the debtor would not have chosen (e.g. the sale of its business), subject to the approval of the court; and
- its powers to manage and dispose of its assets.

More precisely, the purposes and outcomes of each proceeding are as follows:

- for safeguard proceedings, helping the debtor (which is not cash flow insolvent) to solve difficulties (financial, economic and legal) that it is not able to overcome and facilitating the reorganisation of the debtor in order to allow the continuation of its economic activity, the maintenance of employment and the discharge of liabilities.

This proceeding can lead to:

- the adoption of a repayment plan (called a safeguard plan), which is described in greater detail below;

- the closure of the proceeding if the debtor's problems disappear; or

- the conversion into a reorganisation proceeding or a judicial liquidation, if the debtor becomes cash flow insolvent during the safeguard proceeding or if no safeguard plan can be prepared and the business needs to be sold (i.e. a sale plan) or closed (liquidation proceedings);

▪ for accelerated safeguard proceedings, helping the debtor – which is engaged in conciliation proceedings (out of court proceedings), has prepared a draft safeguard plan and may be cash flow insolvent for less than 45 days – to solve any difficulties (financial, economic or legal) that it is not able to overcome and facilitating its reorganisation in order to allow the continuation of its economic activity, the maintenance of employment and the discharge of liabilities.

  This proceeding can lead to:

  - the adoption of a safeguard plan;

  - the closure of the proceeding in the event the debtor's problems disappear; or

  - the conversion into a reorganisation proceeding or judicial liquidation, if the opening conditions of such proceedings are met.

  The main difference with safeguard proceedings is that a draft plan is prepared and negotiated during the conciliation proceedings, which is confidential and preserves the value of the business of the debtor. If an agreement is reached with a majority – but not all – of the creditors, the opening of accelerated safeguard proceedings, after the end of the conciliation proceedings, will enable the court to force the adoption of the plan on dissenting creditors;

▪ for reorganisation proceedings, reorganising the company / the activity of a debtor, which is cash flow insolvent, in order to allow the continuation of economic activity, the maintenance of employment and the discharge of liabilities.

  This proceeding can lead to:

  - the adoption of a repayment plan or a sale plan;

  - the closure of the proceeding if the debtor is able to pay off its creditors and the costs / debts related to the proceeding; or

  - the conversion of the proceeding into a judicial liquidation, if a reorganisation or sale as an ongoing business is clearly impossible; and

▪ for judicial liquidation, if the debtor is cash flow insolvent and its recovery is clearly impossible, ceasing its activity or selling its assets through a global or separate transfer of its rights and assets.

  This proceeding can lead to the adoption of a sale plan or the cessation of the debtor's activity and a piecemeal sale of the debtor's assets.

A summary of the opening conditions and main outcomes of in court proceedings is set out below:

| **In court proceedings** | **Opening conditions** | **Main outcomes[1]** | | |
|---|---|---|---|---|
| | | **Continuation of the business** | | **Cessation of the business** |
| | | *Repayment plan* | *Sale plan* | *Piecemeal sale of assets* |
| **Safeguard proceedings** | ▪ No cash flow insolvency[2]<br>▪ Facing difficulties without being able to overcome them | Safeguard plan[3] | | |
| **Accelerated safeguard proceedings** | ▪ Facing difficulties without being able to overcome them | Safeguard plan | | |
| **Rehabilitation proceedings** | ▪ Cash flow insolvency<br>▪ Being engaged in conciliation proceedings<br>▪ Having prepared a draft safeguard plan | Reorganisation plan and / or sale plan | | |
| **Judicial liquidation** | ▪ Cash flow insolvency<br>▪ Reorganisation clearly impossible | | Sale plan and / or piecemeal sale of assets | |

### 1.1.2 *Common characteristics of in court proceedings*

The opening of in court proceedings results in:

- the appointment of an insolvency judge who supervises the proceedings;
- the appointment of two insolvency practitioners:
  - the creditors' representative, who represents the creditors' interests and is in charge of the debtor's liabilities; and
  - a judicial administrator, who supervises, assists or manages the debtor's business, according to the mission given to him / her by the court;
- the opening of the "observation period", during which a restructuring solution must be found under the supervision of the court, the insolvency judge and the insolvency practitioners. This period is automatic for safeguard / reorganisation proceedings and its duration is limited to a maximum of 12 months for safeguard and 18 months for reorganisation proceedings. In judicial liquidation, this period is not automatic and requires that the court orders an interim continuation of the activity if a sale plan is being considered. The continuation of the activity is then limited to six months;
- the automatic stay, which means that:
  - the debtor is prohibited from paying claims raised before the opening of in court proceedings;

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1 Closure of the proceedings and conversion.

2 Under French law, when the company is unable to pay its current liabilities with its available assets (cash or assets that can be quickly turned into cash), taking into account any credit reserves and moratoria / standstills accepted by creditors.

3 A safeguard plan can include, if necessary, a partial sale (or cessation) of the debtor's activity (please see below for more details).

- creditors have to lodge their claims; and

- regarding these claims, there is an automatic stay / suspension of payment actions or actions to rescind a contract for non-payment of these claims; and

▪ the restriction of the debtor's powers to manage. During safeguard / reorganisation proceedings, in principle managers remain in control of the company (debtor in possession), but:

  - certain acts (outside the normal course of business) are subject to the judge's prior approval;

  - according to the mission given by the court, the administrator supervises or assists the company; and

  - sometimes the court can remove the managers and ask the administrator to manage the company. If there is no vacancy for the management of the debtor or no allegation of mismanagement, the mission of the administrator is usually to supervise or assist the debtor. If the administrator is appointed to manage the company, management is not entitled to act on behalf of the debtor company. As a result of the opening of a judicial liquidation, the debtor no longer has the authority to manage and dispose of its assets. The debtor's rights and actions concerning its assets are exercised by the judicial liquidator.

### *1.1.3 Possible outcomes of in court proceedings*

As mentioned above, possible outcomes depend on the type of proceedings and the debtor's situation. Two outcomes of particular note are a safeguard / reorganisation plan and a sale plan.

▪ Safeguard plan or reorganisation plan

  The aim of safeguard or reorganisation plan is to organise the debtor's restructuring. It mainly provides for a repayment plan of pre-petition claims but can also include various restructuring measures (staff reduction, cessation of a part of the activity, closure of a site or cash contribution).

  The main steps of the preparation and adoption of the plan are as follows:

  - review of the business with the debtor and the judicial administrator;

  - identification by the judicial administrator / the debtor of possible restructuring measures, proposals for repayment of pre-petition debts that may be proposed to creditors and preparation of a draft plan;

  - subject to certain limitations (described below), various proposals for the repayment of debts are possible, such as terms of payment (which can include a staggering of debts over a maximum of 10 years), debt write-off or a debt-to-equity swap;

  - consultation of creditors, through either individual consultation or collective consultation. Individual consultation of creditors occurs if the debtor does not meet certain thresholds.[4] Collective consultation of creditors through classes of affected parties (i.e. committees) occurs in the case of accelerated safeguard proceedings or safeguard or reorganisation proceedings, if the debtor meets certain thresholds or if the insolvency judge orders the constitution of classes of affected parties at the debtor's request when the relevant thresholds are not met. Affected parties (including creditors) are grouped together in different classes according to various objective criteria, defined by the judicial administrator, including, necessarily: (i) the existence of a sufficient community of economic interests; and (ii) a distinction between secured and unsecured creditors.

[4] 250 employees and EUR 20 million of net revenues or EUR 40 million of net revenues.

The main characteristics of classes of affected parties are: (i) creditors are consulted, and vote, on the entire draft plan and not only on the proposals for debt repayment; (ii) it is possible to have different proposals for debt repayment from one class to another; and (iii) subject to certain conditions, the court can adopt the plan, even if an affected party or a class of affected parties voted against it;

- consultation of the works council and creditors appointed as supervisor (*contrôleur*) of the draft plan; and

- a court hearing, during which the court: (i) hears the opinions (non-binding) of the debtor, insolvency practitioners, creditors appointed as supervisor and the representatives of the work councils; and (ii) decides whether or not to adopt the draft plan.

  To be adopted by the court, the draft plan must meet three legal criteria: (i) the continuation of the company's activity; (ii) the maintenance of employment; and (iii) the discharge of liabilities.

▪ Sale plan

  A sale plan consists of the sale of all or part of the debtor's business with a takeover of the debtor's assets / employees chosen by a buyer, who has been selected by the court, without any debts (save for a few exceptions not detailed here).

  The main steps of the preparation and adoption of a sale plan are as follows:

- the court or the insolvency practitioner sets a deadline for the submission of offers;

- the insolvency practitioner calls for tenders, receives and analyses any offers and files them with the clerk's office;

- potential buyers can consult other offers and improve their offers up to two business days before the offer review hearing; and

- the court: (i) hears the opinions of the debtor, insolvency practitioners, creditors appointed as supervisor, representatives of work councils and the public prosecutor; and (ii) chooses the best offer based on the goals of preserving jobs, repaying creditors and ensuring execution of the plan.

### 1.2 Informal restructuring procedures

The French Commercial Code provides for two out of court proceedings: ad hoc proceedings (*mandat ad hoc*) and conciliation proceedings. The goal of these two amicable proceedings is to reach an agreement between the debtor and its creditors.

These proceedings are confidential, voluntary and based on negotiations and they are subject to the creditors' consent on the amicable agreement. Both ad hoc and conciliation proceedings do not automatically stay any pending proceedings and creditors are not barred from taking legal action against the debtor to recover their claims during these proceedings. As a practical matter, it is absolutely necessary to obtain waivers from the creditors.

The main steps and characteristics of these proceedings are as follows:

▪ the debtor asks for the opening of such proceedings by filing a request at the court. During a hearing, the debtor describes its situation to the court's president, as well as the reasons justifying the opening of such proceedings;

▪ if the court's president considers that the opening of proceedings is necessary and that the opening conditions are met, he or she appoints a conciliator / ad hoc trustee and defines the mission of the conciliator / ad hoc trustee. This appointment does not have any impact on the business; rather, the debtor remains in control of the company (debtor in possession) and keeps its power to manage and dispose of the assets;

- the conciliator / ad hoc trustee is in charge of conducting the negotiations between the debtor, its creditors and more generally with all the stakeholders; and

- if the negotiations are successful, an agreement is entered into between the debtor and the stakeholders, under the supervision of the conciliator / ad hoc trustee. Failing that, the proceeding may be terminated, at the debtor's or conciliator's / ad hoc trustee's request, or new out of court proceedings[5] can be opened, at the debtor's request.

The main differences between ad hoc proceedings and conciliation proceedings are:

- opening conditions – French law does not provide for any particular opening conditions for ad hoc proceedings, whereas the opening of conciliation proceedings requires a debtor to be facing a legal, economic or financial difficulty, whether proven or foreseeable, and not to have been cash flow insolvent for more than 45 days;

- duration – there is no time limit regarding ad hoc proceedings, whereas conciliation proceedings are limited to a maximum of five months; and

- effects of the amicable agreement – on the one hand, an amicable agreement reached during ad hoc proceedings has the same binding force as a contract and is not subject to a review or the approval by the court's president or the court. On the other hand, an amicable agreement reached during a conciliation can be: (i) acknowledged by the court's president, which causes the agreement to be binding on the stakeholders and enforceable without further recourse to a judge; or (ii) approved by the court under certain conditions.[6] Such approval will have the same effect as the president's acknowledgement, except that, in addition:

  - the approval judgment will be public but the content of the agreement will otherwise remain confidential; and

  - the creditors who, during the conciliation proceedings, provide new money, goods or services to ensure the continuation of the debtor's business (other than shareholders providing new equity in the context of a share capital increase) will enjoy priority of payment (new money seniority) in the event of subsequent safeguard proceedings, rehabilitation proceedings or judicial liquidation proceedings.

## 2. Restructuring of ESG-related liabilities

### 2.1 Environmental (E): restructuring environmental liabilities

#### *2.1.1 Types of environmental liabilities*

French environmental law provides for three specific sources of obligation (which may result in various sanctions in the case of non-compliance):

- obligations resulting from "Facilities Classified as Environmental Protection" (hereafter FCEP) – any industrial or agricultural operation that is likely to create risks or cause pollution or nuisance (in particular, for the safety and health of local residents or for the protection of environment) is a FCEP, such as the operation of a quarry or a foundry activity.

[5] If the initial out of court proceeding was a conciliation proceeding and ended less than three months before, the debtor can only ask for the opening of an ad hoc proceeding. There is a specific rule that prohibits the opening of a new conciliation proceeding less than three months after the end of the previous conciliation.

[6] There are three conditions: (i) the debtor is not cash flow insolvent, or the agreement reached resolves said cash flow insolvency; (ii) the terms of the agreement ensure that the company will survive as a going concern; and (iii) the agreement does not impair the rights of the non-signatory creditors.

As FCEPs, these activities are subject to specific rules provided for under the French Environmental Code in order to reduce or prevent risks or negative consequences.

The installations covered by the FCEP legislation are listed under a nomenclature which subjects them to a classification system that reflects the seriousness of the risks or inconveniences they may cause.

There are three classification schemes for facilities:

- the declaration system applies to facilities whose activities are the least polluting and / or the least dangerous but which must comply with general environmental regulations. A simple declaration to the prefecture is required;

- the registration system applies to facilities with specific activities,[7] and this system is a simplified authorisation regime. To operate one of these activities, a prior authorisation from the local administrative authority (so called prefect) is required; and

- the authorisation system applies to facilities that present serious risks or nuisance for the environment. Under this system, the operator must apply for an authorisation (given by the prefect) before any operation and demonstrate the acceptability of the risk (for instance, impact and risk studies). In case of the sale of such a FCEP facility, the buyer must obtain an authorisation for changing operator before operating the site;

- obligations resulting from watercourse bodies of water – any intervention on a watercourse body of water (maintenance, works or cleaning) or in its vicinity (the use of fertilizers or physical products) is subject to legal obligations provided under the French Environmental Code. Water discharges or withdrawals are also regulated; and

- obligations resulting from the introduction of regulated products on the market – some products are subject to specific certifications. For instance, there are specific provisions applicable to pressure equipment according to the type of equipment (gas, liquid, vapor steam or solid). As a general matter, all products presenting a high risk for the environment (such as chemical products and explosive products) are regulated on the market by different sources of law.

In environmental matters, the main sources of financial liability arise from the breach of the above legal or regulatory obligations or the obligation of financing the remediation of a site.

More specifically, in the event of a breach of a legal environmental obligation, the various possible sanctions are:

- administrative penalties (possibly with an injunction);
- withdrawal of administrative authorisations;
- orders to perform (for example, obligation to repair damage);
- criminal sentences (including criminal fines); and / or
- civil sentences (for instance, actions brought by local authorities or environmental protection associations leading to civil damages).

Generally, those liabilities and sanctions are specific to operators. However, there are a few exceptions:

- in the context of liquidation proceedings of an operator and provided it is established that the operator's parent company committed a serious fault (*faute caractérisée*) having contributed to

[7] For example, livestock farms, service stations, combustible product warehouses (wood, paper, plastics, polymers and tyres) and cold storage.

its subsidiary's asset deficiency, the court may order the parent company to finance all or part of the remediation / site closure measures of the sites operated by the subsidiary at the end of their activities.

This principle was introduced by Law n°2010-788 dated 12 July 2010 – the so-called "Grenelle 2" – that followed a national political conference on environment issues in France. The introduction of this new principle was the consequence of several court decisions in the context of the liquidation of subsidiaries of important and wealthy group entities facing major environmental cleaning costs, where the court had been unable to hold the parent company liable due to the lack of supporting legal provisions. However, French law does not provide for a legal definition of a serious fault in this context. In practice, the preferred view is that fault does not necessarily have to be intentional as long as it can be proved that the legal entity to be held liable could not ignore that its behavior exposed its subsidiary to a serious risk.

No published case law regarding the application of this provision has been identified. It can be assumed that in the context of large groups of companies exposed to reputational risks, settlement agreements will be negotiated to obtain a voluntary contribution by the parent company to the indemnification of the damages caused; and

- very occasionally, there are case law decisions whereby shareholders may also be held liable on three "ordinary" legal grounds: (i) when the shareholder acts and behaves as if it were the operator (the so-called theory of appearance); (ii) when the shareholder fails to maintain the separate identities of the companies; or (iii) when the subsidiary is considered as a fictitious entity and has been set up as a fraud to evade liability (for example, in the case of under-capitalisation or lack of adequate insurance).

### *2.1.2 Priority given to environmental liabilities*

French insolvency law does not provide for any specific priority or treatment for environmental liabilities.

As a consequence, the treatment of such liabilities will depend on the type of insolvency proceedings opened and the characteristics of the liability (secured or unsecured claims).

During out of court proceedings, the restructuring of environmental liabilities requires the agreement of the creditor concerned and ongoing investigations / actions, if any, that could lead to the operator being fined (administrative, civil or criminal action) are not suspended.

During in court proceedings:

- environmental liabilities, the operative event of which occurred before the opening of the proceedings, are subject to the automatic stay and, depending on the outcome of the proceeding:
  - can be restructured under a repayment plan; or
  - may be partially paid with part of the debtor's asset sale price in case of a sale plan or a piecemeal sale of the debtor's assets. In this scenario, creditors are allocated a legal rank based on the securities and privileges they may have; and
- environmental liabilities that occurred after the opening of the proceedings may be given preferential treatment if it is demonstrated that they are useful for the debtor in court proceedings. For example, according to a specific court decision, site remediation claims are useful for the proceeding because their payment could facilitate the sale of the debtor's business. Failing that, they will be treated as pre-petition environmental liabilities as mentioned above.

### *2.1.3 Disclaimer of environmental obligations*

There is no possible disclaimer of environmental obligations.

### 2.2 Social (S): restructuring health or safety-related liabilities

The employer must ensure the health and safety of its employees.

To comply with this obligation, the employer must implement prevention, information and training measures and assess the occupational risks on each work site. These risks must be documented.

#### *2.2.1 Types of health and safety-related liabilities*

If the employer's obligation is not complied with, civil and / or criminal liability may be incurred as follows:

- civil liability – in the event of endangerment, even if it did not lead to an accident or an illness, the employee may terminate his / her employment contract and refer the matter to the court to try to obtain compensation for the claims leading to the termination. Moreover, in the event of an occupational accident and / or occupational disease, the employee may refer the matter to a civil court to try to obtain financial compensation; and

- criminal or administrative liability – exposing an employee to an identified risk, without taking the necessary preventive measures, is a breach of the employer's obligation to ensure employee safety and health. This failure can lead to criminal and administrative liabilities.

#### *2.2.2 Treatment of health and safety-related liabilities*

- Out of court proceedings

  French insolvency law does not provide for any specific priority or treatment for health and safety-related liabilities during out of court proceedings.

  During these proceedings, the restructuring of health and safety-related liabilities requires the agreement of the creditor concerned and investigations / actions, if any, that could lead to the operator being fined (administrative, civil or criminal action) are not suspended.

- In court proceedings

  During court proceedings, the payment of claims related to an employment contract is, subject to certain conditions and limitations (i.e. a general cap which amounts to circa EUR 73,000 for 2023), guaranteed by a wage guarantee scheme called "AGS" if the employer is not able pay the debts to the employees.

  Case law recognises that payment of the damages due to the employee because of the employer's failure to fulfil its obligation to ensure employee safety and health is guaranteed by the AGS.

  As a consequence, if the relevant conditions are met, AGS will pay the employee the amounts due and then be subrogated to the rights of the employee concerned.

### 2.3 Governance (G): third party releases in favour of directors and officers of the company

There are no general or specific releases of liability under French commercial law in favour of the managers.

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

### 3.1.1 *Approving a restructuring plan*

- Out of court proceedings

  As mentioned above, an out of court agreement is subject to the approval of the court or the acknowledgement of the court's president when it has been negotiated during conciliation proceedings. In this case, the French Commercial Code sets the conditions that must be met to obtain the approval or acknowledgement (please refer to section 1.2 above). These conditions do not include any environmental consideration.

  As a consequence, environmental protection authorities or environmental advocacy groups may not have any influence on the approval / acknowledgement of the conciliation agreement. However, they could have an influence at the stage of negotiations, in their capacity as a creditor of the debtor. As is the case of any creditor invited to negotiate, they are free to refuse the debtor's restructuring proposals. Such refusal could have an impact on the entire negotiation, because out of court proceedings require the agreement of all the creditors who were invited to negotiate.

- In court proceedings

  As mentioned above, any restructuring plan is subject to the approval of the Commercial Court, following three legal criteria (please refer to section 1.1.3). These criteria do not include any environmental considerations.

  However, environmental protection authorities or environmental advocacy groups may have an indirect influence. First, this may occur in their capacity as a creditor of the debtor, insofar as:

  - they could ask the insolvency judge to be appointed as a supervisor (*contrôleur*). This function will give them more power during insolvency proceedings, including the right to information and the right to be consulted (non-binding) on certain subjects; and

  - as is the case with any creditor, they may participate in the preparation of a restructuring plan (safeguard or reorganisation plan), whether by voting in a class of affected parties or by responding to the propositions formulated by the creditors' representative. In this scenario, their influence is limited, as their possible refusal cannot prevent the adoption of the plan if adoption conditions are met.

  Second, in their capacity as a state authority, environmental protection authorities may have an indirect influence. French environmental law remains fully applicable in the context of insolvency proceedings. Therefore, if the draft restructuring plan will have an impact on activities or facilities subject to environmental law, the environmental protection authorities may be consulted via a process that is independent of the plan adoption process. For example, if a sale plan adopted by the court includes an FCEP that is subject to the authorisation scheme (see section 2.1.1 above), the buyer must obtain the authorisation of the prefect to change operator before operating. Otherwise, it will not be authorised to operate the site.

### 3.1.2 *Discretion to consider wider public interest concerns*

As mentioned above, when the court approves or its president acknowledges an out of court agreement or a repayment plan, they are bound by legal criteria.

If these criteria are met, wider public interest concerns may also be taken into account.

For example, in the event of a sale plan, if the court has to distinguish between two bidders who sent similar offers (same price, same number of jobs taken over and same likelihood of sustainability of the activity), the court may take into account wider public interest concerns to choose which offer is the best.

### *3.1.3 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

Please refer to section *3.1.1* above.

## 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

### *3.2.1 Approving a restructuring plan*

- Out of court proceedings

  As mentioned above, an out of court agreement is subject to the approval of the court or the acknowledgement by the court's president if it has been negotiated during conciliation proceedings. In this case, the French Commercial Code defines the conditions that must be met to obtain the approval or acknowledgement.

  These conditions do not expressly include any social considerations. However, in an indirect way, the court can take into account employees' interests. That is because, to approve a conciliation agreement, the court must verify that the agreement: (i) ensures the sustainability of the company's activity; and (ii) does not affect the interests of creditors who are not parties to the agreement.

  The is no legal definition of the sustainability of the company's activity. However, it can usually be said that a business plan showing a return to profitability of the debtor by the 12 to 18 month mark following the execution of the conciliation agreement meets such criteria. The business plan of the management (and related cash flow forecast) is usually subject to an independent review by an external auditor known as an independent business review (IBR).

- In court proceeding

  As mentioned above, any restructuring plan is subject to the approval by the Commercial Court, following three legal criteria. One of these criteria is the maintenance of jobs. However, it is important to note the following:

  - cumulative analysis of the three criteria by the Commercial Court: there is no legal primacy between the three legal criteria. Even if the court is particularly sensitive to the preservation of employment (whether it is a safeguard plan, a rehabilitation plan or a sale plan), the draft plan is analysed on a case-by-case basis, meaning that the plan issued by the court will not necessarily be the one that would preserve the most jobs;

  - the analysis of the "preservation of jobs" criterion is broad. For example, in the event of a sale plan, the court should assess the criterion of the preservation of employment based on the number of jobs taken over and the rights of the employees whose jobs are preserved; and

  - employee representative bodies and employees themselves may have an influence on the approval of the restructuring plan.

  In the case of trade unions, the French Commercial Code does not provide for a specific role for trade unions, but they can provide assistance (legal or financial) to the employees of a company under proceedings. They can also encourage, support or be part of demonstrations or strikes to try to exercise an influence on the outcome of a case (e.g. challenge the restructuring proposed by the management, support a bidder rather than another or promote the allocation of extra indemnities for dismissal on top of the mandatory indemnities according to law and the employment contract).

  In the case of employee representative bodies, the Works Council is the body that represents employees in the company. It must be set up in companies with more than 11 employees. The members of the Works Council are elected by the employees of the company for a maximum period of four years. The powers, composition and functioning of the Works Council depend on the size of the company.

The Works Council may have an influence (variable, according to the situation) on the approval of the debtor's restructuring plan in a number of ways. First, in its capacity as a creditor of the debtor. The Works Council can be a creditor of the debtor (e.g. if the Works Council's operational budget has not been funded by the employer). As is the case with any creditor, in that event the Works Council may participate in: (i) negotiations aimed at reaching an amicable agreement; or (ii) the preparation of a restructuring plan (safeguard or reorganisation plan), whether by voting in a class of affected parties or by responding to the proposals formulated by the creditors' representative.

Secondly, during out of court proceedings, if the Works Council is not a creditor, it does not have any influence on the negotiation of the agreement or the acknowledgment / approval of the amicable agreement. However, if the debtor requests the approval of a conciliation agreement by the court, it shall then inform the Works Council of the content of the conciliation agreement and representatives of the Works Council are called to the attend the court hearing that will hear the request for approval of the conciliation agreement. During in court proceedings, the Works Council must be: (i) informed and consulted on the draft plan (repayment plan or sale plan) and on all envisaged decisions that may have an impact on employment (e.g. staff reductions and changes in working conditions); and (ii) heard by the court before the adoption of the plan (reorganisation plan or sale plan).

Thirdly, within 10 days after the opening of in court proceedings, the Works Council, or if there is no Works Council the employees themselves, must appoint an employee representative for the purpose of the proceedings. If the company has a Works Council, the employee representative's role is mainly limited to the verification of claims and if there is no Works Council, the representative performs the duties assigned to the Works Council (please see below).

#### *3.2.2 Discretion to consider wider public interest concerns*

Please refer to section *3.1.2* above.

#### *3.2.3 Protection of employees rights*

Please refer to section 3.1.2 above.

### 3.3 Board / management conflicts addressed in a restructuring

- Out of court proceedings

  The French Commercial Code does not provide for any specific rule to prevent or address board / management conflicts in the context of out of court proceedings. As a consequence, if such a conflict appears in out of court proceedings, it would be addressed on a case-by-case basis under the supervision of the conciliator / ad hoc trustee.

  However, general corporate law provisions may be used to resolve situations when the corporate governance of a company is blocked because of a conflict (e.g. a conflict of powers / authority between two directors / managers with the same powers or a conflict between the shareholders and managers). In such a case, the appointment of an interim administrator can be requested before the court. The existing directors are then deprived of their power and authority to act on behalf of the company.

  The duration of the mission of the interim administrator and the limitations, if any, to its powers are defined by the court.

- In court proceedings

  In the context of in court proceedings, the French Commercial Code provides for some rules intended to prevent or avoid board / management conflict. As mentioned above, the court might decide to appoint an administrator with the mission to manage the debtor. In this context, the existing directors and managers will lose all their power to act on behalf of the debtor.

  Additionally, managers are prohibited from bidding for the activity or the assets of the debtor company during insolvency proceedings. Exceptionally, the court may authorise a sale in favour of managers at the public prosecutor's request.

  In the context of a reorganisation plan, the court, at the request of the public prosecutor, may make the adoption of the plan conditional on the replacement of one or more managers of the company. Moreover, if managers are also shareholders, the court may: (i) declare the shares non-transferable and decide that the voting rights attached thereto shall be exercised by a legal trustee; or (ii) force their transfer to a third party, despite refusal by the existing shareholders.

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

A practical guide for insolvency practitioners and for environmental protection authorities has been written. This guide has been drafted in order to facilitate the relations between insolvency practitioners and environmental protection authorities in the context of the insolvency proceeding of a company operating facilities classified as FCEP.

It contains a summary of:

- the mandatory obligations applicable to insolvency practitioners as soon as they have been appointed by the court in the context of an insolvency proceeding. For example: (i) the obligation to gather information on the FCEP; (ii) the obligation to issue an environmental report including the existence of identified pollution and urgent measures enforced or to be taken; and (iii) in the context of a liquidation, the obligation to notify the environmental authority of the shutdown of the activity and to implement preliminary measures to ensure the safety of the site to be closed (e.g. storage of dangerous products or closure of energy sources);

- the legal regime of claims related to environmental regulations and related issues; and

- the rules applicable to the transfer of a FCEP to a third party.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

There are no "soft law" instruments which could serve to guide or influence a company to take actions or decisions that protect employees' interests specifically in a restructuring context.

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

The missions of the judicial administrator and creditors' representative are regulated professions. They are subject to strict ethical rules set out in the French Commercial Code and in professional rules established by the French Minister of Justice.

To prevent any potential conflict of interests, the French Commercial Code prohibits judicial administrators and creditors' representatives from practicing another profession or from engaging in any commercial activities.

The ethical rules applicable to judicial administrators and creditors' representatives are based on the following principles:

- independence – regardless of the circumstances, the insolvency practitioner must act with complete independence. He or she must point out any conflicts of interests and refuse missions if it cannot be guaranteed that he / she will act with independence;
- professional secrecy – this rule ensures the absolute confidentiality of discussions;
- financial security – insolvency practitioners are required to:
  - join the AJMJ Guarantee Fund (which protects third parties from the consequences of their civil liability as well as from the non-repayment of the funds entrusted to them);
  - use a dedicated and approved accounting software programme (to ensure transparency in the use of these funds); and
  - have their accounts certified by a statutory auditor twice a year;
- a behaviour adapted to the stakes – insolvency practitioners are required to perform these duties "with dignity, independence, probity, humanity, loyalty and confraternity in keeping with their oath"; and
- ongoing control and monitoring by the national council of judicial administrators and creditors' representatives.

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

For the past 10 years, banks have offered sustainable finance instruments, including green loans and sustainability-linked loans or ESG-linked loans, in order to adapt the financing to social environmental objectives. The ESG-linked loans incorporate mechanisms which provide that the price evolves according to the borrower's performance in ESG terms.

There are two main types of sustainable financing instruments:

- financing dedicated to sustainable projects – the proceeds of the investment or financing are used solely to finance projects with environmental benefits (green bonds / loans), social benefits (social bonds / loans) or both environmental and social benefits (sustainability bonds / loans). This is currently the main type of sustainability financing in the public bond market; and
- sustainability-linked financing (also called sustainability-linked loans, ESG KPI, ESG-linked, ESG adjusted or ESG-ratchet loans / bonds) – the proceeds of financing are used for general corporate purposes, but there is a contractual commitment to meet sustainability performance targets with an indexation of the cost of debt depending on whether or not these are met. The borrower's interest rate can be adjusted up or down depending on whether the sustainability performance targets are fulfilled. This is the main type of sustainable financing on the bank credit and private debt markets.

The first recorded issuances of ESG-linked loans are reported to have taken place in 2017. Considerable freedom is left to the borrower and lenders to determine the terms under which the interest rate will be affected by the achievement of sustainable goals.

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

The Central Bank of France (*Banque de France*) has for many years pursued a policy of social and environmental responsibility (or ESG), translated into concrete actions that contribute to its corporate strategy.

The desire to expand the social responsibility approach has led to the implementation of a strengthened governance structure, and as part of the *Banque de France's* new strategic plan, an ESG strategy for the period 2021-2024 has been defined with action and exemplarity as its watchwords. Its social responsibility approach is structured around four priority areas formalised in an ESG Charter, being:

- action for the preservation of the environment;
- action for the inclusion of human resources and collaborative initiatives;
- action as a sponsor in areas that echoes its missions; and
- investments and purchases for a sustainable economy.

As the Central Bank of France, this encourages other banks to also pursue an ESG policy.

Most of the French banks have developed a code of conduct and ethics to ensure customer interest, employer responsibility and social responsibility.

### 5.3 Promoting ESG by the central bank and regulators

As noted, the Central Bank of France promotes and supports ESG.

Additionally, the banking regulator in France called the ACPR (*Autorité de Contrôle Prudentiel et de Régulation*) supervises banking and insurance activities.

As an active member of the Supervisors Network for Greening the Financial System, launched by the *Banque de France*, the ACPR participates in discussions on the supervision of climate risks and the identification of macroeconomic and financial channels through which these risks could affect the financial system, in particular the banking and insurance sectors.

The ACPR regularly publishes non-binding ESG guidelines to encourage the dissemination of good practices in both: (i) institutions that, due to their business model which is less sensitive to the risks associated with climate change, started later than others; and (ii) more "advanced" institutions that would like to improve their governance system and strengthen operational implementation. These guidelines should be read in conjunction with the guidelines of the European Banking Authority and the European Central Bank, but also those of the Central Banks and Supervisors Network for Greening the Financial System, the Basel Committee on Banking Supervision and the Financial Stability Board.

# GERMANY

# 1. General overview of the restructuring regime

## 1.1 Formal restructuring procedures

There are several possibilities within the German legal framework for restructuring to take place in a court of law. The approach taken depends on the goal sought to be achieved regarding the restructuring of the company. Either the aim is to retain only the actual operations of the company without ensuring the integrity of the legal entity, or to restructure it and keep the legal entity intact.

The setting for these restructuring endeavours is provided by the Insolvency Code[1] or the StaRUG.[2] The Insolvency Code provides for a broad approach which allows for all options. On the downside, it requires much more oversight from the insolvency court over the proceedings. The StaRUG, on the other hand, provides for a soft-touch approach regarding the powers of the management of the company and its publicising. The downside of these proceedings are restricted powers in restructuring debts.

Further changes are to be expected by the continuous harmonisation of the insolvency law within the European Union (e.g. pre-pack proceedings).[3]

### *1.1.1 Insolvency proceedings*

The German Insolvency Code provides for several approaches in restructuring a company. Either the economic value that is the legal entity of the company can be retained, or the operations of the company can be preserved.

In general, the Code is divided into preliminary proceedings and substantive proceedings.

During the preliminary proceedings, the insolvency court is assessing the possibility of commencing the substantive proceedings and takes all necessary steps to retain the status quo regarding the assets of the company. This, most of the time, encompasses the issuing of a far-reaching moratorium, which prevents all creditors of the company from enforcing their rights. Also, most of the time if the operations of the company are continued, the insolvency court will appoint a preliminary insolvency administrator, which will significantly impede the ability of management to exercise its powers. However, it is also possible to take a debtor in possession approach in these proceedings.

If the grounds for insolvency are met and the costs of the proceedings are guaranteed, the court will issue an order commencing the proceedings and will either appoint an insolvency administrator or confirm the debtor in possession approach.

- **Standard insolvency proceedings**

  If a company is insolvent, insolvency is impeding, or the company is over-indebted, the standard insolvency proceeding is applicable. The court appoints an insolvency administrator who takes over the operations of the company. In general, the administrator either liquidates the assets of the company or sells the company itself in an asset or share deal. But it is also feasible that an insolvency plan (discussed below) is used to restructure the company and retain the legal entity.

- **Debtor in possession**

  On the motion of the company to commence a debtor in possession proceeding, the court might issue such an order and appoint a trustee to control the debtor. An application by the

1 Insolvenzordnung.
2 Gesetz über den Stabilisierungs- und Restrukturierungsrahmen für Unternehmen/Act on the Stabilisation and Restructuring of Businesses.
3 Proposal of new insolvency directive harmonising certain aspects of substantive law on insolvency proceedings by the European Commission, https://commission.europa.eu/document/549e7545-092d-4f63-a22d-a591ebda1d42_en.

company must include several documents, such as a finance plan and a concept for the realisation of the proceedings. And it may only be issued in case of an impending insolvency or the over-indebtedness of the company. If the company is already insolvent, debtor in possession proceedings are not applicable.

In general, this proceeding culminates in an insolvency plan.

- **Insolvency plan**

  The insolvency plan is theoretically applicable in each of the aforementioned proceedings. It is possible to restructure the claims of the creditors, the secured claims and subordinated claims. Also, the rights of the shareholders can be affected if the plan provides for it.

  To be accepted, the plan must be approved by the creditors which are put into groups, such as employees and suppliers. To achieve this, the plan must be accepted by the majority of the creditors in a voting meeting, and they must represent more than half of the claims of the creditors voting. If this cannot be accomplished, a cross-class cram down is possible if:

  - the plan is not putting creditors in a situation that is worse than the alternative;
  - the creditors are participating in an adequate manner in the economic value provided by the plan; and
  - the majority of all groups that participate in the voting process have accepted the plan with the necessary votes.

  The insolvency court must confirm the insolvency plan and should consult the insolvency administrator or the trustee, the company and the creditors' committee if one has been appointed. Objections by the parties affected must be filed at the latest in the voting meeting.

  The implementation of the plan is either monitored by the insolvency administrator or the trustee.

### *1.1.2 Restructuring proceedings*

The StaRUG came into force on 1 January 2021 and provides a light touch debtor in possession proceeding (the restructuring proceeding, or *restrukturierungsverfahren*) which has the goal to retain the economic value that is represented in the legal entity of the company. The main prerequisite for such a proceeding is that the entity which is to be restructured faces impending insolvency. If the entity is already insolvent, the restructuring proceeding is not applicable. While insolvency proceedings have to be publicised, a restructuring proceeding is only published if the company requests it.

The restructuring court[4] may in general appoint a restructuring official (*restrukturierungsbeauftragter*) who reports on the proceedings to the court but has no real influence on them. Only in limited cases is the appointment of such an official mandatory, for example if the rights of consumers are to be affected.

The main tool of these proceedings to restructure the debts of the company is the restructuring plan (*restrukturierungsplan*), which allows for the restructuring of some of the debts. Certain debts – wage claims, claims arising from tort and fines – are excluded from being targeted by such a plan. Furthermore, the restructuring court is able to issue a moratorium on enforcing claims against the company. The moratorium might only be targeted towards claims that can be affected by the plan.

To prevent the impossibility of achieving the goals of the restructuring plan, the court may issue a far-reaching moratorium to protect the assets of the company.

[4] The Bundesländer / German states have determined centralized courts for these kinds of proceedings, e.g. the restructuring courts for Bavaria are in Munich, Nuremberg and Bamberg.

To come into effect, the plan must be voted on. Therefore, the creditors that are subjected to the plan are divided into groups (e.g. one group for creditors with rights to separate satisfaction and another group for shareholders). The plan generally must be accepted by all groups. Within each group, at least 75% of the members must accept it. If this quorum is not achieved, there is the possibility of a cross-class cram down if:

- the plan is not putting the creditors in a situation that is worse than the alternative;
- the creditors are participating in an adequate manner in the economic value provided by the plan; and
- the majority of all groups have accepted the plan with the necessary votes. If only two groups have been formed, the acceptance of one group is sufficient.

The restructuring plan can be approved by the restructuring court if the company makes an application to the court. But this is not required for the plan to take effect (discussed below). The major risk of not obtaining a court order is that the stipulations of the plan can be the target of insolvency avoidance.

If the plans deem so, the implementation of the plan is monitored by the restructuring official.

### 1.2 Informal restructuring procedures

In general, informal restructuring proceedings can either be handled out of court, as a consensual agreement between the parties effected, or the rules of the StaRUG can be used to structure such a process. In the latter case, the plan can be agreed upon in the same way as a plan that has been confirmed by the restructuring court (see above). But any doubts concerning the plan are to the expense of the company.

## 2. Restructuring of ESG-related liabilities

In general, all claims against the company have to be handled the same as insolvency or restructuring claims. There are no preferential rights, and each claim can be the target of the provisions of a restructuring (unless otherwise specified) or an insolvency plan.

Environmental and social liabilities may be based on civil claims in tort or in contract. They may also be based on statutory liabilities. If they are based on a statute, the liabilities cannot be restructured to relieve the company of its subsisting statutory obligations post-restructuring.

Another aspect which has to be taken into account is the unpredictability of the law and regulations of the EU and the interaction with German law. For example, the Court of Justice of the European Union (CJEU) ruled in 2021 (C-665/19 P) that claims of the relevant governmental authorities regarding illegal subsidies under European Law can be enforced against the new company that was acquired by another company in an asset deal. This view – that a new legal entity is liable for the repayment of subsidies that the original legal entity received contrary to EU regulations – runs contrary to principle of equal treatment of insolvency claims. Even if this legislation is not directly applicable to a restructuring case, in which the legal entity is retained, it is more than doubtful that these claims can be restructured the same way as other claims or can be affected by a cross-class cram down.

### 2.1 Environmental (E): restructuring environmental liabilities

As mentioned above, environmental liabilities cannot be restructured to relieve the company of its ongoing or subsisting statutory or contractual obligations.

However, it is possible in an insolvency proceeding to disclaim onerous property. For example, a piece of real estate that is subject to continuing and onerous environmental obligations can be disclaimed simply by the relevant declaration of the insolvency administrator to the responsible corporate bodies of a company (the board of directors in case of a joint stock corporation, and the board of management in case of a GmbH / limited liability company). There is no recourse for this body to take against such a decision by the administrator.

Furthermore, the insolvency administrator can declare the non-entry into continuing contractual obligations to relieve the company of such a liability.

The restructuring proceeding of the StaRUG does not provide for such a possibility.

### 2.2 Social (S): restructuring health or safety-related liabilities

The restructuring of health or safety-related liabilities is possible if they are not the subject of ongoing or subsisting statutory or contractual obligations. The insolvency administrator can also declare the non-entry into continuing contractual obligations to relieve the company of such a liability.[5]

The restructuring proceeding of the StaRUG does not provide for such a possibility.

### 2.3 Governance (G): third party releases in favour of directors and officers of the company

Third parties can receive releases of liability under a restructuring plan. However, the releases are subject to certain limitations and requirements. For example, releases must be fair and reasonable, must not prejudice the interests of creditors, and must be approved by the court overseeing the restructuring proceeding. The releases can be granted in exchange for financial contributions to the restructuring plan, or in recognition of other valuable services provided to the restructuring effort. It is important to note that releases are only possible in the context of a restructuring or insolvency plan and cannot be granted as part of a formal insolvency proceeding.

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

#### *3.1.1 Approving a restructuring plan*

A restructuring or insolvency plan does not have to be approved by any environmental protection authority or advocacy group if they are not themselves creditors affected by it.

#### *3.1.2 Discretion to consider wider public interest concerns*

It might be argued that the environmental legalisation in Germany demands that the restructuring / insolvency courts take these public interests regarding environmental protection and the protection of natural resources into account. But there is no formal venue for stakeholder participation in a restructuring / insolvency plan beyond involvement as creditors.

#### *3.1.3 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

In general, there is no formalised involvement of environmental protection authorities or environmental advocacy groups beyond their involvement either as creditors or insofar as they are able to affect any other company in its day-to-day operations.

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[5] It is important to note that such a declaration is not possible in the case of labour contracts. These contracts require a notice of termination. The only change permitted by insolvency law is the reduction of the maximum notice period to three months.

### 3.2 Social (S): influence by the labour authorities, unions or employee / worker advocacy groups in a restructuring

#### *3.2.1 Approving a restructuring plan*

The interests of employees must be taken into account in a restructuring / insolvency plan insofar as the employee representative bodies have to be involved according to the Works Constitution Act (*Betriebsverfassungsgesetz - BetrVG*).

#### *3.2.2 Discretion to consider wider public interest concerns*

The restructuring / insolvency court does not have to consider the wider public interest into account when approving the plan. The fairness test focuses solely on the rights of the creditors.

#### *3.2.3 Protection of employee rights*

A restructuring plan protects the rights of employees, insofar as it cannot affect wage claims.

An insolvency plan must be voted on by the employees.

### 3.3 Governance (G): board / management conflicts addressed in a restructuring

Conflicts arising because of benefits granted in the restructuring / insolvency plan to the board / management of the targeted company may be handled in a number of ways.

One way to handle these potential conflicts is to check the provisions of the plan according to the fairness test.[6]

Furthermore, these benefits might by balanced by taking into account the interests of the other stakeholders, such as employees in relation to the payment of their outstanding benefits.

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

There are no industry guidelines and / or best practices prescribed for the protection of the environment in a restructuring.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

The "Verband Insolvenzverwalter und Sachwalter Deutschlands e. V" (VID) (Registered Association of Insolvency Administrators), as Germany's professional association of insolvency administrators, has published its guidelines on insolvency and debtor in possession proceedings. These guidelines stipulate that the employees of the company have to be informed immediately and continuously on the proceedings and that they are to be instructed especially in relation to their rights to receive insolvency payments.

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

According to the guidelines on insolvency and debtor in possession proceedings of the VID, administrators and trustees have to disclose conflicts of interests in relation to the proceedings as soon as possible, even if they could only give the appearance that the administrator or trustee was not impartial or independent in the sense of the law.

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6 Specifically: (i) the plan is not putting the creditors in a situation that is worse than the alternative; and (ii) the creditors are participating in an adequate manner in the economic value provided by the plan.

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

ESG-linked financial products are being offered by a number of German financial institutions. The Commerzbank AG and the DZ Bank have issued green bonds, while Deutsche Bank AG offers green loans. Furthermore, there are also German asset management firms and funds that have been established to focus on investing in companies that have strong environmental, social and governance performance, such as DWS, Allianz Global Investors and Unions Investment. Finally, the Kreditanstalt für Wiederaufbau (KFW), which issues most of the loans granted by the German Government, ties the granting of such loans to ESG goals.

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

Some German banks have committed to align their lending activities with the goals of the Paris Agreement on Climate Change. For example, the Commerzbank AG announced in 2019 that it will no longer finance coal-fired power plants and Deutsche Bank AG announced such a move in 2020. Some German asset managers have also committed to achieving ESG targets in their investment portfolios. For example, Allianz Global announced in 2019 that it would become carbon neutral by 2023 and would achieve a net-zero emissions portfolio by 2050[7] and DWS announced that it would invest EUR 20 billion in sustainable infrastructure by 2025.

These goals are in line with the EU's action plan on sustainable finance and the EU taxonomy for sustainable activities.

### 5.3 Promoting ESG by the central bank and regulators

The European Central Bank (ECB) has been actively promoting sustainable finance. It appointed a task force in 2019 which published a report on sustainable finance in 2020. The report included recommendations for how the ECB and other authorities could encourage sustainable finance. In 2022, it published its climate agenda for 2022 and 2023.

Additionally, the German Central Bank (the Deutsche Bundesbank) has actively been promoting sustainable finance. It has been working to develop a framework for assessing the environmental and social impact of bank lending. The Bundesbank is also a member of the Network for Greening the Financial System.

On a regulatory level, BaFin has been encouraging financial institutions to disclose information on their exposure to environmental and social risks and published a guide in2020 on integrating ESG risks into investment decision-making. This guide has been updated as recently as 2022.

The German Government has also been working to develop tax incentives for sustainable investment and has been encouraging companies to disclose information on their environmental and social risk exposure. It has committed itself to achieve the UN Sustainable Development Goals for 2030.

[7] In 2021 (Allianz Fact Sheet March 2021), the goal of achieving carbon neutrality was postponed to 2050.

# GUERNSEY

# 1. General overview of the restructuring regime

## 1.1 Formal restructuring procedures

### *1.1.1 Arrangements and reconstructions (SS.105-112 Companies (Guernsey) Law, 2008)*

The Companies (Guernsey) Law, 2008 (Law) includes provisions for "schemes of arrangement", being a compromise or arrangement between a company and its creditors (or any class of creditors) or its members (or any class of members). In an insolvency situation, a scheme of arrangement can be initiated by a liquidator or administrator.

The process involves either the company, a creditor or member, the liquidator or administrator of a company or the receiver of a cell of a protected cell company (Applicant) presenting a compromise or arrangement to the company's creditors (or any class of creditors) or its members (or any class of members). The Applicant will produce a statement explaining the effect of the compromise or arrangement, including the impact on any debenture holders. The Applicant will apply to court to order the convening of meetings of creditors (or a class of creditors) or members (or a class of members), to enable them to vote on the compromise or arrangement. If a majority of 75% in value of creditors (of class of creditors) or members (or class of members) votes in favour, the court may then sanction the arrangement. The court will consider whether the majority is acting in good faith and in the interests of creditors or members, and whether the different interests of creditors or members are such that they should be treated as belonging to a different class of creditors or members. A compromise or agreement sanctioned by the court is binding on all creditors (or class of creditors) or all members (or class of members), the company, the liquidator, the administrator and any receiver.

The existing management would typically remain in control of the company during a scheme of arrangement (unless of course an administrator, liquidator or receiver is already appointed and is the Applicant), with the process being overseen by the court.

### *1.1.2 Administration (SS.374-390 Companies (Guernsey) Law, 2008)*

The Law includes provisions for administration, which is used as a "rescue process" in Guernsey. It is a more common process in Guernsey than a scheme of arrangement.

Administration applies to a company (or cell of a protected cell company) that is insolvent or likely to become insolvent, and where the court considers that an administration may achieve the survival of the company as a going concern and / or a more advantageous realisation of the company's assets. An application for administration can be made to the court by the company, the directors of the company, any member of the company, any creditor, the Guernsey Financial Services Commission or a liquidator of the company. Following the period after presentation of an application, no resolution may be passed to wind up the company and no proceedings may be commenced or continued against the company except with leave of the court. On the making of an administration order, any application for winding up of the company shall be dismissed and during the administration period, no resolution may be passed to wind up the company and no proceedings may be commenced or continued against the company.

The administrator shall, upon appointment, take into their custody or control all property of the company and shall manage the affairs, business and property of the company.

## 1.2 Informal restructuring procedures

While it is possible for a company to agree to an informal restructuring plan with creditors or members, there is no guideline for such a process in Guernsey.

# 2. Restructuring of ESG-related liabilities

## 2.1 Environmental (E): restructuring environmental liabilities

### 2.1.1 *Types of environmental liabilities*

The Environmental Pollution Law (Guernsey) 2004 states the obligations all parties must adhere to under prescribed law. Although there is no separate restructuring provision in company law, there are criminal liabilities that are incumbent on company directors for committing offences against this law.[1]

Where an offence under the law is committed by a body corporate or is proven to be committed with the consent or connivance of, or is attributable to neglect on the part of, a director, that director will be guilty of the offence and proceedings will commence.

### 2.1.2 *Priority given to environmental liabilities*

There is no priority given to environmental liabilities in Guernsey.

### 2.1.3 *Disclaimer of environmental obligations*

It is possible for liquidators in Guernsey to disclaim onerous property with effect from 1 January 2023.

Onerous property includes any personal property of a company, or any property situated outside of the Bailiwick of Guernsey which is unsaleable or not readily saleable or is such that it may give rise to a liability to pay money or perform any other onerous act. An interested party objecting to a disclaimer may apply to the Guernsey court.

## 2.2 Social (S): restructuring health or safety-related liabilities

There is no precedent or prevailing law for allowing health and safety liabilities to be restructured at present.

### 2.2.1 *Types of health and safety-related liabilities*

The Health and Safety at Work Law, enacted by the States of Guernsey, governs an employer's responsibility in the workplace.[2]

### 2.2.2 *Treatment of health and safety-related liabilities*

There is no precedent or prevailing law for allowing health and safety liabilities to be restructured at present, and these liabilities would not receive any special priority.

## 2.3 Governance (G): third party releases in favour of directors and officers of the company

If an arrangement and reconstruction is successfully implemented under the law then this will as a consequence provide a third party release in favour of directors and officers of the company, on the basis that the arrangement or reconstruction will avoid an insolvency process such as administration or liquidation and therefore will avoid any investigations into the affairs of the company and its directors and officers by an administrator or liquidator.

# 3. Protection of stakeholders' interests

## 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

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1 The Environmental Pollution (Guernsey) Law 2004.

2 States of Guernsey Health and Safety Executive – Health and Safety at Work Law (1979).

### *3.1.1 Approving a restructuring plan*

See the discussion in section 1 above.

### *3.1.2 Discretion to consider wider public interest concerns*

The law relating to arrangement and reconstruction does not include any provisions regarding wider public interest concerns. The court has a discretion as to whether to sanction an arrangement and reconstruction, but in exercising this discretion, the primary focus is on the financial interests of creditors.

### *3.1.3 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

There is no specific influence able to be exerted by these entities.

## 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

There is no specific influence, however the court has discretion as to whether to sanction an arrangement and reconstruction.

### *3.2.1 Approving a restructuring plan*

The court has a discretion as to whether to sanction an arrangement and reconstruction and it could consider employees' interests.

### *3.2.2 Discretion to consider wider public interest concerns*

There is no specific influence, however the court has discretion as to whether to sanction an arrangement and reconstruction.

### *3.2.3 Protection of employee rights*

Employee claims have preferential status in insolvency matters. In an arrangement and reconstruction, employees would likely form a separate class of creditors for the purpose of voting on the arrangement and reconstruction. Furthermore, the court will specifically take account of the interests of the various classes of creditors in deciding to whether to sanction an arrangement and reconstruction.

## 3.3 Governance (G): board / management conflicts addressed in a restructuring

The arrangement and reconstruction process in Guernsey does not address any issues of conflict regarding the board / management. The arrangement might propose the issuing of shares, depending on the circumstances. The existing management would typically remain in control of the company during a scheme of arrangement (unless of course an administrator, liquidator or receiver is already appointed and is the Applicant), with the process being overseen by the court.

The Guernsey Financial Services Commission (GFSC) provides a Code of Corporate Governance for the Finance Sector.[3] The Code sets out various responsibilities directors and the company have in terms of governance, accountability, conduct and ethics.

The section on ethics states:

- boards should establish, implement and maintain an effective conflicts of interest policy which sets out standards of expected behaviour, including, among other matters, the treatment of non-compliance with the policy;

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[3] Guernsey Financial Services Commission (GFSC) Code of Corporate Governance – Finance Sector, February 2016.

- directors have a duty to avoid, manage or minimise conflicts of interest and should, wherever possible, arrange their personal and business affairs to avoid direct and indirect conflicts of interest; and
- directors have a fiduciary duty to act in the best interests of the company.

The governance section of the Code states:

- the board should have a clear governance structure which reflects the demands and complexities of the company's business environment, strategy, company values, standards, risk appetite, internal controls and key policies; and
- the board should collectively comprise an appropriate balance of skills, knowledge and competence, considering its members' relevant experience.

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

There is no specific guidance, best practice or precedent for applying law regarding the protection of the environment in a restructuring.

The States of Guernsey have an Environment and Infrastructure Committee. However, there is no evidence of this Committee being involved in a restructuring process.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

The States of Guernsey provide an employment relations portal of documents which governs many aspects of employment, and the responsibility of employers.[4]

There is a specific section for "handling redundancy", which details inadmissible reasons for redundancy and also offers practical guidance to employers, employees, trade unions and employee representatives. Employers should follow a checklist of procedures before finalising plans. In particular:

- if there is a trade union or employees' association, it should be consulted and kept informed of the situation;
- employees should be consulted over proposals to put in place a redundancy when these proposals are still at the formative stage;
- employees should be given adequate information and time to comment or make representations prior to any decision to dismiss being taken;
- employers should thoroughly consider any representations from employees before making any decisions; and
- notes should be kept of any meetings and discussions concerning redundancy.

[4] https://www.gov.gg/employmentrelations.

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

Under the law, there are no restrictions on who can be appointed as a liquidator or administrator in Guernsey. Unlike many other modern jurisdictions (such as England and Wales and Jersey), there is currently no register of approved insolvency practitioners and no requirement for licensing, professional membership, qualifications, residency or any form of insurance.

However, in relation to court appointments, the court will approve the appointment of the office holders and will typically expect them to be experienced and qualified professional insolvency practitioners. Such practitioners may therefore be members of a recognised professional body (such as the Institute of Chartered Accountants in England and Wales), which will have its own guidance on professional ethics and codes of conduct.

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

75% of assets of regulated funds in Guernsey are managed or administered by firms adopting the UN Principles of Responsible Investment (PRI).[5] Additionally, the GFSC has launched the world's first green fund product, which provides a trusted and transparent product for investor access to green investment. The jurisdiction is also a member of the UN Financial Centres for Sustainability Network (FC4S).

Results of a recent survey show 64% of investment managers and fund administrators have seen increased interest in ESG, 93% are aware of Guernsey green finance initiatives and 85% are aligned, or are planning to be aligned with, ESG principles.

Currently, Guernsey's green finance sector is worth £5 billion, with plans to increase this to £56 billion by 2040. This allows Guernsey to have an outsized influence on the sector.

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

The biggest theme within Guernsey funds has been ESG investing, following on from the launch of the GFSC green fund product. Following this, The International Stock Exchange (TISE) created a sustainable finance sector, as well as a transition offering.

The sector as a whole has overwhelmingly responded to the transition and its financing, with investors looking favourably upon this.

### 5.3 Promoting ESG by central banks and regulators

As noted above, the GFSC has been market-leading in adopting the principles of the UN PRIs as well as launching the first green fund product in 2018, which continues to grow.

The GFSC continues to develop a green approach and demonstrate its commitment to develop climate finance through regulatory tools and support of the finance sector in its transition.

The GFSC is engaged with international regulators in order to develop awareness, understanding and capabilities on how to respond to climate-related risks, and continues to contribute to the development of standards.

As noted above, the GFSC is a member of FC4S, but also holds contributory memberships to:

- the Network for Greening the Financial System (NGFS);
- the Taskforce for Nature-Based Financial Disclosures Forum (TNFD);

[5] ESG, Green and Sustainable Investing report, Guernsey Green Finance, 2022.

- the Sustainable Insurance Forum (SIF); and
- IOSCO.

The GFSC will continue to promote and develop activity in this space.

# HONG KONG

## 1. General overview of the restructuring regime

### 1.1 Formal restructuring procedures

The primary court procedure for restructuring debts in Hong Kong is a scheme of arrangement.[1] This is a court-approved compromise or arrangement as between the company and its members and / or creditors or any classes thereof.

In a debt restructuring context, a scheme of arrangement requires:

- the agreement of a majority in number representing at least 75% in value of the creditors (or each class of creditors) present at the creditors' meeting and voting in person or by proxy;[2] and

- approval by the court.[3]

A scheme of arrangement may be proposed by either the company itself or any of its creditors.[4] If the company is being wound up, the scheme can only be proposed by the liquidator or provisional liquidator.[5]

The scheme of arrangement process itself does not provide for a moratorium against creditor actions while the arrangement proposal is being formulated. As creditor actions are automatically stayed when provisional liquidators are appointed,[6] this is often considered as a step-in conjunction with the scheme in order to create a *de facto* moratorium.

There are three stages in the process by which a scheme between a company and its creditors (or a class of creditors) may become binding on dissentients.

First, there must be an application to the court for an order that one or more meetings of the creditors be summoned. The application is made by the company *ex parte*. Second, the proposals must be put to the meeting or meetings, before being considered and approved by a majority in number representing 75% in value of the claims of those present and voting in person or by proxy. Third, if approved by the requisite majority, the court may sanction the proposals, though it is not bound to do so.[7] The court is usually slow to differ from the majority view, as it normally acts on the principle that businessmen are much better judges of what is in their commercial advantage than the court.[8] In an international case, the court also considers whether there is sufficient connection between the scheme and Hong Kong, and whether the scheme is effective in other relevant jurisdictions.[9]

The court may sanction a scheme which is subject to conditions provided that:

- the court does not act in vain;

- the condition is not one which leaves a discretion to a third party to take some steps in order to render the scheme effective;[10] and

- there is clarity and certainly on the face of the scheme and there is no further decision-making process.

1 Companies Ordinance (Cap 622), Part 13 Division 2.
2 *Idem*, s 674.
3 *Idem*, s 673.
4 *Idem*, ss 670(3), 673(3).
5 *Idem*, ss 670(4), 673(4).
6 Companies (Winding Up and Miscellaneous Provisions) Ordinance, s 186.
7 *UDL Argos Engineering & Heavy Industries Co Ltd & Others* [2001] 3 HKLRD 634 at [12].
8 *Re Allied Properties (HK) Ltd* [2020] HKCA 973.
9 *China Singyes Solar Technologies Holdings Ltd* [2020] HKCFI 467 at [7].
10 *Hong Kong Airlines Limited* [2022] HKCFI 3792 at [27].

The party putting forward the scheme has to provide the background and explain the reason for proposing the scheme, identify the proposed classes of creditors and provide any other information the court requires to be able to give directions on convening meetings. This information is provided in the form of an affidavit and a draft explanatory statement and timetable.

The explanatory statement must contain all the information necessary to enable the creditors to form a reasonable judgment on whether the scheme is in their best interests, and hence how to vote.[11] The explanatory statement must state any material interests of the company's directors (whether as directors or as members or creditors of the company or otherwise) and the effect of the arrangement or compromise on those interests.[12] The extent of the information required to be provided will depend on the facts of the particular case. The explanatory statement has to provide creditors with sufficient information about the scheme and its effects, and this is best gauged by a comparison of a creditor's position before and after the scheme.[13]

Creditors are required to be placed into proper classes and separate meetings are required for each class. Where there are different classes of creditors, each of the classes has to reach the requisite majority in order for the scheme to be approved by the court. An incorrect classification of the classes may be challenged at the sanction hearing and will mean the scheme is not approved by the court. The test for classification of classes is based on similarity or dissimilarity of legal rights against the company, not on similarity or dissimilarity of interests not derived from such legal rights.[14] It is the responsibility of the applicant putting forward the scheme to decide whether to summon a single meeting or more than one meeting.[15]

There is also a court application by a liquidator to compromise particular debts of the company with the sanction of either the committee of inspection or the court,[16] which is likely wide enough to encompass an arrangement that could have been the subject of a scheme. This route can only be used when there is no alteration or variation in the rights of the creditors (i.e. the *pari passu* method of distribution) as a result of the proposal.[17]

### 1.2 Informal restructuring procedures

Informal out of court restructurings are conducted primarily on a consensual basis and are not specifically governed by any legislation. Non-statutory guidelines known as the "Hong Kong Approach to Corporate Difficulties" issued jointly by the Hong Kong Association of Banks (HKAB) and the Hong Kong Monetary Authority (HKMA) (HKAB / HKMA Guidelines) provide guidance on a successful workout. Although compliance with the HKAB / HKMA Guidelines is not mandatory, it is strongly supported by the HKAB and HKMA, and all members of the HKAB are expected to use their best endeavours to follow them on the basis that they represent accepted practice of the banking community in Hong Kong.[18] The underlying principles of the HKAB / HKMA Guidelines[19] are:

- when it becomes generally known that a borrower may be experiencing financial problems, banks' initial attitude should be one of support. They should endeavour to ensure the borrower has sufficient liquidity to continue trading until a considered view of its prospects can be reached;
- further decisions should only be made based on reliable information and shared fully with all banks;

[11] *Da Yu Financial Holdings Limited* [2019] HKCFI 2531 at [39].
[12] Companies Ordinance (Cap 622), s 671(3).
[13] *Re Kansa General Insurance Co Ltd* [1999] 2 HKLRD 429 at 437I to 438A.
[14] *UDL Argos Engineering & Heavy Industries Co Ltd & Others* [2001] 3 HKLRD 634 at [26].
[15] *Idem* at [27].
[16] Companies (Winding Up and Miscellaneous Provisions) Ordinance, section 199(2) and Part 1 of Schedule 25.
[17] *Re Moulin Global Eyecare Holdings Ltd & Ors (in liq)* [2007] 2 HKC 486.
[18] HKAB / HKMA Guidelines, Introduction.
[19] *Idem*, Underlying Principles.

- the decision to offer the borrower financial assistance should generally be a collective one by banks; and
- all banks act in a cooperative and expeditious manner in order to agree a restructuring plan.

Out of court restructurings are also common for bond restructurings. This can be done by obtaining the bondholders' consent to swap outstanding bonds for new bonds with different terms, for example a haircut on the principal amount, an extension of the maturity date and / or a change in the coupon terms. As out of court restructurings are based on noteholders' voluntary participation, the debtor company will have to pay dissenting / holdout noteholders for the full sums due. Hence, the minimum participation condition threshold in the bond documentation is usually set at a high level (85% by value or above) to avoid holding out noteholders.

## 2. Restructuring of ESG-related liabilities

### 2.1 Environmental (E): restructuring environmental liabilities

All persons having pecuniary claims against the company, whether actual or contingent, are treated as creditors, and their claims are capable of being included as relevant claims in a scheme of arrangement.[20] Environmental liabilities should therefore be capable of being restructured in the same way as ordinary liabilities of a company.

There are no specific restrictions or conditions that apply when restructuring environmental liabilities.

#### *2.1.1 Types of environmental liabilities*

Environmental liabilities under Hong Kong law include:

- civil claims such as claims in contract[21] and claims in tort;[22] and
- statutory liabilities such as:
  - fines – which may be imposed for various statutory offences under Hong Kong legislation, such as discharging waste, polluting matter or poisonous or noxious matter into the waters of Hong Kong in a water control zone,[23] allowing vessels within Hong Kong waters to emit smoke more than the statutory prescribed time,[24] manufacturing, importing or exporting prohibited substances which deplete the ozone layer without a license,[25] unauthorised use of land or premises for the disposal of waste,[26] failure to dispose of chemical waste with a license or deliver them to a prescribed reception point,[27] or carrying out construction work outside the statutory prescribed time or not in accordance with the conditions of a construction noise permit;[28] or
  - remediation / clean-up costs – for example, under the Dumping at Sea Ordinance (Cap 466), where the Director of Environmental Protection is satisfied that dumping or incineration at sea has occurred outside the scope of a permit, the Director may do anything reasonably necessary to protect the marine environment and prevent interference

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20 *Re Universal Dockyard Ltd* [2004] 1 HKLRD 935 at [39] to [41].
21 For example, a tenant under a lease agreement may be subject to contractual obligations to remove waste products from the leased premises, not to cause pollution, or generally to comply with all environmental regulations.
22 For example, a party may be liable under the tort of nuisance, the tort of negligence or the common law rule of *Rylands v Fletcher* if it causes damage or pollution to other party's land.
23 Water Pollution Control Ordinance (Cap 358), s 8.
24 Shipping and Port Control Ordinance (Cap 313), s 50.
25 Ozone Layer Protection Ordinance (Cap 403), s 4.
26 Waste Disposal Ordinance (Cap 354), s 16.
27 Waste Disposal (Chemical Waste) (General) Regulation (Cap 354C), s 8(5).
28 Noise Control Ordinance (Cap 400), s 6.

with other legitimate uses of the sea.[29] The Director is entitled to recover expenses reasonably incurred in carrying out his / her actions from such persons who have been convicted of an offence in consequence of the act or omission which made it appear to the Director to be necessary to carry out the actions.[30]

There is generally no distinction as to how the various types of environmental liabilities are treated under a scheme. There is no express prohibition in the legislation against restructuring fines under a scheme and it is likely that statutory liabilities are susceptible to be restructured under a scheme.

### *2.1.2 Priority given to environmental liabilities*

Certain liabilities may be given priority treatment under a proposed scheme if they would have priority in liquidation. Environmental liabilities do not in general fall within any of the statutorily-prescribed categories of preferential debts which receive priority in a liquidation.[31] Environmental liabilities may possibly be classified as secured for priority debts where:

- they fall within the scope of statutory debts the liability and amount of which are determined by or under any provision in any Ordinance;[32]
- they are secured by a charge, mortgage or other form of security interest (for example, in a finance transaction a lender takes a mortgage over a borrower's land); or
- the liabilities can be categorised as part of the expenses of the provisional liquidation / receivership.[33]

### *2.1.3 Disclaimer of environmental obligations*

While a scheme can in principle restructure environmental liabilities, it does not relieve a company of its ongoing or subsisting statutory or contractual obligations post-restructuring.

A liquidator / provisional liquidator may apply to the court to disclaim onerous property.[34] Usually, the most common cases are leasehold or unsaleable land property.[35] In principle, onerous property could include property such as a plant or a factory which is subject to continuing and onerous environmental obligations that are to be performed over a substantial period of time and which will involve expenditure that may not be recovered.[36] Persons interested in the property may make an application requiring the liquidator to decide whether he / she will disclaim. The liquidator shall not be entitled to disclaim the property if he / she does not disclaim within 28 days from the date of the application or such further period as the court may allow.[37]

The extent to which the disclaimer of onerous property may be used to relieve a company of its statutory environmental obligations is uncertain, given there are no Hong Kong case authorities on this issue. The likely issues are whether environmental licenses are treated as property of a

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29 Dumping at Sea Ordinance (Cap 466), s 23(1).
30 *Idem*, s 23(2).
31 Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap 32), s 265.
32 *Idem*, ss 265(1)(d), 265(6). Statutory debts are usually referred to tax liabilities.
33 For example, a landlord is entitled to full payment of rent ahead of other creditors from a tenant which is being wound up if the premises are being used "for the convenience of the winding up" (*Halkirk Co. Ltd v Carrian Holdings Ltd* [1985] HKLR 21).
34 Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap 32), s 268.
35 *Re Tan & Sons Co Ltd* [2003] 3 HKC 648.
36 While there is no case authority in Hong Kong directly on this point, s 268 provides that "Where any part of the property of a company which is being wound up consists of land of any tenure burdened with onerous covenants, of shares or stock in companies, of unprofitable contracts, or of any other property that is unsaleable, or not readily saleable, by reason of its binding the possessor thereof to the performance of any onerous act, or to the payment of any sum of money."
37 Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap 32), s 268(4).

company, and the tension between the polluter pays principle in environmental law[38] and the interests of creditors in an insolvency proceeding.[39]

## 2.2 Social (S): restructuring health or safety-related liabilities

Similar to the restructuring of environmental liabilities, health or safety-related liabilities can be restructured under a scheme in the same way as ordinary liabilities of a company. All persons having pecuniary claims against the company, whether actual or contingent, are treated as creditors, and their claims are capable of being included as relevant claims in a scheme of arrangement.[40] There are no special restrictions or conditions that apply when restructuring health or safety-related liabilities.

### *2.2.1 Types of health and safety-related liabilities*

Health and safety liabilities under Hong Kong law include:

- civil claims such as claims in contract[41] and claims in tort;[42] and
- statutory liabilities such as:
  - fines – for example, selling food or drugs unfit for human consumption (an offence under section 54 of the Public Health and Municipal Services Ordinance (Cap 132)) and the failure to maintain a workplace in a condition that is, so far as reasonably practicable, safe and without risks to health (an offence under section 6 of the Occupational Safety and Health Ordinance (Cap 509)); and
  - remediation costs – for example, under the Public Health and Municipal Services Ordinance (Cap 132), the Director of Food and Environmental Hygiene may serve a notice requesting the owner of a premises which is in a state injurious or dangerous to health to cleanse or disinfect the premises. Where the owner fails to comply with any of the requirements under the notice, the Director may execute any work necessary to remedy the situation and recover any expenses thereby incurred from the recipient of the notice.[43]

### *2.2.2 Treatment of health and safety-related liabilities*

There is generally no distinction as to how the various types of health or safety-related liabilities are treated under a scheme. There is also generally no express prohibition under the legislation against restructuring fines under a scheme and it is likely that statutory liabilities are susceptible to be restructured under a scheme. Health and safety-related liabilities may possibly be classified as secured for priority debts where:

- the amounts are due in respect of work injury compensation under the Employees' Compensation Ordinance (Cap 282);[44]

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38 Which is adopted in Hong Kong's environmental policies, e.g. sewage service charges.

39 There are conflicting English and Scottish decisions: *Re Mineral Resources Ltd* [1999] 1 All ER 746, *Re Celtic Extraction Ltd* (in liquidation) [1999] 4 All ER 684, *Doonin Plant Limited* [2018] CSOH 89 and *Dawson International* [2018] CSOH 52.

40 *Re Universal Dockyard Ltd* [2004] 1 HKLRD 935 at [39] to [41].

41 For example, a party that supplies defective or unsafe goods may be liable for breach of an express term of the contract or the implied term that the goods are of merchantable quality under s 16 of the Sale of Goods Ordinance (Cap 26).

42 For example, a party may be liable under the tort of negligence when it manufactures goods or supplies services where a duty of care arises. For example, in the case of *Lam Mo Bun v Hong Kong Aerosol Co Ltd & Others* [2001]1 HKLRD 540, the manufacturer of insecticide spray was held liable for injuries from an explosion after use as there was inadequate labelling and instructions.

43 Public Health and Municipal Services Ordinance (Cap 132), s 14.

44 Which is a preferential debt in a winding up pursuant to ss 265(1)(cb) and 265(ce) of the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap 32).

- they fall within the scope of statutory debts the liability and the amount of which are determined by or under any provision in any Ordinance;[45]
- they are secured by a charge, mortgage or other form of security interest (for example, in a finance transaction where a lender takes a mortgage over a borrower's land); or
- the liabilities can be categorised as part of the expenses of the provisional liquidation / receivership.[46]

### 2.3 Governance (G): third party releases in favour of directors and officers of the company

It is possible for a scheme to provide for third party releases, on the condition they are necessary in order to give a scheme efficacy.[47]

Third party releases have been allowed to release guarantees of the debt sought to be compromised in the scheme given by associated companies of a debtor company.[48] Courts have also permitted the release of a principal obligor's liability where the debt compromised in the scheme is that of a guarantor.[49] A deed of contribution is not required for a guarantor's scheme in Hong Kong to discharge debts owed by the principal obligors.[50]

The precise extent to which third party releases are allowed in favour of directors and officers of the company is not clear in Hong Kong.

There are no reported decisions in Hong Kong directly on third party releases granted in favour of directors and officers of the company. However, it has been explained in obiter[51] that a scheme may also release any claims or purported claims by the scheme creditors against other third parties, including directors, legal advisors, financial advisers and various other intermediaries. As the release of a third-party right is only permissible if it is required to give efficacy to the scheme, it would not be permissible for a company to include releases that are not necessary and to allow third parties associated with the company to escape from unrelated liabilities.[52]

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

#### *3.1.1 Approving a restructuring plan*

There is no requirement for a scheme to be approved by environmental protection authorities or environmental advocacy groups. A scheme is only required to be approved by creditors and the court.

#### *3.1.2 Discretion to consider wider public interest concerns*

There is no case law in Hong Kong concerning the extent to which the court may consider environmental issues in deciding whether to approve a scheme. However, it is to be noted that the approval process for a scheme primarily focuses on the rights and interests of creditors and does not include a wider public interest assessment.

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[45] Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap 32), ss 265 (1)(d) and 265(6).

[46] For example, a landlord is entitled to full payment of rent ahead of other creditors from a tenant which is being wound up if the premises are being used "for the convenience of the winding up" (*Halkirk Co Ltd v Carrian Holdings Ltd* [1985] HKLR 21).

[47] *Century Sun International Limited* [2021] HKCFI 2928 at [19].

[48] *China Singyes Solar Technologies Holdings Limited* [2020] HKCFI 467, *Century Sun International Limited* [2021] HKCFI 2928.

[49] *Unity Group Holdings International Limited* [2022] HKCFI 3419.

[50] *Idem* at [17].

[51] *Century Sun International Limited* [2021] HKCFI 2928 at [18], citing the English decision of *Re Lecta Paper UK Ltd* [2021] 1 BCLC 511.

[52] *Idem* at [19], citing the English decision of *Re Lehman Brothers International (Europe)* [2010] BCC 272.

#### *3.1.3 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

There are no statutory provisions which grant environmental protection authorities or environmental advocacy groups standing to air their views or concerns in a restructuring.

### 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

#### *3.2.1 Approving a restructuring plan*

There is no requirement for a scheme to be approved by labour authorities, unions or employee / worker advocacy groups. A scheme is only required to be approved by creditors and the court.

#### *3.2.2 Discretion to consider wider public interest concerns*

There is no case law in Hong Kong concerning the extent to which the court may consider labour issues in deciding whether to approve a scheme. However, the fairness and reasonableness determination made at the scheme approval stage primarily focus on the rights of creditors and does not incorporate a wider assessment of the employees' interests. It is also made clear in case law[53] that individuals holding divergent views based on their private interests not derived from their legal rights against the company is not a ground for calling separate meetings in voting on a proposed scheme.

#### *3.2.3 Protection of employee rights*

There are no statutory provisions which grant labour authorities, unions or employee / worker advocacy groups standing to air their views or concerns in a restructuring.

### 3.3 Governance (G): board / management conflicts addressed in a restructuring

As noted in section 1 above, material interests of the company's directors (whether in their capacity as directors or members or creditors of the company or otherwise) are required to be disclosed in the explanatory statement concerning a scheme.[54]

If the directors or management personnel are receiving shares or options pursuant to a management incentive plan or options scheme, these matters would very likely have to be disclosed in the explanatory statement, to enable the creditors to form a reasonable judgment on whether the scheme is in their best interests or not.

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

We have not identified any industry guidelines and / or best practices prescribed for the protection of the environment in a restructuring.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

The Labour Department has issued "Guidelines on What to Do if Wage Reductions and Retrenchments are Unavoidable" (LD Guidelines). The LD Guidelines set out the recommended practice of employers and what employees can do when wage reductions or retrenchments are unavoidable.

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53 *UDL Argos Engineering & Heavy Industries Co Ltd & Others* [2001] 3 HKLRD 634 at [26]-[27].

54 Companies Ordinance (Cap 622), s 671(3).

For example, the LD Guidelines recommend the following on retrenchments:

- employers should ensure the retrenchment criteria are objective, fair, non-punitive and non-discriminatory;[55]
- employers should ensure the termination package is no less favourable than that provided in the Employment Ordinance (Cap 57) and the employment contract;[56]
- to soften the blow of retrenchment, and to demonstrate additional support for people being forced to change jobs, employers should also try to be as generous as possible with ex-gratia payments;[57]
- employers should clearly explain all the details, and the methods of calculation, to each retrenched employee whatever the final payment decided upon;[58]
- employers should give each employee a reference on an organisation letterhead certifying that the retrenchment had to be made because of circumstances beyond the organisation's control and was unrelated to the performance of the employee to facilitate the employee being able to seek a new job;[59] and
- employers should make clear to retrenched employees that once the organisation's situation returns to normal, all retrenched employees would be given priority in future recruitment.[60]

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

The Hong Kong Institute of Certified Public Accountants (HKICPA) has issued a Code of Ethics for Professional Accountants in the HKICPA Members' Handbook. Part E, section 500 of the HKICPA Members' Handbook specifically deals with professional ethics in liquidation and insolvency (HKICPA Ethics Code). The HKICPA Ethics Code extends to insolvency practitioners acting as "administrator, manager, adjudicator or any other similar role, however described in respect of a scheme of arrangement between a company and its creditors".[61]

Professional accountants are required to comply with the five fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour.[62] The HKICPA Ethics Code provides a framework which insolvency practitioners can use to identify actual or potential threats to compliance with the fundamental principles and determine whether there are any safeguards that may be available to mitigate them.[63]

Examples are provided in the HKICPA Ethics Code as guidance to insolvency practitioners as to when they should accept appointments, including those related to restructuring work.

It is generally accepted that a liquidator or a provisional liquidator of an insolvent company may normally accept an appointment as administrator, manager or adjudicator of a scheme of arrangement of an insolvent client provided he / she is satisfied there are no circumstances that give rise to an unacceptable threat.[64]

Other than appointment as a liquidator or provisional liquidator, practitioners should not accept an appointment as administrator, manager or adjudicator of a scheme of arrangement of an insolvent client where there has been a significant professional relationship with a client (e.g.

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55 LD Guidelines, para 3.7.1.
56 *Idem*, para 3.7.2.
57 *Idem*, para 3.7.3.
58 *Idem*, para 3.7.4.
59 *Idem*, para 3.7.5.
60 *Idem*, para 3.7.6.
61 Professional Ethics in Liquidation and Insolvency, HKICPA Members' Handbook, para 500.4(b).
62 *Idem*, para 500.4(b).
63 *Idem*, para 500.9.
64 *Idem*, para 500.91.

audit-related work). The restriction may not apply to situations which clearly do not impair, and would not be perceived as impairing, the practitioner's objectivity. This may occur in situations where the scheme assets and liabilities are substantially different from the assets and liabilities of the company that was previously audited.[65]

The HKICPA Ethics Code does not carry the force of law.

In relation to hard law, there is no comprehensive statutory or legislative instrument governing conflict of interests for restructuring professionals. However, there are the following restrictions or requirements imposed by specific statutory provisions and case law:

- persons nominated as liquidators or provisional liquidators of an insolvent liquidation are required to make a disclosure statement as to certain relationships with the company and their reasons for believing that such relationships would not result in having a conflict of interest or duty;[66]

- liquidators should not only be independent and impartial but should also be seen to be so. Any conflict of interests or even over-familiarisation should be discouraged. On the other hand, it is not every connection or action that can give rise to an allegation of an appearance of lack of independence and impartiality on which the court should act;[67]

- liquidators may obtain funding from creditors or third parties to pursue litigation, but in the process the liquidators should remain in control of the intended litigation and should not surrender their independence in any way;[68] and

- the professional fees in a scheme must be disclosed in the explanatory statement, with a detailed breakdown to allow the court and the scheme creditors to assess the reasonableness of the costs.[69] The court may sanction the scheme on the condition that all the restructuring and other expenses be subject to taxation and any cost savings resulting therefrom be distributed to the scheme creditors.[70]

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

Many banks in Hong Kong have launched ESG / sustainability financing programmes or ESG / sustainability linked loans for eligible environmentally sustainable green projects, or for corporate funding to improve sustainability performance targets.[71]

The Hong Kong Government has launched a Government Green Bond Programme (GGBP) up to a maximum principal amount of HK $200 billion.[72] As a core component of the programme, the Green Bond Framework sets out how the Hong Kong Government intends to issue green bonds under the GGBP to fund new financing or the refinancing of green projects that are consistent with its vision to improve the environment, combat climate change and transition to a low carbon economy.[73]

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

Most banks in Hong Kong have an international footprint and have signed on to commitments to achieve ESG targets. For example, HSBC has joined the UN-convened Net Zero Banking Alliance

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65 *Idem*, para 500.85.
66 Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap 32), ss 262C and 262D.
67 *Re Akai Holdings Ltd & Another* [2001] 2 HKLRD 411 at [421 A-B].
68 *Idem* at [422 G-I] and HCCW 386 of 2006 judgment dated 8 October 2015 at [8].
69 *Da Yu Financial Holdings Limited* [2019] HKCFI 2531 at [39]-[44].
70 *Idem* at [44].
71 Banks which have reported issuing such loans include BOCHK, HSBC and Hang Seng Bank.
72 Hong Kong Government Green Bond Programme - Overview (hkgb.gov.hk).
73 Hong Kong Government Green Bond Programme - Framework (hkgb.gov.hk).

as a founding member and is a member of the Equator Principles. Banks in Hong Kong with a more focused local presence are likewise active in achieving ESG targets. For instance, the Bank of East Asia Limited focuses on ESG risk management and sets targets on green lending, while Hang Seng Bank Limited has set targets on carbon neutrality.

### 5.3 Promoting ESG by the central bank and regulators

The Hong Kong Monetary Authority (HKMA) has undertaken various efforts to promote ESG financing, including by:

- developing a common assessment framework on Green and Sustainable Banking to assess the "greenness baseline" of individual authorised institutions;[74]

- conducting pilot climate risk testing to assess the climate resilience of the banking sector as a whole and facilitate capability building of participating banks and banking practitioners for managing climate risks;[75] and

- engaging in or supporting various international and regional collaborations, such as the Principles for Responsible Investment, the Central Banks and Supervisors Network for Greening the Financial System and the Task Force on Climate-Related Financial Disclosures.

Further, the Hong Kong Exchanges and Clearing Limited (HKEx) first introduced the ESG Reporting Guide in 2013 in the Listing Rules and since then has continued to upgrade the disclosure obligations of listed issuers. The ESG Reporting Guide comprises two levels of disclosure obligations: "mandatory disclosure requirements" and "comply or explain" provisions on 12 aspects of environmental and social issues.

The SFC has issued circulars on disclosures relating to ESG funds[76] and to also require fund managers that are managing collective investment schemes to take climate-related risks into consideration in their investment and risk management processes and make appropriate disclosures.[77]

In May 2020, the Green and Sustainable Finance Cross-Agency Steering Group (CASG) was set up and is co-chaired by HKMA and the Securities and Futures Commission (SFC), with members such as the Environment Bureau. The CASG aims to coordinate the management of climate and environmental risks in the financial sector, accelerate the growth of green and sustainable finance in Hong Kong and support the Government's climate strategies.[78] The CASG has, to date:

- launched its green and sustainable finance strategy for Hong Kong and five key action points;[79]

- published its preliminary feasibility assessment of carbon market opportunities for Hong Kong;[80] and

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74 HKMA Press Release (13 May 2020), accessible at: Common Assessment Framework on Green and Sustainable Banking (hkma.gov.hk).

75 HKMA Press Release (30 December 2021), accessible at: Hong Kong Monetary Authority - HKMA Publishes the Results of the Pilot Climate Risk Stress Test.

76 SFC Circular to Management Companies of SFC-Authorised Unit Trusts and Mutual Funds – ESG Funds (29 June 2021).

77 Circular to Licensed Corporations: Management and Disclosure of Climate-Related Risks by Fund Managers (20 August 2021).

78 HKMA Press Release (5 May 2020), accessible at: Hong Kong Monetary Authority - Joint Statement on the Establishment of the Green and Sustainable Finance Cross-Agency Steering Group (hkma.gov.hk).

79 HKMA Press Release (17 December 2020), accessible at: Hong Kong Monetary Authority - Cross-Agency Steering Group Launches its Strategic Plan to Strengthen Hong Kong's Financial Ecosystem to Support a Greener and More Sustainable Future (hkma.gov.hk).

80 HKMA Press Release (30 March 2022), accessible at: Hong Kong Monetary Authority – Cross-Agency Steering Group Releases Assessment of Carbon Market Opportunities for Hong Kong and Next Steps (hkma.gov.hk).

- administered a three-year pilot scheme known as the “Pilot Green and Sustainable Finance Capacity Building Support Scheme” to provide subsidies for the training and acquisition of relevant professional qualifications in sustainable finance as part of a collaborative effort to build capability for the industry.

Additionally, the HKMA published on 30 December 2021[81] a section on climate risk management in its supervisory policy manual to provide guidance to authorised institutions on the key elements of climate-related risk management, and to set out the HKMA's approach to, and expectations in, reviewing authorised institutions' climate-related risk management in line with the CASG's strategic plan.

[81] GS-1: Climate Risk Management.

# INDIA

# 1. General overview of the restructuring regime

## 1.1 Formal restructuring procedures

### *1.1.1 Corporate insolvency resolution process*

The main procedure for restructuring in India – the corporate insolvency resolution process (CIRP) – is prescribed under the Insolvency and Bankruptcy Code 2016 (IBC) and the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations 2016 (CIRP Regulations).

The CIRP for a corporate debtor can be initiated before the national company law tribunal (NCLT) having territorial jurisdiction over the place where the registered office of the corporate person is located, upon non-payment of debts. The minimum amount of default for the initiation of a CIRP is INR 1 crore (approximately US $120,720). The CIRP against a corporate debtor can be initiated by a financial creditor, operational creditor (i.e. trade creditors, employees / workmen and governmental authorities) or the corporate debtor itself, upon there being a default as mentioned above.

Significantly, with the initiation of the CIRP under the IBC: (i) the board of directors of the corporate debtor stands suspended and its powers are exercised by an interim resolution professional (IRP) (akin to an administrator) under the scrutiny of a committee of creditors (COC); and (ii) a moratorium is declared.[1] During the continuation of the moratorium, the following actions are prohibited:

- the institution of suits or continuation of pending suits or proceedings against the corporate debtor, including the execution of any judgment, decree or order in any court of law, tribunal, arbitration panel or other authority;
- transferring, encumbering, alienating or disposing by the corporate debtor of any of its assets or any legal right or beneficial interest therein;
- any action to foreclose, recover or enforce any security interest created by the corporate debtor in respect of its property; and
- the recovery of any property by an owner or lessor where the property is occupied by or in the possession of the corporate debtor.

The CIRP under the IBC must be completed within 330 days,[2] although this timeline is amenable to extension and is usually exceeded.[3]

The COC generally comprises the unrelated financial creditors of the corporate debtor and its consent by 66% value of debts is required for key decisions with respect to the corporate debtor, including any sale of assets, incurring insolvency costs and importantly approving a resolution plan. The IBC also provides that a CIRP may be withdrawn with a vote of 90% of the COC.[4]

The IBC requires the approval of a resolution plan – otherwise, the corporate debtor must be liquidated. For the most part, "connected parties" are not permitted to participate. Resolution plans can include provisions for restructuring the corporate debtor by way of merger, demerger or amalgamation – other than simply share acquisitions – although there is still some ambiguity on whether a demerger or asset sale is possible.

A resolution plan generally respects the following insolvency waterfall: insolvency costs, secured creditors at par with priority workmen and employee dues, secured financial creditors, unsecured financial creditors, unsecured trade creditors, statutory dues and then remaining unsecured

1 IBC, s 14.
2 *Idem*, s 12.
3 *Essar Steel India Limited v Satish Kumar Gupta and Ors* (2020) 8 SCC 531.
4 IBC, s 12A.

creditors. However, recent decisions have enhanced the standing of statutory dues[5] and certain forms of employee dues.[6] Even so, some decisions of the bankruptcy court permit the COC, in its commercial wisdom, to alter the senior-junior security interests of financial creditors on the ground that this alteration is required to revive the corporate debtor as a going concern.[7] Once a resolution plan is approved, trade creditors and dissenting financial creditors are required to be paid their distributions under the plan in priority in time to others.[8] Unsecured financial creditors presently rank ahead of unsecured trade creditors. This distinction is unique to India and is sought to be reversed through legislative amendments under discussion.

The commercial wisdom of the COC is supreme and the power of the NCLT to interfere in commercial decisions taken is limited to grounds such as the resolution plan being in violation of applicable law.

From the date of approval of the resolution plan by the NCLT, the IBC absolves the corporate debtor from liability for pre-CIRP offences (such as anti-bribery violations) committed by the erstwhile management of the corporate debtor.

The IBC also provides that a corporate debtor is to be liquidated if:

- the COC cannot agree on a workable resolution plan within the period of the CIRP;
- the COC decides to liquidate the corporate debtor during the period of the CIRP;
- the NCLT rejects the resolution plan; or
- the corporate debtor contravenes the provisions of a resolution plan that has been approved by the NCLT.

Under the liquidation process, a liquidator can realise amounts for the payment of creditors by way of, *inter alia*:

- the sale of piecemeal assets;
- the sale of undertakings or businesses of the corporate debtor on a going concern basis; or
- the sale of the corporate debtor itself as a "going concern".

#### *1.1.2 Pre-pack*

In India, recently the Pre-Packaged Insolvency Resolution Process (PPIRP) for micro, small and medium-sized enterprises (MSMEs) was introduced.[9] The minimum threshold for initiating a PPIRP is INR 10 lakh (approximately US $12,072). The PPIRP provides the "best of both worlds", by combining elements such as speed, efficiency and flexibility of an informal process with the binding effects and structure of a formal process under the aegis of the NCLT.

### 1.2 Informal restructuring procedures

The primary regime for informal out of NCLT restructuring in India is under the circular issued on 7 June 2019 by the Reserve Bank of India – namely, the Prudential Framework for Resolution of Stressed Assets (7 June Framework).

5 *State Tax Officers v Rainbow Papers Limited* (Supreme Court order dated 6 September 2022).
6 *Jalan Fritsch Consortium v Regional Provident Fund Commissioner & Anr* (Supreme Court order dated 30 January 2023).
7 *K Sashidhar v Indian Overseas Bank & Ors* (Supreme Court order dated 19 March 2019) and *Jaypee Kensington Boulevard Apartments Welfare Association & Ors v NBCC (India) Ltd & Ors* (Supreme Court order dated 24 March 2021).
8 *Jaypee Kensington Boulevard Apartments Welfare Association & Ors v NBCC (India) Ltd & Ors* (Supreme Court order dated 24 March 2021).
9 Introduced by Act No. 26 of 2021, s 8 (w.e.f. 4 April 2021).

The 7 June Framework addresses a number of issues that had plagued its predecessor regimes. Among other things, it lays down the framework for the execution of an inter-creditor agreement (ICA) which can serve as the framework for lenders to act jointly for agreeing a mechanism to address default and a consequent resolution plan or enforcement action.

The 7 June Framework has proved to be an important tool for debtors and their promoters to resolve stress without the spectre of the IBC. This framework allows for several different ways in which stress may be resolved, including restructuring and one-time settlement. Similar to the IBC, for the full benefits of the 7 June Framework, often times a complete change in ownership is required (i.e. no connected party sales). However, there are several workarounds where sponsors can retain ownership and, practically, this is how the 7 June Framework has been mostly used.

The 7 June Framework does not cover several important categories of lenders who may easily feature in the list of creditors of a company – foreign lenders, foreign portfolio investors, mutual funds, PF trusts and liabilities such as those of trade creditors, which cannot be restructured under the 7 June Framework. Therefore, there is a strong possibility of holdouts.

Under the 7 June Framework, the decision of a majority of lenders (75% by value and 60% by number) is binding on the entire lender class of the debtor. However, dissenting lenders are required to be paid their liquidation value.

## 2. Restructuring of ESG-related liabilities

### 2.1 Environmental (E): restructuring environmental liabilities

There is lack of clarify as far as the restructuring of environmental liabilities is considered within the IBC, though it can be argued these liabilities (such as fines and penalties) can be restructured under a resolution plan in the same way as ordinary trade and statutory liabilities of a company.[10] However, not all liabilities of a company under Indian law can be restructured and extinguished. For example, India follows the principle of "absolute liability" when dealing with extremely hazardous waste or "inherently dangerous" activity,[11] and it is quite likely that a court would find that such "absolute liability" (whether presently due or contingent in nature) cannot be restructured under a resolution plan.

The concept of absolute liability is inherently a no-fault liability concept, which makes an entity liable when dealing with extremely hazardous waste or inherently dangerous activity, even if there is no negligence on its part. This principle was first practically examined and applied by the Supreme Court in the "*Oleum Gas Leak Case*".[12] In that case, Mr MC Mehta filed a petition before the Supreme Court for closing the manufacturing activities of Shriram Foods and Fertilisers, as it was producing hazardous substances and was located next to a heavily populated area in Delhi. During the pendency of the case, one of the units operated by Shriram Foods and Fertilisers leaked oleum gas and caused severe damage (including injuries) to the local population. The Supreme Court emphasised that the principle of absolute liability would be applied when an entity is "carrying on inherently dangerous activities".

The Supreme Court also noted that the rule of absolute liability is stricter than the rule of strict liability and does not allow any exceptions to the liability arising out of inherently dangerous activities carried out by an entity. According to this rule, once the activity carried on is hazardous or inherently dangerous, the person or entity carrying on the activity is liable to make good the loss caused to any other person by the activity irrespective of whether reasonable care was taken while carrying on the activity.

The principle of "absolute liability" further gained recognition from the Supreme Court and was reaffirmed in the "Bhopal Gas Tragedy Case",[13] in which a factory operated by Union Carbide

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10 IBC, s 53(1)(e).

11 *M.C. Mehta v Union of India* (Supreme Court order dated 20 December 1986); *Union Carbide Corporation v Union of India* (Supreme Court order dated 3 October 1991).

12 *M.C. Mehta v Union of India* (Supreme Court order dated 20 December 1986).

13 *Union Carbide Corporation v Union of India* (Supreme Court order dated 3 October 1991).

Company in Bhopal led to a major leakage and resulted in deaths of over 3000 people from the leakage. The Supreme Court held that an entity engaged in inherently dangerous activities will have absolute liability. The Bhopal gas leak also led to the enactment of the "Public Liability Insurance Act 1991", which makes it mandatory for entities engaged in handling hazardous substances to take insurance. The objective of the legislation is to provide public liability insurance, with the aim of offering swift assistance to individuals or persons affected by accidents occurring while handling any hazardous substance and for matters connected therewith or incidental thereto.

It is pertinent to note that as far as the resolution regime under the IBC is concerned, the principle of "absolute liability" in relation to a company undergoing insolvency proceedings is untested, given the IBC is still fairly nascent.

Nevertheless, as noted above, it is quite likely a court would find that "absolute liability" (whether presently due or contingent in nature) cannot be restructured under a resolution plan and a bidder may have to price in such a liability in its bid and / or provide compensation as and when such a liability arises.

India also follows the principle of "polluter pays" – that is, the entity that pollutes the environment must pay to reverse the damages caused by its acts. Indian courts have previously directed companies to pay and compensate for damages caused due to their activities,[14] including compensation, and have even required the relocation of concerned factories. It cannot be ruled by the court that, post-acquisition of a corporate debtor under the IBC, a bona fide buyer is to make good claims by way of compensation arising from the actions of previous management.

Given the IBC is still fairly nascent (enacted in 2016), there is lack of clarity and precedents on these issues.

### 2.1.1 *Types of environmental liabilities*

Environmental liabilities under Indian law could encompass:

- civil claims; and
- statutory liabilities, such as:
  - fines – may be imposed for various statutory offences under the Environment (Protection) Act 1986[15] (EPA 1986), the Air (Prevention and Control of Pollution) Act 1981[16] (Air Act) and the Water (Prevention and Control of Pollution) Act 1974[17] (Water Act).. These include the failure to maintain air pollution control equipment on industrial or trade premises, the discharge of untreated trade effluents, oil, chemical, sewage or other polluting matters, and the failure to store, use or deal with hazardous substances in such a manner so as not to cause pollution to the environment. In additional to fines and penalties, these statutes also provide penalties in the form of imprisonment, although a bona fide bidder under the IBC could claim protection from such criminal liabilities;[18] and
  - remediation / clean-up costs – for example, under the Air Act, the relevant pollution control board has the power to direct closure of a premise or regulate any operation.[19]

### 2.1.2 *Priority given to environmental liabilities*

As mentioned above, there is lack of clarity under Indian insolvency law regarding the treatment of certain environmental liabilities, though fines and penalties imposed by governmental

14 *Vellore Citizens Welfare Forum v Union of India (UOI) and Ors* (Supreme Court order dated 28 August 1996).
15 EPA 1986, s 15.
16 Air Act, ss 37, 39.
17 Water Act, ss 43-45A.
18 IBC, s 32A.
19 Air Act, s 31A.

authorities would fall within the ambit of operational dues and would have a low ranking under the liquidation waterfall prescribed under the IBC. However, there are exceptions to this. For example, where an enterprise has engaged in a hazardous or inherently dangerous activity, any ensuing harm could, under the principle of "absolutely liability" or "polluter pays", sit outside the insolvency / liquidation waterfall. As noted, however, the scope of this possible exception remains untested.

#### *2.1.3 Disclaimer of environmental obligations*

Disclaimer would be difficult to achieve in a CIRP. The IBC, in the first instance, requires that the corporate debtor must be restructured as a going concern. This means together with all its properties. Therefore, in principle, the CIRP does not allow the disclaimer of a particular property. That said, recently a new provision has been added under which the resolution professional can sell assets of the debtor rather than sell the entire debtor, but only if no bidder comes forth for the entire debtor. In practice, it may be possible that bids are received for non-polluted assets, and the polluted assets would be effectively disclaimed (in substance) and left to liquidation.

Unlike a CIRP, liquidation under the IBC permits the trustee to disclaim onerous property from the debtor's estate without describing whether a polluted property would fall within this category. This remains an untested proposition.

### 2.2 Social (S): restructuring health or safety-related liabilities

Similar to the restructuring of environmental liabilities, health or safety-related liabilities can be restructured under a scheme in the same way as other creditors of a corporate debtor. There are no special restrictions or conditions that apply when restructuring health or safety-related liabilities.

Though the Indian Supreme Court has held that there should be no "hydra heads" (or surprises),[20] it remains unclear whether this extends to liabilities that are yet to crystallise, such as product liability tort claims or asbestos claims which may accrue in the future. While generally resolution plans provide for their whitewash, it is yet to be seen how the NCLTs may treat such liabilities, and it cannot be ruled out that a resolution applicant may be required to pay such claims at a later stage, even though resolution applicants have protections from any criminal liability arising due to such actions under the IBC. Additionally, and more relevant for asbestos claims, the position under "absolute liability" could equally apply here as well, depending on the facts and circumstances of each case.

#### *2.2.1 Types of health and safety-related liabilities*

There is a very wide gamut of such laws. For example, health or safety-related liabilities under Indian law could encompass:

- civil claims from employees and workmen in case of bodily harm or death of an employee or workmen; and
- statutory liabilities such as fines and penalties under the Factories Act 1948,[21] the Petroleum Act 1934[22] and the Occupation Safety, Health and Working Conditions Code 2020.[23] Fines may be imposed for the failure to maintain prescribed safety measures, sub-standard samples, non-maintenance of safety equipment for employees and workmen, exposure to harmful substances, non-maintenance of health or medical records of workers, non-appointment of competent and trained employees and neglect in handling harmful products.[24]

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20 *Essar Steel India Limited v Satish Kumar Gupta and Ors* (2020) 8 SCC 531; *Ghanashyam Mishra and Sons Private Limited v Edelweiss Asset Reconstruction Company Limited and Ors* (2021) 9 SCC 657.
21 Factories Act, ss 41B, 41C, 92, 96.
22 Petroleum Act, s 23.
23 Occupation Safety, Health and Working Conditions Code, s 12.
24 IBC, s 32A.

#### *2.2.2 Treatment of health and safety-related liabilities*

Fines and penalties imposed by government authorities on account of health and safety-related violations would fall within the ambit of operational dues and would receive a low ranking under the liquidation waterfall prescribed under the IBC. There is no special priority prescribed to health and safety related claims under Indian insolvency law.

### 2.3 Governance (G): third party releases in favour of directors and officers of the company

Indian insolvency law does not provide releases to third parties (such as directors) for past breaches committed by them.

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

#### *3.1.1 Approving a restructuring plan*

There is no requirement for a resolution plan under the IBC to be approved by any environmental authority or environmental advocacy group. However, these stakeholders have a say in the underlying project itself. For example, the law may require the approval of the environment protection agency before a project can proceed. The IBC does not, and cannot, disturb this requirement. Thus, if the resolution plan proposes changes to what was originally submitted to the relevant environment protection agency, the consent of that specific regulatory authority will again be required to implement the resolution plan.

#### *3.1.2 Discretion to consider wider public interest concerns*

The IBC is essentially a creditor restructuring tool and tries to restrict the discretion of the NCLT. The NCLTs can only reject a resolution plan if it is in violation of any applicable law (including environmental laws) or does not conform to the payment principles prescribed under the IBC. To this end, an advocacy group could intervene in the resolution plan hearings stating that the business and revival plan envisaged in the resolution does not conform to environmental laws. However, practically, we have not seen this, since it is the duty of the resolution professional as well to ensure the resolution plan complies with environmental laws.

#### *3.1.3 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

There are no statutory provisions which grant environmental protection authorities or environmental advocacy groups standing to air their views in a restructuring.

### 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

#### *3.2.1 Approving a restructuring plan*

There is no requirement for a resolution plan under the IBC to be approved by labour authorities, unions or employee / worker advocacy groups. Only the approval of the NCLT and COC is required for approval of a resolution plan. However, these groups can object to the distribution under the resolution plan if it is not in accordance with the IBC and they can also object on the basis that the resolution plan breaches Indian laws. Given the purpose of the IBC is revival, in practice workmen and employee complaints in resolution plan hearings are given due regard by the NCLT.

#### *3.2.2 Discretion to consider wider public interest concerns*

The NCLT does not have such a power. Under previous laws, plan approval hearings were time consuming.

Therefore, it is a policy prescription under the IBC to curtail the NCLT's discretion. However, as mentioned previously, the resolution professional is required to ensure the resolution plan complies with applicable laws. Therefore, there are enough checks and balances in the process.

#### *3.2.3 Protection of employee rights*

There are no statutory provisions which grant labour authorities, unions or employee / worker advocacy groups standing to air their views in a restructuring. However, as mentioned above, they can object on grounds of the plan not complying with the IBC or applicable laws. Given their importance to the revival of the debtor, NCLTs do give them a reasonable hearing.

### 3.3 Governance (G): board / management conflicts addressed in a restructuring

Under Indian insolvency law, in the case of a CIRP and liquidation, the board of directors and management of the corporate debtor stand suspended, and their powers are vested in the resolution professional (RP), who acts under the supervision of the COC and the NCLT. The erstwhile board of directors and management have no say during the CIRP of the corporate debtor. Further, pursuant to section 29A of the IBC, the erstwhile management or promoter are not permitted to be part of the management or control of the corporate debtor in any manner under a resolution plan. The purpose of section 29A is that management cannot benefit from their own wrongs.

In certain circumstances (such as a PPIRP or where the management is eligible under section 29A), they may bid and retain their position in the debtor. Under the insolvency waterfall, any payments or incentives to them would typically rank bottom of the liquidation / insolvency waterfall.

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

There is no prescribed "soft law" framework for the protection of the environment specifically in the restructuring context. However, general industry guidelines have been prescribed, which may be applicable to corporate entities.

The Confederation of Indian Industry (CII), which is a business association in India, has formulated a voluntary code of conduct[25] for its members, which lays down the following recommendations for organisations in relation to ESG principles:

- as a responsible corporate citizen, the organisation should integrate ESG principles in business;
- the organisation should establish clear policies and systems to conform to the highest standards of moral, ethical, transparent and fair conduct, encourage fair and equitable treatment of all stakeholders and avoid practices like bribery (including receiving bribes), corruption, insider trading, market manipulation and anti-competitive practices; and
- organisations are encouraged to extend their sustainability principles, ethics practices and code of conduct to their supply chain and sourcing partners.

The Ministry of Corporate Affairs (MCA) released the National Guidelines on Responsible Business Conduct[26] (NGRBC) in 2019 as a framework for guiding Indian multinational corporations in their overseas operations, in addition to aligning with applicable local national standards and norms governing responsible business conduct. These principles also capture key international

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[25] Guidelines on Integrity and Transparency in Governance and Responsible Code of Conduct, Confederation of Indian Industry. February 2020. (https://www.cii.in/pdf/CII%20Guidelines%20on%20Integrity%20Transparency%20in%20Governance%20and%20Responsible%20Code%20of%20Conduct_Feb%202020_Final.pdf).

[26] National Guidelines on Responsible Business Conduct, Ministry of Corporate Affairs, Government of India, March 2019. (https://www.mca.gov.in/Ministry/pdf/NationalGuildeline_15032019.pdf).

developments in the sustainable development agenda and business responsibility field such as the UN Guiding Principles for Business and Human Rights, the UN Sustainable Development Goals, the Paris Agreement on Climate Change and Core Conventions 138 and 182 on Child Labour by the International Labour Organisation.

According to the MCA, the NGRBC are designed to be used by all businesses, irrespective of their ownership, size, sector, structure or location, and it is expected that all businesses investing or operating in India, including foreign multinational corporations, follow these guidelines.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

There is no prescribed "soft law" framework for the protection of employee rights specifically in a restructuring context.

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

The Insolvency and Bankruptcy Board of India (IBBI) has laid down a code of conduct for insolvency professionals while undertaking assignments under the IBC, and it has the force of law. The following measures have been provided under the code to avoid any potential conflict of interest:[27]

- insolvency professionals are bound to act with objectivity in their professional dealings by ensuring their decisions are made without any conflict of interest, whether directly connected to the insolvency proceedings or not;
- insolvency professionals are also required to disclose the details of any conflict of interests to the stakeholders, whenever they come across such conflicts during an assignment;
- insolvency professionals have been restricted from acquiring any of the assets of the debtor, whether directly or indirectly;
- in cases where insolvency professionals are dealing with a debtor's assets during liquidation or a bankruptcy process, they are also required to ensure that they or their relatives do not knowingly acquire any such assets, unless it is shown that there was no impairment of objectivity, independence or impartiality in the liquidation or bankruptcy process and the IBBI's approval had been obtained;
- insolvency professionals are also required to disclose the existence of any pecuniary or personal relationship with any of the stakeholders entitled to distribution under the IBC, and the concerned debtor;
- insolvency professionals are required to disclose whether they were employees of or have been in the panel of any financial creditor of the corporate debtor to the committee of creditors and to the insolvency professional agency (IPA) of which they are a professional member;
- insolvency professionals are required to disclose their relationship, if any, with the corporate debtor, other professionals engaged by them, financial creditors, interim finance providers and prospective resolution applicants to the respective IPAs of which they are a member; and
- insolvency professionals are required to ensure disclosure of the relationship, if any, of the other professionals engaged by them, with themselves, the corporate debtor, the financial creditor, the interim finance provider, if any, and the prospective resolution applicant to the IPAs of which they are a member.

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[27] First Schedule, Insolvency and Bankruptcy Board of India (Insolvency Professionals) Regulations 2016. (https://ibbi.gov.in//uploads/legalframwork/213cd7f2c53374800f7cf1e881b58d51.pdf).

As of November 2022, there are three IPAs registered with the IBBI: the Indian Institute of Insolvency Professionals of ICAI, the ICSI Institute of Insolvency Professionals and the Insolvency Professional Agency of Institute of Cost Accountants of India. These IPAs have their own respective codes of conduct which apply to their members, containing measures to avoid conflicts of interest. However, these codes have largely been formulated on the basis of IBBI's code of conduct and contain similar or identical provisions for the avoidance of conflicts of interest.

Additionally, all the IPAs have jointly formulated a statement of best practices concerning the role of insolvency professionals in avoidance proceedings. This statement acts as a guide to all insolvency professionals undertaking the identification of avoidance transactions and filing applications before the NCLT. However, this statement also provides for mostly identical measures as laid down by the IBBI in its code of conduct.

Moreover, the professionals conducting valuation under the IBC (i.e. registered valuers) are also guided by their own code of conduct.[28] This code is also somewhat identical to the IBBI's code of conduct, with some specific measures laid down for registered valuers:

- valuers are prohibited from dealing in securities of any company after they first become aware of the possibility of their association with the valuation; and
- valuers are restricted from taking up any assignment if they or any of their relatives or associates are not independent in terms of association with the debtor.

As of November 2022, there are 16 registered valuer organisations (RVO) registered with the IBBI. Some of these RVOs also have their own respective codes of conduct which apply to their members, containing measures to avoid conflicts of interest. However, these codes have largely been formulated on the basis of code of conduct prescribed for valuers and contain similar or identical provisions for avoidance of conflict of interest.

Therefore, it can be said that by and large, the IBBI's code of conduct is the guiding force behind all the measures enumerated under various instruments, whether having the force of law or not, in relation to preventing any conflict of interest during any restructuring exercises being undertaken under the provisions of the IBC.

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

As of December 2021, a total of 75 Indian issuers had issued green, social and sustainability related bonds amounting to US $19.5 billion in three different currencies. The US $20 million green deal from Nagar Nigam Ghaziabad in 2021 marked the debut of local governments in the Indian green, social and sustainability market.[29] Out of these issuances, as of March 2021, Indian renewable energy developers such as Greenko, ReNew Power, Adani Green Energy, Azure Power, JSW Hydro, Continuum Green Energy, Hero Future Energies and NTPC had issued green bonds to the tune of US $11.2 billion through 21 issuances, with these green bonds providing cost advantages due to favourable hedging costs.[30] Further, as of August 2022, the ESG-related mutual funds in India reached a fund size of INR 11,981 crores (approximately US $1.5 billion).[31] Although this was a decrease from March 2022 when they were valued at INR 12,450 crores (approximately US $1.6 billion), it was an increase almost by a factor of five from INR 2,268 crores (approximately US $270 million) in March 2019.[32]

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28 Annexure – I, Companies (Registered Valuers and Valuation) Rules 2017.

29 S Bhattacharya, N Kumar and P Lonika, "India State of the Market 2021", Climate Bonds Initiative, May 2022.

30 S Garg, R Jain and G Sidhu, "Financing India's Energy Transition Through International Bond Markets, Council on Energy, Environment and Water", August 2021.

31 A Usmani, "ESG Mutual Funds In India Are Having A Reality Check", BQ Prime, 3 October 2022.

32 C Madia, "ESG Funds Rise 5x in Four Years to Rs 12,450 Crore, Shows Data", Business Standard, 24 April 2022.

India also gained a place as the second-largest green bond issuer among emerging markets and developing economies in 2021, with an issuance of US $5.9 billion, wherein most of the proceeds from these bonds were allocated to renewable energy, airport infrastructure and a municipality.[33]

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

The RBI has recently conducted a survey of 34 leading commercial banks regulated by it to assess the status of climate risk and sustainable finance in these banks.[34] This survey provided an overview of proactivity shown by banks in implementing ESG related measures and incorporating ESG in their lending / investment portfolios, some highlights of which are as follows:

- 56% of the surveyed banks had discussed the need to enhance lending or investment towards sustainable finance during the previous and current financial year;
- 32% of the surveyed banks have mobilised new capital to scale up green lending / investment or set a target for incremental lending / investment for sustainable finance;
- 56% of the surveyed banks had decided to gradually reduce their exposure to high carbon emitting / polluting businesses in the coming year;
- 35% of the surveyed banks had initiated discussions with their large corporate borrowers regarding plans to reduce their carbon emissions and had also offered to support them in the process;
- 53% of the surveyed banks had come up with an ESG strategy;
- 79% of the surveyed banks had taken measures to decrease carbon emissions arising from their operations and increase the proportion of renewable energy in their total sourced electricity; and
- 24% of the surveyed banks had announced plans to become carbon neutral, with another 26% intending to do so within the next 12 months.

### 5.3 Promoting ESG by the central bank and regulators

The Finance Minister of India announced in her Budget Speech 2022-23 that as a part of the Government's overall market borrowings in 2022-23, sovereign green bonds will be issued for mobilising resources for green infrastructure and the proceeds will be deployed in public sector projects which help in reducing the carbon intensity of the economy.[35] Accordingly, the Government of India has now brought in a Framework for Sovereign Green Bonds. The proceeds raised from these sovereign green bonds would be used to finance expenditure for eligible green projects falling under categories such as renewable energy, energy efficiency, clean transportation, climate change adaptation, sustainable water and waste management, pollution prevention and control, green buildings, sustainable management of living natural resource and land use and terrestrial and aquatic biodiversity conservation.[36]

The RBI joined the Central Banks and Supervisors Network for Greening the Financial System (NGFS) as a member on 23 April 2021, to benefit from the membership of NGFS by learning from and contributing to global efforts on green finance, and it recently also published the Statement of Commitment to Support Greening India's Financial System.[37] Through this statement, the RBI committed to:

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33 Emerging Market Green Bonds Report 2021, International Finance Corporation, June 2022.
34 Report of the Survey on Climate Risk and Sustainable Finance, Reserve Bank of India, July 2022.
35 Budget 2022-23, Speech of Ms. Nirmala Sitharaman, Minister of Finance, Government of India, 1 February 2022, para 103.
36 File No. 2891146/2022/Finance Unit, Department of Economic Affairs, Ministry of Finance, Government of India, 9 November 2022.
37 RBI Press Release No. 2021-2022/1143, 3 November 2021.

- exploring how climate scenario exercises can be used to identify vulnerabilities in RBI supervised entities' balance sheets, business models and gaps in their capabilities for measuring and managing climate-related financial risks;
- integrating climate-related risks into financial stability monitoring; and
- building awareness about climate-related risks among regulated financial institutions and spreading knowledge about issues relating to climate change and methods to deal with them accordingly.

The Sustainable Finance Group, Department of Regulation at the RBI recently carried out a survey to assess the status of climate risk and sustainable finance in leading scheduled commercial banks and concluded that although banks have begun taking steps in climate risk and sustainable finance, there remains a need for concerted effort and further action in this regard.[38]

Additionally, the Securities and Exchange Board of India (SEBI) has introduced a framework for business responsibility and sustainability reporting by listed entities[39] in 2021 which is based on the National Guidelines on Responsible Business Conduct. This has revised the earlier requirement of providing a business responsibility report, which was laid down by the SEBI in 2012. According to the SEBI, the reporting is intended to have quantitative and standardised disclosures on ESG parameters to enable comparability across companies, sectors and time as such disclosures will be helpful for investors to make better investment decisions. This filing has been made mandatory for the top 1000 listed companies by market capitalisation and is voluntary for the financial year 2021-22.

The SEBI has also introduced the concept of green debt security in its regulations,[40] which define such securities as being those the funds from whose issuance would be utilised for projects or assets falling under categories such as renewable and sustainable energy.

The International Financial Services Centres Authority also recently published a report on sustainable finance.[41] The objective of this report was to recommend a framework to develop a world-class sustainable finance hub at the International Financial Services Centre (IFSC).

38 Report of the Survey on Climate Risk and Sustainable Finance, Reserve Bank of India, July 2022.
39 SEBI Circular No. SEBI/HO/CFD/CMD-2/P/CIR/2021/562, 10 May 2021.
40 Securities and Exchange Board of India (Issue and Listing of Non-Convertible Securities) Regulations 2021, reg 2(q).
41 Report of the Expert Committee on Sustainable Finance, International Financial Services Centres Authority, 3 October 2022.

# INDONESIA

## 1. General overview of the restructuring regime

### 1.1 Formal restructuring procedures

The in-court restructuring procedure known as suspension of debt repayment or *penundaan kewajiban pembayaran utang* (PKPU) is regulated under Law Number 37 Year 2004 concerning Bankruptcy and Suspension of Debt Repayments (Law 37/2004). The application for a PKPU may be filed by the debtor with more than one creditor, or by creditor(s), so that the debtor can propose a reconciliation plan which includes an offer to pay part or all of its outstanding debts.

If an application for a PKPU is submitted by the debtor, the Commercial Court shall, within a maximum period of three days from the date of registration of the application, grant the temporary PKPU and shall appoint a Supervisory Judge and one or more administrator(s) who manage the debtor's property together with the debtor (Temporary PKPU). If the application for a PKPU is submitted by creditor(s), the Commercial Court shall grant the Temporary PKPU within a maximum period of 20 days from the date of the registration of the application letter. The Temporary PKPU will last for 45 days from when the court order is granted (Temporary PKPU Period).

If the reconciliation plan cannot be approved by creditors within the Temporary PKPU Period, the creditors must determine the granting or rejection of a permanent PKPU with a view to enabling debtors, administrators and creditors to consider and approve the reconciliation plan at the next meeting or hearing (Permanent PKPU). The Permanent PKPU shall not exceed 270 days after the decision on the Temporary PKPU has been rendered (Permanent PKPU Period). The granting of the Permanent PKPU shall be determined by the Commercial Court based on:

- approval of more than half of the number of concurrent creditors (unsecured creditors) whose rights are recognised and temporarily recognised, who are present in the court session and who represent at least two thirds of all the recognised claims and their proxies who are present in the court session; and

- approval of more than half of the number of creditors who have their claims secured by lien, fiducial security, mortgage, hypothec, or other collateral rights, who are present in the court session and who represent at least two thirds of all the claims of the creditors or their proxies who are present in the court session.

If the Temporary PKPU Period is over, but the creditors do not approve the Permanent PKPU, or if the Permanent PKPU has been granted but no Reconciliation Plan has been reached, the debtor must be declared bankrupt by the Commercial Court.

During the Temporary PKPU Period or the Permanent PKPU Period, the debtor without approval from the administrator may not perform administrative or ownership actions upon all or part of its property. If the debtor breaches this prohibition, the administrator has the right to do everything necessary to ensure the debtor's property is not harmed due to the actions of the debtor.

During the Temporary PKPU Period or the Permanent PKPU Period, the debtor may not be forced to pay the debt and all acts of execution which have been initiated in order to obtain the settlement of the debt shall be suspended.

The PKPU does not apply to:

- claims secured by lien, fiduciary security, mortgage, hypothec or other collateral rights;

- claims for maintenance, supervision or education costs which have to be paid; or

- privileged claims (e.g. employee claims) for certain assets which are owned by the debtor as well as the entire debtor's property.

The payment of all debts, other than those listed in the preceding paragraph which existed before the PKPU was granted, may not be enforced during the operation of the PKPU unless debt repayment is made to all creditors, according to the balance of their respective receivables.

However, any creditor with an outstanding debt owed to the debtor or receivables outstanding may set off the relevant debts and receivables, provided the debts and receivables or legal actions which give rise to such debts and receivables have occurred prior to the PKPU.

A reconciliation plan can be accepted by creditors based on:

- approval of more than half of the number of concurrent creditors whose rights are recognised and temporarily recognised, who are present in the creditors' meeting, and who represent at least two thirds of all the recognised claims or temporarily recognised claims from the concurrent creditors or their proxies who are present at the meeting; and

- approval from more than half of the creditors who have their claims secured by lien, fiducial security, mortgage, hypothec, or collateral right which are present and represent at least two thirds of all the claims of the said creditors or their proxies who are present at the meeting.

If the reconciliation plan is accepted by the creditors (Reconciliation), the Commercial Court must issue a decision on the validation of Reconciliation along with its reasons. However, the Commercial Court must reject the validation of the Reconciliation if:

- the debtor's property, including assets for which the right to withhold assets is to be exercised, is substantially greater than the amount agreed in the Reconciliation;

- the implementation of the Reconciliation is not sufficiently guaranteed;

- the Reconciliation is achieved due to fraud, or collusion with one or more creditors, or due to the use of other dishonest measures and regardless of whether the debtor or any other parties cooperate to achieve this; and / or

- service fees and costs incurred by experts and administrators have not been paid or there are no guarantees for their payment.

The Commercial Court's decision cannot be challenged. However, the Attorney General may file a cassation against such decision.

If the Commercial Court refuses to validate the Reconciliation, then in the same decision the Court must declare the debtor bankrupt and the decision must be announced in the Official Gazette of the Republic of Indonesia and in at least two daily newspapers within a maximum period of five days after the decision is received by the Supervisory Judge and the Receiver.

The Reconciliation which has been validated shall bind all creditors, except for secured creditors who do not approve the reconciliation plan. The secured creditors who do not approve the reconciliation plan shall be compensated with an amount which is the lower of the collateral value or the actual value of the loan which is directly secured by the collateral right.

### 1.2 Informal restructuring procedures

Informal out of court restructurings are conducted on a consensual basis and are not specifically governed by any laws and regulations. However, the Minister of State Owned Enterprises has issued Regulation of Minister of State Owned Enterprises Number PER-2/MBU/02/2023 regarding Guidelines for the Governance and Significant Corporate Activities of State Owned Enterprises (MSOE Reg. 2/2023).

MSOE Reg. 2/2023 only applies to State Owned Enterprises (BUMN) and one significant corporate activity that has been addressed is "restructuring". According to Article 122 of MSOE Reg. 2/2023, the boards of directors of BUMNs shall submit restructuring proposals to the Minister or general meeting of shareholders for their approval, which should be granted based on the results of reviews of the conditions of the relevant BUMN. The reviews should cover the following aspects at the least:

- financial aspect;

- legal aspect;
- business aspect;
- social aspect;
- organisational / management aspect;
- operational aspect; and / or
- systemic and procedural aspect.

The restructuring proposals that have been approved by the Minister or general meeting of shareholders shall be carried out in accordance with the prevailing laws and regulations.

## 2. Restructuring of ESG-related liabilities

### 2.1 Environmental (E): restructuring environmental liabilities

Law 37/2004 is silent on whether environmental liabilities can be restructured under a reconciliation plan in the same way as ordinary liabilities of a company. In practice, any pecuniary claims against a company may be restructured under a PKPU reconciliation plan.

#### *2.1.1 Types of environmental liabilities*

Environmental liabilities under Indonesian law can encompass the following:

- claims in tort[1] and claims in contract; and
- statutory liabilities, such as:
  - fines. For example, under Law Number 32 Year 2009 concerning Environmental Protection and Management as amended by Governing Regulation in lieu of Law Number 2 Year 2022 concerning Job Creation (Environmental Law),[2] an administrative fine will be imposed, for example, on any person who, due to his / her negligence, commits an act that causes the ambient air quality standard, water quality standard, seawater quality standard or standard criteria for environmental damage to be exceeded in a manner that is not in accordance with his / her business license; and
  - restoration. For example, under the Environmental Law, if the person in charge of the business entity and / or activity fails to restore the marine quality, the Ministry of Environment or governor may appoint a third party to carry out the marine quality restoration at the cost of the person in charge of the business and / or activity.

As mentioned above, Law 37/2004 is silent on whether environmental liabilities can be restructured under a reconciliation plan in the same way as ordinary liabilities of a company.

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1 The Environment Law stipulates the following:
(a) the governmental institutions and regional government in charge of environmental affairs shall be authorised to file litigation for compensation and certain measures against businesses and / or activities causing environmental pollution and / or damage which resulted in environmental loss (article 90 of the Environmental Law);
(b) the public has the right to file a group representative's claim for their own interests and / or the benefit of the public if they suffer losses due to the pollution and / or environmental damage (article 91 of the Environmental Law); and
(c) the environmental organisation has a right to file lawsuit for the sake of preserving environmental functions (article 92 of the Environmental Law).

2 There is other environmental legislation including but not limited to Law Number 41 Year 1999 concerning Forestry as lastly amended by Governing Regulation in lieu of Law Number 2 Year 2022 concerning Job Creation; and Law Number 18 Year 2013 concerning Prevention and Eradication of Forest Destruction as amended by Governing Regulation in lieu of Law Number 2 Year 2022 concerning Job Creation.

However, in practice, any administrative fines against a company may be restructured under a PKPU reconciliation plan.

### *2.1.2 Priority given to environmental liabilities*

In the context of tax debt, the state is qualified as a preferred creditor that has the right of precedence for tax debt on assets belonging to the taxpayer.[3] However, the Constitutional Court has ruled that the payment of workers' wages outweighs all types of claims, including tax debts.

Law 37/2004, the Indonesian Civil Code (ICC), and the Environment Law are silent on whether environmental liabilities are qualified as preferential receivables / preferential debts. However, environmental liabilities can be categorised as state receivables, as defined by Government Regulation in lieu of Law Number 49 Year 1960 concerning State Receivable Affairs Committee (Perppu 49/1960).[4] Unlike tax debts, the category of state receivables in bankruptcy and PKPU is not clear and is still being debated among practitioners.

One may say that state receivables should fall within the category of preferential debts which will receive priority in the settlement of the bankruptcy estate as stated in article 1137 of the ICC.[5] Others disagree with this view because Perppu 49/1960 does not expressly provide that state receivables fall within the category of preferential debts.

Article 160 of Regulation of Minister of Finance Number 240/PMK.06/2016 Year 2016 concerning the Management of State Receivables (PMK 240/2016), as the implementing regulation of Perppu 49/1960, states that "if the debtor and / or debt guarantor are in bankruptcy proceedings at a court, the management of state receivables will still be carried out." Further, article 161 of PMK 240/2016 stipulates that "if the debtor and / or debt guarantor has been declared bankrupt, then the management of state receivables will be carried out with due observance of the provisions under bankruptcy law".

Articles 160 and 161 of PMK 240/2016 can be interpreted such that state receivables cannot be restructured based on a PKPU reconciliation plan because even if the debtor is in a PKPU state or the reconciliation plan has been ratified by the Commercial Court, the Ministry of Finance can still collect state receivables with a forced letter based on Perppu 49 /1960 and PMK 240/2016.

Due to the ambiguity concerning state receivables' position in bankruptcy and PKPU proceedings, whether state receivables are treated as preferential debts will depend on the Supervisory Judge and administrator. In practice, the administrator or receiver initially categorises state receivables as concurrent debts, but the Supervisory Judge may decide to designate state receivables as preferential debts. In some cases, the Supervisory Judge still determines state receivables as concurrent debts. In such cases, the Ministry of Finance may continue to carry out the process of enforcement of state receivables by issuing decrees for determining the amount of state receivables, distress warrants or warrants for confiscation, or by conducting a force body (*gijzeling*).

### *2.1.3 Disclaimer of environmental obligations*

Even though environmental liabilities can be restructured under a PKPU reconciliation plan, this does not mean that the company is free from its obligations to comply with laws and regulations

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3 Article 21 paragraph (1) of Law Number 6 Year 1983 concerning General Tax Provisions and Procedures as lastly amended by Governing Regulation in lieu of Law Number 2 Year 2022 concerning Job Creation (Law 6/1983).

4 Article 8 of Perppu 49/1960 defines state receivable as "the amount of money that must be paid to the state or entities which are either directly or indirectly controlled by the state based on a regulation, agreement or any reason". Tax is also categorised as a state receivable, but as stipulated under the Elucidation of article 8 of Perppu 49/1960, it is settled separately in accordance with the law on tax collection by distress warrant, i.e. Law Number 19 Year 1997 concerning Tax Collection by Distress Warrant as amended by Law Number 19 Year 2000.

5 Article 1137 of the ICC stipulates: "The priority of the state's treasury, the auction offices and other public institutions stipulated by high authority, the order in which they are be implemented, and the time of the duration, are regulated by the relevant special law".

related to environmental protection. If the company continues to pollute the environment, then the company may be subject to administrative sanctions again, including criminal sanctions.

## 2.2 Social (S): restructuring health or safety-related liabilities

Similar to the restructuring of environmental liabilities, health or safety-related liabilities can be restructured under a reconciliation plan in the same way as elaborated in section 2.1 above.

### *2.2.1 Types of health and safety-related liabilities*

Health and safety-related liabilities under Indonesian law can encompass the following:

- claims in tort[6] and claims in contract; and
- statutory liabilities such as fines. For example, under Government Regulation Number 86 Year 2019 regarding Food Safety, an administrative fine will be imposed, for example, on any business actors who violate the sanitation requirements and / or food safety that causes damage to a consumer's health, the amount of which amount depends on the level of violation and size of the business. The administrative fine for a serious offence committed by a large-scale business is IDR 100,000,000 (one hundred million rupiah).

### *2.2.2 Treatment of health and safety-related liabilities*

Health or safety-related liabilities are susceptible to being restructured under a PKPU reconciliation plan. These liabilities can be deemed as state receivables (outlined above) due to the ambiguity of state receivables' position in bankruptcy and PKPU proceedings, and whether state receivables are treated as preferential debts will depend on the Supervisory Judge and administrator.

## 2.3 Governance (G): third party releases in favour of directors and officers of the company

According to article 104 of Law Number 40 Year 2007 concerning Limited Liability Company as amended by Government Regulation in lieu of Law Number 2 Year 2022 concerning Job Creation (Company Law), if a bankruptcy occurs due to the fault or negligence of the board of directors and the bankruptcy assets are not sufficient to pay off all liabilities of the company, every member of the board shall be jointly and severally liable for all liabilities not paid off from the bankruptcy assets. This liability shall also apply to persons found to be at fault or negligent if they were members of the board of directors within a five year period prior to the bankruptcy declaration decision. The same shall also apply to the board of commissioners.

However, members of the board of directors and / or board of commissioners shall not be liable for the company's bankruptcy if they can prove that:

- the bankruptcy was not due to their fault or negligence;
- they performed their management duties in good faith, with due care and with full responsibility in the interests of the company and in accordance with the purposes and objectives of the company;
- they had no conflict of interest, either directly or indirectly, over the acts of management taken; and / or
- they took measures to prevent the occurrence of bankruptcy.

The Elucidation of article 104 of the Company Law states that a lawsuit must be filed in a Commercial Court to prove the fault or negligence of a member of the board of directors.

[6] A consumer may file claims in tort based on article 1365 of the ICC in conjunction with article 71 paragraph (2) of Law 18/2012 against the food maker because the food maker fails to comply with the sanitation requirements which causes damage to the consumer's health.

Law 37/2004 and the Company Law do not prohibit third party releases in favour of members of the board of directors and / or the board of commissioners. However, there have been no reported decisions or discussions in Indonesia on this issue.

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

#### *3.1.1 Approving a restructuring plan*

There is no requirement for a reconciliation plan to be approved by the Ministry of Environment and Forestry and / or other environmental protection authorities or environmental advocacy groups. A reconciliation plan only needs to be approved by creditors (i.e. concurrent creditors and secured creditors) and the Commercial Court.

#### *3.1.2 Discretion to consider wider public interest concerns*

There are no court decisions in Indonesia concerning the extent to which the court may consider environmental issues in deciding whether to approve a reconciliation plan. Law 37/2004 provides the legal basis for the Commercial Court to reject a reconciliation plan, namely:

- the debtor's property, including assets for which the right to withhold assets is to be exercised, is substantially greater than the amount agreed in the Reconciliation;
- the implementation of the Reconciliation is not sufficiently guaranteed;
- the Reconciliation is achieved due to fraud, or collusion with one or more creditors, or due to the use of other dishonest measures and regardless of whether the debtor or any other parties cooperate to achieve this; and / or
- service fees and costs incurred by experts and administrators have not been paid or there is no guarantee for their payment.

#### *3.1.3 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

There are no statutory provisions that grant environmental protection authorities or environmental advocacy groups standing to air their views / concerns in a restructuring.

### 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

#### *3.2.1 Approving a restructuring plan*

There is no requirement for a reconciliation plan to be approved by the Ministry of Manpower, Manpower Agencies, unions or employee / worker advocacy groups. A reconciliation plan only needs to be approved by creditors (i.e. concurrent creditors and secured creditors) and Commercial Court.

#### *3.2.2 Discretion to consider wider public interest concerns*

There are no court decisions in Indonesia concerning the extent to which the court may consider labour issues in deciding whether to approve a reconciliation plan. Law 37/2004 provides the legal basis for the Commercial Court to reject a reconciliation plan, namely:

- the debtor's property, including assets for which the right to withhold assets is to be exercised, is substantially greater than the amount agreed in the Reconciliation;
- the implementation of the Reconciliation is not sufficiently guaranteed;

- the Reconciliation is achieved due to fraud, or collusion with one or more creditors, or due to the use of other dishonest measures and regardless of whether the debtor or any other parties cooperate to achieve this; and / or

- service fees and costs incurred by experts and administrators have not been paid or there is no guarantee for their payment.

#### *3.2.3 Protection of employee rights*

There are no statutory provisions that grant the Ministry of Manpower, Manpower Agencies, labour unions or employee / worker advocacy groups standing to air their views / concerns in a restructuring.

Labour unions and / or employee(s) are not involved in any creditors' meeting because they do not have the right to vote at the creditors' meeting. The reconciliation plan which has been ratified by the Commercial Court shall bind all creditors, including preferred creditors such as employees, except for secured creditors who do not approve the reconciliation plan.[7]

However, if the reconciliation plan is ratified by the Commercial Court, a cassation petition may be submitted not only by the debtor and creditors who are parties to the first-level hearing but also by the creditors who are not parties to the first-level hearing and are dissatisfied with the Commercial Court's decision.[8]

There is no case law on where the petition for cassation was submitted by employees due to dissatisfaction with the reconciliation plan ratified by the Commercial Court. However, there was a case where the employees of PT Kertas Leces (Persero) (a state owned company) submitted a petition for nullifying a ratified reconciliation plan to the Surabaya Commercial Court due to the negligence of the debtor (PT Kertas Leces (Persero)) in fulfilling the content of the ratified reconciliation plan. The Surabaya Commercial Court granted the employees' petition and nullified the ratified reconciliation plan and this decision was affirmed by the Supreme Court.[9] However, the Supreme Court and the Surabaya Commercial Court did not discuss the legal standing of the employees as preferred creditors in this case as the judges only focused on the negligence of PT Kertas Leces (Persero) in fulfilling the ratified reconciliation plan.[10]

On another note, with regard to preferred debts, the Constitutional Court has ruled that the payment of workers' wages outweighs all types of claims including tax debts.[11]

### 3.3 Governance (G): board / management conflicts addressed in a restructuring

Any member of the board of directors or board of commissioners (BOD / BOC) is entitled to submit his / her receivables to the receiver accompanied by calculations or written statements / evidence showing the nature and amount of the receivables. These members of the BOD / BOC are qualified as concurrent creditors. If the receiver approves the relevant receivables, these members of the BOD / BOC can vote on the reconciliation plan at the creditors' meeting.

In terms of asset distribution, article 189 paragraph (2) of Law 37/2004 vests the Supervisory Judge with the authority to determine the amount of the concurrent creditors' portion. In practice, the members of the BOD / BOC will receive payment less than the other concurrent creditors.

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7 The secured creditors who do not approve the reconciliation plan shall be compensated in the amount of the lowest value among the collateral value or the actual value of the loan which is directly secured with the collateral right.

8 Article 11 of Law 37/2004.

9 Supreme Court decision number 43PK/Pdt.Sus-Pailit/2019 in conjunction with Surabaya Commercial Court decision number 1/Pdt.Sus.Pembatalan.Perdamaian/18/PN.Niaga.Sby and Surabaya Commercial Court decision number 5/Pdt.Sus-PKPU/PN.Niaga.Sby.

10 One may say that a preferred creditors do not have legal standing in submitting a petition for nullifying a ratified reconciliation plan because the preferred creditors are not involved at the creditors' meeting.

11 Constitutional Court's decision number 67/PUU-XI/2013.

In addition to the above, under Law Number 40 Year 2007 concerning Limited Liability Company (Law 40/2007), a member of the BOD shall not be authorised to represent the company if the relevant member of the BOD has a conflict of interest with the company. If a member of BOD has a conflict of interest, the following are authorised to represent the company:

- other members of the BOD who have no conflict of interest with the company;
- the BOC, if all members of BOD have a conflict of interest with the company; or
- another party appointed by the general meeting of shareholders, if all members of BOD and BOC have a conflict of interest with the company.

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

We have not identified any industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

The Minister of Manpower just issued a regulation with the objective to provide protection and maintain the work continuity of workers and the business continuity of certain export-oriented labour-intensive industries (IPKBEs) in light of the impact of changes in the global economy, namely Regulation of Minister of Manpower Number 5 Year 2023 regarding the Adjustment of Wages and Working Hours for IPKBE Affected by Global Economic Changes (MOM Reg. 5/2023). This regulation entered into force on 8 March 2023.

MOM Reg. 5/2023 provides certain types of IPKBEs which have been given the opportunity to adjust their working hours and wages in order to prevent employment termination, namely the:

- textile and apparel industry;
- footwear industry;
- leather and leather goods industry;
- furniture industry; and
- children's toy industry.

However, such IPKBEs must meet the following criteria:

- having workers of at least 200 people;
- the percentage of labour cost in total production costs shall be at least 15%; and
- production shall depend on requests for orders from the United States and countries in the European continent as evidenced by an order request letter.

The IPKBEs that meet the foregoing criteria are entitled to adjust their working hours and wages provided that such adjustment shall be made based on agreements between the relevant IPKBE and their employees and may only be applied for a period of no longer than six months from the effective date of MOM Reg. 5/2023.

The companies that are not qualified as IPKBEs may follow the Circular Letter of Minister of Manpower and Transmigration Number SE.643/MEN/PHI-PPHI/IX/2005 Year 2005 regarding the

Prevention of Employment Termination, which suggests that employers take alternative steps to avoid employment termination, namely:

- to perform production cost efficiency;
- to reduce the wages of workers at the managerial level;
- to reduce overtime;
- to offer early retirement opportunities for workers who meet the requirements; and
- to temporarily furlough workers.

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

There are three insolvency practitioners' associations in Indonesia, namely:

- *Asosiasi Kurator dan Pengurus Indonesia* (AKPI);
- *Ikatan Kurator dan Pengurus Indonesia* (IKAPI)*;* and
- *Himpunan Kurator dan Pengurus Indonesia* (HKPI).

Each organisation has its own codes of conduct which only apply to its members. However, the codes of conduct of each organisation in principle provide general guidelines as to how the receiver (*kurator*) and administrator (*pengurus*) should deal with potential conflicts of interest. For example, the code of conduct of IKAPI provides:

- in each appointment, members must act independently and free from the influence of anyone;
- what is meant by "conflict of interest" is the relationship between the receiver or administrator and debtors, creditors, and / or other parties that may hinder the implementation of their duties with full responsibility in accordance with applicable laws and regulations. Conflicts of interest that can affect the implementation of receiver and administrator duties must be avoided:
  - prior to the appointment: the member must refuse the appointment if it turns out that, at the time of appointment, there was a conflict of interest or, based on the information obtained, the member believes that a conflict of interest may arise; and
  - after the appointment: members must immediately disclose the conflict to the Supervisory Judge, creditors, the committee of creditors (if any) and debtors if it turns out that after the appointment that there is in fact a conflict that has arisen; and
- members, partners, employees and relatives (in the broadest sense) may not obtain goods or gain an interest in bankruptcy assets controlled by members unless obtained based on applicable laws and regulations.

Further, Law 37/2004 also stipulates that the appointed receiver or administrator must be independent and have no conflict of interest with debtors or creditors and must not currently be handling bankruptcy cases and / or PKPU proceedings for more than three entities.

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

ESG-based investment has rapidly developed all over the world and Indonesia is no exception. In our banking industry, the implementation of ESG commenced as early as 2009 with the inclusion of ESG criteria in banks' financial reports. However, there are still many banks that have not fully implemented ESG principles.

The Indonesian banking industry has continuously committed to supporting ESG principles aiming for sustainable development.

Many Indonesian banks have their own programme which provides financing for renewable and affordable clean energy, environmentally sustainable projects and buildings, clean water and sanitation, climate action, zero hunger and other matters. This approach is also reflected in more favourable terms in interest rates for businesses that fulfil some or all ESG criteria. One real implementation is by not providing loans to business entities which may potentially harm the environment.

Bank Rakyat Indonesia (BRI), a leading Indonesian state-owned bank which focuses on small and medium scale businesses, commits and has strengthened the implementation of ESG principles, marked with the issuance of the Sustainability Report. In 2022, BRI issued a green bond with a total value of Rp. 15 trillion for a three year period. In addition, BRI has also inaugurated the electric vehicle recharging station for public use in its headquarters to support the Government to reach the net-zero emission target in 2060 or earlier.

Bank Negara Indonesia (BNI), another leading Indonesian state-owned bank, has implemented sustainable finance as its main value, work culture, corporate strategy, operational policy and corporate operation procedure. As of June 2021, BNI had invested in a green portfolio for a total amount of Rp. 139.4 trillion, representing 24.5% of its total credit facility.[12]

As of September 2022, Bank Central Asia (BCA), the biggest private bank in Indonesia, had channelled through sustainable financing or credit, fulfilling ESG principles, in the total amount of Rp. 172.7 trillion. This was a 18.6% year on year increase from the previous year.[13]

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

In 2022, the Central Bank set its strategy to increase the Sustainable Financial Instrument (SFI), identifying: (i) the importance of developing green financial instruments and investments to support more sustainable economic growth; (ii) the importance of developing the ecosystem for SFI; and (iii) the need for a programme on capacity building and sustainable technical support in increasing understanding and expertise of all related parties.

Currently, the Financial Service Authority (OJK) has completed the Roadmap for Financial Sustainability Stage II (2021-2025). This roadmap includes all interested parties and is expected to be used as a guideline for the financial service sector and as a reference for the relevant government ministries / institutions in developing innovative financing. The OJK has confirmed that at least eight banks, either state-owned or private, are ready and have implemented financial sustainability, namely Bank Mandiri, BRI, BNI, BCA, Bank Muamalat, Bank BJB, Bank Artha Graha Internasional and BRI Syariah.

The implementation of ESG principles in infrastructure has also received an important boost during the Indonesian presidency of the G20 in 2022. This initiative became the first to be enacted by the Ministry of Finance in infrastructure financing. In 2022, the Ministry of Finance, with the support of the United Nations Development Programme (UNDP) and the Canadian Government through a grant managed by the World Bank, succeeded in developing a Framework and Manual of ESG for infrastructure financing. The implementation of ESG principles in infrastructure financing will be conducted through stages until 2025, commencing with the housing and water resources sectors in 2022.[14]

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12 https://www.bni.co.id/id-id/perseroan/bni-esg.

13 https://keuangan.kontan.co.id/news/tumbuh-186-pembiayaan-esg-bca-tembus-rp-1727-triliun-per-september-2022.

14 https://www.kemenkeu.go.id/informasi-publik/publikasi/berita-utama/Implementasi-ESG-Wujud-Nyata-Tindak-Lanjut-Agenda.

### 5.3 Promoting ESG by the central bank and regulators

There are many standards and criteria for ESG principles. Although still within the scope of ESG, each standard is set by an institution, company or organisation with a different focus.

Most of the regulations on ESG are governed on a sector-by-sector basis and are heavily dependent on the regulatory policy of each sector. For example, the OJK has issued Regulation OJK Number 51 of 2017 on the implementation of sustainable financing for financial service institutions, securities issuers and public companies. The focus of this regulation is to create sustainable development which could protect the economic stability and national economic system, emphasising harmony / synchronisation between economical, social and environmental aspects.

As noted above, in 2022, the Central Bank also set out its strategy to increase the SFI.

# JAPAN

# 1. General overview of the restructuring regime

## 1.1 Formal restructuring procedures

### *1.1.1 Rehabilitation proceeding under the Civil Rehabilitation Act*

Under the Civil Rehabilitation Act, rehabilitation procedures are essentially debtor in possession (DIP) procedures, under which the court may appoint a supervisor to supervise the rehabilitation of the debtor.[1] However, the court may appoint a trustee in certain circumstances.[2] The process is outlined in further detail below.

- Commencement of proceeding

  The proceeding commences with a court order, when the threshold requirement of the debtor being insolvent (or on the verge of insolvency) is satisfied,[3] and when there are no other statutory grounds not to commence the proceeding.[4] A petition to commence the proceeding can be filed by the debtor and certain creditors.[5]

- Proposal of rehabilitation plan

  Within the period specified by the court after the expiration of the period for creditors' filings of proof of claims, the rehabilitation debtor must prepare a potential rehabilitation plan and submit it to the court. There is no exclusivity in terms of the formulation of a plan as creditors too are allowed to formulate and submit their draft plans to the court.[6] When a proposed rehabilitation plan is approved by the creditors' meeting, the court will issue an order of confirmation of the rehabilitation plan, barring exceptional cases.[7]

- Disclosure of material information

  Under rehabilitation proceedings, the debtor is expected to disclose material information to the creditors at some of the important stages of the proceedings. According to standard practice, the rehabilitation debtor verbally discloses material information, available at the time, along with other materials at the introductory creditors' meeting held immediately after the filing of the commencement of proceedings.[8]

  Also, in connection with the sale of all or part of the debtor's business prior to the confirmation of the restructuring plan (and therefore outside of the plan), the court is required to hear the creditors' opinions prior to transfer of the debtor's business to a third party.[9] According to standard practice of the Tokyo District Court, prior to the official hearing proceedings, the rehabilitation debtor provides the creditors with an outline of the proposed business transfer and holds a briefing session for the creditors about the proposed business transfer.

  Throughout the proceedings, interested persons, including creditors, may inspect documents and any other items submitted to the court or prepared by the court.[10] There is, however, no formal obligation to file or prepare any disclosure document as rigid or detailed as a disclosure statement under a Chapter 11 proceeding in the United States.

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1 Civil Rehabilitation Act, s 54(1).
2 *Idem*, s 66.
3 *Idem*, s 21(1).
4 *Idem*, s 33(1).
5 *Idem*, s 21(2).
6 *Idem*, s 163(1).
7 *Idem*, s 174(1).
8 Rules of Civil Rehabilitation, s 61(1)
9 Civil Rehabilitation Act, s 42(2).
10 *Idem*, s 16(1)

In order to approve a proposed rehabilitation plan, it is necessary to obtain the consent of both: (i) the majority in terms of the head count of the holders of voting rights; and (ii) the persons who hold voting rights that account for not less than half of the total amount of voting rights.[11]

The court must confirm the rehabilitation plan approved by the creditors' meeting in order for the plan to become effective. In exceptional cases, including where the best interests of creditors test is not satisfied, where the rehabilitation plan is unlikely to be carried out (or complied with) or where the resolution provided in the rehabilitation plan is contrary to the common interests of rehabilitation creditors, the court will issue an order of disconfirmation of the rehabilitation plan.[12]

A rehabilitation plan must include clauses concerning the following matters:

- modification of some or all of the rights of rehabilitation creditors;
- payment of common benefit claims and claims with general priority; and
- the contents of known post-commencement claims (if any).[13]

Therefore, only rehabilitation claims and post-commencement claims are subject to restructuring under a rehabilitation plan. Importantly, secured claims (to the extent "covered" by the appraised value of the relevant collateral) will not be subject to the rehabilitation proceeding, save for certain limited exceptions.

"Rehabilitation claim" means any unsecured claim on assets arising against a rehabilitation debtor resulting from a cause that occurred before the commencement of rehabilitation proceedings (excluding any claim that is a common benefit claim or claim with general priority).[14]

"Post-commencement claim" means any unsecured claim on assets arising from a cause that occurred after the commencement of rehabilitation proceedings (excluding any claims that are a common benefit claim, a claim with general priority or a rehabilitation claim).[15]

"Common benefit claims" means, essentially, costs that shall be borne jointly by rehabilitation creditors in order to carry out rehabilitation proceedings and ensure the purpose of the proceedings is realised, such as claims for expenses for: (i) court proceedings performed for the common interest of rehabilitation creditors; and (ii) the rehabilitation debtor's business after commencement of rehabilitation proceedings.[16] Common benefit claims may be paid at any time without going through rehabilitation proceedings.[17]

### *1.1.2 Reorganisation proceeding under the Corporate Reorganisation Act*

Under the Corporate Reorganisation Act, the court appoints an administrator or trustee.[18] However, a quasi DIP-type reorganisation proceeding has also been adopted through practice, with the court appointing the incumbent manager(s) of the reorganisation company as trustee(s). An outline of the process is provided below.

- Commencement of proceeding

  The proceeding commences with a court order, when the threshold requirement of the debtor being insolvent (or on the verge of insolvency) is satisfied, and when there are no other statutory grounds not to commence the proceeding. A petition to commence the proceeding can be filed by the debtor stock company, certain creditors or shareholders.

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11 *Idem*, ss 172-3(1).
12 *Idem*, s 174(2).
13 *Idem*, s 154(1).
14 *Idem*, s 84(1).
15 *Idem*, s 123(1).
16 *Idem*, s 119.
17 *Idem*, s 121.
18 Corporate Reorganisation Act, s 67(1).

- Proposal of rehabilitation plan

  Within the period specified by the court after the expiration of the period for creditors' filings of proof of claims, the trustee must prepare a potential reorganisation plan and submit it to the court. There is no exclusivity in terms of the formulation of a plan as a reorganisation company, as well as reorganisation creditors and shareholders, are allowed to formulate and submit their draft plans to the court.[19] When a proposed reorganisation plan is approved by the creditors' meeting, the court will issue an order of confirmation of the reorganisation plan, barring exceptional cases.[20]

- Disclosure of material information

  Under reorganisation proceedings, the trustee is expected to disclose material information to the creditors at some of the important stages of the proceedings. According to standard practice, the trustee verbally discloses material information, available at the time, along with other materials at the introductory creditors' meeting held immediately after filing of the commencement of proceedings.[21]

  Also, in connection with a sale of all or part of the debtor's business prior to the confirmation of the restructuring plan (and therefore outside of the plan), the court is required to hear the opinions prior to transfer of the reorganisation company's business to a third party.

  In addition, prior to the plan approval process by the creditors, the trustee usually holds a session to explain the outline of the proposed plan to the creditors.

  Throughout the proceedings, interested persons, including creditors, may inspect documents and any other objects submitted to the court or prepared by the court.[22] Again, there is no formal obligation to file or prepare any disclosure document as rigid or detailed as a disclosure statement under a United States Chapter 11 proceeding.

A resolution on a proposed reorganisation plan will be made by each of the separate classes. While the court has the authority to further divide classes, in general, classification of claims in the reorganisation proceeding will be:[23]

- secured reorganisation claims;
- reorganisation claims with general statutory liens or any other general priority;
- general unsecured claims;
- consensually subordinated reorganisation claims;
- shares of a class which is preferred in terms of the distribution of residual assets; and / or
- shares other than those set forth above.[24]

Each right holder will have different resolution requirements. For example, while the threshold for general unsecured claims is a majority, for secured claimants, if the secured claims are going to be impaired in terms of their amounts, a three-fourths supermajority (in terms of amounts) will be required.

The court must confirm the reorganisation plan approved by the creditors' meeting for the plan to become effective. The court shall confirm the reorganisation plan if all the statutory requirements,

19 *Idem*, s 184(1).
20 *Idem*, s 184(2).
21 Rules of Corporate Reorganisation, s 16.
22 Corporate Reorganisation Act, s 11(1).
23 *Idem*, s 196(2).
24 *Idem*, ss 196(1), 168(1).

including "the content of the reorganisation plan is fair and equitable" and "the reorganisation plan is feasible for implementation",[25] have been met. Although the best interests of creditors test is, unlike civil rehabilitation proceedings, not specifically provided as a requirement, it is interpreted that the payment to each of the reorganisation creditors under the reorganisation plan must exceed the theoretical amount of payment calculated based on the liquidation value of the company.[26]

The reorganisation plan must specify:

- the modification of the rights of some or all of the reorganisation creditors or shareholders;
- the directors, accounting advisors, auditors, executive officers, accounting auditors and liquidators of the reorganisation company;
- the payment of common benefit claims;
- the method for procuring funds to repay debts;
- the use of any earnings beyond the amount expected under the reorganisation plan;
- the amount or estimated amount of money to be allocated to dividends in compulsory execution and the use of such money;
- the amount or the estimated amount of money in order to extinguish security interests and the use of such money; and
- the content of known post-commencement claims, if there are any.[27]

Compared to civil rehabilitation proceedings, corporation reorganisation proceedings are characterised by the fact that claims with security interests are also subject to restructuring.

"Reorganisation claim" means a claim on property arising against the reorganisation company that has resulted from a cause that occurred before the commencement of reorganisation proceedings, as well as each item of section 2(4) of the Corporate Reorganisation Act, none of which fall within the scope of secured reorganisation claims or common benefit claims.

"Secured reorganisation claim" means a claim secured by any security interest that exists on the property of the reorganisation company as at the time of the commencement of reorganisation proceedings, which has arisen from a cause that occurred before the commencement of reorganisation proceedings or reorganisation claims, to the extent the claim is secured by the security interest on the assumption that the property that is the subject matter of the security interest will retain its market value as of the time of commencement of reorganisation proceedings.[28]

"Post-commencement claims" means a claim on property arising from a cause that occurred after the commencement of reorganisation proceedings.

"Common benefit claims" means, essentially, costs that shall be borne jointly by reorganisation creditors in order to carry out reorganisation proceedings and ensure the purpose of the proceedings is realised, such as claims for expenses for: (i) court proceedings performed for the common interest of reorganisation creditors; and (ii) the reorganisation company's business after commencement of reorganisation proceedings.[29] Common benefit claims may be paid at any time without going through reorganisation proceedings.[30]

25 *Idem*, s 199(2).
26 I Makoto, *Corporate Reorganisation Act: Special Liquidation Law*, Japan: Yuhikaku, 2020, [672].
27 Corporate Reorganisation Act, s 167.
28 *Idem*, s 2(10).
29 *Idem*, s 127.
30 *Idem*, s 132(1).

### 1.2 Informal restructuring procedures

Various guidelines have been established for restructuring procedures other than formal restructuring procedures. Some examples are the Guidelines for Business Revitalisation of Small and Medium Enterprises and the Guidelines on Management Guarantees.

In addition, there also exist restructuring procedures carried out by institutions established under the law, such as that of the Small and Medium Business Revitalisation Council established under section 134 of the Act on Strengthening Industrial Competitiveness, and the Business Turnaround ADR organised by the Japanese Association of Turnaround Professionals, which has been certified as a dispute resolution business under the Act on Strengthening Industrial Competitiveness.

Moreover, conciliation procedures at a court can also be utilised through special conciliation as provided under the Act on Special Conciliation for Expediting Arrangement of Specified Debts.

Additional support through debt purchase is also available as part of the business revitalisation support services provided by the Regional Economy Vitalisation Corporation of Japan (REVIC).

These informal restructuring procedures are unique in that, as a rule, they target only financial claims and do not target trade claims and other non-financial claims, secured or unsecured. Although exceptions can be made to involve non-financial claims, they very rarely, if ever, are.

All of these restructuring procedures remain under the control of the company while the procedures are ongoing.

In principle, the drafting of a restructuring plan and unanimous consent thereto by all of the involved (financial) creditors is required in order to make the plan effective with respect to all of the above-noted procedures. In addition, in such procedures, creditors' meetings or appearances for special conciliation are held in order to hear the opinions of targeted creditors and to reach a resolution.

All of these procedures are aimed at obtaining the approval of the restructuring plan by each and every one of the involved / targeted creditors – i.e. unanimous consent is required.

However, the procedure for special conciliation is a little different from other procedures. Under this procedure, the court may order the payment of money, delivery of an object, or any other provision of economic benefit if the court finds it appropriate. [31] This order becomes binding if two weeks have elapsed without objection from the relevant creditor.[32]

Save for a court's authority to render its ruling in the procedure for special conciliation, none of the above-noted procedures requires or involves court approval or the approval of any organisation other than targeted creditors, although relevant bodies (but not the court) are permitted to state their opinions about the restructuring plan proposed and to intervene between targeted creditors and debtors.

## 2. Restructuring of ESG-related liabilities

Under formal restructuring procedures (in court), generally ESG-related liabilities are treated in the same way as other types of claims against the debtor. There are no special restrictions or conditions that apply when restructuring environmental liabilities.

Under informal restructuring procedures (out of court), as discussed above, since only debt against financial institutions is subject to restructuring, ESG-related liabilities are generally not restructured in the procedures.

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[31] Act on Special Conciliation, s 17.
[32] *Idem*, s 18(1).

## 2.1 Environmental (E): restructuring environmental liabilities

Generally, environmental liabilities can be restructured in the same way as the ordinary liabilities of a company. There are no specific provisions which restrict the discharge of environmental liabilities under restructuring procedures.

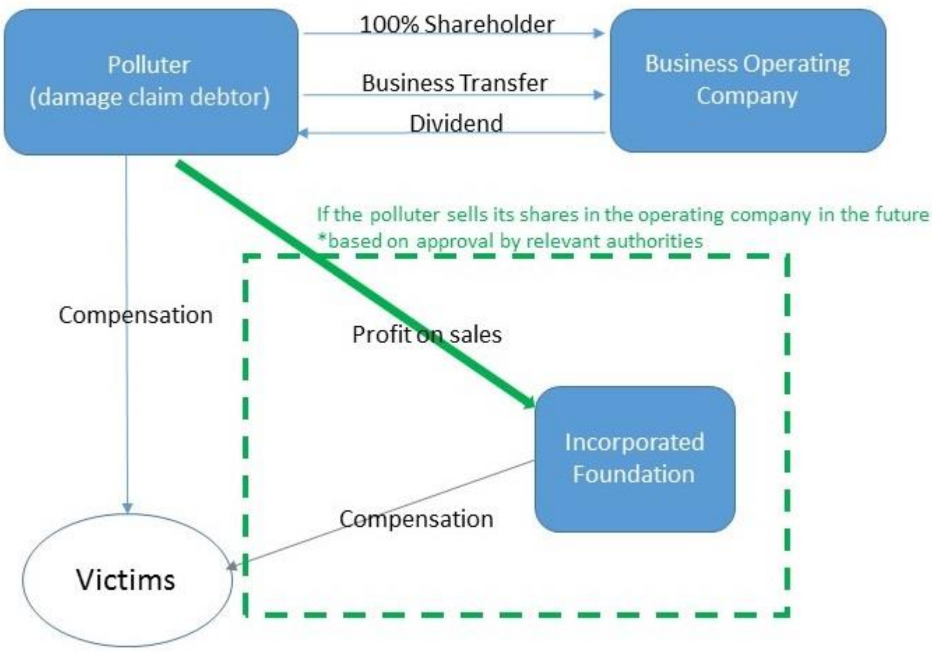
However, a restructuring plan may not provide for the reduction or release of administrative and criminal fines that arose prior to the commencement of a restructuring procedure.[33]

Some administrative payments under a public compensation system, such as the system under the Act on Compensation for Pollution-Related Health Damage, involve a fund to recover civil liabilities caused by environmental pollution.[34] Since such payments cannot be restructured as explained above, to that extent, the environmental liabilities are protected from reduction or release under restructuring proceedings.

For some serious environmental pollution cases where a company causes severe health problems to an unspecified large number of people, a special legal framework may be established to prevent the liabilities from being restructured under restructuring proceedings.

For example, a chemical company that caused serious water pollution and health damage to neighbouring residents was split into two entities under the Act on Special Measures. One of these is only for carrying out compensation affairs making use of a fund established from the income of the other entity which continues its core business.[35]

The main purposes of this scheme are: (i) to separate the business from the polluter (debtor), which owes sizeable debts to victims, thereby enabling healthy business operations to generate funds for continuous compensation; and (ii) to separate profits on transfers of shares in the business operating company from the polluter (debtor). This is depicted below.




### 2.1.1 *Types of environmental liabilities*

33 Civil Rehabilitation Act, s 155(4); Corporate Reorganisation Act, s 168(7).

34 For example, a public agency collects the imposition on pollution load from polluters to cover a part of the expenses for the payment of the compensation benefits for the victims of environmental pollution: see Act on Compensation for Pollution-Related Health Damage, s 52.

35 Act on Special Measures Concerning Relief for Victims of Minamata Disease and Solution of Minamata Disease Issue.

- Civil claims:
  - claims in tort. In addition to the ordinary tort responsibilities based on the perpetrators' wilful act or negligence,[36] some special environmental regulations provide for strict liability (i.e. tort liability that does not require negligence of the perpetrator). For example, the responsibility of businesses in relation to the discharging or underground permeation of hazardous substances, or for damage resulting therefrom,[37] and responsibility in relation to emission into the atmosphere of a substance harmful to human health in association with business activities at a factory or place of business causing fatal or bodily harm to a person;[38] and
  - claims in contract. A party that sells environmentally polluted real estate may be liable for breach of a contract that contains terms and conditions on certain environmental requirements[39] or for cure of non-conformity.[40]
- Statutory liabilities:
  - fines imposed for violations of environmental regulations, such as the Water Pollution Prevention Act and Air Pollution Control Act. Some municipal ordinances also provide for fines for violations of regulations; and
  - remediation / clean-up costs, such as those imposed on an entity that collects industrial waste, violating the requirements,[41] and those imposed in the case where damage has been caused to natural parks protected under the law.[42]

#### *2.1.2 Priority given to environmental liabilities*

There are no provisions which specifically grant priority to environmental liabilities under restructuring procedures.

However, as general rule, a claim for expenses for the debtor's business and the administration and disposal of assets after the commencement of restructuring procedures is classified as a common benefit claim, which may be repaid in preference to rehabilitation / reorganisation claims at any time without going through restructuring procedures.[43] Therefore, where an environmental liability fulfils such requirements, the liability can be prioritised under the restructuring procedures.

#### *2.1.3 Disclaimer of environmental obligations*

Under formal restructuring procedures, property subject to environmental obligations may not be disclaimed or abandoned, in contrast to bankruptcy proceedings which allow the bankruptcy trustee to abandon such property based on court approval if the cost of meeting the obligations exceeds the benefit arising from the property for bankruptcy creditors.

Selling such property to a third party is common, but it does not relieve a company of its environmental obligations in relation to the property. As mentioned above, generally environmental liabilities that arose prior to the commencement of restructuring procedures can be restructured in the same way as ordinary liabilities of a company. This does not relieve a company of its liabilities that arose after the commencement of restructuring procedures.

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36 Civil Code, s 709.
37 Water Pollution Prevention Act, s 19.
38 Air Pollution Control Act, s 25.
39 Civil Code, s 415.
40 *Idem*, s 562.
41 Waste Management and Public Cleaning Act, s 19-4.
42 Natural Park Act, ss 21(3), 34(1).
43 Civil Rehabilitation Act, ss 119(2), 121; Corporate Reorganisation Act, ss 127(2), 132.

## 2.2 Social (S): restructuring health or safety-related liabilities

Generally, health or safety-related liabilities can be restructured in the same way as the ordinary liabilities of a company. There are no special restrictions or conditions that apply when restructuring health or safety-related liabilities.

However, a restructuring plan may not provide for the reduction or release of administrative and criminal fines that arose prior to the commencement of a restructuring procedure.[44]

### *2.2.1 Types of health and safety-related liabilities*

- Civil claims:
  - claims in tort. In addition to the ordinary tort responsibilities based on the perpetrator's intention or negligence,[45] some special regulations provide for strict liability, which does not require negligence of the perpetrator. For example, manufacturers, or any persons that use a name, trade name, trademark or other type of indication, are liable to compensate for loss or damage if death or bodily injury to others have resulted from a defect in a delivered product that was manufactured, processed, imported, or on which certain indications including its name, trade name, or trademark were used;[46] and
  - claims in contract. A party that supplies defective or unsafe goods may be liable for breach of a contract that contains terms and conditions on satisfactory quality.[47] According to court precedents, an employer generally owes a duty to take safety precautions in relation to its employees, and where an employer breaches this duty and that breach causes damage to employees, the employer is liable for that damage.
- Statutory liabilities
  - fines, for example, those imposed for violations of food regulations, such as the Food Sanitation Act, or failing to take the necessary measures to prevent dangers associated with equipment used in the workplace under the Industrial Safety and Health Act; and
  - remediation costs. For example, an employer must take the necessary measures to prevent dangers associated with machinery, tools or any other such equipment in the workplace.[48] If there is a factual circumstance that violates the regulations, the Director of the Prefectural Labour Bureau or the Chief of the Labour Standard Inspection Offices may order the violating employer, operator, lessor of machinery or other such equipment, or building lessor to stop all or part of its work, to stop or alter the use of all or part of a construction, equipment or raw material, or to do any other thing that is necessary to prevent an industrial injury.[49]

### *2.2.2 Treatment of health and safety-related liabilities*

There are no provisions which restrict the discharge of health and safety-related liabilities under restructuring procedures.

As noted above, a restructuring plan may not provide for the reduction or release of administrative and criminal fines that arose prior to the commencement of a restructuring procedure (although it is possible to change payment terms).[50]

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44 Civil Rehabilitation Act, s 155(4); Corporate Reorganisation Act, s 168(7).
45 Civil Code, s 709.
46 Product Liability Act, s 3.
47 Civil Code, ss 415, 562.
48 Industrial Safety and Health Act, s 20.
49 *Idem*, s 98.
50 Civil Rehabilitation Act, s 155(4); Corporate Reorganisation Act, s 168(7).

There are no provisions that specifically grant priority to health and safety-related liabilities under restructuring procedures.

However, as general rule, a claim for expenses for the debtor's business and the administration and disposal of assets after the commencement of restructuring procedures is classed as a common benefit claim, which may be repaid in preference to rehabilitation / reorganisation claims at any time without going through restructuring procedures.[51] Therefore, where a health and safety-related liability fulfils such requirements, the liability is prioritised under the restructuring procedures.

### 2.3 Governance (G): third party releases in favour of directors and officers of the company

There is no law which provides third party releases in favour of directors or officers of a company under restructuring procedures.

Restructuring procedures under Japanese law proceed only for the entity or individual that filed the procedures, not for any other entity or individual (such as a director of the debtor company). Under restructuring procedures, when the court finds it necessary, it may make an assessment decision on a claim for damages based on the company debtor's officers' liability.[52] Under this procedure, generally, the debtor may obtain a court order for responsibility of officers more quickly than under ordinary litigation proceedings.

In addition, a derivative action filed by shareholders against a debtor's officer, pending at the time of commencement of restructuring proceedings, is discontinued as a result of the commencement.[53] Although the debtor may substitute for a party (i.e. the shareholders) in that case, this may be, in some sense, a release of the defendant officers from harsh accusations by the shareholders.

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

#### *3.1.1 Approving a restructuring plan*

A restructuring plan under in-court insolvency proceedings is subject only to the approval (i.e. an order of confirmation) of the creditors and the court, not to the approval of any other regulatory bodies, such as environmental protection authorities.

However, it is possible for regulatory bodies to indirectly influence the relevant court's plan confirmation process.

Under civil rehabilitation proceedings, the court issues an order of disconfirmation of the rehabilitation where the rehabilitation plan is unlikely to be executed.[54] Therefore, if a regulatory body concerning the rehabilitation debtor's license to continue its business objects to the granting of the license (or renewal thereof), the court may issue a disconfirmation order.

Under corporate reorganisation proceedings, where a proposed reorganisation plan provides for matters that require permission, authorisation, a license, or any other disposition by an administrative agency, the court shall give regard to the opinions of the administrative agency concerned with such matters.[55]

Therefore, if the authority relevant to the debtor's reorganisation plan (e.g. the regulatory body of the license necessary to continue the debtor's business in order to achieve the plan) states opinions

51 Civil Rehabilitation Act, ss 119(2), 121; Corporate Reorganisation Act, ss 127(2), 132.
52 Civil Rehabilitation Act, s 143; Corporate Reorganisation Act, s 100.
53 Civil Rehabilitation Act, s 40-2(1); Corporate Reorganisation Act, s 52-2(1).
54 Civil Rehabilitation Act, s 174(2)(iii).
55 Corporate Reorganisation Act, s 187.

contrary to important points in the plan, the court may have no choice but to issue an order of disconfirmation.

As such, regulatory bodies may indirectly influence the plan confirmation process by the courts.

### *3.1.2 Discretion to consider wider public interest concerns*

Under formal restructuring procedures, subsequent to the approval of creditors, the court issues an order of confirmation of the plan. Some requirements to confirm / disconfirm the plan are provided in the law, but public interest concerns are not specifically provided therein.[56]

However, as noted above, regulatory bodies may be involved in the plan approval process indirectly. Such regulatory bodies may consider public interest concerns in their opinions, and the opinions affect the decision of confirmation / disconfirmation by the courts.

### *3.1.3 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

There are no statutory provisions which grant environmental protection authorities or environmental advocacy groups standing to air their views or concerns in a restructuring.

However, as noted above, regulatory bodies may be indirectly involved in the plan approval process.

## 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

In cases of in-court insolvency proceedings, in some situations labour unions[57] will have the opportunity to state their opinions to the court. Specifically:

- the court must hear the opinions of labour unions before making an order to commence the proceedings;[58]
- the court must hear the opinions of labour unions before granting permission to transfer the entirety or a significant part of the debtor's operations or business; [59] and
- labour unions may state their opinions on whether the proposed plan should be approved.[60]

However, the opinions of labour unions in each situation do not have the power to overturn the court’s decisions.

In addition, the date of a creditors’ meeting must be notified to the labour union,[61] and, where an order of confirmation or disconfirmation of the plan is made, the order must be notified to the labour union.[62]

### *3.2.1 Approving a restructuring plan*

A restructuring plan is subject only to the approval (i.e. an order of confirmation) of the creditors and the court, not to the approval of any other regulatory bodies, such as labour authorities.

56 Civil Rehabilitation Act, ss 174(1), 174(2); Corporate Reorganisation Act, s 199(1)(2).
57 That is, a labour union consisting of the majority of the rehabilitation debtor's employees and other workers (if any relevant labour union exists), or the representative of the majority of the rehabilitation debtor's employees and other workers, if there is no labour union consisting of the majority of the rehabilitation debtor's employees and other workers.
58 Civil Rehabilitation Act, s 24-2; Corporate Reorganisation Act, s 22(1).
59 Civil Rehabilitation Act, s 42(3); Corporate Reorganisation Act, s 46(3)(iii).
60 Civil Rehabilitation Act, s 174(3); Corporate Reorganisation Act, s 188.
61 Civil Rehabilitation Act, s 115(3); Corporate Reorganisation Act, s 115(3).
62 Civil Rehabilitation Act, s 174(5); Corporate Reorganisation Act, s 199(7).

However, as noted above, regulatory bodies may be indirectly involved in the plan approval process.

### 3.2.2 *Discretion to consider wider public interest concerns*

Under formal restructuring procedures, the court issues an order of confirmation of the rehabilitation plan, except in any of the cases set forth in the law. The exceptions do not specifically include public interest concerns.[63]

However, as noted, regulatory bodies may be indirectly involved in the plan approval process. Such regulatory bodies may consider public interest concerns in their opinions, and the opinions affect decision of confirmation / disconfirmation by the courts.

### 3.2.3 *Protection of employee rights*

Under civil rehabilitation proceedings, salaries of employees of the debtor company are generally prioritised under the procedure as claims with general priority, which may be paid at any time without going through rehabilitation proceedings.[64] Under corporate reorganisation proceedings, salaries of employees of the debtor company for the six months preceding the commencement of proceedings are categorised as common benefit claims, which may be paid at any time without going through reorganisation proceedings.[65]

Termination of employment based on redundancy is restricted according to court precedents, as the same rule applicable in a pre-insolvency proceeding will still apply even after the commencement of an in-court insolvency proceeding. That is, the following four factors must be considered in establishing the validity of a termination based on redundancy:

- necessity of personnel reduction;
- efforts to avoid termination by redundancy;
- reasonableness of the selection process of the employees subject to termination; and
- due process, including sufficient explanation to, and faithful consultation with, the affected employees.

Although the fact the employer is going through restructuring procedures is likely to be taken into consideration, it is not necessarily the case that termination by redundancy as part of a restructuring process will always be deemed valid.

## 3.3 Governance (G): board / management conflicts addressed in a restructuring

Under civil rehabilitation proceedings, a rehabilitation debtor, even after a rehabilitation proceeding is commenced against it, has the right to carry out its business or administer or dispose of its assets.[66]

However, the rehabilitation debtor has the obligation, *vis-a-vis* creditors, to carry out its business or administer or dispose of its assets and conduct rehabilitation proceedings in a fair and sincere manner.[67] That is, the board / management of the rehabilitation debtor is prohibited from pursuing their own interests at the expense of the stakeholders' interests.

On the other hand, under corporate reorganisation proceedings, the right to manage the reorganisation company's business and to administer and dispose of the company's property

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63 Civil Rehabilitation Act, s 174(1)(2); Corporate Reorganisation Act, ss 199(1), 199(2).
64 Civil Rehabilitation Act, s 122.
65 Corporate Reorganisation Act, s 130(1).
66 Civil Rehabilitation Act, s 38(1).
67 *Idem*, s 38(2).

shall be vested exclusively in a trustee appointed by the court.[68] Therefore, the board / management does not have the power to control or influence the formulation of a restructuring plan.

However, a management member may be appointed as a trustee by the court in the case where:

- the management member has not engaged in any illegal management activities;
- the primary creditor does not object to the appointment;
- the sponsor (if any) does not object to such appointment; and
- the management member will not impede the smooth proceeding of corporate reorganisation.

In that case, as a trustee, the management member shall perform his / her duties with the due care of a prudent manager.[69] The management member owes such duties to the stakeholders of the debtor company, including creditors, shareholders, and the debtor company itself. As such, the management member of the debtor is prohibited from pursuing his / her own interests at the expense of other stakeholders' interests.

Under formal restructuring procedures, where the directors or management personnel are also creditors to the debtor company, they are allowed to exercise voting rights in relation to the restructuring plan.

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

Specifically in a restructuring context, we do not yet have any "soft law" instruments which serve to guide or influence a company to take or make environmentally responsible actions or decisions in Japan. This may be a result of there having been very few cases of in-court restructuring cases, especially in the recent years. In the last decade, we have been seeing more and more out of court workouts where only the financial creditors are being bound to restructuring plans.

In addition, as will be discussed in section 5.1 below, a growing number of potential sponsors for distressed debtors are interested in ESG matters in relation to their investment process, and as a result, are beginning to incorporate environmental due diligence or human rights due diligence. Such a trend may provide momentum for the creation of the above-mentioned "soft law" instruments in the restructuring context.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

There are no specific guidelines or best practices at present.

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

There are no specific guidelines or best practices at present.

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68 Corporate Reorganisation Act, s 72(1).

69 *Idem*, s 80(1).

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

According to the "Green Finance Portal" website operated by the Ministry of the Environment,[70] sustainability-linked bonds/ loans[71] and green bonds / loans are utilised in Japan.

The Ministry of the Environment issued "Green Bond and Sustainability Linked Bonds Guidelines / Green Loan and Sustainability-Linked Loan Guidelines 2022" after several updates since the "Green Bond Guidelines" issued in March 2017.

The main characteristics of each type of financing are as follows:

- Sustainability-linked bonds / loans:
  - the borrower takes actions to achieve ambitious sustainability performance targets (SPTs), and the degree of improvement is linked to the terms of the financing;
  - unlike green loans, the proceeds of sustainability-linked loans are not limited to specific projects; and
  - transparency is ensured through post-financing reporting on the relevant matters.
- Green bonds / loans:
  - the proceeds are allocated exclusively to green projects;
  - the proceeds are tracked and managed in a reliable manner; and
  - transparency is ensured by reporting after the issuance of the bonds.

A growing number of investment players, including potential sponsors for distressed debtors, are interested in ESG matters. Such potential sponsors are beginning to incorporate due diligence concerning environmental matters or human rights matters of debtors. In response to this trend, the Ministry of Economy, Trade and Industry has released "Guidelines on Respecting Human Rights in Responsible Supply Chains" and the Ministry of the Environment has released "Introduction to Environmental Due Diligence for Value Chains - With Reference to the OECD Guidance."

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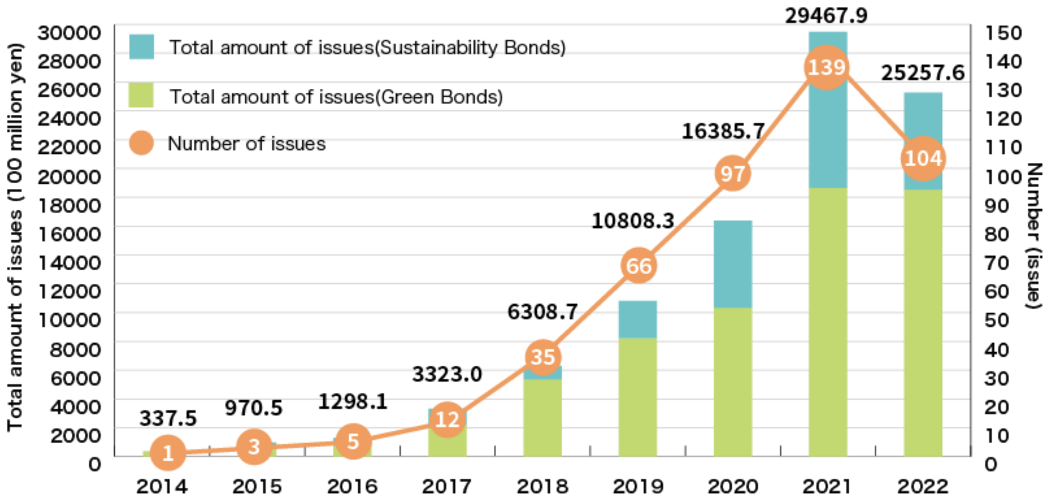
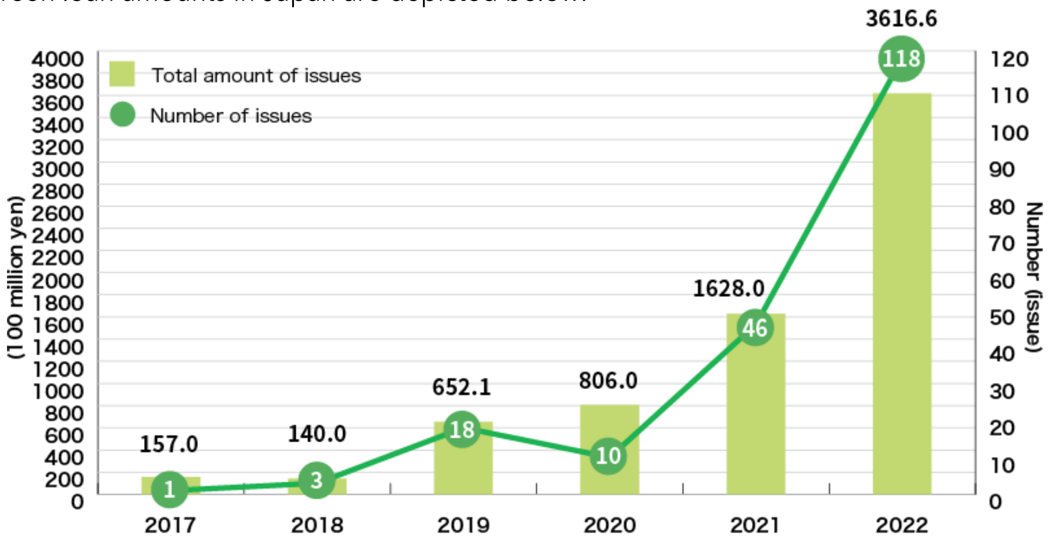
[70] Green Finance Portal (env.go.jp).
[71] Sustainability Linked Loan Issuance List (Domestic) | Issuance Data | Loans | Green Finance Portal (env.go.jp).

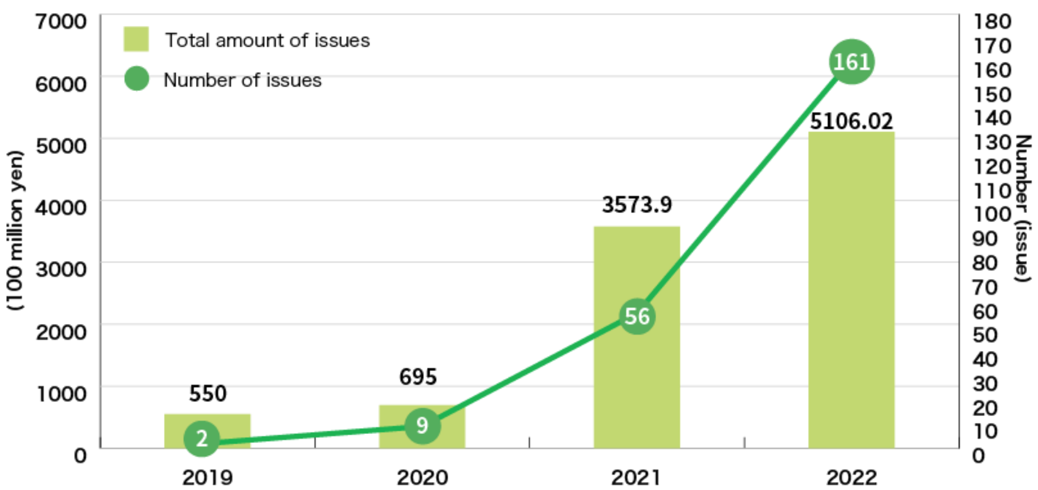
The issuance of green bonds and sustainability bonds by Japanese companies and other entities is depicted below:[72]




Green loan amounts in Japan are depicted below:[73]




Sustainability Linked Loan Amounts in Japan[74]




72 Market Status (Domestic and Global) | Issuance Data | Bonds | Green Finance Portal (env.go.jp).
73 Market Status (Domestic and Global) | Issuance Data | Loans | Green Finance Portal (env.go.jp).
74 Green Finance Portal (env.go.jp).

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

The Japanese Bankers Association[75] makes ESG-related statements in its Code of Conduct.

Specifically, the following is noted in the Code:

- offering high quality financial services. The explanation of this item includes the following statement: "It is becoming a mainstream concept among investors to think that giving consideration to the ESG factors is rational and suits the needs of society and the benefits of trustors. In this regard, there are expectations for banks and other financial institutions to provide financial support, in terms of funding and other aspects, to help realise a sustainable society and solve social issues";
- communication with society;
- respect for human rights;
- active employment of diverse human resources and healthy and safe workplaces; and
- tackling environmental and other issues.

Additionally, the Japan Securities Dealers Association has issued "Initiatives for Promoting SDGs in the Securities Industry", which includes a "Declaration of Promoting Sustainable Finance."

Further, some banks have their own guidelines regarding ESG. For example, Mitsubishi UFJ Financial Group (MUFG) has its own policies and guidelines for the environment, society and governance. MUFG participates in a variety of initiatives to fulfil its social responsibilities as a financial institution, including the United Nations Environment Programme (UNEP) Net-Zero Banking Alliance.

### 5.3 Promoting ESG by the central bank and regulators

The Bank of Japan (BOJ), the central bank of the Japanese Government, published "The Bank of Japan's Strategy on Climate Change" on 16 July 2021. Also, the BOJ issued "Principal Terms and Conditions of the Funds-Supplying Operations to Support Financing for Climate Change Responses" to support financing of the private sector in relation to its efforts to address climate change.

Further, the Japan Exchange Group Inc and Tokyo Stock Exchange Inc jointly published a "Practical Handbook for ESG Disclosure" on 31 March 2020, which is aimed at encouraging the disclosure of information useful for investors, especially for the investors who take into account ESG factors when evaluating mid-term to long-term corporate value. Moreover, the Japan Exchange Group has itself issued ESG-related policies such as the "Environmental Vision and Policy."

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75 An organisation whose members consist of banks, bank holding companies, and bankers' associations in Japan. As of 1 December 2022, it has 114 Full Members (banks), 3 Bank Holding Company Members (bank holding companies), 76 Associate Members (banks and bank holding companies), 53 Special Members (regional bankers associations) and 1 Sub-Associate Member, for a total of 247 members.

# KENYA

## 1. General overview of the restructuring regime

In Kenya, there are two main restructuring options under two separate laws:

- schemes of arrangement under the Companies Act 2015 (Companies Act); and
- company voluntary arrangements (CVAs) under the Insolvency Act 2015 (Insolvency Act).

Both of these processes are commenced by directors of the relevant company undergoing restructuring in conjunction with creditors and there are certain approval thresholds that need to be met before they take effect. The key point to note is that both processes need to be approved by the court before they can be implemented. Arguably, this approval is meant to cement the official and binding nature of the processes since they do at some point bind even creditors who do not support them.

The CVA under the Insolvency Act is more likely to be pursued when the company is insolvent. It should be noted that the Insolvency Act envisages scenarios where administrators or liquidators can commence a CVA. For schemes of arrangement under the Companies Act, in addition to liquidators, administrators and the company, creditors can also commence a scheme of arrangement. Schemes under the Companies Act are also utilised for solvent amalgamations and restructurings.

While the above processes need court sanction to take effect, this does not mean that companies, creditors and other stakeholders cannot enter into their own contractual restructuring arrangements. The general rule under Kenyan law is that once the parties have exercised their freedom to contract, the Kenyan courts cannot interfere with that freedom.[1] Kenyan courts[2] have also inferred that English court decisions[3] have held that the autonomy of the will of the parties should be respected and the law of contract should give effect to the reasonable expectations of the contracting parties unless it is shown that a contract was entered into fraudulently or under a misrepresentation.[4] The point here is that if, for example, a company and its creditors enter into a compromise agreement on the repayment of debts, a court would not interfere with such an arrangement and would respect the parties' freedom to contract. This is despite the fact that the compromise may not have been commenced through the procedures under the Companies Act.

### 1.1 Formal restructuring procedures

#### *1.1.1 Schemes of arrangements or compromises under the Companies Act*

A scheme of arrangement or compromise (in contrast to a CVA) is a procedure under the Companies Act. A company may make a compromise or arrangement with its members or creditors (or any class of them). There is nothing in the legislation that prescribes the subject matter of a scheme or what it should or should not entail and therefore the particulars of the process itself are determined by the relevant stakeholders. In theory, a scheme could be a compromise or arrangement about anything the company and its creditors or members may properly agree on among themselves. A company can effect almost any kind of internal reorganisation, merger or demerger using a scheme, as long as the necessary approvals have been obtained under the Companies Act. The use of the words "arrangement" or "compromise" is based more on practice and the words do not have a prescriptive legal meaning. "Arrangement" is defined in the Companies Act, but not in an exhaustive manner.[5] In practice, a "compromise" envisages the existence of a dispute (disagreement) which is solved by parties settling their differences by making mutual concessions. Arrangements do not necessarily need compromises or the existence

1 *John Chamia & Others v Board of Trustee National Social Security Fund & Another* [2013] eKLR.
2 *Aineah Liluyani Njirah v Aga Khan Health Services* [2013] eKLR.
3 *Darlington Borough Council v Wiltshier Northern Limited* [1995] 1 WLR 68, 76.
4 *Ecuricor Courier (K) Ltd v Benson David Onyango & Another* [2008] eKLR, where the Court of Appeal referred to the case of *L'Estrange F Graucob Limited* [1934] 2 KB 394.
5 An "arrangement" is defined to include a reorganisation of the company's share capital by the consolidation of shares of different classes, or by the division of shares into shares of different classes, or by both of these methods.

of a dispute and as such reference to a scheme of arrangement includes a compromise, reconstruction and amalgamation. These concepts will be referred to as schemes or schemes of arrangement below.

### *1.1.2 What is the procedure for a scheme of arrangement?*

Schemes can be proposed between a company and its creditors or any class of its creditors, or between the company and its members or any class of its members.

An application to court for the approval of a scheme of arrangement can be made by:[6]

- the company;
- any creditor or member of the company; or
- if the company is in liquidation or under administration, the liquidator or administrator.

On application, the court may issue preliminary orders for a meeting to be held by the creditors (or class of creditors) or by the members (or class of members) and the modalities for convening such meetings. Once the orders are made, the company is obligated to ensure that each notice convening the meeting that is sent to a creditor or member includes, or is accompanied by, a statement which provides the following information:

- the effect of the proposed scheme, any material interests of the directors (whether as directors or shareholders or as creditors) and the effect of those interests on the scheme; and
- where the proposed scheme affects the rights of debenture holders, the company is obliged to include in the statement similar disclosures as those made with respect to the directors – that is, an explanation of the debenture holders' material interests and the effect of those interests on the scheme.[7]

### *1.1.3 Voting for approval of the scheme of arrangement*

Once the meeting has been convened, the threshold required for the approval of a scheme is 75% in value of either the creditors or a class of creditors, or the members or a class of members, present and voting in person or by proxy.[8]

Once the voting threshold has been met, the company, any creditor or member, or the liquidator / administrator may apply to court for the sanctioning of the scheme.

Once a scheme has been sanctioned by the court, it is binding on the creditors or class of creditors, including the creditors who may not have consented and / or voted for the scheme. The scheme also binds the company and the liquidator or administrator. The order of the court sanctioning a scheme has no effect until a copy of it has been lodged with the Registrar of Companies.

### *1.1.4 Ancillary orders a court can make upon sanctioning of a scheme*

Once an order approving a scheme is made, the court can also make orders in relation to the following matters, which would be contained in the proposal filed in court (if such matters are before the court):

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6 Companies Act, s 923(2).

7 It is an offence not to provide this information and each officer found guilty may be liable to a fine not exceeding KES 500,000. For the purpose of s 924, an officer of the company is defined to include an administrator, liquidator or the trustee of a debenture holder. As such, debenture holders may be held liable for not providing information to the company.

8 Companies Act, s 926.

- the transfer to the transferee company of the whole or any part of the undertaking and of the property or liabilities of a transferor company;
- the allotting or appropriation by the transferee company of any shares, debentures, policies or other similar interests in the company that, under the scheme, are to be allotted or appropriated by the company to or for any person;
- the continuation by or against the transferee company of any legal proceedings pending by or against a transferor company;
- the dissolution, without liquidation, of a transferor company;
- the provision to be made for any persons who, within such period and in such manner as the court directs, dissent from the scheme; and
- such incidental, consequential and supplemental matters as are necessary to secure that the reconstruction or amalgamation is fully and effectively carried out.

Once the court pronounces on matters related to the transfer of property and liabilities of a company, the property is deemed to vest in the transferee company, as do the liabilities. Transferred property is deemed to be free from all charges and / or encumbrances if the court issues such an order.

Each company affected by the order is required to file the order with the Registrar of Companies within seven days of the court making the order.

Unlike in the case of monitors under the Insolvency Act, the Companies Act is not clear on who supervises the process but since the process is sanctioned by the court, the court would presumably have overall oversight. The concerned stakeholders would also retain the right to challenge the actions of any person appointed by the court to implement the process if they do not comply with the court orders. Where the company is also under administration or in liquidation under the Insolvency Act, the administrator or liquidator would be in charge of the process.

### *1.1.5 CVA*

A CVA is defined in the Insolvency Act to mean a composition or arrangement proposed by the directors of a company which sets out the solutions that the directors propose be adopted to change the fortunes of a financially distressed company. It takes effect once approved by the court.[9] A proposal for a CVA is made by the directors of the company and, if approved by the creditors and the court, a monitor is appointed to oversee the implementation of the arrangements under the proposals. Where a company is in administration, the administrator also has the right to propose that the company enters into a CVA if he / she deems it fit that such course would be the best for the insolvent company.[10]

### *1.1.6 Moratorium during a CVA*

The directors of a company applying for a CVA have the right to also apply for a moratorium preventing any legal action against the company by creditors before the CVA is finalised. Unlike administration, the effect of the moratorium in a CVA is not set out in the Insolvency Act and its effect is therefore dependent on the nature of the orders given by the court.

There are eligibility criteria applied to determine whether a company qualifies for a moratorium during a CVA, including the requirement that the debts of the company should not exceed KES 1 billion. Companies with debts that exceed this monetary threshold are not eligible for a moratorium. In addition, the moratorium is only valid until such time that the creditor meetings are held to approve a CVA.

9 Insolvency Act, s 630.
10 *Idem*, s 625(4)(a).

When a company's directors propose a CVA, for a moratorium to take effect, an application has to be made to court. The moratorium is only effective during the period between when the proposal is made and when the proposal takes effect. One implication of a moratorium is that the company is restricted in obtaining credit or paying its debts and liabilities during this period. Further, any steps taken to enforce security over the company's property can only occur with the sanction of the court and the court may impose conditions on the sanction. Also, approval of the court is required where proceedings are commenced against the company or its property.

Security given by a company at a time when a moratorium has effect in relation to the company can only be enforced if, at that time, reasonable grounds existed for believing that enforcement of the security would benefit the company. A company in respect of which a moratorium has effect may dispose of any of its property only if there are reasonable grounds for believing the disposal will benefit the company and the disposal is approved by the moratorium committee. It is important to note, however, that a company may transfer property as if it were not subject to the security only where the holder of the security consents, or the court gives its approval.

### *1.1.7 Procedure for commencing a CVA*

The proposal for a CVA (once prepared) is to be provided to the creditors and the shareholders of the insolvent company. The proposal may contain the name of the individual the persons proposing the CVA wish to act as provisional monitor, and this could also be the administrator. It should be noted that the monitor is required to be a qualified insolvency practitioner under the Insolvency Act.

Once an administrator is appointed in an administration, he / she is obligated to prepare a proposal setting out how he / she intends to achieve the objectives of the administration. In terms of the Insolvency Act, the administrator may include the proposal for a CVA while preparing the proposals for the administration.[11]

Where the monitor appointed is not the administrator or the liquidator, the monitor (who is deemed to be a provisional monitor before confirmation by the court) is required to submit a report to the court within 30 days of receiving notice of his / her appointment, setting out the following:

- whether, in the monitor's opinion, the proposal has a reasonable prospect of being approved and implemented;
- whether, in the monitor's opinion, meetings of the company and of the company's creditors should be convened to consider the proposal; and
- if the monitor believes those meetings should be convened, the date, time and place it is proposed to hold the meetings.

The directors making the proposal for a CVA are obligated to provide information to enable the monitor to prepare the report, including: (i) a document setting out the terms of the proposal; and (ii) a statement of the company's financial position containing particulars such as information relating to its creditors, debts, other liabilities and assets as prescribed by the Insolvency Regulations. The information must be provided 14 days before the proposal is lodged in court for approval. The provisional monitor may be removed from office by an application made to court by a creditor, the makers of a proposal or the monitor if he / she has failed to file the report within the prescribed time or is unable to act by reason of some incapacity.

Once the monitor files a report in court, if he / she is not the liquidator or administrator and if the report contains a proposal that creditors' meetings should be convened to approve the proposal for a voluntary arrangement, he/ she is obligated to convene the meetings as prescribed in the proposals unless the court otherwise directs. Where the monitor is the administrator or liquidator, the convening of the creditors' meetings is based on the administrator's or liquidator's discretion. The persons to be summoned to a creditors' meeting are all the creditors of the company of whose claims and addresses the provisional monitor is aware.

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[11] *Idem*, s 566.

### 1.1.8 *Approval of a proposal by a creditors' and shareholders' meeting*

Where the monitor proposes that creditors' and shareholders' meetings should be called, the main purpose of the meetings is to decide whether to approve the proposal for a CVA with or without modifications. The creditors' meeting is required to appoint a chairman as the first order of business who will oversee the conduct of the meeting. Once appointed, during the first meeting the chairman is required to divide the creditors into three classes for voting purposes, with the first class comprising secured creditors (if any), the second class comprising preferential creditors (if any) and the third class comprising unsecured creditors.

An approval or modification of a proposal is deemed to be passed:

- if passed by a majority of the members of the company present (either in person or by proxy) at the meeting of the company and by a majority (in number and value) of each group of creditors present (either in person or by proxy) at the meeting of creditors; or

- if, despite not being not approved by a majority of the members, it is approved by a majority (in number and value) of each of the classes of creditors.

From the above, it would appear that a combination of both thresholds may not be necessary for a decision to be deemed to have been made. This is because, in circumstances where the first threshold is not met but a decision has been approved by a majority (in number and value) of each of the classes of creditors, then the decision is still held to have been validly passed. The consequence of this is that the votes of the shareholders do not have an impact where the company has creditors.

Secured creditors enjoy certain protections in relation to their security rights. If the proposal or a modification to it affects the right of a secured creditor of the company to enforce the creditor's security, it may not be approved unless:

- the secured creditor consents to it; or

- if the secured creditor does not consent to it, the secured creditor:

  - would be in a position no worse than if the company was in liquidation;

  - would receive no less from the assets to which the secured creditor's security relates, or from their proceeds of sale, than any other secured creditor having a security interest in those assets that has the same priority as the secured creditor's; and

  - would be paid in full from those assets, or their proceeds of sale, before any payment from them or their proceeds is made to any other creditor whose security interest in them is ranked below that of the secured creditor, or who has no security interest in them.

The above carve-out protects secured creditors who do not consent to proposals.

Any creditor or member who was entitled to attend and vote at a meeting has the right to make an application to the court seeking an order for the approval of a proposal with or without modifications. The court is duty bound, before making an order, to have regard to the various interests and rights accruing to different classes of creditors and should make an order only if a proposal or modification:

- has been approved by a majority of the secured creditors' class;

- does not discriminate among the members of the dissenting group or groups of creditors and ensures that they will be no worse off than they would have been if the company had been liquidated; and

- respects the priorities of preferential creditors over unsecured creditors.[12]

### 1.1.9 How is a CVA implemented and what are the consequences?

When a proposal takes effect as a CVA, the monitor becomes responsible for "monitoring" the implementation of the arrangement by the directors in the interests of the company and its creditors and monitoring compliance by the company with the terms of the arrangement.[13]

### 1.1.10 Moratorium

The directors of a company have the option of applying to court to be granted a moratorium against legal action while the company is reorganising its affairs. Only eligible companies are allowed to apply for a moratorium. A company is ineligible if:

- it is in liquidation, under administration or a receiver has been appointed over its assets, or it underwent administration within 12 months prior to the application for a moratorium;
- it underwent a CVA within 12 months prior to the application for a moratorium;[14] or
- the company has debts due under an agreement that exceed KES 1 billion, whether or not such debts are contingent or certain.

The application for a moratorium accompanies the application for a CVA. Where a company elects to apply for a moratorium, the application to court for a CVA proposal should also include, inter alia, a statement to the effect that the company is eligible for a moratorium under the Insolvency Act. Unlike administration, a moratorium is not automatic.

A moratorium takes effect on the date the application is filed in court. Once effective, the monitor has to advertise in at least two newspapers and in the Kenya Gazette informing the public that a moratorium over the company is in effect. The moratorium comes to an end on the date the creditors' and shareholders' meetings are held to approve a CVA proposal.

### 1.1.11 Who does the CVA bind?

On taking effect, a CVA binds:[15]

- every member of the company who:
  - was entitled to vote at the meeting of the company (whether present or represented at the meeting or not); or
  - would have been so entitled if the member had received notice of that meeting; and
- every person (including a secured creditor and a preferential creditor) who:
  - was entitled to vote at the meeting of creditors (whether present or represented at the meeting or not); or
  - would have been so entitled if the person had received notice of that meeting, as if the member or person were a party to the arrangement.

It is not, however, clear whether this applies to instances where the CVA was orchestrated by an administrator, as the Insolvency Act speaks of a CVA proposed by the directors of the company as opposed to an administrator. The management of the debtor remains in office to implement the

12 *Idem*, s 629.
13 *Idem*, s 633.
14 *Idem*, s 640.
15 *Idem*, s 630 (2).

CVA. However, a monitor has to be appointed to "supervise" the implementation of the CVA and make appropriate recommendations to the court in case of breach or deviation.

### 1.2 Informal restructuring procedures

The restructuring options discussed in section 1.1 above have a significant feature: they need to be approved by the court before they can take effect. That being said, debtors and creditors in Kenya are at liberty to enter into arrangements that do not necessarily form part of the processes envisaged in the Companies Act or Insolvency Act. Some of these forms of restructuring debt are:

- refinancing – this involves paying off an existing loan or loans by taking a new loan or loans, usually on different terms. The main advantage of this is that it is the least disruptive option available and would help revive confidence in the company; the disadvantage is that it is difficult to attract investors to a company on the verge of insolvency. Typically, what would be seen here is that a company with debts that are about to mature would approach another lender to refinance the existing debt. The result is that the company is afforded more time to repay the debts it owes and a revision of the payment terms;

- debt rescheduling – a borrower may opt to defer debt service repayments and apply for new and extended maturity terms for existing loans. The borrower would need to approach lenders or creditors for approval / consent to explore this option to, for example, pause payments or reduce payment amounts during a given period and then increase the amount of the monthly instalments; and

- debt for equity swap – some lenders may be agreeable to swapping their debt with equity in the companies. An example of this avenue of restructuring is the recent debt restructuring undertaken in respect of Kenya Airways, where the Kenyan Government and other local lenders converted the bulk of their debt to shares.

## 2. Restructuring of ESG-related liabilities

### 2.1 Environmental (E): restructuring environmental liabilities

There is still no proof of strict environmental culpability in cases of environmental damage, despite the progressive Constitution of Kenya (2010) making great strides in promoting environmental conservation and protection, with many environmental restoration and protection initiatives being left to the states. The states' desire and obligation to protect people's rights to a clean, healthy environment, as well as the fact the environment is seen as the primary source of the majority of the resources required for the realisation of economic and social rights, necessitates environmental liability.

The Companies Act and the Insolvency Act are the primary statutes guiding the restructuring of companies. They cover the alteration and consolidation of a company's share capital as well as regulating compromises, arrangements, reconstructions and amalgamations. It is therefore fitting that under the Companies Act for example, there are provisions that provide for environmental liability to be imposed on the directors of a company.

Under section 143 of the Companies Act, a director has the duty to promote the success of the company and must be considerate of the impact the operations of the company have on the community and the environment. Further, under sections 655(4)(b) and 656(b), directors of a company are required to specify in their business review / report information on any environmental matters, and this is inclusive of the business of the company on the environment.[16] The Insolvency Act, however, is not as prescriptive as the Companies Act.

Evidently, directors can be held liable for the environmental failures of their companies, as it is their duty to not only be cognisant of the impact operations of the company have on the community and the environment, but also report the same in their annual reports. In terms of restructuring, there is no set law that governs environmental liability in restructuring. However, it is

16 *Idem*, ss 655(4)(b) and 655(6)(b).

worth noting that a general regime of environmental liability for companies exists under the Constitution of Kenya (2010).

In the Preamble of the Constitution, the environment is hailed as the heritage of the Kenyan people and it is stated that the people of Kenya are determined to sustain it for the benefit of future generations. Article 42 of the Constitution provides that everyone has the right to a clean and health environment, which includes the right to have the environment protected for the benefit of present and future generations. Furthermore, articles 69 and 70 of the Constitution provide for the obligation of the Government to protect the environment and ensure the enforcement of environmental rights.

These constitutional provisions bind companies, as they have environmental obligations as artificial persons under the Constitution. Breach of these obligations could result in the enforcement of environmental rights against the company and sanctions such as compensation for any victim of the right to a clean and healthy environment. The section below explores the restructuring of environmental liabilities under Kenyan law and practice.

#### *2.1.1 Types of environmental liabilities*

Environmental liability refers to an obligation a company has to a third party which may result in future payments due to past events in order to compensate a third party for harm caused by environmental damage of the company. Liabilities that may arise can be categorised as legal obligations, contractual obligations and court-mandated obligations.

Legal obligations with regard to environmental liability refers to obligations found in statue or regulations, for example rehabilitation of land. Contractual liability arises out of a company's internal commitment to environmental safeguards. Court-mandated obligations refers to obligations in the form of a fine or compensation as a result of a court decision.

#### *2.1.2 Priority given to environmental liabilities*

Schedule 2 of the Insolvency Act sets out the order of priority of debts / liabilities of a company that is in liquidation. The priority of claims / liabilities is designated as first, second, third and unsatisfied priority claims. It is instructive to note that Schedule 2 does not prescribe specific rankings based on environmental liabilities and therefore from this perspective there is no prescribed priority that is granted for environmental liabilities.

Under each priority level, no mention is made of environmental liability such as land claims, pollution claims or restitution claims for communities affected by environmental issues caused by the company.

#### *2.1.3 Disclaimer of environmental obligations*

There is no law that prohibits the disclaiming of environmental liability during restructuring. However, it should be noted that third parties have a strong legal regime under the Constitution of Kenya, the Companies Act and the Environmental Management and Coordination Act, among other laws that have been used in court by affected communities to claim damages, and action from companies to mitigate or stop their environmental liabilities.

### 2.2 Social (S): restructuring health or safety-related liabilities

The insolvency and restructuring regime has largely remained unchanged until 2016, when new company laws and insolvency laws were enacted. These laws are still in their formative stages in terms of application and the development of jurisprudence on various areas. Health and safety is one of these areas. The ESG landscape is generally in its emerging stages and many stakeholders are just coming to terms with what ESG means and what measures need to be adopted to promote it in business and restructuring. Generally, from a legal and practical perspective, restructurings do not typically involve differentiation of ordinary liabilities from health or safety related liabilities.

That being said, the COVID-19 pandemic has led to changes to working life as it was conventionally understood by both companies and employees. Employees are looking for more flexible work environments. Potential employees are also interested in working for companies that are active champions of ESG in their culture and work policies. In cognisance of the new labour trends, Parliament is seeking to amend employment laws through the Employment (Amendment) Bill 2021. The Bill is aimed at addressing increased employee burnout and promoting employees' work life balance. Manufacturers have had to change how they market their products and services to consumers given the recent legislative changes. However, even beyond legal requirements, consumers are driving change by demanding socially responsible behaviour from companies, which goes beyond the traditional annual corporate social responsibility public relations event. With increased consumer activism in Kenya and in this day and age of social media cancel culture, companies have realised that consumers want to be associated with brands that are sensitive to climate change and sustainability concerns but can very quickly turn on brands that are found to be continuing practices on the wrong side of this trend.

Another key area of focus under the "social" umbrella is gender equality, which is enshrined in the Constitution. The Capital Markets Authority has issued Guidelines on Corporate Governance Practices by Publicly Traded Companies, which require boards to implement policies that assure diversity, including female diversity, in their composition. The NSE (Nairobi Stock Exchange) has also set a goal for Kenya's 65 listed businesses for at least a third of the board members to be female.

Data privacy has risen to the forefront of consumer concerns in recent years. Following global landmark data privacy breaches, governments have begun to regulate data protection, commencing with the landmark General Data Protection Regulations (GDPR) driven by the European Union. In Kenya, the Data Protection Act 2019 is steadily being implemented with the release of various data protection regulations in 2021, which will impact how organisations in Kenya manage the data that they collect. Purpose, openness, participation, constraints on usage and collection limitations have to be considered by organisations collecting personal data.

### 2.3 Governance (G): third party releases in favour of directors and officers of the company

In order to foster and sustain economic growth, governance matters have become increasingly important. A core framework for governance-related matters is the Companies Act, which in many instances places personal liability on directors of companies to ensure compliance, and the Insolvency Act, which also places various duties on directors. Moreover, many companies are choosing to follow global industry best practice and opting into standards and reporting indexes such as the IFC Performance Standards, Sustainability Accounting Standards Board and the Global Reporting Initiative. Accordingly, the Central Bank of Kenya and the Nairobi Stock Exchange have launched guidelines that require the board of directors and senior management to take an active role in formulating and implementing ESG strategies, policies and reporting requirements. This, together with the Companies Act, places a greater responsibility on the directors of companies to report on matters related to ESG issues.

The Central Bank of Kenya Guidance requires financial institutions to disclose climate-related information under the framework of the Task Force on Climate-Related Financial Disclosures. The guidance has placed reporting obligations on the board of directors and senior management.

The liability of directors can generally be split into two categories: duties owed under the Companies Act and duties owed under the Insolvency Act.

#### *2.3.1 Companies Act*

The Companies Act codifies certain duties that directors need to take into account in their capacities as directors. If these duties are breached, the directors may be held liable personally in the event it is determined during a liquidation that they acted contrary to their duties. Below are some of the duties under the Companies Act that are significant in a case such as this:

- the duty to promote the success of the company – directors are required to act in good faith and in ways that would promote the company's success for the benefit of members, having regard to the long-term consequences of their decisions, the interests of employees, the impact of the company's operations on the community and the environment and the need to act fairly as between directors and members;

- the duty to exercise independent judgment – this duty requires directors not to fetter their discretion when exercising their powers.[17] It is expected that every decision a director makes is based on their independent judgment of the situation and matters at hand; and

- the duty to exercise reasonable care, skill and diligence – this duty is heavily subjective and is based on the skills and experience that a director actually had. The Companies Act, however, mitigates the subjective nature of this duty by adding an objective element, making it a dual subjective / objective threshold.[18]

In light of the foregoing, it may be said that the overarching role directors have with regard to the company is to promote its success and to preserve, protect and grow the company's investments.

However, in an insolvency scenario, the duty to promote the success of the company gradually shifts to a duty to act in the best interests of the company's creditors. Section 143 of the Companies Act sets out the duty to promote the success of a company but qualifies this duty in subsection (3) by stating that "the duty imposed by this section has effect subject to any law requiring directors, in certain circumstances, to consider or act in the interests of creditors of the company". This implies that, when facing a solvency crisis, the directors should be careful to deliberately protect the value of the company's assets and minimise losses to creditors as far as possible.

Directors can be exposed to various claims for personal liability arising from breach of the above duties. The Companies Act provides that any provision that purports to exempt a director from liability for negligence, default, breach of duty or breach of trust in relation to the company is void[19] and any provision where the company or associated company is seeking to indemnify a director for such liability is also void.[20]

A court may relieve directors from liability if they acted honestly and reasonably. However, it will only do so if, in its opinion, and having regard to all the circumstances of the case, the director ought fairly to be excused.[21] The relief may be in full or in part, and on such terms as the court thinks fit. As such, if a claim is brought against a director and it is proven that he / she acted honesty and reasonably, then the court may dismiss the claim.

The Companies Act also sets out various penalties depending on the particular duty that has been breached by a director. It is important to note that a director in breach will be personally liable to the company and in addition, shall be liable to repay the company for any loss incurred. Personal assets may also be attached if a finding of liability is made by the court.

The Companies Act imposes fines ranging from Kenya Shillings one hundred thousand to one million (KES 100,000 to KES 1,000,000) where a director is found liable. These fines are discretionary and it's upon the court to determine what penalty to impose. Furthermore, officers may be held liable for defaulting on certain acts, for example, failure to keep proper records.

### *2.3.2 Insolvency Act*

Under the Insolvency Act, where a company is performing badly or is in financial difficulty, there is a potential for directors to become liable for the company's losses.

The law does not expressly state at what point directors should cease trading and what steps they need to take but the general standards as set by case law are that the directors ought to take every

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17 *Idem*, s 144.
18 *Idem*, s 145.
19 *Idem*, s 194(2).
20 *Idem*, s 194(3).
21 *Idem*, s 763.

step and minimise the potential loss to creditors. As a result, directors can be held liable for wrongful trading or fraudulent trading.

The Insolvency Act provides that if, in the course of the liquidation of a company, it appears that a person knew or ought to have known that there was no reasonable prospect that the company would avoid being placed in insolvent liquidation, the liquidator may make an application to the court and the court may make an order declaring the person to be liable to make such contribution to the company's assets as the court considers appropriate.[22] This extends to corporate directors, not just individuals.

No order can be made if the court is satisfied the person took steps to avoid potential loss to the company's creditors as the person ought reasonably to have taken.[23] If the liquidator decides to investigate the director's conduct, the director would need to prove that his / her actions were reasonable. A key consequence of being found guilty of wrongful trading is that the court may also disqualify the relevant director from being or acting as a director of a company or a limited liability partnership for any period not exceeding 15 years.[24]

The consequences of fraudulent trading are the same as the consequences of wrongful trading. If in the course of liquidation of the company it appears that any business of the company has been carried on with the intent to defraud creditors, or for any other fraudulent purpose and the liquidator believes that such persons participated (directly or indirectly) in the business with the knowledge that the business was being carried on in that manner,[25] the court may order the person to make such contributions to the company's assets as the court considers fair and reasonable.[26]

Fraudulent trading is also a criminal offence under the Companies Act[27] and the offence is applicable whether or not the company has been liquidated or is in liquidation. A person found guilty of fraudulent trading is liable on conviction to imprisonment for a term not exceeding 10 years or a fine not exceeding KES 10,000,000 or to both.[28]

There is a lower burden of proof in order to prove wrongful trading compared to proving fraudulent trading. In principle it is therefore easier for a liquidator to obtain an order for wrongful trading than for fraudulent trading and the consequences are the same as the court on consideration of the application may order the director to contribute personally.

It should be noted that the structure and content of a scheme of arrangement or a CVA is not set out in law and this means is that the directors who are making proposals begin on a blank slate. As a result, they can propose third party releases, for example of their obligations under guarantees, but a proposal to release their liability will be subject to various stages of confirmation or approval. These stages would include: (i) the approval of the creditors during the voting stage; the (ii) approval of the court once the proposals are filed in court and the court determines whether the interests of the company and creditors are catered for; and (iii) for CVAs specifically, the confirmation by the monitor in his / her report on the suitability of a CVA.

That being said, the CVA is binding for as long as the company is going through the CVA process and in the event the CVA becomes ineffective and for example the company goes into liquidation or administration, a liquidator or administrator would then have the right and power to investigate whether any transgressions were committed by the directors as discussed above.

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22 Insolvency Act, s 506(5).
23 *Idem*, s 506(6).
24 *Idem*, s 506(8)(a).
25 *Idem*, s 505(1).
26 *Idem*, s 505(2).
27 Companies Act, s 1002.
28 *Idem*, s 1002(3).

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

In Kenya, ESG discourse is still at its infancy stages and various stakeholders are just beginning to inculcate ESG-oriented policies within their businesses. That being said, Kenya does have environmental protection laws but from a restructuring perspective approval of restructuring proposals is not strictly tied to environmental issues, and the key theme has been on the repayment of debts owed.

As indicated above, approval of restructuring proposal is by the High Court. There is no express requirement that proposals also be submitted to environmental protection authorities, but from a plain reading of the environmental laws, it is arguable that the proposals should adhere to any environmental standards set by law in case the proposal has an element on environmental protection. As an illustration, if a restructuring proposal included projects that have some impact on the environment, Kenya law requires that plans for such projects be submitted to the environmental protection authority for verification and analysis on whether it may have a negative impact on the environment (commonly referred to as an environmental impact assessment, after which, if approval is granted, the project receives a licence to go ahead). Courts in Kenya regularly enforce environmental laws, although we are yet to see case law specific to a restructuring proposal that has been subjected to environmental laws or compliance with them.

As an example, in 2020, the Mombasa Land and Environment Court awarded compensation to the inhabitants of a settlement and concluded that the community's rights to life, a healthy environment, the greatest possible quality of health and clean and safe water had been violated. The court also ordered the Kenyan Government and two businesses to pay damages. The lead poisoning from a local smelter that recycled batteries had caused terrible effects on the environment and the health of the community. Consequently, the residents of the settlement were awarded the equivalent of US $13 million in compensation.

It would be expected that a concerned stakeholder would have the right to approach the courts for redress and / or remedy if a restructuring proposal potentially had harmful effects on the environment. In such a case, it would be up to the court to determine, based on the merits of the case, whether there had been or there was potential for the environment being harmed. It would then be up to the court to make the appropriate orders, for example ordering compliance with or implementation of environmentally-friendly proposals.

#### *3.1.1 Approving a restructuring plan*

As indicated above, restructuring plans require court approval. The approval of restructuring proposals is not strictly tied to environmental concerns, but note the analysis provided above.

#### *3.1.2 Discretion to consider wider public interest concerns*

See above for discussion of this issue.

#### *3.1.3 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

See above for discussion of this issue.

### 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

Health or safety-related liabilities refer to any costs, expenses or obligations that may arise from any form of environmental law or occupational safety and health law. Article 43 of the Constitution provides for the right to the highest attainable standard of health and the right to clean and safe water in adequate quantities.[29] Furthermore, under the Constitution, the Government is tasked with the control of air and noise pollution, other public nuisances and outdoor advertising.[30] Article 46 also provides that consumers are entitled to the protection of their health, safety and economic interests.[31] The enforcement of the above stated rights is usually through the court system as enshrined in article 70 in the Constitution.[32]

The safety liability of employees is covered under the Occupational Safety and Health Act (2007) (OSHA), which makes provisions for general health considerations such as cleanliness, overcrowding, ventilation, lighting, drainage of floors and sanitary conveniences.[33] Furthermore, the OSHA sets out general safety provisions and chemical safety provisions.[34] The enforcement of these rights is through local authorities or the court system.[35] Companies that do not adhere to the health and safety standards under the OSHA can be sued by employees in a court of law.

Nevertheless, there are approval thresholds for restructuring plans (see section 1 above) and employees are critical in these processes. Unionised employees are represented by their unions, which advocate for their rights. In a restructuring, given the need for approval by employees since they are by law considered to be preferential creditors, it would be expected that restructuring plans would involve proposals that address any health, safety or other concerns that employees have. Otherwise, the proposal would risk failing for lack of approval. In addition, labour issues in Kenya are dealt with by the labour court, a special court established through the Constitution whose mandate is to adjudicate over employment matters only. This is a unique milestone in Kenya and employees who may feel disgruntled by a recurring plan that perhaps does not address safety, health or other concerns, may approach the court seeking redress.

#### *3.2.1 Approving a restructuring plan*

These issues are considered above.

#### *3.2.2 Discretion to consider wider public interest concerns*

These issues are considered above.

#### *3.2.3 Protection of employee rights*

These issues are considered above.

### 3.3 Governance (G): board / management conflicts addressed in a restructuring

In CVAs, directors remain in control of companies but they are usually under the supervision of a qualified insolvency practitioner referred to as a monitor. This occurs after the CVA becomes effective after approval by the court, and the monitor becomes responsible for "monitoring" the implementation of the arrangement by the directors in the interests of the company and its creditors and monitoring compliance by the company with the terms of the arrangement. The role of monitor is to ensure that the arrangements under the terms of the CVA proceed accordingly and to report on progress to creditors. The monitor is an officer of the court and must act impartially and objectively. Therefore, in performing this function, he / she must balance the interests of the creditors and the company. A monitor's obligations also include dealing with a failure of a CVA in bringing it to a close (this is often set out in the terms of the proposal).

For CVAs, what this means is that the directors have to adhere to the terms of the CVA – otherwise, any creditor or the monitor can approach the court for a remedy.

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29 Constitution of Kenya (2010), arts 43(1)(a) and 43(1)(d).
30 *Idem*, Fourth Schedule, Part 2 (3).
31 *Idem*, art 46.
32 *Idem*, art 70.
33 Occupational Safety and Health Act (2007), Part VI.
34 *Idem*, Part IX.
35 *Idem*, s 53.

For schemes of arrangement, unlike in the case of monitors under the Insolvency Act, the Companies Act is not clear on who supervises the scheme but since the process is sanctioned by the court, the court would presumably have overall oversight. The concerned stakeholders would also retain the right to challenge the actions of any person appointed by the court to implement the process if they do not comply with the court's orders. Where the company is also under administration or in liquidation under the Insolvency Act, the administrator or liquidator would be in charge of the process.

Ultimately, the directors would still be bound by their statutory and common law obligations in the performance of their duties. As an example, directors are obligated to act in the best interests of the company and to avoid conflicts of interest and therefore, in situations where there are board or management conflicts, a qualified stakeholder such a creditor would have the right to approach the court for remedy and hold the directors liable for breach of their duties.

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

We have not identified any industry guidelines and / or best practices prescribed for the protection of the environment in a restructuring.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

We have not identified any industry guidelines and / or best practices prescribed for the protection of employee rights in a restructuring.

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

We are not aware of any specific industry guidelines or codes of conduct.

## 5. ESG in financing

Over the past few years, ESG considerations have gained popularity among different parties such as corporations, investors, regulators and consumers of goods. Corporations are taking into account key considerations in ESG issues as a value addition rather than a risk mitigation measure. Investors are now prioritising ESG and sustainability issues as a key metric for assessing potential investment projects. Financial institutions, with regard to public-private partnerships, are looking to assist governments in the development of infrastructure that is sustainable and takes into account the community it serves and the environment around it.

Further, there has been a shift in Kenya to prioritise the use of renewable energy. The Government has aimed to increase the production of renewable energy in its overall Least Cost Power Development Plan for the years 2017 to 2037.[36] By 2037, it is anticipated that just over 60% of the nation's installed electricity capacity will come from renewable sources.[37]

Kenya has a strong legal framework for environmental protection. This entails article 42 of the Constitution that provides the right to a clean and health environment and article 69 of the Constitution that requires the State to fulfil its mandate with regard to environmental preservation and protection.

Furthermore, the Kenyan Government since 2017 has made steps towards committing to climate change and environmental protection. The Government of Kenya was one of the first countries to ratify the Paris Climate Agreement. In 2017, the Government banned the use, manufacture and

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36 EPRA, Least Cost Development Plan, 48.

37 IRENA Report, 2018, 9, available at: https://www.irena.org/media/Files/IRENA/Agency/Publication/2018/Apr/IRENA_Report_GET_2018.pdf.

importation of single use plastic bags for both commercial and household packaging. Since then, manufacturers have sought to make packaging that is environmentally friendly.

Furthermore, Kenya at COP 26 made several commitments towards net zero emissions. Since then, Kenya has launched the Kenya Carbon Emissions Reduction Tool that is a data driven policy-making tool assessing project emissions generated by various sectors with the aim of developing action plans and long-term energy strategies on reduction of the measured emissions.[38] Further, Kenya has developed the Kenya Private Sector Strategy on Climate Change Solutions and the National REDD+ Strategy.[39] The former applies to the private sector and guides the implementation of climate change-oriented solutions that are geared to low carbon emissions. The latter is a strategy developed to reduce emissions from deforestation and ensure sustainable management of forests.

Kenya further made several commitments at COP 27 on upholding the goal for net zero emissions and the use of renewable energy by decommissioning power plants that utilise non-renewable energy such as coal and oil. Further, the Kenyan Government at COP 27 signed a deal with Fortescue Future Industries to establish a green hydrogen and ammonia plant in a bid to meet commitments of utilising green energy.[40]

Gender equality, which is a significant focal area under the "social" umbrella of ESG, is a principle that the Constitution upholds.[41] According to the Capital Markets Authority's (CMA) Guidelines on Corporate Governance Practices by Publicly Traded Companies, boards must undertake procedures that ensure diversity in their membership, including gender diversity.[42] The Nairobi Securities Exchange (NSE) has also set a target that at least a third of the board members at Kenya's 65 listed companies must be women.

Under the governance ambit of ESG, the Kenyan Government through the Central Bank of Kenya (CBK) and the NSE, has released the Guidance on Climate-Related Risk Management that mandates board directors and senior management to have an active role in the making and implementation of company-formulated ESG strategies and policies.[43] Furthermore, both directors and senior management are required to be actively involved in helping their companies meet reporting requirements on ESG considerations. The CBK has also issued guidelines that require financial institutions to disclose any climate-related issues in accordance with the Task Force on Climate-Related Financial Disclosures framework. Under this guidance note, each institution is required to submit a quarterly report to the CBK illustrating the progress of its implementation.[44]

For listed firms in Kenya, the NSE has released the ESG Disclosure Guidance Manual (NSE Guidelines) in collaboration with the Global Reporting Initiative (GRI). The NSE Guidelines offer listed businesses a manual for gathering, analysing, and disclosing ESG information about their commercial activities.[45] With mandatory reporting starting in November 2022, listed businesses on the NSE are required to disclose publicly their ESG performance at least annually. The CMA on the other hand released a Corporate Governance Code for Listed Companies in 2015. This Code provides a number of guidelines that businesses should incorporate into their operational frameworks. It calls for them to either put the Code's principles into practice or justify any deviations. Now, businesses are urged to conduct a governance audit at least once a year to ensure that they are adhering to good governance principles.[46]

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38 https://www.imperial.ac.uk/news/234494/kenya-carbon-emission-reduction-tool-kcert/ The tool can be accessed at: https://kcert.ilabafrica.ac.ke/.

39 https://www.standardmedia.co.ke/national/article/2001459628/kepsa-launches-private-sector-strategy-on-climate-change and https://www.un-redd.org/sites/default/files/2022-05/NATIONAL%20REDD%2B%20STRATEGY%202022.pdf.

40 https://www.fmgl.com.au/in-the-news/media-releases/2022/11/08/fortescue-future-industries-to-join-forces-with-the-government-of-kenya-to-eliminate-fossil-fuels-from-kenya's-fertiliser-supply-chain.

41 Constitution of Kenya (2010), arts 27(3) and 27(8).

42 Recommendation 2.1.5, Guidelines on Corporate Governance Practices by Publicly Traded Companies.

43 Guidance on Climate-Related Risk Management, 6.

44 *Ibid*.

45 https://www.nse.co.ke/wp-content/uploads/NSE-ESG-Disclosures-Guidance-Manual.pdf.

46 Recommendation 2.11, Guidelines on Corporate Governance Practices by Publicly Traded Companies.

### 5.1 ESG-linked loans, bonds or investments

The Kenya Green Bond Programme (KGBP) was introduced in 2017 with the goal of enhancing "green" investments by creating a domestic green bond market. The Kenya Bankers Association, NSE, Climate Bonds Concept, Financial Sector Deepening Africa, and FMO – Dutch Development Bank – brought the KGBP initiative together. Classes of bonds are labelled "green" if the issuer agrees to utilise the bond proceeds exclusively to finance or refinance "green" projects, assets, or commercial operations with an environmental benefit.

In 2019, the CMA launched a Policy Guidance Note on Green Bonds. By August 2019, the CMA approved the issuance of Kenya's first unlisted green bond. The green bond was issued by Acorn Project (Two) Limited Liability Partnership.

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

Pioneered by the Kenya Bankers' Association (KBA), the banking sector came together in 2013 to put together the Sustainable Finance Initiative (SFI) Principles: a Kenya-specific set of harmonised guidelines for sustainable development to be adopted across the industry in pursuit of meeting Vision 2030.[47] The SFI Principles are five principles that are focused on economic viability, inclusive growth, social and environmental risk management, resource scarcity and business ethics and values.[48] The Equator Principles, IFC Sustainability Framework, Nigeria Sustainable Banking Principles, African Development Bank (AfDB) Green Growth Policy, and Global Reporting Initiative (GRI) Guidelines are only a few of the best-practice standards that the principles harmonise with.[49]

Further, banks and mortgage financing businesses must incorporate the possibilities and risks associated with climate change into their governance structure, strategy, and risk management frameworks, according to the guidance note on climate-related risk management that the CBK published in 2021.

### 5.3 Promoting ESG by the central bank and regulators

As noted above, the CBK has published its Guidance on Climate-Related Risk Management, which requires banks and mortgage finance companies to integrate the opportunities and risks arising from climate change in their governance structure, strategy and risk management frameworks.[50] In addition to green banking practice and climate risk disclosure, banks can collaborate with their clients by offering advice on sustainable projects, in light of ESG principles. Banks act as trusted financial advisors in various business aspects, therefore, to ensure ESG compliance banks can offer corporations advice in complying ESG principles and guidelines.

As noted above, the CMA has also included ESG considerations in its Corporate Governance Code in the assessment of the strength of corporate governance frameworks for listed entities.[51] Further, the CMA and the NSE are signatories of the Marrakech Pledge that seeks to bring together all African Capital Market Regulators and Exchanges to act in favour of sustainable development by developing green capital markets, with a focus on promoting Africa as a prominent regional green financial marketplace and an attractive destination for green and climate-resilient investments.

47 https://www.fmo.nl/esg-in-kenya.
48 https://sfi.kba.co.ke/industry-principles#:~:text=Enhancing%20best%20business%20practice%2C%20leadership,inclusivity%20enabled%20by%20new%20technology.
49 https://www.greenfinanceplatform.org/policies-and-regulations/sustainable-finance-guiding-principles-adopted-kenyas-banking-industry.
50 EPRA, Least Cost Development Plan, 48.
51 Recommendation 2.3.6, Guidelines on Corporate Governance Practices by Publicly Traded Companies.

# MALAYSIA

# 1. General overview of the restructuring regime

## 1.1 Formal restructuring procedures

In Malaysia, there are three formal restructuring procedures provided for in the Companies Act 2016 (CA 2016): schemes of arrangement, judicial management and corporate voluntary arrangement.

### *1.1.1 Schemes of arrangement*

A scheme of arrangement is a statutory mechanism to carry out a formal compromise to bind all dissenting creditors and members, provided the statutory voting thresholds have been met.

A scheme of arrangement can be initiated by the company itself, its creditors or members, the liquidator (if the company had previously been wound up), or the judicial manager (if the company is under a judicial management order).[1]

One of the main benefits of a scheme of arrangement is that the company in distress can apply for a court-supervised restraining order, which essentially prohibits various forms of recovery and enforcement actions against the company.[2] When granting the restraining order, the court can impose certain conditions and may vary or discharge the restraining osrder upon the application of a creditor.[3] At the first instance, the restraining order granted is only for a period of not more than three months and the court may, on the application of the company, extend this period for not more than nine months, provided certain requirements are met.[4]

In a scheme of arrangement, the management powers of the company in distress remain with the board of directors.

A scheme of arrangement consists of three main stages:[5]

- Convening stage

  This is the first stage, and it involves an application to the court for leave to hold court-convened meeting(s) under section 366 of the CA 2016 for the purposes of considering and voting on the proposed scheme of arrangement. At this stage, it is incumbent upon the scheme company to adduce evidence of sufficient quality to persuade the court to act on the scheme and the company has a duty to make full and frank disclosure of all relevant facts and matters to the court, including the classification of creditors, the realistic prospects of success of the proposed scheme, as well as any allegation of abuse of process.[6] In terms of the classification of creditors, the test for identifying classes is that a class must be confined to those persons whose rights are not so dissimilar as to make it impossible for them to consult together with a view to their common interest.[7]

- Meeting stage

  This is the second stage, and it is where the court-convened meetings are held. Before the meetings take place, the creditors and / or members involved must be provided with an explanatory statement which sets out the effect of the compromise or arrangement under the proposed scheme, and in particular stating any material interests of the directors, whether as directors, members or creditors of the company or otherwise, and any different treatment of

1 CA 2016, s 366(1).
2 *Idem*, s 368.
3 *Idem*, s 368(1).
4 *Idem*, s 368(2).
5 *Sentoria Bina Sdn Bhd v Impak Kejora Sdn Bhd & Ors* [2021] 12 MLJ 690 (HC); *Mansion Properties Sdn Bhd v Sham Chin Yen & Ors* [2021] 1 MLJ 527; *Airasia X Bhd v BOC Aviation Ltd & Ors* [2021] 10 MLJ 942 (HC).
6 *Airasia X Bhd v BOC Aviation Ltd & Ors* [2021] 10 MLJ 942 (HC).
7 *Ibid*.

creditors and / or members with similar interests. In order for a proposed scheme of arrangement to be approved, it must be agreed to by 75% of the total value of the creditors or class of creditors or members or class of members present and voting either in person or by proxy at each meeting.

- Sanction stage

  This is the third and final stage. Provided the proposed scheme of arrangement has been duly approved by the scheme creditors and / or scheme members (as the case may be) at the meeting(s), the scheme company then applies for a sanction order from the court under section 366(4) of the CA 2016. In considering whether a sanction order should be granted, the court will take the following matters into consideration:[8]

  - whether there has been compliance with the provisions of the relevant statute;
  - whether the creditors and / or members have been correctly classified; and
  - whether the scheme of arrangement is such that an intelligent and honest person who is a member of the class concerned and acting in respect of his / her interest might reasonably approve.

### 1.1.2 *Judicial management*

Judicial management is a new corporate rescue mechanism under the CA 2016 where a qualified insolvency practitioner may be appointed by the court as judicial manager to manage the affairs of an insolvent company.

A judicial management order can be applied for by the company in distress acting pursuant to a members' resolution or a directors' resolution, the directors acting pursuant to a members' resolution or a directors' resolution, or a creditor (including a contingent or prospective creditor).[9]

A judicial management order is only granted in cases where it can be shown there is a reasonable probability of rehabilitating the company or of preserving all or part of its business as a going concern, or that otherwise the interests of creditors would be better served than by resorting to a winding up.[10]

Judicial management is not available to companies which are licensed institutions or operators of designated payment systems regulated under the laws enforced by the Central Bank of Malaysia, and companies subject to the Capital Markets and Services Act 2007.[11] The courts have held that the phrase "companies subject to the Capital Markets and Services Act 2007" in section 403 of the CA 2016 includes public listed companies.[12]

Unlike a scheme of arrangement, the management powers of the company will lie with the judicial manager upon the making of a judicial management order by the court.[13]

A moratorium will also be automatically triggered upon the filing of an application for a judicial management order. The moratorium will be effective until the application is heard and disposed of.[14]

A judicial management order shall remain in force for a period of six months from the date of the making of the order, unless the judicial management is otherwise discharged, but the court may, on the application of a judicial manager, extend this period for another six months subject to such

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8 *In Re Sateras Resources (Malaysia) Bhd* [2005] 6 CLJ 194 (HC); *Sentoria Bina Sdn Bhd v Impak Kejora Sdn Bhd & Ors* [2021] 12 MLJ 690 (HC).

9 CA 2016, s 405(1).

10 *Idem*, s 404.

11 *Idem*, s 403.

12 *Re Scomi Group Bhd* [2022] 7 MLJ 620.

13 CA 2016, s 414(2).

14 *Idem*, s 410.

terms as the court may impose.[15] A judicial management order provides a company with another automatic moratorium which stays all legal proceedings against the company.[16]

Within 60 days of the granting of the judicial management order (or such longer period as the court may allow), the judicial manager must table a statement of proposal setting out its rehabilitation plan at the creditors' meeting.[17] Once the proposal is approved by 75% of the total value of creditors whose claims have been accepted by the judicial manager, it shall be binding on all creditors of the company whether or not they have voted in favour of the proposal.[18]

### *1.1.3 Corporate voluntary arrangement*

Corporate voluntary arrangement is a binding arrangement or agreement made between a company and its creditors to reach a compromise on the whole or part of the company's debts and their repayment without the need for any court approval or order. Even though no court approval or order is required, certain documents must still be lodged with the court.

A corporate voluntary arrangement can be initiated by either one of the following:

- directors of the company (if the company is not under liquidation or judicial management);[19]
- the judicial manager (if the company is under judicial management);[20] or
- the liquidator (if the company is under liquidation).[21]

Unlike under judicial management, the company directors still retain their powers of the day-to-day management of the company throughout the corporate voluntary arrangement.

Briefly, a corporate voluntary arrangement involves the following processes:

- Where the directors of a company or the Official Receiver intend to make a proposal for a voluntary arrangement, the directors or Official Receiver shall appoint a nominee and shall submit to the nominee a document setting out the terms of the proposed voluntary arrangement and a statement of the company's affairs.[22]
- Thereafter, the nominee shall submit to the directors a statement indicating his / her opinion on the following:[23]
    - whether the proposed voluntary arrangement has a reasonable prospect of being approved and implemented;
    - whether the company is likely to have sufficient funds available during the proposed moratorium to enable the company to carry on its business; and
    - whether the meetings of the company and its creditors should be summoned to consider the proposed voluntary arrangement.
- The company is required to file various documents with the court, as set out in section 398(1) of the CA 2016.

15 *Idem*, s 406(1).
16 *Idem*, s 411(4).
17 *Idem*, s 420.
18 *Idem*, s 421(3).
19 *Idem*, s 396(1).
20 *Idem*, s 396(3)(a).
21 *Idem*, s 396(3)(b).
22 *Idem*, s 397(1).
23 *Idem*, s 397(2).

- A moratorium is triggered upon the completion of the above steps, without the need for a court order. This is provided the requirements in the Eighth Schedule of the CA 2016 are met. In the first instance, the moratorium is valid for 28 days and can be extended to an additional 60 days, subject to the consent of the nominee, members of the company and 75% in value of the creditors.[24]

- Where a moratorium is in force, the nominee shall summon a meeting of the company and a meeting of its creditors at the time, date and place the nominee thinks fit.[25] The CA 2016 does not allow for modifications to be made to the proposed voluntary arrangement in any of the meetings. As such, the proposed voluntary arrangement must be approved as it is or rejected by the members and creditors. The required majority to approve a proposal for voluntary arrangement in the creditors' meeting shall be 75% of the total value of creditors present and voting at the meeting either in person or by proxy.[26] A simple majority is required to pass a resolution to approve the proposal for voluntary arrangement in a meeting of members.[27]

Corporate voluntary arrangement is not available to the following categories of companies:[28]

- a public company;

- a company which is a licensed institution, or an operator of a designated payment system regulated under the laws enforced by the Central Bank of Malaysia;

- a company which is subject to the Capital Markets and Services Act 2007; and

- a company which creates a charge over its property or any of its undertaking.

### 1.2 Informal restructuring procedures

Companies in financial distress are free to choose mediation as an out of court restructuring procedure, whereby parties jointly appoint an impartial and independent third party, known as a mediator, who will then assist / facilitate negotiations between parties to seek to arrive at a mutually beneficial and acceptable outcome. Mediation is voluntary in that parties cannot be forced to mediate their dispute unless they are willing to.

The Malaysian Government has also introduced the Corporate Debt Restructuring Committee (CDRC) as a pre-emptive measure to provide a platform for corporate borrowers and their creditors to work out a feasible debt resolution without having to resort to legal proceedings. This initiative was put in place to ensure that all avenues are made available to assist distressed corporations to resolve their debt obligations. Companies facing financial distress and difficulties in servicing their debt obligations can seek assistance from the CDRC on a voluntary basis, with the CDRC's role being to mediate between companies and their lenders in arriving at a viable debt restructuring arrangement.

Companies seeking assistance from the CDRC must fulfil the following broad eligibility criteria:

- aggregate indebtedness of RM 10 million or more;

- at least two financial creditors;

- not in receivership or liquidation, except for those companies where receivers have been appointed only over certain specified assets and the directors remain in control over the companies' overall operations; and

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[24] *Idem*, Eighth Schedule.
[25] *Idem*, s 399(1).
[26] *Idem*, s 400(2).
[27] *Idem*, s 400(3).
[28] *Idem*, s 395.

- experiencing difficulties in servicing their debt obligations but may not have already defaulted.

Any company listed on the Main Market or ACE Market of Bursa Malaysia Securities Berhad and classified as a PN17 or GN3 company (as the case may be) would also qualify for this.

## 2. Restructuring of ESG-related liabilities

### 2.1 Environmental (E): restructuring environmental liabilities

#### *2.1.1 Types of environmental liabilities*

A company may be subjected to both criminal and civil environmental liabilities in Malaysia. Under the Environmental Quality Act 1974 (EQA 1974), pollution or contamination of the air, water or soil beyond acceptable conditions or without holding the required permits or approvals may result in penalties of fines and / or imprisonment. Directors, managers and other officers of a company could be held personally liable for environmental offences committed by the company, unless they can show they exercised all due diligence to prevent the occurrence of the offence.

A company could also have civil claims brought against it under tort law. For example, a company which discharges waste into land which seeps into groundwater and pollutes neighbouring land and water sources could be held liable for negligence for breach of its duty of care, or under the rule in *Rylands v Fletcher,*[29] for the "escape" of the waste from its operations, or under nuisance or trespass for physical invasion onto the neighbours' land and water sources.

#### *2.1.2 Priority given to environmental liabilities*

Under insolvency laws, environmental liabilities do not rank ahead of other creditors' financial claims.

Examples of environmental liabilities are liabilities for remedial action required by the authorities or for damages to plaintiffs who successfully bring civil actions against the company. Under the EQA 1974 or the CA 2016, environmental liabilities of the aforementioned nature are not recognised as secured or priority debts.

#### *2.1.3 Disclaimer of environmental obligations*

Under the Contaminated Land Management and Control Guidelines (Guidelines) issued by the Department of Environment of Malaysia (DOE), it is the responsibility of current landowners to determine whether there is the presence of subsurface contamination on their land. In the event land contamination is detected, the landowner is required to determine if there is any unacceptable human health risk to the onsite and offsite human receptors and ecological risks and, if so, propose to the DOE a remediation action plan. If the current landowner confirms through a proper environmental site assessment that the subsurface contamination is not caused by its current or historical onsite operations, it is the responsibility of the landowner to identify the polluters who will be directly responsible for the subsequent remediation. However, if the polluter identified is no longer in operation, the responsibility for the remediation shall be borne by the current landowner.

Although these Guidelines are presently not enacted as legislation, the DOE in practice generally adopts the approaches set out in the Guidelines. There is no provision in the EQA 1974 for the disclaimer of such environmental obligations.

In principle, environmental liabilities can be restructured under a scheme of arrangement, corporate voluntary arrangement as well as judicial management. However, the extent to which environmental liabilities can be restructured in Malaysia is far from certain as there has yet to be any reported cases in Malaysia on this issue.

[29] [1861-73] All ER Rep 1.

Similarly, it is also uncertain as to whether properties subject to environmental obligations can be disclaimed under the available restructuring mechanisms. In terms of judicial management, the process in Malaysia (unlike Singapore) does not allow for the disclaimer of onerous property by a judicial manager.

## 2.2 Social (S): restructuring health or safety-related liabilities

Health or safety-related liabilities can be restructured under a scheme as ordinary liabilities of a company.

The party bringing the claim would fall within the widely defined meaning of a "creditor",[30] so long as the party is able to demonstrate it has pecuniary claims against the company[31] which can be admitted to proof in the event the company is wound up. These pecuniary claims may include contingent, unproven or unliquidated claims. There are no special restrictions or conditions that apply when restructuring health or safety-related liabilities. As schemes of arrangement in Malaysia are generally driven by the debtor company (unlike the winding up or judicial management processes), in practice it is possible that the debtor company may treat these types of claims as premature and thus refuse to include these liabilities in the scheme.

### *2.2.1 Types of health and safety-related liabilities*

In Malaysia, health or safety-related liabilities include:

- civil claims such as claims in tort (e.g. negligence relating to the latent defects of goods supplied)[32] and claims pursuant to contract; and
- statutory liabilities such as:
    - fines imposed pursuant to breaches of duties and / or obligations arising out of health and safety legislation, including the Occupational Safety and Health Act 1994 (OSHA 1994)[33] and the Factories and Machinery Act 1967 (FMA);[34] and
    - remediation costs under section 48(6) of the OSHA 1994, where the officer appointed under the OSHA 1994 may recover costs of the action from the occupier or person having responsibility or control of the place of work, plant, substance or process, in exercising his / her powers under section 48(5) of the OSHA 1994 in proceeding to render inoperative the place of work, plant, substance or process by any means he / she deems best.

### *2.2.2 Treatment of health and safety-related liabilities*

Under section 527(1) of the CA 2016, employees' compensation under any written law, as well as remuneration payable in case of the death of employees, are given priority over all other unsecured debts. The debts that are given priority could include those arising from health and safety-related liabilities.

## 2.3 Governance (G): third party releases in favour of directors and officers of the company

There are no statutory provisions in Malaysia which expressly prohibit the release of third party liabilities *vis-à-vis* directors and officers of the scheme company. However, there are also no

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30 *Asiabio Capital Sdn Bhd v Seacera Group Bhd & Ors (Al Amin Strategic Commodity Sdn Bhd & Ors, intervener)* [2021] MLJU 2886, paras 23 and 24; *Re Butterworth Products & Industries Sdn Bhd (Khaw Saw Mooi & Ors, Petitioners)* [1992] 1 MLJ 429, 433G-433F.

31 See *Capital City Property Sdn Bhd v Achwell Property Snd Bhd* [2021] MLJU 749, paras 19-20.

32 In *Sundram A/L Veeriah v Magninificient Diagraph Sdnbhd* [2010] MLJU 1342, the court allowed the plaintiff's claim against the defendant for breach of duty on grounds that the defendant owes the plaintiff a duty of care to ensure that the drill did not suffer from any latent defects and could have been used safely by the plaintiff.

33 See for example, OSHA 1994, ss 19, 23 and 62.

34 See for example, FMA, s 51.

reported cases in Malaysia to date which directly address the issue of whether third party releases can be granted in favour of directors and officers of the scheme company.

While the High Court[35] has held that it is permissible for a scheme of arrangement to provide for a third party arrangement involving the company's guarantor who is not a party to the scheme of arrangement, the court did not provide guidance on the factors to be taken into consideration when determining whether the release of third parties' liabilities would be allowed.

In another case,[36] the High Court was of the view that a restraining order (granted in a scheme of arrangement) could extend to the guarantor company, if the guarantor was an integral component of the scheme and the scheme would not be workable without the guarantor company. Although the court in *Sentoria* was not directly concerned with the issue of whether a third party release *vis-à-vis* a guarantor is allowed in a scheme of arrangement, based on the High Court's reasoning on the issue on the restraining order, it is arguable the High Court in *Sentoria* would have similarly allowed a scheme of arrangement which also seeks to release the liability of the guarantor company.

The Singapore Court of Appeal[37] recently laid down guidelines for determining whether a release of third parties' liabilities should be allowed. Firstly, a proposed scheme might compromise liabilities owed by third parties to the applicant company's creditors if there is a sufficient nexus or connection between the release of those liabilities and the relationship between the company and the creditors. Secondly, the court's focus will primarily be on the merits and the reasonableness of the inclusion of such third party releases in the proposed scheme, taking into account the factors to be considered at the sanction stage.

Generally, third party releases would be allowed in circumstances where the third parties involved are part of the same corporate group as the scheme company, and the debts of the scheme company and the third parties relate to the same transaction, as in the case of *Pathfinder*. In *Pathfinder*, the Singapore Court of Appeal was of the view that a third party release was necessary in that case as "otherwise liability and enforcement risks would merely be shifted between members of the corporate group and the overall restructuring objective would be entirely unmet."

As section 210(1) of the Singapore Companies Act 1967 is similar (although not *in pari materia*) to section 366 of the CA 2016, Singapore's case law on the issue would be of guidance and persuasive authority in Malaysia.

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

#### *3.1.1 Approving a restructuring plan*

A restructuring plan does not have to be approved by environmental protection authorities or any environmental advocacy group. A restructuring plan is only subject to the approval of shareholders and creditors and in some cases, such as a scheme of arrangement, the court.

#### *3.1.2 Discretion to consider wider public interest concerns*

There is yet to be any reported case in Malaysia where the court has had to consider the extent to which environmental issues are to be taken into consideration when deciding whether to sanction a scheme of arrangement. As noted above, the matters taken into consideration by the court at the sanction stage are matters that concern the interests of the creditors as opposed to matters concerning public policy.

35 *Re Khondker Yarad Ahmed; ex p MIDF Amanah Ventures Sdn Bhd* [2016] 3 CLJ 637 (HC).
36 *Sentoria Bina Sdn Bhd v Impak Kejora Sdn Bhd & Ors* [2021] 12 MLJ 690 (HC).
37 *Pathfinder Strategic Credit LP and another v Empire Capital Resources Pte and another appeal* [2019] SGCA 29.

However, even where public policy concerns can be taken into consideration, as in the case of judicial management, such powers are exercised only in exceptional circumstances. For instance, in the Singapore case of *Re Bintan Lagoon Resort Ltd,*[38] the Singapore High Court emphasised that there is a high threshold in meeting the public interest consideration under the judicial management process. The same is likely to apply in Malaysia.

#### *3.1.3 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

While there are no statutory provisions which grant environmental protection authorities or environmental advocacy groups locus standi to air their views or concerns in a restructuring, there have been cases where environmental advocacy groups and activists have taken a stand against non-eco friendly companies in general. For example, in the case of *Tan Bun Teet & 2 Ors v Tun Dr Mahathir Bin Mohamad & 30 Ors,*[39] three individuals, one of whom was the chairman of an environmentalist movement called "Save Malaysia Stop Lynas", filed a lawsuit challenging the Government's decision to renew the company's operating licence in relation to the operation of one of the world's largest rare earth plants in Gebeng, Pahang. However, the court held that there was no evidence of any illegality, procedural impropriety, irrationality and / or unreasonableness on the part of the respondents *vis-à-vis* the issuance of the fourth licence to Lynas and Lynas was compliant with the relevant laws.

### 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

#### *3.2.1 Approving a restructuring plan*

Generally, companies' restructuring procedures have to be approved by members and creditors, and in some cases the court. There is no governing legislation requiring a restructuring procedure to be approved by labour authorities. Although an employee or employees' representative is a member of the committee of creditors in the context of judicial management, they have no voting rights over the restructuring plan.[40]

#### *3.2.2 Discretion to consider wider public interest concerns*

There is no case law discussing the extent to which an approving body may consider environmental and / or labour issues in deciding whether to approve a restructuring plan proceeding. The court's discretion in sections 405 and 406 of the CA 2016 focuses on the interests of creditors and does not include a broader assessment of the interests of employees.

#### *3.2.3 Protection of employee rights*

There are no Malaysian statutory provisions which grant rights to labour authorities, unions or employee / worker advocacy groups to have the standing to air their views / concerns in restructuring.

However, in the context of judicial management, the committee of creditors must consist of at least one employee or the trade union, provided the employees are members of the trade union and the employer recognises the union.[41] This indicates that a trade union is entitled to represent any members at a meeting of creditors summoned to consider the judicial manager's proposals.

The trade union representing the employees has a right to attend the meetings of the committee of creditors as non-voting delegates but cannot preside over the meetings of the committee of creditors.[42]

38 [2005] 4 LSR (R) 336.
39 [2021] 10 CLJ 799.
40 Companies (Corporate Rescue Mechanism) Rules 2018, rr 36(3) and 36(4)(a).
41 *Idem*, r 36(1)(a).
42 *Idem*, r 36(4)(a).

It will also be sufficient for the trade union to file only one proof of debt where there is more than one claim for wages or salaries by the company's employees under judicial management.[43]

Further, when it comes to retrenchment arising from restructuring, the court can rely on collective agreements if retrenchment exercises are carried out without following the procedure stipulated in the collective agreement.[44]

### 3.3 Governance (G): board / management conflicts addressed in a restructuring

Board / management conflicts are generally addressed via the disclosure requirements. In this regard, as noted above, section 369(1) of the CA 2016 imposes an obligation on the party who summons the court-convened meetings to send to the scheme creditors and / or scheme members an explanatory statement explaining the effect of the proposed scheme and, in particular, stating any material interests of the directors (whether as directors or as members of the company or otherwise) and any differential treatment for creditors and / or members with similar interests.

For listed companies, the explanatory statement must also include details of the interests of the directors, major shareholders and / or persons connected with them in the proposed scheme.[45]

Further, as noted in section 1 above, the scheme company bears the duty of absolute transparency and to unreservedly disclose all material information to assist the court in determining the classification and the composition of the creditors, how the creditors' meeting(s) are to be conducted and to address any allegation of an abuse of process and / or if the application is not made bona fide. Arguably, this would also impose a duty against the scheme company to disclose any conflicts of interest.

In cases where the scheme creditors consist of directors or management personnel, their votes could potentially be disregarded on the basis they are related creditors. In the case of *Re Top Builders Capital Berhad and others (No 2)*,[46] the High Court explained that there is no absolute rule that votes of intercompany creditors and / or related party creditors must be discounted or disregarded.

The question whether to discount or disregard the votes is a matter of discretion for the court based on the particular facts of the case. Some of the factors to be taken into account in deciding whether the votes should be discounted or disregarded are:

- whether the benefits the creditors would likely derive from the scheme are clearly better than the alternative liquidation scenarios;
- whether there is any clear and obvious likelihood of the creditors achieving a better scheme;
- whether the exercise of the votes by the intercompany creditors or related party creditors was driven by any special or ulterior interest that was "adverse" to the interests of the creditors;
- whether the opposing creditors pressing for such a discount have any self-interest and / or ulterior motive;
- whether the adjudicated debts of the intercompany creditors and / or related party creditors are genuine or questionable; and
- whether the percentage of independent creditors who had voted in the scheme is such that it reflects a desire on the part of an overwhelming majority in value and in number of the scheme creditors wanting the scheme.

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43 *Idem*, r 20(1).

44 Industrial Relations Act 1967, s 30(5).

45 See Appendix 13B, Chapter 13 of the Main Market Listing Requirements of Bursa Malaysia Securities Berhad and Appendix 13B of the ACE Market Listing Requirements of Bursa Malaysia Securities Berhad.

46 [2022] MLJU 1 (HC).

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

Bank Negara Malaysia (BNM), the Central Bank of Malaysia, has issued the Climate Change and Principle-Based Taxonomy (BNM Taxonomy), which sets out the BNM's expectation for financial institutions to take into account climate change considerations when evaluating and making decisions on financing. The BNM Taxonomy's guiding principles are to be incorporated as part of financial institutions' due diligence assessments on financing for existing and prospective customers, and for investment decisions in financial assets.

The BNM has also issued an exposure draft on Climate Risk Management and Scenario Analysis, which is a document that set out the material financial risks posed by climate change to the safety and soundness of financial institutions. Upon it coming into force, financial institutions shall comply with the policy document at the entity and consolidated levels, and the requirements apply to both financial and non-financial subsidiaries of financial institutions and the board of directors.

As such, in a situation of restructuring where there are existing banking facilities, the financial institution concerned would have to take into account these requirements set out by the BNM.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

The Code of Conduct for Industrial Harmony (Code) was introduced as a set of guidelines for employers and employees on the practice of industrial relations for achieving greater industrial harmony. The Code provides for matters concerning the redundancy and retrenchment of workers. The Code identifies the appropriate measures to be adopted before retrenching employees in a restructuring exercise. In the context of the Code, "restructuring" refers to a restructuring of workforce requirements but the guidelines would apply equally where a corporate restructuring gives rise to the collective termination of employment.

For example, the Code recommends that:

- employers should, where redundancy is likely, consult with their employees' representatives or their trade union, as appropriate, and consult with the Ministry of Labour and Manpower;[47]
- employers should take positive steps to avert or minimise reductions of the workforce by the adoption of appropriate measures[48] such as the limitation of recruitment,[49] the restriction of overtime work,[50] the restriction of work on the weekly day of rest,[51] a reduction in the number of shifts or days worked a week,[52] a reduction in the number of hours of work,[53] or re-training or transfer to other departments / work;[54] and
- before deciding the workforce size in a case of restructuring, employers should communicate early with the employees through their representatives or trade unions.

If retrenchment becomes unavoidable in a restructuring procedure, despite having taken appropriate measures, the Code recommends appropriate steps such as:[55]

- employers should give as early a warning as practicable to the employees concerned;

47 Code, cl 20.
48 *Ibid*.
49 *Idem*, cl 20(a).
50 *Idem*, cl 20(b).
51 *Idem*, cl 20(c).
52 *Idem*, cl 20(d).
53 *Idem*, cl 20(e).
54 *Idem*, cl 20(f).
55 *Idem*, cl 22(a).

- employers should introduce schemes for voluntary retrenchment and retirement and for payment of redundancy and retirement benefits;
- employers should retire workers beyond their normal retirement age;
- employers should assist, in cooperation with the Ministry of Human Resources, the workers to find work outside the undertaking;
- employers should terminate employment over a longer period; and
- employers should ensure that no such announcement is made before the employees and their representatives or trade union have been informed.

The Code further suggests that employers should select employees to be retrenched in accordance with objective criteria. Such criteria, which should have been worked out in advance with the employees' representatives or trade union, as appropriate, may include:[56]

- the need for the efficient operation of the establishment or undertaking;
- the ability, skill, experience and occupational qualifications of individual workers required by the establishment or undertaking;
- consideration of length of service and status (non-citizens, casual temporary, permanent);
- age;
- family situation; and
- such other criteria as may be formulated in the context of national policies.

Moreover, employers should give priority to engagement or re-engagement of previous employees when considering the hire of new workers.[57]

The Code also suggests that the above appropriate measures shall form part of the employment policy of the establishment or undertaking.[58]

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

Restructuring professionals (better known as insolvency practitioners in Malaysia) are guided by, among others, the Insolvency Guidance Notes (Guidance Notes) provided by the Malaysian Institute of Accountants (MIA).

In terms of conflicts of interests, the Guidance Notes provide:

- the possibility of a conflict of interest should be carefully considered prior to any insolvency practitioner consenting to act or accepting an appointment. Conflicts, actual or potential, should be avoided;
- where it is apparent at the time the insolvency practitioner is approached to consent to act that there will be a conflict of interest if consent is given, then the insolvency practitioner should not consent to act. When the insolvency practitioner is requested to consent to act and his / her review of the information available is such that he / she forms an opinion that a conflict of interest may arise during the appointment or administration, consent to act should not be given unless all relevant parties (including the court where appropriate) are advised of the possibility of a conflict arising, and they do not object to the appointment;

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56 *Idem*, cl 22(b).
57 *Idem*, cl 23.
58 *Ibid*.

- if, during the course of an appointment or administration, a conflict or apparent conflict arises, the insolvency practitioner should, as soon as practicable, fully disclose details of the matter to the appointor, committee of inspection, creditors, the court or other appropriate body, depending upon the form of administration and the circumstances;

- where there has been a material professional relationship with a client, no insolvency practitioner or employee of the practice should accept appointment as liquidator, provisional liquidator or receiver of the client, if the client is insolvent. A material professional relationship with a client arises where a practice or the insolvency practitioner in question is carrying out, or has during the previous two years carried out, material professional work, whether of a continuing nature or not, for that client. Material professional work would include the following:

  - where a practice or person has carried out, or has been appointed to carry out, audit work for a company or individual to which the appointment is being considered; or

  - where a practice or person has carried out one or more assignments whether of a continuing nature or not, of such overall significance or in such circumstances that the insolvency practitioner's objectivity in carrying out a subsequent insolvency appointment could be or could reasonably be seen to be prejudiced; and

- insolvency practitioners should be particularly aware of the difficulties likely to arise from the existence of intercompany transactions or guarantees in group, associated or family-connected company situations. Acceptance of an insolvency appointment in relation to more than one company in the group or association may raise issues of conflict of interest.

The Guidance Notes are not prescriptive in nature and are strictly for guidance only.

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

In Malaysia, the increasing awareness among borrowers and investors of the synergy between ESG investing and Islamic finance, the investment approaches and principles of which have a strong emphasis on sustainability, has led to considerable interest in ESG-compliant debt market products, especially those involving Islamic finance elements.

Major Malaysian banks have adopted the concept of sustainability-linked loans and have offered such loans to corporate borrowers, whereby the proceeds can be allocated for general corporate purposes to improve the sustainability profile of the borrower, through alignment of loan pricing (interest rates) to the borrower's performance against ESG-related performance targets.[59]

The local capital market is instrumental in addressing ESG issues by allocating capital market resources towards ESG factors. Malaysia initiated the Sustainable Responsible Investment (SRI) Sukuk (Islamic bonds) in 2014[60] and has since been a prominent leader in the issuance of sustainable bonds among ASEAN countries, accounting for US $3.9 billion of issuance value as of November 2021.[61] Some notable examples include the world's first green SRI Sukuk in 2017,[62]

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[59] Examples based on reportings on CIMB Bank on 22 October 2020: https://www.cimb.com/en/newsroom/2020/sarawak-energy-secures-its-first-sustainability-linked-loan-sll-of-rm100-million-from-cimb.html; HSBC Amanah on 28 February 2020: https://www.businesstoday.com.my/2020/02/28/hsbc-amanah-provides-leading-edge-sustainability-linked-financing/.

[60] Information about the SRI bond and sukuk issued in Malaysia accessible at: https://www.bixmalaysia.com/Learning-Center/Sustainable-Responsible-Investment-Center.

[61] "Malaysia is Prime Issuer of Sustainability Sukuk in ASEAN, with US $3.9 Billion of Total Issuance", Press Release on 23 Feb 2022: https://www.ey.com/en_my/news/2022-press-releases/01/malaysia-is-prime-issuer-of-sustainability-sukuk-in-asean-with-uss3-9-billion-of-total-issuance.

[62] "SC Announces the Issuance of Malaysia's First Green Sukuk – An Innovative Channel to Address Global Funding Gaps in Green Financing under its Sustainable & Responsible Investment (SRI) Sukuk Framework", Media Release on 27 July 2017: https://www.sc.com.my/resources/media/media-release/malaysias-first-green-sukuk-under-scs-sustainable-responsible-investment-sukuk-framework.

and the Government of Malaysia issued the world's first US dollar sustainability Sukuk amounting to US $800 million in 2021. The proceeds will be used for eligible social and green projects aligned to the United Nations' Sustainable Development Goals (SDGs) Agenda.[63]

In 2022, the Labuan Financial Services Authority officiated reportedly the world's first Shariah-Compliant ESG Digital Asset Exchange,[64] a blockchain ecosystem for companies to raise fund in ESG and Shariah-compliant manner through digital securitisation of their assets (securities token offering).

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

Malaysian ESG-related frameworks to guide banks to embed sustainability in their business practices and operations, such as the Climate Change and Principle-Based Taxonomy (CCPT), the Value-Based Intermediation Financing and Investment Impact Assessment Framework (VBIAF) and the Task Force on Climate-Related Financial Disclosures (TCFD), have been adopted or are in the midst of adoption by major banks in Malaysia. In conformity with the VBIAF and as part of its sustainability drive, HSBC Amanah launched its Triple Bottom Line Framework as a guide to its classification of financing and measurement of the impact of financing via the "3Ps", namely planet, people and prosperity, on 28 September 2022.

The RHB Group has made notable strides in ESG within the area of investment banking by being the sole and lead arranger in major ESG-linked bonds issuance programmes. The group's commitment to ESG is also evident through the extension of RM 5 billion for its green financing activities to promote the transition to a low-carbon and climate-resilient economy through lending, capital markets, advisory and investment by 2025.

The Maybank Group issued its ESG Risk Management Framework in January 2022, incorporating an ESG risk assessment in the group activities to ensure the group will not offer financing to customers not aligned with its ESG position. Having invested substantially in the Malaysian ESG Equity Growth Fund, the group strengthens its commitment to the ESG agenda with the launch of its own MAMG Global Environment Fund that invests in global equity funds focusing on new energy, sustainable food, water, circular economy, smart environment and clean and efficient transport.

Further to the CIMB Group's earlier commitments to achieve net zero greenhouse gas emissions and to mobilise RM 30 billion in sustainable finance under its Green, Social, Sustainable Impact Products and Services Framework by 2024, the group has in May 2022 enhanced its commitment to achieve ESG targets through collaboration with the Malaysian Stock Exchange (Bursa Malaysia). As part of the collaboration, CIMB Bank will offer sustainable finance offerings for Malaysian public listed companies (PLCs) in alignment with the ratings model of the FTSE4Good Bursa Malaysia (F4GBM) index, an initiative which aims to improve ESG performance among Malaysian PLCs.

### 5.3 Promoting ESG by the central bank and regulators

In line with Malaysia's value proposition as a centre for Islamic finance and sustainable investments, major financial market regulators in Malaysia such as the Central Bank of Malaysia (Bank Negara Malaysia or BNM), the Securities Commission Malaysia (SC), the Malaysian Stock Exchange (Bursa Malaysia) and the Labuan Financial Services Authority (Labuan FSA) have undertaken immense efforts to lay the groundwork and to promote ESG financing in Malaysia.

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[63] "World's First Sovereign US Dollar Sustainability Sukuk Issuance by The Government of Malaysia", Press Release on 22 April 2021: https://www.mof.gov.my/portal/en/news/press-release/world-s-first-sovereign-u-s-dollar-sustainability-sukuk-issuance-by-the-government-of-malaysia.

[64] "Green-X Aims to Serve as Marketplace for Digitisation and Tokenisation of International Islamic Finance", Announcement on 20 September 2022: https://www.greenprocapital.com/home/green-x-aims-to-serve-as-marketplace-for-digitization-and-tokenization-of-international-islamic-finance/?utm_source=rss&utm_medium=rss&utm_campaign=green-x-aims-to-serve-as-marketplace-for-digitization-and-tokenization-of-international-islamic-finance.

As noted above, in November 2019, the BNM issued the Value-Based Intermediation Financing and Investment Impact Assessment Framework (VBIAF) Guidance Document,[65] which has since become the foundation for ESG considerations in the financial sector, and while it is premised on Shariah tenets, its framework has universal application for financial institutions targeting the incorporation of ESG measures in their operations. Recently, the BNM issued a policy document on Climate Risk Management and Scenario Analysis,[66] aimed at monitoring the management of climate-related risks of licensed financial institutions to achieve a just and orderly transition towards a low-carbon economy.

The SC has launched various initiatives and frameworks to push the ESG agenda and drive SRI. In 2014, the SC launched the SRI Sukuk Framework,[67] which lays the foundation for a conducive and systematic ecosystem for both retail and sophisticated investors desiring to participate in the sustainable debt market by aligning definitions and standards to the SDGs, with an emphasis on transparent reporting. The key distinguishing feature of this Framework is the requirement to have external reviews at pre and post issuances which are crucial in providing independent opinion and verification on the issuer's sustainable objectives. In 2018, the SC established the SRI Sukuk and Bond Grant Scheme (formerly known as the Green SRI Sukuk Grant Scheme), which was expanded in 2021 and again in 2022 to encourage more participants. The scheme covers up to 90% of the actual costs incurred by issuers on external assessments conducted to ensure their compliance with the SRI Sukuk Framework. In 2019, the SC released the SRI Roadmap for the Malaysian capital markets, which comprises various initiatives aimed at facilitating more ESG financing through the role of the capital market. In mid-2022, the SC launched the SRI-linked Sukuk Framework to facilitate fundraising by companies in addressing sustainability concerns such as the ESG agenda, with features that relate to the issuer's sustainability performance commitments.

Bursa Malaysia has issued specific guidance[68] on ESG reporting and has ESG-linked disclosure requirements as a listing rule, both of which must be observed by Malaysian PLCs. Bursa Malaysia, together with FTSE, has also launched the FTSE4Good Bursa Malaysia Index in 2014, which is designed to identify Malaysian companies demonstrating strong ESG practices, helping ESG-aware investors to align their investments with ESG factors.

As an initiative of the Labuan International Business and Financial Centre (Labuan IBFC), whose regulatory authority is Labuan FSA, to proactively develop new platforms that integrate Islamic finance, the ESG agenda and digital financial innovations, Labuan has recently established itself as an Islamic Digital Asset Centre (IDAC), a fund-raising and investment hub with a niche in ESG and Shariah-compliant activities. Labuan FSA is expected to issue guidelines on digital assets to strengthen the governance of IDAC soon.

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65 Information on Value-Based Intermediation Financing and Investment Impact Assessment Framework - Guidance Document accessible at: https://www.bnm.gov.my/-/value-based-intermediation-financing-and-investment-impact-assessment-framework-guidance-document.

66 BNM policy document on Climate Risk Management and Scenario Analysis, accessible at: https://www.bnm.gov.my/documents/20124/938039/PD_Climate-Risk-Mgmt-Scenario-Analysis-Nov2022.pdf.

67 "SC introduces Sustainable and Responsible Investment Sukuk Framework", Media Release on 28 August 2014: https://www.sc.com.my/resources/media/media-release/sc-introduces-sustainable-and-responsible-investment-sukuk-framework.

68 Bursa Malaysia's Sustainability Reporting Guide and Toolkits (3rd Edition) accessible at: https://bursasustain.bursamalaysia.com/droplet-details/resources/sustainability-reporting-guide-3rd-edition.

# MEXICO

## 1. General overview of the restructuring regime

### 1.1 Formal restructuring procedures

The formal restructuring procedure in Mexico is known as "*concurso mercantil*" and its framework is contained in the "*Ley de Concursos Mercantiles*" (Commercial Insolvency Law). During this procedure, the company remains under the control of the existing management and the conciliator appointed by the Federal Institute of Insolvency Experts (IFECOM, for its initials in Spanish) will supervise the company's operations.

However, the conciliator can request the court to remove the existing management if he / she believes it is better for the bankruptcy estate. In case the debtor is removed from the administration of its company, the conciliator will take over the control of the company.

The restructuring procedure must take place during the conciliation stage, which lasts 185 days. The period will begin when the declaration of insolvency resolution is published in the National Official Gazette. The term of 185 days can be extended for 90 days if the conciliator or more than 50% of creditors request it. Furthermore, a second extension can be requested by the debtor and 75% of the creditors.

To be valid, the reorganisation agreement must not contain provisions against the public order and ought to be entered by more than 50% of:

- the recognised amount of unsecured claims and subordinated claims;[1] and
- the recognised amount of secured and special privileged claims.[2]

In cases where the debtor has subordinated creditors that represent at least 25% of the total amount of the recognised creditors mentioned above, the reorganisation agreement must be entered by the recognised creditors that represent at least 50% of claims, excluding subordinated creditors. However, this provision will not be applied if the subordinated creditors admit the terms agreed by the recognised creditors.

The labour and tax creditors will not subscribe to the reorganisation agreement. Nonetheless, the debtor can enter individual agreements with its labour creditors if these agreements do not aggravate the debtor's situation. Furthermore, the Law allows the debtor to request the tax authorities' remission of tax debts.[3]

The debtor or the conciliator must present before the court the proposal of the reorganisation agreement when they consider it has been approved the majority of recognised creditors. The court must publish the proposed agreement and creditors will have 15 days to express their opinion or subscribe it. Once the 15 day period ends, the conciliator must present to the court the reorganisation agreement entered by the debtor and the required majority of its creditors.

The day after the conciliator presents the reorganisation agreement, the court must give five days to the creditors to raise their objections regarding the authenticity of their authorisation to the agreement and exercise their right of veto.

The agreement can be vetoed by the ordinary creditors that did not enter the agreement, whose combination of claims represent more than 50% of the total amount of all the common debt. The

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[1] According to article 222 Bis of the Commercial Bankruptcy Law, subordinated claims are those held by creditors that have agreed to subordinate their rights concerning common or unsecured claims, as well as those held by commercial companies belonging to the same corporate group as the debtor.

[2] According to the Commercial Code or laws of their subject matter, creditors with special privilege are all those who have a special privilege or a right of retention.

[3] The Federal Tax Code provides that the debtor that has been declared insolvent and has entered a reorganisation agreement with its creditors can request for a partial waiver of the debts existing at the time of being declared insolvent.

common creditors will be banned from exercising their veto right if the agreement foresees the full payment of their debt.

Once the mentioned period of five days ends, the court must verify if the reorganisation agreement complies with the requirements provided by the Law and that it is not contrary to public order provisions.

The agreement will be binding on:

- the debtor;
- common creditors;
- subordinate creditors;
- secured creditors that entered the agreement;
- special privileged creditors that entered the agreement; and
- secured and special privileged creditors that did not enter the agreement but whose claims or guarantees will be fully paid.

The resolution in which the Bankruptcy Court approves the reorganisation agreement will terminate the insolvency proceeding. The resolution will be the only document that will govern the obligations between the debtor and its creditors. The standby periods, waivers and other benefits provided by the agreement will only concern the debtor, not its guarantors, unless the creditors agree otherwise.

### 1.2 Informal restructuring procedures

In Mexico, there is no framework for out of court restructurings or workouts.

## 2. Restructuring of ESG-related liabilities

### 2.1 Environmental (E): restructuring environmental liabilities

The Commercial Bankruptcy Law in Mexico does not contain a special regulation to restructure environmental liabilities.

The fines that the environmental authorities can impose for the infringement of the environmental laws would be considered tax claims in a formal insolvency proceeding. Also, if a company is declared liable for causing damages to the environment in a judicial proceeding, taking into consideration that the beneficiary of the economic compensation that the company may be sanctioned to pay is the government, such liability would also be considered a tax claim.

Tax claims cannot be restructured throughout a reorganisation agreement entered between the debtor and the creditors. The debtor must request the authorities' remission of the debt.

#### *2.1.1 Types of environmental liabilities*

In Mexico, there are multiple laws that contain administrative, civil or criminal liabilities for the infringement of environmental laws regarding several relevant matters such as the atmosphere, water, biodiversity and soil. The applicability of the laws will depend on the activities of the debtor.

According to the Law of Environmental Liabilities (*Ley de Resposabilidades Ambientales*), the liabilities for the damages caused to the environment can arise from the measurable loss, modification, deterioration, prejudice or affectation to the ecosystem, elements or natural resources, regarding their chemical, physical or biological constitution, the interactive relationship between them, as well as the environmental services they provide.

The Law of Environmental Liabilities, in article 10, mentions that every person or entity that damages the environment directly or indirectly because of its actions and / or omissions will be liable and will be obliged to repair the damages, or if repairing the damages is not possible, the person or entity will have to pay environmental compensation, as well as take all the necessary actions to avoid any further environmental damage.

Article 11 indicates that the liabilities for the damages caused to the environment will be subjective when they are generated because of illegal acts and omissions made by the person or company, with the exceptions contained in the law. It also mentions that if the damages are caused by a willful act or omission (meaning any active conduct or omission against the environmental laws, regulations, and norms), the person responsible will have to pay an economic penalty.

On the other hand, article 12 indicates that the liability will be objective when the damages caused are derived directly or indirectly from:

- any action or default concerning hazardous materials or waste;
- the use and operation of vessels in coral reefs;
- highly risky activities, meaning those concerning the generation or management of corrosive, reactive, radioactive, explosive, toxic, inflammable or biologically-infectious substances in the General Law of Ecological Balance and Protection to the Environment; or
- items contained in article 1913 of the Federal Civil Code – specifically, when a person uses mechanisms, instruments, devices, motor vehicles or dangerous substances, the person is liable for the damages caused, even if he / she / it has not acted illegally, unless he / she / it proves the damages were caused because of inexcusable fault or negligence of the victim.

Some examples of the environmental liabilities a company may be subject to are those arising under:

- the General Law of Ecological Balance and Protection to the Environment (*Ley General del Equilibrio Ecológico y Protección al Ambiente*) (articles 171 to 175);
- the General Law for the Prevention and Management of Waste (*Ley General para la Prevención y Gestión Integral de los Residuos*) (articles 106 to 115);
- the General Law of Forest Sustainable Development (*Ley General de Desarrollo Forestal Sustentable*) (articles 156 to 162);
- the General Law of Wildlife (*Ley General de Vida Silvestre*) (articles 122 to 130); and
- the Nation Waters Law (*Ley de Aguas Nacionales*) (articles 119 to 123)

There are other more specific laws that also contain environmental liabilities for companies, such as the Law of Organic Products (*Ley de Productos Orgánicos*), the Law of Biosecurity of the Genetically Modifies Organisms (*Ley de Bioseguridad de Organismos Genéticamente Modificados*), the Law of the Promotion and Development of Bioenergetics (*Ley de Promoción y Desarrollo de los Bioenergéticos*) and the General Law of Climate Change (*Ley General de Cambio Climático*).

### ***2.1.2 Priority given to environmental liabilities***

As indicated above, environmental liabilities caused before the bankruptcy proceeding will have the priority of tax claims, which means they will be paid after: (i) labour claims for wages and employee benefits for a period of two years preceding the date of the insolvency judgment; and (ii) secured claims.

Environmental liabilities caused during the insolvency proceeding can be considered a claim against the estate, and accordingly the company will have to pay them as an ordinary expense of its operations and business.

### *2.1.3 Disclaimer of environmental obligations*

The law does not contain any provisions that regulate specifically whether property subject to environmental obligations can be disclaimed or abandoned under a restructuring procedure.

However, if a certain property is not necessary for the company's ordinary business, the conciliator can decide whether it would be better to sell it.

## 2.2 Social (S): restructuring health or safety-related liabilities

In Mexico, health and safety liabilities, such as the those arising from product liability tort claims and asbestos claims, can be restructured in the same way as ordinary debt claims. The Commercial Bankruptcy Law does not contain special restrictions or conditions to restructure such liabilities.

According to article 127 of the Commercial Bankruptcy Law, in cases where a creditor has been sentenced in a proceeding or arbitration before the clawback date by an unappealable judgment or award that declares the existence of a claim against the debtor, the creditor must present a certified copy of the judgment to the Bankruptcy Court and the conciliator. The Bankruptcy Court will be obliged to recognise the claim in the recognition of claims judgement that must be issued in the insolvency proceeding.

Consequently, if the debtor has been sentenced to indemnify a creditor because of health and safety liabilities, the claim must be recognised and restructured in the insolvency proceeding, most probably as an unsecured debt, unless the debtor granted the creditor a collateral before the bankruptcy proceeding to secure the payment of the indemnification.

### *2.2.1 Types of health and safety-related liabilities*

In Mexico, companies can be subject to all kinds of health and safety-related liabilities, such as tort claims or asbestos claims. The victim must claim compensation for the damages caused by the company through a civil action.

For example, according to article 1913 of the Federal Civil Code and the Civil Code in Mexico City, when a person uses mechanisms, instruments, devices, motor vehicles or dangerous substances, he / she is liable for the damages caused, even if he / she has not acted illegally, unless he / she proves the damages were caused due to inexcusable fault or negligence on the part of the victim.

Article 1915 of those Codes indicates that the compensation must be chosen by the victim, whether in the form of damages or restoration of the situation before the damage occurred.

According to the Federal Labour Law, companies are also liable for the damages caused to their employees for the accidents that take place during and because of a risk at their job, as well as the sickness caused to the employee by the activities of their job.

The compensation to the employee will depend on the salary of the employee, as well as the degree of injury or disability suffered or if the accident or sickness resulted on the death of the employee.

### *2.2.2 Treatment of health and safety-related liabilities*

Health and safety liabilities claimed through a civil action do not have any special priority or ranking in an insolvency proceeding. According to the Commercial Insolvency Law, if the company has been sentenced to pay compensatory and / or punitive damages to a victim, the claim would be considered an unsecured claim, provided it does not meet the requirements to be considered as another kind of claim.[4]

On the other hand, the compensation to employees derived from health and safety liabilities are given an absolute priority under the Constitution of the Mexican United States, Commercial Insolvency Law and the Federal Labour Law.

Article 123, section XXIII of Heading A of the Constitution indicates that the claims in favour of employees for their salary or earned income in the last year, as well as compensation, will have preferential treatment before any other claim in the case of the insolvency or liquidation of a company.

Furthermore, article 113 of the Federal Labour Law provides that earned income in the last year, as well as compensation owed to employees, must have priority over the employer's assets over any other claim, including secured claim, tax claims and claims in favour of the Mexican Institute of Social Security.

### 2.3 Governance (G): third party releases in favour of directors and officers of the company

According to the Commercial Insolvency Law, the standby periods, waivers and other benefits provided by the agreement will only concern the debtor, not its guarantors, unless the creditors agree that the terms of the restructuring plan will also extend to the debtor's guarantors.

The law does not provide any restrictions or conditions that apply when third party releases of liabilities are sought in favour of the directors and officers of the company in relation to potential claims against them.

Nonetheless, the Commercial Insolvency Law indicates that companies cannot include in their bylaws any benefits or liability exclusions that limit, release, substitute or compensate the liabilities of which directors or relevant employees may be responsible for. However, a company can subscribe to insurance agreements, bonds or guarantees that may cover the amount of the compensation related to damage and losses caused by directors and / or relevant employees, unless the damage and losses result from wilful acts.[5]

Directors and relevant employees of the company are liable and responsible for compensating the company for damages and losses that caused it to become insolvent. The claim of liability for the company to obtain compensation for damages by losses caused by directors and relevant employees can be filed by the debtor or its shareholders.[6]

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

#### *3.1.1 Approving a restructuring plan*

The restructuring plan is only subject to the approval of the Bankruptcy Court, which must verify it complies with the public order as well as the requirements contained by the law.

However, once approved by the Bankruptcy Court, other regulatory bodies might need to approve the agreement for it to be implemented. If the plan will impact the environment in any way, the parties will certainly need for the environmental protection authorities to approve it or issue the necessary permissions and licences.

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4 Commercial Bankruptcy Law, art 22.
5 Commercial Bankruptcy Law, article 270 Bis.
6 *Ibid*.

#### *3.1.2 Discretion to consider wider public interest concerns*

According to article 164 of the Commercial Insolvency Law, the Bankruptcy Court must be satisfied that the restructuring plan does not contravene the public order, which includes environmental concerns.

#### *3.1.3 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

Environmental protection authorities and environmental advocacy groups do not have any standing to air their views or concerns in restructuring proceedings. Only the debtor, creditors, the public prosecutor and the conciliator are involved in the restructuring process. Thus, environmental protection authorities and environmental advocacy groups are not directly or indirectly involved in the process or negotiations.

However, as mentioned before, if the implementation of the approved plan would negatively impact on the environment, then environment protection authorities and environmental advocacy groups could deny any required licenses or permissions upon which the plan depends.

### 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

Labour creditors cannot subscribe to the reorganisation agreement. Nonetheless, the debtor can enter individual agreements with its labour creditors if these agreements do not aggravate the debtor's situation. Consequently, unions, employees, worker advocacy groups and even labour authorities are relevant for the restructuring of individual labour claims agreements.

However, unions and labour authorities must be notified about the beginning of the insolvency proceeding. As a result, they could air their views and concerns to the Bankruptcy Court in a restructuring process. The Bankruptcy Court could consider labour issues in deciding whether to approve a restructuring plan in the sense that, as mentioned, they are obliged to make sure it does not contravene public order matters.

Furthermore, the only creditors that can execute against a seized asset of the insolvency estate are the employees, in the case when such seizure is ordered by a labour court or authority to secure the payment of labour claims for wages and employee benefits for a period of two years preceding the date of the insolvency judgment. In that sense, employees could have a standing view or decision on the restructuring plan if it contains provisions that impact the seizure of assets.

#### *3.2.1 Approving a restructuring plan*

As noted, the restructuring plan is only subject to the approval of the Bankruptcy Court, which has to verify it complies with the public order as well as the requirements contained by the law.

While the labour creditors cannot subscribe to the reorganisation agreement, the debtor can enter individual agreements with its labour creditors if these agreements do not aggravate the debtor's situation. Consequently, it might be the case that a labour authority may need to approve the restructuring of individual labour claims agreements.

#### *3.2.2 Discretion to consider wider public interest concerns*

According to article 164 of the Commercial Insolvency Law, the Bankruptcy Court must be satisfied that the restructuring plan does not contravene the public order, which includes labour concerns.

#### *3.2.3 Protection of employee rights*

Unions and labour authorities must be notified about the proceeding. As a result, they could air their views and concerns to the Bankruptcy Court in a restructuring process. The Bankruptcy Court could consider labour issues in deciding whether to approve a restructuring plan in the sense that, as mentioned, they are obliged to make sure it does not contravene public order matters.

Additionally, employees that have a claim against the debtor are part of the proceeding. Thus, they can appeal, as any other creditor can, the judgment in which the reorganisation agreement is approved by the court, arguing that it contravenes the public interest because it violates employees' rights.

### 3.3 Governance (G): board / management conflicts addressed in a restructuring

In Mexico, the restructuring plan must be entered between the debtor and the creditors that hold the simple majority of unsecured and subordinated claims and creditors that hold the simple majority of secured and privileged claims. Consequently, directors and management do have the power to control or influence the formulation of a restructuring plan.

There are no legal provisions that regulate the negotiations that a board of directors or management may seek post-restructuring for committing to continue their services for the company. As a result, market standards and practice would apply on resolving potential conflicts regarding such situations.

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

Some of the main industry guidelines or best practices relating to the protection of the environment that may be applicable in a restructuring process are:

- the Equator Principles, which have environmental and social standards that credit institutions must consider for granting funding over US $10 million;
- the Sustainable Development Goals of the 2030 Agenda adopted by the UN Assembly, which establishes an action plan that benefits people, the planet and prosperity, and has the intention to strengthen universal peace and access to justice;
- certifications that a company may receive through different international norms, such as the ISO or the OHSAS. An example of these type of norms would be the ISO 14001:2015, Environmental Management Systems, which provides a framework for companies and sets the international standard that specifies requirements for an effective environmental management system.

Furthermore, a legislative proposal was presented in the Chamber of Senators called "*Ley General de Economía Circular*" or "General Law of Circular Economy", the objective of which is to safeguard the right to live in a healthy environment for people's development, health and wellbeing. Furthermore, the law aims to reduce the environmental impact caused by economical activities by minimising the waste of materials and reduce the consumption of raw materials through their reutilisation, recycle and redesign.

Finally, on 15 February 2023, the Law of Circular Economy in Mexico's City was approved to promote a more sustainable consumption amount the city's population, as well as to establish a framework for companies to reduce their negative impact on the environment.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

In Mexico, there are several guidelines or best practices that should be observed to take actions or decisions to protect employees' interests in a restructuring context, such as:

- the C173 – Protection of Workers' Claims (Employer's Insolvency) Convention, 1992 (No. 173);
- R180 – Protection of Workers' Claims (Employer's Insolvency) Recommendation, 1992 (No. 180); and

- the Criteria issued by the Federal Institute of Insolvency Experts regarding the protection of employees' interests and claims.

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

In Mexico, there are bar and school associations that have created codes of conduct for lawyers which could guide restructuring professionals to avoid or resolve a conflict of interests, such as the Professional Ethics Code of the Barra Mexicana, Colegio de Abogados, A. C., the Ethics Code of the Asociación Nacional de Abogados de Empresa, Colegio de Abogados A.C. and the Code of Ethics of the Ilustre y Nacional Colegio de Abogados de México.

Furthermore, the Federal Institute of Insolvency Experts has issued several non-binding criteria to interpret the Commercial Bankruptcy Law and a Code of Conduct which could serve as soft law instruments in relation to avoid potential conflicts of interests regarding the appointment and activities of conciliators, liquidators and examiners.

The Commercial Insolvency Law also contains several provisions regarding the conflicts of interest that insolvency specialists (i.e. registered conciliators, liquidators and examiners) may have in the insolvency proceeding in which they have been appointed. Therefore, if a specialist finds himself or herself in one of the prescribed circumstances, he or she must resign, or the parties can ask for his or her removal from the proceeding. The Federal Institute of Insolvency Experts has interpreted some of these circumstances and has issued non-binding criteria to understand if a certain action can be considered a conflict of interest.

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

In Mexico, ESG-linked loans, bonds and investments have become more popular in the last few years. In 2016, only two bonds were issued for MXN $3 million and in 2021 they reached MXN $82,325,000, and the issuance of these kinds of bonds is expected to grow even more and represent 50% of the total bonds to be issued in the country by 2026.[7]

The first "green loan" of Latin America was subscribed in Mexico in 2018 by Iberdrola Mexico with different international financial entities for the amount of US $400 million. [8]

Also, Mexico City is the first city in Latin America to issue a "green loan" for an investment of US $50 million by private investors to fight climate change by reducing carbon dioxide with LED illumination and improving public transportation in the city.[9]

The "*Fideicomisos Instituidos en Relación con la Agricultura"* (FIRA for its initials in Spanish), which are four public trusts the purpose of which is to facilitate access to credit by projects related to agriculture, livestock, poultry, agribusiness, fishing and other rural activities, has issued multiple green bonds for MXN $800 million and one social bond for MXN $250 million. The obtained resources were destined to agriculture and reforestation projects, as well as the efficient use of water and renewable energy.[10]

Finally, Banobras, the National Bank for Public Works and Services of Mexico, in 2017 and 2018 reaffirmed its commitment with the climate agenda to issue MXN $1,036.68 million pesos for green and social bonds for sustainable projects, infrastructure works and the strengthening of financial institutions.[11]

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7 https://www.forbes.com.mx/negocios-bonos-sustentables-podran-representar-50-mercado-mexico-2026/.
8 https://www.iberdrola.com/sostenibilidad/inversiones-bonos-verdes.
9 https://apolitical.co/solution-articles/es/ciudad-de-mexico-se-convierte-en-el-primer-bono-verde-de-emision-de-america-latina.
10 https://greenfinancelac.org/es/nuestras-iniciativas/bonos-verdes-sociales-y-tematicos/.
11 https://www.fira.gob.mx/Nd/ESG-ambiental.jsp.

### 5.2 Financial institution (banks and funds) and their commitment to achieve ESG targets

Financial institutions have signed on to commitments to achieve ESG targets in their lending portfolios and to apply ESG risk management policies in Mexico.

For example, Banco Mercantil del Norte, S.A. Institución de Banca Multiple Grupo Financiero Banorte signed the United Nations Environment Programme (UNEP) Net-Zero Banking Alliance in April 2021.

Furthermore, multiple Mexican banks, such as Banco del Bajío, S.A. Institución de Banca Múltiple, Banco Mercantil del Norte, S.A. Institución de Banca Multiple Grupo Financiero Banorte, Banco Regional S.A. (Banregio), BBVA México, CIBanco S.A. and Grupo Financiero Banamex, are members of the UNEP Commitment to Climate Action.

Financial institutions in Mexico, including Banco Mercantil del Norte, S.A. Institución de Banca Multiple Grupo Financiero Banorte, Banco Santander S.A., CIBanco S.A. and Banco Sabadell, are members of the Equator Principles.

Also, the Mexican Banks Association has established protocols with the goal to institutionalise sustainable development, setting up five principles, which include the management of environmental and social risks in investment processes or granting loans, as well as promoting the financing of projects for social and environmental sustainability.

Furthermore, in 2016 a Sustainability Protocol for financial institutions was launched to reach an agreement on guidelines regarding principles to manage environmental and social risks in investment processes or loans.

Finally, Nacional Financiera (NAFIN for its initials in Spanish), which is one of the Mexican development banks, has established a Social and Environmental Policy, which is a guideline to promote, among other things:

- lending money to companies with projects that aim to advance national economic sustainable development by establishing a better use of natural resources and respect of human rights;
- the fulfilment of international standards such as the Equator Principles and the IFC; and
- the development of social and environmental projects financed by NAFIN among borrowers, investors and other interested parties.

### 5.3 Promoting ESG by the central bank and regulators

Banco de Mexico (BANXICO), the Mexican Central Bank, has a Consultive Counsel of Green Finances called "*Consejo Consultivo de Finanzas Verdes*", which is a representative organ of the Mexican financial sector that promotes the financing of projects and investments that generate environmental positive impact.

The organ was created in 2016 in response to the growing necessity to develop a sustainable financial market in Mexico, in which its main players can attend challenges related to climate change, taking into consideration the risks and opportunities in all of the economy sectors.

Its main objectives are to:

- promote the discussion on how to drive the financing of projects that generate positive environmental impacts;
- discuss the necessity to attend new financial risks and challenges related to environmental, social and corporative government factors;
- propose incentives and mechanisms that provoke positive changes to the practices in the market, available investment vehicles and existing regulations;

- conduct strategic alliances with international institutions and experts in green financing for the creation of local capacities through the exchange of better practices and specialised financing education; and
- emphasise to authorities, regulators and interest groups the public policies that benefit the development of a sustainable financial market, allowing the creation of long-term value, the efficient use of natural resources and the transition to a low-carbon economy.

The Consultive Counsel of Green Finances has created the "Green Bonds Principles MX" or "*Principios de Bonos Verdes MX*" in order to generate common standards that may guide the processes of the issuance of green bonds in the Mexican market, as well as to give investors certainty about the environmental benefits of their investment.

# NEW ZEALAND

## 1. General overview of the restructuring regime[1]

The notion of restructuring corporate affairs without bringing to account both environmental and social issues is to ignore the irrefutable evidence that the long-term survival of an organisation depends upon the acknowledgement, and acceptance, of the connection between a customer and the world the customer lives in.

Regard for employee welfare and wellness, social sustainability, environmental risk aversion, promotion and alignment to climate-friendly regulation are the firm's social capital. Its right to exist is tempered by the endurance of its focus and contribution toward constant improvement of its standing in environmental affairs.

Restructuring is a deliberate activity and develops within a framework of intended outcome. The restructuring may be triggered by circumstances that have befallen the firm or by conscious choice to alter the way the firm does business. How it may have reached this point, the use of its resources, the way it contributes to its society and the focus on how it can protect its environment are critical considerations for the restructuring activity and essential for sustainability of both the company and the world we live in.

### 1.1 Formal restructuring procedures

New Zealand law enables applicants to approach the courts to resolve issues relating to any restructuring plan or proposal. Typically, applications are to obtain orders or directions involving a specific element of a restructuring proposal rather than an engagement involving all matters relating to the restructuring. The closest to a fully supervised restructuring plan is found in Part 15 of the Companies Act 1993 (Act) and is considered in section *1.1.1* below.

#### *1.1.1 Approval of arrangements, amalgamations, and compromises*[2]

Upon the application of a company, any of its shareholders or a creditor, approval may be granted for an arrangement, an amalgamation or a compromise. When granted, the order is binding on the company and on such other persons, or classes of persons, as the court may specify, and with terms and conditions the court may see fit in the circumstances. The court in *Weatherston*[3] made it clear that the procedure requires both initial and final approval of the court.[4]

- ***Control of the process***

  The court has determined that "it is plain that the legislature intended that under the Part XV procedure the court should have a broad discretion, limited only by the policy and purposes of the Act."[5]

  That broad discretion entitles the court to make an order, or orders, that lie within the scope prescribed in the following sections of Part 15:

  - an order that any notice of the application will contain such information and be produced in a form as the court thinks fit. The notice must be delivered to such persons, or classes of persons, as the court may specify;[6]

  - an order directing the holding of a meeting of shareholders, or any class of shareholders, or creditors or any class of creditors, to consider, and if thought fit, to approve the

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[1] Unless otherwise stated, the issues addressed in this paper relate to a company. In large part, the relevant law is the Companies Act 1993 (Act).
[2] Act, Part 15.
[3] *Weatherston v Waltus Property Investments Limited* [2001] 2 NZLR 103.
[4] *Idem,* para 6.
[5] *Idem*, para 31.
[6] Act, s 236(2)(a).

proposal in a manner the court may specify. The court may determine the shareholders or creditors which will constitute a class of shareholders or creditors;[7]

- an order requiring that a report on the proposed arrangement or amalgamation or compromise be prepared for the court by a person specified by the court. If the court sees fit, the report is to be provided to shareholders or creditors or any class of shareholders or creditors, as well as any other person the court considers will be interested;[8]

- an order as to the payment of costs incurred in the preparation of any such report;[9] and

- an order specifying the persons who shall be entitled to appear and be heard on the application to approve the arrangement, amalgamation or compromise.[10]

As these provisions show, control as to the form of the proposal is clearly vested in the court. The substance of the proposal will need to be conceived, outlined and intended by the proponent.

- ***Steps required***

Determination of the outcome of a proposal is, broadly speaking, a two-step process. First, the court defines how the proposal is to be conducted and then secondly deliberates upon the results once resolutions have been considered and voted upon. Additionally, the court is mindful of the activity within these two polar points and will assess the probity of the process undertaken between them.

In *Weatherston,*[11] the court approved a four-step[12] process to be used as a test against which the activity must be held when considering whether to sanction a proposal. The four steps are:

- that there has been compliance with the statutory provisions as to meetings, resolutions and the application to the court;

- that the scheme has been fairly put before the class or classes concerned, and that if a circular or circulars have been sent out (whether before or after the making of the application to the court), they give all the information reasonably necessary to enable the recipients to judge and vote upon the proposals;

- that the class was fairly represented by those who attended the meeting, and that the statutory majority are acting bona fide and are not coercing the minority in order to promote interests adverse to those of the class whom they purport to represent; and

- that the scheme is such that an intelligent and honest person of business, a member of the class concerned and acting in respect of his / her interest, might reasonably approve.

The courts have subsequently added a further two tests: the fifth being a consideration of there being any public policy reasons why the approval should be declined, and the sixth being whether the scheme is fair and reasonable.[13]

- ***Approval thresholds***

Section 236(2)(b) of the Act invites the court to prescribe the requirements for the holding of a meeting and for the shareholders or creditors to "consider, and if thought fit to approve, in

7 *Idem*, s 236(2)(b).
8 *Idem*, s 236(2)(c).
9 *Idem*, s 236(2)(d).
10 *Idem*, s 236(2)(e).
11 See above, n 3, para 32.
12 The four steps were formulated by Smith J in *Re CM Banks Ltd* [1944] 248 at 253.
13 Refer to Heath and Whale, published by Lexis Nexis, 2nd edition, para 14.21.

such manner as the court may specify". By this dictum, the court may establish the voting threshold that must be reached for the resolution to be affirmed. Regardless of the scope provided, it is likely to be that a resolution is not affirmed unless a majority in number support it and that their vote represents at least 75% in value of those entitled to vote and who do vote.

Upon a proposal being considered for approval, the court may make additional orders which provide authority to ensure the sanctioned arrangement, amalgamation or compromise will be given full effect.[14] These can include:

- the transfer or vesting of real or personal property, assets, rights, powers, interests, liabilities, contracts and engagements;
- the issue of shares, financial products or policies of any kind;
- the continuation of legal proceedings;
- the liquidation of any company;
- the provision to be made for persons who voted against the proposal; and
- such other matters that are necessary or desirable to give effect to the proposal.

- ***Court involvement***

The court becomes closely involved with the facts of the restructuring plan contended for. Upon the application, the court can establish the form and content of the proposal as well as how it is to be considered by the affected parties. Upon receiving the response from the affected parties, the court must agree to sanction the proposal. If it does so, it may augment the outcome by the making of orders to give full effect of the sanctioned proposal.

- ***Restrictions***

The court may impose restrictions, limitations or accretions as it sees fit. The proposal as tendered by the application may end up in a different form and with altered content after the court has considered it. The safest way to ensure the proposal is not subjected to alteration by the court is to provide for the reasonable expectations of affected persons and make available sufficient information to allow for an informed decision to be made.

## 1.2 Informal restructuring procedures

There are two further statutory-based restructuring models that can be used to reconstruct the affairs of a company. The first is a compromise with creditors and the second is voluntary administration, both of which are considered in detail below.

### *1.2.1 Compromises with creditors*[15]

The most adaptable of the two options is the law relating to compromises with creditors. The framework of the law is general in nature and provides a high degree of flexibility to the proponent as a result.

- ***Control of the process***

The board of directors, a receiver, a liquidator or, with the leave of the court, any creditor or shareholder of the company (Person) may propose a compromise if that Person has reason to believe the company is, or will be, unable to pay its debts.[16]

14 Act, s 237(1).
15 *Idem,* Part 14.
16 *Idem,* s 228(1).

The most likely Person to propose a restructuring compromise is the board of directors. However, if a creditor or shareholder is minded in doing so, the court, on providing consent, may order the company to supply such details of other creditors as may be required to enable the creditor, or shareholder, to propose the compromise.[17]

- ***Steps required***

The proponent must compile, in relation to each class of creditors, a list of all known creditors that would be affected by the compromise and record against each creditor the estimated amount owed and the number of votes the claimant will be entitled to cast in respect of the proposed resolution. One dollar of claim, admitted for voting purposes, will count as one vote for the claimant.

After compiling the list, the proponent must deliver a notice to each creditor and each of the Persons, describing the intention to convene a meeting for the purpose of voting on the resolution.[18] The notice must contain a statement that provides the following information:[19]

- the name and address of the proponent and the capacity in which the proponent is acting;
- the address and telephone number to which enquiries can be made during normal business hours;
- the terms of the proposed compromise and the reasons for it;
- the reasonably foreseeable consequences for creditors of the compromise if approved;
- the extent of any interest of a director in the proposed compromise;
- an explanation that the proposed compromise, and any amendment to it, will be binding on all creditors if the resolution is approved; and
- details of any procedure proposed for varying the compromise following its approval.

The proponent must also provide a copy of the prepared list of creditors, and the notice must be delivered to the Registrar of Companies for registration.[20]

- ***Approval thresholds***

Unless it states otherwise, the proposal is only affirmed if all classes of creditors identified by the proponent in the list vote in support of it.[21] Within each class of creditors, a resolution is adopted if a majority in number representing 75% in value of the creditors, or class of creditors, entitled to vote and who do vote, affirm the resolution.[22]

The proponent must give written notice of the outcome of the voting to each known creditor, the company, any receiver or liquidator and the Registrar of Companies.[23]

The approved resolution may be varied in accordance with the procedure framed within the proposal and adopted within the resolution. Alternatively, a variation may be proposed by way of the same process that the proposal was originally adopted.[24]

17 *Idem*, s 228(2).
18 *Idem,* s 229(2)(a).
19 *Idem*, s 229(2)(b).
20 *Idem,* s 229(2).
21 *Idem*, s 230(3).
22 *Idem*, cl 5 of Schedule 5.
23 *Idem*, s 230(4).
24 *Idem*, s 231(1).

If a variation is adopted, it must be notified to the Registrar of Companies and the variation can have no effect until notice is provided.

- ***Court involvement***

  Freedom to adopt the proposal is left to the persons that are affected by it. However, on the application of the proponent, directions may be sought regarding any procedural requirement or to waive or vary any such requirement if the court is satisfied that it would be just to do so.[25]

  The court may also order that, for a specific period,[26] proceedings in relation to a debt owed are stayed, or that a creditor refrains from taking any other measure to enforce payment.[27] Despite the restrictions the court may impose, the rights of a secured creditor remain unaltered in relation to its interest in collateral property.

  If the court is satisfied, on the application of the creditor who was entitled to vote on the compromise, that insufficient notice was provided, or there was some material irregularity in obtaining approval of the compromise, or, in the case of a creditor who voted against the compromise, that the compromise would be unfairly prejudicial, the court may order that the creditor is not bound by the compromise or make such other order as it thinks fit.[28]

  An application made by an affected creditor must be made within 10 working days of the notice of the voting on the compromise being provided.[29]

- ***Restrictions***

  Although the proponent may structure a proposal in any way that may serve the desired outcome, it will be of little value unless it is affirmed by the creditors affected. The proponent will need to be mindful of the statutory provisions relating to the payment of preferential creditors. If consideration is not given to these expectations, it is unlikely that support will be given to the proposal, and it may fail as a result.

### *1.2.2 Voluntary administration*[30]

Voluntary administration, or VA as it is often referred to, is the model introduced in New Zealand with effect from 1 November 2007.

The VA model is an admirable example of legislators providing law with a prescriptive purpose. The model offers the potential for business recovery, while at the same time providing limitations designed to contain recovery activity within a reasonable framework. On the one hand, the model conceives of freedom to develop a recovery plan in an entrepreneurial manner but on the other, it requires compliance expectations to be met so that entrepreneurial hope does not override creditor interests.

- ***Control of the process***

  The administration commences by the appointment of an administrator.[31] The parties that may appoint are the company, a secured creditor having a charge over the whole, or substantially the whole, of the property of the company, a liquidator, an interim liquidator, and the court on the application of a creditor, a liquidator, the Financial Markets Authority, or the Registrar of Companies.[32]

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25 *Idem*, s 232(1)(a).
26 The period referred to commences no earlier than the date that the notice was given of the proposed compromise and no later than 10 working days after the date of the notice of the outcome of the voting.
27 Act, s 232(1)(b).
28 *Idem*, s 232(3).
29 *Idem*, s 232(4).
30 *Idem*, Part 15A.
31 *Idem*, s 239D.
32 *Idem*, s 239H.

Only a natural person, who is not disqualified, may be appointed as an administrator.[33] By far the greatest number of appointments stem from a resolution adopted by the board authorising the company to appoint. The board may only appoint if, in its view, the company is insolvent or may become insolvent.[34]

Once appointed, the administrator has control of the company's business, property and affairs,[35] and can carry on the business as well as manage the company's property and affairs.[36] If the administrator is so minded, he or she may terminate the business or sell its property.[37] Once appointed, the administrator may perform any function the officers could perform prior to the appointment.[38] The appointment of an administrator does not remove the directors from office but they have no authority to act unless by prior written approval of the administrator.[39]

- ***Steps required***

The VA model is framed with specific requirements and goals in mind. The appointment of an administrator by the directors is an occurrence that admits that the circumstances of the company can no longer be managed by the board.

On the presumption of insolvency, creditors will have a greater interest in the affairs of the company than the shareholders.[40] Once the company is in VA, the future of the company, through the medium of the administrator, is to be determined by the creditors.

The VA programme is designed to inform creditors of their exposure and the rights they have in respect of that exposure. Typically, the start and end of the VA are bound by the appointment and then the resolution of creditors to decide the company's future. The interval between the polar points is known as the convening period.

The convening period cannot be any longer than 20 working days,[41] unless court consent is obtained.[42] For that outcome, the administrator must apply to the court with reasons why the statutory length is not adequate. Consent will be determined with reference to issues such as the size and complexity of the affairs of the insolvent company.

The general timeframe for a VA, and the steps involved, are set out below. Note that the time span between intervals refers to working days:[43]

Day 0 Appointment made.

Day 1 Notice to the Registrar of Companies and to secured creditors.[44]

Day 3 Public notification and notice to known creditors convening the first meeting.[45]

Day 5 Receipt of directors' statement of current position.[46]

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33 *Idem*, s 239F.
34 *Idem*, s 239I.
35 *Idem*, s 239U(a).
36 *Idem*, s 239U(b).
37 *Idem*, s 239U(c).
38 *Idem*, s 239U(d).
39 *Idem*, s 239X.
40 Which prior to the appointment was for the board of directors to use the resources of the company to create shareholder wealth.
41 Act, s 239AT(2).
42 *Idem*, s 239AT(3).
43 Refer to section 2 of the Act to obtain the definition of a working day.
44 For the purposes of this requirement of the model, a secured creditor is a party that has a security interest over the whole or substantially the whole of the property of the company: Act, s 239ADW.
45 *Idem*, s 239AO.
46 *Idem*, s 239AF.

Day 8 First meeting held for the purpose of resolving to confirm the administrator, to consider appointing a creditors' committee and to consider the directors' tabled statement of current position.[47]

Day 20 Unless the convening period is extended by the court, provide notice to creditors of the watershed meeting, and issue the administrators' report providing detail on the business, property, affairs and financial circumstances of the company.[48]

Day 25 Conduct the convened watershed meeting.

The fundamental purpose of the watershed meeting is to allow the creditors the opportunity to determine the future of the company. Throughout the period of the VA, the administrator must analyse the affairs of the company and report the results of that investigation in the administrators' report. The report is to be delivered to creditors no later than the last day of the convening period.

The purpose of the report is to provide sufficient detail to allow the creditors to make an informed decision about the future of the company.[49] The decision the creditors must make to decide the future of the company is through one of only three options[50] available to them. They are to resolve that:

- the company execute a deed of company arrangement;
- the VA should come to an end; or
- a liquidator is appointed.

The administrator is required to provide an opinion, and give reasons for that opinion, to assist creditors in resolving upon the options.

- ***Approval thresholds***

The outcome of the VA is a matter to be determined by the creditors. VA is a collective process where all creditors can exercise their right to vote. In contrast to liquidation, a secured creditor may elect to vote without risk of converting its status to that of an unsecured creditor.

A related entity[51] may vote but conditions exist. Notice in writing must be provided by the related entity to the administrator before a relevant resolution is put that the related entity intends to vote upon.

In the circumstances where the related entity does vote, it must then, within 10 working days, make an application to the court to seek consent for the vote to be included in the resolution voted upon.

The court will consider the issue by questioning whether, if the vote is to be counted, it would be contrary to the interests of the creditors as a whole or would prejudice the creditors who voted against the resolution, or for it.[52]

The collective voice of the creditors is determined by way of resolution at a creditors' meeting. A resolution is affirmed if more than half the creditors, or class of creditors, vote in support of the resolution and their aggregate vote represents 75% in value of the creditors who are entitled to vote and who do vote.

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47 *Idem*, s 239AN.
48 *Idem*, s 239AT.
49 *Idem*, s 239AS.
50 Arguably a fourth option is to adjourn the meeting for a late time but for no longer than 30 working days: Act, s 239AZ.
51 Refer to Act, s 239AM(3) to identify what the term related entity means.
52 *Idem*, s 239AM(2).

- ***Court involvement***

  In addition to the power of the court to rule on related entities' right to vote, the court may be required to be involved in circumstances where an application is made for a liquidation order. The application may be made before the appointment of the administrator or during the VA. The court may adjourn the liquidation proceedings if it is of the view that it is in the best interests of the creditors of the company that the VA continues.[53]

  The court also has a general power to make any order that it thinks appropriate about how VA should operate in relation to a company.[54] Examples, but not an exhaustive list, of the court's power under this authority include:[55]

  - terminating the VA;
  - orders to protect creditors during the VA;
  - the validity of the administrator's appointment;
  - to provide a response to an administrator when seeking directions;
  - to supervise the administrator or deed administrator;
  - to order the administrator or deed administrator to remedy any default;
  - to respond to when the office of the administrator or deed administrator is vacant; and
  - to make a prohibition order in relation to a person the court considers is unfit to act as administrator or deed administrator by reason of persistent failures to comply or the seriousness of the failure to comply.

  Parliament has expressly proposed that the VA model is as free from court involvement as can be achieved. There is though recourse to the court for any matter that will require independent authority on matters relevant to the VA.

- ***Restrictions***

  Restrictions relating to VA are found within the rights for it to be initiated. Legislation entitles an administration to commence if it will maximise the chances of the company, or as much as possible of its business, continuing in existence[56] or, if that is not possible, the administration will result in a better outcome for creditors and shareholders than immediate liquidation.

  By way of those provisions, VA enables scope for business recovery that is only limited by the balance of what may be reasonable in the circumstances. An element of entrepreneurship will be necessary if recovery, reconstruction, and rehabilitation is to occur.

  The direct costs[57] of these dynamics at play are to be borne by the administrator.[58] In that light, there are no restrictions so long as the administrator can, and does, bear the cost of that activity.

  However, that freedom is limited by the obligations of the company to its creditors and shareholders at the commencement of the VA. The administrator will be restricted in the use

53 *Idem*, s 239ABV.
54 *Idem*, s 239ADO.
55 *Idem*, Sub-Part 17.
56 *Idem*, s 239A(a).
57 *Idem*, s 239ADH. Refer also to s 239ADI for liability for rent and s 239Y for obligations to employees.
58 Note that the obligation to meet costs and the freedom associated, does not necessarily extend to business being conducted pursuant to a deed of company arrangement. When a deed of company arrangement is executed, operations control and management will typically revert to the board of the company, with the deed administrator having high-level oversight and control.

of the property and resources of the company if any plan for business would result in a depreciation of the value of that property or resources.

## 2. Restructuring of ESG-related liabilities

The company comes into existence at the will of the shareholders that meet the statutory requirements for its incorporation. A coincidental requirement is for the incorporating shareholders to appoint a director that will manage the affairs of the company.

Essential requirements are associated with this role. In earlier times, the obligation was bound largely by needs to act in the best interests of the company, to ensure its continued solvency and to create shareholder wealth. Those needs have not altered but can no longer be conducted without reference to the external resources the company exploits. The corporate citizen cannot act indifferently – instead it must express genuine concern and exhibit acts of preservation for the environment in which it trades and the people that live within it.

Companies, in the hands of its directors, can fall victim to the dynamics of the marketplace that at times result in an insolvent circumstance. Liquidation may be a serious threat to be considered. The natural tendency of directors is to strive to overcome insolvency and to commit the use of resources to achieve a recovery. At times of restructuring, and striving to achieve survival, the notion of best practice for the environment will often be relegated. The following section of this chapter addresses matters that directors must concern themselves with when restructuring the affairs of a company to ensure they do not attempt to achieve an outcome for the company at the expense of the environment.

### 2.1 Environmental (E): restructuring environmental liabilities

The Resource Management Act 1991 (RMA) is the legislation in New Zealand enacted to promote the sustainable management of the natural and physical resources of the country.[59]

In the RMA, "sustainable management" means managing the use, development and protection of natural and physical resources in a way, or at a rate, which enables people and communities to provide for their social, economic, and cultural wellbeing.[60]

Given the depth and breadth of its ideals, the RMA has had a troubled journey since its enactment, based on the reality that any attempt to unify a population with such lofty principles will inevitably invite dissent and discord.

The place where breaches, innocent or deliberate, may occur is while in the pursuit of economic stability. The corporate entity has the potential to be an infringer when restructuring activity is taking place.

The RMA is the watchdog for the environment. It is active in its protective endeavours and takes infringement seriously, with penalties that are intended to curb indifference to its requirements. Offences and resulting penalties are to be found in sections 338 and 339 of the RMA. Some examples are listed below:

- a person contravenes or permits a contravention of restrictions in relation to land, subdivision, the coastal marine area, the beds of certain rivers and lakes, water or the discharge of contaminates;[61]
- there is dumping and incineration of waste in a coastal marine area;[62] and

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59 RMA, s 5(1).
60 *Idem*, s 5(2).
61 *Idem*, s 338(1)(a).
62 *Idem*, s 338(1A).

- the failure to provide information[63] or the wilful obstruction of the provision of information.[64]

Offences against the RMA are criminal and upon conviction a natural person may be imprisoned for up to two years or fined up to NZ $300,000.[65] In the case of a person other than a natural person, the fine can be up to NZ $600,000. If the offence is a continuing offence, the convicted person will be liable to a daily fine of up to NZ $10,000[66] for some of the offences and up to NZ $1,000 each day for others.

### *2.1.1 Types of environmental liabilities*

Environmental liabilities can be determined by different enforcing authorities. District and Regional Councils are a prominent point of enforcement given their power to consent and regulate matters that may result in environmental infringements. Some central government agencies will have similar scope. Issues concerning consents applied for land use, coastal permits, water permits or discharge permits will be heard in the Environmental Court.[67]

Types of liabilities can include the following:

- compliance obligations – these will include costs related to site investigations and the remediation resulting from a regulatory response to a circumstance. This may include the obligation to manage the effects of pollution arising from industrial activity that may pose a risk to human health or the environment. It may also include obligations relating to the treatment of water, excavations, reconstructing damaged properties and the corrective measures required for negative impacts of an acquired or formerly owned property;

- regulatory liabilities – these may include obligations relating to the manufacture, use and disposal of harmful substances, remediation and monitoring of effects and the prevention of harm arising from hazardous substances such as asbestos;

- civil liabilities – common law claims can run in parallel to regulatory action. Remedies may include damages, injunctive relief and abatement. The losses suffered which may have resulted in a civil claim could include damage to property, unlawful interference with a person's enjoyment of land or rights associated with that land; and

- contractual liabilities – environmental obligations may reside in established contracts. These may exist in sales contracts, leasehold interests and development agreements.

### *2.1.2 Priority given to environmental liabilities*

There is no priority given to environmental liabilities when a company enters a formal state of insolvency. There is a provision, however, which may achieve a preferential status for a creditor over the general body of unsecured creditors. This is where a creditor protects, preserves the value of or recovers assets of the company for the benefit of the company's creditors. Such activity can elevate the preserver of value to the full extent of their claim.[68]

### *2.1.3 Disclaimer of environmental obligations*

When a company is in liquidation, the liquidator is entitled to disclaim onerous property[69] that is "unsaleable, or not readily saleable, or that may give rise to a liability to pay money or perform an onerous act".

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63 *Idem*, s 338(2).
64 *Idem,* s 338(3).
65 *Idem*, s 339 (1).
66 *Idem*, s 339(1A).
67 Refer to https://environmentcourt.govt.nz.
68 Act, cl 1(1)(e) of Schedule 7.
69 *Idem*, s 269.

The effect of the disclaimer is to end, from the disclaimer date, the rights, interests and liabilities of the company in relation to the property disclaimed. The effect of the disclaimer may be to undermine the environmental obligations otherwise able to be imposed upon the company, for example pursuant to the provisions of the RMA.

In a 2021 decision[70] handed down by the Victorian Court of Appeal in Australia, the Court set aside a disclaimer notice, with one of the reasons stated as being that consideration must be given to the principles underpinning the Environment Protection Authority (EPA).

The facts of the case are useful to illustrate when an environmental issue will outweigh other legal entitlements.

The Australian Sawmilling Company Pty Limited (TASCO) was placed into liquidation by way of a creditors' voluntary winding up. TASCO owned land that had large stockpiles of mixed construction and demolition waste that had been accumulated by the previous owner that operated a materials recycling business on the land.

Prior to their appointment, the liquidators were on notice that TASCO was facing environmental issues relating to both pollution and a fire hazard. In that knowledge, the liquidators obtained an indemnity from a company that had been TASCO's sole shareholder up to approximately two months before the appointment of the liquidators.

The deed provided that if there was any shortfall in the available assets of TASCO, the indemnifier agreed to indemnify the liquidators for an unlimited amount as to environmental liabilities as well as AU $500,000 for expenses, remuneration and claims other than environmental liabilities.

On 3 April 2019, the liquidators wrote to the EPA recording that they had gained full control of the company and that the powers of the directors had been suspended.

On 29 April 2019, the EPA wrote to the liquidators informing them that it had decided to exercise its power to enter the land and conduct a clean-up of the land and that it would proceed to do so without further notice. Additionally, the correspondence recorded that the EPA would seek to recover from the liquidators as occupiers any reasonable costs incurred by the EPA in conducting the clean-up.

On 30 April 2019, the liquidators filed a notice of disclaimer of onerous property, contending that the estimated clean-up costs would exceed the value of the land after clean-up had occurred. The post clean-up value estimate was AU $11,155,000.

The court of first instance set the disclaimer aside on the ground that it would cause substantial prejudice to the EPA and the State. Relevantly, if the disclaimer stood, the EPA would not be able to obtain recourse to any payment that the indemnifier may be exposed to on the ground that the liquidators would no longer be occupiers. The setting aside was granted.

TASCO appealed that decision, arguing that the liquidators were not occupiers of the land, whether the disclaimer were to be effective or not, and that the disclaimer would not cause prejudice to EPA or the State. Additionally, TASCO argued that the judge's exercise of discretion miscarried.

Regarding the first contention, the Court of Appeal found against TASCO, ruling that a liquidator readily falls within the scope of someone in control of the premises, and that the liquidators were occupiers as a result.

On the second contention, the court confirmed the judge of first instance to be correct on the basis that the EPA's ability to gain the benefit of the indemnity would be denied if the liquidators were no longer occupiers. In that situation, the EPA would be prejudiced.

70 *The Australian Sawmilling Company Pty Limited (In Liquidation) & Ors v Environment Protection Authority & Ors* [2021] VSCA 294.

As to the third contention for appeal, the notion of miscarriage, the court affirmed that for the applicants to succeed on this point they must show that the judge acted upon a wrong principle, allowed extraneous or irrelevant matters to guide him, mistook the facts or failed to take into account a relevant consideration. The Court of Appeal decided that the applicants failed to demonstrate that the judge's exercise of discretion was miscarried.

The applicants failed and the setting aside of the disclaimer remained.

It is conceivable that this decision would become authority in New Zealand should the facts of any matter suggest it should be so.

#### *2.1.4 Summary of restructuring environmental liabilities*

When restructuring corporate affairs in New Zealand, the objective description relating to the principles of the RMA will be useful guidance as to the boundaries or limits of any activity or proposed activity. Those objective elements are:

- sustaining the potential of natural and physical resources (excluding minerals) to meet the reasonably foreseeable needs of future generations;[71]
- safeguarding the life-supporting capacity of air, water, soil and ecosystems;[72] and
- avoiding, remedying, or mitigating any adverse effects of activities on the environment.[73]

Prospective restructuring that is considerate of those objective requirements is likely to fare well in its endeavours.

### 2.2 Social (S): restructuring health or safety-related liabilities

The Health and Safety Act 2015 imposes an obligation to ensure that workers and others are given the highest level of protection from workplace health and safety risks so far as is reasonably practical. Abridged requirements are described below:[74]

- protecting workers and other persons against harm to their health, safety and welfare by eliminating or minimising risks;
- providing for fair and effective workplace representation, consultation, cooperation and resolution of issues in relation to work health and safety;
- encouraging unions and employer organisations to take a constructive role in promoting improvements in work health and safety;
- promoting the provision of advice and training in relation to health and safety; and
- providing a framework for continuous improvement and progressively higher standards of work, health and safety.

The obligation to protect the welfare of workers is patently clear and planners involved in restructuring an enterprise will need to adopt the spirit of the law rather than adopting a perfunctory approach to compliance.

71 RMA, s 5(2)(a).
72 *Idem*, s 5(2)(b).
73 *Idem*, s 5(2)(c).
74 Health and Safety at Work Act, s 3.

### 2.2.1 *Types of health and safety-related liabilities*

The Health and Safety Act imposes an active due diligence duty on those in a governance role to proactively manage workplace health and safety. The Act introduces the acronym PCBU, meaning "Persons Conducting a Business or Undertaking". This will include any legal person conducting any business of any sort or size, alone or with others and whether or not it is for profit or gain.[75]

Section 36 imposes a duty of care upon the PCBU to ensure that the health and safety of other persons is not put at risk from work carried out as part of the conduct of the business or undertaking.[76] This will include:

- the provision and maintenance of a work environment that is without risks to health and safety;[77]
- the provision and maintenance of safe plant and structures;[78]
- the provision and maintenance of safe systems of work;[79]
- the safe use, handling and storage of plant, substances and structures;[80]
- the provision of adequate facilities for the welfare of workers in carrying out work for the business or undertaking, including ensuring access to those facilities;[81]
- the provision of any information, training, instruction or supervision that is necessary to protect all persons from risks to their health and safety arising from work carried out as part of the conduct of the business or undertaking;[82] and
- monitoring the health of workers and the conditions at the workplace for the purpose of preventing injury or illness of workers arising from the conduct of the business or undertaking.[83]

The duty is cast upon the PCBU. The definition of PCBU extends to the person conducting a business or undertaking alone or with others.[84] The duty will therefore extend to all directors administering the affairs of the company.

### 2.2.2 *Treatment of health and safety-related liabilities*

The provisions of the Health and Safety Act are not to be taken lightly. If a person has a duty, as described in the previous section, the penalties for non-compliance can be onerous.

A person who is not a PCBU or an officer of a PCBU is liable on conviction for imprisonment not exceeding five years or a fine not exceeding NZ $300,000 or both.[85] A person who is a PCBU or an officer of a PCBU is liable on conviction for imprisonment not exceeding five years or a fine not exceeding NZ $600,000 or both.[86] For any other person, that person is liable on conviction to a fine not exceeding NZ $3 million.

## 2.3 Governance (G): third party releases in favour of directors and officers of the company

For third party releases to be effective in a restructuring plan, they will need to be provided for in the arrangements sought to be affirmed by the creditors convened.

75 *Idem*, s 17(1)(a).
76 *Idem*, s 36(2).
77 *Idem*, s 36(3)(a).
78 *Idem*, s 36(3)(b).
79 *Idem*, s 36(3)(c).
80 *Idem*, s 36(3)(d).
81 *Idem*, s 36(3)(e).
82 *Idem*, s 36(3)(f).
83 *Idem*, s 36(3)(g).
84 *Idem*, s 17(3)(a)(i).
85 *Idem*, s 47(3)(a).
86 *Idem*, s 47(3)(b).

If a company enters VA, as noted, a moratorium protects a director or the director's spouse or relative[87] from being forced to meet a guarantee of liability.[88] The meaning of liability is extended to include "other obligation", suggesting that an obligation that has arisen from, say, a health and safety at work breach may be subjected to the provisions of the moratorium.

This limitation, however, is confined to the director, his or her spouse and related parties. The clear policy objective is to stop a creditor from initiating a collection process that will distract the third-party debtor from the proposed restructuring plans and frustrate the outcome accordingly.

However, the moratorium only lasts for the period of the administration. At the time of the watershed meeting, the creditors determine the future of the company by resolution. If the option is chosen to proceed with the restructuring plans by means of a deed of company arrangement, provision will need to be made, in the terms of the deed, for a continuation of the moratorium. If not, its endeavours are likely to suffer from the distraction that results from the imposing demand on the likely very limited time and capital available to the guarantor.

The creditor will need to make a reasoned choice as to whether it is better to forego the right to pursue the guarantor in favour of supporting the restructuring plan. Importantly, the terms of a continuing moratorium will be crammed down upon a dissenting creditor.

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

#### *3.1.1 Approving a restructuring plan*

There is no requirement for a restructuring plan to be approved by an environmental protection authority. However, section 12 of the Environmental Protection Authority Act 2011 states that the objective of the Act is to contribute to the efficient, effective and transparent management of New Zealand's environmental and natural and physical resources. Together with the Resource Management Act, discussed in section 2.1 above, any restructuring plans that may be at odds with the legislation will be susceptible to failure.

#### *3.1.2 Discretion to consider wider public interest concerns*

Most restructuring plans will be undertaken without court involvement. Where a proposal does require the sanction of the court, as in the case of a Part 15 scheme of arrangement, the relevant law would allow the court to consider the wider public interest.

#### *3.1.3 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

In circumstances where new capital is sought to be introduced as a necessary requirement of a restructuring plan, investors are likely to be influenced by publicly available news of environmentally sensitive issues. If the proponent of a restructuring plan is blind to the nuances of public sentiment, then funding expectations may not be as fruitful as may be required.

In 2019, a New Zealand environmental activist group filed court proceedings against seven major New Zealand companies alleging that they have not done enough to reduce greenhouse gases. The plaintiff alleges that the emissions cause harm and that it is in the face of scientific evidence that continued emissions will advance global warming and continue to cause harm. This action is at a very high level but is instructive in its pursuit that strong sentiment exists in New Zealand on environmental matters.[89]

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87 Refer to s 2 of the Act for a definition of "relative".

88 Act, s 239 ABJ(1).

89 Refer to *Michael John Smith v Fonterra Co-operative Limited, Genesis Energy Limited, Dairy Holdings Limited, New Zealand Steel Limited, Z Energy Limited, New Zealand Refining Company Limited and BT Mining Limited – SC 149/2021* [2022] NZSC 35.

### 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

#### *3.2.1 Approving a restructuring plan*

There is no right that a labour authority, union or employee advocacy group has to prevent a person proposing a restructuring plan. However, the efficacy of any restructuring activity will only be as good as there is reasonable alignment with the needs, wants and desires of its employees to facilitate a positive outcome.

#### *3.2.2 Discretion to consider wider public interest concerns*

As noted above, most restructuring plans will be undertaken without court involvement. Where a proposal does require the sanction of the court, as in the case of a Part 15 scheme of arrangement, the relevant law would allow the court to consider the wider public interest.

#### *3.2.3 Protection of employee rights*

In a restructuring, employees will be considered to the extent that the proposer of the plan perceives employees to be a relevant feature of the restructuring. The dynamic around the consideration of employees exhibited by the proposer will be matched by the degree of influence that the employees can bring to bear upon the process.

In the circumstances of a liquidation of an entity,[90] employees are granted the status of being preferential creditors. Their preferential rights are limited[91] to the realisation value of inventory and accounts receivable. If funds are available within the category in which employees will rank, they are paid rateably.

### 3.3 Governance (G): board / management conflicts addressed in a restructuring

A hierarchical tension will always arise across the various organs of corporate enterprise. At one end exists the philosophical standpoint that directing the resources of the enterprise is the core activity of management and that its crucial attention to detail is what keeps it solvent and worthy of continued investment. At the other end sits the notion that results are achieved through the delivery of output and high-level contemplation of results are of little value unless hands are placed upon the tasks that need to be undertaken.

The role of governance must include considerations of harmony across all factions of the organisation so that each level is rewarded appropriately and in a manner that matches the desire of the individual to occupy their chosen section of the organisation.

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

Pressure exists in New Zealand to be socially responsible. Free market capitalism is now somewhat tempered by environmental and social considerations. Corporate social responsibility (CSR) proposes that business should play a positive role in the community and be considerate of both the environmental and social consequences when making business decisions. This requirement will frequently be at odds with the earlier mandate of commerce which was essentially to create shareholder wealth.

Best practice is achieved by developing strategies that engage all stakeholders. While customers may be at the forefront of outward-looking thinking, for the CSR focused company, employees,

90 That may result because of the restructuring.

91 As well as some other limitations, such as quantum of claim and a limitation of the ability to claim outside of the prescribed time limit from within which the claim has accrued.

suppliers, the community, and its environment will receive consideration in addition to the company's shareholders.

A driver in the adoption of best practice will be the link, now well accepted as being in existence, between the sincere acceptance of CSR and a desirable result for the environment. Capital raising and obtaining skilled employees that have an empathy with the policies of the company are just two objective elements that are likely to result in a competitive advantage.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

Restructuring often involves adding or removing employees. Generally, in either situation, cultural changes take place in the organisation and the potential for harm to the individual employee may occur. Protection is afforded to employees by the Employment Relations Act 2000. Subpart 1 of Part 6A of that Act provides for the protection of employees if, as a result of a proposed restructuring, their work is to be performed by another person.

The proposer of the restructuring must be aware of the changes that may come down upon the employees and must act in a fair and reasonable way. To the extent that it affects an employee, the employer must explain the following:

- the reason for the restructuring;
- the nature of the restructuring and how it may affect employees;
- any anticipated redundancy and how that will be treated;
- the time frame available for employees to consider any proposal;
- the roles that will continue for employment because of the restructuring;
- opportunities for redeployment in other related companies; and
- any retraining opportunities that may exist.

In every instance, the employer must provide a written copy of the proposal and allow sufficient time for a response to be made.

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

Restructuring activity may be undertaken by any person considered to be competent enough to provide appropriate advice and propose a restructuring plan. For smaller businesses, a guiding involvement may come from the company's accountant or lawyer. For a SME or larger company, the bigger internationally branded accountants and business advisors may feature. Each different group of service providers will have their own code of conduct.

In New Zealand, insolvency practitioners must be licenced and a member of RITANZ.[92] They must also comply with the Insolvency Practitioners Regulation Act 2019.

IPs are bound by a Code of Conduct, with a primary purpose of the Code being to:

> Set standards of conduct of those involved in formal insolvency and restructuring assignments which protect the integrity of the insolvency system and are fair, effective, practical and readily understood.

"Conflict of interest" in the Code is defined as being:

[92] Restructuring Insolvency and Turnaround Association New Zealand Incorporated.

> Any circumstance, relationship or other fact relevant to the member's or firm's (or any of its partners, directors or managerial employees) own financial, business, property or personal interests which in reality will or reasonably may impair the rendering of objective insolvency and restructuring services.

Any breach of the Code will result in the issue being the subject of regulatory investigation and disciplinary action where appropriate.

## 5. ESG in financing

New Zealand's investment community has developed a Stewardship Code with an intent to transition New Zealand's financial system to strategically align with international trends and recommendations.

The combined involvement of New Zealand's major banks and major investors has resulted in the stewardship that involves the responsible allocation and management of capital by investors. The purpose is to create and preserve long term value for current and future generations.

The Stewardship Code provides that stewardship:

- promotes sound investor and corporate governance through the adoption of business practices that lead to sustainable outcomes for our environment, society and economy;
- helps investors build trust between companies and other issuers, key stakeholders and their community;
- encourages collaboration, and is most effective when asset owners, fund managers and other entities in the investment community work together, drawing upon an agreed set of expectations; and
- enables investors to be clear about their expectations and opens the way for deeper consideration of material environmental, social and governance matters.

The Stewardship Code is a significant alignment of the major banking and investment communities in New Zealand that manages a sizeable portion of the investment capital in New Zealand.

### 5.1 ESG-linked loans, bonds or investments

The New Zealand Government offers green bonds, which it describes as nominal fixed income bonds to provide finance for specific government projects with climate change mitigation and environmental outcomes.[93]

The New Zealand Sovereign Green Bond Framework outlines the Government's climate and environmental priorities and sets the basis for identifying, evaluating, selecting and reporting on expenditures included in the green bond programme.[94]

The New Zealand Government is committed to the reduction of the country's carbon footprint and aims to reach net zero carbon emissions by 2050.The issue of green bonds is a contributor to that outcome.

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

ANZ Bank is New Zealand's largest bank. It promotes on its website an ANZ Business Green Loan and states that "taking action can help address our planet's sustainability challenges and future-proof your business."[95] All major banking institutions in New Zealand have a similar offering for ESG-based applications.

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93 https://debtmanagement.treasury.govt.nz/government-securities/green-bonds.
94 https://debtmanagement.treasury.govt.nz/resource/new-zealand-sovereign-green-bond-framework.
95 https://www.anz.co.nz/business/borrow/anz-business-green-loan/.

By these means, the banking and investment fraternity is showing commitment to New Zealand meeting its ESG targets and contributing to achieve that result.

### 5.3 Promoting ESG by the central bank and regulators

The Reserve Bank of New Zealand[96] states on its website that it seeks to contribute the Government's objective of a sustainable, productive and inclusive economy. The Reserve Bank goes on to say that it will set monetary policy to conceive of such matters as climate change, and factor into its decision-making such issues when carrying out its functions.

The Government has also passed legislation making climate-related disclosures mandatory for some large financial market participants.[97]

[96] New Zealand's Central Bank.

[97] The Financial Sector (Climate-Related Disclosures and Other Matters) Amendment Act 2021.

# NIGERIA

## 1. General overview of the restructuring regime

### 1.1 Formal restructuring procedures

On 1 January 2021, the Companies and Allied Matters Act (CAMA) 2020 came into force and introduced administration and company voluntary arrangement (CVA) as restructuring options in addition to the existing formal restructuring procedure of arrangement and compromise.

#### *1.1.1 Arrangement and compromise*

Arrangement and compromise is a court-supervised scheme procedure which facilitates a change in the rights or liabilities of stakeholders of the company such as members, debenture holders or creditors of a company or any class of them. This also means that a scheme may be initiated as a response to the needs of the company or these stakeholders.

A scheme is sanctioned by the court,[1] provided it has been approved by at least a three-quarter majority in value of shares of members voting at separate meetings of the company or a meeting of the creditors or class of creditors.

Upon application to the court for the scheme to be sanctioned, the court refers the scheme to the Securities and Exchange Commission (SEC) for investigation of the fairness or otherwise of the scheme.

After the SEC reverts on the fairness of the scheme and the court is satisfied with the report, the court shall sanction the scheme and to this extent the scheme becomes binding on all the creditors or class of creditors or on the members or class of members or the company (even dissenting creditors and members), or the liquidator and contributories in the case of a company being wound up.

A six-month moratorium[2] prohibits the presentation of a winding up petition or enforcement action by a creditor (secured or unsecured) against any company undergoing a scheme with its creditors or its assets.

However, a secured creditor can apply to court to discharge the six month moratorium where the assets of the company sought to be enforced by the creditor do not form part of the company's pool of assets to be considered under the arrangement and compromise proceeding.

Additionally, a scheme of merger is to be approved by the SEC or Federal Consumer and Competition Protection Commission (FCCPC), Central Bank of Nigeria (CBN), National Insurance Commission (NAICOM) or National Pension Commission (PENCOM), or any other relevant regulator established by an Act of the National Assembly, particularly where the business is within a specially regulated industry such as the finance or insurance sectors.

#### *1.1.2 Administration*

Administration is a formal business restructuring procedure which may or may not be (at the discretion of the administrator) a management-displacing process to rescue the whole or any part of a company's undertaking as a going concern; or to achieve a better result for the company's creditors as a whole[3] if that is not possible; or realising property for distribution to secured and preferential creditors.[4] Pursuant to section 443 (1) of the CAMA, a person may be appointed as administrator of a company by:

1 CAMA, ss 711 and 715.
2 *Idem*, s 717.
3 *Idem*, s 444 (1).
4 If the primary purposes will fail, an administrator may apply for the company to be simply put into liquidation.

- an administration order of the court where the court is satisfied the company is or is likely to become unable to pay its debts and an administration order is likely to achieve the purpose of administration;[5]
- the company or its directors out of court; or
- the holder of a floating charge in respect of the company's property.[6]

However, an administrator shall not be appointed by the holder of a floating charge if, prior to the commencement of the CAMA and the coming into effect of its provisions on administration, a receiver or manager of the company is in office.[7] Also, a company or its directors may appoint an administrator out of court,[8] unless a receiver of the company is in office.[9]

Upon appointment, after due notice to all relevant parties and publications, the administrator is required to make a statement setting out proposals for achieving the purpose of the administration[10] and to send a copy of the same to the Corporate Affairs Commission (CAC) and every creditor of the company of whose claim and address he / she is aware of, and every member of the company of whose address he / she is aware before the end of 30 days from the day on which the company entered administration.[11] Subsequently, the proposals – which may include a proposal for voluntary arrangement[12] or scheme of arrangement and compromise or reconstruction[13] – shall be presented at the initial creditors' meeting[14] for approval with or without modifications.[15] Section 510(1)(a) of the CAMA excludes from the administrator's statement of proposal any action which affects the right of a secured creditor of the company to enforce its security.

Where an administrator reports to the court that an initial creditors' meeting failed to approve the proposals presented to it or a revision thereof, the court may provide that the appointment of an administrator shall cease to have effect from a specified time, adjourn the hearing conditionally or unconditionally, and make an interim order.[16]

While a company is in administration, no resolution shall be passed for the winding up of the company and nor can an order be made for its winding up.[17] Further, no step shall be taken to enforce security over the company's property except with the consent of the administrator or the permission of the court,[18] and no legal process, including legal proceedings, execution, distress or diligence shall be instituted or continued against the company or property of the company except with the consent of the administrator or permission of the court.[19]

For cessation, except where the administration is extended by the court to a period not exceeding six months, by consent of each secured creditors and more than 50% of the unsecured debts,[20] the administration shall cease automatically within one year of taking effect.[21] Where the administrator

5 CAMA, s 449.
6 By section 446 of the CAMA, an administrator is an officer of the court, whether or not he / she is appointed by the court.
7 CAMA, s 454(c).
8 *Idem*, s 459.
9 *Idem*, s 462.
10 *Idem*, s 486(1).
11 *Idem*, ss 486(4) and 486(5).
12 Here, the directors may make a proposal to creditors for a composition in satisfaction of the company's debts or a scheme of arrangement of its affairs and a nominee subsequently for the purpose of supervising the implementation of the voluntary arrangement.
13 CAMA, s 486(3).
14 *Idem*, s 488 CAMA.
15 *Idem*, s 490(1).
16 *Idem*, ss 492(1) and 492(2).
17 *Idem*, s 479(2).
18 *Idem*, s 480(2)(a).
19 *Idem*, s 480(4).
20 *Idem*, s 515(1).
21 *Idem*, s 513.

was appointed by the court, the court has to discharge the administration order and a copy of the order must be forwarded to the CAC by the administrator within 14 days.[22]

#### *1.1.3 CVA*

This process is only truly a formal alternative if it as a consequential decision of a liquidator or administrator. It is otherwise ordinarily an out of court process initiated by the company or its directors.

### 1.2 Informal restructuring procedures

Management-led corrections or negotiations – informal creditor workouts (ICWs) or multi-creditor workouts (MCWs) – thrived as informal restructuring alternatives prior to the advent of the CVA under the CAMA. These out of court transactions entailed amicable agreements between parties, debt settlement, distressed equity injections and asset for debt swaps or assets for equity swaps. However, in the absence of any stay or standstill agreement, these transactions remain prone to breaches owing either to a race to collect syndrome from creditors or bad faith, dilatory tactics and recalcitrance from the debtor.

#### *1.2.1 CVA*

As indicated, this is a management-retaining, out of court procedure that primarily allows directors of a company to make a proposal to creditors for composition in satisfaction of debts or a scheme of arrangement.

A CVA can be initiated by directors or an administrator / liquidator[23] with a proposal for a nominee to supervise the implementation of the CVA.

The nominee is to file a report of the proposal to the court stating whether, in his / her opinion, meetings of the company and of its creditors should be summoned to consider the proposal. The members' and creditors' meeting(s) summoned decide whether to approve the CVA proposal with or without modifications. A meeting so summoned shall not approve any proposal or modification which affects the right of a secured creditor of the company to enforce its security, except with the concurrence of the creditor concerned, nor approve any preferential debt of the company to be paid otherwise than in priority to non-preferential debts.[24] The outcome of the meetings is to be filed with the court and the nominee is to file relevant returns with the CAC upon implementation of the proposal.[25] At the members' meeting, the CVA proposal is deemed approved on a simple majority vote,[26] while for the creditors' meeting an approval of a proposal or a modification in a proposed CVA is made when three-quarters or more (in value) of those entitled to vote at the meeting vote in favour of it.[27]

## 2. Restructuring of ESG-related liabilities

### 2.1 Environmental (E): restructuring environmental liabilities

Generally, there is no distinction as to how environmental liabilities are treated under a restructuring procedure. There is no express prohibition against restructuring environmental liabilities, and they are treated in the same way as ordinary liabilities of a company.

#### *2.1.1 Types of environmental liabilities*

Environmental liabilities that a company may be subject to in Nigeria include:

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[22] *Idem*, s 524.
[23] *Idem*, s 434.
[24] *Idem*, s 437.
[25] *Idem*, s 442.
[26] Insolvency Regulation, reg 2.23.
[27] *Idem*, reg 2.11(4c)(II).

- statutory liabilities such as fines. The National Environmental Standards Regulations and Enforcement Agency (Establishment) Act 2007[28] (as amended) established the National Environmental Standards Regulations and Enforcement Agency (NESREA), the major federal body responsible for protecting Nigeria's environment and enforcing all environmental laws, regulations, guidelines and standards. The NESREA Act provides for fines in respect of various statutory offences such as violation of air quality and atmosphere protection, noise pollution, ozone protection, water quality standards, land resources and watershed quality, the discharge of hazardous substances and related offences; and

- civil claims such as claims in tort and claims in contract for losses arising from environmental disasters.

#### *2.1.2 Priority given to environmental liabilities*

There is no explicit provision stipulating that priority should be given to environmental liabilities during a restructuring procedure. No priority is given to environmental liabilities under Nigerian insolvency law and these liabilities would be treated as ordinary unsecured liabilities or claims against the company.

#### *2.1.3 Disclaimer of environmental obligations*

The CAMA[29] provides for the disclaimer of onerous property by a liquidator with the leave of the court where any part of the property of the company in liquidation consists of unprofitable contracts or any other property that is unsaleable, or not readily saleable, or is such that it may give rise to the performance of any onerous act or a liability for the payment of any sum of money – provided that, where the property has not come to the knowledge of the liquidator within one month after the commencement of the winding up, the power to disclaim may be exercised at any time within 12 months after the liquidator has become aware thereof or such extended period as may be allowed by the court.

To this extent, in the case of properties like factories or plants which may feature restrictive environmental obligations or liabilities, a liquidator can disclaim any property afflicted with environmental liabilities claims. However, not having been expressly stated by the law, it is uncertain that such similar powers will be available to an administrator in a restructuring process albeit an administrator will always have the leverage of seeking the court's directions to resolve such an issue.[30]

### 2.2 Social (S): restructuring health or safety-related liabilities

Generally, there is no distinction as to how health and safety-related liabilities are treated under a restructuring procedure. There is no express prohibition against restructuring health and safety-related liabilities. Specifically, under an administration, health and safety-related liabilities could potentially be treated as a preferential (priority) payment, being connected to liabilities to employees.

#### *2.2.1 Types of health and safety-related liabilities*

Health or safety-related liabilities under Nigerian law can encompass:

- civil claims such as claims in tort and claims in contract; and

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[28] There are several other environmental regulations such as the National Environmental (Healthcare Waste Control) Regulations 2021, the National Environmental (Food, Beverages and Tobacco Sector) Regulations 2009, the National Environmental (Textile, Wearing Apparel, Leather and Footwear Industry) Regulations 2009 and the National Environmental (Standards for Telecommunications / Broadcasting Facilities) Regulations 2011.

[29] *Idem*, s 663.

[30] *Idem*, s 500.

- statutory liabilities such as contributions and obligations under the Employees' Compensation Act 2010 (ECA). This legislation makes provisions for compensation for any death, injury, disease or disability arising out of or in the course of employment and for related matters.

#### *2.2.2 Treatment of health and safety-related liabilities*

There is no explicit provision stipulating that priority should be given to health and safety-related liabilities during a restructuring procedure. However, the insolvency laws recognise preferential payments by a liquidator under a winding up and empower an administrator[31] to make a distribution to the creditors of the company in line with the distribution priority as obtainable under a winding up.[32]

In a winding up, contributions and obligations of the company under the ECA are treated as preferential payments ranking in priority to all other debts excluding secured creditors and liquidation expenses. To this extent, in an administration, any health and safety-related liabilities pursuant to the ECA may be treated as a preferential (priority) payment.

As noted, the ECA makes provision for compensation for any death, injury, disease or disability arising out of or in the course of employment – including mental stress, occupational disease, hearing impairments, injuries outside the normal working place and temporary or total disability

Hence any obligation under these examples may be treated under preferential payments.

Notably, the ECA provides that where an employer becomes insolvent, any amount due or required by an employer to be paid to the Employees' Compensation Fund shall constitute a lien in favour of the Fund payable in priority over all liens, charges or mortgages of every person, wherever created or to be created, with respect to the property or proceeds of property, real, personal or mixed, used in or in connection with or produced in or by the industry with respect to which the employer was assessed or the amount became payable, except liens for wages due to employees by their employers.[33] The lien created in favour of the Fund shall remain valid and in force with respect to each assessment until the expiration of five years from the end of the calendar year for which the assessment was levied.

### 2.3 Governance (G): third party releases in favour of directors and officers of the company

There is no explicit provision prohibiting a duly appointed insolvency practitioner (IP) or office holder in a restructuring procedure from issuing third party releases of liability under a restructuring plan. However, it should be noted that the conduct of the office holder may be challenged by any affected stakeholder for being prejudicial or unfair.

Generally, in the case of directors and officers of the company, section 91(1) of the CAMA considers void any provision, whether contained in the articles of the company or in any contract with a company or otherwise, which purports to exempt any officer of the company or any person employed by the company as auditor from, or indemnifying him / her against any liability which by virtue of any rule of law would otherwise attach in respect of any negligence, default, or breach of trust of which he / she may be guilty in relation to the company.

Specifically, where any officer of the company or auditor has reasonable apprehension that a claim may be made against him / her in respect of any negligence, default, breach of duty or trust, he / she may apply to the court for relief, and the court on the application shall have the same power to relieve the person.[34]

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31 *Idem*, s 502(2).
32 *Idem*, s 657.
33 ECA, s 70.
34 CAMA, s 738(2).

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

#### *3.1.1 Approving a restructuring plan*

Restructuring plans such as an arrangement and compromise are approved by the courts and, as noted above, may also be required to be approved by the SEC or the FCCPC, the CBN, NAICOME or PENCOM, or any other relevant regulator established by an Act of the National Assembly. There is no specific requirement for a scheme to be approved by environmental protection authorities or environmental advocacy groups.

#### *3.1.2 Discretion to consider wider public interest concerns*

The court, in sanctioning the scheme, is expected to consider the fairness or otherwise of the scheme, relying on the SEC's report. The discretion is not at large, and the primary focus for the court in sanctioning a scheme remains the rights and interests of the creditors – as opposed to wider public interests such as environmental concerns – and in the case of an administration, achieving the purpose of the administration.

#### *3.1.3 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

We are not aware of any express statutory provisions granting environmental protection authorities (such as NESREA) or environmental advocacy groups the right to air their views or concerns in a restructuring. However, where the restructuring is being undertaken by regulated entities in regulated sectors, the notification to or approval by relevant regulatory agencies before commencing scheme proceedings may present an opportunity for influence and / or expression of environmental issues, particularly since there are administrative channels of communications between state-based regulators.

### 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

#### *3.2.1 Approving a restructuring plan*

There is no requirement for a restructuring plan to be approved by labour authorities, unions or employee / worker advocacy groups. However, in many cases, including unionised industries, they may be critical for the success of a restructuring plan and are usually managed, irrespective of the fact that, strictly, the restructuring plan only needs to be by the court, creditors and members of the company.

#### *3.2.2 Discretion to consider wider public interest concerns*

As stated earlier, in a scheme, the court is only technically concerned with the fairness or otherwise of the scheme relying on the report of the SEC. However, wider public concerns such as the policy position of the Government to save or protect an industry may influence things, particularly as labour claims are connected to preferential credit claims in a restructuring.

#### *3.2.3 Protection of employee rights*

Generally, there are no statutory provisions which grant labour authorities, unions or employee / worker advocacy groups standing to air their views or concerns in a restructuring, but labour authorities or unions are critical in heavily unionised or high labour industries.

As noted above, certain employee rights and interests under the ECA are also ordinarily considered priority or preferential payments during restructuring (administration) and winding up.

### 4.3 Governance (G): board / management conflicts addressed in a restructuring

Board / management conflicts can be managed effectively in a restructuring through, for instance, the duty for directors to provide the IP with a statement of affairs or accurate representations, the disclosure requirements under the restructuring and the provisions of the law on the fairness and reasonableness of the restructuring plan as a condition precedent to sanctioning by the court.

Also, the Nigerian Code of Corporate Governance 2018 entrenches disclosure obligations on the company and its officers to the effect that any related party relationships and transactions must disclose any director's interest in contracts either directly or indirectly with the company or its subsidiaries and holding companies, their purpose and their financial magnitude necessary to understand whether the transactions have been at arm's length and that the company has not suffered any loss or disadvantage from the transactions.

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

We have not identified any industry guidelines and / or best practices prescribed for the protection of the environment in a restructuring.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

It appears that there is a shortage of soft law instruments which serve as a guide or influence a company to take actions or decisions that protect employees' interests in a restructuring context.

The substantive law (the CAMA)[35] already provides for the protection of employee rights by the ranking of wages, salaries and deductions made from the remuneration of employees and contributions of the company under the Pension Reform Act as a priority (preferential) payment. Additionally, section 10 of the Labour Act is to the effect that the transfer of any contract of employment from one employer to another shall be subject to the consent of the worker and the endorsement of the transfer upon the contract by an authorised labour officer.

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

An IP is one or more persons duly accredited by the CAC to undertake insolvency proceedings in line with the provisions of the CAMA. The relevant soft law instrument guiding the appointment or accreditation of IPs is the Insolvency Regulations 2022. The Insolvency Regulations make no explicit provisions on the avoidance of potential conflict of interests by IPs. They merely provide[36] basic conflict situations issues by reference to the IP not being appointed to act where he / she acted as a director or auditor of the company, or is a connected person.

However, it is expected that IPs, being part of other professional bodies such as the Business Recovery and Insolvency Practitioners Association of Nigeria (BRIPAN) and the Nigerian Bar Association (NBA), will further comply with any relevant codes of ethics during the restructuring.

BRIPAN has a code of ethics which regulates IPs and also addresses conflicts of interest issues. The more recently accredited NBA Section of Business Law is also collaborating with the Commercial Law Network of Nigeria, a United Kingdom-funded research programme on ethics.

[35] *Idem*, s 657.
[36] Insolvency Regulations, reg 1.08.

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

Recently, activities relating to ESG have gained traction in Nigeria and, in line with the mandate of the Central Bank of Nigeria (CBN) as stipulated in the "Nigerian Sustainable Banking Principles" (NSBPs), many banks in Nigeria have adopted ESG principles in their business operations.

Also, the introduction of green and social bonds in the Nigerian capital market has provided the Government, companies, organisations and individuals with access to funds to finance infrastructural projects. Generally, green bonds and social bonds have played a great role in the development of ESG in Nigeria. In 2021, the SEC introduced "Rules on Social Bonds", wherein social bonds remain a type of debt instrument where the proceeds exclusively finance or refinance new and / or existing government projects, including social amenities.

There are also "Green Bond Rules 2018" which regulate Nigeria's sovereign issuance of sovereign green bonds in 2017 – the proceeds of which were used to finance green projects such as the Energising Education Project, the Rural Electrification Project and the Afforestation Project.

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

Many Nigerian banks have adapted the NSBPs in their business operations. For instance, Access Bank Plc debuted its Naira Green Bond issuance in 2019 and recently successfully closed its US $50 million Reg S Step-Up Green Notes in the international capital market via a private placement. The net proceeds from the issuance of the bond will be used by the bank for the financing or refinancing, in part or in full, new and / or existing projects and / or assets meeting the eligibility criteria set out in the Bank's Green Financing Framework dated 18 November 2021.

### 5.3 Promoting ESG by the central bank and regulators

In 2012, the CBN and the Bankers' Committee collaborated to establish the mandatory sustainable banking framework under the NSBPs.

The NSBPs require banks, discount houses and development finance institutions to develop a management approach that balances the environmental and social risks identified with the opportunities to be exploited through their business activities. The NSBPs cover: environmental and social risk management; environmental and social footprint; human rights; women's economic empowerment; financial inclusion; environmental, social and governance; collaborative partnerships; and reporting.

Many regulators and laws are also adopting ESG-compliant policies that will drive innovation, market resilience and sustainable economy. For instance:

- the CAMA[37] mandates directors to always have regard to the impact of the company's operations on the environment in the community where it carries on business operations;
- the Petroleum Industry Act 2021[38] (PIA) empowers the "Host Community Development Trust" to finance and execute projects for the benefit and sustainable development of the host communities;
- the Federal Competition and Consumer Protection Commission (FCCPC) is empowered to administer the provisions of the Federal Competition and Consumer Protection Act 2018 which protect the rights of consumers, including the right to safe, high-quality goods and the right to disclosure of prices of goods and services;
- the Nigerian Stock Exchange's (NSE) Sustainability Disclosure Guidelines – approved in 2018 for public companies – make sustainability / ESG reporting mandatory for companies listed on

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[37] CAMA, s 305(3).

[38] *Idem*, s 239.

the Premium Board of the NSE and further stipulate core principles on ESG and prescribed reporting requirements on ESG performance for listed companies; and

- principle 26 of the Nigerian Code of Corporate Governance (NCCG) requires companies to pay adequate attention to sustainability issues – including environmental, social, occupational and community health and safety – to ensure successful long-term business performance and a reputation as responsible corporate citizens, contributing to economic development.

# PEOPLE'S REPUBLIC OF CHINA

## 1. General overview of the restructuring regime

There are two types of in-court restructuring proceedings available under the Enterprise Bankruptcy Law of the People's Republic of China (EBL): reorganisation and reconciliation.[1] Informal out of court restructurings are conducted by some bankruptcy practitioners, but they are not specifically governed by the EBL.

### 1.1 Formal restructuring procedures

There are two management modes of formal restructuring procedures under the EBL: administration and debtor in possession (DIP).

The court will appoint an administrator to take charge of the debtor's management in general practice. The administrator will manage and dispose of the debtor's assets after taking the assets into custody under the insolvency procedures.[2]

In reorganisation proceedings, the debtor can also apply to the court to manage its own business, in which case the administrator will only have a supervisory role and will not be involved in daily operational decision-making.[3] The Supreme People's Court of the PRC (SPC) issued the "Minutes of the National Working Conference on the Trial of Civil and Commercial Cases by Courts" in 2019 (2019 SPC Meeting Minutes), and they clarify that the court may approve the debtor's DIP application if the following conditions are met:

- the debtor's internal governance mechanism still works normally;
- the DIP is favourable for its continuance of operation;
- the debtor has not hidden or transferred its assets; and
- the debtor has not materially acted against the interests of the creditors.

The 2019 SPC Meeting Minutes further confirm that the administrator should supervise the DIP process. If the debtor is found to materially act against creditors' interests or to have other aspects that are not suitable for the DIP, the administrator can apply to the court for termination of the DIP. If the administrator fails to apply to the court, the interested parties, such as creditors, may apply instead.[4]

The process of restructuring involves the stages set out below.

First, the administrator needs to investigate the property status of the company and review the claims filed by creditors.

Secondly, the court calls the first creditors' meeting, and this meeting will be held within 15 days of the expiry of the term for lodging a claim.[5] Pursuant to the EBL, the creditors' meeting exercises the following powers:

- verifying the claims;
- applying to the court to replace the administrator and review the fees and remuneration of the administrator;
- supervising the administrator;

[1] Enterprise Bankruptcy Law of the People's Republic of China (EBL), Part 8 (Reorganization), Part 9 (Reconciliation).
[2] *Idem*, s 25.
[3] *Idem*, s 73.
[4] 2019 SPC Meeting Minutes, s 111.
[5] EBL, s 62.

- selecting and replacing creditors' committee members;
- deciding to continue or stop the business of the debtor;
- adopting a reorganisation plan;
- adopting a settlement agreement;
- adopting the management plan of the debtor's property;
- adopting a plan for the realisation of the bankruptcy estate;
- adopting the distribution plan of the bankruptcy estate; and
- other powers and functions the court considers should be exercised by the creditors' meeting.

Next, the administrator or the DIP proposes a draft reorganisation plan pursuant to requirements stipulated by the EBL.

Then creditors are divided into several groups to cast votes on the draft plan, and where the level of support satisfies the legal requirements, the plan will be deemed approved by the group.[6]

Finally, if the plan is passed by the creditors' meeting, the court will issue a ruling to confirm the plan upon application by the administrator. After that, the court will rule to terminate the proceeding and the execution of the plan commences.[7] During this period, the value will be distributed to the creditors according to the legal hierarchy and on a *pari passu* basis unless the plan stipulates otherwise.

As stated above, creditors are classified into the following groups when voting on the draft reorganisation plan:[8]

- secured claims;
- labour and pension claims;
- tax claims; and
- unsecured claims.

Unsecured creditors, however, may sometimes be divided into a small-claim groups and an ordinary unsecured class depending on necessity and individual cases.

When half or more of the creditors in the same voting group, representing two thirds or more of the total amount of the creditors' claim, vote in favour of the draft restructuring plan, the plan is deemed to be passed by this group. When all voting groups vote in favour of the plan, the draft plan is deemed to be passed by the creditors' meeting.[9]

Within 10 days from the date when the reorganisation plan is passed by the creditors' meeting, the debtor or the administrator shall apply to the court for approval of the reorganisation plan. If the court, after examination, finds that the provisions of EBL are met, it shall, within 30 days from the date of receipt of the application, rule that the approval is granted, terminate the reorganisation procedure and make a public announcement.

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6 *Idem*, s 82.
7 *Idem*, s 86.
8 *Idem*, s 113.
9 *Idem*, s 84.

If one or more voting groups vote against the plan, the court will have, upon an application made by the administrator, discretion to decide whether to exercise its cram down power, subject to certain criteria prescribed by law. The court may exercise the power to cram down the plan if it meets the following requirements:

- the secured creditors will be paid off from the value of the collateral and the losses incurred from postponed payment will be compensated in a fair manner, provided that the secured claims have not been materially damaged, or the relevant voting group has approved the draft plan;
- wages and other expenses of the employees, and taxes, shall be paid off, or the relevant voting group has approved the draft plan;
- the repayment proportion of an unsecured creditor's claim shall not be lower than that in a liquidation scenario at the time when the draft plan is submitted for approval;
- the draft plan can bring a fair and just adjustment to the rights and interests of capital contributors;
- the draft plan treats the members of the same voting group fairly and the hierarchy of creditors' claims does not violate the provisions of article 113 of the EBL; and
- the debtor's business plan is feasible.[10]

Bankruptcy expenses, including administration expenses and remuneration of the administrator and other procedural expenses, as well as debts incurred during the proceeding for the common benefit of the creditors (including new money borrowed for continuous operation and liabilities incurred for the assumption of contracts), are not subject to restructuring. Secured creditors enjoy priority to the extent of the value of the collateral, except for claims related to (or arising from) the administration of the collateral.

### 1.2 Informal restructuring procedures

As indicated above, the EBL does not specifically provide for out of court workouts. However, some documents were issued by the SPC and the Central Government recently to promote informal restructuring procedures, including:

- the "Notice of the SPC on Issuing the Minutes of the National Court Work Conference on Bankruptcy Trials" (2018 SPC Meeting Minutes), published on 4 March 2018;[11]
- the "Reform Programme to Accelerate the Improvement of the Exit System of Market Subjects", issued by the National Development and Reform Commission (NDRC), the SPC and other ministries, published on 22 June 2019;[12]
- the 2019 SPC Meeting Minutes, published on 8 November 2019;[13] and

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10 *Idem*, s 87.

11 Section 22 states that "exploring and promoting the connection between the out of court restructuring system and the in court reorganisation system. Before a company enters into reorganisation procedures, creditors may conduct out of court business negotiations with the debtor, capital contributors, and other interested parties to prepare a reorganisation plan. After reorganisation procedures are launched, a draft reorganisation plan may be prepared based on the reorganisation plan and submitted to the court for adjudication."

12 This document proposes to "research and develop a pre-reorganisation system, achieve the effective connection among the out of court restructuring system, the pre-reorganisation system, and the in court reorganisation system, strengthen the credibility and binding force of out of court restructuring, and define the legal status and institutional content of pre-reorganisation."

13 This document provides for the extension of the effect of out of court restructuring agreements in the formal reorganisation procedures.

- the "Opinions of the State Council on Conducting Pilot Work on Business Environment Innovation", published on 31 October 2021.[14]

Summarising the above documents, the guidance regarding out of court procedures prior to a formal proceeding has the following principles in common:

- effectiveness of arrangement between debtor and creditor: prior to petitioning for reorganisation, the debtor may negotiate an arrangement with major creditors. If there is a draft plan formulated during the out of court stage, creditors may vote pursuant to the same standards prescribed by the EBL. The court recognises the effectiveness of a draft plan that has been passed by creditors' voting prior to a formal proceeding;

- estoppel rule: consensus reached by the debtor and the creditor based on autonomy of will shall continue to be binding upon both in a formal proceeding;

- interim administration: during the pre-reorganisation period, an administrator (or interim administrator) may be designated by the court. The administrator will be responsible for ascertaining assets and debts and leading the formulation of a reorganisation plan. In this stage, the interim administrator does not take over the debtor's company and the debtor still owns operation autonomy for maintaining its business value as a going concern; and

- linking debt restructurings to reorganisation proceedings: hybrid of out of court debt restructurings and judicial proceedings extend the effectiveness of out of court workouts and improve efficiency and certainty of in court proceedings.

## 2. Restructuring of ESG-related liabilities

### 2.1 Environmental (E): restructuring environmental liabilities

There are no special restrictions or conditions that apply to restructuring environmental liabilities under the PRC law.

#### *2.1.1 Types of environmental liabilities*

There are three types of environmental liabilities under the PRC law:

- civil environmental liabilities[15] – for those who cause ecological damage, the infringer shall bear tort liability,[16] including compensation for damages and restitution. For those who deliberately pollute the environment and damage the ecology in violation of the law causing serious consequences, the infringed has the right to request corresponding punitive damages.[17] If the ecological damage is repairable, the state authorities or organisations specified by law have the right to request the infringer to assume responsibility for the repair within a reasonable period time;[18]

- criminal environmental liabilities[19] – those who violate state regulations (including discharge, dumping or the disposal of radioactive waste, waste containing infectious disease pathogens, toxic substances or other harmful substances, or serious pollution of the environment) shall be sentenced to fixed-term imprisonment of fewer than three years or detention, and a fine or a single fine. If the circumstances are serious, fixed-term imprisonment of more than three years

[14] This document selects some cities to carry out the pilot programme of innovation in the business environment. The first batch of pilot cities is Beijing, Shanghai, Chongqing, Hangzhou, Guangzhou and Shenzhen. It requires "the implementation of the pre-reorganisation system"; "the system for the selection and appointment of bankruptcy administrators and the pre-reorganisation system shall be further improved, and the relevant creditors of the bankrupt company shall be allowed to recommend a bankruptcy administrator, and the bankruptcy administrator shall be designated by the court."

[15] Civil Code of the People's Republic of China (Civil Code), Part 7.

[16] *Idem*, s 1229.

[17] *Idem*, s 1232.

[18] *Idem*, s 1234.

[19] Criminal Law of the People's Republic of China (Criminal Law), s 338.

and fewer than seven years and a fine are applicable. For specific circumstances, fixed-term imprisonment of more than seven years and a fine are applicable; and

- administrative environmental liabilities[20] – companies, institutions and other producers and operators who emit pollutants illegally shall be fined and ordered to correct.[21] Some may even be required to restrict production, discontinue production or shut down.[22]

### *2.1.2 Priority given to environmental liabilities*

There are no clear provisions regarding any priority for environmental liabilities pursuant to the EBL and the classes of priority claims are subject to the prescription set forth in section 113 of the EBL (outlined above).

### *2.1.3 Disclaimer of environmental obligations*

There are no rules regarding disclaiming of environmental obligations under the PRC law.

## 2.2 Social (S): restructuring health or safety-related liabilities

### *2.2.1 Types of health and safety-related liabilities*

There are three types of health or safety-related liabilities under the PRC law:

- civil health or safety-related liabilities – whoever infringes upon another person and causes personal injury shall pay the related compensation, such as the medical fee or nursing fee.[23] Employers shall bear tortious liability for any injury or damage caused to other people by their employees in the course of their work.[24] Where a product defect endangers the personal or property safety of others, the infringed party may request that the producer or the seller assume tort liability, including the cessation of infringement, the removal of obstruction and the elimination of danger;[25]

- criminal health or safety-related liabilities – whoever violates the safety provisions in the course of production and operations, thereby causing an accident involving heavy casualties or causing other serious consequences, shall be sentenced to criminal detention or fixed-term imprisonment;[26] and

- administrative health or safety-related liabilities – where a production and operation entity commits any illegal act or violation of laws concerning work safety, its workplaces may be sealed and dangerous articles may be detained.[27]

### *2.2.2 Treatment of health and safety-related liabilities*

Pursuant to the hierarchies provided by the EBL, subsequent to repayment of bankruptcy expenses and debts incurred for common benefits, priorities are granted to employee wages, medical and disability subsidies, compensation expenses and pension insurance and basic medical insurance expenses that should be borne by individual employees, as well as the compensation that should be paid to the employees legally.[28]

For those liabilities that have not been covered by legislation, the court may reasonably decide the payment sequence on a principle that requires compensation for personal injuries to be

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20 Environmental Protection Law of the People's Republic of China (EPL), Part 6.
21 *Idem*, s 59.
22 *Idem*, s 60.
23 Civil Code, s 1179.
24 *Idem*, s 1191.
25 *Idem*, s 1205.
26 Criminal Law, ss 134-137.
27 Provisions on Supervision and Accountability of Work Safety Supervision Duties and Administrative Law Enforcement Liability, s 21.
28 EBL, s 113.

treated better than compensation for properties, claims incurred under private laws to be treated better than those incurred under public laws and compensatory claims to be treated better than punitive claims.

Compensation for personal injuries arising from a debtor's tortious acts may obtain the same preferential treatment as labour and pension claims under section 113 of the EBL, unless the claims are punitive. Punitive damages can only get paid when all claims provided by section 113 of the EBL are cleared.

### 2.3 Governance (G): third party releases in favour of directors and officers of the company

No rules or practices are referable under the PRC law.

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

#### *3.1.1 Approving a restructuring plan*

A reorganisation plan is subject to the court's approval, as outlined in section 1 above.

#### *3.1.2 Discretion to consider wider public interest concerns*

As mentioned above, the court approves the reorganisation plan pursuant to the EBL unless certain contents within the plan explicitly violate laws and regulations. There are no particular rules relating to environmental concerns under an insolvency scenario.

#### *3.1.3 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

No rules or practices are referable under the PRC law.

### 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

#### *3.2.1 Approving a restructuring plan*

Please see section 1 above for details.

#### *3.2.2 Discretion to consider wider public interest concerns*

Please see section 1 above for details.

#### *3.2.3 Protection of employees' rights*

Employees' rights are protected by the EBL in the following ways:

- when a debtor petitions the court for initiation of a proceeding, an arrangement of labour claims settlement, including the payment of wages and social security expenses, shall be submitted to the court together with the petition files;
- a representative of the employees or the labour union of the debtor is entitled to attend creditors' meetings and express opinion on matters relating to labour rights. If a creditors' committee is established during the proceeding, the representative of the debtor's labour union will become a member with the ability to participate in the operation of the committee;

- employees are not required to lodge claims with the administrator, while the administrator is obliged to find out the employees' claims and publicise the results for employees to raise objections if there are errors; and

- labour claims are categorised as a voting class to participate in the vote of the plan.

### 3.3 Governance (G): board / management conflicts addressed in a restructuring

The PRC law is silent on this issue. However, in practice, some restructuring plans may contain management incentive schemes, which mostly are subject to main creditors' attitudes. If the original shareholders of the debtor are cleared out through the plan, main creditors obtain shares under the plan as part of their repayments, and the creditors may consider offering options to the management for post-restructuring business running purposes. Under such circumstances, negotiation between the management and the creditors can be intense and outcomes in individual cases vary tremendously. Given that sample cases are rare, there is no standard market practice in consensus.

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

There are no industry guidelines nor practical standards regarding environmental issues under a restructuring context at the national level.

However, the Intermediate People's Court of Guiyang has issued "Guidelines on Handling Eco-Environmental Issues Involved in the Trial of Enterprise Bankruptcy Cases" recently. This newly published document makes an initial effort to draw practitioners' attention to the handling of ecological and environmental problems involved in bankruptcy cases, exploring methods of solving difficult problems in guaranteeing funds for ecological environment remediation and trying to connect the bankruptcy proceedings to the handling of ecological and environmental problems under judicial supervision.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

"Opinions on Several Issues concerning the Implementation of the Circular of the State Council on Further Promoting Employment and Re-Employment" is a set of guidelines jointly promulgated by the Ministry of Human Resources and Social Security (former name: the Ministry of Labour and Social Security) and several ministries of the State Council in 2006. The guidelines require that all relevant authorities shall, according to their respective duties, offer guidance to debtors entering insolvency proceedings, supervise the implementation of the plan for the settlement of employees and, jointly with relevant debtors, offer guidance and training for the employees who have to find another jobs on the market, so as to help the employees understand the policies relating to re-employment, the possible solution to difficulties and where to get help.

In May 2016, the All-China Federation of Trade Unions (ACFTU) issued "Implementation Opinions on Further Doing a Good Job in Poverty Relief for Staff and Workers", which clarifies that trade / labour union organisations shall cooperate with local governments to properly address employee resettlement and social security issues in the merger and bankruptcy reorganisation / liquidation of enterprises, especially in coal and steel production industries that have gone through mass reduction of overcapacity in the recent decades.[29]

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[29] Implementation Opinions on Further Doing a Good Job in Poverty Relief for Staff and Workers, Part 3.

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

Pursuant to section 24(3) of the EBL, any liquidation group, law firm, accounting firm, bankruptcy liquidation firm or other social institution or individual shall not serve as an administrator if the entity:

- has received criminal punishment for intentional crimes;
- has had its professional certificate revoked;
- has an interest in the case; or
- has been found incompetent by the court for other reasons.

The SPC has formulated the "Provisions on the Appointment of Administrators in the Trial of Insolvency Cases" (PAATIC), which prescribes guidelines in relation to avoiding conflicts of interest for restructuring professionals. Key points from the guidelines are as follows:

- If a professional institution satisfies of the following circumstances that may affect the faithful performance of its duties as an administrator, it may be deemed to have interest in the case:
  - holding outstanding rights and claims against the debtor or creditor;
  - having provided long-term services to the debtor within three years before commencement of the proceeding;
  - acting as the controlling shareholder or actual controller of the debtor or creditor at the time being or within three years before commencement of the proceeding; or
  - acting as financial and / or legal counsel of the debtor or creditor at the time being or within three years before commencement of the proceeding.[30]
- If a member of the professional institution satisfies any of the following circumstances that may affect the faithful performance of his or her duties as an administrator, he or she may be deemed to have interest in the case:
  - the circumstances specified in section 23 of PAATIC as stated above;
  - acting as a director, supervisor or senior manager of the debtor or creditor at the time being or within three years before commencement of the proceeding; or
  - having a conjugal relationship, blood relationship in the direct line, next of kinship or relationship by marriage with the controlling shareholder, director, supervisor or senior management of the debtor or creditor.[31]

There are no industry guidelines or soft law frameworks to assist restructuring professionals to avoid a conflict of interest in performing their duties specifically, because they have passed the conflict check already by going through the court's appointment procedures.

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

In 2021, the People's Bank of China (PBC) launched two new structural monetary policy instruments to encourage capital to invest more in green and low-carbon areas. One is the Carbon Emission Reduction Supporting Tool, which supports the development of three key

[30] PAATIC, s 23.
[31] *Idem*, s 24.

carbon reduction areas: clean energy, energy conservation and carbon emission reduction technology. The other is a special refinancing loan to support the clean and efficient use of coal, supporting seven areas such as large-scale clean production of coal and the use of clean combustion technologies.

For commercial bank loans that meet certain requirements, the PBC will provide low-cost financial support at an interest rate of 1.75%, which is the lowest rate the PBC can offer. By March 2022, financial institutions had issued loans under these two policies in the amount of RMB 244.2 billion, of which carbon emission reduction loans led to an annual reduction of 47.86 million tons of carbon dioxide equivalent.[32]

By 2021, Chinese market players had issued labelled green bonds at the amount of US $109.5 billion (RMB 706.3 billion) in both domestic and overseas markets, including US $68.2 billion (RMB 44.01 billion) that was issued in line with the Climate Bond Initiative's definition, representing an increase of 186% on a year-over-year basis. China is the second largest green bonds market in the world in terms of both cumulative and annual amount of issuance according to the Climate Bonds Initiative.[33]

At present, ESG disclosure by financial institutions has become a focus of policy making and market attention. Meanwhile, the catalogue of projects supported by green bonds has been upgraded, unifying market standards of the national green bond issuance.

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

The China Banking and Insurance Regulatory Commission (CBIRC) issued the "Green Finance Guidelines for the Banking and Insurance Industry" on 1 June 2022, requesting financial institutions to promote green finance at a strategic level and increase their support for the green, low-carbon and circular economy. The key points include:

- establishing policy mechanisms to enhance the capacity in supporting green and low-carbon transition;[34]
- strengthening the management of green investment and financing processes;[35]
- strengthening internal control and risk management by incorporating ESG requirements into management processes and comprehensive risk management systems as well as enhancing ESG disclosure;[36] and
- strengthening the regulation on green financing in banking and insurance industries while granting them a one year transition period for financial institutions to establish necessary policies, processes and mechanisms for regulation purposes.[37]

The steps taken by Chinese financial institutions in areas relating to green and low-carbon financing are at a primary stage. However, according to public information disclosed, municipal banks such as the Industrial Bank,[38] Bank of Jiangsu,[39] Bank of Huzhou,[40] Chongqing Rural

32 China ranks first in the world in terms of green loan stock size (http://www.gov.cn/xinwen/2022-03/08/content_5677832.htm).
33 Climate Bonds, China Green Bond Market Report 2021 (https://www.climatebonds.net/files/reports/cbi_china_sotm_2021_0.pdf).
34 Green Finance Guidelines for the Banking and Insurance Industry, Part 3.
35 *Idem*, Part 4.
36 *Idem*, Part 5.
37 *Idem*, s 35.
38 The Industrial Bank, CRS Report (https://www.cib.com.cn/cn/aboutCIB/social/report/equator.html).
39 Bank of Jiangsu and Bank of Jiangsu have adopted the Equator Principles (http://www.jsbchina.cn/CN/gsyw/cgsyw/gsywzx/13660.html).
40 Bank of Huzhou, Social Responsibility Report 2021. (http://www.hzccb.com/portal/zh_CN/upload/Attachment/20220428145942898.pdf).

Commercial Bank,[41] Mianyang City Commercial Bank,[42] Bank of Guizhou[43] and Bank of Chongqing[44] have adopted the Equator Principles already.

### 5.3 Promoting ESG by the central bank and regulators

The promotion of ESG in financing by these entities is outlined above.

Additionally, more documents are being issued at various levels to improve financial awareness of environmental protection and market entities' contributions to social responsibilities. In particular:

- in 2020, the Ministry of Ecology and Environment, together with the NDRC, the Central Bank, the CBIRC and the China Securities Regulatory Commission (CSRC), jointly issued the "Guidance on Promoting Investment and Financing to Address Climate Change", putting forward the task of addressing climate change via investment and financing at the national level. The guide constructs a set of investment and financing mechanisms that would be compatible with the purpose of carbon peaking and carbon neutrality; and

- in 2021, the Central Bank also issued "Guidelines on Environmental Information Disclosure for Financial Institutions", encouraging commercial banks, capital management institutions, trust companies and insurance companies to disclose environmental information to the public at least once a year.

The CSRC also published several amendments and guidelines to encourage public companies to prepare a social responsibility report and disclose in their periodic reports the "measures taken to reduce their carbon emissions and their effects" as well as the "consolidation and expansion of the results of poverty reduction and rural revitalisation".

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41 The official website of the Chongqing Rural Commercial Bank, https://www.cqrcb.com/cqrcb/aboutus/whjj/index.html.

42 Mianyang City Commercial Bank, Social Responsibility Report 2021 (https://www.mycc-bank.com/data/tosend/resource/upload/%E7%BB%B5%E9%98%B3%E5%B8%82%E5%95%86%E4%B8%9A%E9%93%B6%E8%A1%8C2021%E5%B9%B4%E5%BA%A6%E7%A4%BE%E4%BC%9A%E8%B4%A3%E4%BB%BB%E6%8A%A5%E5%91%8A.pdf).

43 Bank of Guizhou, Annual Report of 2021(https://www.bgzchina.com/Attachments/2022/04/2021%E5%B9%B4%E5%BA%A6%E6%8A%A5%E5%91%8A.pdf).

44 Bank of Chongqing, Annual Report (A Shares) of 2021 (http://www.cqcbank.com/data/tosend/resource/upload/20220331/2021%E5%B9%B4%E5%BA%A6%E6%8A%A5%E5%91%8A%EF%BC%88A%E8%82%A1%EF%BC%89.pdf).

# POLAND

## 1. General overview of the restructuring regime

### 1.1 Formal restructuring procedures

The court procedures for restructuring debts in Poland are regulated in the Restructuring Law of 15 May 2015, as amended.[1] The court procedures that happen strictly in court are:

- expedited arrangement proceedings (Polish: *przyspieszone postępowanie układowe*);
- arrangement proceedings (Polish: *postępowanie układowe*); and
- deep reform restructuring proceedings (Polish: *postępowanie sanacyjne*).

All of the above are court-supervised procedures which enable a company to enter a binding arrangement with its creditors to modify or adjust their respective rights and entitlements. Once an arrangement is approved by the court, it becomes binding on all creditors covered by the arrangement, including dissenting creditors.

The key substantive requirements for an arrangement are:

- the arrangement must be approved by a majority in number representing two thirds in value of the creditors (or each class of creditors), provided that dissenting classes of creditors can be crammed down if the creditors voting in favour hold at least two thirds of debt in the aggregate and the dissenting classes will not be satisfied to a lesser degree than in case of a liquidating insolvency; and
- the arrangement must be approved by the court.[2]

Arrangement proposals may be made either by the existing management, creditors' council, court supervisor, court administrator or creditors holding more than 30% of the total debt (with certain exclusions).

All of the court proceedings give the company a protective moratorium to provide it with breathing space to formulate and negotiate the terms of the restructuring. The scope and timeline of the moratorium differs depending on the type of proceeding. The company remains under the supervision of the court.

The deep reform restructuring proceeding is clearly the one where the company may undergo the more significant reorganisation measures. One feature of the regime which is not present in other proceedings is that a deep reform restructuring administrator has the power to avoid unprofitable contracts, which have not yet been performed in full or in part before the opening of the proceedings. Exercise of the avoidance tool has the effect of putting an end to the rights, interests and liabilities of the company in relation to the avoided contract upon the approval of the judge-commissioner. However, interested parties may apply to challenge the decision of the judge-commissioner if the restructuring administrator misinterpreted the significance of avoidance for the deep-reform restructuring proceedings or did not consider the important interests of the counterparty.

The process of implementing an arrangement differs depending on the type of restructuring proceeding.

In particular:

- expedited arrangement proceedings can be conducted if the amount of contentious claims does not exceed 15% of the amount of all claims entitled to vote on the arrangement. An arrangement vote can be held once the list of claims has been prepared and approved in a simplified manner;

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1 Unified test published on 23 July 2021, Journal of Laws in 2022, item 1588.

2 Restructuring Law, art 19.

- arrangement proceedings can be conducted if the amount of contentious claims exceeds 15% of the amount of all claims entitled to vote on the arrangement. An arrangement vote can be held once the list of claims has been prepared and approved; and

- deep reform restructuring proceedings allow the debtor to implement reorganisation measures and organise an arrangement vote by the creditors after the list of claims has been prepared and approved.

The dynamics of restructuring measures are importantly different in the above proceedings. While a restructuring plan is shared with creditors for the purpose of preparing for the arrangement vote in expedited arrangement proceedings and in arrangement proceedings as a justification of arrangement proposals, a creditor’s vote in deep-reform restructuring proceedings takes into account the results of the implementation of reorganisation measures envisaged in the restructuring plan previously approved by the judge-commissioner and adopted by the deep-reform restructuring administrator.

If the requisite majority of creditors approve the arrangement, the company then applies for the court’s approval of the arrangement (approval stage). The court will refuse to approve the arrangement if:

- it violates the law (in particular if the arrangement envisages the grant of unlawful public aid);

- it is obvious that the arrangement will not be performed, provided that such obviousness is presumed in case the debtor fails to perform its obligations after the commencement date; or

- in case of expedited arrangement proceedings, the amount of contentious claims exceeds 15% of all claims entitled to vote on the arrangement.

The court may refuse to approve the arrangement in case its terms grossly harm the creditors who voted against the arrangement and raised objections.[3]

The arrangement covers:

- personal claims that came to existence before the commencement date (subject to statutory exceptions);

- interest accruing after the commencement date;

- contingent claims for as long as the condition is satisfied during the performance of the arrangement; and

- executory contracts are covered to the extent not performed in full or in part prior to the commencement date and only if the debtor's counterparty rendered its performance prior to the commencement date and did not receive the debtor's reciprocal performance.

Various categories of claims are excluded from the arrangement, most notably employees’ claims, claims of the Fund of Guaranteed Employment Claims and claims for the discontinuation of breaches. While secured claims are in principle excluded, secured creditors may not opt out of the arrangement in case the debtor came up with arrangement proposals that envisage full satisfaction within the deadlines specified in the arrangement or satisfaction not lower than from the secured creditor's collateral.[4]

Debtors’ claims may in principle be restructured in any manner allowed by law, in particular by way of debt rescheduling, deferral into instalments, debt reduction, debt for equity swap and / or varying the terms of the collateral.

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3 *Idem*, art 165.
4 *Idem*, art 151.2a.

The rights of certain creditors may not be impaired beyond the levels guaranteed by the Restructuring Law. In particular, the terms of the restructuring of employment-related claims (assuming an employee / employees consented to the coverage of their claims by an arrangement) may not fall foul of the laws regulating minimum wages. In turn, the restructuring of social security dues, contributions to the Employment Fund of Guaranteed Employee Benefits and the Bridge Retirement Fund, social security and medicare contributions of the debtor and other dues of the debtor towards the Social Security Office may only be rescheduled or put into instalments with the exclusion of the other restructuring modes.

As discussed previously, an arrangement may be approved even if a voting majority is not reached in certain voting classes, provided creditors holding at least two thirds of all claims voted for the arrangement and the dissenting creditors will be satisfied to a degree not less than in case of liquidating insolvency. This simple and general approach is likely to be elevated to much more sophisticated cross- class cram down provisions imported from the European Preventive Restructuring Directive.[5]

## 1.2 Hybrid restructurings

The Restructuring Law introduced in 2016 a separate procedure called the procedure for the approval of arrangement (Polish: *postępowanie o zatwierdzenie układu*), which then held certain characteristic features:

- the debtor could conduct the proceedings on its own, but assisted by a court supervisor on the basis of an agreement concluded with him / her;
- the debtor could itself set the commencement / arrangement / date prior to which the debts would have been subject to an arrangement;
- the debtor, assisted by the court supervisor, would prepare arrangement proposals and seek creditors' votes on the arrangement;
- the debtor would not enjoy a moratorium and hence a standstill arrangement could have been key to the process; and
- once voted through by the creditors, the arrangement would have been subject to a review and approval by the restructuring court (court stage).[6]

The above proceedings were modified by way of fast-track legislation at the time of COVID-19 to become the so-called simplified restructuring proceeding. A few important elements were then added:

- a moratorium for the benefit of the debtor for the four-month length of proceedings;
- an increased role for the court supervisor, who would need to approve the debtor's actions outside the ordinary course of business; and
- a ban on termination of certain agreements key for the debtor's business that was imported from other restructuring proceedings.

The simplified restructuring proceeding turned out to be an extremely efficient tool at the time of COVID-19 that facilitated a quick restructuring of various Polish businesses affected by the pandemic. While the simplified restructuring proceeding was introduced by a special statute, the Restructuring Law was amended in late 2021, whereby the procedure for approval of an arrangement was allowed to be conducted in two ways:

- close to the original 2016 regulation and without a moratorium; and

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5 See point 21 of the Governmental Bill dated 24 May 2022 on amendments to Restructuring Law and Insolvency Law.

6 Restructuring Law, art 210 et seq.

- patterned after the simplified restructuring proceeding and with a moratorium.[7]

It is more likely than not that the latter will be resorted to more often, and arguably more often than the other types of restructuring proceedings going forward.

### 1.3 Informal restructuring procedures

Informal out of court restructurings are conducted primarily on a consensual basis and are not specifically governed by any legislation. Implementation of a standstill to allow for the preparation and analysis of detailed information and accompanying discussions and negotiations may be an important element of an informal restructuring. There was an initiative taken in the past jointly by the Polish Banking Association and the Polish Association of Restructuring Professionals aimed at elaborating a model standstill agreement for the Polish market. While a representative group of banks participated in this effort (completed in 2015), there has not been subsequent research and / or findings on how the model agreement has been practically used thereafter.

## 2. Restructuring of ESG-related Liabilities

### 2.1 Environmental (E): restructuring environmental liabilities

Generally, environmental monetary liabilities can be restructured pursuant to an arrangement in the same way as ordinary liabilities of a company. As mentioned above, any monetary claims against a company created before the opening of the restructuring proceedings are covered by the arrangement, including contingent claims. There are no special restrictions or conditions that apply when restructuring environmental monetary liabilities. Thus, any environmental fines imposed on the debtor prior to the opening of restructuring proceedings (or the date of arrangement in proceedings for approval of the arrangement) will be subject to the arrangement and, if approved, will be satisfied in accordance with the arrangement.

The issue is more complex when it comes to non-monetary environmental claims, such as those resulting from an administrative decision imposing on the debtor an obligation to conduct remediation of the land or cease infringement.

As a rule, the arrangement includes monetary and non-monetary claims. The latter are not converted into monetary claims at the opening of the restructuring proceedings, but only for the purpose of voting on the arrangement are placed on the list of claims in an amount corresponding to their value. Thus, the arrangement proposals should respond to the specifics of these liabilities, either by appropriately modifying the manner in which they are to be discharged, or by providing for satisfaction by payment of a sum of money specified in the arrangement. Further, the Restructuring Law provides that if a creditor has objected to the restructuring of its claim as a non-monetary claim, or if restructuring of a non-monetary claim is not possible, the claim is transformed into a monetary claim. If the creditor does not make any objections, no conversion will occur, and the claim will be satisfied as a non-cash claim in the manner specified in the arrangement.

Therefore, environmental liabilities as non-monetary claims will be subject to the arrangement and will be satisfied in accordance with it. However, it seems that any modification of the debtor's environmental liabilities will result in the court's refusal to approve the arrangement on the grounds that it violates the law. In other words, on the one hand, the debtor's environmental obligations will be covered by the arrangement, but on the other hand, they will not be capable of being modified by the arrangement, since the debtor will have to perform them in accordance with the obligation imposed on it by an administrative authority.

However, not every non-monetary (including environmental) claim will be subject to the arrangement. A claim for non-infringement of rights cannot be subject to an arrangement. This is because the nature of these rights under which a creditor can claim protection are inalienable rights or are inextricably linked to property held by the debtor such as a claim for non-infringement of a boundary or gas emissions.

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[7] *Idem*, art 226 a-h.

### 2.1.1 *Types of environmental liabilities*

By way of background, environmental liabilities under Polish law can encompass:

- civil claims such as:
  - tort claims;[8] and
  - claims under contracts; and
- statutory liabilities such as:
  - fines. For example, fines may be imposed for various statutory offences, such as the failure to conduct tests of soil and land contamination required to be performed by a decision and / or failure to store the results of the tests for the required period of five years; failure to notify the regional director of environmental protection of historical surface pollution; carrying out remediation of historical surface pollution not in accordance with the established remediation plan or, despite an obligation, not submitting a draft remediation plan to the regional director of environmental protection; using soil for earthworks if the permissible content of the risk-causing substance is exceeded; and violations of the terms of the decision on permissible noise levels; and
  - remediation / clean-up costs. For example, under the Environmental Law,[9] responsible for historical land contamination (i.e. contamination of the land surface occurred before 30 April 2007, or that resulted from activities that were completed before 30 April 2007) is the owner of the land in question, and it is the owner who is obliged to carry out remediation, unless the owner is able to identify another entity that is the perpetrator of the contamination. In that case, liability for the damage then falls on the perpetrator of the historical pollution. The legislator also lists cases that relieve the landowner from the burden of the remediation activities. The obligation to carry out remediation is then assumed by the Regional Director of Environmental Protection.

There is generally no distinction as to how the various types of monetary environmental liabilities are treated pursuant to an arrangement. Statutory monetary liabilities are covered by the arrangement (if they were imposed before opening of the restructuring proceedings) and can be reduced under the arrangement (with the exception of social security claims). Non-monetary environmental liabilities depending on their nature are also covered by the arrangement, but because it would be contrary to law to modify them, the debtor's obligations in this regard cannot be reduced by an arrangement. As mentioned above, claims for restitution of property and claims for discontinuation of breaches of rights cannot be covered by an arrangement.

### 2.1.2 *Priority given to environmental liabilities*

Under Polish law, certain liabilities may be given favourable treatment under a proposed arrangement if the liabilities would have priority in bankruptcy liquidation. Claims secured by a mortgage or pledge may be included in the arrangement only if the arrangement proposals provide for their full satisfaction within the period specified in the arrangement. This means that environmental monetary claims (e.g. fines or other administrative fees) whose payment has been secured on the debtor's assets will be included in the arrangement only if the arrangement proposals provide for their full satisfaction, or with the consent of the creditor (i.e. the state treasury or municipality on behalf of which the authority acts).[10]

As mentioned above, non-monetary environmental claims covered by the arrangement cannot be reduced.

[8] Polish Code, arts 415-449 – Journal of Laws of 18 May 1964, No. 16, Item 93, as amended.
[9] Law on the Protection of the Environment of 27 April 2001 – Journal of Laws 2001 No. 62, Item 627, as amended.
[10] Restructuring Law, art 151.2.

### 2.2 Social (S): restructuring health or safety-related liabilities

Similar to the restructuring of environmental liabilities, health or safety-related liabilities can be restructured pursuant to an arrangement in the same way as ordinary liabilities of a company. As mentioned above, any monetary claims against a company that came to existence before the opening of proceedings are covered by the arrangement, including contingent claims. In principle, there are no special restrictions or conditions that apply when restructuring health or safety-related liabilities. However, the following claims are specifically excluded from the arrangement.

- alimony claims;
- illness benefit work disability benefits, disablement pensions and death benefit pensions; and
- claims for the conversion of rights under an annuity agreement into a life pension.[11]

In addition, claims with respect to the contributions towards the debtor's health insurance and other obligations towards the Social Security Fund may only be rescheduled or deferred.

#### *2.2.1 Types of health and safety-related liabilities*

For background, health or safety-related liabilities under Polish law can encompass:

- civil claims such as torts claims (including claims for punitive damages)[12] and claims under contracts; and
- statutory liabilities such as:
  - product liability. Under Polish law, not only the producer but also other entities dealing with a dangerous product may be liable;[13] and
  - liabilities under compliance orders, for example under a decision issued by the State Labour Inspection requiring that an employer should cease and desist certain activities in case an infringement results in a direct life or health hazard to the employees or other persons performing works.[14]

#### *2.2.2 Priority given to health and safety-related liabilities*

There is generally no distinction as to how the various types of monetary health or safety-related liabilities are treated pursuant to an arrangement. Statutory monetary liabilities are covered by the arrangement (if they arose before opening of the restructuring proceedings) and can be reduced under the arrangement, with the exception of social security claims. Non-monetary liabilities, depending on their nature, are in principle also covered by the arrangement but because it would be contrary to law to modify them, the debtor's obligations in this regard cannot be converted into monetary claims and reduced by an arrangement.

As identified, there are certain categories of claims that are specifically excluded from an arrangement. Yet, in case certain health or safety-related claims were secured on the debtor's assets, they could only be covered by the arrangement if the arrangement proposals provided for their full satisfaction or with the consent of creditor.

### 2.3 Governance (G): third party releases in favour of directors and officers of the company

Polish restructuring law treats shareholders and directors of the debtor as well as their affiliates as suspected parties from the perspective of an arrangement vote. Such parties are in principle

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11 Idem, art 151.1.
12 Polish Civil Code, art 445.
13 *Idem*, art 449.
14 Article 11 of the Law on the State Labour Inspection of 13 April 2007 (unified text – Journal of Laws of 1 August 2022 item 1614).

deprived of rights to vote on an arrangement.[15] There is no legal basis in the Restructuring Law to link an arrangement and / or its outcome to third party releases in favour of directors and officers of a company. Such releases would not be inconceivable though in connection with out of court or hybrid restructurings.

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

#### *3.1.1 Approving a restructuring plan*

There is no requirement for an arrangement to be approved by environmental protection authorities or environmental advocacy groups. An arrangement only needs to be voted through by the creditors and approved by the court.

#### *3.1.2 Discretion to consider wider public interest concerns*

There is no case law in Poland concerning the extent to which the court may consider environmental issues in deciding whether to approve an arrangement. However, it is conceivable that a restructuring court would decline to approve an arrangement based on a restructuring plan that ignores environmental concerns on the basis that an arrangement violates the law.

#### *3.1.3 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

There are no statutory provisions which grant environmental protection authorities or environmental advocacy groups standing to air their views or concerns in a restructuring.

### 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

#### *3.2.1 Approving a restructuring plan*

There is no requirement for an arrangement to be approved by labour authorities, unions or employee / worker advocacy groups. An arrangement only needs to be voted through by the creditors and approved by the court.

#### *3.2.2 Discretion to consider wider public interest concerns*

There is no case law in Poland concerning the extent to which the court may consider social issues in deciding whether to approve an arrangement.

#### *3.2.3 Protection of employee rights*

Under the Restructuring Law, special rules apply when restructuring employees' liabilities. These liabilities may be covered by an arrangement only if the employees give their unconditional and irrevocable consent.[16] However, proposals for the restructuring of labour liabilities may not provide for such a reduction that would cause the salary received by the employees to be lower than the statutory minimum wage, even if the employees agree to this.[17] Employees' liabilities in restructuring proceedings should be satisfied on an ongoing basis – hence, employees who decide to take part in the rescue of the debtor's enterprise do so primarily in order to keep their jobs.

If the restructuring requires redundancies, rules governing collective redundancies apply provided the total number of employees is at least 20 and within 30 days at least:

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15 Restructuring Law, art 116.
16 *Idem*, art 151.2.
17 *Idem*, art 163.1.

- 10 employees are dismissed in companies hiring 20-99 employees;
- 10% of the workforce is dismissed in companies with less than 299 employees; or
- 30 employees are dismissed in larger companies with at least 300 employees.

Collective redundancies must be consulted on with trade unions or employees' representatives and notified to the labour office. The purpose of the consultations is the possibility of avoiding or reducing collective redundancies and measures to support affected employees, including, in particular, opportunities for retraining or obtaining alternative employment.

Moreover, if it is necessary to select employees for dismissal from among those employed in the same or similar jobs then clear, objective, non-discriminatory and fair selection criteria must be determined and applied. Essential selection criteria include the employee's suitability for work, qualifications and professional skills, professional experience, seniority and availability. Social criteria can be applied as subsidiary criteria, for example family status (especially single parenting), disability, having other sources of income or the ease of finding new employment. The selection criteria cannot discriminate against employees, particularly on grounds of gender, age, disability, race, religion, nationality, political opinion, union membership, ethnic origin, religion or sexual orientation.

If it is intended to make at least 50 employees redundant within a period of three months, an outplacement procedure (so-called monitored redundancies) should be observed. The scope and forms of assistance for the dismissed employees, concerning in particular job placement, vocational counselling or training, should be agreed with the relevant labour office. Moreover, in the case of monitored redundancies, measures should be taken that are aimed at providing the dismissed employees with labour market services in a form of a structured programme and may fund a training allowance at the request of the employee.

The opening of deep reform restructuring proceedings affects employment relationships and has, with regard to the rights and obligations of employees and employers, the same effects as the declaration of bankruptcy, save that the rights of the bankruptcy trustee are exercised by the administrator. If in the proceedings headcount is expected to be reduced using the aforementioned administrator’s rights, a restructuring plan shall additionally specify the rules for dismissing employees, in particular the number of employees to be dismissed, the period in which they are to be dismissed and the proposed criteria of dismissing employees. Those rules should be objective and reasonable in economic terms.[18]

## 2.2 Governance (G): board / management conflicts addressed in a restructuring

Board / management conflicts are addressed in a restructuring in several ways. First, directors of the debtor as well as directors of affiliates of the debtor are excluded from an arrangement vote. Second, in two court proceedings and in one hybrid proceeding, a court supervisor is mandatorily appointed. The role of the supervisor is to monitor the debtor's management and approve of transactions outside the ordinary course of business. Third, in the case of deep reform restructuring proceedings, the debtor's own management is in principle (subject to certain exceptions) removed and the managerial duties are performed by a court-appointed administrator. Yet, in each court restructuring proceeding, the court may remove the managerial powers of the debtor and appoint an administrator if:

- the debtor breached the law (deliberately or not) in the course of the exercise of management which resulted in a harm to creditors or a risk of such harm in the future;
- it is clear that how the management is performed does not guarantee the implementation of the arrangement or a curator was appointed for the debtor (in case the debtor's management has lost legal capacity to bind or represent the debtor); or

[18] *Idem*, art 314.

- the debtor does not follow the instructions of the judge-commissioner or court-supervisor – in particular, it has not filed legally-compliant arrangement proposals by the deadline specified by the judge-commissioner.[19]

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

We have not identified any industry guidelines and / or best practices prescribed for the protection of the environment in a restructuring.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

We have not identified any industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring.

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

The Code of Ethics of the Nationwide Chamber of Restructuring Advisors prescribes general guidelines as to how the profession of a restructuring advisor should be performed.[20] In particular, when performing restructuring roles, a restructuring advisor must abide by the principles of professionalism, independence, honesty and due diligence.

Furthermore, the restructuring advisor is bound to report to the judge that he / she is unable to perform duties in a relevant proceeding if that person:

- is a creditor or debtor of the principal debtor;
- is or was a spouse of the principal debtor or a relative of the principal debtor or a creditor of the principal debtor;
- has adopted the debtor or was adopted by the debtor or a spouse to such adopted person or was in a factual relationship with the debtor running the same household with him / her;
- was an employee of the debtor based on an employment relationship or performed work or services for the debtor on the basis of a different legal relationship, save for the restructuring advisory services referenced in the Law on the License of Restructuring Advisors;
- was a member of governing body of the debtor, procurator or attorney-in-fact of the debtor or is or was within two years prior to the filing of restructuring motion a partner or shareholder of the debtor holding shares or stock exceeding 5% of the equity of the debtor or creditor; or
- was a partnership or company affiliated with the debtor or was a member of a governing body, procurator or attorney-in-fact of such a partnership or company or within two years prior to the filing of the restructuring motion was a partner or shareholder of such entity holding shares or stock exceeding 5% of the equity of the debtor's affiliate.[21]

In addition, a restructuring advisor is not allowed to withhold the performance of his / her / its duties in a proceeding due to the non-payment of renumeration.[22]

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19 *Idem*, art 239.
20 Code of Ethics of Restructuring Advisor, adopted unanimously by the Nationwide Assembly of Delegates from the Regional Chambers of Trustees held on 20 June 2015 in Łódź.
21 *Idem*, s 11.
22 *Ibid*.

In terms of hard law, the Restructuring Law itself contains rules aimed at the avoidance of conflicts of interest. In particular, under article 24.2 of the Restructuring Law, a restructuring advisor cannot be appointed as a supervisor or an administrator in the circumstances referred to in section 11 of the Code of Ethics (see above). In addition, a restructuring advisor who performed the role of a supervisor cannot be appointed an administrator in a proceeding concerning the same debtor. Prior to undertaking the first action in front of the court or judge-commissioner, the supervisor and / or administrator must file a statement confirming the non-existence of circumstances excluding their appointment. Finally, a supervisor or administrator may be removed or replaced by the court on various grounds specified in the Restructuring Law. While none of those refers specifically to a conflict of interest situation, this situation could on its merits be a reason for the replacement, removal or lack of appointment.

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

Financiers in Poland have paid growing attention to ESG issues, and the availability of financing and its cost tends to depend on actions taken and goals set in the field of sustainable development, which means the company's investments are assessed in terms of environmental, social and corporate management. The first financing project in Poland with such an evaluation mechanism took place in 2019, where a consortium of banks granted a loan to a Polish company from the energy sector where an external rating agency evaluated ESG factors in relation to the borrower.

In turn, ESG-linked bonds are not yet common in Poland and there seem to have been only two remarkable projects in Poland in which two state-controlled companies – Tauron SA and Orlen SA – issued sustainability linked bonds in Poland.[23]

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

Polish financial institutions are committed to the use of ESG-linked financial instruments. The sources of this commitment are manifold, but the main ones are the society and clients of financial institutions, who expect that their funds are invested in businesses preventing climate change and that seek to achieve the 2030 Agenda's Sustainable Development Goals. In addition, the European Union adopted a 2050 climate neutrality target and the European Green Deal, where EUR 1 trillion needs to be raised between 2021-2027, including funds from private sources.[24]

Finally, financial institutions have changed their strategies themselves, implementing requirements imposed by financial regulators.

### 5.3 Promoting ESG by the central bank and regulators

Poland is subject to various EU laws in the area of ESG, which are either directly applicable or have been or will be implemented into the domestic law. The most relevant of those are:

- Directive 2014/95 EU of the European Parliament and of the Council of 22 October 2014 amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups;
- Directive 2011/92/EU of the European Parliament and he Council of 13 December 2011 on the assessment of the effects of certain public and private projects on the environment;
- Regulation (EU) 2020/852 of the European Parliament and of the Council of 18 June 2020 on the establishment of a framework to facilitate sustainable investment and amending Regulation (EU) 2019/2088;

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23 See Global Legal Group: International Comparative Legal Guide: Environmental, Social & Governance Law 2023, Chapter on Poland, 7.

24 *Ibid*.

- Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosure in the financial service sector (SFRD);
- Regulatory technical standards constituting an implementing act of SFRD and adopted by the European Commission on 6 April 2022; and
- Corporate Sustainability Reporting Directive (CSRD) – 2022/2464/EU that came into force on 5 January 2023.

The last regulation aims to ensure that a broader set of large companies as well as listed SMEs will be required to report on sustainability issues and investors and other stakeholders will have access to the information they need to assess investment risks arising from climate change and other sustainability issues.

Various laws in Poland, including energy, environment protection, water, waste and trade unions laws, as well as the labour code and commercial companies code, have been or will be amended to implement EU directives.

Additionally, the Polish Insurance Chamber, Foundation for Reporting Standards Association of Stock Market Issuers and Polish Banking Association has prepared the Set of Main ESG Indicators According to the SFRD, which are in essence reporting guidelines for Polish businesses.

Finally, according to the statement of the President of the National Bank of Poland, the Bank's investment in green bonds and sustainability finance reached nearly EUR 600 million as of early 2022.

# RUSSIA

# 1. General overview of the restructuring regime[1]

## 1.1 Formal restructuring procedures

The three main rehabilitation procedures in Russia are financial rehabilitation, external administration and amicable settlement.[2] Another option, available only for individuals, is debt restructuring.[3]

Usually the application of the rehabilitation procedures takes place only after the completion of the initial stage of corporate insolvency (the supervision stage), during which the court-appointed interim manager assesses the debtor's financial standing and the first creditors' meeting decides whether to liquidate the company or introduce the financial rehabilitation stages.[4]

Only unsecured creditors and tax authorities are entitled to vote for the approval of the rehabilitation plan in the course of financial rehabilitation and external administration.[5] If a secured creditor waives the right to force execution by means of foreclosure, that creditor is also entitled to vote.[6]

In any case, secured creditors are entitled to vote in the course of debt reschedulings of individuals and amicable settlements.[7]

Generally, there are no restrictions on the types of debts, liabilities or claims that can be restructured under the available rehabilitation procedures.

Decisions to initiate rehabilitation procedures are subject to the approval of the court supervising the insolvency case.[8]

### *1.1.1 Financial rehabilitation*

This procedure may be introduced if the creditors and the court believe there is a reasonable chance of the debtor avoiding insolvency liquidation.

During supervision, the debtor company (based on a decision of its shareholders), or third persons in agreement with the debtor, may request the creditors present at the first creditors' meeting to sanction the introduction of financial rehabilitation. If the creditors vote in favor, the court will resolve to commence the financial rehabilitation. However, the creditors may vote against the introduction of financial rehabilitation and instead opt to proceed to external administration or liquidation.[9]

During this stage, the debtor's management remains in place and business operations continue.[10]

At the same time, the Insolvency Law sets forth certain limitations that need to be taken into account. First, the temporary administrator's approval is required for: (i) any transaction involving the company's assets with a value of 5% or more of the book value of the debtor's assets as of the date of commencing supervision; and (ii) granting / receiving loans, assignment of rights, transferring debts, granting guarantees / suretyships and putting the debtor's assets into trust.[11]

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1 In this chapter, the restructuring procedures set forth by the Insolvency Law are collectively referred to as rehabilitation procedures. This is because in the Russian jurisdiction, the term "restructuring" (реорганизация) applies to the corporate procedure of a company's conversion (e.g. when one company is merged with another, or is integrated therein).

2 Articles 76, 93, 150 of the Federal Law No. 127-FZ dated 26 October 2002 "On Insolvency (Bankruptcy)" (Insolvency Law).

3 Insolvency Law, art 213.2.

4 *Idem*, art 73.

5 *Idem*, arts 12 and 15.

6 *Idem*, art 18.1(3).

7 *Idem*, arts 150, 213.2.

8 *Idem*, arts 80, 93, 150, 213.2.

9 *Idem*, arts 12, 15.

10 *Idem*, art 82.

11 *Idem*, art 81.

Second, the debtor (its management) is prohibited from acquiring shares from its shareholders, issuing bonds or paying dividends, approving reorganisation or liquidation, establishing branches or representative offices or participating in joint ventures, associations and holding companies.[12]

The court introduces financial rehabilitation for the period (not exceeding two years) stated in the petition requesting the introduction of financial rehabilitation.[13] If the claims of all creditors are discharged in full before the end of the period established by the court, the debtor may petition the court for an early termination of financial rehabilitation and the bankruptcy proceedings in connection with the reinstatement of the debtor's solvency.[14]

At the financial rehabilitation stage, the debtor presents a plan for repaying the outstanding debts, which can envisage, among other things, writing off a certain part of the debts. The plan must be approved by the court.[15]

If the debtor succeeds in repaying its debts, the insolvency proceedings are terminated.[16] In our experience, this stage can be effective, especially if there is an investor seeking to acquire the distressed assets of the insolvent debtor.

### *1.1.2 External administration*

External administration has the same objective as financial rehabilitation: restoration of the debtor's solvency. The principal difference is that during this stage, the debtor's management is dismissed, and a court-appointed administrator manages the debtor according to an external administration plan, which is prepared by the administrator and approved by the creditors' meeting. External administration must be completed within 18 months, but in some instances this term may be extended.

During external administration, the administrator is entitled to refuse to execute certain transactions, which are then not fulfilled by the parties at all or in part, if the transactions impede the restoration of the debtor's solvency or if the debtor's execution of the transactions entails losses for the debtor (and if the transactions concluded by another entity under comparable circumstances would entail similar losses).[17]

### *1.1.3 Debt restructuring*

Debt restructuring is applied to individuals to repay their debts within three years. The debtor may initiate the procedure if it is contemplating insolvency, if it is unable to pay its debts and / or if it has insufficient property to pay.[18]

The starting point is the draft debt restructuring plan, which has to be prepared by either the debtor or a creditor. If no draft plan is presented within two months after the court's decision to initiate bankruptcy proceedings, the financial manager should propose the seizure of property.[19]

The plan is subject to approval by a simple majority at the first creditors' meeting. If the vote is in favour of the plan, the plan must be approved by the court. The court can enforce the restructuring plan even if it is not approved by the creditors' meeting, provided the court finds that the rescheduling will satisfy substantially more claims (at least 50% of registered claims) than the immediate seizure of property.[20]

12 *Ibid*.
13 *Idem*, art 88.
14 *Idem*, art 86.
15 *Idem*, art 88.
16 *Ibid*.
17 *Idem*, art 94.
18 *Idem*, art 213.1.
19 *Idem*, art 213.17.
20 *Idem*, art 213.17(4).

The Insolvency Law also sets forth the so-called "cram down" option, which enables the court to approve the restructuring plan regardless of the decision of the creditors' meeting.

The restructuring is terminated by virtue of a court decision if all claims have been satisfied. If not all claims are satisfied, the creditors may file a motion with the court to cancel the debt rescheduling plan no later than 14 days before the end of the period provided for repayment.[21]

#### 1.1.4 *Amicable settlement*

The creditors and the debtor company or an individual are entitled to enter into a settlement agreement at any stage of the insolvency proceedings.[22]

The amicable settlement is subject to court approval, on the condition that the following preferred creditors' claims have been fully repaid:[23]

- claims connected with bodily injuries and other injuries to health; and
- claims of employees regarding their salaries and severance payments and royalties to the authors of items of intellectual property.

Once a settlement agreement is concluded and the court approves it, the insolvency proceedings are terminated.[24]

### 1.2 Informal restructuring procedures

Out of court bankruptcy proceedings were introduced in September 2020 to allow individuals with minor outstanding debts to take advantage of a simplified bankruptcy process. The procedure is administered by government services centres (institutions providing day-to-day services to individuals).

Out of court bankruptcy is available to individuals with debts no lower than RUB 50,000 (approximately US $800) but not exceeding RUB 500,000 (approximately US $8,000). If the individual fulfils these criteria, the government services centre inputs information about the individual into the Unified Federal Register of Information on Bankruptcy.[25] This triggers the following consequences:[26]

- the individual is exempted from satisfying creditors' claims, except for claims not indicated in their application, and debts for alimony, compensation for moral damage and tort claims;
- the penalties, fines and interest under the obligations of the debtor do not accrue;
- the debtor is prohibited from taking new loans or acting as a surety; and
- the debtor must inform the government services centre about acquiring ownership of any property or other significant improvement in their financial status.

Out of court bankruptcy is terminated after six months from the time the information was included in the Unified Federal Register of Information on Bankruptcy. The debtor is discharged from the obligations indicated in the application.[27]

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21 *Idem*, art 213.22.
22 *Idem*, art 150(1).
23 *Idem*, art 158.
24 *Idem*, art 159.
25 *Idem*, art 223.2
26 *Idem*, art 223.4.
27 *Idem*, art 223.5.

## 2. Restructuring of ESG-related liabilities

### 2.1 Environmental (E): restructuring environmental liabilities

Generally, environmental liabilities can be restructured under all the rehabilitation procedures in the same way as ordinary liabilities of a company. There are no special restrictions or conditions that apply when restructuring environmental liabilities.

#### *2.1.1 Types of environmental liabilities*

Russian law provides for civil, administrative and criminal liability for environmental offences.

- Civil liability / compensation

  The Environmental Protection Law[28] provides for full compensation for damage, including lost profit, caused by pollution and / or contamination of the environment.[29] The amount to be compensated is calculated under statutory approved guidelines or, in their absence, should be equal to the amount of actual costs incurred in order to restore the polluted / damaged environment.[30]

  The Law also provides for an extended period of limitation (20 years) for claiming damages resulting from environmental pollution.[31]

  The owner of the property (or a long-term tenant being its primary user)[32] shall be deemed primarily responsible for its maintenance and clean-up, unless another responsible person is duly identified under the applicable rules (laws or contracts).[33]

  This obligation follows the property and applies regardless of whether the owner is actually responsible for the contamination, or whether the owner was aware of the contamination prior to purchasing the property.

  The Russian Land Code requires owners and tenants to perform certain land protection measures,[34] including eliminating the consequences of land contamination. If the actual polluter is identified, the owner / tenant may recover compensation from the polluter for the damages incurred (including decontamination costs). If the polluter is not identified, no compensation will be recovered.

- Administrative liability

  In addition to civil liability, contamination or other environmental damage may lead to administrative liability under the Russian Code of Administrative Offences.

  Depending on the circumstances, the scope of administrative penalties may take the form of: (i) fines that may be charged to the polluting entity and / or its officers; and (ii) suspension of the polluting entity's activities for a certain period.

  The scope of potential liability depends on the particular offence. For instance, the discharge of hazardous substances in the air without a special permit[35] may trigger:

  - a fine of up to RUB 250,000 (US $3,900) for the polluting entity;

28 Federal Law No. 7-FZ of 10 January 2002, "On Protection of the Natural Environment".
29 *Idem*, arts 77-78.
30 *Idem*, art 77(3).
31 *Idem*, art 78(3).
32 In many cases, owners of buildings or other capital constructions do not own the land beneath their property. They use the land on the basis of land lease agreements.
33 Russian Civil Code, art 210; Russian Land Code, art 13(2).
34 Russian Land Code, art 13.
35 Code of Administrative Offences, art 8.21

- a suspension of the polluting entity's activities for a period of up to 90 days; and / or
- a fine of up to RUB 50,000 (US $770) in respect of the polluting entities' officers.

Soil deterioration may trigger:[36]

- a fine of up to RUB 80,000 (US $1,250) for the legal entity;
- a suspension of the polluting entity's activities for a period of up to 90 days; and / or
- a fine of up to RUB 30,000 (US $470) in respect of the polluting entities' officers.

There are numerous other examples of administrative liability for environmental violations.

- Criminal liability

  Russian law does not recognise criminal liability with respect to legal entities. Only individuals (including officers of entities responsible for environmental damage) may be subject to criminal liability.

  Most of these environmental crimes involve violations of environmental laws and / or pollution that cause or threaten: (i) human life and health; or (ii) substantial damage to wildlife, plants, forestry, agricultural or other natural resources.

  The scope of potential penalties depends on the particular situation / type of the offence. For instance, air pollution that has caused harm to human health may result in:

  - a fine of up to RUB 200,000 (US $3,000) or up to 18 months' salary;
  - community service (up to 480 hours);
  - correctional labor (up to two years);
  - compulsory labor (up to two years); and / or
  - imprisonment for up to two years.

  Air pollution that has caused human death may result in:

  - compulsory labour (from two to five years); and / or
  - imprisonment for up to five years.

### *2.1.2 Priority given to environmental liabilities*

There are no special restrictions or conditions that apply when restructuring environmental liabilities.

The Insolvency Law envisages the following levels of priority for creditors' claims:[37]

- Highest priority: current expenses, which are monetary obligations that arise after the commencement of the insolvency proceedings (i.e. when the court accepts the insolvency application for consideration). Such claims have priority over the claims of all other creditors. The Insolvency Law sets out the following order for settling current expenses:

[36] *Idem*, art 8.6.
[37] Insolvency Law, art 134.

- court expenses, the insolvency practitioner's remuneration and expenses associated with the insolvency practitioner's engagement of other persons whose participation is mandatory under the Insolvency Law;
- claims regarding salaries and severance payments that occurred after the commencement of the insolvency proceedings;
- expenses associated with engaging persons whose participation in the insolvency proceedings is required but not mandatory (e.g. accountants and attorneys);
- utility and maintenance charges; and
- other current obligations.

▪ First priority: claims connected with bodily injuries and other injuries to health.

▪ Second priority: claims from employees regarding their salaries and severance payments, and royalties to the authors of items of intellectual property.

▪ Third priority: claims of all other creditors, including claims of state bodies (e.g. federal, regional government, tax, customs and pension funds).

The property available for distribution, including proceeds from the sale of assets, will subsequently be allocated among creditors of each priority level on a pro rata basis.

Secured creditors enjoy a special status during the insolvency proceedings, having the right to foreclose on the collateral and receive preferential repayment of their claims out of the proceeds. However, unlike an ordinary out of insolvency foreclosure, the Insolvency Law stipulates certain requirements and conditions for insolvency foreclosure to protect the rights of other non-secured creditors and the debtor.

For instance, during the financial rehabilitation or external administration stages, a secured creditor is entitled to enforce the pledge / mortgage and receive the entire amount of the proceeds. However, courts are allowed to prohibit foreclosure on the pledged assets if this will entail the inability to reinstate the debtor's solvency. Additionally, written consent must be obtained from a secured creditor if the pledged assets are put up for sale together with other assets. However, courts are entitled to circumvent such consent if the secured creditor acts in bad faith and the simultaneous sale of the pledged and non-pledged assets is more efficient than their separate sale.

The claims of third priority creditors for damages in the form of lost profits and for recovery of penalties (fines) and other financial sanctions, including sanctions for non-performance or improper performance of payment obligations, are recorded separately in the register of creditors' claims and are subject to satisfaction after the principal amounts due and interest due are repaid.[38]

Based on established court practice, in some cases the claims of creditors affiliated with the debtor may be subordinated – that is, only satisfied only after the satisfaction of the claims of all of the first, second and third priority creditors.[39]

### *2.1.3 Disclaimer of environmental obligations*

While a rehabilitation procedure can in principle restructure environmental liabilities, it does not relieve a company of its ongoing or subsisting statutory or contractual obligations (including environmental ones) post-restructuring.

Failure to comply with an order to eliminate a breach of environmental protection rules is an administrative offence.[40]

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38 *Idem*, art 137.
39 Review of case law by the Presidium of the Supreme Court of the Russian Federation, 29.01.2020.
40 Code of Administrative Offences, art 19.5.

### 2.2 Social (S): restructuring health or safety-related liabilities

Similar to the restructuring of environmental liabilities, health or safety-related liabilities can be restructured under a scheme in the same way as a company's ordinary liabilities.

However, an amicable settlement is subject to court approval on the condition that the claims of employees regarding their salaries and severance payments have been fully repaid.[41]

### 2.3 Governance (G): third party releases in favor of directors and officers of the company

There are no statutory provisions that enable third party releases in favour of directors and officers of the company.

As mentioned above, debt rescheduling (applied to individuals) can be used in a separate case to release the directors and officers from liability.

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

#### *3.1.1 Approving a restructuring plan*

There is no requirement for rehabilitation procedures to be approved by environmental protection authorities or environmental advocacy groups. Procedures only need to be approved by the court and the creditors.

#### *3.1.2 Discretion to consider wider public interest concerns*

There is no case law in Russia concerning the extent to which the court may consider environmental issues in deciding whether to approve a rehabilitation procedure.

#### *3.1.2 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

There are no statutory provisions which grant environmental protection authorities or environmental advocacy groups the right to air their views or concerns in a restructuring.

### 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

#### *3.2.1 Approving a restructuring plan*

There is no requirement for rehabilitation procedures to be approved by labour authorities, unions or employee / worker advocacy groups. Rehabilitation procedures need to be approved by the court and the creditors.

#### *3.2.2 Discretion to consider wider public interest concerns*

There is no case law in Russia concerning the extent to which the court may consider public interest concerns in deciding whether to approve a scheme.

#### *3.2.3 Protection of employee rights*

As indicated, amicable settlements are subject to court approval on the condition that the claims of employees regarding their salaries and severance payments have been fully repaid.[42]

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41 Insolvency Law, art 158.
42 *Ibid.*

### 3.3 Governance (G): board / management conflicts addressed in a restructuring

We have not identified any regulation regarding board / management conflict in relation to negotiations for post-restructuring shares or options (e.g. under a management incentive plan or options scheme) in return for a commitment to continue their service for the company post-restructuring.

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

We have not identified any industry guidelines and / or best practices prescribed for the protection of the environment in a restructuring.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

We have not identified any industry guidelines and / or best practices prescribed for the protection of employee rights in a restructuring.

As noted, under the Insolvency Law, amicable settlements are subject to court approval on the condition that the claims of employees regarding their salaries and severance payments have been fully repaid.[43]

Accordingly, such creditors' claims are repaid before the reorganisation by means of the commencement of a settlement agreement.

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

We have not identified any industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to.

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

Over the last several years, Russia has substantially progressed in terms of ESG regulations and voluntary market practices, including in terms of green and sustainability-linked debt finance practices.

In particular, in 2021 the Government approved the main goals and guidelines for Russia's sustainable development,[44] as well as criteria for green and adaptation projects.[45] These two documents are unofficially known as Russia's Green Taxonomy.

Green projects should fall within one of the areas defined in the Taxonomy, be aimed at achieving the Paris Agreement goals and have a positive environmental effect (along with meeting some other specific requirements).

Certain types of projects, such as those relating to renewables, EV charging infrastructure and reforestation, are considered "green" for Taxonomy purposes without meeting additional criteria.

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43 *Ibid.*

44 Decree of the Government of the Russian Federation No. 1912-r of 14.07.2021 "On Approval of the Goals and Main Directions for Sustainable (including Green) Development of the Russian Federation".

45 Decree of the Government of the Russian Federation No. 1587 dated 21.09.2021 "On Approval of Criteria for Sustainable (Including Green) Development Projects in the Russian Federation and Requirements for Verification System of Sustainable (Including Green) Development Projects in the Russian Federation".

Most projects must meet additional criteria and may require verification of environmental effects. For example, the production of steel, aluminum and cement is subject to carbon intensity limits (i.e. GHG emissions per tonne of production).

The authorities are debating whether Taxonomy-compliant projects shall be entitled to regulatory incentives, such as subsidies for: (i) lenders to compensate lost income when providing loans or purchasing bonds at an interest rate lower than market average; and / or (ii) borrowers to compensate the interest paid to the lenders under standard rates.

Currently, the authorities are working on a "Social Taxonomy" to kick off social bonds and loans to finance projects in healthcare, education, SMEs, basic infrastructure and accessibility.

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

Quite a number of Russian banks (both domestic and subsidiaries of multinational banks) have launched green finance and ESG-linked finance programmes for clients investing in renewables, green buildings, clean transportation, pollution prevention and control and other climate / environmentally sound projects.

Several banks in Russia have also provided ESG / sustainability-linked loans to some of Russia's major corporations (such as metals producers), whereby the interest rate of a credit facility or the loan quantum are linked to various ESG metrics such as carbon emissions.

According to some estimates, the value of the Russian banks' ESG-linked loan portfolios exceeds RUB 1.2 trillion (US $18.5 billion).[46]

A number of major Russian banks are promoting internal ESG practices such as purchasing renewable power or certificates, as well as multiple employee-focused initiatives.

### 5.3 Promotion of ESG by the central bank and regulators

The Russian Ministry of Finance and the Bank of Russia have presented a Financial Market Development Strategy through 2030. Among other things, the Strategy encourages companies to consider ESG factors when making investment decisions.

The Bank of Russia has issued an Information Letter on Recommendations for Boards of Directors of Public Joint Stock Companies to Consider ESG Factors as well as Sustainability Issues, and a checklist for determining board readiness to implement the ESG policy.[47]

Additionally, a number of Russian major corporations have established ESG business units and are developing relevant corporate governance practices.

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[46] Frank Media, 12 September 2022.

[47] Letter of the Bank of Russia No. IN-06-28/96 dated 16.12.2021 and Letter of the Bank of Russia No. IN-06-28/96 dated 16.12.2021 are available in Russian http://www.cbr.ru/crosscut/lawacts/file/5757.

# SINGAPORE

## 1. General overview of the restructuring regime

### 1.1 Formal restructuring procedures

The main procedure for restructuring debts in Singapore is a scheme of arrangement.[1] This is a court-supervised procedure which enables a company to enter a binding arrangement with its creditors to modify or adjust their respective rights and entitlements. Once a scheme of arrangement is approved by the court, it becomes binding on all creditors subject to the scheme, including dissenting creditors.[2]

The key substantive requirements for a scheme of arrangement are:[3]

- the scheme must be approved by a majority in number representing three-fourths in value of the creditors (or each class of creditors); and
- the scheme must be approved by the court.

A scheme of arrangement may be proposed either by the existing management through a debtor in possession (DIP) process,[4] or by a judicial manager[5] who is an independent insolvency practitioner.

Under the DIP process, the company can seek a protective moratorium to provide it with breathing space to formulate and negotiate the terms of the restructuring.[6] The company remains under the supervision of the court. The court can impose conditions on the moratorium[7] and has the discretion to discharge or vary the moratorium if a creditor applies for such a discharge or variation.[8]

Under the judicial management process, there is similarly a protective moratorium[9] and the judicial manager is also under the supervision of the court.[10] A judicial manager is appointed to serve one or more of the following purposes:

- the survival of the company as a going concern;
- the approval of a scheme of arrangement; and / or
- a more advantageous realisation of the company's assets or property than on a winding up.

One feature of the judicial management statutory regime which is not present in the DIP regime is that a judicial manager has the power to disclaim onerous property.[11] Onerous property refers to unprofitable contracts, or any property which is not readily saleable or which may give rise to a liability of the company to pay money or perform any other onerous act.[12] A disclaimer has the effect of putting an end to the rights, interests and liabilities of the company in relation to the property disclaimed as from the date of the disclaimer.[13] However, interested parties may apply to set aside the disclaimer where the loss caused by the disclaimer outweighs any advantage gained

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1 Companies Act 1967 (Companies Act), s 210; Insolvency, Restructuring and Dissolution Act 2018 (IRDA), Part 5 (Scheme of Arrangement).
2 Companies Act, s 210(3AA); *Pathfinder Strategic Credit LP v Empire Capital Resources Pte Ltd* [2019] 2 SLR 77 (*Pathfinder*, [27].
3 Companies Act, s 210.
4 IRDA, Part 5 (Scheme of Arrangement).
5 *Idem*, Part 7 (Judicial Management) and s 117.
6 *Idem*, s 64; *Re IM Skaugen SE* [2019] 3 SLR 97, [41]-[42].
7 *Idem*, s 64(5)(a).
8 *Idem*, s 64(10)(a).
9 *Idem*, ss 95 and 96.
10 *Idem*, s 115.
11 *Idem*, s 230.
12 *Idem*, s 230(2).
13 *Idem*, s 230(3).

by the judicial manager.[14] In section 2 below, we discuss the uncertainties as to whether the power of disclaimer might be used by a judicial manager to relieve a company of its ongoing environmental obligations.

The process of implementing a scheme is generally the same whether it is proposed under a DIP or judicial management process. It involves several stages.

First, an application is filed seeking the court's leave to convene a creditors' meeting to vote on the scheme (leave stage).[15] At the leave stage, the company must disclose information to assist the court in determining whether and how the creditors' meeting is to be conducted. There must be sufficient disclosure to enable the court to determine key issues, such as the classification of creditors, the proposal's realistic prospects of success, and any allegation of abuse of process.[16]

Second, the company then issues a notice of the creditors' meeting and provides the proposed scheme together with a statement explaining the effect of the scheme (explanatory statement) to the creditors.[17] The explanatory statement must give, as far as possible, all the information reasonably necessary to enable the creditors to determine how to vote,[18] and must disclose any material interests of the directors and the effect of the scheme thereon.[19]

Third, if the requisite majority of creditors have approved the scheme, the company then applies for the court's approval of the scheme (approval stage). The court will approve the scheme only if:

- the statutory provisions have been complied with;
- the creditors who attended the meeting were fairly representative of the class of creditors and the statutory majority did not coerce the minority; and
- the scheme is one which a person of business or an intelligent and honest person, being a member of the class concerned and acting in respect of his / her interest, would reasonably approve.[20]

As an alternative to the multi-stage process described above, a company may also implement a "pre-pack" scheme. This is an expedited procedure which bypasses the leave stage and the creditors' meetings.[21] Once the company obtains the requisite approvals of the creditors for the scheme (e.g. through lock-up agreements or voting undertakings), the company can proceed directly to apply for the court's approval of the scheme (the approval stage).

Any pecuniary claims against a company may be restructured under a scheme, including contingent, unproven or unliquidated claims.[22] There are no restrictions on the types of debt which may be restructured under a scheme.

One aspect of the scheme process which bears further elaboration is the classification of creditors for voting purposes. As will be discussed in sections 2 and 3 below, classification serves as a limited form of protection for creditors who are owed environmental or healthy and safety-related liabilities because there are generally no special restrictions or conditions when restructuring such liabilities.

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14 *Idem*, s 232.
15 Companies Act, s 210(1).
16 *Pathfinder*, [50].
17 Companies Act, s 211.
18 *The Royal Bank of Scotland NV (formerly known as ABN Amro Bank NV) v TT International Ltd* [2012] 2 SLR 213 (*TT International*), [65]; *SK Engineering & Construction Co Ltd v Conchubar Aromatics Ltd* [2017] 2 SLR 898, [88].
19 Companies Act, s 211(1)(a).
20 *TT International*, [70].
21 IRDA, s 71; *Re DSG Asia Holdings Pte Ltd* [2022] 3 SLR 1250, [26].
22 *SAAG Oilfield Engineering (S) Pte Ltd v Shaik Abu Bakar bin Abdul Sukol* [2012] 2 SLR 189, [29]-[30], [48]-[50]; *Re Swiber Holdings Ltd* [2018] 5 SLR 1358, [29].

The proper classification of creditors is crucial in a scheme process, as it functions as a form of minority protection.[23] A group of creditors is required to be classed separately if the scheme favours (or prejudices) that group of creditors differently from how they would be favoured (or prejudiced) in the event of the most likely scenario in the absence of scheme approval (referred to as the "comparator").[24] The comparator is usually a insolvent liquidation scenario.[25]

Ordinarily, a scheme must be approved by all classes of creditors, meaning that the scheme must be commercially acceptable to each class, failing which any class could potentially veto the scheme. From a practical perspective, this encourages a debtor to formulate the terms of the restructuring such that it respects or follows the priorities afforded to the debts in a liquidation, so as to streamline and minimise the number of classes. For example, a debt that would have priority in a liquidation will usually be given priority in a scheme as well. If the scheme fails to respect that priority, it is likely that the creditors who are owed those affected debts would be classed separately and can therefore veto the scheme.

That said, even if there are one or more dissenting classes of creditors, a scheme may be approved through a "cross-class cram down" under certain conditions.[26] There are various protections to ensure that the dissenting classes of creditors are treated fairly in a cross-class cram down. For example, the scheme must not discriminate unfairly between the classes of creditors, and must be fair and equitable to each dissenting class.[27] The creditors of the dissenting class must also receive under the scheme at least what they would be estimated to receive if the scheme is not effected (usually, this refers to the estimate of their recovery in a liquidation scenario).[28] As such, even in a cross-class cram down, the rights of the dissenting class of creditors still receive a degree of protection.

Drawing together the threads of the discussion above, the implication in practical terms is that it is crucial to first determine what rights and priorities a particular debt would have in the comparator, as that would usually guide how the debt is treated in a restructuring under a scheme.

### 1.2 Informal restructuring procedures

Informal out of court restructurings are conducted primarily on a consensual basis and are not specifically governed by any legislation. There are non-statutory frameworks, such as the Association of Banks in Singapore's Principles & Guidelines for Restructuring of Corporate Debt in Singapore (ABS Guidelines), which provide recommendations on facilitating successful restructurings. For example, the ABS Guidelines encourage the following actions to be taken in a consensual restructuring:

- early provision of information by debtors which is complete, accurate and independently verified;
- equal sharing of information;
- implementation of a standstill to allow for the preparation and analysis of detailed information and accompanying discussions and negotiations;
- active involvement of senior management;
- appointment of a lead bank early in the restructuring process to manage and coordinate the restructuring process;
- appointment of a steering committee to represent the lenders' interests; and

23 *TT International*, [141].
24 *TT International*, [133]-[141]; *Pathfinder*, [87]-[88].
25 *TT International*, [142]; *Pathfinder*, [88(a)].
26 IRDA, s 70.
27 *Idem*, s 70(3)(c).
28 *Idem*, s70(4)(a).

- appointment of a special accountant or independent financial adviser.

Out of court workouts through consent solicitation exercises are also commonplace for bond restructurings, where an issuer seeks the consent of holders of debt securities to amend and / or waive breaches of the terms of those debt securities. Some bond restructurings may proceed directly under the "super majority" provisions in bond issues or related trust deeds, meaning that once the requisite majority consents to such amendment or waiver, the decision is binding on all bondholders, including those who did not consent to the same.

## 2. Restructuring of ESG-related liabilities

### 2.1 Environmental (E): restructuring environmental liabilities

Generally, environmental liabilities can be restructured under a scheme in the same way as ordinary liabilities of a company. As mentioned above, any pecuniary claims against a company may be restructured under a scheme, including contingent, unproven or unliquidated claims.[29] There are no special restrictions or conditions that apply when restructuring environmental liabilities.

#### *2.1.1 Types of environmental liabilities*

For background, environmental liabilities under Singapore law can encompass:

- civil claims, such as claims in tort[30] and claims in contract;[31] and
- statutory liabilities such as:
  - fines. For example, under the Environmental Protection and Management Act 1999 (EPMA),[32] fines may be imposed for various statutory offences, such as the failure to maintain air pollution control equipment on industrial or trade premises,[33] the discharge of untreated trade effluent, oil, chemical, sewage or other polluting matters,[34] and the failure to store, use or deal with hazardous substances in such a manner as not to cause pollution to the environment;[35] and
  - remediation / clean-up costs. For example, under the EPMA, the National Environment Agency (NEA) may direct the owner or occupier of premises to take certain remedial actions if the NEA has reason to believe that the emission of air impurities, the discharge of trade effluent or the emission or discharge of any hazardous substance or toxic substance from any premises is likely to cause pollution of the environment or be injurious to public health or safety.[36] Where the owner or occupier fails to comply with the NEA's orders, the Director-General of Environment Protection (Director-General) may enter upon the premises and execute such work as may be necessary.[37] Any expenses reasonably incurred by the Director-General in this regard may be recovered from the person in default.[38]

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29 *SAAG Oilfield Engineering (S) Pte Ltd v Shaik Abu Bakar bin Abdul Sukol* [2012] 2 SLR 189, [29]-[30], [48]-[50]; *Re Swiber Holdings Ltd* [2018] 5 SLR 1358, [29].

30 For example, a party may be liable under the tort of nuisance or the tort of negligence if it caused damage or pollution to another party's land. See generally, for example, *PEX International Pte Ltd v Lim Seng Chye* [2020] 1 SLR 373.

31 For example, a tenant under a lease agreement may be subject to contractual obligations to remove waste products from the leased premises, not to cause pollution, or generally to comply with all environmental regulations.

32 Apart from the EPMA, there are various other pieces of environmental legislation including but not limited to the Environmental Public Health Act 1987, the Hazardous Waste (Control of Export, Import and Transit) Act 1997 and the Prevention of Pollution of the Sea Act 1990.

33 EPMA, s 10.

34 *Idem*, s 16.

35 *Idem*, s 24.

36 *Idem*, s 39(1).

37 *Idem*, ss 39(3), 41(b).

38 *Idem*, ss 47, 51.

There is generally no distinction as to how the various types of environmental liabilities are treated under a scheme. Statutory liabilities are susceptible to be restructured under a scheme[39] and, unlike some jurisdictions, there is no express prohibition against restructuring fines under a scheme.

### 2.1.2 *Priority given to environmental liabilities*

However, as mentioned in section 1 above, certain liabilities may be given priority treatment under a proposed scheme if such liabilities would have priority in liquidation.[40] Environmental liabilities do not fall within any of the statutorily prescribed categories of preferential debts which receive priority in a liquidation.[41] However, there are exceptions where environmental liabilities could be classified as secured or priority debts, for example:

- remediation or clean-up costs incurred by the Director-General (described above) are secured by a first charge on the premises in respect of which the costs and expenses were incurred, if the owner of the premises (as opposed to the occupier of the premises) is the party liable to pay such costs and expenses;[42]

- the liabilities are secured by a charge, mortgage or other form of security interest (for example, in a financing transaction where a lender takes a mortgage over a borrower's land); or

- the liabilities are elevated to a priority debt pursuant to the judicial management expenses principle (a common law principle which treats a liability under an existing lease as though it were an expense incurred by the judicial manager, in circumstances where the judicial manager retains possession of leased property for the benefit of the judicial management).[43]

### 2.1.3 *Disclaimer of environmental obligations*

While a scheme can in principle restructure environmental liabilities, it does not relieve a company of its ongoing or subsisting statutory or contractual obligations post-restructuring. For example, a company that continues to emit pollutants or hazardous substances after it emerges from a restructuring could be liable for new offences that attract additional fines. In practice, this means that a company that intends to continue operating its plant or factory (as opposed to selling it) would need to ensure that it has the resources post-restructuring to be able to meet its environmental obligations.

However, under a judicial management process, a judicial manager has the power to disclaim onerous property (as noted above). In principle, onerous property could include property such as a plant or a factory which is subject to continuing and onerous environmental obligations that are to be performed over a substantial period of time and which will involve expenditure that may not be recovered.[44] Where a judicial manager wishes to disclaim property that is subject to certain environmental laws,[45] the judicial manager is required to notify the relevant regulator 28 days

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39 See generally *Chew Eu Hock Construction Co Pte Ltd (under judicial management) v Central Provident Fund Board* [2003] 4 SLR(R) 137, where it was held that claims by the Central Provident Fund (CPF) (Singapore's social security savings scheme) for outstanding contributions were validly compromised under a scheme which gave the claims the same treatment as ordinary unsecured debts.

40 Or whichever is the appropriate comparator.

41 IRDA, s 203. The categories of preferential debts under s 203 of the IRDA include the costs and expenses of the winding up, wages and salary, retrenchment benefits, work injury compensation, CPF contributions and taxes.

42 EPMA, s 53(1).

43 *Re Swiber Holdings Ltd* [2018] 5 SLR 1358, [87]-[90]. For example, in an unreported decision (*In the matter of NK Ingredients Pte Ltd* HC/OS 72/2019, HC/SUM 551/2020, HC/ORC 1676/2020), the Singapore High Court made an order declaring that the costs of removing waste products and decommissioning a plant were to be regarded as expenses of the judicial management.

44 See the English Court of Appeal decision *In re SSSL Realisations (2002) Ltd* [2006] Ch 610, [36], citing *Transmetro Corporation ltd v Real Investments Pty Ltd* (1999) 17 ACLC 1314. While English cases are not binding in Singapore, they may be persuasive, particularly where the statutory provisions in Singapore are adopted from or materially similar to the English provisions.

45 Namely, the EPMA, Control of Vectors and Pesticides Act 1998, Environmental Public Health Act 1987, Hazardous Waste (Control of Export, Import and Transit) Act 1997, Radiation Protection Act 2007, Sewerage and Drainage Act 1999 and Transboundary Haze Pollution Act 2014.

before issuing a notice of disclaimer.[46] This ensures the relevant regulatory authority has the opportunity to address any issues relating to the property under the relevant environmental legislation.[47]

The extent to which the power of disclaimer may be used to relieve a company of its statutory environmental obligations is uncertain, as there are no reported decisions in Singapore relating to the issue. The Singapore disclaimer provisions are adopted from the United Kingdom, where there are conflicting decisions relating to the application of the disclaimer regime to environmental licences, centred around the issue whether the interest in protecting the environment should take precedence over the interest in ensuring a fair and orderly insolvency proceeding.[48]

Under a DIP process, the company has no power to disclaim onerous property.

## 2.2 Social (S): restructuring health or safety-related liabilities

Similar to the restructuring of environmental liabilities, health or safety-related liabilities can be restructured under a scheme in the same way as ordinary liabilities of a company. As mentioned above, any pecuniary claims against a company may be restructured under a scheme, including contingent, unproven or unliquidated claims.[49] There are no special restrictions or conditions that apply when restructuring health or safety-related liabilities.

### *2.2.1 Types of health and safety-related liabilities*

For background, health or safety-related liabilities under Singapore law can encompass:

- civil claims, such as claims in tort[50] and claims in contract;[51] and
- statutory liabilities such as:
  - fines. For example, selling unsafe food or food containing prohibited substances are offences under the Sale of Food Act 1973, and failing to take such measures as are reasonably practicable and necessary to ensure the safety and health of employees at work is an offence under section 12 of the Workplace Safety and Health Act 2006 (WSHA); and
  - remediation costs. For example, under the WSHA, the Commissioner may serve a remedial order directing a person to remedy any danger on a workplace that is affecting the safety, health and welfare of the persons at work.[52] Where the person fails to comply with the order, the Commissioner may take appropriate measures to prevent unauthorised entry or access to the area or the equipment or plant affected and may recover the costs and expenses incurred from the person served with the order.[53]

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46 IRDA, s 230(4)(a), read with the Second Schedule.

47 Singapore Parliamentary Debates, Official Report (1 October 2018) volume 94 sitting 83, Second Reading of the Insolvency, Restructuring and Dissolution Bill (Edwin Tong Chun Fai, Senior Minister of State for Law).

48 See A Keay and P de Prez, "Insolvency and Environmental Principles: A Case Study in a Conflict of Public Interests" (2001) 3(2) *Environmental Law Review* 90-112, which discusses *Re Mineral Resources ltd* [1999] 4 All ER 746 and *Re Celtic Extraction Ltd* [1999] 4 All ER 684.

49 *SAAG Oilfield Engineering (S) Pte Ltd v Shaik Abu Bakar bin Abdul Sukol* [2012] 2 SLR 189, [29]-[30], [48]-[50]; *Re Swiber Holdings Ltd* [2018] 5 SLR 1358, [29].

50 For example, a party may be liable under the tort of negligence for the negligent manufacture, distribution or supply of goods in circumstances where a duty of care is established. See generally, for example, *The Sunrise Crane* [2004] 1 SLR 300 (High Court); [2004] 4 SLR 715 (Court of Appeal), which held that a party had a duty to take reasonable care to prevent reasonable care to prevent dangerous goods from doing injury or damage to persons or property which was likely to come into contact with them. See generally, for the requirements to establish a claim under the tort of negligence, *Spandeck Engineering (S) Pte Ltd v Defence Science & Technology Agency* [2007] 4 SLR(R) 100.

51 For example, a party that supplies defective or unsafe goods may be liable for breach of an express term of the contract or the implied term of satisfactory quality imposed by virtue of s 14 of the Sale of Goods Act 1979.

52 WSHA, s 21.

53 *Idem*, s 21(9).

#### *2.2.2 Treatment of health and safety-related liabilities*

There is generally no distinction as to how the various types of health or safety-related liabilities are treated under a scheme. Statutory liabilities are susceptible to be restructured under a scheme[54] and, unlike some jurisdictions, there is no express prohibition against restructuring fines under a scheme.

However, as mentioned in section 1 above, certain liabilities may be given priority treatment under a proposed scheme if such liabilities would have priority in liquidation.[55] Some examples of health or safety-related liabilities that may have preference or priority in liquidation are:

- all amounts due in respect of work injury compensation under the Work Injury Compensation Act 2019, which is a preferential debt in a winding up pursuant to section 203 of the IRDA;
- liabilities secured by a charge, mortgage or other form of security interest (for example, in a financing transaction where a lender takes a mortgage over a borrower's land); or
- liabilities elevated to a priority debt pursuant to the judicial management expenses principle (a common law principle which treats a liability under an existing lease as though it were an expense incurred by the judicial manager, in circumstances where the judicial manager retains possession of leased property for the benefit of the judicial management).[56]

### 2.3 Governance (G): third party releases in favour of directors and officers of the company

As a starting point, it is possible for a scheme to provide for third party releases.

There are two aspects that govern whether a third-party release will be allowed by the court.

The first is whether there is a sufficient nexus or connection between the release of the third party liability and the relationship between the company and the scheme creditors.[57] This requirement must be met in order for the court to have the requisite jurisdiction to give effect to the third party release.

The second is whether the third party release sought is fair and reasonable in the circumstances, having regard to the factors to be considered at the approval stage.[58] As mentioned in section 1 above, when deciding whether to approve a scheme, the court will consider whether creditors who attended the meeting were fairly representative of the class of creditors and whether the scheme is one which a person of business or an intelligent and honest person, being a member of the class concerned and acting in respect of his / her interests, would reasonably approve.

Third party releases have been allowed in circumstances where the relevant third parties were related companies of the debtor within the same corporate group, and the debts of the scheme company and the third parties arose under the same issuance of notes.[59] The rationale in permitting third party releases of debts, at least where related companies are concerned, is to allow a holistic group restructuring to be effective. In *Pathfinder* (at [81]), the Singapore Court of Appeal explained that the third party releases sought in that case were necessary "since otherwise

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54 See generally *Chew Eu Hock Construction Co Pte Ltd (under judicial management) v Central Provident Fund Board* [2003] 4 SLR(R) 137, where it was held that claims by the Central Provident Fund (CPF) (Singapore's social security savings scheme) for outstanding contributions were validly compromised under a scheme which gave the claims the same treatment as ordinary unsecured debts.

55 Or whichever is the appropriate comparator.

56 *Re Swiber Holdings Ltd* [2018] 5 SLR 1358, [87]-[90]. For example, in an unreported decision (*In the matter of NK Ingredients Pte Ltd* HC/OS 72/2019, HC/SUM 551/2020, HC/ORC 1676/2020), the Singapore High Court made an order declaring that the costs of removing waste products and decommissioning a plant were to be regarded as expenses of the judicial management.

57 *Pathfinder*, [77].

58 *Idem*, [76].

59 The related debts being the primary debt owing under the notes, and the guarantee debts owing by related party guarantors. See generally, *Pathfinder*, [72]-[82].

liability and enforcement risks would merely be shifted between members of the corporate group and the overall restructuring objective would be entirely unmet".

There have been no reported decisions in Singapore regarding whether third party releases can be granted in favour of directors and officers of the company and the principles applicable to the granting of such releases.[60] In principle, the "sufficient nexus" test might be met for a proposed third party release, even if the third parties are not members within the same corporate group. For example, in the Federal Court of Australia decision of *Re Opes Prime Stockbroking Ltd* [2009] FCA 813, which was cited with approval by the Singapore Court of Appeal in *Pathfinder*, the third party releases were granted in favour of not just another company in the corporate group, but also certain banks, liquidators and receivers. However, the precise extent to which third party releases are allowed in favour of directors and officers of the company is not clear in Singapore.

In any event, the inclusion of third party releases in favour of directors and officers would have to be disclosed pursuant to the various disclosure requirements described in section 1 above. Furthermore, it is prescribed that the scheme explanatory statement must disclose any material interests of the directors and the effect of the scheme thereon.[61]

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

#### *3.1.1 Approving a restructuring plan*

There is no requirement for a scheme to be approved by environmental protection authorities or environmental advocacy groups. A scheme only needs to be approved by the court and the creditors.

#### *3.1.2 Discretion to consider wider public interest concerns*

There is no case law in Singapore concerning the extent to which the court may consider environmental issues in deciding whether to approve a scheme. The fairness and reasonableness determination made at the scheme approval stage primarily focuses on the rights and interests of the creditors and does not incorporate a wider public interest assessment.

Even if the court is empowered to consider the public interest when approving a scheme, it is likely that such a power would be exercised cautiously or only in exceptional circumstances. An analogy can be drawn with cases relating to judicial management, in which the courts have narrowly interpreted the statutory provisions which empower the court to make a judicial management order on public interest grounds.[62] In *Re Bintan Lagoon Resort Ltd*, the court held that the power "should not be lightly exercised even if it may be in the public interest to do so" and "it should not only be opportune but also importunate that the power be exercised."[63] The court framed the inquiry as whether there would be a "serious economic or social impact" if the company were to collapse.[64]

#### *3.1.3 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

There are no statutory provisions which grant environmental protection authorities or environmental advocacy groups standing to air their views or concerns in a restructuring. However, certain regulated entities, such as electricity licensees and designated public utilities providers, are

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60 In practice, it is not uncommon for schemes in Singapore to provide for releases of personal liability in favour of directors and officers, for example in relation to actions taken in connection with the restructuring of the company.

61 Companies Act, s 211(1)(a).

62 IRDA, s 91(10)(a).

63 [2005] 4 SLR(R) 336, [13].

64 *Idem*, [14].

statutorily required to give notice to the relevant regulatory agencies[65] before commencing scheme proceedings[66] and to include the relevant regulatory agencies as party to the scheme proceedings.[67] No judicial management order may be made in relation to electricity licensees and designated public utilities providers without the consent of the relevant regulatory agencies.[68]

Separately, as mentioned in section 2 above, where a judicial manager wishes to disclaim property that is subject to certain environmental laws,[69] the judicial manager is required to notify the relevant regulator 28 days before issuing a notice of disclaimer.[70] This ensures that the relevant regulatory authority has the opportunity to address any issues relating to the property under the relevant environmental legislation.[71]

## 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

### *3.2.1 Approving a restructuring plan*

There is no requirement for a scheme to be approved by labour authorities, unions or employee / worker advocacy groups. A scheme only needs to be approved by the court and the creditors.

### *3.2.2 Discretion to consider wider public interest concerns*

There is no case law in Singapore concerning the extent to which the court may consider labour issues in deciding whether to approve a scheme. The fairness and reasonableness determination made at the scheme approval stage (as described in section 1 above) primarily focuses on the rights and interests of the creditors and does not incorporate a wider assessment of the employees' interests.

### *3.2.3 Protection of employee rights*

Generally, there are no statutory provisions which grant labour authorities, unions or employee / worker advocacy groups standing to air their views or concerns in a restructuring.

In the context of judicial management, where employees of a company are members of a trade union that is recognised by the company under the Industrial Relations Act 1960, the trade union functions as an intermediary for the employees. The trade union is entitled to represent any its members at a meeting of creditors summoned to consider the judicial manager's statement of proposals.[72] The trade union may also, with the permission of the court, apply to the court to seek orders to protect the interests of its members if the company's affairs, business and property are being or have been managed by the judicial manager or interim judicial manager in a manner that is or was unfairly prejudicial to their interests.[73] The trade union may also make representations to the judicial manager on behalf of those employees in respect of any matter connected with their employment contracts.[74]

65 The Energy Market Authority and the Public Utilities Board respectively.
66 Electricity Act 2001, s 29(7)(e); Public Utilities Act 2001, s 44I(1)(e).
67 Electricity Act 2001, s 29(8)(b); Public Utilities Act 2001, s 44I(2)(a).
68 Electricity Act 2001, s 29(7)(a); Public Utilities Act 2001, s 44I(1)(f).
69 Namely, the EPMA, Control of Vectors and Pesticides Act 1998, Environmental Public Health Act 1987, Hazardous Waste (Control of Export, Import and Transit) Act 1997, Radiation Protection Act 2007, Sewerage and Drainage Act 1999 and Transboundary Haze Pollution Act 2014.
70 IRDA, s 230(4)(a), read with the Second Schedule.
71 Singapore Parliamentary Debates, Official Report (1 October 2018) volume 94 sitting 83, Second Reading of the Insolvency, Restructuring and Dissolution Bill (Edwin Tong Chun Fai, Senior Minister of State for Law).
72 IRDA, s 116(2)(a).
73 *Idem*, s 116(2)(a), read with s 115.
74 *Idem*, s 116(2)(b).

### 3.3 Governance (G): board / management conflicts addressed in a restructuring

Board / management conflicts are largely addressed in a restructuring through the disclosure requirements under the scheme regime, as well as the fairness and reasonableness requirements imposed by the court when deciding whether to approve the scheme. These requirements are discussed in greater detail in section 1 above. If the directors or management personnel are receiving shares or options pursuant to an incentive plan as part of the restructuring, such matters would likely have to be disclosed in the scheme explanatory statement in order to enable the creditors to assess whether the allocation of loss and the division of benefits is fair and in their commercial interests.[75]

Furthermore, if the directors or management personnel are also scheme creditors, their votes on the scheme might also be disregarded in the vote count on the basis that they are related creditors.[76]

Outside the restructuring context, listed companies in Singapore are also subject to various regulations which help to address conflict of interest concerns regarding remuneration of directors and key management personnel. For example, under the Singapore Exchange (SGX) Mainboard Rules (SGX Mainboard Rules), a listed company must obtain the approval of independent shareholders where it intends to grant shares under a share option plan to a controlling shareholder or its associates,[77] or to a director or an employee which would increase the grantee's holding to 5% or more of the total number of options available to participants of that kind.[78] There are also various requirements to disclose information in relation to share option schemes,[79] and limits on the number of shares that can be issued to directors and employees under such schemes.[80]

Listed companies are also required to comply with the Code of Corporate Governance 2018 (Code), failing which they must explain the reason for any variation from the provisions of the Code and explain how the practices it had adopted are consistent with the intent of the relevant principles of the Code.[81] For example, the Code provides that:

- the board must have a formal and transparent procedure for developing policies on director and executive remuneration and fixing the remuneration packages for individual directors and key management personnel;[82]
- no director can be involved in deciding their own remuneration;[83]
- performance-related remuneration must align with the interests of shareholders, stakeholders, and the company's long-term success;[84]

75 See *Re DSG Asia Holdings Pte Ltd* [2022] 3 SLR 1250, [38], citing the English High Court decisions of *In re Sunbird Business Services Ltd* [2020] Bus LR 2371 and *Re Virgin Atlantic Airways Ltd* [2020] EWHC 2376 (Ch), where it was held that "[f]or creditors to be able to make an informed decision whether to agree to a scheme, they need information that enables them to assess whether the allocation of loss and the division of benefits is fair and in their commercial interests."

76 See *SK Engineering & Construction Co Ltd v Conchubar Aromatics Ltd* [2017] 2 SLR 898, [40]-[42] in which the Court of Appeal set out guidelines as to when a scheme creditor would be deemed to be a related creditor (at [40]-[42]) and held that the votes of related creditors ought to be wholly discounted (at [67]).

77 SGX Mainboard Rules, r 853.

78 *Idem*, r 854.

79 *Idem*, Part VIII.

80 *Idem*, r 845.

81 *Idem*, r 710; Code, Introduction paragraph 8.

82 Code, principle 6.

83 *Ibid.*

84 *Idem,* principle 7.

- a significant, appropriate proportion of executive directors' remuneration and the remuneration of key management personnel must be linked to corporate and individual performance;[85] and
- the remuneration of non-executive directors must be appropriate to their contributions, such as effort, time and responsibilities.[86]

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

We have not identified any industry guidelines and / or best practices prescribed for the protection of the environment in a restructuring.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

The Tripartite Advisory on Managing Excess Manpower and Responsible Retrenchment (Advisory) is a set of guidelines jointly promulgated by the Ministry of Manpower, the National Trades Union Congress and the Singapore National Employers Federation. The Advisory sets out guidelines relating to how Singapore businesses should seek to retrench employees in a responsible manner.

For example, the Advisory recommends that:

- retrenchment should be considered as a last resort, after other feasible options (e.g. flexible work schedule, wage adjustments, shorter work-week, no-pay leave) have been considered and exhausted;[87]
- employers should engage unions and employees to discuss and reach an agreement before implementing retrenchment measures;[88]
- employers should ensure objectivity in the selection of employees for retrenchment and not discriminate against employees on grounds of age, race, gender, religion, marital status and family responsibility or disability. Selection should be based on objective criteria such as the ability, experience, and skills of the employee to support the company's sustainability, workforce transformation and / or future business needs;[89]
- before the public notice of retrenchment, employers should communicate early to their employees about the efforts to manage business challenges and the intent to retrench;[90]
- employers should ensure that retrenchment is carried out in a respectful manner and should consider good practices such as providing a longer notice period where possible, preparing managers responsible for notifying employees of retrenchment to deliver the news in a sensitive manner, and assigning human resources personnel and union representatives to be on site to take feedback and answer queries from retrenched employees;[91]
- as far as possible, employers should pay a reasonable retrenchment benefit to enable the affected employees to move on to new employment opportunities;[92] and

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85 *Idem,* principle 7.1.
86 *Idem,* principle 7.2.
87 Advisory, paragraphs 2 and 9.
88 *Idem,* paragraph 7 and Annex A.
89 *Idem,* paragraph 10.
90 *Idem,* paragraph 13.
91 *Idem,* paragraph 14.
92 *Idem,* paragraph 17.

- employers should make practical efforts to help affected employees look for alternative jobs, possibly with the help of intermediaries such as employment / placement agencies.[93]

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

The Insolvency Practitioners Association of Singapore's (IPAS)[94] Code of Professional Conduct and Ethics (IPAS Code) prescribes general guidelines as to how insolvency professionals who are members of IPAS should deal with potential conflicts of interest, without specific reference to restructuring scenarios. The IPAS Code prescribes that insolvency professionals:

- take reasonable steps to identify circumstances that could pose a conflict of interest;[95]

- apply necessary safeguards in situations of conflict, such as notifying the client of the circumstances giving rise to the conflict and obtaining their consent to act in such circumstances;[96]

- apply additional safeguards such as using separate teams, implementing procedures to prevent access to information and to maintain security and confidentiality, and regularly reviewing the application of safeguards by a senior individual not involved with the relevant client engagements; and[97]

- decline to accept an engagement or resigning from one or more conflicting engagements if a conflict of interest creates a threat to one or more of the fundamental principles, including objectivity, confidentiality or professional behaviour, that cannot be eliminated or reduced to an acceptable level through the application of safeguards.[98]

Unlike the Legal Profession (Professional Conduct) Rules 2015 which apply to lawyers in Singapore, the IPAS Code does not carry the force of law.

In terms of hard law, there is no comprehensive statutory or legislative instrument governing conflicts of interests in relation to restructuring professionals. However, there are the following restrictions and duties imposed by specific statutory provisions and case law:

- a person cannot act as a judicial manager of a company if he / she is in a position of conflict of interest;[99]

- when seeking litigation funding to pursue avoidance actions, if the judicial manager is aware of an actual or potential conflict of interest, he / she must make a full and frank disclosure of the interest and obtain the approval of a three-fourths majority in value of the creditors;[100]

- a scheme manager and judicial manager must act in an objective, independent, fair and impartial manner when adjudicating the creditors' proofs of debt, and cannot favour the interests of his / her appointers over that of the creditors;[101] and

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93 *Idem,* paragraph 18.
94 IPAS is a non-governmental organisation for insolvency professionals in Singapore. Membership to the organisation is voluntary. It is not necessary to be a member of IPAS in order to qualify as a licensed insolvency practitioner in Singapore.
95 IPAS Code, paragraph 9.1.
96 *Idem,* paragraph 9.3.
97 *Idem,* paragraph 9.4.
98 *Idem,* paragraph 9.5.
99 IRDA, s 91(3)(b) (court-ordered judicial management) and s 94(3)(e) (judicial management by resolution of creditors). The statute does not define what is a "conflict of interest" for the purpose of these provisions.
100 Insolvency, Restructuring and Dissolution (Assignment of Proceeds of an Action) Regulations 2020, reg 4(8).
101 *TT International*, [67], [75]. It was also observed in *TT International* at [77] that a "proposed scheme manager is inherently in a position of conflict because if he successfully resuscitates the company, he is

- in a scheme, the fees of restructuring professionals must be disclosed to the scheme creditors.[102] Outside the scheme context, insolvency practitioners such as liquidators, judicial managers, receivers and managers must submit costs schedules setting out estimates of their fees for work anticipated to be done, which are subject to the approval of the court or other approving body, such as the committee of creditors in judicial management.[103]

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

ESG / sustainability-linked loans have gained traction and prominence in Singapore in recent years. Many Singapore banks have launched ESG / sustainable financing programmes which provide financing for projects such as renewable energy, green buildings, clean transportation, pollution prevention and control and the development of environmentally sustainable projects.[104] Banks in Singapore have also issued ESG / sustainability-linked loans which peg the interest rate of a credit facility or the loan quantum to various ESG metrics.[105] The major local banks have also set substantial targets for their sustainable finance portfolios, with DBS targeting a sustainable finance portfolio of S $50 billion by 2024,[106] UOB targeting S $30 billion by 2025[107] and OCBC targeting S $25 billion by 2025.[108]

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

Singapore banks have also adopted the Equator Principles[109] (which prescribe a set of principles for the assessment, management and monitoring of environmental and social risks when financing projects). DBS has also joined the United Nations Environment Programme's Net-Zero Banking Alliance, which requires its members to commit to various efforts aimed at reducing the greenhouse gas emissions of their lending and investment portfolios to sustainable levels, such as

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remunerated, inter alia, for managing the scheme and reviving the company. Therefore, there are undeniable incentives for the proposed scheme manager to prefer the interests of his appointers (not infrequently, the company itself as is the case here) over those of their creditors from the outset. He must, nevertheless, seek to strike the right balance and manage the competing interests of successfully securing the approval of his proposed scheme and uncompromisingly respecting the procedural rights of all involved in the scheme process." The proposed scheme manager in that case was found to be in an "unacceptable position of unavoidable conflict of interest" as he was concurrently acting as the nominee for individual voluntary arrangements filed by the company's director-shareholders (at [78]).

102 *The Royal Bank of Scotland NV (formerly known as ABN Amro Bank NV) v TT International Ltd* [2012] 4 SLR 1182, [24]-[32].

103 See *Kao Chai-Chau Linda v Fong Wai Lyn Carolyn* [2016] 1 SLR 21 generally. See also IRDA, s 113 as regards the approval of a judicial manager's remuneration and expenses.

104 Examples of such programmes include DBS Bank's Sustainable and Transition Finance Framework & Taxonomy (https://www.dbs.com/sustainability/responsible-banking/responsible-financing), OCBC Bank's sustainable financing programme for small-medium enterprises (https://www.ocbc.com/business-banking/smes/loans/sustainable-financing), and UOB's sustainable financing frameworks (https://www.uobgroup.com/uobgroup/sustainable-financing.page#framework).

105 Banks that have reported issuing such loans include DBS (https://www.dbs.com/sustainability/responsible-banking/sustainable-financing/sustainable-linked-transactions), Bank of Singapore (https://www.bankofsingapore.com/media-releases/2021/bank-of-singapore-factors-in-sustainability-for-investment-financing.html), OCBC Bank (https://www.ocbc.com/group/media/release/2021/ocbc-fortune-reit-sll.page?).

106 The Business Times, DBS boosts sustainable finance target to S$50b by 2024 (4 February 2021), https://www.businesstimes.com.sg/banking-finance/dbs-boosts-sustainable-finance-target-to-s50b-by-2024.

107 The Business Times, UOB raises sustainable finance target to $30 billion by 2025 (16 February 2022), https://www.straitstimes.com/business/banking/uob-raises-sustainable-finance-target-to-30-billion-by-2025

108 The Business Times, OCBC, riding growth wave, targets S$25b sustainable finance portfolio by 2025 (22 June 2022), https://www.businesstimes.com.sg/banking-finance/ocbc-riding-growth-wave-targets-s25b-sustainable-finance-portfolio-by-2025.

109 The latest iteration of the Equator Principles, EP4 (issued in July 2020) is accessible at https://equator-principles.com/a_pp/uploads/The-Equator-Principles_EP4_July2020.pdf. The major Singapore banks, DBS, UOB and OCBC Bank, have adopted the Equator Principles: https://equator-principles.com/members-reporting/.

transitioning their portfolios, setting targets for emissions reduction, publishing emissions data and reporting progress of their transition strategy and actions.[110]

### 5.3 Promoting ESG by the central bank and regulators

The Monetary Authority of Singapore (MAS), which is the central bank of Singapore, has also undertaken various efforts to promote ESG financing. These efforts include:

- the US $2 billion Green Investments Programme, under which the MAS place funds with asset managers committed to driving regional green efforts out of Singapore and contributing to MAS' other green finance initiatives, including developing green markets and managing environmental risks;[111]
- the Sustainable Bond Grant Scheme, which provides grants to issuers of sustainability-linked bonds to offset the costs of conducting external reviews or ratings done for the purpose of demonstrating alignment with any internationally recognised green, social, sustainability and sustainability-linked principles or standards;[112]
- the Green and Sustainability-Linked Loan Grant Scheme, which provides grants to defray the expenses of engaging independent service providers to validate the green and sustainability credentials of qualifying loans, as well as grants to encourages banks to develop green and sustainability-linked loan frameworks;[113]
- the issuance of Guidelines on Environmental Risk Management for banks,[114] insurers[115] and asset managers,[116] which provides guidelines on issues such as governance and strategy, risk management and disclosure of environmental risk information; and
- engaging in various international and regional collaborations such as the Basel Committee on Banking Supervision Task Force on Climate-Related Financial Risks, the G20 Sustainable Finance Working Group, and Network for Greening the Financial System, to develop global standards, enhance best practices, and inform financial supervisory and central banking policies.[117]

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110 Members of the Net-Zero Banking Alliance are required to sign a Commitment Statement as a pre-requisite for joining the organisation. The Commitment Statement is accessible at: https://www.unepfi.org/wordpress/wp-content/uploads/2021/04/UNEP-FI-NZBA-Commitment-Statement.pdf.

111 MAS Media Release, New US$2 billion Investments Programme to Support Growth of Green Finance in Singapore (11 November 2019), accessible at https://www.mas.gov.sg/news/media-releases/2019/new-us$2-billion-investments-programme-to-support-growth-of-green-finance-in-singapore.

112 MAS Schemes and Initiatives, Sustainable Bond Grant Scheme, accessible at: https://www.mas.gov.sg/schemes-and-initiatives/sustainable-bond-grant-scheme.

113 MAS Media Release, MAS Launches World's First Grant Scheme to Support Green and Sustainability-Linked Loans (24 November 2020), accessible at: https://www.mas.gov.sg/news/media-releases/2020/mas-launches-worlds-first-grant-scheme-to-support-green-and-sustainability-linked-loans.

114 MAS Guidelines on Environmental Risk Management (Banks) (December 2020), accessible at: https://www.mas.gov.sg/-/media/MAS/Regulations-and-Financial-Stability/Regulations-Guidance-and-Licensing/Commercial-Banks/Regulations-Guidance-and-Licensing/Guidelines/Guidelines-on-Environmental-Risk---Banks/Guidelines-on-Environmental-Risk-Management-for-Banks.pdf.

115 MAS Guidelines on Environmental Risk Management (Insurers) (December 2020), accessible at: https://www.mas.gov.sg/-/media/MAS/Regulations-and-Financial-Stability/Regulations-Guidance-and-Licensing/Insurance/Regulations-Guidance-and-Licensing/Guidelines/Guidelines-on-Environmental-Risk-Management-Insurers.pdf.

116 MAS Guidelines on Environmental Risk Management (Asset Managers) (December 2020), accessible at: https://www.mas.gov.sg/-/media/MAS/Regulations-and-Financial-Stability/Regulations-Guidance-and-Licensing/Securities-Futures-and-Fund-Management/Regulations-Guidance-and-Licensing/Guidelines/Guidelines-on-Environmental-Risk-Management-for-Asset-Managers.pdf.

117 MAS International and Regional Collaborations, accessible at: https://www.mas.gov.sg/development/sustainable-finance/international-and-regional-collaborations.

The SGX also updated its Mainboard Rules in January 2022 to address the issue of sustainability, introducing mandatory obligations on listed companies in certain industries[118] to make climate-related disclosures consistent with the recommendations of the Task Force on Climate-Related Financial Disclosure[119] and obligations on directors of listed companies to undergo training on prescribed sustainability matters,[120] among other changes.

118 The mandatory disclosure requirements will apply to all listed companies in the financial industry, agriculture, food and forest products industry and energy industry from the financial year commencing 1 January 2023, and will apply to all listed companies in the materials and building industry and transportation industry from the financial year commencing 1 January 2024: Mainboard Rules, Practice Note 7.6 Sustainability Reporting Guide, at paragraph 4.9. These industries were selected as they have been identified by the Task Force on Climate-related Financial Disclosures as being most affected by climate change.

119 Mainboard Rules, r 711B(1)(aa).

120 *Idem*, r 720(7).

# SOUTH AFRICA

# 1. General overview of the restructuring regime

## 1.1 Formal restructuring procedures

The South African restructuring regime received an overhaul in 2011 with the promulgation of the new Companies Act.[1] Chapter 6 of the Companies Act introduced a new concept in South Africa known as "business rescue", while maintaining the mechanism available to a board of directors of a company or a company's liquidator to propose a compromise or other arrangement between a company and its creditors.[2]

### *1.1.1 Business rescue*

Business rescue is the eminent restructuring procedure in South Africa. It entails the appointment of a business rescue practitioner (BRP), a licensed professional who takes over management control of the financially distressed[3] company, but may delegate powers to existing management, and is tasked with developing, publishing and implementing a business rescue plan,[4] provided the plan is approved by the creditors (and sometimes shareholders) of the company.

Like many restructuring procedures around the world, under business rescue proceedings, a moratorium against enforcement action by creditors – except with the leave of the BRP or the court,[5] and with certain exceptions such as criminal proceedings against the company or its directors[6] or proceedings by a regulatory authority in the execution of its duties[7] – provides the distressed company with respite pending the publication of the business rescue plan.

Business rescue is intended to be a swift process, and strict timelines are provided in the Companies Act for the steps in the process to unfold. A financially distressed company may commence business rescue proceedings either by the adoption of a board resolution to that effect,[8] or upon application to the court[9] by an "affected person", being a creditor, shareholder, employee or trade union representing the company's employees.[10] When a company enters business rescue, affected persons must be given notice of the commencement of business rescue proceedings[11] and, if business rescue was initiated by a company resolution, the BRP must be appointed within five business days.

The BRP must, as soon as possible after his / her appointment, investigate the company's affairs, business, property and financial position, and having done so, consider whether there is a reasonable prospect of the company being rescued.[12] To rescue the company means to achieve the goals of business rescue as set out in the Companies Act, being to develop and implement a plan to restructure the company's affairs in a manner that maximises the likelihood of the company continuing in existence on a solvent basis or, if that is not possible, achieving a better return for the company's creditors or shareholders than would result from the immediate liquidation of the company.[13] Should the BRP conclude at any time during business rescue proceedings that there is no longer a reasonable prospect of the company being rescued, the practitioner must inform the

1 Act 71 of 2008.
2 Companies Act, s 155. Prior to the new Act, a company could propose a compromise in terms of s 311, Act 61 of 1973.
3 *Idem,* s 128(1)(f) provides that for a company to be "financially distressed", it must appear to be reasonably unlikely that it will be able to pay all of its debts as they become due in the ensuing six months or alternatively it must appear that the company will become insolvent in the ensuing six months.
4 *Idem,* s 140(1)(d).
5 *Idem,* s 133.
6 *Idem,* s 133(1)(d).
7 *Idem,* s 133(1)(f).
8 *Idem,* s 129.
9 *Idem,* s 131.
10 See the definition of "affected person" in the Companies Act, s 128(1)(a).
11 *Idem*, ss 129(3), 131(8)(b).
12 *Idem,* s 141(1).
13 *Idem*, s 128(1)(h), read with s 128(1)(b).

court, the company and all affected persons and apply to the court to place the company in liquidation.[14]

At the first meetings of creditors and employees' representatives, both of which must be held within 10 business days of the BRP's appointment, the BRP must, among other things, inform creditors and employees respectively whether he / she believes there is a reasonable prospect of rescuing the company.[15] The creditors and employees may then determine whether a creditors' committee and employees' committee should be appointed.[16]

Arguably, the BRP's most important duty in business rescue is the development and publication of the business rescue plan, which must be done after engagement with affected persons and must detail how the company is to be rescued and how its debts are to be restructured. The business rescue plan is required to be published within 25 business days after the BRP's appointment or such longer time as may be allowed by the court, on application by the company or by the holders of a majority of the creditors' voting interests.[17] More often than not, the BRP will obtain creditors' approval to extend the time period for publication of the business rescue plan.

The business rescue plan must contain certain prescribed background information[18] and must also contain the restructuring proposal setting out, among other things, the extent to which the company is to be released from the payment of its debts, the ongoing role of the company, the order of preference in which creditors are to be paid and the benefits of adopting the business rescue plan as opposed to if the company were to be placed in liquidation.[19] The Companies Act is not prescriptive as to the types of restructuring proposals that may be made in a business rescue plan, and plans may provide for, among other things, proposals to compromise creditors' claims, the sale of the company's business, the purchase creditors' claims by a new investor, the conversion debt to equity, or a combination of these and more.

Within 10 business days after publishing the business rescue plan, the BRP must hold a meeting of creditors and shareholders, if applicable, to consider and vote on the plan.[20] For the business rescue plan to be adopted, at least 50% of the non-related creditors and at least 75% of all the creditors attending the meeting must vote in favour of the adoption of the business rescue plan.[21] Importantly, creditors do not vote in separate classes and all creditors, save for subordinated creditors, have a voting interest equal to the value of the amount owed to that creditor by the company.[22] Should the plan alter the rights of shareholders, it must be approved by a majority of each affected class of shareholders who vote.[23] Once the business rescue plan has been adopted, it becomes legally binding on all creditors and shareholders, whether or not they attended the meeting to consider the business rescue plan, including those that voted against the business rescue plan.[24] It is not a requirement that the business rescue plan be approved by a court.

During business rescue proceedings, the BRP has the power to suspend, and apply to the court to cancel, certain contractual obligations of the company,[25] although a BRP may not suspend any provisions of employment contracts. This is an example of the protection provided to employees during business rescue proceedings. Employees' claims that become due and payable during the company's business rescue proceedings rank ahead of all other unsecured claims against the

14 *Idem*, s 141(2)(a).
15 *Idem*, ss 147(1)(a)(i), 148(1)(a).
16 *Idem*, ss 147(1)(b), 148(1)(b).
17 *Idem*, s 150(5).
18 *Idem*, s 150(2)(a) – this includes an asset list, which indicates the assets subject to creditors' security, a list of creditors indicating which creditors are secured, preferent or concurrent in terms of the laws of insolvency and, importantly, a probable dividend that would be received by creditors in their specific classes if the company were to be placed in liquidation.
19 *Idem*, s 150(2)(b).
20 *Idem*, s 151(1).
21 *Idem*, s 151(2).
22 *Idem*, s 145(4).
23 *Idem*, s 152(3)(c).
24 *Idem*, s 152(4).
25 *Idem*, s 136(2).

company, save for the BRP's remuneration and costs.[26] The Labour Appeal Court has also ruled that a company in business rescue may only start retrenchment proceedings upon the publication of the business rescue plan,[27] which underlines the elevated status of employees in business rescue.

Employees' claims are the most explicitly protected in business rescue and, although there are no other substantial restrictions imposed by the Companies Act on the types of claims that may be restructured, other pieces of legislation dealing with, for instance, mining,[28] prevent a company from restructuring certain claims and continuing to trade. We will consider this in greater detail in the sections below.

Under business rescue proceedings, no distinction is drawn in voting or ranking between unsecured creditors who would have preferred claims under insolvency proceedings[29] in terms of the Insolvency Act.[30] The only preferences under business rescue are provided in respect of business rescue costs, employees and providers of post-commencement finance. Despite this, creditors who would under insolvency proceedings, for instance, have their claims settled as a first charge upon the realisation of certain property, would be afforded the same preference under business rescue proceedings.[31]

### 1.1.2 *Compromise or arrangement with creditors*

Section 155 of the Companies Act provides for a company to enter into a compromise or arrangement with its creditors, which may be proposed either by the company's board of directors or by the company's liquidator, should it be in liquidation.

Under the section 155 procedure, the company's existing management remains in control of the company, unless it is in liquidation, in which case the liquidator(s) will have taken control of the company's assets. The section 155 procedure is therefore akin to certain "debtor in possession" procedures in other jurisdictions around the world.

The procedure under section 155 entails the publication of a proposal to creditors (the section 155 arrangement) which must contain substantially the same prescribed background information as a business rescue plan, along with the restructuring proposal to be voted on by creditors of the company. The section 155 arrangement may propose that a debt moratorium be imposed,[32] but unlike business rescue, it is not automatic.

At the meeting of creditors to consider the proposal, creditors must vote, and if it is supported by a majority in number, representing at least 75% in value, of the creditors or class of creditors at the meeting, it will be deemed to have been approved by creditors.[33] An important distinction between the section 155 arrangement and a business rescue plan is that for a section 155 arrangement, creditors must vote in separate classes and the proposal must be adopted by each class of creditors whose rights are affected by the proposal.[34]

Once the proposal is adopted by creditors, the company may apply to the court for an order approving the proposal and the court may sanction the compromise or arrangement as set out in the adopted proposal if it considers it just and equitable to do so.[35] When deciding whether to

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26 *Idem*, ss 135(1), 135(3).
27 *South African Airways (SOC) Ltd and Others v National Union of Metalworkers of South Africa obo Members and Others* 2021 (2) SA 260 (LAC).
28 Mineral and Petroleum Resources Development Act 28 of 2002.
29 *Commissioner, South African Revenue Service v Beginsel NO and Others* 2013 (1) SA 307 (WCC).
30 Act 24 of 1936.
31 A business rescue plan which unfairly disadvantages certain creditors may be set aside. There is no reported case law on this being done, but in *Tyre Corporation Cape Town (Pty) Ltd and Others v GT Logistics (Pty) Ltd (Esterhuizen and Another Intervening)* 2017 (3) SA 74 (WCC) the court refused to grant an order to place a company in business rescue on the basis that its proposed business rescue plan was "fundamentally unfair and objectionable".
32 Companies Act, s 155(3)(b)(i).
33 *Idem*, s 155(6).
34 *Ibid*.
35 *Idem*, s 155(7)(b).

sanction the proposal, the court has a broad discretion which must be exercised with reference to the particular circumstances of the case.[36] If the company is in liquidation, the order may further provide for the discharge of the company's liquidation proceedings. The adopted proposal only becomes final and binding on all of the company's creditors or on the members of the relevant classes of creditors on the date that the court order sanctioning the proposal is filed with the Companies and Intellectual Property Commission.[37]

Section 155 provides explicitly that only "financial" obligations towards creditors of the company may be restructured.[38] Apart from this, no additional restrictions are imposed by section 155 in terms of what types of claims may be restructured. As mentioned above in relation to business rescue, there are certain types of statutory claims that practically cannot be restructured, as doing so would affect the business's ability to continue to trade. We will consider these in greater detail below.

### 2.4 Informal restructuring procedures

Apart from the formal procedures provided in legislation, a company may opt for an informal restructuring by agreement with its creditors, whereby the company's management remains in control of the company and engages with and enters into agreements with its creditors on an individual basis.

The Companies Act provides that, should the board of a company have reasonable grounds to believe the company is financially distressed, it must either file for business rescue or it must provide each affected person with a written notice indicating the company is financially distressed and the company's reasons for not entering into business rescue.[39] This is a major impediment for informal restructurings as it means that they must take place before the company is in financial distress, unless the company informs each of its creditors that it is in fact in financial distress which, barring extraordinary circumstances, no company would choose to do.

However, should a prudent board of a company act early, before the company is in financial distress, informal restructurings are of value as they are comparatively inexpensive and bring less of a reputational risk to the company.

Informal restructurings are by their nature more flexible. As such, there are no formal requirements as to information that ought to be shared by the company, save for the general requirements under the Companies Act[40] and the Promotion of Access to Information Act[41] with regards to access to company records for members of the public. In addition, the board of the directors of a company remain bound by any contractual obligations of the company such as shareholders' agreements as well as by the company's memorandum of incorporation, which may provide additional information rights to any person, but no such right may negate or diminish any mandatory protection of any record under the Promotion of Access to Information Act. Ultimately, however, it is more likely that creditors will agree to any sort of restructuring if the company shares all relevant information with creditors in informal restructuring discussions.

Because an informal restructuring is done entirely by agreement and there is no "cram down" on dissenting creditors, they generally do not require approval by a court or another statutory authority. However, claims by statutory authorities against a company, such as claims for tax and

36 *Ex Parte De Villiers and Another NNO: In Re Carbon Developments (Pty) Ltd (in liquidation)* 1993 (1) SA 493 (A) 508. This decision was in relation to a scheme of arrangement under s 311 of the Companies Act 61 of 1973, which was repealed by the Companies Act 2008.

37 Companies Act, s 155(8)(c) read with the definition of "file" in s 1.

38 *Idem*, s 155(2).

39 *Idem*, s 129(7).

40 Section 26(2) provides that a person may inspect or copy the securities and/or directors' register of a profit company and the members' register of a non-profit company upon the payment of prescribed maximum fee.

41 Act 2 of 2000, which provides in s 50(1) that a person may request access to a company's records if that record is required for the exercise or protection of their rights. In terms of s 68(1), the company may refuse such a request if, among other things, the disclosure of the record would be likely to cause harm to the commercial or financial interests of the company.

statutory fines, would, of course, necessarily require the relevant authority's approval in order to be restructured.

## 2. Restructuring of ESG-related liabilities

### 2.1 Environmental (E): restructuring environmental liabilities

South Africa's Bill of Rights[42] contains a specific provision on the environment,[43] which demonstrates the extent to which, at least in theory, environmental rights are protected in South Africa under its post-apartheid Constitutional dispensation. Despite this, environmental liabilities are not specially protected or elevated under South Africa's restructuring and insolvency laws. Nonetheless, South Africa's environmental legislation does impose certain practical restrictions on the restructuring of environmental liabilities and, given that South Africa's public policy is infused with an elevated respect for the environment since the promulgation of its Constitution in 1996, the common law may yet develop to impose more explicit restrictions on dealing with environmental obligations during restructuring procedures.

#### *2.1.1 Types of environmental liabilities*

Environmental liabilities in South Africa include:

- civil claims, being legal claims grounded in the private law spheres of contract[44] and delict;[45]
- statutory liabilities imposed in terms of environmental legislation, such as:
  - fines. For instance, sections 34(1) to (3) of the National Environmental Management Act[46] (NEMA) provide that a court may award damages, compensation or a fine equal to the cost incurred or likely to be incurred by an organ of state in rehabilitating the environment or preventing damage to the environment against an offender, with the court's order to have the same force and effect as if it had been given in a civil action;
  - rehabilitation obligations. For example, the Mineral and Petroleum Resources Development Act[47] (MPRDA) imposes various obligations on holders of mining rights and permits to give effect to general objectives under the NEMA and specifically to remedy any environmental damages resulting from mining operations. Any applicant for an environmental authorisation relating to prospecting, exploration or mining must provide financial provision for the rehabilitation, closure and ongoing post-decommissioning management of negative environmental impacts;[48] and
- constitutional remedies for the breach of environmental rights contained in the Bill of Rights.[49]

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42 Chapter 2 of the Constitution of the Republic of South Africa 1996.

43 Section 24 of the Constitution provides that everyone has the right "to an environment that is not harmful to their health or well-being; and to have the environment protected".

44 For instance, a tenant under a lease agreement may be contractually obliged to comply with environmental or mining legislation, including rehabilitation obligations.

45 A party may be sued for its environmental law breaches under the law of delict which claim may be based on the delict of private nuisance, which occurs when a person interferes with an owner or lawful occupier's use and enjoyment of land. In light of s 24 of the Constitution, the common law may develop delictual claims flowing from breaches of this section of the Constitution (Kidd, *Environmental Law in South Africa*, 26.3.5). Section 28(1) of the National Environmental Management Act 107 of 1998 imposes a general duty of care upon every person to take reasonable measures to prevent pollution or degradation of the environment.

46 Act 107 of 1998.

47 Act 28 of 2002.

48 Section 24P of the NEMA.

49 See *Hichange Investments (Pty) Ltd v Cape Produce Co (Pty) Ltd t/a Pelts Products and Others* 2004 (2) SA 393 (E).

There is no direct restriction on the treatment of environmental liabilities under the restructuring procedures in Chapter 6 of the Companies Act, nor does the Insolvency Act[50] provide for specific preferences in respect of environmental claims.

However, where a company attempts to compromise its financial obligations under the MPRDA, its mining or prospecting right may be revoked due to the company's contravention of the terms and conditions of the mining right.[51] The practical implication is that a mining company will have great difficulty in continuing to trade should it attempt to compromise its environmental obligations.

### *2.1.2 Priority given to environmental liabilities*

As already mentioned, there are no explicit limitations on the extent to which a restructuring proposal[52] may compromise or restructure historic environmental liabilities. Statutory fines against a company in liquidation or business rescue are mere unsecured claims and rank concurrent with other pre-liquidation or pre-business rescue debts.

Although environmental liabilities are not specifically preferred in terms of the Insolvency Act or the Companies Act,[53] there are certain instances where such liabilities will have a preference or will even be secured.[54] Where liabilities would under insolvency proceedings be settled as a first charge upon the realisation of certain property, those claims would likely, although not necessarily, be afforded the same preference under a business rescue plan or section 155 arrangement. Examples of this include:

- in insolvency proceedings, the costs of maintaining, conserving and realising any encumbered assets, including immovable property, are secured by the proceeds of that property.[55] It is conceivable that these costs may include rehabilitation costs under the NEMA or the MPRDA;[56]

- environmental liabilities that are secured by real property. For instance, if the financial provision for rehabilitation is provided in the form of a guarantee from a financial institution, that guarantor may register a mortgage over the property concerned; or

- the liabilities may become preferred claims where a company under business rescue has ongoing post-commencement remediation obligations and the costs thereof may be seen as post-commencement finance and therefore rank ahead of unsecured claims,[57] or such costs may be specifically preferred in a business rescue plan post-business rescue as they could be seen to be critical costs for the company's survival.

### *2.1.3 Disclaimer of environmental obligations*

Unlike various other jurisdictions, liquidators in South Africa do not have the ability to disclaim onerous property. Thus, in situations where an immovable property has ongoing onerous environmental obligations, it can have the result that no party is willing to purchase the property and the company under liquidation is not able to fulfil the environmental obligations imposed by statute. As argued by Stander,[58] this is an area of South African insolvency law that perhaps

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50 Act 24 of 1936.
51 Section 47(1) of the MPRDA.
52 A business rescue plan or s 155 arrangement.
53 Section 99 of the Insolvency Act provides for preferences in respect of certain statutory obligations which do not include any environmental obligations.
54 A "restructuring proposal" refers to either a business rescue plan or s 155 arrangement.
55 Section 89(1) of the Insolvency Act. *De Wet en Andere NNO v Stadsraad van Verwoerdburg* 1978 (2) SA 86 (T) at 101E-F provides that there is not an exhaustive list of costs that fall under this section.
56 See L Stander, "The Claim Against an Insolvent for Environmental Damage" in P Omar (ed) *International Insolvency Law: Themes and Perspectives* (2008) 350-351 in which Stander argues that such environmental claims should be secured by a charge on immovable property to which it relates.
57 In terms of s 135(2) of the Companies Act.
58 See above, n 56; see also A Stander, *Die Opskorting van Omgewingsgedinge in Insolvensie* (2014) 3 Stell LR; A Stander, *Enkele Relevante Aspekte ten opsigte van Risko's waar Maatskappye Aanspreeklik is vir Omgewingsbenadeling* (2012) 24 SA Merc LJ 148-176.

requires reform as it may leave a company in a position where it owns an economically valueless asset with continually accruing environmental obligations, which ultimately is detrimental to the environment.

Section 136(2) of the Companies Act allows a BRP to suspend contractual obligations of a company which may become due during its business rescue proceedings and also allows the BRP to apply to the court to permanently cancel contractual obligations. This only applies to business rescue proceedings and not the compromise procedure under section 155 of the Companies Act.

A question that may arise, and which has not been considered by our courts in reported judgments, is whether a BRP may suspend or cancel a company's contractual obligations to fulfil a third party's statutory environmental obligation. The fact that South Africa's Bill of Rights contains explicit environmental rights suggests that public policy considerations may weigh heavily against the BRPs powers under section 136(2) where environmental rights are threatened.

Under the MPRDA, any disposal of a mining right is subject to the consent of the Minister.[59] Whether a business rescue practitioner may alienate a mining right and compromise outstanding obligations relating to the right is yet to be decided in a reported case.

## 2.2 Social (S): restructuring health or safety-related liabilities

Similar to environmental obligations, there are no specific restrictions on the restructuring of health or safety-related liabilities, subject to certain exceptions which we consider below.

### *2.2.1 Types of health and safety-related liabilities*

Health or safety-related liabilities in South Africa include:

- civil claims, being legal claims grounded in the private law spheres of contract[60] and delict;[61] and
- statutory liabilities imposed in terms of health and safety-related legislation, such as:
  - fines. For instance, fines may be imposed under the Occupational Health and Safety Act[62] (OHSA) on employers who fail to sufficiently provide for employees' health and safety as required in terms of the OHSA, while the Meat Safety Act[63] imposes fines on parties who fail to comply with essential national standards[64] relating to, for instance, hygiene management practices, and the Compensation for Occupational Injuries and Diseases Act[65] (COIDA) provides that the Director-General may impose fines on employers[66] who do not report accidents suffered by employees up to the amount of compensation claimed by the employee from the Compensation Fund;[67] and

59 MPRDA, s 11.
60 For example, a party that supplies unsafe goods may breach the express terms of a sale agreement or, in the context of a consumer agreement, may breach the implied warranty of quality provided for in s 56(2) of the Consumer Protection Act 68 of 2008.
61 A manufacturer may be held liable for harm caused by defective manufacture of a product where the manufacturer is at fault. In *Wagener v Pharmacare Ltd* [2003] 2 All SA 167 (SCA), it was confirmed that fault (negligence or intent) must be proven on the part of the manufacturer. However, where a consumer suffers harm as a result of goods, s 61 of the Consumer Protection Act 68 of 2008 provides for strict liability on the part of the producer, importer, distributor or retailer, in other words no negligence needs to be proven when the Consumer Protection Act applies.
62 Section 38, Act 85 of 1993.
63 Act 40 of 2000.
64 *Idem*, s 19(1)(d).
65 Act 130 of 1993.
66 *Idem*, s 39(9).
67 The Compensation Fund is established in terms of s 15 of the COIDA to provide compensation to employees who suffer injuries, diseases or death during the course and scope of their employment.

- compliance directives. An inspector under the OHSA may, for instance, direct employers to take steps to safeguard the health or safety at any person at a workplace[68] and a failure to comply will result in a fine referred to above.

### *2.2.2 Treatment of health and safety-related liabilities*

The Insolvency Act provides for a preference in respect of certain statutory health and safety-related obligations under liquidation proceedings. In particular:

- all amounts which were due by the insolvent company to the Compensation Commissioner in terms of the COIDA immediately prior to the liquidation of the company.[69] This includes fines and assessments[70] imposed by the Compensation Commissioner; and

- all amounts which were due by the insolvent company to the Mines and Works Compensation Fund, established in terms of the Occupational Diseases in Mines and Works Act.[71]

Under insolvency proceedings, the above liabilities rank behind a portion of employees' claims. Although not required to do so, a restructuring proposal in terms of Chapter 6 may also provide for the above preferences, or at least would provide that the above creditors receive a dividend that is equal to or better than the expected outcome in a liquidation.

In addition to the above statutory preferences under a liquidation, other instances where health and safety-related liabilities may enjoy a preference under restructuring proceedings include:

- health and safety-related liabilities that are secured by real property; and

- the liabilities may become preferred claims in situations where, for instance, a liability is incurred during a company's business rescue proceedings, with the effect that it will be seen as post-commencement finance and therefore rank ahead of unsecured claims.[72]

## 2.3 Governance (G): third party releases in favour of directors and officers of the company

There is nothing *per se* preventing a business rescue plan or a section 155 arrangement from providing for releases of third parties, and directors and officers of the company in particular. We will consider business rescue plans and section 155 arrangements separately.

### *2.3.1 Third party releases in a business rescue plan*

It is often stated that the provisions of Chapter 6 are not prescriptive as to the types of proposals that a business rescue plan may contain[73] and, in principle, as long as the plan is adopted by the requisite majority of creditors (and shareholders if applicable), it becomes binding on the company, creditors and shareholders.

Unlike under a section 155 arrangement, the Companies Act does not specify whether a business rescue plan affects the liability of sureties of the company, and it has yet to be decisively held whether a business rescue plan which is adopted and provides for third party suretyships to be restructured is binding on sureties.[74]

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68 OHSA, s 30.
69 Section 99(1)(a) of the Insolvency Act refers to the repealed Workmen's Compensation Act 30 of 1941, which was repealed in terms of s 100(1) of the COIDA. In terms of s 12(1) of the Interpretation Act 33 of 1957, a reference to the repealed act must be interpreted as a reference to the corresponding re-enacting provisions of the substituting act.
70 In terms of s 83 of the COIDA.
71 Act 78 of 1973. Section 99(1)(c) refers to the Pneumoconiosis Compensation Act 64 of 1962, which was repealed in terms of s 136 read with the Schedule of Act 78 of 1973.
72 In terms of s 135(2) of the Companies Act.
73 Commentary on s 150 of the Companies Act contained in *Henochsberg on the Companies Act 2008*.
74 In *Tuning Fork (Pty) Ltd t/a Balanced Audio v Greeff and another* 2014 (4) SA 521 (WCC), the court indicated that the restructuring of principal obligations under a business rescue plan will result in the

Whether a business rescue plan may provide for the release of directors' and officers' liability for non-contractual claims such as claims for negligence, claims for the breach of directors' fiduciary duties and claims for trading under insolvent circumstances is a separate question and one which has not been decided in reported judgments.

There is nothing in Chapter 6 preventing a business rescue plan from allowing the restructuring of potential non-contractual obligations of directors towards creditors, but one may conceive of circumstances in which an aggrieved creditor may successfully apply to have a business rescue plan set aside even if it is adopted by the requisite majority of creditors in value where it is contrary to public policy or the Constitution.[75]

### *2.3.2 Third party releases in a section 155 arrangement*

Section 155(9) of the Companies Act provides specifically that an arrangement or compromise in terms of section 155 does not affect the liability of any person that is a surety of the company. As mentioned above, this contrasts with the provisions relating to business rescue, which do not specifically prevent sureties' liabilities being restructured. This suggests that there is a greater restriction on the restructuring of third party liabilities under a section 155 arrangement than under a business rescue plan.

There is substantial case law in which courts have contemplated the meaning of "arrangement" and "compromise" under the Companies Act 1973,[76] and because these terms are not defined in the Companies Act, the interpretation by the courts of these terms, albeit under the previous Companies Act provisions, remain of value, if not binding.[77]

It has been held that an "arrangement" refers to something wider than a "compromise"[78] and that there is not a limitation to what an arrangement can entail except that it cannot achieve something contrary to the general law or be entirely *ultra vires* the company.[79] Should the requisite majority of creditors agree thereto, the courts have held that there is nothing *per se* preventing the discharge of third party obligations under an arrangement,[80] albeit in respect of arrangements under the Companies Act 1973.

The court retains a discretion to sanction or refuse to sanction a section 155 arrangement[81] and its decision may be guided not only by whether the requisite majorities of creditors voted for the arrangement, but also by considerations of public policy.[82] In *Mahomed v Kazi's Agencies (Pty) Ltd*,[83] the court went as far as to state that "the court ought not to sanction a compromise where the probable result of such a course will be to allow evil-doers to go unpunished".

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accessory obligations being similarly restructured. In *New Port Finance Company (Pty) Ltd and another v Nedbank Limited* [2015] 2 All SA 1 (SCA), the court held that, on those particular facts, the validity of the debts under the deeds of suretyship were not affected by the restructuring of the company's obligations in terms of a business rescue plan.

75 See also *Tyre Corporation Cape Town (Pty) Ltd and Others v GT Logistics (Pty) Ltd (Esterhuizen and Another Intervening)* 2017 (3) SA 74 (WCC), in which a court refused to grant an order to place a company in business rescue on the basis that tis proposed business rescue plan was "fundamentally unfair and objectionable".

76 Section 311 of the Companies Act 61 of 1973 dealt with creditor schemes of arrangement and was repealed by the Companies Act 71 of 2008.

77 H Klopper and R Bradstreet, "Averting Liquidations with Business Rescue: Does a Section 155 Compromise Place the Bar Too High?" (2014) 3 Stell LR 551.

78 *Ex Parte Cyrildene Heights (Pty) Ltd* 1966 (1) SA 307 (W) at 308.

79 *Idem*, 309.

80 *Idem*, 310; *Du Preez and Another v Garber: In re Die Boerebank Bpk* 1963 (1) SA 806 (W) at 812.

81 Companies Act, s 155(7)(b) provides that the court may sanction the proposal "if it considers it just and equitable to do so".

82 Commentary on s 155 of the Companies Act contained in *Henochsberg on the Companies Act, 2008*. In *Ex Party Chenille Corporation of SA (Pty) Ltd and another: In Re Chenille Industries (Pty) Ltd* 1962 (4) SA 456 (T) at 465, the court held that "if it appears that directors … have done any wrong to the company for which compensation could or might be recovered … then the court, in the interests of the public, and commercial morality, should weigh that as one of the factors justifying rejection of the compromise."

83 1949 (1) SA 1162 (N), 1171.

This indicates that although in principle a section 155 arrangement may provide for third party releases, a court retains a broad discretion to refuse to sanction the arrangement and the release of third parties should the court find that it is not just and equitable in the circumstances.

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

#### *3.1.1 Approving a restructuring plan*

There is no requirement that a restructuring proposal be approved by any environmental authorities. A business rescue plan only needs to be approved by creditors (and shareholders in certain instances), while a section 155 arrangement must be approved by creditors and sanctioned by a court in order to be binding on all creditors.

#### *3.1.2 Discretion to consider wider public interest concerns*

There is nothing preventing a business rescue practitioner from considering broader public interest concerns in a business rescue plan of a company, including environmental concerns.

The Companies Act aims to "provide for the efficient rescue and recovery of financially distressed companies, in a manner that balances the rights and interests of all relevant stakeholders".[84] In certain instances, it could be argued that relevant stakeholders would include environmental authorities. Ultimately, however, it is up to the creditors to adopt or reject a business rescue plan and, as long as the plan sufficiently provides for their interests, it is likely that environmental concerns will not be a determining factor. It is conceivable that an environmental authority could successfully apply to the court to set aside a business rescue plan if it does not sufficiently provide for the fulfilment of a company's obligations under environmental legislation, although this has not been done before.

When deciding whether to sanction a section 155 arrangement, the court does have the discretion to consider wider public interest concerns[85] and retains a broad discretion to refuse to sanction an arrangement if, in the particular circumstances, it is not just and equitable to do so. Although no precedent exists where a court has refused to sanction an arrangement based on environmental concerns, there is nothing preventing a court from environmental concerns into account when considering whether to sanction an arrangement.

#### *3.1.3 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

No formal provision is made for environmental authorities or advocacy groups to participate in a restructuring. It is up to a BRP's discretion whether to engage with such groups, but there is no statutory obligation for him / her to do so.

As mentioned in section 2 above, in instances where mining rights or licenses are owned by a company under business rescue, the Minister's consent is required in order to alienate any mining right or license and in this way the Minister may indirectly influence the proposals contained in a business rescue plan or under a section 155 arrangement should the arrangement contemplate the disposal of mining rights.

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84 Companies Act, s 7(k).

85 *Ex Party Chenille Corporation of SA (Pty) Ltd and another: In Re Chenille Industries (Pty) Ltd* 1962 (4) SA 456 (T)

### 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

#### *3.2.1 Approving a restructuring plan*

Although employees and trade unions have substantial rights to participate in the business rescue proceedings and in the development of the proposed business rescue plan,[86] employees and trade unions can only vote to approve the business rescue plan to the extent they are creditors of the company.[87]

In respect of a section 155 arrangement, employees will be required to vote in their own class if the arrangement is going to alter their rights in any way. Employees therefore have the ability to approve or reject a proposal under section 155 in these circumstances.

#### *3.2.2 Discretion to consider wider public interest concerns*

Should a business rescue plan fail to correctly provide for the statutory preference in respect of employees' claims under business rescue,[88] or should the business rescue plan infringe upon employees' statutory rights in any other way,[89] employees may apply to court for the business rescue plan to be amended or set aside.[90]

#### *3.2.3 Protection of employee rights*

An often-stated policy goal of business rescue is the preservation of employment opportunities, and this is reflected in the substantial rights afforded to employees under the business rescue provisions in Chapter 6 of the Companies Act.

Among the rights explicitly provided for in Chapter 6 for employees and trade unions representing employees during the business rescue process are:

- to receive notice of the commencement of business rescue proceedings, and the appointment of the BRP;[91]
- to receive notice of each court proceeding, decision, meeting or other relevant event concerning the business rescue proceedings;[92]
- to participate in any court proceedings arising during the business rescue proceedings;
- to form a committee of employees' representatives,[93] which:[94]
    - may consult with the BRP about matters relating to the business rescue proceedings, but may not direct or instruct the BRP;
    - may, on behalf of employees, receive and consider reports relating to the business rescue proceedings; and

86 We consider these rights in greater detail below.
87 Companies Act, s 144(3)(f).
88 As provided for in ss 135(1) and 144(2) of the Companies Act.
89 Section 5(4)(b)(i)(bb) of the Companies Act states that the provisions of the Labour Relations Act 66 of 1995 (LRA) prevail in the case of an inconsistency between the LRA and the Companies Act.
90 See the (non-binding) decision of Justice LTC Harms in the dispute resolution proceedings between the *Airline Pilots' Association of South Africa and South African Airways SOC Ltd (in business rescue)* (7 May 2021), where the arbitrator held that a business rescue plan which derogates from the preferences for employees' claims provided for in Chapter 6 is *ultra vires*.
91 Companies Act, ss 129(3), 129(4).
92 *Idem*, s 144(3)(a).
93 *Idem*, s 144(3)(c).
94 *Idem*, s 149(1).

- must act independently of the BRP to ensure fair and unbiased representation of the employees' interests;

- to be consulted by the BRP during the development of the business rescue plan;[95]
- to make submissions at the meeting where the business rescue plan is to be considered and voted on by creditors;[96] and
- if a proposed business rescue plan is rejected, employees may also propose the development of an alternative plan.[97]

Employees' claims that become due during the business rescue proceedings rank ahead of all other unsecured claims against the company, save for business rescue costs,[98] while employees' claims that became due before the company's business rescue proceedings are also given priority and rank ahead of all pre-commencement unsecured claims.[99]

The Companies Act provides that the Labour Relations Act (LRA) prevails where there is a conflict between the provisions of these Acts[100] and therefore employees' rights remain fully protected during the business rescue process. In fact, it could be said that employees have more rights under business rescue than they do outside of business rescue, as the Labour Appeal Court has ruled that a BRP may not commence any retrenchment procedures before a business rescue plan is published.[101]

## 3.3 Governance (G): board / management conflicts addressed in a restructuring

### *3.3.1 Business rescue proceedings*

When a company is placed under business rescue, the BRP takes over full management control of the company in substitution for its board and pre-existing management.[102]

The existing directors of a company are not provided with any rights to participate in the company's business rescue proceedings except to the extent that the BRP may delegate functions to them. The directors are not included among "affected persons" and, to the extent they may be creditors of the company, they are not considered to be "independent" creditors. Directors therefore do not have a say in the formulation of the business rescue plan, except to the extent that the BRP may allow in his / her discretion, and directors can never have a deciding vote in the approval of the business rescue plan.

In theory, this should limit the possibility of board conflicts during business rescue, subject to one important proviso. Because the board of directors may initially place the company in business rescue and appoint the BRP, there is always a risk that the BRP may be a puppet of the board of directors, or even if not explicitly so, the BRP may feel a degree of loyalty towards the persons who appointed him / her and therefore may be less inclined to take tough actions against them.

Ostensibly to address this risk, it is a requirement that the BRP who is appointed does not have any relationship with the company that may lead a reasonable and informed third party to question the integrity, impartiality or objectivity of the BRP.[103] Furthermore, any affected person may apply to

95 *Idem*, s 144(3)(d).
96 *Idem*, s 144(3)(e), read with s 152(1)(c).
97 *Idem*, s 144(3)(g)(i).
98 *Idem*, s 135(1).
99 *Idem*, s 144(2).
100 *Idem*, s 5(4)(b)(i)(bb).
101 *South African Airways SOC Ltd (in business rescue) and others v National Union of Metalworkers and others* 2021 (2) SA 260 (LAC).
102 Companies Act, s 140(1)(a).
103 *Idem,* s 138(1)(e).

court to remove the BRP should this requirement not be met,[104] or alternatively on the basis of a conflict of interest or lack of independence of the BRP.[105]

### *3.3.2 Section 155 arrangement*

Because a section 155 arrangement may be proposed by the company's board of directors, it is possible that the board may attempt to favour themselves to the detriment of creditors or third parties. Generally, directors have a fiduciary duty towards the company, must act in the company's best interests and may not use their position as director to gain an advantage for themselves or a third party.[106] Directors may be held liable for losses suffered by the company due to the director failing to adhere to the required standards of conduct.[107] These provisions of course remain applicable when the board of a company makes a proposal in terms of section 155.

The background information that is required to be included in the proposal[108] ought to give creditors enough information to make an informed decision whether to vote for or against the proposal. Furthermore, should an arrangement be approved by creditors, as has been discussed above, a court still retains a broad discretion to refuse to sanction the arrangement should it not be "just and equitable" to do so, and in exercising such discretion may consider the public interest and "commercial morality".[109]

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

There are not any industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

As mentioned in the previous section, employees' rights under business rescue are well protected in terms of the provisions of Chapter 6 of the Companies Act and all employees' rights under the LRA remain in place.

The LRA provides for the National Economic Development and Labour Council to issue codes of good practice on particular employment law issues and those codes must be taken into account when interpreting the LRA.

The code that is most relevant to restructuring is the Code of Good Practice: Dismissal Based on Operational Requirements,[110] which provides guidelines to employers for the correct procedural and substantive requirements in order to carry out dismissals based on operational requirements (i.e. retrenchments).

The Code provides the following guidelines for retrenchments:

- because retrenchment is a "no fault" dismissal and because of its human cost, the LRA places particular obligations on an employer, most of which are directed towards ensuring that all possible alternatives to dismissal are explored and that the employees to be dismissed are treated fairly;

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104 *Idem*, s 139(2)(d).
105 *Idem*, s 139(2)(e).
106 Section 76 of the Companies Act sets out the standards of directors' conduct.
107 Companies Act, s 77.
108 *Idem*, s 155(3)(a).
109 *Ex Party Chenille Corporation of SA (Pty) Ltd and another: In Re Chenille Industries (Pty) Ltd* 1962 (4) SA 456 (T), 465.
110 GN 1517 of 16 July 1999: Notice of code of good practice on dismissal based on operational requirements.

- the obligations placed on an employer are both procedural and substantive. The purpose of consultation is to enable the parties, in the form of a joint problem-solving exercise, to strive for consensus if that is possible. The matters on which consultation is necessary are listed in section 189(2).[111] In order for this to be effective, the consultation process must commence as soon as a reduction of the workforce, through retrenchments or redundancies, is contemplated by the employer, so that possible alternatives can be explored.[112] The employer should in good faith keep an open mind throughout and seriously consider any proposals put forward;

- the LRA provides for the disclosure by the employer of information on matters relevant to the consultation. Although the matters on which information must be disclosed are specified in section 189(3),[113] the list in that section is not a closed one. If considerations other than those that are listed are relevant to the proposed dismissal or the development of alternative proposals, they should be disclosed by the consulting party. In the event of a disagreement about what information is to be disclosed, any party may refer the dispute to the Commission for Conciliation Mediation and Arbitration;[114]

- the period over which consultation should extend is not defined in the LRA and what is a reasonable period will be determined with reference to the particular circumstances. Proper consultation will include:

    - the opportunity to meet and report back to employees;

    - the opportunity to meet with the employer; and

    - the request, receipt and consideration of information;

- if one or more employees are to be selected for dismissal from a number of employees, the LRA requires that the criteria for their selection must be either agreed with the consulting parties or, if no criteria have been agreed, be fair and objective. Therefore, the various codes of good practice promulgated under section 203(2) of the LRA code of are protected;

- criteria that infringe a fundamental right protected by the LRA when they are applied can never be fair. These include selection on the basis of union membership or activity, pregnancy or some other unfair discriminatory ground. Criteria that are neutral on the face of it should be carefully examined to ensure that when they are applied, they do not have a discriminatory effect. For example, to select only part-time workers for retrenchment might discriminate against women, since women are predominantly employed in part-time work;

- selection criteria that are generally accepted to be fair include length of service, skills and qualifications. Generally, the test for fair and objective criteria will be satisfied by the use of the "last in, first out" (LIFO) principle. There may be instances where the LIFO principal or other criteria need to be adapted. The LIFO principle, for example, should not operate so as to undermine an agreed affirmative action programme. Exceptions may also include the retention of employees based on criteria mentioned above which are fundamental to the successful operation of the business. These exceptions should, however, be treated with caution;

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111 This section requires the parties to attempt to reach consensus on, among other things, appropriate measures to avoid dismissals.

112 As mentioned in the previous sections, it has been held in the *SAA v NUMSA* case that retrenchment consultations during business rescue may only commence once the business rescue plan is published.

113 The relevant information that must be provided includes: (a) reasons for proposed dismissals; (b) alternatives that the employer considered before proposing dismissals; (c) number of employees affected and job categories affected; (d) proposed method for selecting employees to be dismissed; (e) the time when dismissals are likely to take effect; (f) severance pay proposed; (g) assistance offered to employees likely to be dismissed; (h) possibility of future re-employment; (i) number of employees employed by employer; and (j) number of employees the employer has retrenched in the preceding 12 months.

114 The Commission for Conciliation Mediation and Arbitration is the body established under s 112 of the LRA to deal with labour disputes.

- employees dismissed for reasons based on the employer's operational requirements are entitled to severance pay of at least one week's remuneration for each completed year of continuous service with the employer, unless the employer is exempted from the provisions of section 196. This minimum requirement does not relieve an employer from attempting to reach consensus on severance pay during the period of consultation. The right of the trade union, through collective bargaining, to seek an improvement on the statutory minimum severance pay is not limited or reduced in any way;

- if an employee either accepted or unreasonably refused to accept an offer of alternative employment, the employee's right to severance pay is forfeited. Reasonableness is determined by a consideration of the reasonableness of the offer of alternative employment and the reasonableness of the employee's refusal. In the first case, objective factors such as remuneration, status and job security are relevant. In the second case, the employee's personal circumstances play a greater role; and

- employees dismissed for reasons based on the employer's operational requirements should be given preference if the employer again hires employees with comparable qualifications, subject to:

  - the employee, after having been asked by the employer, expressing within a reasonable time from the date of dismissal a desire to be rehired; and

  - a time limit on preferential rehiring. The time limit must be reasonable and must be the subject of consultation.

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

As alluded to in the previous section, Chapter 6 of the Companies Act provides that a BRP may not have any other relationship with the company under business rescue such as would lead a reasonable and informed third party to conclude that the integrity, impartiality or objectivity of the BRP is compromised by that relationship. Furthermore, a BRP may be removed by a court on the grounds of a conflict of interest or lack of independence.

There is no specific code of conduct applicable to all restructuring professionals. In order for a person to be licensed and appointed as a BRP, he / she must, inter alia, be a member of good standing of a legal, accounting or business management profession accredited by the Companies and Intellectual Property Commission.[115] A BRP therefore remains bound by the professional association's code of conduct of which he / she is a member. Therefore, restructuring professionals who form part of the legal or accounting professions are not bound by codes of conduct that are necessarily specific to the precise types of ethical questions faced in restructuring matters.

On the other hand, the SARIPA Code of Ethics, which applies only to members of SARIPA, is specifically tailored for restructuring professionals, being liquidators, trustees of insolvent estates and BRPs. Some relevant provisions in the SARIPA Code include:

- practitioners[116] must be honest, truthful and conscientious in the performance of their services and must avoid all relationships and direct or indirect interests that will adversely influence, impair, or threaten their integrity or in any manner create the impression of doing so;[117]

- practitioners must render and perform their services free from any improper influence or pressure and in an impartial and independent manner:

[115] In terms of CIPC Notice 29 of 2021, the professional associations accredited by the CIPC for this purpose include the Legal Practice Council, the South African Institute of Chartered Accountants, the South African Restructuring and Insolvency Practitioners' Association (SARIPA) and the Turnaround Management Association.

[116] Practitioners refers to members of SARIPA.

[117] SARIPA Code, r 3.

  - in the best interests of the general bodies of creditors of estates and affected persons as defined in the Companies Act;
  - in compliance with the general powers and duties of BRPs provided for in section 140 of the Companies Act;
  - in compliance with the general powers and duties of a liquidator as provided for in the Companies Act 1973; and / or
  - in compliance with the general powers and duties as set out in the Insolvency Act;[118]
- practitioners:
  - owe a fiduciary responsibility to creditors and affected persons and generally all parties involved; and
  - have a duty to be fair and act without bias in assessing the competing interests of stakeholders;[119] and
- practitioners may not accept any appointment:
  - if they are disqualified from doing so in terms of the provisions of section 55 of the Insolvency Act and section 372 of the Companies Act 1973 or for any other legal reason; or
  - if they will be unable to render and perform their services in respect of any such estate impartially or independently by reason of relationships or direct or indirect interests or for whatever other reasons. Practitioners may not by means of any misrepresentation or reward or offer of any reward, whether direct or indirect, induce or attempt to induce any person to vote for their appointment.

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

Various ESG-linked financial instruments have been developed in South Africa in recent years. The Johannesburg Stock Exchange has segments both for sustainability-linked bonds and green bonds[120] on its bond market.

Sustainability-linked bonds incentivise the achievement of ESG metrics by issuers by providing economic benefits, such as an interest rate adjustment, to issuers that meet specific ESG targets.

Green bonds raise capital that is ring-fenced specifically to finance "green" or environmentally friendly projects. Unlike sustainability-linked bonds, which merely incentivise the attainment of ESG targets, green bonds may only be used to finance specific projects and thereby impose contractual obligations on the issuer.[121]

Like their global counterparts, many South African financial institutions offer "ESG enhanced" indexes to retail investors such as ESG-linked exchange traded funds and unit trusts, which only include companies that meet specific ESG prerequisites.[122]

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118 *Idem*, r 4.
119 *Idem*, r 7.
120 JSE: Sustainability (https://www.jse.co.za/our-business/sustainability) (accessed on 10 December 2022).
121 See also: T Sentle and D Wilken, "Sustainable Finances v Green Loans: Key Differences to Look out For" (https://www.cliffedekkerhofmeyr.com/en/news/publications/2022/Practice/Finance/finance-and-banking-alert-3-november-2022-sustainable-finances-vs-green-loans-key-differences-to-look-out-for.html) (accessed on 10 December 2022).
122 For instance, the Satrix MSCI Emrging Markets ESG Enhanced ETF and the Sygnia Itrix S&P Global 1200 ESG ETF.

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

Most of South Africa's large financial institutions and banks in particular offer ESG products and have adopted ESG policies and frameworks that aim to assist in the attainment of the United Nations Sustainable Development Goals.[123]

South Africa's big four corporate and investment banks form part of the Equator Principles Association and in 2015 Standard Bank became the first African bank to chair the Equator Principles Association.[124]

The Investec Group was the first South African bank to join the United Nations Environment Programme Net-Zero Banking Alliance in October 2021 and is presently the only South African bank that is part of this alliance.[125] This initiative requires its members to commit to certain ESG targets and ultimately to have the member banks' lending and investment portfolios to have net zero emissions by 2050 or sooner.[126]

Although there is no banking-specific legislation which imposes explicit ESG requirements on banks, they are subject to the Companies Act and therefore banks' Social and Ethics Committee must address the 10 Principles of the UN Global Compact and furthermore must comply with King IV in terms of disclosure requirements.[127]

### 5.3 Promoting ESG by the central bank and regulators

The South African Reserve Bank (SARB) and National Treasury are actively involved in pursuing policies to promote ESG in financing and the SARB is a member of the Network for Greening the Financial System.

In April 2022, South Africa's first national Green Finance Taxonomy was launched. It aims to provide investors, issues, lenders and other financial sector participants with a means to track, monitor and demonstrate their credentials in environmental sustainability. The Taxonomy aims to standardise and catalogue a minimum set of assets, projects, and sectors that are eligible to be defined as "green" or environmentally friendly.[128]

The primary policy mandate of the SARB is to maintain price stability in South Africa in the interests of balanced and sustainable economic growth.[129] The SARB therefore does not impose explicit policies to incentivise or disincentivise certain behaviours by financial institutions. However, by creating a transparent regulatory framework, assisting in the development of an official green finance taxonomy and improving information flows within financial markets, the SARB aims to foster a regulatory environment where ESG considerations can more effectively inform investment decisions.[130]

In the context of retirement funds, regulation 28 of the Pension Funds Act[131] has, since 2011, required that before investing in an asset, a fund must consider ESG factors that may materially affect the sustainable long-term performance of that asset.[132] In June 2019, the Financial Sector

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123 See, for instance, Nedbank's Sustainable Development Goals Issuance Framework, April 2019; ABSA Group Limited 2020 Environmental, Social and Governance Report.

124 Standard Bank becomes first African bank to chair Equator Principles Association (https://equator-principles.com/chair-standard-bank/) (accessed on 10 December 2022).

125 UNEP Finance Initiative Members: Net-Zero Banking Alliance (https://www.unepfi.org/net-zero-banking/members/) (accessed on 10 December 2022).

126 UNEP Finance Initiative Commitment Statement (https://www.unepfi.org/net-zero-banking/commitment/) (accessed on 10 December 2022).

127 King IV Report on Corporate Governance in South Africa (November 2016).

128 National Treasure Media Statement, *South Africa's First National Green Finance Taxonomy Launched to Assist the Financial Sector Response to Climate Change and Support Sustainable Development* (1 April 2022).

129 Constitution of South Africa 1996, s 224.

130 South African Reserve Bank Annual Report 2021/2022 at 48.

131 Act 24 of 1956.

132 Regulation 28(2)(c)(ix) of Act 24 of 1956.

Conduct Authority issued a guidance note on how funds must comply with this regulation and how funds must seek to ensure the sustainability of their investments and assets.[133] The guidance note furthermore sets out the FSCA's expectations regarding ESG-related disclosure and reporting requirements relating to sustainability. The guidance note is not legally binding but is rather "soft law" that provides guidance to retirement funds.

[133] Financial Sector Conduct Authority Guidance Note 14, June 2019.

# SPAIN

## 1. General overview of the restructuring regime

Until 2009, the only solution to insolvency (either current or imminent)[1] in Spain was a formal insolvency proceeding called "*concurso de acreedores*". Since 2023, a simplified special procedure (*procedimiento especial*) for micro-enterprises[2] has also applied.

Since 2009, out of court pre-insolvency tools have also been developed. Currently, there is only one type of informal restructuring proceeding: restructuring plans (*planes de reestructuración*), which occur mainly out of court during the pre-insolvency period (although not only). Restructuring plans may also be proposed where there is a likelihood of insolvency.[3]

### 1.1 Formal restructuring procedures

The "*concurso de acreedores*" is the only formal insolvency proceeding in Spain, which provides for either the continuity of the company or its liquidation. According to the Spanish General Council of the Judiciary, the average duration of these proceedings in Spain was 44.6 months (almost four years) in 2021.[4]

In both scenarios, the debtor needs to comply with disclosure of information obligations, including the provision of a list of creditors and an inventory of assets and liabilities. At the beginning of the procedure, creditors will be given a one month term to lodge their claims so the insolvency practitioner or liquidator can verify the information provided by the debtor and produce their own list of creditors and inventory.

#### *1.1.1 Continuity scenario*

Under the continuity scenario, the general rule is that the debtor remains in possession but subject to the intervention of the court-appointed insolvency practitioner.

An arrangement with creditors is proposed[5] after the insolvency practitioner produces their initial report (to which they attach their own list of creditors and inventory). The arrangement includes a stay and / or reduction but it can also foresee structural changes (mergers, split offs and global assignments of assets and liabilities), as well as debt for equity swaps or conversions to profit participating loans (PPLs). The arrangement could also foresee a limitation in the debtor's powers to dispose of its assets during the term of the arrangement and it could grant certain functions (i.e. certain supervision duties) to the insolvency practitioner after its approval.

There are certain prohibitions in the content of the arrangement.[6] For example, the arrangement may not alter the legally established order of claims. Furthermore, with regard to public claims and labour claims, the following content is prohibited:

- a change in the applicable law;

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1 Article 2.3 of the Royal Legislative Decree 1/2020, which approves the recast text of the Bankruptcy Law (Spanish Bankruptcy Law), defines "current insolvency" as the situation in which the debtor is not able to comply with its due obligations in a regular manner. On the other hand, "imminent insolvency" is defined as the situation in which the debtor foresees that it will not be able to comply with its obligations within the next three months.

2 Spanish Bankruptcy Law, art 685 defines micro-enterprises as those with less than 10 workers on average in the last year and with either liabilities of less than EUR 350,000 or a turnover of less than EUR 700,000.

3 Spanish Bankruptcy Law, art 584 defines "likelihood of insolvency" as the situation in which it is objectively foreseeable that, if no restructuring agreement is reached, the debtor will not be able to pay its future obligations as they fall due in the next two years.

4 See the public data available at: https://www.poderjudicial.es/cgpj/es/Temas/Transparencia/ch.Estimacion-de-los-tiempos-medios-de-duracion-de-los-procedimientos-judiciales.formato1/?idOrg=29&anio=2021&territorio=Espa%C3%B1a&proc=Concursos.

5 Either by the debtor or creditors with over 20% of the total liabilities of the insolvent debtor, in accordance with section 315 of the Spanish Bankruptcy Law.

6 Spanish Bankruptcy Law, art 318.

- the change of debtor, without prejudice to the fact that a third party assumes the payment obligation without releasing the debtor;
- the modification or extinction of the guarantees they may have; or
- the conversion of the claims into equity, profit participating loans or any other claims of characteristics or rank different from those of the original claim.

Finally, the arrangement may not imply any reduction and / or stay with respect to: (i) the claims that correspond to the percentages of the social security contributions to be paid by the employer for common contingencies and for professional contingencies; or (ii) the claims that correspond to the percentages of the workers' quota (relating to common contingencies for accidents at work and occupational disease). This is discussed in further detail in section 2.2.2 below.

The insolvency practitioner will evaluate the proposal and creditors will have a two month term (which may be extended for another two months) in order to vote on it.

The proposal needs to be voted on by the necessary majorities prior to being court approved. There are different thresholds depending on the potential content of the arrangement. [7] The general rules are the following:

- if the arrangement includes an immediate payment of the claims with less than a 20% reduction or a payment in full in less than three years, the arrangement will be approved if the liabilities of those that voted in favour exceed the liabilities of those who opposed;
- if the arrangement includes reductions of up to 50% or stays of up to five years, the approval threshold will be 50% of the total amount of ordinary claims; and
- if the arrangement includes any other content, the approval threshold will be 65% of the total amount of ordinary claims.

The arrangement with creditors (*convenio*) constitutes an agreement between the debtor and all or some of its creditors, or some classes of creditors, and guarantees the continuity of the company and its activity. The continuity of the business should thus allow for the repayment of the agreed amounts, within the agreed term and with the established guarantees. If that is not possible, the company should then initiate its winding up or, alternatively, it could negotiate and obtain court approval of a rearrangement with creditors.

Once approved by the relevant majority of creditors, the arrangement may be considered for its court sanctioning. In this case, the control is *ex ante*, as creditors who have not voted favourably and / or the insolvency practitioner could oppose its approval. If this were the case, there will be a side proceeding (*incidente concursal*). The court will only sanction the arrangement if no creditors oppose it, if it has ruled favourably on the arrangement in the side proceeding, and if it does not rule *ex officio* that there are grounds for opposition even if no party has raised the issue. [8]

### *1.1.2 Liquidation scenario*

The wind-up scenario implies the liquidation of the company's assets. The court appoints an insolvency practitioner as liquidator, who substitutes the previous directors and executes the liquidation of the assets.[9]

The liquidation includes the possibility of selling the whole business or part of it through a pre-pack proceeding in a very initial stage of the proceeding. Despite resulting in a change of ownership, this

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[7] *Idem*, art 376.

[8] *Idem*, arts 389 and 392.

[9] The Spanish Bankruptcy Law eliminated the need for a plan elaborated by the liquidator which needed to be court-approved and that established the rules for the liquidation in each specific proceeding. Article 421 of the Spanish Bankruptcy Law now refers to the obligation of the liquidator to sell the assets and rights of the estate "in the most convenient manner for the interest of the insolvency proceeding".

is currently one of the restructuring trends which will allow for the preservation of Spanish businesses.

Pre-packs were first introduced by precedents of the Barcelona Commercial Courts in 2020.[10] In September 2022, the implementation of the EU Directive on Preventive Restructuring Frameworks (EU Directive) in Spain[11] formally introduced pre-packs in the Spanish legislation, following the precedents of the Barcelona Commercial Courts. Recently, Madrid Commercial Courts have construed the pre-packaged sales regime in Spain and differentiated them from other types of "accelerated sales" in their guidelines for the appointment of an expert "pre-packer" in the pre-insolvency phase.[12]

The Spanish pre-pack procedure is similar to that included in the Proposal for a Directive of the European Parliament and of the Council harmonising certain aspects of insolvency law.[13] It includes a preparation phase during the pre-insolvency period, which corresponds to the request to the court for the appointment of an expert to collect bids for the acquisition of the production unit during that pre-insolvency period. An appointment by the court of such an expert, and the ensuing bids that are solicited by the expert, results in a sale that is public, independent, transparent and competitive. When the company petitions for insolvency, it should attach the best binding offer obtained by the expert and the request to the court to approve the pre-pack sale. Once the insolvency proceeding is declared (liquidation phase), the sale can be carried out swiftly, quickly and within approximately three weeks of the insolvency opening.

The acquirer can cherry-pick the assets and liabilities comprising the business unit they bid for, or alternatively bid for the business as a whole. Regarding the labour force, the acquirer only assumes liability for the pending salaries and social security-related obligations of the workforce that is included in the offer.[14] In this case, the buyer assumes the obligation to continue or restart the activity of the business for at least two years.[15] Procedurally, the court will grant a term of three to 10 days to the workers' representatives and the secured creditors to file allegations prior to authorising the sale.[16]

There is an alternative to the pre-pack procedure to also save the businesses under a liquidation scenario at an early stage of the proceeding: an accelerated sale. In this scenario, the debtor may submit, together with its formal insolvency petition, a binding written proposal from a creditor or third party for the acquisition of one or more production units. Accelerated sales differ from pre-pack sales insofar as no expert is appointed during the pre-insolvency period. In this scenario, the judge will grant a 15 day term for creditors to make any allegations they deem appropriate about the proposal and for any interested party to submit an alternative binding proposal. If more than one bid is made, the insolvency practitioner will have a five day term to issue an evaluation report on the proposals. After the evaluation, bidders will be granted a three day term to improve their offers and within the three days following the end of this period, the judge will approve the offer

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10 *In re CRAIL LINGUISTICS, S.L.* and *LINGUISTICS SYSTEMS INSTITUTE, S.L.* [2020] AJM B 71/2020, 30 October 2020 (CENDOJ reference 08019470072020200002).

11 Law 16/2022 on the reform of the consolidated text of the Bankruptcy Law, approved by Royal Legislative Decree 1/2020 for the transposition of Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks, on discharge of debt and disqualifications, and on measures to increase the efficiency of procedures concerning restructuring, insolvency and discharge of debt, and amending Directive (EU) 2017/1132 (Directive on restructuring and insolvency).

12 *Guía de buenas prácticas para el nombramiento del experto en fase preconcursal (Prepack)* released in February 2023 and available at: https://www.cemad.es/wp-content/uploads/2023/02/Guia-de-Buenas-Practicas-de-Venta-de-Unidades-Productivas.pdf.

13 Title IV of the proposal (arts 19 to 35) refers to pre-pack proceedings. However, Spain would still need to ensure that parties closely related to the debtor are eligible to acquire the debtor's business or part thereof in the same conditions as third parties would, if they meet the criteria specified in the proposal under its art 42.

14 In this regard, under art 224.1.3° of the Spanish Bankruptcy Law, it would be possible to request the Commercial Court to exclude the part of the salaries of the workforce that is included under the perimeter of the offer covered by the Salary Guarantee Fund ("*Fondo de Garantía Salarial*").

15 Spanish Bankruptcy Law, art 224 septies, subsection 2. Failure to comply with this commitment will give rise to any affected party being able to claim compensation from the acquirer for the damages caused.

16 *Idem*, art 518.

that is most advantageous for the interests of the insolvency proceeding, also within three days. In the case of accelerated sales, the acquirer must assume the obligation to continue or restart the activity with the production unit or units to which they refer for at least three years.[17]

The most relevant accelerated sale up to date has been the recent sale of the business of the Abengoa companies, which showed that this procedure might not be as fast as the law foresees (it took approximately six months, which is over four to six times what the procedure is intended to last for).

## 1.2 Informal restructuring procedures

With the transposition of the EU Directive,[18] Spain reformed its Bankruptcy Law and introduced restructuring plans as the only out of court restructuring procedure. These take the place of the previous out of court payment arrangements, which were not used in practice, and refinancing agreements, which had a much more limited scope and could only compulsorily extend to financial claims.

Currently, the content of restructuring plans is much broader and there is much more flexibility than the past refinancing agreements. The plan may affect almost any creditors, and not just creditors with claims of a financial nature. Creditors and affected parties (i.e. shareholders)[19] need to be included in their relevant classes, which will vote separately. The plan may include a stay, a reduction, a swap into a profit participating or subordinated loan, shares or any instrument of a different legal rank than the original claim, the modification and / or extinction of personal guarantees or security, the change of debtor or the modification of the law applicable to the debtor. It may also include a restructuring not only of the liabilities, but also of the assets of the debtor or its equity and it can include the sale of a business unit or of the business as a whole and any other operating modification that is deemed necessary.[20] The debtor may also terminate senior management contracts in the best interests of the restructuring and may include the compensation that arises from those terminations under the plan.

Limitations[21] to the claims that may be affected by the plan include:

- food and maintenance claims in family relationships;
- claims that arise from extra-contractual civil liability; and
- labour claims other than senior management contracts (discussed in further detail in section 3.3 below).

Public claims may only be affected under certain circumstances and with many limitations (for example, the plan can only include a stay of up to six to 12 months, depending on the circumstances).

Regarding any modification or termination of the employment relationship that takes place in the context of the restructuring plan, this shall be carried out in accordance with the applicable labour legislation, including, in particular, the rules on information and consultation of employees.[22] Indeed, the formal content of the restructuring plan will include the measures that have been adopted or are to be adopted to inform and consult with employees in accordance with the applicable labour legislation.[23]

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17 *Idem*, art 224 bis, subsection 1, paragraph 2. Failure to comply with this commitment will give rise to any affected party being able to claim compensation from the acquirer for the damages caused.

18 See above, n 11.

19 Spanish Bankruptcy Law, arts 614 and 631.

20 *Idem*, art 616.1.

21 *Idem*, arts 616 and 616 bis on "Affected claims" and "Public claims", respectively.

22 *Idem*, art 628 bis.

23 *Idem*, art 633.11ª.

The restructuring plan framework operates on the principle of minimum judicial intervention. Therefore, the debtor remains in possession (with no supervision of any kind), and the negotiation and voting on the plan are informal and function without the interference of regulated processes or court orders. Nevertheless, the debtor may apply to the court in order to obtain the additional protection of a moratorium. Besides, either the debtor or creditors with a certain stake in the liabilities of the company may request the Commercial Court to appoint a restructuring expert to intervene in the negotiations, assist in the drafting of the restructuring plan and provide the Commercial Court with the necessary reports (i.e. on the valuation of the company).

Only the affected parties, which need to be duly notified, vote on the proposed plan. The general rules on majorities within each class are the following:[24]

- if the class is composed of secured creditors, it will be considered that the class has approved the plan if over 75% of the amount of the liabilities of that class have voted in favour;
- if the class is composed of any other creditors, the threshold amount is two thirds; and
- if the plan requires the consent of shareholders, the ordinary quorum and threshold will be required (without any relevance of its specific content and even if under a non-restructuring scenario the thresholds required could be higher).

A court may sanction a plan:[25]

- in those cases in which the plan is consensual (i.e. the relevant majority is obtained within each class and is therefore approved by all the classes without exception, as well as the debtor and, if affected, shareholders); and
- in those cases in which the plan is non-consensual (i.e. it is not accepted by all the classes) if:
    - either a simple majority of classes, including one class with creditors that are either secured or with a general privilege (mainly public claims), accept the plan; or
    - at least one "in the money" class (according to the valuation of the restructuring expert) accepts the plan.

The Commercial Court will only intervene at the end of the process in order to sanction a restructuring plan that already satisfies the necessary majorities. The sanctioning will be compulsory under certain circumstances (i.e. to extend the effects of the plan to dissenting creditors within a class or to apply cram-down or cram-up, to extend the effects of the plan to the shareholders of the debtor company or to protect DIP financing).[26] The control of the court is not *ex ante* but will be *ex post*, through a system of challenges to the ruling that sanctions the plan.

The first plan that was sanctioned was that of Xeldist Congelados. S.L.U.[27] In this case, there were actually challenges to the plan which derived in the effects of the plan not being extended to the challenging creditors.[28]

## 2. Restructuring of ESG-related liabilities

### 2.1 Environmental (E): restructuring environmental liabilities

24 *Idem*, art 629. There are specific rules on how syndicated pacts affect the voting under art 630. Article 631.4° determines the threshold for the shareholders.
25 *Idem*, arts 638 and 639.
26 *Idem*, art 635.
27 *In re XELDIST CONGELADOS, S.LU.* [2022] AJM3 Pontevedra 189/2022, 2 December 2022.
28 *In re XELDIST CONGELADOS, S.LU.* [2023] AP Pontevedra 179/2023, 10 April 2023 (CENDOJ reference 36038370012023100069).

### 2.1.1 *Types of environmental liabilities*

Article 45 of the Spanish Constitution recognises the right to enjoy an adequate natural environment as an inextricable condition for the development and pursuit of human nature, together with the duty to preserve it. It also establishes that those who fail to comply with the obligation to use natural resources diligently and to protect nature will be obliged to repair the damage caused, notwithstanding administrative or criminal sanctions that could also correspond.

This constitutional mandate, together with the need to implement the European Directive 2004/35/CE of the European Parliament and of the Council of 21 April 2004 on environmental liability with regard to the prevention and remediation of environmental damage, motivated the enactment in Spain of Law 26/2007 on Environmental Liability. This Law introduced an administrative framework for environmental liability based upon the principles of unlimited risk prevention and the "polluter pays" principle.[29]

Liability depends on the economic activity of the business. Specifically:

- businesses with high environmental risks associated with their economic activity[30] have the obligation to cover the costs of prevention (preventive action) and reparation (remedial action) of environmental damage in any case; and
- other businesses not included in this Law will only have to cover reparation costs when they have caused environmental damage through negligence or fraud. Other than that, they will only have to pay for prevention costs.

### 2.1.2 *Priority given to environmental liabilities*

Law 26/2007 establishes an administrative liability regime, whereby the infringement of the duties set out therein entails the imposition of financial penalties, notwithstanding any civil liabilities that could additionally derive from tort claims pursued by impacted parties.

Under an insolvency scenario, the financial penalties for these concepts that would arise would be classified depending on the time at which the events giving rise to the penalty took place. In particular:

- if the claim results from an obligation arising after the opening of the insolvency proceedings and until the termination of the insolvency proceedings, it will be considered a claim against the insolvency estate (*créditos contra la masa*). Claims against the insolvency estate are: (i) payable upon maturity; and (ii) have super-priority over any unsecured claims, that is to say, over claims with a general privilege, ordinary claims and subordinate claims;[31] and
- if the event giving rise to the penalty occurred prior to the declaration of insolvency proceedings, the credit corresponding to the penalty is classified as a subordinate claim, notwithstanding the existence of correspondent subsidiary liabilities of third parties.[32] Subsidiary liabilities are discussed in further detail in section *2.1.3* below.

There was previously controversy in Spain with regard to the date to be taken into account to classify penalty claims – being either: (i) the time at which the event that gave rise to the infringement took place; or (ii) the time at which the obligation arose. This controversy has now been resolved by the Supreme Court[33] by analysing the time when the act or omission that is being punished (i.e. the non-compliance with the environmental obligations) took place.

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29 As referred to under the Whereas (2) of the mentioned European Directive 2004/35/CE.
30 There are defined in the 26/2007 Law under its Annex III, such as, for example, companies in the field of waste management, including the collection, transport, recovery and disposal of waste and hazardous waste.
31 Spanish Bankruptcy Law, arts 242.1.13°, 244 and 245.2.
32 *Idem*, art 281.1.4°, which classifies credits for fines and other pecuniary penalties as subordinate claims.
33 STS, Civil Chamber, 504/2011, 1 July 2011 (CENDOJ reference 0 28079110012011100474). In this ruling, the Spanish Supreme Court held that "the question of the insolvency classification of claims for

On the other hand, civil liabilities that could additionally derive from torts would be classified as claims against the insolvency estate if they arise after the insolvency opening.[34] If they arose prior to the insolvency opening, they could be classified as either:

- claims against the insolvency estate, if they are related to death or personal damages which, as explained above, have super-priority over unsecured claims;[35] or

- claims with a general privilege (*créditos con privilegio especial*) with priority in payment over ordinary and subordinated claims and not affected by an arrangement with creditors unless the creditors vote in favour of the arrangement, if they are not related to death or personal damages.[36]

### *2.1.3 Disclaimer of environmental obligations*

Under restructuring plans, there are certain limitations to the creditors that may be affected by the plan. For ESG-related liabilities, these limitations expressly include the non-contractual liabilities that derive from torts. Furthermore, given that sanctions and penalties that could derive from ESG-related liabilities would constitute public claims, they could only be subject to a restructuring plan if certain requirements are met. The Spanish Bankruptcy Law has expressly banned the possibility to affect public claims under a restructuring plan by:

- reductions;

- a change of debtor (without prejudice to a third party assuming the payment obligation of the debtor, with no release of the debtor);

- a modification or extinction of security; or

- debt for equity swaps or conversion of debt into profit participating loans or into any instruments of characteristics or rank other than those of the original one.

Consequently, the only content that could affect public claims would be a stay, which is also limited to a six month term (if a deferment on the affected public claims had been already granted prior to the approval of the plan) or to a 12 month term (if the affected public claims had not previously been deferred).[37]

Furthermore, a stay on public claims may only be proposed under a restructuring plan if the debtor certifies that it is up to date in the payment of tax and social security obligations. In practice, this means that only public claims that have not reached their maturity date or those that have been deferred (and not over two years) may be subject to a plan.

Under Law 26/2007, penalties may give rise to two types of sanctions, depending on the severity of the infringement: (i) a fine that may vary from EUR 10,001 to EUR 2 million; or (ii) suspension or termination of authorisations to carry out the economic activity.[38] It is relevant to point out that there is a subsidiary liability for the payment of any pecuniary obligations or other duties imposed as a consequence of this Law,[39] including:

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administrative penalties must be resolved by taking into account not the time when the obligation arose, but the time when the penalised conduct was committed. This is the determining factor in the regime also applicable to the penalty, in congruence, on the one hand, with the guiding principles of the power to impose penalties, including the principle of non-retroactivity, which makes it impossible to penalise conduct that was not already criminalised in the regime in force at the time it was committed, and, as anticipated, also with a restrictive interpretation of the credits against the estate, in order to safeguard equality between creditors".

34 Spanish Bankruptcy Law, art 242.1.13°.
35 *Idem*, art 242.1.1°.
36 *Idem*, art 280.5°.
37 *Idem*, art 616 bis.
38 26/2007 Law on Environmental Liability, art 38.
39 *Idem*, art 13.

- the *de facto* and *de jure* managers and administrators of a company;
- the managers or administrators of entities that have ceased their activities, with regard to the duties and obligations pending at the time of such cessation, if they have not done what is necessary for their compliance or have adopted agreements or taken measures causing the non-compliance.
- those who succeed in any capacity to the entity liable for the activity causing the damage; and
- members of insolvency administrations and liquidators of companies who have not done what is necessary to comply with the duties and obligations accrued prior to insolvency.

Therefore, property subject to environmental obligations may not be disclaimed or abandoned under either an out of court or formal procedure in Spain. On the contrary, it would give rise to the subsidiary liability regime of either the directors of the company and / or the court-appointed insolvency administrators and liquidators.

## 2.2 Social (S): restructuring health or safety-related liabilities

### *2.2.1 Types of health and safety-related liabilities*

Based on the recognition of the right of workers in the workplace to the protection of their health and integrity, Law 31/1995 on the Prevention of Occupational Risks establishes the various obligations which guarantee this right, as well as the actions of the Public Administrations which may have a positive impact on the achievement of this objective.

Failure by employers to comply with the obligations contained in this Law[40] will give rise to: (i) administrative liabilities; as well as, where appropriate (ii) criminal and civil liabilities for the damages that may derive from such non-compliance.

In accordance with the provisions of Royal Legislative Decree 5/2000, approving the revised text of the Law on Offences and Penalties in the Social Order, administrative offences in the social order are the actions or omissions of the different parties responsible, as defined and sanctioned in the aforementioned Law and in the laws of the social order. Specifically, articles 11, 12 and 13 classify offences in the area of occupational risk prevention and, from article 39 onwards, list the responsibilities and penalties, all of which are of a pecuniary nature.

### *2.2.2 Treatment of health and safety-related liabilities*

As noted above, under a formal insolvency procedure, an arrangement with creditors may not affect certain claims that are related to ESG liabilities. Specifically in relation to health and safety-based liabilities, these include:

- the claims that correspond to the percentages of the social security contributions to be paid by the employer for common contingencies and for professional contingencies; and
- the claims that correspond to the percentages of the workers' quota, which relates to common contingencies or accidents at work and occupational disease.

In the same way as for environmental liabilities, for liabilities related to health and safety, any infringement results in financial penalties. Depending on the time at which the events giving rise to the penalty took place, they are classified as follows:

- if the claim results from an obligation arising after the opening of the insolvency proceedings and until the termination of the insolvency proceedings, it will be considered a claim against the insolvency estate (*créditos contra la masa*), which is payable upon maturity;[41] and

[40] Law 31/1995 on the Prevention of Occupational Risks, art 42.
[41] Spanish Bankruptcy Law, art 242.1.13°.

- if the event giving rise to the penalty occurred prior to the declaration of insolvency proceedings, the credit corresponding to the penalty is classified as a subordinate claim, notwithstanding any correspondent subsidiary liabilities of third parties such as directors of the company or its administrators or liquidators.[42]

Furthermore, the Spanish Bankruptcy Law grants the following priorities to occupational health issues:

- claims against the insolvency estate, payable upon maturity:
  - those claims that arise both before and after the opening of the insolvency proceeding for compensation derived from accidents at work and occupational disease, regardless of the date of the decision that declares it;[43] and
  - those claims that arise from surcharges on employment benefits for non-compliance with occupational health obligations after the insolvency opening and until the judge orders the cessation of professional or business activity, or declares the termination of the insolvency proceeding;[44] and
- claims with a general privilege (with priority in payment over ordinary and subordinated claims and not affected by an arrangement with creditors unless the creditors would vote in favour of the arrangement): those claims that arise prior to the insolvency opening for the capital costs of social security for which the insolvent debtor is legally responsible and the surcharges on employment benefits for non-compliance with occupational health obligations that arise prior to the insolvency opening.[45]

### 2.3 Governance (G): third party releases in favour of directors and officers of the company

As a general rule, in Spain third parties do not receive releases of liability under a restructuring plan.

Exceptionally, the effects of a restructuring plan may be extended to the personal guarantees and / or security granted by a group company not affected by the restructuring plan if the enforcement of the guarantee could cause the insolvency of both the guarantor and of the debtor.

Given that is the only exception, third party releases cannot be sought in favour of directors and officers of the company in relation to potential claims against them personally.

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

#### *3.1.1 Approving a restructuring plan*

In Spain, the Commercial Court has jurisdiction to sanction the plan and applies the formal requirements under the Spanish Bankruptcy Law.

#### *3.1.2 Discretion to consider wider public interest concerns*

The Commercial Court has no degree of latitude or discretion to consider wider public interest concerns in deciding whether to approve the plan.

42 *Idem*, art 281.1.4°, which classifies credits for fines and other pecuniary penalties as subordinate claims.
43 *Idem*, art 242.1°.
44 *Idem*, art 242.11°.
45 *Idem*, art 280.1°.

### 3.1.3 *Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

Spanish legislation does not foresee the possibility for environmental protection authorities or environmental defence groups to intervene in the restructuring plan, as only creditors with claims affected by the restructuring plan will be involved in the approval of the plan.

## 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

### 3.2.1 *Approving a restructuring plan*

Under Spanish law, the labour force has relevance under certain insolvency solutions. For example:

- in the event the insolvency proceedings result in the sale of a production unit or the business as a whole, the offer will need to set out the impact it will have on the labour force;[46]
- where the sale of a production unit or the business as a whole is proposed, the Commercial Court will always grant a 15 day term to file for objections on the sale;[47]
- in the event the sale of a production unit or the business as a whole takes place by public auction, the Commercial Court may authorise a sale of less than 15% in price compared to the best economic offer if it considers this option will better guarantee the sale of the productive unit and will save more jobs;[48]
- under an accelerated sale scenario, workers may found a cooperative or labour company to make an offer for the business unit. If the workers' offer is equal or higher in value to the alternative acquisition proposals, the Commercial Court will give priority to the workers' offer;[49] and
- if an arrangement with creditors envisages the acquisition by a third party either of all the assets and rights assigned to the professional or business activity of the insolvent debtor, or of certain production units, then while the acquirer undertakes the commitment to continue that activity, it may not be admitted by the Commercial Court without the prior hearing of the workers' representatives.[50]

### 3.2.2 *Discretion to consider wider public interest concerns*

In Spain, there is no discretion of the court to consider wider public interest concerns, outside of the specific events relating to workers noted above.

### 3.2.3 *Protection of employee rights*

Under the Spanish Bankruptcy Act:

- in an out of court restructuring scenario, the workers' representatives retain all their functions regarding notification, consultation (negotiations) and legal procedure, which will follow labour laws as in a non-distressed scenario;[51]
- there is an obligation to notify the opening of the formal insolvency proceeding to the legal representatives of the workers, even in cases in which they have not formally appeared before the Commercial Court in the proceeding.[52] The notification obligation falls on the insolvency

46 *Idem*, art 218.
47 *Idem*, art 219.
48 *Idem*, art 212
49 *Idem*, art 224 bis, subsection 6.
50 *Idem*, art 342.
51 See above, nn 22 and 23.
52 Spanish Bankruptcy Law, art 28.4.

practitioner, who needs to inform the workers' representatives expressly of their right to appear as a party in the proceedings;[53]

- following the declaration of insolvency, workers' representatives retain all the powers attributed to them by the specific labour legislation in the event of the substantial modification of working conditions, transfer, dismissal and suspension of contracts and reduction of working hours for economic, technical, organisational or production reasons;[54] and

- in an insolvency proceeding, the legal representatives of the workers have standing to request from the Commercial Court, on behalf of the workers, the substantial modification of working conditions, transfer, dismissal, suspension of contracts or reduction of working hours of a collective nature which affect the employment contracts in which the insolvent party is the employer.[55]

### 3.3 Governance (G): board / management conflicts addressed in a restructuring

There are no insolvency provisions in Spain to specifically deal with the potential conflict of interest arising from the existing directors or management to try to influence the formulation of a restructuring plan by negotiating for post-restructuring shares or options in return for continuing their service for the company. However, general company law rules would apply and these duly address a potential conflict of interest. In fact, the general duty of loyalty of the directors to the company requires directors to abstain from voting about any issues in which they would have a potential conflict.[56]

Further, while Spanish law does not allow for labour claims to be affected by a restructuring plan, it does allow the termination of senior management contracts if this is required in the best interests of the restructuring. This implies that Spanish law is giving more relevance to other stakeholders (i.e. creditors, suppliers and the collective workforce) than to senior management and directors.

Furthermore, since September 2022, creditors (as well as the debtor) have been entitled to prepare and request the sanctioning of a restructuring plan by the court. This indirectly implies that any unreasonable requests from the company and its management or directors could lead to creditors filing their own plan.

On the other hand, the restructuring plan could oblige shareholders (who also act as management or directors in practice on many occasions in Spain) to accept a capital decrease to zero and a later capital increase in which they would have no pre-emptive rights (that is to say, to lose their stake in the company). Nonetheless, this measure can only be imposed on shareholders under an imminent or current insolvency scenario, but not where there is a mere likelihood of insolvency.[57]

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

Industry guidelines and incentives to influence a company to adopt environmentally responsible measures are issued at both a European and local level but do not address specifically a restructuring scenario.

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53 *Idem*, art 254.
54 *Idem*, art 169.2.
55 *Idem*, art 171.1.
56 Articles 228 c) and 229 of the Royal Legislative Decree 1/2010, approving the revised text of the Capital Companies Act.
57 Spanish Bankruptcy Law, art 631.4.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

There are no specific soft law instruments in Spain to protect employee rights in a restructuring.

Nonetheless, it must be pointed out that the rationale behind accelerated sales and / or pre-pack sales in most cases is to preserve the activity of companies and at least part of their labour force. This reflects a shift in the Spanish legislation towards the protection of non-shareholder stakeholders, such as the labour force.

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

Court-appointed insolvency practitioners in Spain are either lawyers or economists with over five years of experience in insolvency law. Thus, they need to be part of a regional bar or a regional chartered economist's association.

The legal advisors to debtors and creditors will be also part of a bar within the Spanish jurisdiction and most financial advisors involved will also be part of a regional chartered economist's association.

Consequently, the rules on conflicts of interest of these organisations will be applicable to most restructuring professionals. They all foresee that the professional must avoid the conflict of interest and cannot represent two or more parties with interests in the same matter unless they have the express and written consent of all the parties. [58]

## 5. ESG in financing

Given that Spain is a Member State of the European Union, the future years in Spain will be much influenced by the "European Green Deal" under the communication of the European Commission on 11 December 2019.[59]

Authors and scholars have praised the transversality of the European Green Deal, which includes an Annex with a roadmap of 47 specific actions under 10 categories as it will be essential to the actions of the European Union in the future.[60]

### 5.1 ESG-linked loans, bonds or investments

Overall, Spain's ESG financing market is rapidly developing, and there is significant potential for investors and financiers in the restructuring and insolvency field to explore ESG-linked opportunities in the country.

Some of the novel features of ESG-linked loans or investments in Spain include:

- loans tied to sustainability variables, where conditions vary depending on the achievement of sustainability objectives;
- green loans with a positive environmental impact, which target the financing of projects or assets complying with the Green Loan Principles;

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[58] As examples, see art 51 of the Royal Decree 135/2021, by means of which the General Statute of Spanish Lawyers is approved; art 3.2.1 of the Rules of the Right of Defence, of the Lawyer Profession and the Lawyers of Madrid of Madrid's Bar Association; and art 4.5 of the Deontology Code of the Chartered Economists; Association of Madrid.

[59] Communication from the Commission to the European Parliament, the European Council, the Council, the European Economic and Social Committee and the Committee of the Regions, European Green Deal, COM/2019/640 final.

[60] S Centeno, J Del Saz-Orozco and C Carazo, "El Pacto Verde Europeo: La transformación del marco regulatorio de la Unión Europea para lograr una sostenibilidad competitiva de la economía" in Paz, J.M., Delgado, M.L. (Coords.) "Estudios Jurídicos sobre Sostenibilidad: Cambio Climático y Criterios ESG en España y la Unión Europea. Editorial Aranzadi, 2023.

- eco-financing, which encourages sustainable investments by improving resource efficiency and reducing environmental impacts; and
- ESG bonds, where the use of funds has a positive impact on society.

According to the 2022 Yearly Report of the Spanish Observatory of Sustainable Financing (OFISO):[61]

- loans tied to sustainability variables reached EUR 60,134 million, a year on year increase of 9%;
- green loans amounted to EUR 30,0777 million, with a 64% increase on 2021;
- ESG bonds amounted to EUR 21,777 million, which was a decrease of 24% over the amount in 2021. The total 2022 amount was composed of EUR 16,552 million in green bonds, EUR 2,000 million in social bonds and EUR 3,225 million in sustainable bonds; and
- 54% of new corporate (non-banking) bond issuances in Spain in 2022 were ESG-based.

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

Spain's financial institutions, including banks and funds, have made significant commitments towards achieving ESG targets in their lending and investment portfolios.

During the 2019 UN Climate Change Conference (COP 25) in Madrid, 23 credit institutions in Spain, which represent 95% of the Spanish banking sector, made a joint commitment on climate action. The primary goal of this commitment is to facilitate the transition to a low-carbon economy, reflecting the increasing awareness and importance of ESG considerations in Spain's financial sector.[62]

Banco Santander, the largest bank in Spain, is a founding member of the Net-Zero Banking Alliance (NZBA).[63] Santander has committed to align its lending and investment portfolios with net-zero greenhouse gas emissions by 2050.[64] The bank has also set targets for reducing its own operational emissions and increasing its renewable energy usage.[65]

BBVA, Spain's second largest bank, has allocated EUR 86 billion between 2018 and 2021 towards sustainability: 80% to climate action and 20% to inclusive growth. This amount includes loans, project finance, brokered bonds and socially responsible investment funds.[66] During 2022, it issued a EUR 1,250 million green bond and a EUR 425 million green bond.[67]

CaixaBank, the country's third largest bank, has joined as a member of UNEP FI and the Collective Commitment to Climate Action, pledging to mobilise private sector finance for sustainable development and to align its business strategy with the objectives of the Paris Agreement and the

[61] Available at: https://www.bolsasymercados.es/docs/BME/docsSubidos/Sostenibilidad/Informe-Anual-OFISO-La-Financiacion-Sostenible-Espana-2022.pdf.

[62] See page 6/15 of the "Banco de España supervisory expectations relating to the risks posed by climate change and environmental degradation" published by Banco de España on 23 October 2020, available at: https://www.bde.es/f/webbde/INF/MenuVertical/Supervision/Normativa_y_criterios/Recomendaciones_BdE/Banco_de_Espana_supervisory_expectations_relating_to_the_risks_posed_by_climate_change_and_environmental_degradation.pdf.

[63] https://www.santander.com/en/press-room/press-releases/2021/04/santander-becomes-a-founding-member-of-the-net-zero-banking-alliance.

[64] https://www.santander.com/en/press-room/press-releases/2021/02/santander-group-sets-ambition-to-be-net-zero-by-2050-supported-by-first-decarbonization-targets.

[65] https://www.santander.com/en/press-room/press-releases/2022/08/santander-world-leader-in-renewable-energy-financing-in-the-first-half-of-the-year#:~:text=Santander%20has%20been%20carbon%2Dneutral,CO2%20emissions%20by%2035.4%25.

[66] https://www.bbva.com/en/sustainability/bbva-channeled-35-4-billion-euros-in-sustainable-financing-in-2021-up-72/.

[67] See above, n 62.

Principles for Responsible Banking.[68] During 2022, it issued a EUR 1,000 million social bond and two EUR 1,000 million green bonds.[69]

### 5.3 Promoting ESG by the central bank and regulators

The Bank of Spain and other regulatory bodies in Spain have been taking steps to promote ESG practices in financing. The Bank of Spain participates in the Network for Greening the Financial System, a global network of central banks and supervisors focused on promoting sustainable finance.[70]

The Bank of Spain has also issued supervisory expectations aimed at explicitly setting out how its supervised institutions should progress in order to take account of the risks posed by climate change and environmental degradation in their business model and strategy, governance, risk management and disclosures to third parties.[71]

Additionally, the Spanish Government has introduced several initiatives to support ESG-linked financing, such as the "ICO financing projects related to sustainability".[72]

These policies and initiatives reflect the growing awareness and importance of ESG considerations by Spain's financial regulators.

68 https://www.caixabank.com/en/sustainability/sustainable-transition/esg-risk-management.html
69 See above, n 62.
70 See Annual Report 2022 of the Network for Greening the Financial System of April 2023, available at: https://www.ngfs.net/sites/default/files/medias/documents/ngfs_annual_report_2022.pdf.
71 See above, n 63.
72 J Sedano and L Villar, "Spotlight: Sustainable Finance Instruments in Spain", available at: https://www.lexology.com/library/detail.aspx?g=365870d8-5fcc-46cc-9919-045da97b54f4#:~:text=The%20Spanish%20National%20Promotional%20Bank,guarantees%20in%20all%20Member%20States).

# SWITZERLAND

## 1. General overview of the restructuring regime

### 1.1 Formal restructuring procedures

The main procedure for restructuring debts in Switzerland is the composition procedure (also called the debt restructuring procedure) according to article 293 et seq of the Swiss Federal Code on Debt Enforcement and Bankruptcy (DEBA).

The debt moratorium is a tool that allows companies to undertake restructuring and reorganisation measures under a court-supervised procedure, with the aim of increasing the prospects of recovery and protecting stakeholder value by avoiding often more value-destructive bankruptcy liquidations. Alternatively, a settlement can be achieved between the debtor (company in distress) and all pre-filing creditors – a so-called "composition agreement" (haircut). Any pecuniary claims against a company may be restructured; there are no restrictions on the types of debt which may be restructured under such an agreement. In particular, there are generally no special restrictions or conditions when restructuring environmental or health and safety-related liabilities owed to the respective creditors. However, some types of claims have a legal privilege, as for example claims based on an employment contract or pension fund scheme. Such claims can only be restructured with the consent of the respective creditors – otherwise, they must be paid in full.

If over-indebtedness can be eliminated within eight months (during the provisional moratorium) and the company is solvent, the moratorium will be lifted and the company is viable again (under certain conditions this procedure is not public, so it is called a silent moratorium). If this is not possible, the company could try to enter into a definitive moratorium to organise for a composition agreement with its creditors. Such a proceeding is public and all creditors have to file their claims with the administrator. The definitive moratorium is limited to a maximum of 24 months (in complex cases). If no solution is found until then, the company will undergo bankruptcy proceedings.

The composition procedure involves four stages.

First, the moratorium can be initiated by a petition to the composition court: (i) by the debtor together with a current balance sheet, a profit and loss statement and a liquidity plan or equivalent documents showing the debtor's current and future assets and income situation, as well as a provisional reorganisation plan; or (ii) by a creditor who would be entitled to file a bankruptcy petition. The court has to approve the moratorium, unless there is obviously no prospect at all of reorganisation or confirmation of a composition agreement (approval stage).

A composition moratorium will normally not be published at first if the company can continue its operations under the supervision of a court-appointed administrator (so called debtor in possession). After a certain time, however, the company will have to disclose the moratorium to all its stakeholders in order to retain control over communication. In any case, provided there is sufficient liquidity, the company is still fully operational as the debtor remains in principle in control of the ongoing business.

However, a court-appointed administrator supervises day-to-day management and may release binding instructions to the executive bodies. In certain cases, the administrator can apply to the court to replace the management. Certain material transactions, including the disposal of fixed assets, accepting pledges or raising debt capital, will require the approval of the court. Furthermore, the moratorium might have an impact on the structuring of workstreams with clients and suppliers and the respective contractual terms.

The court-appointed administrator is generally a lawyer and not a restructuring officer as he / she is only supervising the management and not taking any strategic decisions. The debtor company has the possibility to make suggestions to the court about the identity of the administrator and could organise for a sort of "beauty contest" among potential administrators.

After a provisional stage of a maximum of eight months, the court has to decide whether it approves the definite moratorium. It will do so if the debtor and the administrator prove that there are prospects for a reorganisation or confirmation of a composition agreement.

Once the definite moratorium is confirmed, the administrator takes an inventory of all the debtor's assets and asks the creditors by public notice to submit their claims. The administrator convenes a creditors' meeting as soon as a draft agreement ready for negotiation is available.

Second, consent of the creditors to the debtor's settlement offer, and thereby passing the restructuring plan (consent stage), requires meeting the following thresholds: (i) approval by the majority of the creditors representing at the same time at least two thirds of the total amount of the claims; or (ii) approval of one quarter of the creditors representing at least three quarters of the total amount of the claims.

Not included in the threshold calculation are creditors privileged under bankruptcy law (their claims must be guaranteed in order for the agreement to be confirmed at all), as well as creditors of secured claims insofar as they are covered by the pledge (to this extent they are not subject to the agreement at all).

Third, the composition agreement is subject to the approval of the composition court (confirmation stage), whereby the following conditions must be satisfied:

- the value of debtor's offer must be in proper proportion to its possibilities, which generally means that the composition dividend must be higher than the potential liquidation dividend in a bankruptcy;
- the full satisfaction of the registered privileged creditors as well as the fulfilment of the liabilities entered into during the moratorium with the consent of the administrator (so called post-filing claims) must be adequately secured; and
- in the case of an ordinary composition agreement, the shareholders must make an appropriate restructuring contribution.

Fourth, the confirmed composition agreement must be implemented according to its content (implementation stage).

As an alternative to the above, a company may also conduct a "pre-pack" restructuring. In the absence of an explicit legal basis, several district courts have approved the transfer of business units of a debtor in a pre-pack transaction simultaneously with the grant of a provisional debt restructuring moratorium, in certain cases even without appointing a provisional administrator. However, this should be an exception in cases where the transaction is obviously in the best interests of the creditors.[1]

In a more recent leading case on Swiss pre-pack restructurings, the Swiss Federal Supreme Court[2] has confirmed the previous legal practice of privately pre-negotiated, confidential pre-pack restructurings in Switzerland and thus provided legal certainty under Swiss law, in particular regarding:

- the general admissibility of pre-packs;
- the approval of pre-packs by the competent composition court without a hearing of the creditors; and
- the (largely excluded) rights to appeal by creditors, which provide substantial deal security for potential buyers since the court-authorised transaction is protected against claw-back and avoidance claims.

Such approval may generally be granted if the sale is, based on the court's reasonable discretion, to the creditors' advantage in comparison with bankruptcy proceedings and an urgent sale is essential to the success of a restructuring.

1 *Bzger Bülach*, EC200010-C/Z1.
2 BGer 5A 827/2019.

Hence, a swift restructuring by way of a pre-negotiated sale of certain assets or an entire business during a (silent) composition moratorium is not only possible under Swiss law but may minimise the loss of value and negative publicity which is normally associated with public bankruptcy proceedings in Switzerland.

### 1.2 Informal restructuring procedures

Informal out of court restructurings are conducted primarily on a consensual basis and are not specifically governed by any legislation (so called debt workouts). The statutory framework for such consensual restructurings is provided in articles 725 to 725c of the Swiss Code of Obligations (CO). They may include various measures such as standstill agreements and subordination agreements with creditors, debt-equity swaps, capital injections and transfers of (parts of) businesses to another existing or newly established company (hive-off vehicle) by way of an asset deal.

Since such proceedings always take place close to insolvency, there is a risk of subsequent avoidance or clawback claims. In addition, out of court restructuring procedures must be implemented under great time pressure, as the law obliges the management to quickly apply for a debt restructuring moratorium – otherwise the directors face the risk of civil and criminal liability due to delay in bankruptcy.

Swiss banks have their own non-statutory framework for debt workouts but do not always abide by that industry standard.

Out of court workouts through consent solicitation exercises are also commonplace for bond restructurings, where an issuer seeks the consent of holders of debt securities to amend and / or waive breaches of the terms of those debt securities.

## 2. Restructuring of ESG-related liabilities

### 2.1 Environmental (E): restructuring environmental liabilities

Generally, environmental liabilities can be restructured under a composition agreement in the same way as ordinary liabilities of a company. As mentioned above, any pecuniary debt claims against a company may be restructured under a composition agreement, including contingent, unproven or unliquidated claims. There are no special restrictions or conditions that apply when restructuring environmental liabilities. However, if the creditor is a state authority, depending on the relevant law, additional procedural steps must be observed on the basis of which the authority must make its decision to participate in a restructuring (e.g., a decision to accept a haircut). Based on the principle of federalism in Switzerland, it may therefore be that different cantonal laws are applicable in each case, insofar as the application of federal law is not involved.

#### *2.1.1 Types of environmental liabilities*

For background, environmental liabilities under Swiss law can encompass:

- civil claims, such as claims in tort (article 41 et seq of the CO and article 679 of the Swiss Civil Code (CC))[3] and claims in contract; and
- statutory liabilities, such as:
  - fines. For example, under the Federal Act on the Protection of the Environment (EPA),[4] fines may be imposed for various statutory offences, such as exceeding certain emission

[3] According to the said provision of the Swiss Civil Code, a party may be liable if it caused damage or pollution to another party's land.

[4] Apart from the EPA, there are various other pieces of environmental legislation, including but not limited to the Federal Act on the Protection of Waters (WPA), Federal Act on the Protection of Nature and Cultural Heritage (NCHA), Federal Act on Forest (ForA), Federal Act on Protection Against Dangerous Substances and Preparations (ChemA), Ordinance on the Avoidance and the Disposal of Waste

limits,[5] the failure to maintain air pollution control and the failure to use or deal with hazardous substances in such a manner as not to cause pollution to the environment;[6] and

- remediation / clean-up costs. For example, under the EPA, the Federal Office for the Environment (FOEN) or the cantonal authorities may direct the owner or occupier of premises to take certain remedial actions if they have reason to believe that the emission of air impurities, or the emission or discharge of any hazardous substance or toxic substance from any premises is likely to cause pollution of the environment or be injurious to public health or safety.

There is generally no distinction as to how the various types of environmental liabilities are treated under a composition agreement. Statutory liabilities are susceptible to be restructured under a composition agreement and, unlike some jurisdictions, there is no express prohibition against restructuring fines under a scheme.

### *2.1.2 Priority given to environmental liabilities*

As mentioned in section 1 above, the approval of a composition agreement by the composition court requires that privileged claims are satisfied in full. Environmental liabilities do not fall within any of the statutorily-prescribed categories of preferential debts which receive priority in a bankruptcy liquidation. However, there are exceptions where environmental liabilities could be classified as secured debts, for example if the liabilities are secured by a security interest (for example, in a financing transaction where a lender takes a mortgage over a borrower's land).

### *2.1.3 Disclaimer of environmental obligations*

While a composition agreement can in principle restructure environmental liabilities, it does not relieve a company of its ongoing or subsisting statutory or contractual obligations post-restructuring. For example, a company that continues to emit pollutants or hazardous substances after it emerges from a restructuring could be liable to new offences that attract additional fines. In practice, this means that a company that intends to continue operating its plant or factory (as opposed to selling it) would need to ensure it has the resources post-restructuring to be able to meet its environmental obligations.

Unlike other jurisdictions, such as Singapore and the United Kingdom, the company and its administrator have no power to disclaim onerous property (i.e. property such as a plant or a factory which is subject to continuing and onerous environmental obligations that are to be performed over a substantial period of time and which will involve expenditure that may not be recovered). Hence, no power of disclaimer may be used to relieve a company of its statutory environmental obligations. In other words, the Swiss legislator is of the opinion that the interest in protecting the environment in Switzerland should take precedence over the interest in ensuring a fair and orderly insolvency proceeding which may lead to the opening of bankruptcy proceedings if the environmental burden of a distressed company is too high.

## 2.2 Social (S): restructuring health or safety-related liabilities

Similar to the restructuring of environmental liabilities, health or safety-related liabilities can be restructured under a composition agreement in the same way as ordinary liabilities of a company. As mentioned above, any pecuniary claims against a company may be restructured under a composition agreement, including contingent, unproven or unliquidated claims. There are no special restrictions or conditions that apply when restructuring health or safety-related liabilities. However, the composition agreement does not relieve a company of its ongoing or subsisting statutory or contractual obligations post-restructuring.

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(ADWO), Federal Act on the Reduction of CO2 Emissions (CO2 Act), Ordinance on Air Pollution Control (OAPC), Noise Abatement Ordinance (NAO), Ordinance on the Remediation of Contaminated Sites (CSO), Radiological Protection Act (RPA), and Federal Law on Protection Against Hazards by Non-Ionising Radiation and Sound (NISSG).

[5] EPA, art 61.

[6] ChemA, art 49 et seq.

#### 2.2.1 *Types of health and safety-related liabilities*

For background, health or safety-related liabilities under Swiss law can encompass:

- civil claims, such as claims in tort[7] and claims in contract;[8] and
- statutory liabilities, such as:
  - fines. For example, selling faulty products or unsafe food are offences under article 16 et seq of the Federal Law on Product Safety (PrSG) and article 63 et seq of the Federal Act on Foodstuffs and Utility Articles (FSA), and failing to take the necessary measures to ensure the safety and health of employees at work is an offence under article 112 of the Federal Law on Accident Insurance (UVG); and
  - remediation costs. Safety authorities may serve a remedial order directing a person to remedy any danger that is affecting the safety, health and welfare of persons. Where the person fails to comply with the order, the authorities may take appropriate measures to prevent unauthorised entry or access to the area or the equipment or plant affected and may recover the costs and expenses incurred from the person served with the order.

#### 2.2.2 *Treatment of health and safety-related liabilities*

There is generally no distinction as to how the various types of health or safety-related liabilities are treated under a composition agreement. Statutory liabilities are susceptible to be restructured under a composition agreement and, unlike some jurisdictions, there is no express prohibition against restructuring fines under a composition agreement.

However, as mentioned in section 1 above, certain liabilities may be given priority treatment under a proposed composition agreement if they would have priority in a bankruptcy liquidation. Apart from claims based on an employment contract or a pension fund scheme, some examples of health or safety-related liabilities that may have preference or priority in liquidation are:

- all amounts due in respect of work injury compensation under the UVG, which is a preferential debt in a winding up pursuant to article 219(4), 1st Class B of the DEBA; and
- liabilities secured by a security interest (for example, in a financing transaction where a lender takes a mortgage over a borrower's land).

### 2.3 Governance (G): third party releases in favour of directors and officers of the company

There is no statutory provision or case law in Switzerland as to whether third party releases of debts can be granted in favour of directors and officers of the company (for example in relation to their actions taken in connection with the restructuring of the company), related party guarantors, banks, liquidators and debts of other group companies. Regarding the latter, Swiss law does not provide for any group restructuring rules. Instead, each and any legal entity within a corporate group is considered and treated separately for restructuring purposes.

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

[7] For example, a party may be liable for the negligent manufacture, distribution or supply of goods under Swiss tort law (CO, art 42, 55; Federal law on product liability (PrHG)).

[8] For example, a party that supplies defective or unsafe goods may be liable for breach of an express term of the contract or the implied term of satisfactory quality imposed by virtue of CO, art 197.

#### *3.1.1 Approving a restructuring plan*

There is no requirement for a composition agreement to be approved by environmental protection authorities or environmental advocacy groups. A composition agreement only needs to be approved by creditors and the court. However, as mentioned in section 2 above, authorities will have to abide by their own procedural laws with respect to whether they may approve a restructuring plan.

#### *3.1.2 Discretion to consider wider public interest concerns*

There is no statutory provision or case law in Switzerland concerning the extent to which the court may consider environmental issues in deciding whether to approve a composition agreement. The criteria to be met at the agreement confirmation stage (as described in section 1 above) primarily focus on the rights and interests of the creditors and do not incorporate a wider public interest assessment, not even the preservation of jobs. However, in practice it can be witnessed that some courts also take the public interest into consideration even though there is no legal basis for that. In most cases, it is argued that the preservation of jobs (e.g. in a court approved hive off or pre-pack transaction) reduces the priority liabilities of the subsequent bankruptcy estate.

#### *3.1.3 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

There are no statutory provisions in Switzerland which grant environmental protection authorities or environmental advocacy groups standing to air their views or concerns in a restructuring. There are also no other formal ways in which these parties may be indirectly involved in a restructuring process to safeguard environmental interests (e.g. by reviewing environmental licences or taking part in plan formulation or negotiations). However, they may have an impact on the court's decision by shaping the public opinion through media and other informal channels. In addition, in certain areas, the approval of a moratorium may lead to the withdrawal of a license or concession.

### 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

#### *3.2.1 Approving a restructuring plan*

There is no requirement for a composition agreement to be approved by labour authorities, unions or employee / worker advocacy groups. A composition agreement only needs to be approved by creditors and the court.

#### *3.2.2 Discretion to consider wider public interest concerns*

There is no statutory provision or case law in Switzerland concerning the extent to which the court may consider labour issues in deciding whether to confirm a composition agreement. The criteria to be met at the agreement confirmation stage (as described in section 1 above) primarily focus on the rights and interests of creditors and do not incorporate a wider assessment of employees' interests, except for their pecuniary claims that might be privileged to a certain extent and therefore have to be paid in full. However, in practice courts may nevertheless take the public interest into consideration.

#### *3.2.3 Protection of employee rights*

Generally, there are no statutory provisions in Switzerland which grant labour authorities, unions or employee / worker advocacy groups direct involvement in an in court restructuring. In contrast, out of court restructurings are subject to wider participation rights of employee groups or unions.

In any case, the company will have to grant its employees or any unions or labour protection authorities the right to be heard before starting a mass layoff. Otherwise, the company risks damages claims from its employees. Such claims might be privileged to a certain extent and therefore increase the financing requirements of a composition agreement. The same applies to claims due to unfair dismissal by the employer.

There are also no other formal ways in which these parties may be indirectly involved in a restructuring process to safeguard employees' interests, for example by monitoring the protection of employee rights or taking part in plan formulation or negotiations. However, they may have an impact on the court's decision by shaping the public opinion through media and other informal channels.

### 3.3 Governance (G): board / management conflicts addressed in a restructuring

Board / management conflicts are largely addressed in a restructuring through the disclosure requirements under the moratorium regime, as well as the conditions for deciding whether to confirm the composition agreement in the confirmation stage. If the directors or management personnel are receiving shares or options pursuant to an incentive plan as part of the restructuring, such matters would likely have to be disclosed in the explanations regarding the draft agreement to enable the creditors to assess what is in their commercial interests.

Outside the restructuring context, listed companies in Switzerland are also subject to article 732 et seq of the CO and the Stock Exchange Listing Rules, which help to address conflict of interest concerns regarding the remuneration of directors and key management personnel. According to these rules, the listed company must disclose such renumeration and obtain the approval of the General Assembly.

SIX Swiss Exchange (SIX) listed companies are also required to comply with the Directive on Information relating to Corporate Governance (Corporate Governance Directive), which includes disclosure requirements with respect to board renumeration, failing which they must explain the reason for any variation from the provisions of the Directive.

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

We have not identified any industry guidelines and / or best practices prescribed for the protection of the environment in a restructuring in Switzerland.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

There are no "soft law" instruments (such as industry guidelines, best practices, recommendations, codes of conduct and standards) in Switzerland which are not legally binding but serve to guide or influence a company to take actions or decisions that protect employees' interests specifically in a restructuring context.

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

There are no specific regulations concerning insolvency practitioners (IPs) in Switzerland. The responsibility for monitoring IPs lies with the relevant cantonal Supervisory Commissions for Attorneys-at-Law. Accountants are generally overseen by EXPERTsuisse, the specialist association for auditing, taxes and fiduciary experts, as well the Federal Audit Oversight Authority (FAOA). Certain cantons in Switzerland require an administrator patent (Sachwalterpatent).

The Swiss Federal Law on Lawyers' Free Circulation (commonly known as the Swiss Attorney Act), the rules of professional conduct of the Swiss National Bar Association and the cantonal bar associations as well as the Code of Conduct and Professional Ethics of EXPERTsuisse prescribe general guidelines as to how insolvency professionals should deal with potential conflicts of interest, without specific reference to restructuring scenarios.

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

The number of ESG-linked finance transactions is constantly increasing in the Swiss financial market. The sustainable bond market is particularly active. The SIX is responsible for the listing of such bonds. It categorises the bonds according to the International Capital Market Association (ICMA) principles and differentiates between green bonds, social bonds, sustainability bonds and sustainability-linked bonds, with green bonds being the most prevalent type. Switzerland's Federal Government actively issues sustainable bonds and facilitates industry growth.[9]

Banks in Switzerland have also issued sustainability-linked loans which peg loan costs to a company's ESG performance (as calculated by various ESG metrics).[10] However, compared to the sustainable bond market, ESG-linked credit financing is not yet as developed in Switzerland.

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

Considering Switzerland's position as a global wealth management hub, sustainable investing (SI) has become a key aspect of Swiss banks' ESG efforts. Swiss banks commonly divide their SI strategy into subcategories, including research, transparency, impact assessment, ESG-risk management, process integration, proxy engagement and systematic exclusion of investment recipients.[11] Furthermore, the Swiss Banking Association (SBA) mandates asset managers to examine and adequately consider clients' ESG preferences.[12]

UBS and Credit Suisse are founding members of the United Nations Environment Programme's Net-Zero Banking Alliance (NZBA), which requires its members to commit to various efforts aimed at reducing the greenhouse gas emissions of their lending and investment portfolios to sustainable levels, such as transitioning their portfolios, setting targets for emissions reduction, publishing emissions data and reporting progress of their transition strategy and actions.[13] Most major Swiss banks are signatories of the UNEP FI's Principles for Responsible Banking (PRB). Around 200 financial service providers active in the Swiss market are Swiss Sustainable Finance (SSF) members. The SSF is a non-profit organisation that focuses on impact investments, ESG education, market studies and SI in wealth and asset management.[14]

Furthermore, some banks have launched autonomous foundations that promote social and environmental values, namely by partnering up with and funding suitable organisations and projects.[15]

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9 The Federal Government sees a functional sustainable bond framework as a means to adopt the 2030 Sustainable Development Strategy (2030 SDS): see https://www.newsd.admin.ch/newsd/message/attachments/72632.pdf.

10 One example is the Basel Cantonal Bank (BKB): see https://www.bkb.ch/de/geschaeftskunden/finanzierungen/nachhaltige-finanzierungen/sustainability-linked-loans.

11 For example, Credit Suisse (https://am.credit-suisse.com/international/en/asset-management/esg.html), Vontobel (https://am.vontobel.com/en/esg-investing), and Pictet (https://am.pictet/en/globalwebsite/global-articles/company/responsible-investment/tab/ResponsibleEconomics/5PillarsOfResponsibleInvestment).

12 https://www.swissbanking.ch/_Resources/Persistent/a/5/e/0/a5e0845f065a60699df88910ae675b7082e69411/SBA_Guidelines_investment_advice_and_portfolio_management_EN.pdf.

13 Members of the Net-Zero Banking Alliance are required to sign a Commitment Statement as a pre-requisite for joining the organisation. The Commitment Statement is accessible at: https://www.unepfi.org/wordpress/wp-content/uploads/2021/04/UNEP-FI-NZBA-Commitment-Statement.pdf.

14 https://www.sustainablefinance.ch/en/workgroups-_content---1--3036.html.

15 Prominent examples include the UBS Optimus Foundation (https://www.ubs.com/global/en/ubs-society/philanthropy/optimus-foundation.html) and the Julius Baer Foundation (https://www.juliusbaer.com/en/julius-baer-foundation).

### 5.3 Promoting ESG by the central bank and regulators

The Swiss National Bank (SNB), which is the central bank of Switzerland, has undertaken various efforts to promote ESG financing. The SNB's annual sustainability report[16] sets out how it puts the principles of sustainability into practice in its operational activities, with regard to its employees, society and the environment. Since 1996, the SNB had been pursuing an environmental management policy centred on an annual eco-performance assessment and aimed at reducing resource consumption. Since 2018, the previously published environmental report evolved into a sustainability report with the addition of two further key areas: employees and society. However, due to the fact that the SNB's mandate is statutorily limited,[17] ESG-related interventionism is only foreseen if ESG-risks have an impact on price stability or financial stability or trigger financial risks for the SNB.[18]

The SNB as well as the FINMA (Swiss Financial Market Supervisory Authority) are members of the Network of Central Banks and Supervisors for Greening the Financial System (NGFS).

SIX allows listed companies to notify the SIX Exchange Regulation (SER) that they issue a sustainability report in line with an internationally recognised standard.[19] These reports are then published by SIX for the purpose of informing market participants.[20]

Pursuant to article 964a et seq of the Swiss Code of Obligations, certain companies of public interest that are subject to an ordinary audit also have statutory non-financial reporting requirements that can roughly be divided into four categories:

- reporting on corporate social responsibility as a whole;
- reporting on metals and minerals business;
- reporting on child labour; and
- reporting on payments to government agencies.

These rules provide for the duty to report on areas such as the environment, social issues, labour issues, human rights aspects and the fight against corruption. If the company controls other domestic or foreign companies, the report must also include these companies.

As of 2024, Switzerland will refine these reporting requirements in accordance with the Task Force on Climate-Related Financial Disclosures (TCFD) recommendations.[21]

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16 https://www.snb.ch/en/iabout/snb/org/id/snb_org_eco.

17 See art 99 of the Swiss Federal Constitution (https://www.fedlex.admin.ch/eli/cc/1999/404/en) and Federal Act on the Swiss National Bank (https://www.fedlex.admin.ch/eli/cc/2004/221/en).

18 See recent Report of the Swiss Federal Council, Switzerland's highest executive authority: https://www.newsd.admin.ch/newsd/message/attachments/73603.pdf.

19 https://www.six-group.com/en/products-services/the-swiss-stock-exchange/market-data/shares/sustainability-reporting.html.

20 Almost all issuers apply the Global Reporting Initiative (GRI) standard, e.g. UBS and Vontobel. At present, (January 2023), the only exception is Credit Suisse which applies the Sustainability Accounting Standards Board (SASB) standard.

21 https://www.admin.ch/gov/en/start/documentation/media-releases.msg-id-91859.html.

# THAILAND

## 1. General overview of the restructuring regime

### 1.1 Formal restructuring procedures

The in-court restructuring procedure in Thailand is commonly referred to as a "business rehabilitation proceeding" under the Bankruptcy Act B.E. 2483 (1940) (BA), which is overseen by the Central Bankruptcy Court as well as the official receiver (who is a state-appointed authority).

The procedure can be initiated by either a voluntary debtor or a creditor or creditors filing a petition with the court for business rehabilitation. The following conditions are required for the filing of the petition:[1]

- the debtor is insolvent or unable to pay its debts which have become due;
- the debtor owes a definite amount of not less than 10 million Thai Baht to one or more creditors; and
- there is reasonable cause to believe there are good prospects for rehabilitation of the debtor's business.

Upon the court's receipt of a business rehabilitation petition for its consideration, and until termination of the procedure, an automatic stay will be imposed on the debtor and its creditors.[2] Under this moratorium, the debtor's business and assets shall be carried on by an office holder, namely a planner, and protected from other legal proceedings initiated by its creditors. In effect, the debtor is prohibited from, among other things, making any disposal, distribution or transfer of assets, as well as making repayment of debts, creating new debts or creating any encumbrance over its own property, unless such action is necessary for continuation of its normal business operations. At the same time, creditors will be prohibited from initiating or pursuing civil lawsuits against the debtor or conducting legal execution against its assets, and thus shall be legally obliged to participate in the business rehabilitation proceedings to pursue the repayment of their debts.

While taking the petitioner's business rehabilitation petition, as well as objections of the objecting debtor and / or creditors into consideration, the court will issue an order for business rehabilitation if the aforementioned conditions for filing of the petition are met and it is apparent the filing is in good faith.[3]

Following the issuance of the order, the court will usually appoint a planner, who is tasked with carrying on the debtor's normal business operations on its behalf and preparing a business rehabilitation plan. Only the debtor, its executives or persons registered at the Debtor Business Rehabilitation Office can be appointed as a planner. At the time of submission of a business rehabilitation petition, the petitioner is required to propose a planner. If the objecting debtor and / or creditors propose another person to be the planner or the court deems that the person who has already been proposed is not suitable to be the planner, the planner will likely be chosen by the creditors' meeting and, subsequently, appointed by the court.[4]

Appointment of the planner by the court will result in a transfer of the power and duty to manage the debtor's business and assets from its executives to the planner.[5] In addition, the debtor's executives are required to provide detailed information concerning the debtor's business and assets to the planner,[6] who shall also refer this information to the official receiver.

As mentioned above, one of the main duties of a planner is to prepare a business rehabilitation plan within a maximum period of five months from the date of announcement of their

1 BA, s 90/3.
2 *Idem*, s 90/12.
3 *Idem*, s 90/10.
4 *Idem*, s 90/17.
5 *Idem*, s 90/25.
6 *Idem*, s 90/34.

appointment.[7] The plan shall contain various issues as required by the BA, for example the name and qualifications of the plan administrator, as well as their powers, details of the debtor's business and assets, classification of creditors, how and when repayment of debts to each class of creditors will be carried out and how additional financial assistance will be obtained.[8]

It is to be noted that classification of creditors serves a significant purpose of protecting creditors against unfair treatment since unsecured creditors whose claims are similar in nature are to be classified in the same group under the plan[9] and the creditors in the same group thereunder shall be treated equally.[10] In practice, however, the classification also serves as a tool for the planner to pursue a "cram down" of dissenting creditors during voting in a creditors' meeting.

Meanwhile, within one month from the date of the announcement of the appointment of the planner, all creditors are required to file for the repayment of monetary debts incurred prior to the date of the order for rehabilitation of the debtor's business with the official receiver, even if the debts are still conditional or have not become due yet.[11] The official receiver will take into consideration the debt repayment applications, supporting documents, objections of the debtor and / or creditors, as well as further witnesses and evidence of all involved parties, and determine the amount of indebtedness owed to each creditor.[12] This process will be conducted alongside the main business rehabilitation proceedings and can take from a few months to more than six months in certain unique cases. If a creditors' meeting is to be held in the meantime, the official receiver will determine the voting rights of the creditors pursuant to their initial opinion on the indebtedness of each creditor.[13] It is to be noted that these debts to be filed for repayment are debts which will be "restructured" under the business rehabilitation plan.

For a business rehabilitation plan to become effective and binding on all creditors, the plan has to be accepted by the creditors' meeting and, subsequently, approved by the court.

Upon submission of the plan by the planner, the official receiver will call for a creditors' meeting to consider the plan.[14] The plan will be deemed accepted by the creditors' meeting if either of the following thresholds is met:[15]

- the plan is accepted by all groups of creditors, with a majority of creditors having at least two thirds of the total amount of debts owed to the creditors in each group, that are present and cast their votes in the creditors' meeting; or

- the plan is accepted by at least one group of creditors, with a majority of creditors present and casting their votes having at least two thirds of the amount of debts owed to all creditors in that group, provided that the aggregate amount of debts owed to the creditors in every group voting in acceptance of the plan is not less than 50% of the creditors in all groups that are present and cast their votes in the creditors' meeting.

From the aforementioned principle, it is apparent that, if the planner can secure acceptance from one group of creditors having the amount of debts owed to them of at least 50% of the debts of all creditors, the plan will be deemed accepted by the creditors' meeting. It might be easier if the planner has the support of secured creditors, considering the fact that each secured creditor having at least 15% of the debts of all creditors will be classified as a group, while the remaining secured creditors will also be classified as a group.[16]

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7 *Idem*, s 90/43.
8 *Idem*, s 90/42.
9 *Ibid*.
10 *Ibid*.
11 *Idem*, s 90/26.
12 *Idem*, s 90/32.
13 *Idem*, s 90/30.
14 *Idem*, s 90/44.
15 *Idem*, s 90/46.
16 *Idem*, s 90/42 bis.

Once a business rehabilitation plan is accepted by the creditors' meeting, the plan will be referred to the court for approval.[17] The court will consider the plan, together with the analysis report prepared by the official receiver, statement of the planner, and objections of the debtor and / or creditors who did not vote in acceptance of the plan.[18] Although the court has a certain degree of discretion, the court is likely to approve the plan if the following conditions are met:[19]

- the plan contains complete particulars;[20]
- proposals for the repayment of debts do not lead to unequal treatment between creditors in the same group[21] and, if the plan is not accepted by all groups of creditors, such proposals must be in accordance with the order prescribed by law in connection with the distribution of property in bankruptcy proceedings,[22] unless the creditors have given consent; and
- the successful implementation of the plan will result in creditors receiving repayment in the amount of not less than what they would receive in the case where the court adjudges the debtor bankrupt.

After the court approves the business rehabilitation plan, the power and duty to manage the debtor's business and assets will be transferred from the planner to the plan administrator.[23] The terms and conditions of the plan, especially those concerning repayment of debts, will become effective and binding on all creditors.[24] Thereafter, the plan administrator will proceed to operate the debtor's business, manage its assets, obtain necessary funds for future operation and make repayments to all creditors according to the plan.

## 1.2 Informal restructuring procedures

There is neither any legislation nor guidelines in Thailand that govern out of court restructuring. However, it is a normal practice for financial institutions or other major loan providers to seek consensual restructuring of the provided facilities, and the debtor is usually called to discuss, among other things, a standstill period, extension of repayment terms, and / or a haircut of interest amounts. There may be several of these sessions and the debtor might need to negotiate with several banks, in the case of a syndicated loan, before any conclusion can be reached between the parties.

Usually, it is only in the case where the debtor is uncooperative, or all major creditors cannot agree to the informal restructuring that the creditors will initiate legal action against the debtor.

## 2. Restructuring of ESG-related liabilities

## 2.1 Environmental (E): restructuring environmental liabilities

Under the BA and other Thai legislation, environment-related liabilities owed by the debtor can be restructured in business rehabilitation proceedings, similar to other unsecured claims against the debtor.

### *2.1.1 Types of environmental liabilities*

As mentioned above, debts incurred prior to the date of issuance of an order for rehabilitation of the debtor's business shall be filed for debt repayment and will be restructured under a business rehabilitation plan.[25] However, this does not include obligations to act or refrain from acting and

17 *Idem*, s 90/56.
18 *Idem*, s 90/57
19 *Idem*, s 90/58.
20 *Idem*, s 90/42.
21 *Ibid.*
22 *Idem*, s 130.
23 *Idem*, s 90/59.
24 *Idem*, s 90/60.
25 *Idem*, s 90/26.

only involves monetary claims, examples of which, concerning environmental liabilities, are as follows:

- compensation for damages. For example, under the Enhancement and Conservation of National Environmental Quality Act B.E. 2535 (1992) (ECNEQA), a debtor who owns or possesses a source of pollution which causes harm to another person's life, body, health, sanitation or assets might have to pay compensation for such damages, including compensation for expenses[26] or, in the case where the debtor damages natural resources owned by the state or which are in the public domain of the state, the debtor might have to compensate the state for such damages.[27] Further, under the Hazardous Substances Act B.E. 2535 (1992) (HSA), a debtor who manufactures, imports, transports, refers, exports or possesses hazardous substances might be liable for damages incurred from such hazardous substances;[28]

- compensation for expenses of the official authority. For example, expenses the official authority has to spend in order to get rid of the pollution under the ECNEQA,[29] or expenses the official authority has to spend to amend or relieve damages to persons, animals, plants, or the environment under the HSA;[30] and

- fines. For example, a debtor who violates the ministerial regulation concerning quality control of water drainage or air exhaustion under the Factory Act B.E. 2535 (1992) (FA)[31] or the ministerial regulation concerning using, maintaining, transporting, eliminating, disposing of hazardous substances under the HSA[32] will be subject to a fine.

It is to be noted that in certain cases directors or executives of a company will be liable alongside the company. For example, under the ECNEQA, the Supreme Court has ruled that the directors of a company which causes environmental damages shall be liable together with the company. Similarly, directors who are responsible for a company's action which breaches the FA or HAS shall be liable for a fine, together with the company.

### *2.1.2 Priority given to environmental liabilities*

Other than secured debts which have the highest priority in repayment, priority is given to unsecured debts in business rehabilitation proceedings under the BA and repayment thereof under the plan has to conform with the priority given to unsecured debts under bankruptcy proceedings, which can be specified as follows:[33]

- expenses incurred in administration of the deceased debtor's estate;

- expenses incurred by the official receiver in management of the debtor's property;

- expenses incurred in connection with the deceased debtor's funeral as suitable for condition of life;

- fees for collection of property in bankruptcy proceedings;[34]

- fees incurred by the plaintiff creditor and lawyer's fees as determined by the court or the official receiver; and

- taxes and duties due within six months prior to issuance of a receivership order (in this case issuance of a business rehabilitation order) and money which employees are entitled to

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26 ECNEQA, s 96.
27 *Idem*, s 97.
28 HSA, s 63.
29 ECNEQA, s 96.
30 HSA, s 69.
31 FA, s 45.
32 HSA, s 71.
33 BA, s 130.
34 *Idem*, s 179(3).

receive prior to such date in return for service performed for the employer debtor under labour protection laws.[35]

There will be no expenses for items 1, 3 and 4 above in business rehabilitation proceedings.

Nonetheless, environmental liabilities are not given any priority and are ranked similarly to those of other unsecured creditors.

### *2.1.3 Disclaimer of environmental obligations*

As noted above, under business rehabilitation proceedings, debts filed for repayment which are to be restructured under a business rehabilitation plan shall be monetary claims for debts incurred prior to the date of issuance of the order for rehabilitation of the debtor's business.[36] Thus, if environmental liabilities have been occurring continuously before and after issuance of the order, only the portion which occurred prior to the order may be haircut under the plan, while the remaining liabilities will have to be dealt with outside of the proceedings.

Nonetheless, if the continuing environmental liabilities outweigh the benefits the debtor receives from certain assets or contracts, the plan administrator can disclaim such assets or contracts based on the notion that they are onerous within two months from the date the plan administrator acknowledges the court's order for approval of the plan.[37]

Upon disclaiming the onerous assets or contracts, the affected creditors can file for debt repayment for compensation even if the debts were incurred after the date of issuance of the order for rehabilitation of the debtor's business, and their claims will be repaid in accordance with the plan.[38]

## 2.2 Social (S): restructuring health or safety-related liabilities

Under the BA and other Thai legislation, health or safety-related liabilities owed by the debtor can be restructured in the business rehabilitation proceedings similar to other unsecured claims against the debtor.

### *2.2.1 Types of health and safety-related liabilities*

Examples of health and safety-related monetary liabilities which might be filed for repayment and restructured under a business rehabilitation plan under the BA are as follows:

- compensation for damages. For example, tort claims for damages incurred from food poisoning or negligence of a debtor which caused harm to other people; and

- fines. For example, a debtor who violates the ministerial regulation concerning quality control of production of foods, ingredients, production process and packaging, or foods that are prohibited from being manufactured, imported or distributed under the Food Act B.E. 2522 (1979) (FA),[39] or the ministerial regulation concerning management of safety, health, and environment in the work place under the Safety, Occupational Health, and Environment at Work Act B.E. 2554 (2011) (SOHEWA),[40] or the ministerial regulation concerning medicine and environmental health service under the Control of Occupational Diseases and Environmental Diseases Act B.E. 2562 (2019) (CODEDA),[41] will be subject to a fine.

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35 Civil and Commercial Code, s 257 and other provisions under the Labour Protection Act B.E. 2541 (1998) (LPA).
36 BA, s 90/26.
37 *Idem*, s 90/41 bis.
38 *Idem*, ss 90/41 bis, 90/42(10).
39 FA, ss 47-51.
40 SOHEWA, s 53.
41 CODEDA, s 42.

#### *2.2.2. Treatment of health and safety-related liabilities*

Similar to the case of environmental liabilities specified in sections *2.1.2* and *2.1.3* above, health and safety-related liabilities do not have priority in business rehabilitation proceedings under the BA, and assets and contracts which come with onerous liabilities may be disclaimed under the plan.

### 2.3 Governance (G): third party releases in favour of directors and officers of the company

Once the court approves a business rehabilitation plan, the plan becomes binding on all creditors in relation to repayment of debts which can be filed for repayment. However, the plan can only govern the debts owed by the debtor to these creditors and cannot alter or release liabilities any third party might have with the same creditors, for example in their capacity as a guarantor or joint debtor.[42]

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

As mentioned in section 1, in order for a business rehabilitation plan to become effective and binding, it has to be accepted by the creditors' meeting and approved by the court.

Environmental protection authorities or advocacy groups may influence the process if they are creditors. In such a case, they can affect the acceptance and approval process by requesting for revisions of the plan, voting against the plan in the creditors' meeting, and / or objecting against the plan to the court. However, these rights belong to every creditor and are not specific to environmental groups.

#### *3.1.1 Approving a restructuring plan*

As mentioned in section 1, a business rehabilitation plan is subject to acceptance by the creditors' meeting and approval of the court.

#### *3.1.2 Discretion to consider wider public interest concerns*

Although the BA prescribes the conditions for the court to consider[43] and, if these conditions are met, the court usually approves the plan, the court still has the discretion to take into consideration other significant issues, for example fairness in general or adverse effects that approval or non-approval of the plan may cause to other interested parties. Despite the fact the Supreme Court has not considered environmental public concerns as one of these issues which might affect the decision of the court, it still might be another factor for the court to consider when the court is deciding whether to approve the plan.

#### *3.1.3 Influence of environmental protection authorities or environmental advocacy groups in a restructuring*

As mentioned above, creditors can have direct influence in the business rehabilitation proceeding by either voting against the plan in the creditors' meeting and / or objecting against the plan to the court.

Furthermore, environmental protection authorities or advocacy groups, in their capacity as a creditor, can raise their concerns in the creditors' meeting, and, even if they do not vote in favour of the plan, they can object against the plan and will be given the opportunity to present their case before the court.

42 BA, s 90/60.
43 *Idem*, s 90/58.

### 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

Although labour claims may be more protected than other unsecured creditors, the rights of labour authorities, unions, or employee / worker advocacy groups remain mostly the same as other creditors.

#### *3.2.1 Approving a restructuring plan*

This is addressed in sections 1 and *3.1.1* above.

#### *3.2.2 Discretion to consider wider public interest concerns*

This is addressed in sections 1 and *3.1.2* above.

However, it is to be noted that, in practice, a business rehabilitation plan might be frowned upon by the court if employees' rights are significantly affected by the plan, especially concerning repayment terms and conditions.

#### *3.2.3 Protection of employees' rights*

This is addressed in sections 1 and *3.1.3* above.

In addition, it is to be noted that payment owed to employees under the Civil and Commercial Code and LPA have priority in repayment schemes in business rehabilitation proceedings.[44]

### 3.3 Governance (G): board / management conflicts addressed in a restructuring

It is not uncommon for the court to appoint the debtor as the planner. In such a case, the debtor's board of directors will remain in control and continue to manage the debtor's business and assets, while preparing for the plan's implementation. In addition, it is also common for the planner, who is the debtor, to propose itself as the plan administrator for the creditors' meeting and the court's approval.

However, it is not common for the plan to include direct benefits such as a salary or expenses or the provision of new shares in the company for the plan administrator who is the debtor and / or the board of directors because this might adversely affect the view the court has of the plan and its relative fairness to the creditors.

Nonetheless, if there are indications that the planner and / or plan administrator, who is the debtor, cannot manage its business and assets for the benefit of all creditors, there are a few solutions which can be sought by a creditor:

- objecting to a business rehabilitation petition which proposes that the debtor becomes the planner and proposing an alternative planner for the creditors' meeting to vote on and for the court's approval;[45]
- vote in the creditors' meeting against a business rehabilitation plan which proposes that the debtor becomes the plan administrator;
- propose that the plan be revised by changing the plan administrator (this would still need the approval of the creditors' meeting).[46] If the planner does not allow such revision, despite the creditors' meeting giving its approval, the creditors' meeting can still appoint a new planner;[47]

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44 *Idem*, ss 90/58(2), 130.
45 *Idem*, s 90/17.
46 *Idem*, s 90/45.
47 *Idem*, s 90/51.

- object to a business rehabilitation plan which proposes that the debtor becomes the plan administrator to the court; and

- report to the official receiver and request the official receiver to file a petition to the court to revoke the plan administrator if the plan administrator does not conform to the plan, performs its duties dishonestly, causes damages to the creditors or the debtor or is no longer suitable to be the plan administrator.[48]

## 4. "Soft law" framework

We have not identified any soft law framework, such as industry guidelines and / or best practices, that is prescribed for the protection of the environment or employee rights in relation to restructuring processes or codes of conduct relating to the avoidance of conflicts of interest specifically applicable to restructuring professionals.

However, there are codes of conduct or professional frameworks implemented by financial institutions, regulators of financial institutions and the Stock Exchange of Thailand which may indirectly be applied to restructuring. This is discussed in section 5 below.

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds, and investments

Many Thai banks have launched ESG-related financing products. For example:

- Siam Commercial Bank provided a sustainability-linked loan in the amount of 6 billion Thai baht to Indorama Ventures due to its confidence in Indorama Ventures' vision for sustainability and effective international practices.[49] Siam Commercial Bank has also implemented its ESG investment products by making ESG factors important factors the bank considers in relation to the funding approval process and performance monitoring process;[50]

- Kasikorn Bank (KBank) has granted sustainable financing and investment worth more than 16 million Thai baht and intends to achieve 200 billion Thai baht in sustainable funding by 2030;[51]

- Krungsri (Bank of Ayudhya PCL) has launched its Solar Roof Lending Programme for businesses wishing to install solar roofs;[52]

- EXIM Thailand provides ESG Loans to combat global warming and climate change;[53] and

- TMBThanachart Bank (TTB) offers green loans that promote financing solar energy, biomass energy and waste management projects, as well as sustainability-linked loans. TTB is also the first Thai commercial bank to issue green bonds in Thailand.[54]

Additionally, some Thai banks and financial institutions actively engage in ESG-linked loans, bonds, or investments, such as Krungthai Bank[55] and Bangkok Bank.[56]

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48 *Idem*, s 90/67.
49 https://www.scb.co.th/en/about-us/news/jun-2022/sustainability-linked-loan.html.
50 https://www.scb.co.th/en/personal-banking/investment/esg-invest.html.
51 https://www.kasikornbank.com/en/News/Pages/ESG-Strategy-2023.aspx.
52 https://www.krungsri.com/en/newsandactivities/krungsri-banking-news/solar-roof-lending-program.
53 https://media.thaigov.go.th/uploads/document/142/2022/02/pdf/Doc_20220222112935000000.pdf.
54 https://www.ttbbank.com/en/sustainability/environmental-sustainability/climate-finance.
55 https://krungthai.com/en/sustainability/growing-together/sustainable-finance.
56 https://www.bangkokbank.com/en/About-Us/Corporate-Governance/Responsible-Lending-Policy.

### 5.2 Financial institutions (banks and funds) and their commitment to achieving ESG targets

On 13 August 2019, at the Bangkok Sustainable Banking Forum 2019,[57] the Bank of Thailand and the Thai Bankers' Association, together with 15 commercial banks, adopted the Sustainable Banking Guidelines on Responsible Lending, which set out four key factors: leadership and responsible lending commitment, stakeholder engagement, internal implementation mechanisms and transparency.[58] The objective of the Sustainable Banking Guidelines on Responsible Lending is to set the minimum expectations for responsible lending practices in relation to all commercial banks in Thailand.

In August 2022, the Thai Bankers' Association announced its ESG Declaration to set a clear direction for banking sectors in promoting ESG and raising awareness about sustainability. Under the ESG Declaration, the members of the Thai Bankers' Association agreed as follows:[59]

- governance: to ensure good corporate governance and effective oversight at the board level, with clear accountability and responsibility at the management level regarding the ESG agenda;
- strategy: to integrate ESG into business strategies and define frameworks for sustainable finance to support Thailand in making a harmonious transition towards a net zero society, as committed;
- ESG risk management: to incorporate ESG into relevant risk management processes;
- financial products: to utilise digital technology to increase financial accessibility, as well as to help customers achieve net zero emissions and sustainable growth;
- communication: to communicate and collaborate with all stakeholders in raising public awareness of ESG issues; and
- disclosure: to develop monitoring and reporting systems in line with Thailand's regulatory frameworks and global sustainability disclosure standards.

### 5.3 Promotion of ESG by the central bank and regulators

In Thailand, ESG has gradually become an important factor in the banking industry and for large corporations, especially for those corporations listed on the Stock Exchange of Thailand. The Bank of Thailand, the Securities and Exchange Commission, the Office of Insurance Commission and the Thai Bankers' Association play an important role in promoting ESG in the market.

Of particular note:

- the importance of ESG can be seen through the establishment of the Working Group on Sustainable Finance (WG-SF), which was founded to cooperate on a sustainable agenda and support the Thai economy in achieving the Sustainable Development Goals;[60]
- in 2017, the Regulators Steering Committee was established by the Bank of Thailand (BOT), the Securities and Exchange Commission (SEC), the Office of Insurance Commission (OIC), and the Ministry of Finance to discuss policy issues;
- subsequently, in 2019, the BOT, SEC, and OIC established the Working Group on Sustainable Finance (WG-SF) for the benefit of enhancing sustainable finance throughout Thailand's financial sector;
- in 2019, the Bank of Thailand and the Thai Bankers' Association, together with 15 commercial banks, adopted the Sustainable Banking Guidelines on Responsible Lending; and

57 https://www.bot.or.th/Thai/BOTMagazine/Pages/256204Knowledge02.aspx#.
58 https://www.tba.or.th/wp-content/uploads/2019/08/Guidelines-ResponsibleLending.pdf.
59 https://www.bot.or.th/English/AboutBOT/Activities/Pages/JointPress29082022.aspx.
60 https://www.bot.or.th/Thai/SustainableBanking/Documents/Sustainable_Finance_Initiatives_for_Thailand.pdf.

- in August 2022, the Thai Bankers' Association launched its ESG Declaration to support a strong collective commitment among the banking sector to expedite sustainable development.

# THE NETHERLANDS

## 1. General overview of the restructuring regime

### 1.1 Formal restructuring procedures

In the Netherlands, insolvency procedures are codified in the Dutch Bankruptcy Act (DBA). Currently, the DBA has three insolvency procedures with legislative amendments pending before the Dutch Government for the codification of a fourth procedure, being the Dutch pre-pack.[1] The existing DBA procedures are:

- bankruptcy (*faillissement*);
- suspension of payment (*surseance van betaling*); and
- composition plan procedure outside of bankruptcy (*akkoordprocedure buiten faillisssement*, the WHOA procedure) under the Act on Confirmation of Composition Plan (*Wet homologatie onderhands akkoord*, the WHOA).

While all three insolvency procedures have some form of court involvement, the WHOA procedure is a preventive restructuring procedure aimed at avoiding insolvency, as it is the Dutch implementation of the EU Restructuring Directive.[2] Therefore, we will discuss the bankruptcy and suspension of payment as the relevant formal restructuring procedures (in court) in the Netherlands, and we will discuss the WHOA procedure as a formal restructuring procedure (out of court).

#### *1.1.1 Bankruptcy*

Bankruptcy is the main insolvency procedure under the DBA. It is aimed at liquidation of the estate of a Dutch legal or natural person. If a person has ceased to pay its debts, the Dutch courts may declare it bankrupt on either: (i) the person's own request; or (ii) at the request of one or more of its creditors. A person may also be declared bankrupt for reasons of public policy (*openbaar belang*), although this is rarely used in practice.

The relevant Dutch court will – upon the declaration of bankruptcy – appoint a bankruptcy trustee (*curator*) and a supervisory judge (*rechter-commissaris*). The bankruptcy trustee will be responsible for the management and liquidation of the bankruptcy estate (*faillissementsboedel*). The bankrupt debtor will no longer have the power of disposition over its assets. The supervisory judge will be responsible for supervising the management and liquidation of the bankruptcy estate as performed by the bankruptcy trustee.

The bankruptcy trustee will liquidate the bankruptcy estate and pay the creditors of the bankrupt debtor the amount they are due in accordance with the priority of their claims. The creditors are required to submit their claims with the bankruptcy trustee for verification, which occurs at a verification meeting (*verificatievergadering*). The estate claims (*boedelvorderingen*), such as the costs of the bankruptcy and the salary of the bankruptcy trustee, are paid first. Then preferential claims are paid, such as the claims of the Dutch Tax Authorities. After that, ordinary unsecured claims (*concurrente vorderingen*) are paid. Secured claims have a separate treatment in bankruptcy. The holders of security rights may exercise their rights as if there was no bankruptcy. This means they can enforce their security rights in bankruptcy and redeem their claims from the collateral. Any unpaid amounts are treated as ordinary unsecured claims and will be paid *pari passu*.

While the purpose of a bankruptcy procedure is the liquidation of the bankrupt estate, the procedure also allows for the restructuring to occur. The bankrupt debtor may provide its creditors with a composition plan (*akkoord*) for the restructuring of its debts or as a liquidation plan. The creditors are allowed to vote on the plan. The plan is adopted if it is accepted by: (i) a

[1] The pre-pack has not been codified yet. Therefore, we will not discuss it in further detail in this chapter.
[2] Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks, on discharge of debt and disqualifications, and on measures to increase the efficiency of procedures concerning restructuring, insolvency and discharge of debt, and amending Directive (EU) 2017/1132 (Directive on restructuring and insolvency).

simple majority of the admitted creditors who appeared at the creditors' meeting; and (ii) who together represent at least half of the admitted or provisionally accepted claims by value of the total claims of the bankruptcy estate.

Once the plan is adopted by the requisite majority, the debtor may ask the court to confirm (*homologeren*) the plan. The court will confirm the plan, unless:

- the value of the bankruptcy estate exceeds what is offered under the plan;
- performance of the composition plan is not sufficiently guaranteed; or
- the composition plan was the result of fraud, undue preference of one or more creditors or other unfair methods, regardless of whether the company or any other party has cooperated therewith.

Once the composition plan is confirmed by the court, it is binding on all affected creditors, including dissenting, abstaining and absent creditors. However, a composition plan in bankruptcy only affects ordinary unsecured creditors and in principle does not affect secured creditors. Therefore, the use of composition plans in bankruptcy is not often used in practice as it cannot bind secured creditors.

### *1.1.2 Suspension of payment*

Suspension of payment is another formal insolvency procedure under the DBA. The main purpose of the suspension of payment is the restructuring of the debts of the bankrupt debtor. If an entity foresees that it will no longer be able to pay its creditors, it can request a suspension of payment. The relevant Dutch court will immediately grant a provisional suspension of payment (*voorlopige surseance van betaling*). The court will appoint an administrator (*bewindvoerder*) and a supervisory judge. Subsequently, a creditors' meeting will be scheduled to vote on the definitive suspension of payment. If a suspension of payment is granted, the court will decide on the term of the suspension of payment at a maximum of 1.5 years. During the suspension of payment, the debtor may request an extension of the term thereof one or multiple times for another period of a maximum of 1.5 years.

The suspension of payment is a (semi) debtor in possession (DIP) procedure, but the debtor does not have the full power of management and disposition of its assets. During the suspension of payments, the debtor is not authorised to take any act of management or possession with regard to the estate without cooperation, authorisation or assistance of the administrator. This means the debtor needs to work together with the administrator throughout the suspension of payment.

The main objective of the debtor during the suspension of payment is to restructure its debt through a composition plan. The debtor may provide its creditors with a composition plan. The creditors are allowed to vote on the plan. The plan is adopted if it is accepted by: (i) a simple majority of the admitted creditors who appeared at the creditors' meeting; and (ii) who together represent at least half of the admitted or provisionally accepted claims by value of the total claims of the debtor. Once the plan is adopted by the requisite majority, the debtor may ask the court to confirm the plan. The court will confirm the plan, unless rejection grounds are present (which are essentially the same rejection grounds as set out above in relation to a composition plan in bankruptcy). Once the plan is confirmed by the court, it is binding on all affected creditors. However, a composition plan in suspension of payment – like bankruptcy – only affects ordinary unsecured creditors. It does not affect secured creditors. If the debtor cannot restructure its debts through a composition plan, the suspension of payment may be converted into bankruptcy.

## 1.2 Informal restructuring procedures

In the Netherlands, informal restructurings are generally based on consensual agreements between a debtor and its creditors. There is no legal framework for an informal restructuring without any court involvement. The relevant parties negotiate a consensual deal and will need to agree thereto. However, if they cannot reach agreement consensually, parties may commence a WHOA procedure.

The WHOA procedure is a restructuring procedure that entered into force on 1 January 2021. It is the implementation of the EU Restructuring Directive in the Netherlands. The WHOA procedure is inspired by the United States Chapter 11 procedure and the United Kingdom scheme of arrangement.

The WHOA procedure has various features which make it an attractive tool for restructuring. The WHOA procedure provides *inter alia* for a moratorium, the restructuring of group guarantees, deactivation of *ipso facto* clauses, interim relief measures and rescue financing protection.

The introduction of the WHOA procedure has been a game-changer for the Dutch restructuring practice. The WHOA procedure facilitates restructurings outside of a formal bankruptcy procedure and suspension of payment. It is a DIP proceeding allowing for court confirmation of a composition plan. There are two versions of the WHOA procedure:

- a public WHOA procedure; and
- a private WHOA procedure.

The public WHOA procedure is listed in Annex A of the EU Insolvency Regulation (Recast).[3] Therefore, the public WHOA procedure is subject to a centre of main interests (COMI) test[4] for access to the procedure. It also provides for automatic recognition throughout the EU under the EU Insolvency Regulation (Recast). The private WHOA procedure is not listed in Annex A of the EU Insolvency Regulation (Recast), is not subject to a COMI test, and does not have the benefit of automatic recognition throughout the EU (rather, recognition depends on the conflict of law rules of each jurisdiction). Given that no COMI test applies, the private WHOA procedure is also accessible for foreign debtors that would like to restructure their debt using the WHOA procedure, provided there is sufficient connection with the Netherlands.

The WHOA procedure may be commenced if a debtor is in a position where it is reasonably likely that it will not be able to continue to pay its debts. The debtor may commence the procedure by filing a start declaration. If the debtor commences the WHOA procedure, it will be tasked with drafting the composition plan. However, it is also possible to have a restructuring expert (*herstructureringsdeskundige*) appointed, who will be responsible for the composition plan, while the debtor remains in charge of its business given that the WHOA procedure is a DIP proceeding. Each creditor, shareholder or the works council or employee representative body is able to request the court to appoint a restructuring expert to prepare a composition. The debtor is also authorised to make such a request. For the remainder of this chapter, we discuss the situation where the debtor offers a composition plan, noting that most of the matters discussed below apply *mutatis mutandis* if a restructuring expert is appointed.

Unlike a composition plan in bankruptcy and suspension of payment, a composition plan in a WHOA procedure may affect both secured and unsecured creditors. The debtor may determine to which groups of creditors and shareholders it will offer the plan. Under the plan, rights of creditors and shareholders may be amended. Hence, a composition plan in a WHOA procedure may, for example, lead to a debt write-off, amendment of finance documents, extension of the maturity date and a debt-for-equity swap. The creditors and shareholders may be divided into classes and will vote per class on the composition plan. The plan is adopted in each class if the creditors or shareholders that voted in favour of the plan represent two thirds of the total value of claims for which a vote has been cast in each class. If all classes have adopted the plan, the debtor may request the court to confirm the plan. However, the WHOA procedure also allows for a cross-class cram down: if at least one class of creditors has accepted the composition plan, the debtor may request the court to approve the plan, provided the approving class is an in-the-money class of creditors.

3 Regulation (EU) 2015/848 of the European Parliament and the Council of 20 May 2015 on insolvency proceedings (recast).

4 Pursuant to art 3(1) of the EU Insolvency Regulation (Recast), the court of the member states where the COMI of a debtor is situated shall have jurisdiction to open insolvency proceedings.

The court will confirm the plan, unless certain rejection grounds apply. Various rejection grounds will be assessed *ex officio* by the relevant Dutch court to assess whether due process has been observed. Further, the court confirmation of a composition plan is subject to a "best interests of creditors" test and to an "absolute priority rule" – both inspired by similar requirements in the United States Chapter 11 procedure. The absolute priority rule under the WHOA, however, provides a "reasonableness exception" to be assessed by the relevant Dutch court. The composition as approved by the court is binding on all affected creditors and shareholders (including dissenting, abstaining and absent creditors and shareholders).

## 2. Restructuring of ESG-related liabilities

### 2.1 Environmental (E): restructuring environmental liabilities

There are no special provisions that apply to the restructuring of environmental liabilities in the DBA. Based on case law, environmental liabilities do have another priority separate to ordinary unsecured claims, as environmental liabilities qualify as estate claims. As mentioned in section 1.1 above, estate claims have a higher priority in a bankruptcy procedure. This qualification is also relevant for a WHOA procedure, as the class composition in a WHOA procedure considers the priority of claims, including priority of claims in bankruptcy.

In Dutch legal literature, there had previously been debate on the question of whether environmental claims rank as estate claims. This debate has been settled largely in case law in recent years, as a result of which the general view is that environmental claims qualify as estate claims in a bankruptcy procedure, given that the bankruptcy trustee has to comply with environmental obligations. According to Dutch Supreme Court (*Hoge Raad*) case law, a bankruptcy trustee should comply with environmental requirements, regardless of the circumstances of the bankruptcy. If the bankruptcy trustee does not comply with these requirements, the failure is that of the trustee, acting on behalf of the estate, with the result that the claims qualify as estate claims and will have priority over other claims. This reasoning is also followed by the Administrative Jurisdiction Division of the Council of State (*Afdeling bestuursrechtspraak van de Raad van State*) from an administrative law perspective and the Trade and Industry Appeals Tribunal (*College van Beroep voor het bedrijfsleven*).

#### *2.1.1 Types of environmental liabilities*

The difference in the types of environmental liabilities is not relevant in terms of the treatment of the claims in a restructuring. To the extent this bears any relevance to their priority, reference is made to section *2.1.2* below.

#### *2.1.2 Priority given to environmental liabilities*

As discussed above, most environmental liabilities qualify as estate claims in bankruptcy. This relates to environmental liabilities that arise after a bankruptcy procedure is opened.

However, if an environmental claim arises out of an unlawful act (*onrechtmatige daad*) or contractual breach caused by the bankrupt debtor before the bankruptcy procedure was opened and the bankruptcy trustee cannot be considered responsible for these acts, the claims will be treated the same as ordinary unsecured claims.

#### *2.1.3 Disclaimer of environmental obligations*

In the Netherlands, no specific provisions apply on disclaiming environmental obligations under the DBA.

### 2.2 Social (S): restructuring health or safety-related liabilities

In the Netherlands, no special provisions apply on the restructuring of health and safety-related liabilities (e.g. product liability tort claims and asbestos claims). These claims will be treated as any other ordinary unsecured claims in a bankruptcy, suspension of payment or WHOA procedure.

#### 2.2.1 *Types of health and safety-related liabilities*

The difference between the types of health and safety-related liabilities is not relevant for their restructuring under Dutch law.

#### 2.2.2 *Treatment of health and safety-related liabilities*

Reference is made to sections 1.1 and 2.2 above. Under Dutch law, health and safety-related liabilities generally qualify as ordinary unsecured claims.

### 2.3 Governance (G): third party releases in favour of directors and officers of the company

Dutch law does not specifically allow or restrict third party releases of liability under a restructuring plan, other than for group guarantees under the WHOA procedure as discussed in section 1.1 above. Because there is no clear framework nor any formal guidance from the Dutch courts available based on case law, there is debate in Dutch legal literature on the question of whether it is acceptable to release third parties from their liabilities under a composition plan. This is especially the case in those circumstances where only a majority of creditors is required to accept the composition plan – which means that a dissenting or absent minority may be bound by it without explicitly accepting it.

Briefly put, three types of third party releases may be identified:

- the release of obligations of affiliates of the company with whom creditors do not always have a direct relationship or with whom they may have a direct relationship, but which would ordinarily be in place to protect the creditor against any breach by their debtor (i.e., the entity which is being restructured). For example, guarantees, joint and several liabilities and cross-collateralised obligations;
- the release of obligations of directors, shareholders and other parties which were involved with the debtor before the opening of the relevant insolvency procedure; and
- the release of the obligations of the bankruptcy trustee, lawyers, financial advisers and their respective companies and employees.

The first type of third party release is possible under a WHOA procedure. The WHOA contains a specific provision in the DBA which allows for such third party releases. However, it is uncertain whether this is possible in bankruptcy and suspension of payments.

It is also uncertain whether the second and third types of release are possible in composition plans in the Netherlands (regardless of whether that is a bankruptcy procedure, suspension of payment or a WHOA procedure). According to Dutch legal literature, most authors believe that the release of third party debtors will only apply against the parties who voted in favour of the plan, rather than to all parties who are bound by it. However, from Dutch case law, there have been composition plans in the past which contained third party releases and which have been confirmed by the courts.[5] The third party releases in those plans were, however, effectively not challenged, so it remains uncertain what the outcome would have been if third party releases were challenged by a dissenting creditor.

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5 The composition plan of the Dutch group companies of Lehman Brothers in 2008 contained an example covering the third type of third party release noted above. The composition plan included a provision to waive all liabilities of the bankruptcy trustees, their law firm, all employees of their law firm and all third parties appointed by the bankruptcy trustees. In the composition plan, the so-called "ordinary creditors" had to agree to this waiver, even though they would not have been required to waive these potential liabilities if the composition plan was not accepted and they may not even have voted at all or voted against the plan. The composition plan was accepted by the Dutch courts and to our knowledge not further challenged.

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

#### *3.1.1 Approving a restructuring plan*

In the Netherlands, a bankruptcy, suspension of payments or composition under the WHOA will be approved by the Dutch courts. Assuming the bankrupt entity is not a licensed financial institution, the court is the only authority involved (leaving aside certain regulated sectors, such as the energy sector). Environmental protection authorities and environmental advocacy groups do not have a formal role in the formal insolvency procedures, although they are important stakeholders in practice.

#### *3.1.2 Discretion to consider wider public interest concerns*

Dutch courts have attributed importance to societal interests (*maatschappelijk belangen*) in multiple bankruptcy cases, for example:

- the public interest to ensure that a company is restructured and transferred to a new owner, which according to the Dutch court can be considered as a valid reason based on societal interests to ignore the interest of a specific creditor;
- rights the bankruptcy trustee may have in acting on behalf of the collective creditors of the company compared to one creditor only, which again the court deems valid for reasons of societal interests; and
- the need for efficient settlement and set-off of the bankruptcy estate, which the courts generally do not consider to be of sufficient societal interests to take priority over individual creditors' rights.

When considering the role of the environment in insolvency procedures, it is interesting to assess whether it may be argued that environmental interests are also societal interests which a bankruptcy trustee needs to take into account and give weight to during a bankruptcy procedure. To our knowledge, no such case has been brought before the court yet.

#### *3.1.3 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

As indicated above, while environmental protection authorities and environmental advocacy groups do not have formal approval rights or other consent rights with respect to the restructuring itself in Dutch insolvency procedures, they are important stakeholders that can exert influence. For example, they play a role when reviewing environmental licenses in a formal insolvency procedure.

### 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

Dutch labour law contains the requirement for each company that has 50 or more employees to establish a works council (*ondernemingsraad*) in which the employees of the company are represented. Under certain circumstances, a works council can also be established for companies with less than 50 employees.

The works council is required to be requested for its advice for, *inter alia,* the following topics:

- transfer of control over the company or part thereof;
- vesting, taking or disposing of control over another company, as well as entering into, making material amendments in or cancelling a sustainable cooperation (*duurzame samenwerking*) with another company, including the entry into, materially amending or cancelling an important

financial participation due to or for the benefit of such company;

- cancellation of the business of the company or an important part thereof;
- important reduction, increase or other amendments of the business of the company; and
- an important amendment in the organisation of the company, or in the allocation of tasks within the company.

As the above are highly likely to occur in a restructuring scenario, there have been discussions in Dutch literature about whether the works council should also be asked for its advice on these topics if the company has already filed for bankruptcy, suspension of payments and/or a WHOA procedure.

Based on established Dutch Supreme Court case law, the works council has to be asked for its advice in bankruptcy when the bankruptcy trustee continues the activities of the bankrupt debtor. The bankruptcy trustee needs to ensure compliance with the relevant provisions applicable on works council advice. It is important to note, however, that there is no right for the works council to provide advice on the sale of goods or termination of employment contracts if it results in the termination of the business of the company. In these circumstances, the interest of the creditors to be repaid out of the bankruptcy estate is considered to outweigh the interest of the works council. On the contrary, if the sale of such goods or the termination of such employment contracts is aimed at maintaining the business and arranging a restart of the company, the works council has to be asked to provide its advice.

The position in suspension of payment is less controversial. The company is still trading and responsible for complying with the relevant provisions in law applicable to the works council.

When the WHOA was drafted by the Dutch legislature, the position of the works council was specifically taken into account in the explanatory memorandum (*memorie van toelichting*). As mentioned in section 1.1 above, the works council may take the initiative to commence a WHOA procedure and request the relevant Dutch court to appoint a restructuring expert.

Furthermore, throughout the WHOA procedure, the debtor is in a DIP proceeding. All its obligations remain in force, including its obligation to comply with the relevant provisions in law applicable to the works council.

If a company is required to request the works council for its advice, the board of the company has to provide the works council with a request for advice in relation to its envisaged plans at a moment in time where the works council can still reasonably influence the decision-making process. The board will have to provide the works council with the reasoning behind the envisaged plans, as well as the consequences to the employees and any mitigants for those consequences that have been considered by the board in relation to such plans.

The works council will then have at least one meeting with the board about the envisaged plans before it will provide its advice. Until the works council has provided its advice, the company cannot execute the envisaged plans.

Unless the envisaged plans are executed in accordance with the works council advice, the company is obliged to hold off execution of the plans for a month from the date on which the works council has been informed of its plans. Once the works council advice has been obtained, the company may continue to execute the envisaged plans. The board of the company may deviate from the advice of the works council in whole or in part, but is required to provide its reasoning as to why it has not considered the works council advice. Whether or not sufficient reasons are provided has to be considered on a case-by-case basis.

If: (i) the works council did not provide approval in full and the board continues with the envisaged plans; or (ii) facts or circumstances become known to the works council that it was not aware of when providing its advice and the works council wishes to amend its advice, the works council has the right to initiate proceedings before the Enterprise Chamber of the Amsterdam Court of Appeal

(*Ondernemingskamer*). The Enterprise Chamber will, consequently, assess the petition from the works council with urgency. Before deciding on the underlying matter, it can elect to hear any experts as well as employees of the company. If the Enterprise Chamber considers the appeal of the works council to be valid, it has the option to require the board to withdraw its decision fully or partially and / or to prohibit the board from taking the actions required for the envisaged plans. Any rights obtained by third parties as a result of the decision taken by the board cannot be prejudiced by the ruling of the Enterprise Chamber.

#### *3.2.1 Approving a restructuring plan*

This is outlined above.

#### *3.2.2 Discretion to consider wider public interest concerns*

This is outlined above.

#### *3.2.3 Protection of employee rights*

In bankruptcy, a bankruptcy trustee may terminate employment contracts, but a notice period of six weeks applies and the salary of employees qualify as estate claims, which gives them a higher priority.

Further, under a composition plan in a WHOA procedure, the rights of employees cannot be changed. The WHOA contains a carve-out for employee rights which means that employee rights are excluded from the scope of the WHOA and cannot be part of a composition plan under the WHOA.

### 3.3 Governance (G): board / management conflicts addressed in a restructuring

There are no specific provisions in the DBA that deal with conflicts arising in relation to management in a restructuring.

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

We are not aware of any industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

We are not aware of any specific industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring.

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

The Dutch Association for Insolvency Practitioners (INSOLAD) published practice rules for bankruptcy trustees in April 2019. The practice rules aim to fill gaps where neither the law / statute nor case law provide clarity for bankruptcy trustees as to how to act, and they represent the best practice measures and processes that most bankruptcy trustees believe to be valid. The practice rules solely provide guidance and are not intended to be enforceable or binding in any way.

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

In the Dutch market, we have seen a significant increase in the amount of loans being provided and bonds being issued, as well as investments being made, in accordance with either:

- the sustainability-linked loan principles prepared by the Loan Market Association (LMA), or the sustainability-linked bond principles prepared by the International Capital Markets Association (ICMA); or

- the respective green loan principles and social loan principles of the LMA and the equivalent green bond principles and social bond principles of the ICMA (as well as combinations thereof depending on the nature of the financing).

Although the sustainability-linked loan principles are generally considered to be more suitable for working capital facilities due to their nature, we have also seen project finance and leveraged finance transactions including a margin ratchet related to ESG targets, as well as KPIs and sustainability performance targets. We have also seen a significant increase in lenders generally requiring sustainability reporting by the borrower on an ongoing basis during the term of their loan. This is requested by Dutch banks but also by fund lenders, for example based on the Equator Principles[6] and the Poseidon Principles[7] for project financing and ship financing transactions.

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

Financial institutions in the EU, and also in the Netherlands specifically, are increasingly more focused on achieving ESG targets themselves and requiring their ESG targets to be met. This reflects their commitments as part of the Net-Zero Banking Alliance[8] and the UN Principles for Responsible Banking,[9] as well as the Equator Principles[10] and the Poseidon Principles.[11] It also reflects the significant increase in EU regulatory requirements covering ESG topics to which either financial institutions and funds themselves have to comply with and / or their borrowers have to comply with, such as:

- the Taxonomy Regulation;[12]

- the existing Non-Financial Reporting Directive;[13] and

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6 Equator Principles, EP4, July 2020.

7 Poseidon Principles, A Global Framework for Responsible Ship Finance, June 2019.

8 According to a search on the register of the parties adhering to the Net-Zero Banking Alliance on 3 February 2023, each of ABN AMRO Bank N.V., Coöperatieve Rabobank U.A., ING Bank N.V. and Triodos Bank N.V. are listed as members to the alliance.

9 According to a search on the register of the parties adhering to the UN Principles for Responsible Banking on 3 February 2023, ABN AMRO Bank N.V., Achmea Bank, Berlin Hyp AG, Coöoperatieve Rabobank U.A., De Volksbank, ING, the Netherlands Development Finance Company (FMO) and Triodos Bank N.V. adhere to the UN Principles for Responsible Banking.

10 As per the register of the signatories to the Equator Principles on 3 February 2023, each of ABN AMRO Bank N.V., Coöperatieve Rabobank U.A., De Volksbank, the Netherlands Development Finance Company (FMO), ING Bank N.V, NIBC Bank N.V. and NWB Bank are included.

11 On 3 February 2023, each of ABN AMRO Bank N.V. and ING Bank N.V. are listed as signatories, while we have also seen non-signatories taking into account the Poseidon Principles in their transactions.

12 Regulation (EU) 2020/852 of the European Parliament and of the Council of 18 June 2020 on the establishment of a framework to facilitate sustainable investment, and amending Regulation (EU) 2019/2088.

13 Directive 2014/95/EU of the European Parliament and of the Council of 22 October 2014 amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups.

- the upcoming replacement thereof in the form of the Corporate Sustainability Reporting Directive[14] (all of which are also applicable in the Netherlands).

### 5.3 Promoting ESG by the central bank and regulators

In addition to the regulatory requirements in the EU as mentioned above, the Dutch Central Bank (*de Nederlandsche Bank*) and the European Central Bank (ECB) are both responsible for the supervision of Dutch financial institutions and adhering to the Network for Greening the Financial System. Furthermore, the EU encourages lenders as part of European supervisory law requirements to provide loans to certain borrowers by allowing lenders to maintain less capital on their balance sheet in relation to those loans.

An example can be found in the European capital requirements regulation (CRR).[15] According to article 501a of the CRR, lenders are allowed to calculate their own funds requirements in accordance with the CRR and multiply this with a factor of 0.75 if the loan meets certain requirements relating to exposures to entities that operate or finance physical structures or facilities, systems and networks that provide or support essential public services.

Under the requirements, it is necessary to conduct an assessment of the contribution by the assets being financed to environmental objectives, such as: (i) climate change mitigation; (ii) climate change adaption; (iii) sustainable use and protection of water and marine resources; (iv) transition to a circular economy, waste prevention and recycling; (v) pollution prevention and control; and (vi) protection of healthy ecosystems.

Now that these assets are also likely to be within the scope of assets to apply the Green Loan Principles published by the LMA in cooperation with the Asia Pacific Loan Market Association (APLMA) and the Loan Syndications and Trading Association (LSTA),[16] lenders wanting to provide a loan complying with article 501a of the CRR will most likely also be triggered to follow the Green Loan Principles.

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[14] Directive (EU) 2022/2464 of the European Parliament and of the Council of 14 December 2022 amending Regulation (EU) No 537/2014, Directive 2004/109/EC, Directive 2006/43/EC and Directive 2013/34/EU, as regards corporate sustainability reporting.

[15] Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012.

[16] Green Loan Principles, Supporting environmentally sustainable economic activity, March 2023 - LMA, APLMA and LSTA.

# UGANDA

## 1. General overview of the restructuring regime

### 1.1 Formal restructuring procedures

The Insolvency Act of Uganda 2011 (Insolvency Act) and attendant regulations prescribe formal restructuring procedures in the form of corporate rescue mechanisms such as receivership, administration and arrangements.

Formal restructuring procedures in Uganda are usually adopted where the company's financial circumstances are particularly stressed – most commonly through administration. Generally, an insolvency practitioner takes control of the company's affairs from its directors when the company commences formal restructuring procedures.

The formal restructuring procedures under the Insolvency Act typically involve the following key steps:

- filing of statutory reports such as a statement of affairs, notices, deeds of arrangements, compromises and other related documents;
- petition for interim protective orders and moratoriums;
- insolvency practitioner appointments;
- disclosure of material information;
- conduct of creditors' meetings;
- setting aside of voidable transactions; and
- the payment of creditors' claims.

The Insolvency Act provides for creditor approval thresholds in limited contexts such as arrangements and administrations and only for the purpose of calling creditors' meetings rather than passing restructuring plans. The approval of creditors holding 10% of the value of all claims against the company is required for calling creditors' meetings to consider proposals for restructuring.

For compromises sanctioned by the court under the Companies Act 2012 (Companies Act) to be binding on all creditors, the compromise must have been approved by a majority of creditors representing three fourths in value of the creditors or class of creditors, or members or class of members as the case may be, present and voting either in person or by proxy at the meeting.

A restructuring plan is normally subject to the approval of regulatory bodies (approving bodies), particularly where the company is subject to regulatory control and supervision. The requirements that must be satisfied before the approving body approves a restructuring plan vary depending on the regulated sector and applicable law.

Generally, Ugandan law permits regulators to exercise a degree of discretion in determining and enforcing applicable restrictions on the types of debts, liabilities or claims that can be restructured under the available restructuring procedure(s).

### 1.2 Informal restructuring procedures

Informal restructuring procedures in Uganda are usually implemented by way of a contract between the distressed company and its creditors. In Uganda, the most common examples of informal restructuring procedures include debt restructuring (normally with a refinancing component) and exchange offers, debt for equity swaps (with the agreement of all affected creditors), group reorganisations, receiverships and asset or business divestments.

In informal restructuring procedures, the existing management may retain control if the company remains outside the formal statutory insolvency proceedings to effect a negotiated restructuring with its creditors. However, this is subject to the terms and conditions of the restructuring plan or the contract with creditors in place (if any).

The steps that are usually required under an informal restructuring procedure are largely a matter of contract between a company and its creditors. In practice, where a restructuring involves substantial debt and multiple creditors, the key steps usually involve:

- the establishment of a steering committee by a small group of leading creditors to act as a general point of liaison between the company and the other creditors;
- the negotiation of a standstill agreement, which usually prevents the creditors from taking any enforcement action against the company for a sufficient period of time to allow a more formal restructuring agreement between the company and its creditors, or a major group of its creditors, to be entered into; and
- the negotiation of a restructuring agreement setting out the basis on which the creditors will continue to lend to a company involved in a restructuring.

In informal restructuring procedures, the contract between the company and its creditors will usually spell out the applicable creditor approval thresholds required to pass a restructuring plan.

Restructuring plans in informal restructuring procedures are usually not subject to the approval of the court or other approving bodies, particularly where the company is not a regulated entity. Where the company is subject to regulatory control and supervision, the regulator must approve the restructuring plan. The requirements that must be satisfied before the approving body approves a restructuring plan vary depending on the regulated sector and applicable law.

Where parties in informal restructuring procedures contractually agree to court-sanctioned restructuring schemes in the form of arrangements, compromises and administrations, the Insolvency Act and attendant regulations provide that the court may consider the official receiver's report regarding the terms of the schemes and the conduct of the directors and other officers of the company.

The insolvency regime of Uganda provides no special case restrictions on the types of debts, liabilities or claims that can be restructured. Parties to informal restructuring procedures are free to agree on the nature and type of debts, liabilities or claims that can be restructured in this context.

## 2. Restructuring of ESG-related liabilities

### 2.1 Environmental (E): restructuring environmental liabilities.

Under Ugandan law, environmental liabilities (e.g., clean up or remediation costs imposed by environmental regulations) can be restructured in the same way as ordinary debt claims as no special statutory treatment or consideration is expressly reserved for these liabilities. The applicable law – the Insolvency Act and attendant regulations in particular – do not provide for special restrictions or conditions which apply when restructuring environmental liabilities.

#### *2.1.1 Types of environmental liabilities*

The typical environmental liabilities that a company may be subject to are generally prescribed in the environmental regime of Uganda, which is the National Environment Act 2019 and the attendant regulations. Notable liabilities include fines and penalties, compensation, disclosure or reporting requirements, clean-up or remediation costs and obligations, depending on the nature of the business.

Companies in Uganda may also incur liability under the English common law of nuisance, which is applied by Ugandan courts in the absence of written law where applicable.

#### 2.1.2 *Priority given to environmental liabilities*

The Insolvency Act provides for the priority and ranking of debts and liabilities that must be paid out of the general asset pool, but does not specifically address the priority of environmental liabilities.

However, to the extent the Insolvency Act does not categorise environmental liabilities as preferential claims, such liabilities would normally rank after preferential claims arising from debts due to fixed charge holders, liquidators' fees and expenses, wages, salaries or commissions, compensation or liability for compensation under the Worker's Compensation Act 2000, government taxes and compulsory contributions to the National Social Security Fund.

#### 2.1.3 *Disclaimer of environmental obligations*

The rules and principles applicable to the disclaimer or abandonment of property subject to debts under the restructuring procedure in the Insolvency Act generally apply to environmental obligations. This is because the Insolvency Act does not expressly provide for special exclusion of the application of these rules to property subject to environmental obligations.

In practice, it is common for restructurings involving share sales by limited liability companies to include a disclaimer of historical environmental liabilities (such as breaches of environmental permits by the company or contamination present on the properties) by the new shareholders. In this case, these liabilities do not transfer to the new shareholder(s) if they do not take an active role in the company's management.

In restructurings involving asset sales only, a similar disclaimer is usually agreed upon, in which case the selling company may remain liable for any historical environmental liabilities attached to the assets it has sold.

If the company whose assets are being sold is in administration or likely to become insolvent in the near future, the company will either not provide any indemnities, or if it does, these may be of limited practical value.

### 2.2 Social (S): restructuring health or safety-related liabilities

Under Ugandan law, health and safety-related liabilities (e.g., product liability tort claims and asbestos claims) can be restructured in the same way as ordinary debt claims.

Again, this is because the Insolvency Act and attendant regulations do not provide for special restrictions or conditions in relation to those liabilities.

#### 2.2.1 *Types of health and safety-related liabilities*

The typical health and safety-related liabilities that a company may be subject to in Uganda include fines and penalties, compensation, disclosure or reporting requirements, as well as clean-up or remediation costs and obligations.

These liabilities are prescribed in several statutes of general and specific application and the attendant regulations, including the Occupational Safety and Health Act 2006, the Workers' Compensation Act 2000, the Public Health Act 1935 and the Building Control Act 2013.

In determining liability for health and safety-related claims, Ugandan law also permits the application of English common law principles in relation to product liability and other tort-related claims by Ugandan courts.

#### 2.2.2 *Treatment of health and safety-related liabilities*

The Insolvency Act, which provides for the priority and ranking of debts and liabilities that must be paid out of the general asset pool, does not specifically address the priority of health and safety-related liabilities.

However, to the extent the Insolvency Act does not categorise health and safety-related liabilities as preferential claims, such liabilities would normally rank after preferential claims arising from debts due to fixed charge holders, liquidators' fees and expenses, wages, salaries and commissions, compensation or liability for compensation under the Worker's Compensation Act 2000, government taxes and compulsory contributions to the National Social Security.

### 2.3 Governance (G): third party releases in favour of directors and officers of thecompany

The question of whether third parties (other than the debtor company) may receive releases of liability under a restructuring plan is usually a matter of contract, since it is not expressly addressed in statute. The parties to a restructuring plan may agree on such third party releases by contract to the extent the Insolvency Act and attendant regulations do not expressly provide for special restrictions on doing so.

When adjudicating the questions of third party releases under a restructuring plan in favour of directors and officers of the company, Ugandan courts may also rely on English common law, which is specifically recognised as a source of law (subordinate to written law) by the Judicature Act, Cap. 13 as a useful reference point.

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

#### *3.1.1 Approving a restructuring plan*

The need for court consent in compromises or arrangements is provided for in the Companies Act – which generally applies to all companies, foreign and domestic – as well as sector-specific laws such as the Financial Institutions Act 2004 (as amended), which regulates the banking and financial sector.

#### *3.1.2 Discretion to consider wider public interest concerns*

The approving body has the discretion to consider wider public interest concerns (including environmental concerns) in deciding whether to approve a restructuring plan. The Financial Institutions Act 2004 (as amended) for instance, specifically obliges the sector regulator, the Bank of Uganda (BOU) to take into account public interest considerations as a condition precedent to the approval of a restructuring plan.

#### *3.1.3 Influence by environmental protection authorities or environmentaladvocacy groups in a restructuring*

Environmental protection authorities such as the National Environment Management Authority (NEMA) and the National Forestry Authority (NFA), and environmental advocacy groups, do not generally have the standing to air their views / concerns in a restructuring as no special case need for their views is provided for in the Insolvency Act.

However, while no statutory obligation is placed on the court or approving bodies to consider their views in a restructuring, approving bodies or Ugandan courts may in practice exercise a degree of latitude or discretion in deciding whether to consider their concerns.

Whereas the core regulatory functions such as reviewing environmental licences are strictly reserved for Uganda's environmental protection authorities such as the NEMA and the NFA, environmental advocacy groups may be allowed to indirectly take part in plan formulation or negotiations to the extent possible.

### 3.2 Social (S): influence by labour authorities, unions or employee / workeradvocacy groups in a restructuring

#### *3.2.1 Approving a restructuring plan*

Although a restructuring plan is not subject to the approval of labour authorities, the Employment Act 2006 requires employers to notify the Commissioner for Labour before a restructuring plan affecting 10 or more employees is implemented. In practice, prudent employers usually notify the Commissioner for Labour even where a restructuring plan affects even a single employee.

#### *3.2.2 Discretion to consider wider public interest concerns*

As noted above, the approving body has the discretion to consider wider public interest concerns in deciding whether to approve a restructuring plan.

#### *3.2.3 Protection of employee rights*

Labour authorities, unions and employee / worker advocacy groups have standing to air their views / concerns in a restructuring to the extent that the employees of the concerned company belong to a trade or labour union and are subject to an applicable collective bargaining agreement (CBA). Under the framework of a CBA, these parties may be indirectly involved in a restructuring process to safeguard employees' interests, for example by monitoring the protection of employee rights or taking part in plan formulation or negotiations.

A statutory right to institute legal action against an employer to safeguard employees' interests is reserved for labour unions and employee / worker advocacy groups under the Labour Unions Act 2006.

### 3.3 Governance (G): board / management conflicts addressed in a restructuring

In restructurings where the existing directors or management remain in control of the company and have the power to control or influence the formulation of a restructuring plan, potential conflicts arising in such situations are usually resolved by law or market standards / practice depending on the circumstances.

Legally, the Companies Act places a general duty on directors to act in good faith in the interests of the company, which extends to avoiding conflicts of interest. The Insolvency Act does not expressly exclude the application of this duty in a restructuring context.

In practice, potential conflicts are resolved by: first, determining whether a conflict of interest exists; secondly, disclosing the conflict to other directors or third parties; and thirdly, determining whether to act despite the conflict.

Under Ugandan law, the test of there being a conflict of interest is one of perception and objectivity. The position of Ugandan courts is that it is what a reasonable person would conclude while viewing the transaction from a distance that counts. Conflicts extend to situations in which an individual or corporation is able to exploit a professional or official capacity in some way for their personal or corporate benefit.

Established corporate governance codes such as the United Kingdom Corporate Governance Code and the OECD Code of Corporate Governance also serve as useful references to resolve potential conflicts in restructurings.

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that areprescribed for the protection of the environment in a restructuring

There are generally no "soft law" instruments (such as industry guidelines, best practices, recommendations, codes of conduct and standards) which serve to guide or influence a company to take environmentally responsible actions or decisions specifically in a restructuring context.

By default, companies in a restructuring context usually refer to guidelines or regulations issued by Uganda's environmental protection authorities such as the NEMA and the NFA to take environmentally responsible actions or decisions.

In practice, prudent companies, especially multinationals with a group corporate structure and other regulated entities, usually rely on relevant internal policies to guide their environmentally responsible actions or decision making.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

Generally, no industry guidelines and / or best practices of wide application are prescribed for the protection of employee rights in a restructuring context. In practice, however, companies in Uganda use internally generated policies or international best practices or standards from comparative jurisdictions as reference points.

The Employment Act of Uganda and other related labour laws and regulations also serve as a useful guide or influence a company to take actions or decisions that protect employees' interests specifically in a restructuring context.

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

Restructuring professionals are subject to industry codes of conduct relating to the avoidance of conflicts of interests depending on the field of qualification. The Insolvency Act provides that restructuring practitioners must be qualified lawyers, accountants and chartered secretaries.

The industry guidelines or codes of conduct relating to the avoidance of conflicts of interest that these restructuring professionals are subject to are:

- the Advocates (Professional Conduct) Regulations SI 267-2, which applies to restructuring professionals who are lawyers;
- the Certified Public Accountant (CPA) Code of Professional Conduct, which applies to accountants; and
- the ICSA Code of Professional Ethics and Conduct and the United Kingdom and Ireland Chartered Governance Institute (UKICGI) Code of Professional Ethics and Conduct, which apply to chartered secretaries.

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

ESG-linked loans, bonds and investments have been observed in Uganda. Notable features of these investments include sustainability-linked loans and "green loans" for the financing of environmentally-friendly projects and renewable clean technologies.

The leading financial institutions in Uganda now offer ESG lending and advisory services to major corporate and individual clients and are gradually increasing the proportion of the energy loan book committed towards green energy. Financial institutions have also rolled out deliberate marketing strategies to promote clean energy financing products.

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

Financial institutions have signed on to commitments to achieve ESG targets in their lending and investment portfolios and to apply ESG-risk management policies as a matter of individual preference and policy, since no uniform application of sector-specific ESG guidelines is currently in place. The commitment to achieve ESG targets in lending and investment portfolios or to apply ESG-risk management policies varies from institution to institution.

### 5.3 Promoting ESG by the central bank and regulators

The financial sector regulator, the BOU, is pursuing an ESG financing policy agenda by prioritising ESG principles in its policies and operations. The BOU intends to institutionalise an ESG framework across the regulated financial institutions via its new strategic plan.

Additionally, through a new Climate Change Risk Policy and other programmes, the BOU seeks to require the banking sector to review its business models by strengthening the links between the preservation of the natural environment (including green financing), which supports agriculture, and the risk-adjusted returns sought by shareholders.

There are also plans in place by the BOU to integrate climate risk management in macroprudential and risk-based supervision, as well as the monetary policy framework.

In December 2022, the BOU endorsed the collective efforts of Uganda's development partners to establish an appropriate green financing mechanism and fund (the aBi Finance Ltd Green Agribusiness Taxonomy and Green Finance Fund) to channel resources towards ESG-driven projects.

The BOU is currently compiling data on the extent, emphasis and nature of green financing within the financial sector to inform the development of efficient ESG guidelines for the sector with a focus on net zero carbon plans, among other sustainability issues.

# UNITED ARAB EMIRATES

## 1. General overview of the restructuring regime

The UAE is a federal state comprising seven emirates. While there are some differences in the laws of the various emirates, the laws governing restructuring and insolvency at a federal level are set out in Federal Law No. 9 of 2016, as amended (Bankruptcy Law). Subject to certain exceptions outlined below, the Bankruptcy Law is generally applicable to corporate entities incorporated in the UAE.

The UAE also has a number of "free zones" which, to a greater or lesser extent, are authorised to promulgate their own laws. However, it is only the two financial free zones – the Abu Dhabi Global Market (ADGM) and the Dubai International Financial Centre (DIFC) – that have full jurisdiction to enact and apply their own laws concerning bankruptcy and restructuring. As a general rule, entities incorporated in the ADGM or the DIFC will be subject to the bankruptcy and restructuring laws in the ADGM and the DIFC respectively and not the Bankruptcy Law.

This chapter focuses on the restructuring and bankruptcy laws (R&B) applicable generally to "onshore" UAE companies (i.e. excluding the ADGM and the DIFC). This chapter does not address the UAE law position in relation to the restructuring and bankruptcy of natural persons, for which the principal legislation is Federal Law No. 19 of 2019 on Insolvency, as amended.

The practice of restructuring liabilities of companies via a court-sanctioned process remains in its infancy. Prior to 2016 and the introduction of the Bankruptcy Law, the UAE did not have comprehensive R&B laws. The bankruptcy laws which did exist prior to 2016 were penal in nature and did not seek to facilitate the rehabilitation of viable businesses. As a result, restructurings in the UAE, when they did happen, tended to be implemented on a fully consensual basis and without any involvement from the court. In exceptional cases, bespoke legislation was introduced to facilitate the restructuring of strategically important businesses (e.g. the passing of Decree 57 in 2009 to support the restructuring of the Dubai World group of companies).

Notwithstanding the introduction of the Bankruptcy Law in 2016, adoption of the available processes was initially slow. Debtors, creditors and advisors were generally hesitant to utilise the new tools given, among other factors, the perceived unpredictability of a new regime. This started to change around the time of the COVID-19 pandemic, with a number of high-profile debtors filing for bankruptcy. This has significantly raised the profile of the Bankruptcy Law in the UAE and has enabled key stakeholders (including the UAE courts) to test the law and its available processes in practice. As has been witnessed in other jurisdictions, we anticipate that adoption levels will increase over time as stakeholders become more familiar with the available processes and continued improvements and refinements are made to the law.

The Bankruptcy Law applies to any company incorporated under Federal Decree Law No. 32 of 2021 on Commercial Companies (Companies Law), businesses in the free zones excluding the DIFC and the ADGM (which each have their own R&B regime), civil companies conducting professional business and traders. Additionally, a number of government-owned companies in the UAE are established pursuant to statutory decrees, rather than the Companies Law, and hence fall outside of the ambit of the Bankruptcy Law. Often, their constituting decrees contain provisions governing the rehabilitation and insolvency of such entities. The Bankruptcy Law, however, applies to state-owned companies if their constituting decree or constitutional documents expressly "opt in" to the Bankruptcy Law.

The Bankruptcy Law seeks to promote the rehabilitation of distressed but viable business via a court-controlled restructuring or preventative composition. A separate out of court (and non-binding) process is also available for regulated entities. Insolvent liquidation is also catered for under the Bankruptcy Law. Each of these are addressed in more detail below.

As a final general comment, it is also worth noting that, as a matter of Federal UAE law, the UAE has not entered into any international treaties relating to cross-border insolvency (such as the UNCITRAL Model Law on Cross-Border Insolvency) and is not party to any cooperation agreements relating to concurrent proceedings between the UAE and foreign courts in that regard. The Bankruptcy Law also does not contain any provisions on the recognition of such foreign proceedings, and consequently foreign judgments relating to R&B are enforced if the conditions listed in the Civil Procedure Law (Federal Decree Law No. 42 of 2022) have been satisfied. In practice, this is likely to make formal cross-border restructurings involving UAE entities challenging to implement in practice.

## 1.1 Formal restructuring procedures

### *1.1.1 Preventive composition*

Preventive composition is a debtor-led scheme that may only be opened at the debtor's request. It allows a debtor company which is facing financial difficulties to apply to the court to enter into a compromise agreement with its creditors. Critically though, a debtor company may only apply for a preventative composition if it is facing financial difficulties but is not cashflow insolvent (defined as a failure to pay due debts for more than 30 business days as a result of financial issues) and is not balance sheet insolvent (defined as the value of its assets being less than its due liabilities). In practice, this significantly limits the universe of debtors to which a preventative composition would be available (i.e. financially distressed but not so distressed that it has crossed one of the stated thresholds).

Under a preventative composition, a trustee is appointed by the court to assist with the negotiation of a composition scheme (PC Scheme) and its implementation. A PC Scheme requires approval by both a simple majority in number and two-thirds by value of the creditors whose debts have been permanently accepted. Secured creditors are entitled to vote on a PC Scheme if it affects their secured rights or if they have waived their security interest. Secured creditors cannot, however, have their secured rights compromised absent their consent.

To afford the debtor breathing space to formulate and agree to a PC Scheme, a moratorium on all legal and enforcement proceedings against the debtor applies from the date on which the proceedings are accepted by the court. As an exception to this, secured creditors of the debtor can enforce their security with the court's permission.

Upon approval by creditors, the PC Scheme is submitted to the court for ratification. In order to ratify the PC Scheme, the court must be satisfied it is in the interests of creditors and, specifically, that implementation of the PC Scheme would not result in any creditor being worse off than it would have been had the assets of the debtor been liquidated on the date on which the PC Scheme is voted upon.

As part of the implementation process, the debtor continues to manage the business under the supervision of the trustees, and the court may appoint a coordinating committee of creditors responsible for monitoring the implementation process and reporting on progress to the wider creditors. A counterparty to any contract to which the debtor company is a party may not terminate its contract on the sole basis that the debtor company has filed for preventive composition, if the debtor company continues to perform its obligations under those contracts after the commencement order. However, at the request of the trustee, the court may suspend or terminate a contract if the court considers it necessary to enable the debtor to transact its business; or if rescission of the contract would fulfil the interests of all creditors of the debtor company and would not materially prejudice the interests of the counterparty concerned.

On and from the date of the commencement decision, the debtor is restricted from conducting certain transactions without the court's approval (e.g., paying pre-commencement claims, disposing of assets and borrowing further money).

In connection with a PC Scheme, the court has the discretion to permit the debtor or the supervising trustees to secure additional financing, including on a priority basis. The court has discretion as to the exact priority that is provided, and new money creditors may be granted priority over unsecured creditors and / or be given the benefit of security over the debtor's unsecured assets. The Bankruptcy Law also contemplates that existing secured creditors can be "primed" to the extent the court is satisfied that their interests would not be adversely affected. It is not entirely clear as to how this "priming condition" would be interpreted in practice, however.

### *1.1.2 Restructuring*

The Bankruptcy Law also contemplates that a financially distressed company can be rehabilitated via a restructuring plan (RP).

The RP regime shares many of the features of preventive composition. These include supervision of the process by the court, the appointment of trustees for assisting with negotiations and implementation, the application of a moratorium, the same thresholds for approval of the RP by creditors, the same treatment of secured creditors and the option of securing of additional financing with court approval.

There are, however, some key differences:

- a RP process can be commenced not only by the debtor itself, but also by one or more unsecured creditors of the debtor (or a secured creditor to the extent its debt is not fully secured) if is owed an amount exceeding AED 100,000 and this amount has remained unpaid for at least 30 business days following a formal written notification of the debt to the debtor. In certain circumstances, an RP process can also be commenced by the court, a regulator or a public prosecutor;

- the commencement of a restructuring process requires the debtor company to be either cashflow insolvent (defined as a failure to pay due debts for more than 30 business days as a result of financial issues) or balance sheet insolvent (defined as the value of its assets being less than its due liabilities); and

- under a restructuring process, the debtor generally cedes control of the company to the court-appointed trustee (which has served as a disincentive for companies to file for a RP process).

In the event the RP process fails for any reason (including when the trustees consider the plan impossible to implement, where sufficient creditors do not approve or when the debtor acts in bad faith), the court may declare the debtor insolvent and order an insolvent liquidation.

### *1.1.3 Bankruptcy and liquidation*

The Bankruptcy Law provides for an "end of the line" bankruptcy and liquidation process. This can be commenced by either a debtor or a creditor (with the same thresholds as for a RP process). While a debtor or creditor can specify a preference for bankruptcy and liquidation, the court has discretion to proceed with a RP process if it considers it possible to restructure the company. Bankruptcy and liquidation can also be ordered by the court following the failure of a PC Scheme or a RP process or in the event of bad faith on the part of the debtor.

Under a bankruptcy and liquidation, a trustee appointed by the court determines, liquidates and distributes the assets among the creditors whose debts have been admitted. The order of priority for the distribution of proceeds from the liquidation of assets is as follows:

- secured creditors up to the realised value of their secured asset(s), provided that fees and expenses incurred in connection with the disposal of secured assets are paid before distributions are to the relevant secured creditor;

- preferred creditors; and

- unsecured creditors.

Preferred creditors have a set order of priority, with creditors in a given class being ranked equally.

Preferential debts are as follows:

- any judicial fees or charges, including the fees of trustees and experts and any expenses incurred for the common benefit of the creditors to maintain or liquidate the assets of the debtor;

- unpaid end of service gratuity, wages and salaries of the employees, workers and staff of the debtor periodically paid (save for any kind of allowances, bonuses, other incidental payments or any other benefits), not exceeding a maximum of three months' pay;
- debts of maintenance paid by the debtor under a judgment delivered by a competent court;
- any amounts payable to governmental bodies; and
- fees, costs or expenses incurred after the initiation of the bankruptcy process to procure commodities and services to the debtor or to continue the performance of any other contract that benefits the debtor's business or assets; or any fees, costs or expenses incurred to continue the course of business of the debtor after such date.

#### *1.1.4 Emergency financial crisis*

To deal with the adverse economic impact caused by the COVID-19 pandemic, various changes were introduced in the Bankruptcy Law with effect from 22 October 2020. These include declaration of an emergency financial crisis, being a general situation that affects trade or investment in the UAE, such as a pandemic, natural or environmental disaster or war, subject to determination of its existence and duration by a UAE cabinet with the approval of the Minister of Finance. Cabinet resolution No. 5 of 2021 deemed the circumstances resulting from the COVID-19 pandemic as an emergency financial crisis during the period from 1 April 2020 to 31 July 2021.

Among other things, if an emergency financial crisis has been declared and has not expired, this provides an additional (and more flexible) route for a debtor company to restructure its debts (provided that the cause of the financial issues relate to the declared crisis). Within such a process, a debtor is granted a 40 business day period to negotiate a settlement agreement with its creditors, with that settlement being sanctioned if approved by creditors holding two-thirds by value of the outstanding debt (without any numerosity test). A debtor would also benefit from a moratorium and the ability to raise priority financing. In theory, the process contemplates significantly less involvement from the court. We are not aware of any situation having made use of the emergency financial crisis regime and, so far as we are aware, the period for accessing this process has now expired.

### 1.2 Informal restructuring procedures

Section 3 of the Bankruptcy Law contemplates the issuance of a cabinet resolution for establishing a financial committee responsible for, among other things, supervising out of court restructuring processes for regulated financial institutions in the UAE and monitoring the implementation of the Federal UAE bankruptcy law. Pursuant to Cabinet Resolution No. 4 of 2018 (2018 Resolution), which came into force on 1 March 2018, the Financial Restructuring Committee (FRC) was established with such powers. In 2019, the mandate of the FRC was extended to include all establishments which are regulated by a regulatory authority in the UAE.

The FRC exists to facilitate consensual restructurings between an in-scope debtor and its creditors. It is important to note, however, that the FRC does not have any powers to compel or impose resolutions. The FRC process also does not come with the benefit of a moratorium on legal and enforcement proceedings. In addition, commencement of a formal R&B process (as outlined above) would immediately terminate the FRC process.

Save for the FRC and the emergency financial crisis process, the UAE courts are otherwise heavily involved in formal restructuring processes in the UAE.

### 1.3 Directors' duties

In the ordinary course, directors and managers are not liable for the debts of the company which they represent. In the context of a company facing financial difficulties, however, there are circumstances where such liability may be imposed by reference to the actions (or inactions) of directors or managers. As a general rule, liability will require a causal link to be established between the actions (or inactions) of the directors or managers and the losses which are ultimately suffered by creditors.

It is important to note that the risk of liability attaches not only to those persons formally appointed as directors but also other persons without a formal appointment but who exert operational influence on the company. Accordingly, some of the issues described in this chapter may also apply to, and give rise to potential liabilities for, non-directors.

In practice, this means that directors need to carefully consider how their decisions may impact the rights and interests of creditors.

In the context of financial difficulties, directors' duties are primarily regulated by the Bankruptcy Law and the Companies Law.

Under the Companies Law, directors may be held liable to third parties for fraudulent acts and for violation of any provisions of the law. Importantly, the Companies Law requires any person who is authorised to manage a company to do so in a way which demonstrates due care and diligence in a manner expected of a prudent person. While the law lacks detail in these areas (and, as such, is open to interpretation), in our view, the relevant provisions should be viewed as a very broad tool under which interested parties (including creditors) may look to recover losses from a company's directors. It is feasible that interested parties that have suffered losses by reference to an ESG-related event could seek to pursue a claim against a director by reference to this general duty of care.

In practice, this means that the overarching duty of directors of a company that is in financial difficulties is to protect the interests of its creditors. While the scope of these duties is not entirely clear as a matter of UAE law, it is likely that if a company is in financial distress to the point that it may be unable to pay its debts as they fall due, then the directors may owe a primary duty to the interests of the company's creditors, even to the exclusion of the interests of its shareholders.

This requires the company's directors to carefully consider decisions through the lens of how those decisions might impact the company's creditors.

Under the Bankruptcy Law, a debtor is required to file for bankruptcy proceedings (being a RP process or a bankruptcy and liquidation) if it is cashflow or balance sheet insolvent (see the definitions of these states above). The Bankruptcy Law does not specify exactly when this filing must be made and it is possible to interpret this as affording debtors with a degree of latitude provided they are, at all times, acting with the best interests of creditors is mind. In practice, the strict filing requirement has not resulted in a significant number of filings being made.

The bankruptcy court may also impose civil sanctions on directors and managers in circumstances where a company becomes subject to bankruptcy proceedings, and it transpires that the value of its assets are insufficient to cover 20 per cent of its debts. In such circumstances, the bankruptcy court may, pursuant to article 144 of the Bankruptcy Law, order all or some of the company's directors or managers to contribute towards the remaining debts whenever it is proven that any of them had conducted certain types of behaviour in the lead-up to the bankruptcy proceedings.

The Bankruptcy Law states that these civil sanctions will not apply to a director or manager if it is evidenced that the director or manager did not participate in any of the actions set out above, the director or manager objected to the decision leading to the actions above (evidenced in the board minutes for example) or the court is convinced that the director or manager took all possible precautions to reduce losses to the company's creditors.

In addition to the above civil sanctions, the Bankruptcy Law also contains criminal sanctions that may be imposed on directors and managers of a company. Generally, such sanctions require an element of fraud, deceit or wilful misconduct.

## 2. Restructuring of ESG-related liabilities

As noted in section 1 above, the bankruptcy and restructuring laws in the UAE are nascent and are only now starting to be tested in a handful of live situations. As such, the applicable laws, their interpretation and market practice specifically relating to restructuring ESG-related liabilities are not developed. To assist the reader, we have, however, sought to provide high-level guidance as to how the existing laws *could* be interpreted in the context of a hypothetical case.

### 2.1 Environmental (E): restructuring environmental liabilities

#### *2.1.1 Types of environmental liabilities*

The primary legislation for environmental protection in the UAE is Federal Law No. 24 of 1999 on Environmental Protection and its executive regulations promulgated under Cabinet Decision No. 37 of 2001, as amended. There are a number of other federal laws that deal with specific aspects of environmental protection, such as laws dealing with conservation of aquatic resources (Federal Law No. 23 of 1999 and its executive regulations promulgated under Ministerial Decision No. 21 of 2018), animal welfare (Federal Law No. 16 of 2007) and integrated waste management (Federal Law No. 12 of 2018) and its executive regulations promulgated under Cabinet Decision No. 39 of 2021. In addition, a number of laws have also been enacted by the various emirates. Regulatory authorities have been established pursuant to these laws at the federal and emirate level to deal with enforcement. The key regulatory authority at the federal level is the Ministry of Climate Change and Environment.

These laws set out criminal and civil penalties for environmental offences. Civil sanctions for environmental offences include polluters being liable for costs associated with repairing any damage to the environment caused by their actions and for costs relating to compensating individuals for any harm suffered. Criminal sanctions include both fines and prison sentences.

#### *2.1.2 Priority given to environmental liabilities*

There are no provisions in the Bankruptcy Law laying down special laws for the restructuring of environmental liabilities. As a starting point, environmental liabilities should be capable of being restructured under a preventive composition or RP process in the same way as other liabilities of a debtor. One key consideration, however, will be the identity of the creditor which is owed the environmental liability. If this is a government authority (which could be the case in the case of environmental related fines), the liability would constitute a preferred liability and would not be capable of being restructured without the approval of the government authority. Environment-related liabilities are not, however, afforded preferential treatment as a matter of course.

#### *2.1.3 Disclaimer of environmental liabilities*

Contracts may be disclaimed within a bankruptcy process with the approval of the court. In order to approve this, the court would need to be satisfied that this is necessary to enable the debtor to continue its business, or that disclaiming the contract would fulfil the interests of all the creditors of the debtor company and would not materially affect the interests of the counterparty concerned. Counterparties to disclaimed contracts would be entitled to prove in the process as unsecured creditors.

In theory, the right to disclaim could be used in respect of an ESG-related liability provided the liability arose pursuant to a contract (as opposed to the liability arising as a matter of law or pursuant to a government imposed fine / order).

### 2.2 Social (S): restructuring health or safety-related liabilities

#### *2.2.1 Types of health and safety-related liabilities*

The primary legislation dealing with employment and labour relations and the health and safety of employees in the UAE is Federal Decree Law No. 33 of 2021, as amended (Labour Law), which is supplemented by executive regulations promulgated under Cabinet Decision No. 1 of 2022

(Labour Executive Regulations) and various Ministerial and Cabinet resolutions that have been issued from time to time, including Cabinet Resolution No. 33 of 2022 concerning work injuries and occupational diseases and Ministerial Decision No. 44 of 2022 concerning occupational health and safety and labour accommodation.

These laws set out criminal and civil penalties for non-compliance with prescribed health and labour safety standards. Civil sanctions include negligent employers being held liable for compensating employees for medical and other costs associated with suffering workplace injury, including for costs not covered by mandatory insurances. Criminal sanctions include both fines and prison sentences.

#### *2.2.2 Treatment of health and safety-related liabilities*

As in the case of restructuring of environmental liabilities, health, safety or labour rights-related liabilities can, in theory, be restructured in the same way as other ordinary liabilities of a debtor company. No special restrictions, provisions or conditions apply when restructuring health, safety, or labour-related liabilities in the UAE. Similar to environmental liabilities though, if such amounts were owed to government authorities, they could not be restructured without the consent of such government authority.

Under the Bankruptcy Law, amounts owing to employees are afforded preferential status but this is capped at the equivalent of three months' salary. Any incremental amounts would be regarded as unsecured claims. As such, while the preferential portion could not be compromised without the approval of the relevant employee, in theory it should be possible to compromise incremental amounts owing to employees (which may include health and safety liabilities which the company owes direct to the employee). In practice, however, we expect that any such attempts would be closely scrutinised by the courts (particularly where the company is perceived to have been negligent in causing such damage).

### 2.3 Governance (G): third party releases in favour of directors and officers of the company

The Bankruptcy Law is not prescriptive as to the form which a preventative composition or RP must take.

There are also no restrictions on directors or other third parties benefiting from releases as part of the related plan. That said, as the Bankruptcy Law remains largely untested, it remains to be seen if the courts may scrutinise any such releases (noting the heavy court involvement in reviewing, approving and ultimately sanctioning the plan).

In addition, a sufficient number of creditors would need to be comfortable with such releases forming part of the terms of the plan in order to pass the requisite approval thresholds.

While again untested, we do not consider that the terms of a preventative composition or a RP could release directors or other third parties from criminal liability for prior actions.

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

#### *3.1.1 Approving a restructuring plan*

There is no requirement for a preventative composition or a RP to be approved by environmental protection authorities. Environmental advocacy groups (and similar) do not exist in the UAE in the way that is seen in certain other jurisdictions. As outlined above in section 1, a preventative composition or a RP need only be approved by the court and the requisite majority of creditors.

#### *3.1.2 Discretion to consider wider public interest concerns*

There is no onshore case concerning the extent to which the court may consider environmental issues in deciding whether to approve a restructuring under the Bankruptcy Law. As outlined in section 1, when deciding on the approval of a preventative composition scheme or a RP, the court takes into consideration the rights and interests of the creditors. There is no requirement, however, for the court to take into account wider public interest considerations.

#### *3.1.3 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

There are no statutory provisions which expressly grant environmental protection authorities standing to present their views or concerns in a restructuring. It is possible, however, that if the situation were material enough, the applicable government authority may seek to notify the court of its views.

### 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

#### *3.2.1 Approving a restructuring plan*

There are no statutory provisions which expressly grant government authorities standing to present their employee related concerns in restructuring. Nor is the approval of these authorities required in the context of a preventative composition or a RP. It is possible, however, that if the situation were material enough, the applicable government authority may seek to notify the court of its views.

#### *3.2.2 Discretion to consider wider public interest concerns*

In the context of a court-controlled restructuring, the court has the power to approve the formation of creditor committees to represent the interests of different categories of creditors. In a situation where the rights of employees are to be compromised (or otherwise affected) pursuant to the plan, it is possible that the court may sanction an employee-focused committee to ensure that the interests of employees are taken into account in formulating the plan.

#### *3.2.3 Protection of employee rights*

While legislation exists to protect workers' rights, workers unions (or equivalent) do not exist in the same way that are seen in certain other jurisdictions. Note that recently, following the entry into force of the Labour Law, the Ministry of Human Resources and Emiratisation issued certain ministerial resolutions aiming to establish a framework applicable to collective worker disputes, including Ministerial Resolution No. 47 of 2022 on the regulation of the procedures of labour disputes and complaints, as amended. It is feasible that this framework could be utilised in the context of an onshore UAE bankruptcy process.

### 3.3 Governance (G): board / management conflicts addressed in a restructuring

In addition to the general duty of care which directors owe to creditors in a financially distressed situation (as outlined above), directors are subject to duties to avoid conflicts of interests.

While not expressly catered for in the law, we expect that the court would scrutinise a proposed preventative composition or RP which afforded overly beneficial treatment to continuing directors or management (e.g. the issuance of significant equity stakes) at the expense of creditors (noting that the court is required to ensure that the plan is in the interests of creditors).

In addition, in the context of a RP, it is the trustees that are in control of the debtor company and which will develop the RP. As such, the trustees (who owe fiduciary duties to creditors) would also need to be satisfied with the terms of the plan before this is presented to creditors. A sufficient number of creditors would also need to be satisfied with the proposed arrangement in order for the plan to approved and sanctioned by the court.

## 4. "Soft law" framework

Noting the nascent nature of formal restructuring and insolvency generally in the UAE, we are not aware of any industry guidelines and / or best practices that are prescribed in relation to ESG matters within a restructuring.

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds and investments

In recent years, there have been many examples of green and sustainability-linked financings being raised in the UAE. Major banks in the region have also started developing their own green financing framework to finance environmental and social projects. We have also seen examples of banks securing their own funding from green sources.

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

For now though, adoption and promotion of ESG financings tends to be ad hoc and driven by individual banks and large corporates (as opposed to being commonplace in the market).

Where financings *are* completed with an ESG focus, the relevant documentation tends to borrow market-standard concepts from other international markets. International banks operating in the UAE are also promoting their own requirements based on financings which have been "banked" in other jurisdictions.

### 5.3 Promoting ESG by the central bank and regulators

There is currently limited regulation requiring companies to opt for sustainable practices or their regular disclosure, and compliance with specific ESG standards in the UAE largely remains voluntary (with the exception of certain pre-existing laws relating to the environment, health and safety and workers' rights and governance, some of which are outlined above).

Cabinet Decision No. 2 of 2018 on Corporate Social Responsibility, and, more recently, Cabinet Decision No. 79 of 2022 concerning incentives for commercial companies to begin their social responsibilities introduced a framework applicable to companies subject to the Companies Law, albeit compliance with the framework remains voluntary for now. The 2022 Cabinet Decision expressly makes reference to the role of companies in contributing to economic, social and environmental development.

There are, however, examples of regulatory bodies attributing increasing importance to ESG factors in financial reporting. For instance, in 2020, the UAE Securities and Commodities Authority (SCA) issued the Securities and Commodities Authority Decision No. 3/RM of 2022 concerning Approval of Joint Stock Companies Governance Guide (SCA Governance Guide), pursuant to which public joint stock companies listed on the Dubai Financial Market (DFM) and Abu Dhabi Securities Exchange (ADX) are now required to publish sustainability reports. Both the DFM and the ADX have published guidance on ESG disclosures and sustainable reporting, and require listed companies, in accordance with the SCA's regulations, to produce thorough reports every year detailing their environmental impact, people and culture, adopted labour standards and employee management practices, and data protection policies, among other things.

Pursuant to the SCA Governance Guide, directors of Public Joint Stock Companies are required to ensure compliance with various ESG related factors including:

- maintaining a policy regarding the local community and environment;
- ensuring minimum levels of female representation on the board of directors; and
- the preparation of a report addressing social and sustainable activities of the company.

There are currently no mandatory reporting obligations for private companies, although there have been suggestions that this may also be introduced.

Like other countries, ESG is clearly of strategic importance for the UAE. The UAE became the first GCC nation to commit to the net zero carbon emissions by 2050 target and will host the UN Climate Change Summit, COP 28, in late 2023.

The UAE also recently established the UAE Sustainable Finance Working Group, the aim of which is to facilitate regulatory cooperation in developing sustainable finance in the region. It comprises representatives from the ministries (Ministry of Finance, Ministry of Economy, Ministry of Climate Change and Environment, the Office of the UAE's Special Envoy for Climate Change), financial regulators (the UAE Central Bank, the SCA, the Financial Services Regulatory Authority (i.e. the financial services regulator of the ADGM) the Dubai Financial Services Authority (i.e. the financial services regulator of the DIFC), and UAE stock exchanges (the ADX, the DFM, and Nasdaq Dubai). In its second public statement entitled "2022 Public Statement on Collaboration on Sustainable Finance in the UAE", the Working Group reaffirmed the UAE Government's commitment towards facilitating the adoption of sustainable finance at a national level.

In light of the above, we expect ESG related considerations to continue to inform policy decisions of the UAE Government and with it, regulation which will influence the conduct of business in the UAE.

# UNITED KINGDOM

# 1. General overview of the restructuring regime

## 1.1 Formal restructuring procedures

### *1.1.1 Schemes of arrangement (Schemes) and restructuring plans (RPs)*

Schemes and RPs are restructuring procedures set out in the UK Companies Act 2006. They are tools for UK-incorporated companies, and certain foreign companies with a "sufficient connection" to the United Kingdom, to propose a compromise or arrangement with their creditors or members (or any class of them).

Both Schemes and RPs are court-supervised procedures but, provided the relevant company is not also in an insolvency procedure such as administration or liquidation, the management of the company remains in the control of its directors.

Schemes and RPs can be used for both solvent and insolvent companies and, provided the necessary statutory voting majorities are met (see below) and the Scheme or RP is sanctioned by the court, the Scheme or RP is binding on all of the stakeholders subject to it – whether or not they voted in favour (or voted at all) in relation to the Scheme or RP.

A RP is available to a company which has encountered, or is likely to encounter, financial difficulties that are affecting, or will or may affect, the ability of the company to carry on business as a going concern. The purpose of the RP must be to eliminate, reduce or prevent, or mitigate the effect of, any of those financial difficulties. Insolvency is not a prerequisite for a RP, but given the requirement for financial difficulties, companies that propose a RP are often insolvent on either a balance sheet basis or a cash flow basis.

Schemes have been part of the English restructuring toolkit for decades, whereas RPs are a relatively new restructuring procedure introduced as part of the Corporate Insolvency and Governance Act 2020 (CIGA), which was given Royal Assent in June 2020. Schemes were routinely used to restructure companies in England but a perceived shortcoming of Schemes was an inability to implement a "cross-class" cram down. This could sometimes be addressed by combining a Scheme with a formal insolvency procedure such as a pre-packaged administration sale (see below).

While a Scheme can be used to compromise stakeholders within a particular class, if a class of stakeholders fails to approve the Scheme, that class may in effect have a veto on the implementation of the restructuring. A RP on the other hand can be imposed on an entire class of creditors provided certain safeguard protections are met, including:

- the court must be satisfied that, if the RP was to be sanctioned, none of the members of the dissenting class would be any worse off than they would in the "relevant alternative". The "relevant alternative" is whatever the court considers would be most likely to occur in relation to the company if the RP was not sanctioned; and
- the RP has been agreed to by at least 75% in value of a class of creditors or members who would receive a payment, or have a genuine economic interest in the company, in the event of the relevant alternative.

Even if the voting thresholds have been satisfied, the court ultimately has the discretion as to whether to sanction the Scheme or RP. Among other matters, the court will look closely at whether procedural formalities were satisfied (for example, the convening of stakeholder meetings and the conduct of those meetings) as well as jurisdictional issues, foreign recognition and the overall fairness of the Scheme or RP.

If a particular class of stakeholder has no genuine economic interest in the company (for example, if it can be demonstrated to be completely "out-of-the-money") then it is possible for that class to be completely excluded from the RP voting process but still be bound by it. This is not possible in a Scheme unless it is used in conjunction with a formal insolvency process like administration (see below).

All types of creditors and members can be subject to a RP or a Scheme. Both procedures can apply to any shareholder or secured and unsecured creditor class, including financial creditors, operational / trade creditors and preferential creditors. Both procedures can be used in isolation or in tandem with other restructuring tools, such as an administration or a Part A1 moratorium. The latter was also introduced by the CIGA.

In both Schemes and RPs, valuations of a company's business and assets are critical in order to demonstrate the level of return to stakeholders through the Scheme or RP compared to other outcomes and to demonstrate that the stakeholders being compromised are not financially worse off than in the "relevant alternative". This is particularly important in the context of a cross-class cram down of a dissenting class of stakeholder in a RP and demonstrating that they are no worse off under the RP than in the "relevant alternative".

Stakeholders opposing a Scheme or a RP often bring challenges disputing the valuations obtained by the company and presented in evidence at the court hearings in relation to the Scheme or RP.

In both Schemes and RPs, the restructuring proposals can be made by the company via its directors or, if the company is in an insolvency procedure such as administration (see below), by the relevant insolvency officeholder. If the Scheme or RP is proposed by the relevant company itself outside of an insolvency procedure, the management and control of the company's business during the restructuring remains with the directors of the company. The supervision by the English court in relation to both a Scheme and a RP is solely in relation to the legal mechanics and implementation of the procedure and does not extend to the management of the company's business.

The procedure for both a Scheme and a RP are broadly similar, with each including the following steps:

- the first step is to send a "Practice Statement Letter" setting out certain information in relation to the restructuring proposal, including high level commercial terms and details of the first court hearing, during which the company will apply for an order to convene shareholder and creditor class meetings (the "Convening Hearing" – see below);
- at the Convening Hearing, the court may order that the company convenes stakeholder meetings;
- the notice of stakeholder meetings and explanatory statement are then issued to stakeholders;
- the stakeholders then vote on the terms of the Scheme or RP;
- if the class meetings are successful and the terms of the Scheme or RP are approved by the required majorities (detailed further below), the company will apply to the court for a sanction hearing, during which the court has a discretion as to whether or not to sanction the scheme (the "Sanction Hearing" – see below); and
- if sanctioned by the court, the Scheme or RP binding on all affected creditors and members once notice has been delivered to the Registrar of Companies.

The timeline from the Convening Hearing to the Sanction Hearing is likely to be six to eight weeks to ensure adequate notice is given to stakeholders of the meetings.

Prior to proposing a Scheme or a RP, the company typically engages in extensive negotiations with its creditors and other stakeholders to seek to ensure, as far as possible, the implementation of the restructuring when it is formally launched. In many cases, the company will agree "lock-up" arrangements with its creditors and stakeholders, or certain classes of them.

As noted above, in the event that stakeholders are being crammed down (whether intra-class in the case of a Scheme or intra-class or cross-class in the case of a RP), detailed valuation evidence will usually need to be obtained by the company to justify the treatment of the stakeholders in the restructuring. The company may also consider that it needs to undertake a distressed M&A marketing exercise to properly demonstrate value, the results of which would be submitted in evidence to the court.

The voting threshold for a Scheme is a majority in number and at least 75% in value of the creditors or members (or each class of them) present and voting at the relevant meeting. If one class meeting does not approve the Scheme, the Scheme cannot be implemented.

The voting threshold for a RP is at least 75% in value of the creditors or members (or each class of them) present and voting at the relevant meeting (i.e. unlike in a Scheme, there is no numerosity test). Also, in the event that a class of stakeholders does not approve the RP, the court can still potentially sanction the scheme if it is satisfied the class is no worse off than in the relevant alternative (see above) and if the RP has been approved by at least one class of stakeholders who have a genuine economic interest in the company. As noted above, it is also possible to exclude a class of stakeholders entirely from voting on an RP but still be bound by it if the court is satisfied that that class does not have a genuine economic interest in the company.

For both Schemes and RPs, there are two court hearings to be held, being the Convening Hearing and the Sanction Hearing. In the event the Scheme or RP is challenged, there may be additional court hearings dealing with the challenge.

At the Convening Hearing, the court will consider, among other matters, the proper composition of the classes of creditors and members who will be asked to vote in separate class meetings (see above). The court will also be asked to approve the distribution of an explanatory statement prepared by the company, containing detailed information on the restructuring terms. At the Convening Hearing, the court can also consider whether it has jurisdiction to sanction the Scheme or RP, but the final determination as to jurisdiction is reserved for the Sanction Hearing.

At the Sanction Hearing, the court has a discretion as to whether it will sanction the Scheme or RP, notwithstanding that it may have been approved by the relevant classes voting. The court will consider a number of factors, including (but not limited to): (i) jurisdictional issues; (ii) whether the class meetings were properly represented; (iii) whether a member or creditor of the company could reasonably have approved the Scheme or RP; (iv) whether the Scheme or RP (as applicable) provides a fair distribution of the benefits generated by the restructuring; and (v) whether the procedural requirements of the Companies Act were complied with.

Schemes and RPs are typically used for the restructuring of the interests of financial creditors and the company's members, although Schemes have also been used to compromise other types of claims, such as retail customers of insurance companies and mis-selling claims against financial institutions.

In relation to RPs, the Companies Act 2006 does provide for regulations to be made in the future excluding companies which provide financial services from proposing a RP, although as of June 2023 no such regulations have been made.

### *1.1.2 Administration*

Administration is a procedure designed to give a company "breathing space" and to enable it to be rescued or restructured, or for its business and assets to be sold under the protection of a statutory moratorium.

Administration places a company under the control of an insolvency practitioner, who must achieve one of the statutory objectives, which are, in order of priority:

- to rescue the company as a going concern;
- to achieve a better result for the company's creditors as a whole than would be likely if the company were wound up; and

- realising property in order to make a distribution to one or more secured or preferential creditors.

In practice, the rescue of the company as a going concern is unlikely. In most cases, the administrator will pursue a going concern sale of the business and assets in order to preserve enterprise value and in pursuance of the objective to achieve a better result for the company's creditors as a whole than would be likely if the company were wound up.

An administrator can be appointed by:

- a court order following the filing of an application by stakeholders including:
    - one or more creditors of the company;
    - the company itself;
    - its directors; or
    - a supervisor of a company voluntary arrangement; or
- an "out of court" appointment, being the filing of certain appointment documents at court by:
    - the company;
    - its directors; or
    - a holder of a qualifying floating charge over the company's assets (QFC / QFCH).

In an out of court appointment process, if there is another person or entity entitled to appoint an administrator (for example, the holder of a prior ranking QFC over all or substantially all of the floating charge assets of the business), a notice of intention to appoint (NoIA) must first be served on them prior to a notice of appointment being filed at court. Where a NoIA is given by the company or its directors, such a NoIA may only be given and filed at court if they have a settled intention to appoint an administrator. The NoIA provides those entitled to appoint an administrator with an opportunity to pursue their own appointment, should they wish to do so. However, they may instead choose to consent to the current out of court process. If no action is taken by the QFCH, the appointor may proceed to file a notice of appointment upon the expiry of five business days after service of the NoIA. The NoIA expires after a period of 10 business days – at that point, if the NoA has not been filed, the process of filing the NoIA must begin again or it will lapse.

Although a company or its directors can appoint an administrator using the out of court process, there are certain circumstances where they can only appoint an administrator by court order, including when the company is subject to an outstanding winding up petition. However, an outstanding winding up petition does not prevent a QFCH appointing an administrator using the out of court route.

Upon appointment, an administrator is an officer of the court and acts as agent of the company. He or she has wide-reaching powers to help achieve the purpose of the administration. This includes doing anything "necessary or expedient for the management of the affairs, business and property of the company".

When a company enters administration, it also benefits from a statutory moratorium that prevents creditors from enforcing their rights against the company without the prior consent of the administrator or the court. Where a NoIA has been filed or an administration application has been made to the court, the company will benefit from an interim moratorium pending the determination of the administration appointment. The scope of the interim moratorium is the same as the statutory moratorium in administration. However, if a creditor wishes to enforce its rights subject to the moratorium, it can only apply to the court for permission as no administrator has yet been appointed.

In many cases, an administrator will look to secure the sale of the company's business and assets as a going concern as one of the main ways to achieve the purpose of the administration. This may be after a period of "trading" the company in administration or by way of a "pre-packaged" sale.

A pre-packaged administration sale is a sale where the company enters administration and its business and / or assets are immediately sold by the administrator on terms that have been negotiated and agreed with the proposed purchaser and other stakeholders in advance of the company entering administration.

As noted above, a pre-packaged administration sale may also form part of a wider restructuring and be combined with a scheme of arrangement to cram down the claims of a dissenting class of stakeholders.

It should be noted that there are a number of exit routes from administration, some of which, including company voluntary arrangement, a RP or a Scheme, could result in handing back control of the business to the directors. Other exit options include creditors' voluntary liquidation and dissolution of the company.

Upon the appointment of administrators to the company, the administrators take over control of the company's business and assets from the existing management and all of the directors' executive powers cease. The administrators will act as agents of the company.

The directors and existing management are still obliged to provide the administrators with whatever assistance the administrators require to fulfil their responsibilities. However, the directors and existing management will retain control of the company during the "interim moratorium" period triggered by the filing of an NoIA pending the determination of the administration appointment.

Following the appointment, the administrator must prepare a statement of how he or she proposes to conduct the administration, and distribute that statement to the company's members, creditors and the Registrar of Companies. This statement is known as the administrator's proposals. The administrator's proposals will include, among other things: (i) the current financial position of the company; (ii) what statutory purpose of administration the administrator intends to achieve; (iii) information regarding any asset disposals since the date of administration and the reasons for such disposals; (iv) expected distributions to creditors; and (v) the administrator's remuneration and pre-administration costs. Where an administrator has completed a sale of the business by pre-packaged administration, the administrator is also required to send information regarding the sale to creditors in accordance with the Statement of Insolvency Practice (SIP) 16. If there was no sale of the business by pre-packaged administration, the administrator will need to decide whether he or she should trade the company in administration in order to preserve value of the business and assets and to achieve the intended purpose of the administration.

The administrator must then seek approval of his or her proposals from the company's creditors using either a creditors' decision procedure or by deemed consent. In practice, administrators will typically seek approval of their proposals by deemed consent. However, if the company's creditors do not approve the proposals (with or without modifications), the administrator must then apply to court for approval. An administrator must return to the creditors for approval at various other stages of the administration, including the extension of the administration period or in relation to any increase to the administrators' remuneration.

There are no creditor approvals required. Typically, the company, a creditor, the directors or a QFCH can appoint administrators. However, the interim moratorium period may be disposed of if a QFCH who is on notice of the associated appointment of administrators consents to that appointment.

If the company is authorised or carried on a regulated activity under the Financial Services and Markets Act 2000, the written consent of the Financial Conduct Authority or Prudential Regulation Authority (whichever applies to the company) is required prior to filing an NoIA or notice of appointment (as applicable).

There are also a number of special administration regimes which are available to entities that operate in certain industries and modify the typical administration procedure. For example, companies that carry out a statutory function of a public nature such as water or energy companies or operate in sectors where there is a significant public interest such as financial services institutions will be subject to a special administration regime. The purpose of these modified administration regimes is to ensure that an administrator has the appropriate objectives and powers to achieve those objectives.

There are no restrictions on which debts can be included in an administration.

#### *1.1.3 Part A1 moratorium (Moratorium)*

The CIGA introduced a standalone moratorium procedure designed to allow financially distressed companies time to restructure or seek fresh investment free from enforcement action by certain types of creditors.

The Moratorium will last for an initial 20 business day period but can potentially be extended for longer periods with the relevant consents. During the Moratorium, the company enjoys a payment holiday from most of its non-financial services-related pre-Moratorium debts and is broadly protected from legal or enforcement action by unsecured and preferential creditors, including forfeiture proceedings by its landlords, without the court's permission. However, any "Moratorium debt", being a debt that falls due during or after the commencement of the Moratorium by reason of an obligation incurred during the Moratorium, remains payable during the Moratorium.

The Moratorium is a "debtor in possession" process that allows a company's directors and management to remain in control. However, creditor safeguards are provided in the form of the appointment of a "monitor", who is a licensed insolvency practitioner responsible for supervising the process. The monitor will monitor the company's affairs during the Moratorium period but will not have any direct power to control the conduct of the company during the Moratorium period. Where there is any uncertainty as to how the monitor should act, he or she can apply to the court for directions.

Companies (including overseas companies with a sufficient connection to the United Kingdom) and LLPs are eligible to apply for a Moratorium. However, there are some important financial services entities excluded from using the Moratorium, including insurers, banks, investment banks, investment firms, parties to capital markets arrangements and other financial services-related entities.

The Moratorium is similar to the moratorium that arises upon the appointment of an administrator, whereby, broadly: (i) no insolvency proceedings may be commenced; and (ii) no steps may be taken in relation to forfeiture, enforcement of security (other than in relation to financial collateral) or to commence or continue legal proceedings without court permission (other than certain employment-related claims).

Creditors with pre-Moratorium debts subject to a payment holiday are prevented from applying to the court for permission to take enforcement action. In addition, the Moratorium will not crystallise a floating charge and any chargee is prevented from causing the floating charge to crystallise. This correlates with the purpose of the Moratorium primarily as a rescue tool, and so has the effect of preserving a company's ability to dispose of its floating charge assets in the ordinary course of business during the Moratorium (or if the monitor consents and such disposal will support the rescue of the company as a going concern). However, the company will not be entitled to dispose of other charged property (including hire purchase property) unless the court sanctions the disposal, and any net proceeds of the disposal must be used to discharge the secured debt.

While the company is entitled to a payment holiday in respect of its pre-Moratorium debts, this excludes any debts falling due in relation to the following:

- the monitor's fees and expenses for the Moratorium period;
- any goods and services supplied during the Moratorium;

- rent payments for the Moratorium period;
- wages and salaries;
- redundancy payments; and
- debts or other liabilities arising under a contract or other instrument involving financial services.

The inclusion of the final category above is significant because it means that the company must continue to pay its banks and other lenders throughout the Moratorium, while trade creditors and landlords remain unpaid in respect of any arrears. While this may make sense in a small and medium sized enterprise (SME) context, where it is usually necessary to keep paying the lenders whose support is vital to any anticipated rescue plan, it is less obviously helpful in a large company scenario where, typically, the first step in most restructurings is to put in place a standstill among the financial creditors.

There are two qualifying conditions for a Moratorium, namely: (i) a directors' statement needs to be made that the company is or is likely to become unable to pay its debts as they fall due; and (ii) the monitor must confirm that it is likely the Moratorium would result in the rescue of the company as a going concern.

The initial period of the Moratorium is 20 business days, and may be extended without creditor consent once for a further 20 business days. Where creditor consent has been obtained, a Moratorium may be extended for a period of up to a year in total. For each extension, the two qualifying conditions mentioned above still need to be met. A Moratorium which is already in place can also be extended where a creditors' voluntary arrangement (CVA) has been proposed or similarly at the convening hearing for a Scheme or RP to provide protection until the Scheme or RP is approved and sanctioned.

The monitor must bring the Moratorium to an end if he or she thinks that, among other things:

- the Moratorium is no longer likely to result in the rescue of the company as a going concern;
- the objective of the Moratorium has been achieved;
- he or she cannot carry out the relevant statutory functions because the directors have not provided the necessary information.

Where administration or liquidation occurs within 12 weeks of the end of a Moratorium, any unpaid Moratorium or pre-Moratorium debts not subject to a payment holiday are paid in priority to all other claims, except those subject to a fixed charge.

There are no creditor approvals required to implement a Moratorium. However, to the extent creditor consent is required and / or sought to extend a Moratorium, an amended form of qualifying decision procedure is required, whereby: (i) a majority (in value) of those voting is required to vote in favour of the proposed decision; and (ii) a majority (in number) of pre-moratorium unconnected creditors vote in favour of the proposed decision.

Where a Moratorium is commenced out of court, there is no express court approval required, and the Moratorium will commence at the time the relevant documents are filed at court. However, where an application is made to court to commence a Moratorium, the Moratorium will commence at the time the court order is granted. There are two qualifying conditions, namely: (i) a directors' statement needs to be made that the company is or is likely to become unable to pay its debts as they fall due; and (ii) the monitor must confirm that it is likely that the Moratorium would result in a rescue of the company as a going concern.

## 1.2 Informal restructuring procedures

### *1.2.1 Creditors' voluntary liquidation (CVL)*

A CVL is a voluntarily procedure whereby an insolvent company takes steps to enter liquidation, usually as an alternative to the company being wound up by the court based on a winding up petition served by a creditor.

A CVL may be appropriate if the company has exhausted all alternative forms of informal or formal restructuring without success and is unlikely to be rescued. The business of the company will cease upon the appointment of a liquidator except as may be required for its beneficial winding up. In addition, all contracts of employment are typically terminated, except where a liquidator wishes to retain any employee during a period of post-appointment trading.

The CVL process is instigated by the company's board of directors. The directors are required to resolve to convene a meeting of the company's members, who will then vote to pass a special resolution for the company's winding up and appoint a liquidator. The liquidation is deemed to commence from the passing of the resolution.

Upon appointment, a liquidator is required to collect and realise the company's assets before distributing the proceeds to the company's creditors. In the event of a surplus being available, a distribution is then made to the company's members.

Similar to an administration, a liquidator has wide-reaching powers to fulfil his or functions and duties, including the power to do all such "things as may be necessary for winding up the company's affairs and distributing its assets".

However, unlike in an administration, there is no automatic moratorium on existing proceedings continuing or new proceedings being commenced when a company enters CVL. However, the court may exercise its discretion and order that any particular proceedings are stayed – typically following an application from the liquidator or a stakeholder.

The company's directors and management remain in control of the company until the resolution of the company's members is passed to appoint a liquidator, at which point all their powers cease. However, the directors and management will have a continuing responsibility to assist the liquidator with their enquiries.

As noted above, a CVL process is instigated by the company's board of directors. The directors are required to resolve to convene a general meeting of the company's members. A notice of general meeting is then sent to the company's members. The general meeting is held in accordance with the company's constitution. Typically, at least 14 days' notice must be given to members, but if more than 90% of members consent to short notice, the meeting may be held sooner.

The members are then required to vote to pass a special resolution for the company's winding up and nominate an insolvency practitioner to act as liquidator. The liquidation is deemed to commence from the passing of the resolution.

Where there are perishable assets, assets at risk or it is in the public interest, there is also the ability to appoint a provisional liquidator with limited powers to protect and preserve value in those assets.

However, in the intervening period between the directors' resolution to convene a general meeting and the general meeting taking place, notice is required to be given to any QFCH. Upon giving notice to the QFCH, the special resolution may be passed following the expiry of five business days (beginning on the day the notice was issued) or earlier if the QFCH has consented in writing to the passing of the resolution.

Upon the members passing the resolution for a voluntary winding up, the directors must produce a statement of affairs which outlines the assets available for realisation and available for distribution and provide a notice to the creditors of the company seeking their decision on the nomination of a liquidator. The statement of affairs may accompany the notice or follow separately but, in any event, it must be sent to creditors within seven days of the passing of the resolution to wind up the company and be received no later than the business day before the "decision date". The decision date must be no earlier than three business days after the notice is delivered and no later than 14 days after the resolution to wind up the company was passed.

This decision on the nomination of a liquidator may be made by the deemed consent procedure or by a virtual meeting. If a deemed consent route is used, then creditors do not need to provide any form of acknowledgement that the person nominated by the company's members takes office as liquidator.

The CVL process and liquidator appointment is effectively approved by the company's members and ratified by the creditors save for any formal meeting request (see above).

On the basis that a CVL is typically a terminal process, there are no restrictions on the types of debts, liabilities or claims that can be captured under the CVL process.

### *1.2.2 Company voluntary arrangement (CVA)*

A CVA is a formal procedure that aims to help a company address its financial difficulties by entering into a binding arrangement with its creditors.

A CVA is an arrangement between the company proposing the CVA and its non-preferential unsecured creditors to repay them over a period of time (typically three to five years). While relatively uncommon, secured and preferential creditors can also be compromised during a CVA, but they must provide their express consent.

The company can continue to trade during the CVA and the directors are subject to their usual duties throughout this period, but the company must meet its ongoing trading liabilities as they fall due. This is an obligation on the directors and not the insolvency practitioner acting as supervisor (the CVA Supervisor), who is only responsible for overseeing the implementation of the CVA.

The procedure is available to any company registered in England or Wales. It enables the company to reduce its debt levels and improve its cashflows by coming to an arrangement with its creditors.

Usually, the company will make an agreed, affordable monthly payment to the CVA Supervisor from future profits and / or asset sales. The CVA can also involve a one-off introduction of funding from an external source, such as a shareholder or lender. The CVA Supervisor will distribute the money on a *pari passu* basis among the creditors bound by the arrangement.

The amount paid over the agreed term can vary, from repayment in full to a percentage of the debt. Upon successful completion of the CVA, any shortfall in the amounts owed to those creditors bound by the arrangement will be written off.

With the flexibility of CVAs, they are commonly used to modify or terminate existing contractual obligations. This is often seen with rental obligations, particularly in the retail sector, including a reduction in future rent payments or even closure of certain unprofitable premises. However, a CVA cannot vary or remove a landlord's right to forfeit a lease or other proprietary remedies.

With any CVA proposal, if: (i) approved by 75% in value of unsecured creditors who respond to the decision procedure; and (ii) it is not opposed by more than 50% of unconnected creditors, the CVA will be binding upon the entire body of "non-preferential unsecured" creditors. The CVA does not, however, bind secured or preferential creditors, who retain the same rights as before the CVA was approved. Secured creditors can, if appropriate, seek to enforce their security, albeit typically conversations will have been held with the secured creditor before the proposal is issued.

The process from commencement to approval of the CVA can take between six to eight weeks to complete, during which the company has no protection from its creditors. There is no automatic statutory moratorium in a CVA but an application for a Moratorium can be made, if necessary, under the CIGA (although this is rarely utilised in practice).

The existing management team retains control of the company throughout the CVA and is responsible for ensuring that the company adheres to the terms of the CVA. However, a proposal for a CVA should nominate an insolvency practitioner to supervise its implementation and report to creditors.

To implement a CVA, the directors (often with legal and / or professional assistance) are required to put forward a proposal to the proposed CVA Supervisor (in their capacity as Nominee).

The Nominee, who must be an insolvency practitioner, then has an obligation to conduct an independent review of the proposal and report to the court on: (i) the suitability and viability of the proposal, giving consideration to whether any solvent options are available; (ii) whether a CVA provides a better outcome to the company's creditors than other insolvency options; and (iii) whether it is fair and reasonable.

Ultimately, the Nominee must give an opinion as to whether he or she believes the CVA has a reasonable prospect of being approved and being implemented.

If the Nominee considers that the proposal has a reasonable prospect of approval and implementation, he or she provides a copy of the proposal to the creditors and members of the company and seeks their approval of the CVA.

A CVA proposal can also be put forward by an administrator as an exit route from administration, or by a liquidator (though unlikely in practice), and in these scenarios the officeholder (if acting as Nominee) would seek a decision of the creditors and members without the need to seek an independent review of a Nominee and report to the court.

A decision of the creditors must be conducted via an appropriate decision procedure, being either a virtual meeting or decision by correspondence and the Nominee would generally conduct and / or chair this decision process.

The decision date for the decision procedure of creditors must be no later than 28 days after the filing of the Nominee's report at court. A decision of the company's creditors must be made prior to a decision of the members but can be (and often is) on the same day.

Modifications can be put forward by creditors when considering the proposal. These proposed modifications are then voted upon by creditors. It is not a statutory requirement for directors to consent to the modifications, but under SIP 3.2, the Nominee should report his or her view of any proposed modifications, which the directors may be required to implement if approved.

Upon approval by creditors, the Nominee becomes the CVA Supervisor and the terms of the CVA become legally binding.

A simple majority of shareholders need to agree the proposal at the shareholders' meeting for the CVA to go ahead.

As noted, there must be a vote of creditors of at least 75% in favour of the CVA (by value of debt), and this includes any votes by proxy or post. A second vote is then taken without "connected" creditor participation, and as long as 50% or more vote for acceptance of the CVA, it will be passed.

Secured creditors cannot vote on a CVA, save to the extent their debt is unsecured or where a secured creditor values their security and participates with the residual unsecured balance. This effectively means that debt owed to secured creditors cannot be compromised by a CVA and must be dealt with by direct negotiation between the company and the secured creditor or remain whole. Likewise with preferential creditors, their debt must not be compromised and must be paid in accordance with the ordinary waterfall, unless their expressly consent to an alternative (which would be unusual). All other company debts can be compromised under a CVA.

Once approved, the CVA binds all the non-preferential unsecured creditors of a company who were entitled to vote on the CVA proposal. This means that a CVA binds:

- creditors who voted against the CVA;
- creditors who received notice of the CVA proposal but who did not vote; and
- creditors who would have been entitled to vote but did not receive notice of the CVA proposal, despite being entitled to be notified of it.

## 2. Restructuring of ESG-related liabilities

There is no single, overarching piece of ESG legislation or regulation in the United Kingdom. The ESG regime comprises an array of domestic and EU-derived laws and regulations, including:

- the UK Corporate Governance Code 2018;
- the directors' duties set out in the Companies Act 2006;
- the Listing Rules, the Disclosure Guidance and the Transparency Rules;
- the UK Stewardship Code 2020;
- the Large and Medium-Sized Companies and Groups (Accounts and Reports) Regulations 2008;
- the Climate Change Act 2008;
- the Bribery Act 2010;
- the Corporate Manslaughter and Corporate Homicide Act 2007;
- the Equality Act 2010; and
- the Modern Slavery Act 2015.

It can therefore be difficult for United Kingdom companies to understand precisely how to interpret the term "ESG".

The term was originally coined in a 2004 report titled "Who Cares Wins" by then UN Secretary General Kofi Annan. This report was the product of a UN initiative to integrate sustainability into capital markets. Under the mandate of the UN Global Compact (UNGC) and with support from the International Finance Corporation (IFC), Mr Annan brought together the CEOs of several important financial institutions to essentially deliberate and conceptualise a common baseline for ESG investing. The report argued that embedding ESG factors into capital markets was not only sensible business but would also enable better outcomes for society and create more sustainable markets.

Concurrently with the production of the Who Cares Wins report, the UN Environment Programme's Finance Initiative (UNEP FI) published the Freshfields report. The Freshfields report made the case that because ESG issues are relevant to financial valuation, they fall within core fiduciary duties. These two reports formed the backbone for the launch of the Principles for Responsible Investment (PRI) at the New York Stock Exchange in 2006 and the launch of the Sustainable Stock Exchange Initiative (SSEI) the following year (2007).

More recently, the Task Force on Climate-Related Financial Disclosure (TCFD) was established in 2015 by G20 Finance Ministers and Central Bank Governors within the Financial Stability Board (FSB) and its chair at the time, Mark Carney, then Governor of the Bank of England. The FSB is an international body that monitors and makes recommendations about the global financial system. The TCFD is a framework to operationalise the Paris Agreement's 1.5°C target for the business world. It is expected to propel development in disclosures by enabling transparency about realistic scenario planning, particularly on the physical impacts of climate change, including for investors.

Specifically in the United Kingdom, the Government confirmed in October 2021, in the run-up to COP 26 in Glasgow, that it would introduce the first mandatory TCFD-aligned reporting requirements for the private sector from 6 April 2022. The United Kingdom Government also produced an updated roadmap for sustainability in 2021, entitled "Greening Finance: A Roadmap to Sustainable Investing".

The Financial Conduct Authority (FCA) and the Prudential Regulatory Authority (PRA) have built on the themes of the roadmap to develop the Sustainability Disclosure Requirements (SDR) and investment labels. The SDR presents the United Kingdom with an "opportunity to build a robust regulatory framework to empower consumers, minimise greenwashing and promote sustainable finance". The SDR will mandate the information that sustainable funds will have to disclose in the United Kingdom and also includes three labels to represent different types of ESG / sustainability execution: Sustainable Focus, Sustainable Improvers, and Sustainable Impact. It is similar to what the Sustainable Finance Disclosure Regulation (SFDR) is already doing in the European Union. In December 2022, the FCA opened consultation on the SDR to allow stakeholders to shape a common agreement on the pertinent ESG issues for United Kingdom businesses.

In general, there may be overlap between some ESG issues. However, the categorisation of these issues under E, S, or G is largely dependant on the specific properties of the business and its key stakeholders, including investors and respective regulatory authority. In most cases it is understood that:

- environmental factors are those that pertain to the natural world and the conservation of it. These include the use of, and interaction with, renewable and non-renewable resources;
- social factors are those that affect human life and relationships. This includes the management of human capital, non-human animals, local communities and clients; and
- governance factors refer to the norms and principles for running a company. They have to do with issues linked to countries and / or jurisdictions, or that are common practice in an industry, as well as in the interest of broader stakeholder groups.

Below is an example of more specific ESG factors:

**Environmental**
- Climate change and carbon emissions
- Air and water pollution
- Biodiversity
- Deforestation
- Energy efficiency
- Waste management
- Water scarcity

**Social**
- Customer satisfaction
- Data protection and privacy
- Gender and diversity
- Employee engagement
- Community relations
- Human rights
- Labour standards

**Governance**
- Board composition
- Audit committee structure
- Accounting standards compliance
- Bribery and corruption
- Executive compensation
- Lobbying
- Political contributions
- Whistle blower schemes
- Litigation risk

ESG factors can often be measured (e.g. what the employee turnover for a company is), but it can be difficult to directly assign them a monetary value (e.g. what the cost of employee turnover for a company is). All in all, ESG acknowledges the versatile inter-relationship between environmental, social and governance issues and investment.

## 2.1 Environmental (E): restructuring environmental liabilities

### *2.1.1 Types of environmental liabilities*

With climate change finally being afforded critical consideration on the global agenda, in 2019 the United Kingdom became the first G7 nation to enact legislation aimed at reducing its emissions to net zero by 2050. The United Kingdom continues to develop a reactive and proactive framework designed to ensure that environmental measures, accountability and governance are interweaved into the mindsets and operations of businesses across the economy. This includes, for example, very detailed rules for listed businesses and some FCA regulated businesses around environmental disclosures and forthcoming rules on financial product labelling to tackle "greenwashing".

A range of liabilities can arise as a result of damage to the environment. Such damage will typically encompass air pollution, water pollution and /or land contamination.

The liabilities that may arise as a result of such damage include: (i) contractual liabilities; (ii) civil liabilities; (iii) regulatory liabilities; and (iv) remedial liabilities. However, the specific types of environmental liabilities and the level of regulation a company may be subject to in the United Kingdom is determined by a number of factors including:

- the sector which the company operates in;
- the company's business operations and underlying activities;
- the assets it holds; and
- its key stakeholders (i.e., its shareholders, investors, lenders, employees, counterparties and customers).

Each of these factors contributes to the regulatory and legal regimes in which the business operates and the impact a company has on the environment and thereby the types of liability a company may be exposed to. The rules are often complex – making the cost of compliance considerable and increasing the risk of (inadvertent) breach. For example, a company in the real estate sector which owns and operates numerous mixed-use buildings will need to consider (among other things): energy efficiency and consumption, sustainable materials, waste management, tenants' business operations, water pollution, land contamination and nuisance. Turning to its key stakeholders, it will also need to take into consideration any environmental-related performance indicators put in place by its own management together with investors and lenders. Companies operating within energy intensive industries, aviation or the power generation sector will be subject to the obligations set out in the UK Emissions Trading Scheme (UK ETS), which regulates greenhouse gas emissions-related activities.

Where a breach has occurred, many environmental offences in England and Wales are prosecuted by the appropriate regulator in the criminal courts with penalties normally comprising fines and / or imprisonment. Depending on the nature and underlying causes of the breaches which have occurred, in addition to taking action against the company, regulators such as the Environment Agency or the FCA have scope to take action against the company's directors (for example, when there has been a breach of fiduciary obligations owed towards the company). Civil sanctions may also be imposed in respect of certain environmental offences and include monetary penalties, stop notices, discretionary requirements and enforcement undertakings (the latter being the most often used and as an alternative to criminal proceedings). Environmental regime breaches can trigger remediation obligations such as clean-up (in the pollution or contamination context) or rectification following the issuance of an enforcement notice. Private environmental damages claims may be brought, such as claims for nuisance, negligence and fraudulent misrepresentation.

For example, May 2022 marked the settlement of the long-standing UK Volkswagen NOx Emissions Group Litigation, in which Volkswagen is set to pay out £193m to circa 90,000 drivers across England and Wales. Settlement was reached ahead of a six month trial anticipated to take place in early 2023 and follows a High Court preliminary issues decision in which it was found that Volkswagen had used so-called defeat devices in certain diesel car models in an attempt to circumvent clean air regulations. This case highlights the vast scope for claims to be brought and for companies to be called into question.

### 2.1.2 *Priority given to environmental liabilities*

Environmental liabilities will typically rank as an unsecured claim in an administration or liquidation. However, it is possible that certain environmental liabilities may rank as an expense in the administration or liquidation.

There have been two decisions[1] of the Scottish courts concerning compliance with a notice served under section 59 of the Environmental Protection Act 1990 which required the removal of waste. In each case, the court held that the costs of complying with the section 59 notices were an expense of the liquidation, which would be priority claims. While the outcome of these decisions would not apply directly to insolvency practitioners appointed over English companies, the English courts would likely consider the arguments raised in these cases if required to do so.

### 2.1.3 *Disclaimer of environmental obligations*

In an insolvency, any officeholder will seek to limit their exposure to risk of environmental liabilities. This may include placing the relevant company into liquidation as soon as possible to allow the liquidation the option to disclaim any onerous contracts or property pursuant to section 178 of the Insolvency Act 1986. There has been case law[2] which has determined that waste management licences (which are now a form of environmental permit following the current environmental permitting regime coming into force on 6 April 2008) can be disclaimed as onerous property.

However, the ability to disclaim environmental contracts is limited – as certain categories of contract are expressly excluded from the regime by statute.

## 2.2 Social (S): restructuring health or safety-related liabilities

### 2.2.1 *Types of health and safety-related liabilities*

Health and safety legislation in the United Kingdom is primarily dictated by the Health and Safety at Work etc Act 1974 together with various other pieces of legislation, and forms just one of the key considerations in the multifaceted "social" compendium of ESG. While health and safety legislation is well-established in the United Kingdom, the promotion of social awareness and the establishment of healthy social constructs within business environments is an evolving area, from the introduction of the Modern Slavery Act in 2015 to gender pay gap reporting and businesses taking real action to ensure diversity within workplaces.

In relation to health and safety, it is the nature of a company's business and the activities it, its directors and employees engage in, the severity of the risks imposed in conducting such activities and other indicators including the number of employees – which are all key determinative factors when assessing which health and safety obligations a company, director or employee owes. Workplace health and safety requirements require employers to:

- conduct risk assessments;
- provide an adequate working environment (covering ventilation, heating, lighting, workstations, seating and welfare facilities); and
- provide protective clothing and equipment.

Further, there are specific regulations in place which deal with hazardous materials, including the Controls of Asbestos Regulations 2012, which deals with exposure to asbestos.

Certain health and safety breaches (including failing to produce a written health and safety policy and properly recording significant findings in risk assessments) constitute criminal offences and expose a company to a range of sanctions, including improvement notices, prohibition notices or criminal prosecution under the Health and Safety (Offences) Act 2008. Further, directors, managers

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1 *Doonin Plant Limited (in Liquidation)* [2018] CSOH 89 and *Dawson International plc* [2018] CSOH 52.

2 *Re Celtic Extraction Ltd (in liquidation)* [2001] Ch 475.

or company secretaries may also be held individually liable in instances where the affiliated company is guilty of a health and safety offence or where its commission is in some way attributable to the individual's own actions, consent, connivance or negligence.

While prosecutions are rare, companies can also be convicted of corporate manslaughter under the Corporate Manslaughter and Corporate Homicide Act 2007, as was the case in January 2022, when Deco-Pak (a garden supplies company) was found guilty of the same following a fatal incident caused by machinery used to bag up stones and other gardening paraphernalia.

#### *2.2.2 Treatment of health and safety-related liabilities*

There is a statutory order of priority in English insolvencies which gives preferential treatment to some types of unsecured liabilities (for example, certain unpaid wages of employees and certain taxes). However, there is no specific priority afforded to health and safety-related liabilities. If the relevant claimant of such liability was granted a valid security interest in the assets of the debtor company, this secured interest would rank in priority to unsecured claims depending on the nature of the assets secured and whether the security was fixed or floating. Otherwise, health and safety-related liabilities of an insolvent company will rank as an unsecured claim.

The treatment of health and safety-related liabilities, although fully considered by the insolvency practitioners in the lead up to and immediately after their appointment, may present fewer issues if, for example, the business and assets are sold by way of pre-packaged administration. However, particular care should be taken when there is an intention to trade or otherwise retain the business and assets for a period post-appointment given the insolvency practitioner's role as agent of the company.

### 2.3 Governance (G): third party releases in favour of directors and officers of the company

Releases of third party liabilities are common in English restructurings, in particular Schemes and RPs. A common example is the release of liabilities owed by a guarantor of the principal debtor which has proposed a Scheme or a RP. If the guarantee liability was not released, this would jeopardise the implementation of the debtor company's restructuring, as the guarantor would have a cross-claim against the debtor company if a demand was subsequently made by a creditor under the guarantee.

It is also common for directors, officers and advisers of a company launching a Scheme or a RP to obtain a release of liabilities in relation to preparation and negotiation of the Scheme or RP and the wider restructuring implemented by the Scheme or RP. It would be unusual for such releases to extend to liabilities unrelated to the restructuring and, even if included, the release would only be binding on those stakeholders which were bound by the Scheme or RP (which may not necessarily include all such stakeholders).

However, there is no mechanism available to release directors and officers of a company from any claims by an insolvency practitioner arising as a result of:

- an antecedent transaction (e.g. a transaction at an undervalue or preference);
- misfeasance;
- fraudulent trading; or
- wrongful trading following the administration or liquidation of a company.

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

In a restructuring or insolvency of a company where environmental liabilities are a possible factor, early contact should be made with the Environment Agency, Natural England, the Marine

Management Organisation, the Health and Safety Executive and / or the relevant the local planning authority, as applicable.

Where a sale of the business and assets of the company is envisaged by an insolvency practitioner, they will be required to liaise with the Environment Agency to ensure the application to transfer any environmental permits is completed property and promptly. The insolvency practitioner will also be required to liaise with the Environment Agency if: (i) an environmental permit is required to continue to trade the business; or (ii) a surrender of any environmental permits is envisaged to ensure that any surrender reports are completed properly and that any improvement conditions stipulated as a condition of the surrender are satisfied.

#### *3.1.1 Approving a restructuring plan*

This is addressed in section 1 above.

#### *3.1.2 Discretion to consider wider public interest concerns*

It is conceivable that, to the extent any environmental liabilities are proposed to be compromised by a RP or Scheme, the relevant environmental agency or authority may appear at the Convening Hearing or Sanction Hearing of a RP or Scheme to argue that the terms of such RP or Scheme are unfair.

#### *3.1.3 Influence of environmental protection authorities or environmental advocacy groups in a restructuring*

Any influence by an environmental protection authority or environmental advocacy group in a RP or Scheme is limited to the extent that it is expressly raised by a stakeholder in such proceedings. In a RP or Scheme, the judges will look at the merits and fairness of the proposed RP or Scheme but not the commercial aspects of it (and therefore, by extension, any public policy considerations).

### 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

#### *3.2.1 Approving a restructuring plan*

This is addressed in section 1 above.

#### *3.2.2 Discretion to consider wider public interest concerns*

It is conceivable that, to the extent any employee liabilities are proposed to be compromised by a RP or Scheme, the relevant labour authority, union or employee / worker advocacy group may appear at the Convening Hearing or Sanction Hearing of a RP or Scheme to argue that the terms of such RP or Scheme are unfair.

#### *3.2.3 Protection of employee rights*

In the context of employment, the “S” in ESG generally refers to how employers interact with their employees, customers, supply chain and the community. This includes how employers include employees in their decision-making processes. The potential damage to a company’s reputation by not engaging properly with employees was highlighted clearly when P&O Ferries dismissed nearly 800 employees during an on-line meeting and then replaced them with temporary agency staff. The backlash from employees, trade unions, the general public and the United Kingdom Government dominated the news cycles for several weeks and has had a long-term impact on the company’s standing.

It is important to recognise that while ESG is a significant factor in engaging the workforce, ESG does not change existing employment law in respect of an employer’s obligation to provide information and to consult with employees and / or employee representatives. The obligations to provide information and to consult are set out in the relevant legislation and this is described in more detail below. However, it should be noted that the relevant legislation does not include any obligations for an agreement to be actually concluded with the employees or their representatives.

- *Collective Redundancies (Trade Union and Labour Relations (Consolidation) Act 1992 (TULRCA))*

  If a restructuring plan is likely to result in the redundancies of 20 or more employees at one establishment (an establishment can be wider than a single workplace but may not include the entire organisation) within a period of 90 days or less, the employer must consult with a recognised trade union and / or employee representatives (section 188 of the TULRCA). In addition to collective consultation, the employer must also:

  - consult individually with potentially redundant employees; and

  - notify the Department for Business, Energy and Industrial Strategy (BEIS). Failure to notify the BEIS is a criminal offence.

  The obligation to consult under the TULRCA must "begin in good time" and acts as a standstill period in which the proposed dismissals cannot take effect once consultation has started. Consultation must begin at least 45 days before the first dismissal takes effect where an employer proposes to dismiss more than 100 proposed redundancies and consultation must begin at least 30 days before the first dismissal takes effect where the proposal relates to fewer than 100 proposed redundancies.

  The consultation must be about ways of:

  - avoiding the dismissals;

  - reducing the numbers of employees to be dismissed; and

  - mitigating the consequences of the dismissals and be conducted with a view to reaching agreement on these matters.

  A breach of the obligation to consult under the TULRCA can result in a substantial liability to the employer as it may result in an award of up to 90 days' actual gross pay for each affected employee. The protective award is an order that the employer shall pay the employees for a "protected period". The protective award is designed to punish the employer for not complying with its obligations to consult under the TULRCA and receipt of wages during the protected period will not reduce an employee's entitlement under the protective award. However, while there is an obligation to consult with a view to reaching an agreement, there is no obligation to actually reach an agreement.

- *The Information and Consultation of Employees Regulations 2004 (ICE Regulations)*

  In any restructuring, consideration will need to be given as to whether an information and consultation agreement (I&C Agreement) has been put in place under the ICE Regulations. The ICE Regulations apply to organisations that have 50 or more employees and have a registered or head office or principal place of business in Great Britain. The I&C Agreement will set out the procedures that the employer needs to follow in providing information and consulting employees on important economic and employment-related matters.

  Disputes in respect of the I&C Agreement can be taken to the Central Arbitration Committee (CAC) within three months of the disputed event. If a complaint is upheld, then:

  - the CAC may order that the situation is rectified by a specified date. BEIS guidance states that CAC orders may be enforced through the courts. However, the CAC cannot: (i) alter, undo, delay or prevent any action that an employer has undertaken or proposes to undertake (regulation 22(9)); or (ii) issue an order that has the effect of preventing an employer from implementing a business decision or arrangement, or of requiring the employer to change the decision or arrangement (regulation 9(9)); and

- the employee may apply for a penalty to be imposed against the employer by the Employment Appeal Tribunal (EAT) and the penalty is payable to the Secretary of State. The maximum penalty that can be awarded is £75,000.

- *Transfer of Undertakings (Protection of Employment) Regulations 2006 (TUPE)*

  If the restructuring arrangements involve a transfer of employees from one employer to another under TUPE (a relevant transfer), both the buyer (transferee) and seller (transferor) must inform and (if applicable) also consult representatives of their employees who will be affected by the transfer. There is a list of statutory information that must be provided to the representatives in writing. If an employer envisages measures will be taken in relation to affected employees then the employer that envisages such measures has an obligation to consult the employee representatives about them.

  There are no exceptions for insolvent businesses to avoid the obligations to inform and consult. The insolvent transferor may try the defence that "special circumstances" make information and consultation not reasonably practicable (regulation 13(9) of the TUPE). However, this defence is likely to be narrowly construed.

  The obligation is to provide the statutory information referred to above and, if required in the particular circumstances, to consult about the relevant measures with a view to reaching agreement on them, but there is no obligation to actually conclude an agreement. If the employer fails to provide the required information and / or to consult (if applicable), a claim may be brought by a recognised trade union, elected employee representative or affected employee (regulation 15 of the TUPE). The employment tribunal can award compensation payable to the relevant affected employees of up to 13 weeks' pay for each affected employee.

- *Changes to pensions*

  If the restructuring arrangements involve an organisation that has more than 50 employees in the United Kingdom and the employer is proposing changes to occupational or personal pension schemes where there are direct payment arrangements in place that enable the employer to make contributions for its employees then the employer is required to consult with both active and prospective scheme members or their representatives (Occupational and Personal Pensions Schemes (Consultation by Employers and Miscellaneous Amendment) Regulations 2006).

  The consultation process should be for a minimum of 60 days (regulation 15(4)) and the parties are under a duty to work in a spirit of cooperation, taking into account the interests of employer and employees (regulation 15(2)). The Pensions Regulator can enforce the consultation requirements and may impose a penalty of up to (i) £5,000 for an individual; or (ii) £50,000 for a company, if the employer has failed to comply with the duty to consult without a reasonable excuse. However, the Pensions Regulator does not have the power to reverse a change that the employer has made without meeting the consultation requirements.

- *Health and safety*

  If a restructuring involves changes to the way in which an organisation operates (e.g. changes to premises, staffing ratios, training, introduction of new technologies, etc), there may be health and safety implications that need to be considered.

  Employers must consult with employees on health and safety matters under: (i) the Safety Representatives and Safety Committee Regulations 1977 (which applies where the employer recognises a trade union); and (ii) the Health and Safety (Consultation with Employees) Regulations 1996 (which applies when there is no recognised trade union).

  There are significant implications for failing to comply with obligations under the Health and Safety at Work etc Act 1974 (HSWA). On summary conviction in the Magistrates Court, the maximum fine is unlimited and the maximum prison sentence is six months. On conviction in the Crown Court, the fine is unlimited or a two year prison sentence.

- *Takeovers*

  If the restructuring involves a public offer to purchase all the shares of a listed company, the City Code on Takeovers and Mergers (Takeover Code) will apply. The Takeover Code requires that the bidder and target companies provide relevant information in respect of the offer to employee representatives and / or employees. The information should be provided at the same time as posting the offer document to shareholders.

  There is no obligation to consult employees under the Takeover Code. However, any I&C Agreement will need to be checked as a consultation may be required under the terms of the I&C Agreement.

  In the event of a breach of the employees right to be informed, the breach would be dealt with by the Takeover Panel. The Takeover Panel will determine the consequences depending on the nature of the breach.

### 3.3 Governance (G): board / management conflicts addressed in a restructuring

English company law requires directors of companies to avoid conflicts of interests in connection with their fiduciary duties owed to the relevant company. Section 177 of the Companies Act 2006 also provides that, if a director of a company is in any way, directly or indirectly, interested in a proposed transaction or arrangement with the company, he or she must declare the nature and extent of that interest to the other directors.

In a restructuring of a private equity portfolio company, conflicts can sometimes arise where the sponsor of an operational company being restructured has appointed directors on that company to represent its interests. Often sponsors only appoint directors on holding companies at the top of the corporate structure and executive management team members are appointed directors of the operational companies.

However, where there are shareholder appointees at the level in the corporate structure where the restructuring is being implemented, there is a risk of conflict (e.g., where the sponsor is considering injecting additional funding into the group in exchange for a debt write-off). In the case of conflict, the practical solution is sometimes for the board to form a sub-committee of independent directors and delegate the negotiation of the terms of the restructuring with the company's stakeholders to that sub-committee. It is not unusual to see such sub-committees formed during a restructuring. Early formation of such a sub-committee can allow the independent directors to focus on delivering the desired restructuring outcome. The sub-committee members may agree a formal or informal framework for its conduct.

Conflicts can also arise where management incentive plans (MIPs) are proposed as part of a restructuring. In a restructuring it is commonplace for directors of the relevant company to benefit from MIP and creditors are often willing to agree to MIPs where they are perceived to assist in achieving successful performance of the company post-restructuring. The management would typically be separately advised and would negotiate terms of the MIP directly with the creditors (assuming that the shareholders had no economic interest in the company post restructuring).

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

The United Kingdom's environmental regimes are largely embodied in statute and at common law rather than in industry guidelines.

However, in terms of best practices, it is recommended that in any restructuring or insolvency where environmental issues are a concern, insolvency practitioners: (i) carry out effective due diligence in respect of any potential environmental issues or liabilities; and (ii) engage with the Environment Agency or other relevant environmental agency or authority as soon as possible.

**4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring**

There are a limited number of "soft law" instruments in the United Kingdom that are applicable in protecting employees' interests in a restructuring context. Some of the most relevant examples include:

- 2018 UK Corporate Governance Code (2018 Code)

  The 2018 Code is not law and compliance is not compulsory. The Financial Reporting Council (FRC) asks that companies either follow the 2018 Code or explain why they do not. Even though the 2018 Code only applies to premium listed companies, many smaller companies follow the 2018 Code for best practice.

  Provision 5 of the 2018 Code states that the board should understand the views of the company's key stakeholders, including employees, and should describe in the annual report how the interests of these stakeholders and the matters set out in section 172 of the Companies Act 2006 have been considered in board discussions and decision-making.

  Provision 5 also states that for engagement with the workforce, one or a combination of three workforce engagement methods should be used:

  - a director appointed from the workforce;
  - a formal workforce advisory panel; and / or
  - a designated non-executive director (NED).

- Wates Corporate Governance Principles for Large Private Companies and supporting guidance (Wates Principles)

  The 2018 Code was complemented by the Wates Principles for the governance of large private companies. It is hoped that a wider range of companies than those required to report under the new legislative requirements (section 414CZA of the Companies Act 2006 (CA 2006) requires certain companies to include a section 172 statement) will use the Wates Principles. The Wates Principles are intended to be flexible and high-level. The guidance is not intended to be a set of requirements but to assist companies in understanding how to apply the principles. Principle 6 (stakeholder relationships and engagement) of the Wates Principles includes a section on workface engagement that encourages employers to:

  - consider the impact to stakeholders that the company's activities may have, which could include environmental impacts;
  - engage with stakeholders;
  - ensure that boards should have the facility to receive feedback from discussion with stakeholders; and
  - develop both informal and formal channels to enable meaningful two-way dialogue. This may include engagement with trade unions or employee groups.

- Living wage

  There has been an increase on the focus of the social impact of low pay. In a restructuring it may need to be determined whether the employer is an accredited Living Wage Employer. The living wage is set by the Living Wage Foundation and provides for a voluntary minimum hourly rate of pay calculated according to the basic cost of living. About half of FTSE 100 companies are accredited Living Wage Employers along with about 10,000 smaller companies. If a restructuring proposed to reduce employee wages below the Living Wage, the employer would need to consider both the contractual and reputational issues associated with no longer being an accredited Living Wage Employer.

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

Insolvency practitioners are subject to the "Insolvency Code of Ethics", which aims to help insolvency practitioners meet their professional and ethical obligations.

The Insolvency Code of Ethics provides five fundamental principles for ethics for insolvency practitioners:

- integrity – to be straightforward and honest in all professional and business relationships;
- objectivity – not to compromise professional and business judgments because of bias, conflict of interest or undue influence of others;
- professional competence and due care – to: (i) attain and maintain professional knowledge and skill at the level required to ensure that a client or employing organisation receives competent professional service, based on current technical and professional standards and relevant legislation; and (ii) act diligently and in accordance with applicable technical and professional standards;
- confidentiality – to respect the confidentiality of information acquired as a result of professional and business relationships; and
- professional behaviour – to comply with relevant laws and regulations and avoid any conduct that the insolvency practitioner knows or should know might discredit the profession.

Paragraph 2310 of the Insolvency Code of Ethics provides that insolvency practitioners are required to comply with the fundamental principles and apply the conceptual framework to identify, evaluate and address threats. It also provides that provides that a conflict of interest creates threats to compliance with the principle of objectivity and might create threats to compliance with other fundamental principles.

Paragraph 2311 provides that an insolvency practitioner shall not allow a conflict of interest to compromise professional or business judgment and, where a threat to the principle of objectivity or other fundamental principles cannot be eliminated, an insolvency practitioner shall not accept the proposed insolvency appointment.

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

The appetite for ESG finance has experienced dramatic growth since the first green bond was issued in 2007. Almost EUR 750 billion of ESG bonds and loans were issued in Europe in 2021,[3] with the global ESG finance market estimated to be valued in the region of US $2 trillion.

ESG finance is intended to lead to increased investment in sustainable activities. While there is no single definition for ESG finance, it is described by the UN PRI as investment approaches that "seek to combine financial return with a moral or ethical return". A wide range of ESG finance products have been developed and these include green bonds and loans, social bonds and loans, sustainability-linked bonds and loans and sustainability bonds.

[3] Association for Financial Markets in Europe (AFME).

#### 5.1.1 *Green bonds and loans*

The most established and by far the largest portion of the ESG finance market to date is green bonds and loans. Voluntary but market-accepted guidelines for green bonds and loans are published and updated by the International Capital Market Association (ICMA) and the Loan Market Association (LMA). The ICMA's Green Bond Principles (GBP) defines green bonds as "any type of bond instrument where the proceeds or an equivalent amount will be exclusively applied to finance or re-finance, in part or in full, new and / or existing eligible green projects and which are aligned with the four core components of the GBP". Therefore, while the terms "green bonds" (or "green loans") are often used generically in the context of green and sustainable transactions, the terms should only be used in circumstances where the following four core components apply:

- use of proceeds – the proceeds (or an equivalent amount) are utilised to finance or refinance in part or in full new and / or existing eligible "green projects", being those that will promote progress on environmentally sustainable activities (e.g. infrastructure for clean energy, pollution prevention, procuring low carbon transport solutions, climate change adaptation, etc);

- process for evaluation and selection – outline the decision-making process followed to determine the eligibility of the green projects, including the type of projects the funds are meant to support, the criteria for assessing environmental benefits, and the environmental impact they expect the projects to produce. The processes for project evaluation and selection can be supplemented by a review by a third party;

- management of proceeds – net proceeds (or an equivalent amount) should be moved to a sub-portfolio or otherwise tracked by the issuer or borrower and attested to by a formal internal process that will be linked to the issuer's or borrower's lending and investment operations for projects; and

- reporting – companies should make and keep readily available up-to-date information on the use of proceeds allocation, and report this at least annually such as via newsletters, website updates or filed financial reports on the specific investments made from the green bond or loan proceeds, detailing (wherever possible with regards to confidentiality and / or competitive considerations) the specific projects and amounts invested along with the expected environmentally sustainable impact.

The offering circular for such green bond deals will generally include disclosure of the company's framework (or a summary of the framework) which reflects the four components, including the green projects in respect of which an "amount equal to" the net proceeds will be used. For example, an issuer of green bonds by may disclose in its offering circular that an amount equal to the net proceeds would be used to fund or refinance new or existing eligible green projects related to:

- clean transportation;

- pollution prevention and control;

- sustainable water management;

- renewable energy; and

- energy efficiency in alignment with the GBP.

#### 5.1.2 *Social bonds and loans*

The core principles in respect of social bonds and loans mirror in large part the above principles. However, the main difference being that the proceeds in respect of social bonds and loans must be used to finance or refinance a "social project" (e.g. affordable housing, employment generation, food security and access to essential services).

#### *5.1.3 Sustainability bonds and loans*

Sustainability bonds mirror in large part the above principles for green and social bonds and loans. However, sustainability bonds and loans can be used for the financing or refinancing of a combination of both green and social projects.

#### *5.1.4 Sustainability-linked bonds and sustainability-linked loans*

Sustainability-linked bonds (SLBs) and sustainability-linked loans (SLLs) incentivise the issuer or borrower to improve its performance against certain forward-looking and pre-determined sustainability performance targets (SPTs). They are not conditional on the net proceeds being used for a specific, "green" purpose. In practice, this would typically mean that the pricing on the bond or loan is directly linked to the sustainability performance of the issuer or borrower.

As with green bonds and loans and social bonds and loans, the ICMA and the LMA have produced voluntary but market-accepted guidelines for SLBs and SLLs. The five core principles that apply SLBs and SLLs are:

- selection of one or more key performance indicators (KPIs) – the KPIs should be relevant, core and material to the company's overall business, as well as quantifiable and able to be externally verifiable and benchmarked;
- calibration of one or more SPTs per KPI – SPTs should be "ambitious" and reflect the company's ESG strategy (i.e. represent a material improvement in the respective KPI and be more than a business-as-usual trajectory);
- bond or loan terms – the financial or structural terms of the instrument will vary if the selected KPI(s) do not reach the SPT(s), most commonly that failing to achieve KPIs and / or SPTs will result in a step-up in the coupon or interest rate;
- reporting – the company's performance against KPIs and SPTs should be reported regularly, at least annually; and
- verification – independent and external verification in respect of the company's performance against KPIs and SPTs should be undertaken at least annually, such as by an auditor or an environmental consultant.

#### *5.1.5 Restructuring implications*

The precise implications in respect of a potential restructuring will be dependent on the terms of the relevant bond or loan documents. The legal documents should cover the obligations in respect of the core principles set out above and the consequences of breaching these obligations will be dependent on what the parties have agreed. While it is unlikely that there will be any events of default in respect of breaching any of the core principles (although this should of course be checked), the potential consequences could include: (i) a higher coupon or interest rate on a SLB or SLL which in turn will increase the cost of financing to the entity being restructured; and (ii) the closing off of any other ESG related financing routes if it is not able to comply with current obligations.

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

Financial institutions have shown their commitment to ESG through a range of voluntary industry initiatives that include:

- the International Finance Corporation's (IFC) Environmental and Social Performance Standards – these standards define IFC clients' responsibilities for managing their environmental and social risks. The IFC works with financial institutions to introduce environmental, social, and governance standards, as well as risk management to their lending practices;

- Equator Principles (project finance) – EP 1 (2003); current version EP 4 – the Equator Principles (EPs) are a set of voluntary guidelines which have been adopted by approximately 134 banks and other financial institutions across 38 countries. The EPs provide a framework for identifying, assessing, and managing the environmental and social risks of large infrastructure and industrial projects EPFIs finance using project financing and certain qualifying corporate loans;

- LMA / APLMA / LSTA Green Loan Principles (2018) – as described above, the Green Loan Principles (GLPs) comprise voluntary recommended guidelines, to be applied by market participants on a deal-by-deal basis depending on the underlying characteristics of the transaction, that seek to promote integrity in the development of the green loan market by clarifying the instances in which a loan may be categorised as "green". The GLPs build on and refer to the Green Bond Principles (GBPs) of the International Capital Market Association, with a view to promoting consistency across financial markets;

- UNEPFI Responsible Banking Principles (2019) – the UNEPFI was founded in 1992 as a means by which the United Nations and the global financial sector could work more closely together in developing a more sustainable world. It commits signatories to integrating environmental issues into all aspects of their operations and recommends that signatories report publicly on environmental issues. The UNEPFI Principles for Responsible Banking are a set of global voluntary guidelines for banks. They provide the framework for a sustainable banking system and help the industry to demonstrate how it makes a positive contribution to society. The framework comprises six principles, a document setting out the key steps for signatories, and a reporting and self-assessment template. The UNEPFI has published non-binding guidance to banks on measures to implement each principle;

- the TCFD (2015) – as noted above, the TCFD is advisory body set up by the G20 and the FSB to address concerns around insufficient disclosure of climate-related risks and opportunities for businesses. The TCFD published its final recommendations in June 2017, which are intended to apply to all companies with listed debt or equity in the G20, and additionally to asset managers and asset owners (recognising that these organisations are typically unlisted). In the United Kingdom, all premium listed companies were mandated to report their climate risk exposure in line with the TCFD's recommendations from 1 January 2021, and this will expand to all United Kingdom companies by 2025 (see more detail in section 5.3 below);

- the Task Force on Nature-Related Financial Disclosures (2020) – this is an international initiative that builds on a model developed by the TCFD. Its mission is to provide a framework for how organisations can address environmental risks and opportunities with the ultimate goal of channelling capital flows into positive action. The TNFD is developing an integrated risk management and disclosure framework for organisations to report and act on evolving nature-related risks and opportunities. The TNFD plans to release its final recommendations for the Framework in September 2023;

- the ICMA: Social Bond Principles (2020), Green Bond Principles (2018), Sustainability-Linked Bond Principles (2020) and Sustainability Bond Guidelines (2018) – as referenced in the prior section, these principles are a collection of voluntary frameworks with the stated mission and vision of promoting the role that global debt capital markets can play in financing progress towards environmental and social sustainability; and

- the AFME roadmap, "Governance, Conduct and Compliance in the Transition to Sustainable Finance" (September 2020) – this addresses issues such as corporate purpose, board governance oversight, shareholder activism and greenwashing. The paper sets out 15 key principles that firms may wish to consider when developing their approach. The principles cover objectives and governance, risk management, compliance and monitoring and impact measurement. The AFME intends the paper to serve as a roadmap to assist boards and senior leadership in establishing or furthering their corporate purpose and objectives in relation to sustainable finance.

#### *5.2.1 Restructuring implications*

As most of the above initiatives are voluntary, the implications on a potential restructuring will be dependent on the content of the legal documentation. However, the United Kingdom Government has shown a desire for the United Kingdom to become a "net zero financial centre" and to start adopting some of these voluntary initiatives as mandatory requirements (see further details below in respect of the TCFD). Restructuring professionals will need to ensure that they are up to date on all current mandatory requirements to avoid any potential breaches on a restructuring.

### 5.3 Promoting ESG by the central bank and regulators

The promotion of ESG in the United Kingdom by regulators has largely focused on disclosure requirements. For example:

- PRA supervisory statement SS3/19 and letter dated 1/7/2020 on managing climate-related financial risk

  In 2019, the Bank of England's Prudential Regulation Authority (PRA) issued a Supervisory Statement (SS3/19) that sets expectations for firms regarding their consideration of climate risk across four areas: governance arrangements, risk management, stress testing and scenario analysis, and disclosure.

  The PRA expects firms to address the financial risks from climate change through their existing risk management frameworks, and should consider disclosing how climate-related financial risks are integrated into their governance and risk management processes. This includes the process by which a firm has assessed whether these risks are considered material or principal risks.
  Firms are expected to:

  - embed the consideration of the financial risks from climate change in their governance arrangements;
  - incorporate the financial risks from climate change into existing risk management practice;
  - use long-term scenario analysis to inform strategy setting, and risk identification and assessment; and
  - develop an approach to disclosure on the financial risks from climate change.

- CP22/20: Sustainability Disclosure Requirements (SDR) and investment labels

  The FCA has expressed its concerns in respect of "greenwashing". This is where firms make exaggerated, misleading or unsubstantiated sustainability-related claims about their investment products. In October 2022, the FCA proposed a set of new measures including investment product sustainability labels and restrictions on how terms like "ESG," "green" or "sustainable" can be used. The FCA is proposing to introduce:

  - three sustainable investment product label categories – including one for products improving their sustainability over time – underpinned by objective criteria;
  - restrictions on how certain sustainability-related terms can be used in product names and marketing for products which don't qualify for the sustainable investment labels;
  - a more general anti-greenwashing rule covering all regulated firms;
  - consumer-facing disclosures to help consumers understand the key sustainability-related features of an investment product. This includes disclosing investments that a consumer may not expect to be held in the product;

- more detailed disclosures, suitable for institutional investors or retail investors that want to know more; and

- requirements for distributors of products, such as investment platforms, to ensure that the labels and consumer-facing disclosures are accessible and clear to consumers.

The FCA's consultation period about its proposals has now closed and it is due to publish its proposed rules (having considered responses to the consultation) by the end of 2023.

- UK Green Taxonomy (or dictionary)

  The United Kingdom Government will implement a green taxonomy that will set out the criteria that specific economic activities must meet to be considered environmentally sustainable or taxonomy-aligned. Firms will be required to report against the green taxonomy as part of the SDR regime described above. Certain companies and providers of investment funds will need to disclose which proportion of their activities are taxonomy-aligned.

  In October 2022, the Green Technical Advisory Group (GTAG) published a report containing its advice on the development of a UK green taxonomy. Among other things, the report looks at how to approach onshoring the EU taxonomy set out in Regulation (EU) 2020/852 on the establishment of a framework to facilitate sustainable investment and amending Regulation (EU) 2019/2088 (Taxonomy Regulation), on which the United Kingdom green taxonomy is based. The GTAG recommends the United Kingdom Government should take an "adopt some and revise some" approach. This approach builds on the view that the focus of taxonomy use should be on investors and financial market participants, as well as their regulators. The United Kingdom Government is set to publish an updated Green Finance Strategy in 2023 that will include more information about the green taxonomy.

- TCFD Mandatory Requirements Roadmap

  The United Kingdom Government announced in November 2020 that it intended to make it mandatory for large companies and financial institutions to make climate-related disclosures aligned with the TCFD recommendations by 2025. It is anticipated that a large part of the mandatory requirements will have been implemented by 2023. The roadmap published by the UK TCFD taskforce sets out a disclosure strategy for the following categories of organisation:

  - listed commercial companies. The requirements for premium listed companies apply in relation to financial years beginning on or after 1 January 2021 and the requirements for standard listed issuers apply in relation to financial years beginning on or after 1 January 2022;

  - United Kingdom registered companies. The requirements apply from financial years beginning on or after 6 April 2022;

  - banks and building societies. No additional regulatory requirements are proposed at this time;

  - insurance companies. No additional regulatory requirements are proposed at this time;

  - asset managers, life insurers and FCA-regulated pension schemes. The requirements apply on a phased basis from 1 January 2022; and

  - occupational pension schemes. The requirements apply on a phased basis from October 2021.

- Green gilts

  In an exception to the mandated disclosure requirements set out above, the United Kingdom Government has sought to encourage ESG finance through an issuance of "green" gilts. On 30 June 2021, HM Treasury and the United Kingdom Debt Management Office (DMO) published the United Kingdom Government Green Financing Framework (Framework), setting out the Government’s climate and environmental agenda and detailing how the proceeds of the Government's proposed green gilt issues will be used. The Framework, which is aligned with the core components and key recommendations of the ICMA Green Bond Principles, sets out the basis for the identification, selection, verification and reporting of green projects that are eligible for financing from the green gilt issues. A total of £16 billion has been raised from the green gilt for projects like zero-emissions buses, offshore wind and schemes to decarbonise homes and buildings. This means the United Kingdom is one of the top three biggest national issuers of green bonds in the world.

#### *5.3.1 Restructuring implications*

As part of any restructuring, restructuring professionals will need to ensure compliance with all relevant disclosure requirements.

# UNITED STATES OF AMERICA

## 1. General overview of the restructuring regime

### 1.1 Formal restructuring procedures

The main procedure for restructuring debts in the United States is under the Bankruptcy Code.[1] The Bankruptcy Code is a piece of United States federal legislation and United States bankruptcy proceedings can only take place in United States federal courts (rather than state courts). The Bankruptcy Code is divided into chapters, which describe the types of bankruptcy cases: Chapter 7 (Liquidations); Chapter 9 (Municipalities); Chapter 11 (Reorganisations); Chapter 12 (Family Farmers or Fishermen); Chapter 13 (Individuals); and Chapter 15 (Cross-Border Cases).

Business entities typically file cases under Chapter 11 of the Bankruptcy Code, which are overseen by judges in the United States bankruptcy court.[2] Importantly, bankruptcy courts are essentially "specialised" federal courts, and have jurisdiction only over matters arising under the Bankruptcy Code, arising in a case under the Bankruptcy Code, or "core" matters related to a bankruptcy case.[3] Chapter 11 is designed to be a flexible process to provide a company with a wide array of strategic alternatives while preserving its going concern value. Once a plan is confirmed, it is binding on all creditors, regardless of whether they voted to approve the plan or not.[4]

During a case commenced under Chapter 11 of the Bankruptcy Code, the existing management usually remains in control of the company and operates the business as a "debtor in possession" (DIP), subject to supervision of the bankruptcy court. In certain circumstances, an independent trustee may be appointed to replace a DIP.[5] A Chapter 11 trustee's duties may include matters which a DIP typically perform, such as overseeing the debtor's reorganisation process and managing the debtor's day-to-day affairs, though bankruptcy courts typically tailor a trustee's role for the particular facts and circumstances of a case.[6] It is also common for a debtor to retain a chief restructuring officer (CRO) to oversee the restructuring process.[7]

While a company's management stays in place, there are several other figures that monitor the debtor's actions during a Chapter 11 case:

- the bankruptcy judge assigned to the case must approve all actions of the company which are outside the ordinary course of business;[8]

- in each case, a trustee (US Trustee) serves as the official representative of the government to oversee the administration of the case.[9] The US Trustee's responsibilities include, among other things, appointing official committees of unsecured creditors, reviewing applications for compensation of the professionals appointed in the case, examining pleadings in the case to ensure the Bankruptcy Code is not violated (and objecting where appropriate) and ensuring the debtor timely files required documents (such as monthly operating reports, schedules of assets and liabilities and a statement of financial affairs) and pays quarterly fees; and

1 Codified in 11 U.S.C. §§ 101-1532.
2 The district court has original and exclusive jurisdiction over a bankruptcy case: 28 U.S.C. § 1334(a). The district court ordinarily refers jurisdiction to the bankruptcy court: 28 U.S.C. § 157(a).
3 *Stern v. Marshall*, 564 U.S. 462 (2011).
4 11 U.S.C. § 1141(a).
5 *Idem*, § 1104(a). Ordinarily, an independent trustee is appointed where "cause" is shown. Typically, cause is present where there has been fraud, dishonesty, incompetence or gross mismanagement. See, for example, *In re PRS Insurance Group, Inc.*, 274 B.R. 381 (Bankr. D. Del. 2001).
6 In liquidations under Chapter 7 of the Bankruptcy Code, a trustee is always appointed and is tasked with the administration of the debtor's estate, including liquidating property of the estate for the benefit of creditors: 11 U.S.C. §§ 701-703.
7 It is fairly common for a company's lenders to require that an independent CRO be hired as this ensures that a sophisticated and experienced manager guides the company through a restructuring process. Among a variety of duties, a CRO will often work with lenders, the US Trustee, representatives of unsecured creditors' committees, and other parties in interest on a company's restructuring efforts. Specific tasks may include negotiating the terms of a sale or plan of reorganisation, developing budgets and managing cash flow, and analysing contracts to be rejected.
8 11 U.S.C. § 363(c).
9 28 U.S.C. § 586; 11 U.S.C. § 307.

- often, an official committee of unsecured creditors is appointed in a Chapter 11 case to represent the interests of all unsecured creditors.[10] Once appointed, an unsecured creditors' committee hires its own professionals, analyses the debtor's pre- and post-petition financials, and often negotiates key aspects of the restructuring plan.

The process of restructuring under the Bankruptcy Code begins with filing a petition for relief.[11] Once a petition is filed, the automatic stay is triggered.[12] The automatic stay pauses nearly all acts and proceedings against the debtor to give the debtor "breathing space" so that it can reorganise its affairs. The effect is a worldwide injunction barring almost all actions against the debtor or its property.

For companies with ongoing operations, the bankruptcy court will typically hold a "first day" hearing to approve interim relief within days of the petition being filed.[13] The relief granted often includes items such as:

- jointly administering the cases of related companies; [14]
- paying certain pre-petition claims for critical vendors;[15]
- maintaining the use of bank accounts;[16]
- continuing employee benefits;[17] and
- approving post-petition financing.[18]

The bankruptcy court will then hold a second day hearing which approves the foregoing relief on a final basis and approves the retention of the debtor's professionals.[19] The second day hearing is ordinarily held approximately a month after the first day hearing.

In the days and weeks following the commencement of a Chapter 11 case, a debtor must satisfy several statutory requirements.[20] First, a debtor must file schedules of assets and liabilities and statements of financial affairs within 14 days of the petition date (though this period may be extended).[21] Second, the US Trustee must hold a meeting of the debtor's creditors.[22] At the meeting, a knowledgeable corporate officer of the debtor is made available to answer questions under oath regarding nearly all aspects of the debtor, its business, its financials and its plan for an exit from bankruptcy. Third, the debtor must begin filing monthly operating reports which show a summary of cash flows (including an income statement and balance sheet).[23]

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10 11 U.S.C. § 1102(a)(1).
11 *Idem*, § 301.
12 *Idem*, § 362.
13 *Idem*, § 1107(a) (generally providing for the rights, powers and duties of a DIP). In certain jurisdictions where cases are frequently filed under Chapter 11, the processes for first day hearings are more formalised. See, for example, Del. Bankr. L.R. 9013-1(m) (providing for the processes related to motions filed with a petition).
14 11 U.S.C. § 302; Fed. R. Bankr. P. 1015.
15 See, for example, *In re Just for Feet, Inc.*, 242 B.R. 821, 824-26 (D. Del. 1999).
16 11 U.S.C. § 345.
17 See, for example, *In re CoServ, L.L.C.*, 273 B.R. 487 (Bankr. N.D. Tex. 2002).
18 11 U.S.C. § 364.
19 Most professionals are retained under § 327(a) of the Bankruptcy Code. However, the CRO and other professionals are often retained under § 363 of the Bankruptcy Code, which subjects them to less strenuous compensation requirements: 11 U.S.C. §§ 327; 363.
20 Depending on the jurisdiction, a debtor may have other non-statutory requirements such as an initial debtor interview with the US Trustee.
21 Fed. R. Bankr. P. 1007(b).
22 11 U.S.C. § 341.
23 *Idem,* §§ 1106(a)(1), 704(a)(8); Fed. R. Bankr. P. 2015.

While a debtor transitions into the bankruptcy process, it may engage in a series of actions such as:

- assuming or rejecting executory contracts and unexpired leases;[24]
- selling assets, including substantially all of its assets;[25]
- establishing deadlines by which creditors must file proofs of claim; and
- filing lawsuits against parties that received preferential or fraudulent transfers prior to the petition date.[26]

During this process, a debtor will work on an ultimate strategy for formulating a Chapter 11 plan and exiting from bankruptcy. Under the Bankruptcy Code, the debtor is given an exclusive period of 120 days from the petition date to file a plan and 180 days from the petition date to exclusively solicit votes on a plan.[27] These periods may be shortened or extended for cause. However, the maximum exclusive filing period is 18 months after the petition date and the maximum exclusive solicitation period is 20 months after the petition date.

The two most common outcomes for cases filed under Chapter 11 are: (i) sales of substantially all of the debtor's assets followed by a liquidating plan; and (ii) plans of reorganisation. In the former case, the debtor often obtains court approval of its proposed sale process and bidding procedures and court approval of the sale pursuant to section 363 of the Bankruptcy Code.[28] This provision of the Bankruptcy Code is one of the hallmarks of the Chapter 11 process as it enables, among other things:

- buyers to purchase the debtor's assets free and clear of any liens or other interests, with certain exceptions;[29]
- the transfer, without counterparty consent, of executory contracts and unexpired leases;[30] and
- secured creditors to bid for the debtor's assets up to the full face amount of their claim (commonly referred to as a credit bid).[31]

Often, to overcome potential objections to a sale, parties will agree to a liquidating plan which gives some consideration to lower priority creditors that would otherwise not receive any of the sale proceeds.

Whether pursuing a plan of reorganisation or a plan of liquidation, the debtor will frequently negotiate the terms of a plan among several constituencies with competing interests. Ordinarily, but not always, because of the priority scheme under the Bankruptcy Code, a debtor's primary negotiating partners are the senior most secured creditors.[32] Depending on the facts and circumstances of a particular case, parties may begin negotiating a plan prior to the petition date, or for months or even years following the petition date.

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24 *Idem,* § 365.
25 *Idem,* § 363.
26 Fed. R. Bankr. P. 3003(c)(3).
27 11 U.S.C. § 1121.
28 *Idem,* § 363.
29 *Idem,* § 363(f).
30 *Idem,* § 363(l).
31 *Idem,* § 363(k).
32 Additionally, these creditors often are able to dictate the terms of the use of their "cash collateral", the cash and cash equivalents subject to a security interest or lien in favor of a creditor: 11 U.S.C. § 363(a). In exchange for the debtor's consensual use of cash collateral, secured creditors often impose requirements on a debtor such as prohibiting a plan to be filed without the creditor's consent.

The first step in the plan process is for the debtor to draft and file a plan and accompanying disclosure statement.[33] A Chapter 11 plan may be a plan of reorganisation[34] or liquidation. Each Chapter 11 plan must:

- classify claims and interests;[35]
- specify whether any class is unimpaired;[36]
- describe the treatment of impaired classes;[37]
- treat each claim or interest within a particularly class identically, unless such class agrees to less favourable treatment;[38]
- provide for adequate means of implementation;[39]
- prohibit the issuance of non-voting stock in the debtor's charter;[40] and
- provide that the selection of any officer, director or trustee under the plan will be consistent with the interests of creditors.[41]

Chapter 11 plans frequently contain other provisions, such as the assumption, rejection or assignment of executory contracts or unexpired leases[42] and the settlement of claims.[43] The Bankruptcy Code requires that substantially similar claims and interests be classified together.[44] Plan proponents are given flexibility to create classes of claims and the "substantially similar" requirement will be met where there is a reasonable basis for the structure and the claims and interests have a similar legal status with respect to the debtor.[45] In practical terms, this means that secured, unsecured and subordinated debt must be treated differently and follow the order of distribution in the Bankruptcy Code.

A disclosure statement is meant to provide creditors with adequate information to inform their vote whether to accept or reject a plan.[46] Among other things, a disclosure statement usually contains information regarding:

- the nature and history of the debtor and its books and records;
- the circumstances leading to the Chapter 11 case;
- the debtor's future plans and sources of funding for those plans;
- a summary of the plan including the tax consequences of the plan;
- information about the Chapter 11 case;

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[33] A debtor may also file a motion which approves solicitation and tabulation procedures, the form of ballot and establishing other deadlines.
[34] There are many forms a plan of reorganisation may take. For example, existing equity may or may not survive, there may be a swap of debt for equity, or there may be a rights offering to allow creditors to purchase equity securities. The flexibility permitted to debtors when formulating a plan under Chapter 11 is one of its key benefits.
[35] 11 U.S.C. § 1123(a)(1).
[36] *Idem*, § 1123(a)(2).
[37] *Idem*, § 1123(a)(3).
[38] *Idem*, § 1123(a)(4).
[39] *Idem*, § 1123(a)(5).
[40] *Idem*, § 1123(a)(6).
[41] *Idem*, § 1123(a)(7).
[42] *Idem*, § 1123(b)(2).
[43] *Idem*, § 1123(b)(3).
[44] *Idem*, § 1122.
[45] *In re Armstrong World Indus., Inc.*, 348 B.R. 136, 159 (D. Del. 2006).
[46] 11 U.S.C. § 1125.

- an analysis of recoveries for creditors under the plan; and
- a discussion of the risk factors to be considered.[47]

In short, a disclosure statement is meant to provide creditors with adequate information to inform their vote on whether to accept or reject a plan. Objections to approval of the disclosure statement usually relate to the adequacy of such disclosures but may also focus on whether a plan is patently unconfirmable.[48] If the disclosure statement is approved, the debtor will begin solicitation, which includes transmitting the plan and disclosure statement, notice of confirmation hearing, ballot, voting deadline and other information to creditors entitled to vote.[49]

Voting on a plan occurs on a class-by-class basis and a plan may be confirmed / approved where each class has voted to accept it.[50] A class of claims accepts a plan where it is approved by creditors holding at least two-thirds in dollar amount and more than half in number of the allowed claims in that class which have voted.[51] If this requirement cannot be met, a plan may still be confirmed under a "cram down".[52] A cram down of a particular class may occur when at least one impaired class has accepted the plan, the plan does not discriminate unfairly against any impaired, non-consenting class[53] and the plan is fair and equitable.[54] However, even in a cram down, at least one class of impaired creditors must vote to accept the plan in order for the plan to be confirmed.[55]

If a debtor has obtained the voting necessary or satisfied the cram down requirements, other requirements must be met to confirm the plan, including showing, by a preponderance of the evidence, that:

- the plan complies with the Bankruptcy Code and is not inconsistent with public policy;56
- the plan proponent has complied with the Bankruptcy Code;[57]
- the plan was proposed in good faith;[58]
- the plan provides for the payment of certain costs;[59]
- the plan discloses the identify of officers, directors and trustees who will serve the reorganised debtor following confirmation;[60]

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47 See, for example, *In re Metrocraft Publ'g Servs.*, 39 B.R. 567 (Bankr. N.D. Ga. 1984).

48 If a plan is patently unconfirmable, it is not an efficient use of the debtor's limited resources to commence with solicitation. See, for example, *In re American Capital Equipment, LLC*, 688 F.3d 145 (3d Cir. 2012).

49 Fed. R. Bankr. P. 3017(d). Certain classes of claims may be deemed unimpaired, and because they are not entitled to vote, they may only receive notice of the confirmation hearing and their unimpaired status. Conversely, if a class of creditors is to receive no distributions under the plan, they are deemed to reject the plan and will only receive a notice of the confirmation hearing and that they are deemed to reject the plan.

50 11 U.S.C. § 1129(a)(8).

51 *Idem,* § 1126(c). This is often referred to as the "numerosity" requirement.

52 *Idem,* § 1129(b)(1).

53 This is referred to as the unfair discrimination test. This test focuses on whether there is a dissenting class of the same priority which is subject to a difference in treatment under the plan. If this situation is present, there is a rebuttable presumption that there are sufficient legal or factual distinctions between these classes and the disparity is not unfair. Put another way, a plan unfairly discriminates where it treats similarly situated classes materially different without a compelling justification: *In re Hardeman Cnty. Hosp. Dist.*, 540 B.R. 229, 238 (Bankr. N.D. Tex. 2015).

54 This is referred to as the fair and equitable test. While there are many factors which may be applied depending on a particular class or claim, the fair and equitable test will generally be met where the absolute priority rule is followed. The absolute priority rule requires that senior classes are paid in full before any distributions are made to junior classes: 11 U.S.C. § 1129(b)(2)(B)(ii).

55 *Idem,* § 1129(a)(10).

56 *Idem,* § 1129(a)(1).

57 *Idem,* § 1129(a)(2).

58 *Idem,* § 1129(a)(3).

59 *Idem,* §§ 1129(a)(4), 1129(a)(9)(A), 1129(a)(9)(B)(i), 1129(a)(9)(C), 1129(a)(12).

60 *Idem,* § 1129(a)(5).

- any rate changes proposed by the debtor which are regulated by a governmental entity have been approved;[61]
- the plan satisfies the best interests of creditors test;[62]
- the plan is feasible;[63]
- the plan provides for the continuation of retiree benefits;[64] and
- all transfers of property under the plan are consistent with non-bankruptcy law.[65]

Any creditor, including regulatory authorities that have claims against the debtor, may object to confirmation of a plan on the basis that the plan cannot meet one or more of these requirements.

If a debtor meets all the requirements, the bankruptcy court will confirm the plan pursuant to a "confirmation order." In general, a confirmation order may provide for the general discharge of pre-petition debts, with some exceptions.[66] After a confirmation order is entered, depending on the particular plan, a reorganised debtor may emerge from bankruptcy while a liquidating trust remains behind to resolve outstanding claims and affirmatively litigate claims of the debtor's estate to generate additional recoveries for creditors, such as claims for pre-petition fraudulent transfers.

A bankruptcy plan may also be pre-packaged. The requirements are the same, but under a pre-packaged plan generally all solicitation and voting happens prior to the petition date.[67] The primary benefit of a pre-packaged plan is speed, as a debtor may only be in bankruptcy for a matter of weeks, as opposed to months or years.

### 1.2 Informal restructuring procedures

Out of court restructurings in the United States are generally undertaken on a consensual basis as there are no formal procedures to bind non-consenting creditors. Generally, the company and its creditors reach an agreement to restructure outstanding obligations. Typically, this will happen when the company is facing liquidity pressure. The particular requirements and structure of an out of court restructuring will depend on, among other things, the debt instruments with the company.

## 2. Restructuring of ESG-related liabilities

### 2.1 Environmental (E): restructuring environmental liabilities

The various environmental laws of the United States are somewhat in conflict with the Bankruptcy Code, as the former seek to hold parties responsible for environmental clean-up while the latter often permits companies to restructure or discharge obligations. In general, environmental obligations which arise pre-petition can be restructured and discharged, with several exceptions:

- statutory reclamation fees due to the government.[68] These are fees that mining companies pay to reclaim land which they have disturbed or mined to fund clean-up after the mining is completed. The amounts are set by statute;

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[61] *Idem,* § 1129(a)(6).

[62] *Idem,* § 1129(a)(7). This test requires that each class of impaired creditors either voted to accept the plan or will receive as much as they would have received under a plan under Chapter 7 of the Bankruptcy Code.

[63] *Idem,* § 1129(a)(11).

[64] *Idem,* § 1129(a)(13).

[65] *Idem,* § 1129(a)(16).

[66] Certain debts may not be discharged including debts incurred based on fraud, debts caused by a debtor's willful and malicious injury, certain tax claims and regulatory fines and certain environmental claims: 11 U.S.C. § 523(a).

[67] *Idem,* § 1125(g).

[68] 30 U.S.C. § 1232(a). See, for example, *U.S. v. Ringley*, 985 F.2d 185 (4th Cir. 1993); *In re Jenny Lynn Min. Co.*, 780 F.2d 585 (6th Cir. 1986).

- obligations which are an ongoing harm.[69] This is a continuing contamination which poses an ongoing threat to human health or the environment; and

- environmental liabilities, such as an injunction or clean-up directive.[70] Some courts have determined that such injunctions or clean-up directives are not "claims" because they are not a right to payment.[71]

### *2.1.1 Types of environmental liabilities*

In the United States, environmental law is complicated and encompasses federal, state and local laws and regulations. In general, these laws impose liability based on the type of pollutant.[72] Parties may be liable for fines and clean-up costs under these statutes. Companies may also be liable to others under contract or tort liability.

### *2.1.2 Priority given to environmental liabilities*

In bankruptcy, environmental liabilities may be contingent, and bankruptcy courts will determine when the claim arises by looking to whether the pre-petition conduct was fairly contemplated by the parties.[73]

In general, pre-petition environmental claims are treated as general unsecured claims under the Bankruptcy Code. However, for certain environmental liabilities, such as those arising under the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA), the federal government can impose a lien to recover clean-up costs.[74] This means that their claims have priority over other claims.

In general, the automatic stay stops all pre-petition litigation, including efforts of governmental units. However, there are exceptions to the automatic stay which may apply to environmental claims.[75] For example, if the government is acting in its capacity as a regulator of public health, safety and welfare, the automatic stay does not apply.[76]

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69 See, for example, *In re Peabody Energy Corp.*, 958 F.3d 717 (8th Cir. 2020); *In re GI Holdings Inc*, 654 Fed. Appx. 57 (3rd Cir. 2016); *In re Torwico Elec., Inc.*, 8 F.3d 146 (3d Cir. 1993); *In re Chateaugay Corp.*, 944 F.2d 997, 1008 (2d Cir. 1991).

70 Under the Bankruptcy Code, a "claim" is "[a] right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured;" or the "right to an equitable remedy for breach of performance if such breach gives rise to a right to payment, whether or not such right to an equitable remedy is reduced to judgment, fixed, contingent, matured, unmatured, disputed, undisputed, secured, or unsecured." 11 U.S.C. § 101(5).

71 Compare *Ohio v. Kovacs*, 469 U.S. 274 (1985) (holding that because the only way the debtor could comply with the injunction was to pay money, it was a claim) and *United States v. Whizco, Inc.*, 841 F.2d 147 (6th Cir. 1988) (same) with *United States v. Apex Oil Co.*, 579 F.3d 734 (7th Cir. 2009) (holding that the government's equitable claim for the debtor to fund the clean-up was not dischargeable in bankruptcy); *In re Torwico Elec., Inc.*, 8 F.3d 146 (3d Cir. 1993) (same); *In re Chateaugay Corp.*, 944 F.2d 997, 1008 (2d Cir. 1991) (same).

72 For example, among many other laws, the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (42 U.S.C. §§ 9601 to 9675) (CERCLA) applies to contaminated land; the Clean Air Act (42 U.S.C. §§ 7401 to 7431) (CAA) applies to air pollutants; the Resource Conservation and Recovery Act (42 U.S.C. §§ 6901 to 6992k) (RCRA) applies to hazardous materials; and the Clean Water Act (33 U.S.C. §§ 1294 to 1281a) (CWA) applies to contaminated water.

73 *E.g.*, In re Chateaugay Corp., 944 F.2d 997 (2d Cir. 1991).

74 42 U.S.C. §§ 9607(l), (m) and (r). Certain states also impose super-priority liens for clean-up costs.

75 For example, it does not violate the automatic stay when, using a state environmental law, a lien on the debtor's property is created or perfected. Additionally, it does not violate the automatic stay for the determination of a potentially responsible party under the CERCLA.

76 11 U.S.C. § 362(b)(4). For example, action by the Environmental Protection Agency to compel a debtor's compliance with environmental laws falls within the police power: *In re Commonwealth Oil Refining Co., Inc.*, 805 F.2d 1175, 1183-1184 (5th Cir. 1986), cert denied, 493 U.S. 1005 (1987).

#### *2.1.3 Disclaimer of environmental obligations*

In general, a debtor under the Bankruptcy Code can abandon property which is burdensome or of inconsequential value.[77] However, the United States Supreme Court has held that hazardous property which poses a threat to public health or safety cannot be abandoned.[78] Bankruptcy courts usually apply this exception narrowly, meaning that in general, property can be abandoned unless there is an imminent and identifiable harm.[79]

### 2.2 Social (S): restructuring health or safety-related liabilities

Chapter 11 is a powerful tool for companies to resolve mass tort liabilities such as product liability and asbestos claims as it provides a centralised process to funnel all claims against a debtor to the bankruptcy court, including future or contingent claims. There are several provisions of the Bankruptcy Code which assist companies in dealing with health or safety-related liabilities:

- the automatic stay of section 362 of the Bankruptcy Code pauses all pending actions and enjoins future actions against the debtor in any forum besides the bankruptcy court.[80] Often, the automatic stay will be extended to other parties as well (such as officers and directors, affiliates, and other co-liable parties);

- section 1141 of the Bankruptcy Code provides for the discharge of a debtor's pre-petition obligations.[81] Further, section 524(a) of the Bankruptcy Code allows for an injunction to put in place in a Chapter 11 plan.[82] Together, these provisions prevent a mass tort claimant from asserting claims against the reorganised debtor, including for current and future claimants; and

- section 524(g) of the Bankruptcy Code provides for a channelling injunction into a trust funded under a plan of reorganisation in cases involving liabilities due to asbestos exposure.[83] A channelling injunction ensures that tort claimants may only recover from the trust created under a plan of reorganisation. Bankruptcy courts may allow for channelling injunctions in other cases as well.[84]

However, Chapter 11 is not always an appropriate solution for a company wishing to restructure health or safety-related liabilities.[85]

#### *2.2.1 Types of health and safety-related liabilities*

There are a litany of health and safety-related liabilities a company may face under United States law, including contract and tort law and statutory liability. Examples include the Occupational Safety and Health Act of 1970 (OSHA),[86] various products liability laws[87] and tort law regarding asbestos exposure.

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77 11 U.S.C § 554.
78 *Midlantic Nat. Bank v. New Jersey Dept. of Envtl. Prot.*, 474 U.S. 494 (1986).
79 See, for example, *In re Howard*, 533 B.R. 532 (Bankr. S.D. Miss. 2015), which permitted a debtor to abandon contaminated property which was not an imminent and identifiable harm.
80 11 U.S.C. § 362.
81 *Idem,* § 1141.
82 *Idem,* § 524(a).
83 *Idem,* § 524(g).
84 Channelling injunctions can apply to any types of claims which are "related to" the Chapter 11 case: *In re Combustion Eng'g, Inc.*, 391 F.3d 190, 230 (3d Cir. 2004), as amended (Feb. 23, 2005).
85 For example, *In re LTL Management, LLC*, 64 F. 4th 84 (3d Cir. 2023) involved a debtor seeking to restructure talc-related liability by undertaking a pre-bankruptcy merger where liabilities were transferred to the debtor entity but assets were transferred to a separate entity (a move referred to as a Texas Two Step). Creditors successfully had the Chapter 11 case dismissed as the debtor was not actually in financial distress.
86 29 U.S.C. § 651 et seq.
87 See, for example, Title 15 U.S.C. § 2301: The Consumer Product Safety Act; Title 21 U.S.C. §§ 301-399: The Federal Food, Drug, and Cosmetic Act; Title 49 U.S.C. §§ 30101-30170: The National Traffic and Motor Vehicle Safety Act.

#### *2.2.2 Treatment of health and safety-related liabilities*

In general, any health and safety related liabilities will be treated as unsecured claims under the Bankruptcy Code, though, in specific instances, there may be a reason that a claim may be treated at a higher priority.[88]

### 2.3 Governance (G): third party releases in favour of directors and officers of the company

Third party releases in favour of officers and directors of a company are one of the most highly contested areas of bankruptcy law. Third party releases refer to the ability of a debtor to obtain a release of claims against non-debtor parties in connection with a bankruptcy reorganisation plan. A plan may contain releases of non-debtor parties, such as officers and directors for any and all claims related to their conduct *vis-à-vis* a debtor, other than claims for gross negligence.

Third party releases may be consensual (i.e., binding creditors who specifically accept the release or plan) or non-consensual (i.e., binding all creditors). For the most part, consensual releases are considered non-controversial.[89] However, while they are relatively non-controversial, the question of whether affirmative consent is required, as opposed to simply opting out, is another hotly contested area.[90] As to non-consensual releases, the majority position is that they may be permissible in certain limited circumstances based on the particular facts of the case.[91]

Courts in the Second and Third Circuits typically look to a number of factors to determine whether to approve a non-consensual release, including:

- whether the released parties made substantial contributions to the case;
- whether the claims are channelled or released;
- whether there is an identity of interest between the debtor and the third party; and
- whether a majority of creditors agree to the release.

## 3. Protection of stakeholders' interests

### 3.1 Environmental (E): influence by environmental protection authorities or environmental advocacy groups in a restructuring

#### *3.1.1 Approving a restructuring plan*

As detailed above, the bankruptcy court will determine whether to approve a restructuring plan. Regulatory bodies such as the Environmental Protection Agency (EPA) may choose to object to a plan of reorganisation.

#### *3.1.2 Discretion to consider wider public interest concerns*

The bankruptcy court may be cognisant of certain wider public interest concerns during the course of a case administered under Chapter 11 but in general, this will not affect whether a plan of reorganisation will be approved. As noted, the requirements for approval (or confirmation) of a

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88 For example, if a worker suffers a prepetition injury, the accompanying workers compensation claims may be entitled to priority under the Bankruptcy Code. See, for example, 11 U.S.C. § 507(a)(4).

89 These releases are controversial because there is specific statutory authority only in the asbestos context. See, for example,11 U.S.C. § 524(g).

90 See, for example, *In re SunEdison, Inc.*, 576 B.R. 453 (Bankr. S.D.N.Y. 2017); *In re Indianapolis Downs, LLC*, 486 B.R. 286 (Bankr. D. Del. 2013).

91 See, for example, *In re Master Mortgage Investment Fund, Inc.*, 168 B.R. 930, 935 (Bankr. W.D. Mo. 1994). The most notable recent example is that of Purdue Pharma: see *In re Purdue Pharma, L.P.*, 635 B.R. 26 (S.D.N.Y. 2021). There, Purdue had manufactured opioids and sought to include non-consensual third-party releases for its owners. The District Court found that bankruptcy courts do not have statutory authority to grant non-consensual third-party releases for direct claims.

Chapter 11 plan are governed by specific statutory criteria that do not mention public interest concerns.

### *3.1.3 Influence by environmental protection authorities or environmental advocacy groups in a restructuring*

In general, parties in interest may be heard on any issue in a Chapter 11 case, including environmental protection authorities such as the EPA.[92] These authorities may also be critical in approving the transfer of licenses or permits pursuant to a sale.[93]

## 3.2 Social (S): influence by labour authorities, unions or employee / worker advocacy groups in a restructuring

### *3.2.1 Approving a restructuring plan*

As a party in interest, labour authorities and unions are able to make their voices heard during a Chapter 11 proceeding. They do not, however, have to approve a restructuring plan. Labour unions are often appointed as members of an official committee of unsecured creditors, and that committee typically has a highly influential role in the Chapter 11 case.

### *3.2.2 Discretion to consider wider public interest concerns*

Similar to the above, bankruptcy courts may consider wider public interest concerns, but this will generally not affect whether a plan of reorganisation is actually approved by the court.

### *3.2.3 Protection of employee rights*

There are several provisions of the Bankruptcy Code which protect employees' rights. First, claims for employee wages and contributions to employee benefit plans are given priority up to a set amount.[94]

Second, unlike most other contracts in bankruptcy, a debtor cannot unilaterally reject a collective bargaining agreement with a union.[95] Instead, a debtor must follow certain procedures, including the debtor's good faith negotiations with the union. If, and only if, the balance of the equities supports rejection of the collective bargaining agreement will it be approved. A similar procedure applies for retiree benefits.[96]

## 3.2 Governance (G): board / management conflicts addressed in a restructuring

In Chapter 11, there are several ways board and management conflicts are addressed. The first is that debtors may seek to implement a key employee incentive or retention plan, and that plan typically requires the approval of the bankruptcy court following a hearing and notice to creditors.[97] Courts, US Trustees and official committees are often hesitant to allow any additional payments to be made to management or other insiders and will closely scrutinise any such motion.

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92 For example, § 363(b)(2) contemplates review of potential sales for approval by the Department of Justice (Antitrust Division) and the Federal Trade Commission. Another example is that the transfer of broadcast licenses is subject to the approval of the Federal Communications Commission. *In re NextWave Personal Communications, Inc.*, 200 F.3d 43 (2d Cir. 1999).

93 As described above, Chapter 11 cases often result in a sale of substantially all of the debtor's assets. In those cases, the purchaser is often negotiating with regulatory authorities to ensure licenses and / or permits are transferred so that they can operate the business subsequent to the transfer. See, for example, *In re Bakalis*, 220 B.R. 525 (Bankr. E.D.N.Y. 1998) (noting that sale of interest in bank was subject to regulatory approval); *In re Energy Future Holdings Corp.*, 990 F.3d 728 (3d Cir. 2021) (generally discussing need for regulatory approval by potential purchaser).

94 11 U.S.C. §§ 507(a)(4), 507(a)(5), 507(a)(6).

95 *Idem,* § 1113.

96 *Idem,* § 1114.

97 *Idem,* § 503(c).

Second, in addition to retaining an independent CRO, which is discussed above, it is often best practice for a debtor to appoint independent members to its board of directors prior to commencing a Chapter 11 case (although this is not required). The debtor's board will often approve a plan term sheet and the final plan.

Third, because of the requirements of disclosure in the plan and disclosure statement, any potential self-dealing will be identified. Moreover, because it is not common for management or boards to have equity in a restructured company, the risk is lessened.

## 4. "Soft law" framework

### 4.1 Environmental (E): industry guidelines and / or best practices that are prescribed for the protection of the environment in a restructuring

There are no industry guidelines or best practices prescribed for the protection of the environment in Chapter 11 cases.

### 4.2 Social (S): industry guidelines and / or best practices that are prescribed for the protection of employee rights in a restructuring

There are no established guidelines to ensure the protection of employee rights in a restructuring. Generally, however, all participants in a case will seek to ensure that a business continues to operate as a going concern, which means employees will continue to be employed.

### 4.3 Governance (G): industry guidelines or codes of conduct relating to the avoidance of conflicts of interests that restructuring professionals are subject to

In a bankruptcy case under Chapter 11, a DIP may retain a number of professionals to assist with its restructuring, including counsel, accountants, investment bankers and others.[98] For these professionals to be retained, they must be considered "disinterested", meaning that they:

- are not a creditor, equity security holder or an insider of the debtor;
- were not an officer, director or employee of the debtor within two years of the petition date; or
- do not have an interest "materially adverse" to the debtor or any class of creditors or equity security holders.[99]

In short, this means that a professional cannot represent a debtor if it is a significant party in interest, even if the representation is wholly unrelated to the bankruptcy case and all parties consent.

Because the preparation stage before a bankruptcy case is filed is intensive, companies often incur substantial professional fees prior to the petition date. To ensure that the professionals are not considered creditors, they often receive retainers which can be offset against pre-petition amounts owed.

The key guiding principle for restructuring professionals looking to be retained in a Chapter 11 proceeding is broad disclosure, including ongoing disclosure related to any potential connections with the debtor, creditors or other parties in interest. A debtor will often employ conflicts counsel as well as main bankruptcy counsel to ensure there is no appearance of a potential conflict. Debtor's counsel may also seek to terminate representations of creditors, obtain conflict waivers and create ethical walls.

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[98] *Idem,* § 327; Fed. R. Bankr. P. 2014. Note that certain professionals, such as chief restructuring officers, are not considered "professionals" subject to retention under § 327 of the Bankruptcy Code. See, for example, *In re Nine West Holdings, Inc.*, 588 B.R. 678 (Bankr. S.D.N.Y 2018).

[99] 11 U.S.C. § 101(14).

## 5. ESG in financing

### 5.1 ESG-linked loans, bonds or investments

ESG-related loans, bonds and investments have become increasingly popular in the United States and globally.

Many banks and private equity funds are offering financing which, among other things, has interest rates subject to downward adjustments based on greenhouse gas emissions, procurement spend on sustainable suppliers and other ESG-related metrics.

### 5.2 Financial institutions (banks and funds) and their commitment to achieve ESG targets

A number of financial institutions in the United States, including Goldman Sachs, Morgan Stanley and Wells Fargo, have joined the United Nations Environment Programme (UNEP) Commitment to Climate Action. Organisations such as the Loan Syndications & Trading Association publish guidance on green loan principles, sustainability-linked loan principles, social loan principles and others.[100]

### 5.3 Promoting ESG by the central bank and regulators

The Federal Reserve, the central bank of the United States, is a member of the Network for Greening the Financial System (NGFS), which aims to mobilise the financial sector to address climate change and promote sustainability in finance. However, the Federal Reserve has stated that its goal is not to be a climate policymaker, so it is unclear to what extent the Federal Reserve may issue additional policies on a go-forward basis.

The US Securities and Exchange Commission has taken steps to promote ESG-related financing and created a Climate and ESG Task Force.[101] This task force is responsible for developing ESG initiatives and identifying ESG-related misconduct.

The US Environment Protection Agency and Department of Energy also each have programmes which offer grants and loans for projects related to environmental protection and sustainability.[102]

[100] https://www.lsta.org/app/uploads/2023/02/LSTA-Sustainable-Lending-Library-Feb-2023.pdf.
[101] https://www.sec.gov/securities-topics/enforcement-task-force-focused-climate-esg-issues.
[102] https://www.epa.gov/green-infrastructure/green-infrastructure-funding-opportunities.

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Association of Business Recovery Professionals - R3
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Business Recovery and Insolvency Practitioners Association of Nigeria
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Canadian Association of Insolvency and Restructuring Professionals
Commercial Law League of America (Bankruptcy and Insolvency Section)
Finnish Insolvency Law Association
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International Association of Insurance Receivers
International Women's Insolvency and Restructuring Confederation
Japanese Federation of Insolvency Professionals
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