Corporate Restructuring

The global reach of capital markets, financial difficulties in the eurozone and the multinational nature of many businesses and financial institutions have increased the importance of understanding legal, business and other risks associated with distressed investments in non-U.S. companies.

Distressed debt investors and funds have deepened their involvement in Europe — a trend we expect to continue. Those invested (or interested) in debt of financially distressed foreign companies should understand what restructuring laws and practices may apply, given the potential interplay between U.S. and international restructuring regimes and regulations.

In this section, we examine several issues of importance to investors in foreign companies, who have expanded their use of Chapter 15 of the U.S. Bankruptcy Code, which permits representatives of a foreign debtor to seek cooperation from U.S. bankruptcy courts in support of the foreign debtor's foreign insolvency proceedings. Additionally, European regulatory bodies increasingly are recommending "bail-in" as a method of resolving the affairs of large, systemically important financial institutions (SIFIs) facing insolvency; we weigh the various factors a U.S. court may consider when deciding whether to recognize a non-U.S. regulator's use of this method to convert a non-U.S. SIFI's debt to equity. Focusing on the continuing eurozone crisis, we canvas the potential legal, currency and business risks that might result from the departure of one or more member states. Finally, we discuss the criticism of the use of "exit consents" — a common tool in U.S. bond restructurings — in a recent English court decision.

We also discuss recent developments on two topics of continuing importance in U.S. bankruptcy cases: bankruptcy court jurisdiction to enter final orders in fraudulent transfer actions, and bankruptcy treatment of trademark licensee rights.

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Expanding Use of Chapter 15 Tests Its Protections and Limits

CONTRIBUTING PARTNERS

Van C. Durrer II / Los Angeles

David M. Turetsky / New York

Glenn S. Walter / Los Angeles

Foreign companies engaged in insolvency proceedings abroad and holding assets in the United States increasingly have employed Chapter 15 of the U.S. Bankruptcy Code to achieve their restructuring objectives and avoid the costs and time associated with plenary proceedings of a traditional Chapter 11 filing. As these companies and their creditors test this strategy's protections and limits, there have been significant legal developments in Chapter 15 practice. While foreign debtors have pushed the boundaries of the relief available to them, some creditors have objected and sought to impose more of the restrictions applicable in Chapter 11 on debtors in Chapter 15 cases. In the coming year, we anticipate that more foreign companies will test the Chapter 15 waters — and judicial and creditor scrutiny will continue to increase.

The Appeal of Chapter 15

Enacted in 2005 as part of the Bankruptcy Abuse Prevention and Consumer Protection Act, Chapter 15 incorporates most of the provisions of the United Nations' Model Law on Cross-Border Insolvency and acts as a mechanism by which foreign representatives may seek comity or cooperation from U.S. bankruptcy courts in support of foreign insolvency proceedings. A foreign representative is authorized in the foreign proceeding to administer the debtor's assets or generally to serve as a representative of the foreign proceeding in a Chapter 15 case. Courts have held, however, that judicial appointment of a foreign representative by a foreign court is not required for the foreign representative to be recognized in Chapter 15.[1]

Chapter 15 provisions confer broad powers upon a foreign representative, with only a few enumerated exceptions and catch-all protection provisions. Upon recognition of a foreign proceeding by a bankruptcy court, the foreign representative (which may be a debtor or an unaffiliated entity, such as a liquidator or a trustee appointed in the foreign proceeding) may pursue relief under certain provisions of the Bankruptcy Code that automatically are applicable to Chapter 15 proceedings, including Section 363 (which governs use and sale of debtor property outside the ordinary course of business). An asset sale in a Chapter 15 proceeding can be achieved either by requesting that the bankruptcy court recognize and enforce a sale order issued by a foreign court, or by motion for bankruptcy court approval of the sale under Section 363; the latter approach has become more prevalent.[2]

Foreign representatives are using another interesting tactic in the Chapter 15 context: employing a bankruptcy trustee's "avoidance" powers, despite express statutory exclusion of certain of the Bankruptcy Code's avoidance provisions (*e.g.*, Sections 522, 544, 545, 547, 548, 550 and 724(a)) from relief that is available to them under Section 1521.

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[1] *See Ad Hoc Grp. of Vitro Noteholders v. Vitro S.A.B. de D.V.*, Nos. 12-10542 *et al.*, 2012 WL 5935630, *11 (5th Cir. Nov. 28, 2012) (affirming recognition of foreign representatives appointed by board of directors of foreign debtor rather than by court order).

[2] *See, e.g.*, *In re Qimonda AG*, Case No. 09-14766 (RGM) (E.D. Va. March 10, 2010); *In re Cinram Int'l Inc.*, Case No. 12-11882-KJC (D. Del. July 25, 2012); *In re Elpida Memory, Inc.*, Case No. 12-10947-CSS (D. Del. Nov. 16, 2012).

Some courts have authorized foreign representatives to exercise avoidance powers (powers to unravel and undo transactions detrimental to creditors) that are granted to the representatives under the laws of the jurisdictions in which the relevant foreign proceedings are being pursued,[3] and also have permitted them to pursue avoidance actions under Section 553 of the Bankruptcy Code (relating to avoidance of setoffs) because Section 553 is not listed specifically among the excluded provisions in Section 1521.[4] The willingness of U.S. bankruptcy courts to allow foreign representatives in Chapter 15 cases to commence avoidance actions (previously thought to fall outside a foreign representative's authority) may reduce a primary motivation for foreign debtors to commence plenary Chapter 11 filings rather than ancillary Chapter 15 proceedings.

Increased Scrutiny

Creditors are taking more active roles in Chapter 15 proceedings, resulting in increased litigation and judicial scrutiny.

Emerging Creditor Strategies. A bondholder group has been very active in connection with both Elpida Memory's Chapter 15 case (pending in the U.S. Bankruptcy Court for the District of Delaware) and the company's primary foreign insolvency proceeding (pending in the Tokyo District Court). The bondholders in the *Elpida* Chapter 15 case petitioned the Delaware bankruptcy court to appoint a court representative to facilitate and coordinate cooperation with the Tokyo District Court. The bondholders alleged that Elpida's foreign representatives had failed to adequately apprise the bankruptcy court of the ongoing Tokyo proceedings, to the detriment of the debtors' estates and the interests of U.S. creditors. Although the bankruptcy court declined to appoint a representative, the bondholders' request illustrates that creditors and other constituents also are employing creative Chapter 15 strategies to protect their interests.

> "In 2013, we anticipate that more foreign companies will test the Chapter 15 waters — and judicial and creditor scrutiny will continue to increase."

Limits on Relief. Although Chapter 15 relief is broad, it is far from unlimited. In several recent decisions, U.S. bankruptcy courts have declined to grant requests for relief by foreign representatives. Courts have denied requested relief on the "narrow" exception contained in Section 1506 of the Bankruptcy Code, which provides that such requests may be denied if they would be "manifestly contrary to the public policy of the United States." For example, courts have applied Section 1506 to deny foreign representatives' requests to reject certain intellectual property licenses based on German law without providing the protections set forth in Section 365(n) of the Bankruptcy Code.[5]

Chapter 15 Risks. Relief requested by foreign representatives also may be denied based upon other sections of Chapter 15, even if a bankruptcy court does not directly rely on public policy considerations. A bankruptcy court may deny relief based on Section 1507 (listing factors for courts to consider in granting additional assistance) or Section 1522 (requiring that the interests of creditors and the debtor be sufficiently protected). In the *Vitro S.A.B.* case, the U.S. Court of Appeals for the Fifth Circuit relied upon Sections 1507 and 1522 to affirm a Texas bankruptcy court's decision to deny enforcement of a reorganization plan that had been approved by the Mexican court presiding over Vitro's primary reorganization proceeding. The *Vitro* plan provided for

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[3] *See In re Condor Ins. Ltd.*, 601 F.3d 319 (5th Cir. 2010).

[4] *See In re Awal Bank, BSC*, 455 B.R. 73 (Bankr. S.D.N.Y. 2011).

[5] *See In re Qimonda AG*, 433 B.R. 547 (E.D. Va. 2010); and to access electronic communications in the United States in potential violation of a debtor's due process rights (*In re Toft*, 453 B.R. 186 (Bankr. S.D.N.Y. 2011)).

recoveries to Vitro's existing shareholders, but failed to pay the company's creditors in full and released certain of Vitro's nondebtor subsidiaries from guarantee obligations, thereby extinguishing guarantee claims held by Vitro's bondholders against the nondebtor entities. Although the bankruptcy court denied enforcement of the *Vitro* plan, relying upon the Section 1506 public policy exception, the Fifth Circuit instead relied upon the limitations contained in Sections 1507 and 1522 to affirm, stating that "Vitro has failed to show the presence of the kind of comparable extraordinary circumstances that would make enforcement of such a plan possible in the United States."[6] The Fifth Circuit's holding in *Vitro* suggests that in order to protect creditors, U.S. bankruptcy courts may deny enforcement of relief ordered by a foreign court, even if the bankruptcy court does not rely on public policy considerations in denying such requested relief.

Looking Ahead

Given recent Chapter 15 developments, foreign companies considering this strategy as ancillary to a foreign insolvency proceeding should consider both the relief available to a foreign representative in its native proceeding and that which may be available under various chapters of the U.S. Bankruptcy Code. Foreign companies should seek strategic advice from experienced U.S. bankruptcy counsel about the extent (and limits) of available relief in Chapter 15 proceedings, how their U.S. creditors and other interested parties may react, and whether there are alternatives to accomplish a foreign company's restructuring objectives.

[6] *In re Vitro*, 2012 WL 5935360 at *23.

US Recognition of Non-US Regulatory 'Bail-In' Powers

CONTRIBUTING PARTNER

Mark A. McDermott / New York

The European Commission (EC), the Financial Stability Board (FSB), the Independent Commission on Banking (Vickers Commission) and other bodies have suggested "bail-in" as a method of resolving the affairs of large, systemically important financial institutions (SIFIs) facing insolvency or other crisis.[7] Thus far, only Spain and Switzerland have adopted restructuring laws contemplating this method,[8] but many more European nations are likely to do so in the coming years, as EU member states are required to achieve "substantial compliance" with the proposals by 2018.[9]

[7] Proposal for a Directive of the European Parliament and of the Council Establishing a Framework for the Recovery and Resolution of Credit Institutions and Investment Firms, COM (2012) 280 final, 2012/150 (COD) (June 6, 2012); Recovery and Resolution Planning: Making the Key Attributes Requirements Operational (Financial Stability Board), Nov. 2, 2012; Final Report and Recommendations of Independent Commission on Banking, Sept. 12, 2011.

[8] The Swiss bail-in statute is codified in the Swiss Banking Act, Arts. 28-32. The Spanish bail-in statute was enacted through Royal Decree-Law 24/2012 of Aug. 31, 2012.

[9] *See* Proposal for a Directive of the European Parliament and of the Council Establishing a Framework for the Recovery and Resolution of Credit Institutions and Investment Firms, at Art. 114, COM (2012) 280 final, 2012/150 (COD).

Bail-in allows the home regulator of a troubled SIFI to convert certain classes of debt of the SIFI into equity in the SIFI without the debt holders' consent. In theory, a troubled SIFI with dwindling capital and related capital ratios can, at the stroke of a pen, have its capital and related capital ratios significantly enhanced, thereby bolstering market confidence in its viability. In particular, while bail-in does not contemplate infusions of new equity, its implementation may stem the tide of margin calls that otherwise would be triggered by depleted capital.

> "One question raised by the bail-in approach is the extent to which courts outside a SIFI's home country may recognize and respect the remedy."

The operations of most SIFIs, however, are not limited to their home countries. Rather, they have global operations, and the debt issued by their holding companies or operating subsidiaries may be governed by U.S. law, including, in the case of bonds, the Trust Indenture Act (TIA);[10] may be held by investors outside the home country; and may contain venue provisions requiring that litigated disputes be adjudicated in courts outside a SIFI's home country. Accordingly, one question raised by the bail-in remedy is the extent to which courts outside a SIFI's home country may recognize and respect the remedy.

Outside the SIFI context, it has not been uncommon for holders of debt issued by companies subject to non-U.S. insolvency proceedings to attempt to collect on that debt in U.S. courts notwithstanding the pendency of such insolvency proceedings.[11]

There are two ways that matters concerning recognition of a non-U.S. restructuring proceeding can be brought before a U.S. court. First, a foreign representative of an entity subject to non-U.S. insolvency proceedings may file a petition under Chapter 15 of the U.S. Bankruptcy Code.[12] If the petition is granted and the foreign proceeding is recognized, then the non-U.S. debtor is entitled to many of the protections of the Bankruptcy Code, including the benefit of a stay against efforts by creditors to exercise remedies in the United States.[13] Chapter 15, however, may not be available to all SIFIs, as foreign banks are precluded from filing bankruptcy in the United States[14] (see "Expanding Use of Chapter 15 Tests Its Protections and Limits").

As an alternative to Chapter 15, U.S. creditors may attempt to enforce their rights under their debt instruments in U.S. courts. As noted above, debt instruments commonly have U.S. choice-of-law or venue provisions, and the TIA generally prohibits, outside of Chapter 11, nonconsensual modification of a bondholder's debt maturity and payment terms.[15] Accordingly, U.S. creditors may invoke TIA provisions to seek U.S. court assistance enforcing the original terms of debt that have been restructured in a foreign proceeding. As a general matter, U.S. courts dismiss such actions, based on principles of international comity, if the claimant fails to establish prejudice or injustice as a result of the non-U.S. insolvency proceeding.[16]

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[10] 15 U.S.C. §§ 77aaa-77bbbb.

[11] *See ABN Amro Bank N.V. v. Parmalat Finanziara S.p.A.*, 394 B.R. 696 (S.D.N.Y. 2008) (affirming permanent injunction against attempts to collect on debt that was restructured in Italian insolvency proceeding).

[12] *See* 11 U.S.C. §§ 1504, 1515.

[13] *See* 11 U.S.C. § 1520.

[14] *See* 11 U.S.C. § 1501(c).

[15] *See* 15 U.S.C. § 77ppp(b).

[16] *See Finanz AG Zurich v. Banco Economica*, 192 F.3d 240, 246 (2d Cir 1999).

There are limits, however, to how far a U.S. court will go in recognizing non-U.S. insolvency proceedings that are contrary to U.S. law. A U.S. court will recognize a non-U.S. insolvency proceeding that is unlike a U.S. insolvency proceeding, but the non-U.S. proceeding cannot violate basic notions of fairness. The U.S. Court of Appeals for the Fifth Circuit recently refused to recognize a Mexican insolvency proceeding of a parent holding company that purported to discharge the guarantee obligations of the company's U.S. nondebtor subsidiaries.[17] U.S. courts are split on the propriety of such releases and will enforce them only in extraordinary circumstances.[18] Because the Mexican debtor did not satisfy these U.S. standards, the Fifth Circuit refused to authorize the releases (see "Expanding Use of Chapter 15 Tests Its Protections and Limits").

There is no precedent for a U.S. court recognizing a non-U.S. regulator's unilateral bail-in conversion of a non-U.S. SIFI's debt to equity. If a non-U.S. SIFI were to face a crisis and its debt were in fact converted, U.S. holders of such debt could be expected to challenge the propriety of such bail-in in U.S. courts. While Chapter 11 allows U.S. debtors to reorganize their affairs, among other things, swapping debt for equity much like bail-in, Chapter 11 reorganization plans cannot be confirmed without some indicia of requisite creditor support.[19] Generally, impaired creditors are entitled to vote to accept (or reject) a Chapter 11 plan. The plan is not accepted by creditors of a class unless at least one-half of the creditors voting, holding at least two-thirds in dollar amount of claims, accept the plan.[20]

Chapter 11-like procedural and substantive protections for creditors are nonexistent in a regulatory bail-in. In bail-in, a non-U.S. SIFI's debt may be converted to equity without any advance notice to, input from or assent by holders of the debt instruments being converted to equity. Arguably, this is a fundamental lack of due process for creditors that is so contrary to U.S. policy that a U.S. court should not recognize the non-U.S. regulator's use of the bail-in remedy.

However, strong countervailing considerations suggest that a U.S. court faced with a challenge by a U.S. holder of debt bailed-in by a non-U.S. regulator may dismiss the creditor challenge and recognize the non-U.S. bail-in remedy. While Chapter 11 contemplates creditor due process and participation, there are two other significant U.S. insolvency regimes that, like bail-in, vest considerable authority in U.S. regulators to act swiftly, with little or no input from creditors or other stakeholders. The rationale behind these U.S. laws, like bail-in, ultimately is to protect the public interest.

One such law is the Federal Deposit Insurance Act (the FDIA).[21] Under the FDIA, a bank can be resolved by the Federal Deposit Insurance Corporation (FDIC) with no advance notice to or assent by the bank's creditors — including by transfers of selected assets to a purchaser or "bridge bank."[22] There is a very long history in the U.S. of banks being resolved rapidly — even over a weekend — under the FDIA. This regime, in short, vests great authority exclusively in the hands of the FDIC, much like bail-in.

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[17] *See* Judgment, *Ad Hoc Grp. of Vitro Noteholders v. Vitro SAB de CV*, No. 12-10542 (5th Cir. Nov. 28, 2012).

[18] *See, e.g., Deutsche Bank AG v. Metromedia Fiber Network, Inc.*, 416 F.3d 136, 141-43 (2d Cir. 2005) (describing extraordinary cases in which nondebtor releases are available).

[19] *See* 11 U.S.C. § 1129(a).

[20] *See* 11 U.S.C. § 1126.

[21] 12 U.S.C. § § 1811-1831aa.

[22] *See* 12 U.S.C. § 1821(n).

Likewise, Dodd-Frank contains a new insolvency regime exclusively for large, systemically important financial institutions.[23] Dodd-Frank was enacted in response to the 2008 financial crisis. Under this regime, known as the "Orderly Liquidation Authority," the FDIC may be appointed as receiver of a financial company with virtually the same powers as it has under the FDIA with respect to U.S. banks.[24] Again, such powers may be exercised with no advance notice to, or input from, creditors or other stakeholders. While such powers do not explicitly include the authority to unilaterally convert debt to equity, such powers are implicit, *e.g.*, if the FDIC transfers the institution to a bridge bank, it can later distribute equity in the bridge bank to holders of the bank's debt.

Accordingly, U.S. courts might ultimately conclude that foreign regulatory bail-in of an insolvent foreign SIFI is consistent with U.S. law and public policy. Indeed, bail-in is one of many pieces of legislation (including Dodd-Frank) enacted by numerous countries following the financial crisis that vests home regulators with the significant, centralized authority to act swiftly to avoid or mitigate a national, economic catastrophe. Accordingly, a U.S. court facing a challenge to non-U.S. bail-in likely would be very reluctant to second-guess a determination made by duly constituted, non-U.S. regulatory authorities, that such authorities needed to implement extraordinary bail-in measures in an effort to maintain economic and social stability.

[23] Pub. L. 111-203 (codified as amended in scattered sections of U.S.C.).
[24] *See* 12 U.S.C. § 5390.

Circuit Splits Emerge Regarding Trademark Licensees' Bankruptcy Rights

CONTRIBUTING PARTNERS

Mark S. Chehi / Wilmington

Jose A. Esteves / New York

Ron E. Meisler / Chicago

ASSOCIATE

Carl T. Tullson / Chicago

The U.S. Bankruptcy Code generally protects intellectual property licensees when a licensor files for bankruptcy. In particular, Section 365(n) provides that if the debtor is the licensor under a patent or copyright license that is "rejected" in bankruptcy, the licensee has the option either to retain its rights as they existed on the bankruptcy petition date and continue its performance, or to treat the license as terminated. *See* 11 U.S.C. § 365(n). Section 365(n) was enacted in response to the U.S. Court of Appeals for the Fourth Circuit's decision in *Lubrizol Enterprises, Inc. v. Richmond Metal Finishers, Inc.*, 756 F.2d 1043 (4th Cir. 1985), which held that a licensee of patents, copyrights and trademarks lost its license rights when its license was rejected in bankruptcy.

Although Section 365(n) was enacted to avoid the holding in *Lubrizol* and to protect businesses that depend on licensed intellectual property rights, trademark licensees historically have not benefited from these protections because, on its face, Section 365(n) does not apply to trademark licenses. Accordingly, in the Fourth Circuit at least, even after the enactment of Section 365(n), trademark license agreements that are "executory" may be rejected pursuant to Section 365 with the same adverse results for licensees as in *Lubrizol*: A licensee whose trademark is rejected in bankruptcy can be stripped of its rights to use a licensed trademark.

However, in *Sunbeam Products, Inc. v. Chicago American Manufacturing, LLC*, 686 F.3d 372 (7th Cir. 2012), *cert. denied* 2012 WL 4812510 (U.S. 2012) (to be published in S. Ct.), the U.S. Court of Appeals for the Seventh Circuit reached a different conclusion, creating a split with the Fourth Circuit's decision in *Lubrizol* regarding the rights of a trademark licensee whose trademark license was rejected in bankruptcy.[25] Prior to the *Sunbeam* decision, if a trademark license was rejected in bankruptcy, there was considerable risk that the licensee would lose its right to use the licensed trademark, absent entry into a new licensing agreement. In *Sunbeam*, the Seventh Circuit held that a trademark licensee may continue to use its licensed trademark following the debtor-licensor's rejection of the trademark license. Accordingly, since *Sunbeam*, in the Seventh Circuit at least, when their licenses are rejected, trademark licensees have protections comparable to statutory protections expressly granted under Section 365(n) to licensees of other forms of intellectual property.

Importantly, Section 365(n) protections are relevant and available only if an intellectual property license agreement is "executory" and therefore susceptible to "rejection" by a debtor under Section 365 of the Bankruptcy Code. Accordingly, a trademark licensee that seeks to avoid bankruptcy rejection of a license will want to show that its license terms are non-executory (within the meaning of Section 365), such that the license is not capable of rejection. Likewise, parties negotiating terms of trademark license agreements should consider whether prospective terms will (or will not) result in an "executory" license agreement that is susceptible to rejection in bankruptcy. In this regard, perpetual, royalty-free, exclusive trademark licenses may be non-executory, and the U.S. Court of Appeals for the Third Circuit has so held. *In re Exide Techs.*, 607 F.3d 957 (3d Cir. 2010) (holding that a perpetual, royalty-free, exclusive trademark license agreement was not an executory contract that can be rejected in bankruptcy). Prospective trademark licensees may want to negotiate for such perpetual, royalty-free, exclusive terms to reduce possible risk of future bankruptcy rejection and loss of their trademark use rights.

"Prior to the *Sunbeam* decision, if a trademark license was rejected in bankruptcy, there was considerable risk that the licensee would lose its right to use the licensed trademark."

However, not all federal circuit courts agree that perpetual, royalty-free, exclusive trademark licenses are non-executory. In *Lewis Brothers Bakeries Inc. v. Interstate Brands Corp.* (In re Interstate Bakeries Corp.), 690 F.3d 1069 (8th Cir. 2012),[26] the U.S. Court of Appeals for the Eighth Circuit split with the Third Circuit by holding that a perpetual, royalty-free, exclusive trademark license agreement was executory and subject to rejection in bankruptcy.

This circuit-level split of views about whether perpetual, royalty-free and exclusive trademark license agreements are (or are not) executory agreements susceptible to bankruptcy rejection heightens the importance of the Seventh Circuit's Sunbeam ruling in favor of the rights of trademark licensees whose licenses ultimately are rejected in bankruptcy.

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[25] *See* "Seventh Circuit Rules on Trademark Licensees' Bankruptcy Rights" (July 27, 2012), *available at* http://www.skadden.com/insights/seventh-circuit-rules-trademark-licensees-bankruptcy-rights.

[26] *See* "Rejection of Perpetual, Royalty-Free, Exclusive Trademark License Permitted by Eighth Circuit Ruling: *Lewis Brothers Bakeries Inc. v. Interstate Brands Corp.*" (Oct. 1, 2012), *available at* http://www.skadden.com/insights/rejection-perpetual-royalty-free-exclusive-trademark-license-permitted-eighth-circuit-rulin.

Ninth Circuit Restricts Bankruptcy Courts' Ability to Adjudicate Fraudulent Transfer Actions

CONTRIBUTING PARTNER

Mark A. McDermott / New York

It's been more than 18 months since the U.S. Supreme Court issued its controversial decision in *Stern v. Marshall*.[27] The Court ruled in *Stern* that a bankruptcy judge could not constitutionally enter a final ruling on a debtor's state law "core" counterclaim against a litigant that filed a proof of claim against the debtor's bankruptcy estate, unless the debtor's counterclaim "stems from the bankruptcy itself" or adjudication of the debtor's counterclaim "necessarily" would resolve the creditor's proof of claim.

We previously wrote that the Supreme Court has rendered other rulings that, taken together with *Stern*, suggest bankruptcy judges' authority to enter final rulings in other categories of more significant core proceedings also may be in doubt.[28] In particular, in *Granfinanciera, S.A. v. Nordberg*, the Court ruled that defendants in fraudulent transfer litigation have a constitutional right to a jury trial, and Congress, therefore, cannot assign adjudication of such litigation to a "non-Article III court," *i.e.*, a court other than a federal district court vested with the authority to conduct jury trials, so long as the defendants have not appeared in the bankruptcy proceedings by submitting a proof claim.

As we previously stated, a possible implication of the reasoning in *Granfinanciera*, when combined with *Stern*'s ruling that bankruptcy judges have no constitutional authority to enter final rulings on a debtor's state law counterclaim, is that bankruptcy judges also may be foreclosed from entering final orders in fraudulent transfer actions, at least where the defendants have not filed proofs of claim. The Ninth Circuit Court of Appeals in *Executive Benefits Ins. Agency, Inc. v. Arkison*[29] followed this logic in recently ruling that bankruptcy judges are in fact precluded from entering final judgments in such actions, despite the fact the Bankruptcy Code classifies such actions as "core" proceedings that bankruptcy judges may finally adjudicate.

The implication of *Bellingham* is bankruptcy judges no longer can enter any type of ruling on fraudulent transfer actions at all. The reason is that the Bankruptcy Code creates only two types of bankruptcy proceedings: "core" proceedings and "noncore" proceedings. Whereas bankruptcy judges may enter final rulings in core proceedings, they only may enter proposed findings of fact and conclusions of law in noncore proceedings for further review by the district court, unless the parties consent to entry of final orders. As noted above, the Bankruptcy Code classifies fraudulent transfer actions as core proceedings. If, as the Ninth Circuit ruled, bankruptcy judges cannot enter final orders in such actions, then there arguably is no statutory basis for a judge to enter proposed findings in such actions, as that mechanism is only available for noncore matters — not core, fraudulent transfer actions.

However, the Ninth Circuit took a contrary view. It filled the statutory "gap" created by its ruling — *i.e.*, a "gap" that leaves fraudulent transfer actions unable to be adjudicated by bankruptcy judges in any fashion at all — by concluding that bankruptcy judges effectively

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[27] 131 S. Ct. 2594, rehearing denied 132 S.Ct.56 (2011).

[28] *See* "Chapter 11 Litigation Strategies After the Supreme Court's Decision in *Stern v. Marshall*" (2011), *available at* http://www.skadden.com/insights/chapter-11-litigation-strategies-after-supreme-court%27s-decision-istern-v-marshalli.

[29] No. 11-35162, 2012 WL 6013836 (9th Cir. Dec. 4, 2012).

> "The implication of *Bellingham* is that bankruptcy judges no longer can enter any type of ruling on fraudulent transfer actions at all."

may treat fraudulent transfer actions as noncore proceedings and, therefore, may render proposed findings of fact and conclusions of law in such proceedings for further review by the district court. This position is consistent with the rulings of numerous lower courts post-*Stern*,[30] though it conflicts with dictum from the Seventh Circuit.[31]

Although the Bankruptcy Code provides that parties nonetheless may consent to entry of final orders by bankruptcy judges in noncore matters, one of the controversies created by *Stern* is the type of consent necessary to evidence a party's agreement to entry of final orders. The Supreme Court held that a creditor's submission to a bankruptcy court's jurisdiction by filing a proof of claim did not constitute consent to adjudication of a separate litigation against the creditor.

The Ninth Circuit addressed this issue in its *Bellingham* decision. As an initial matter, the court noted there are certain bankruptcy rules that could be construed as requiring express consent, *i.e.*, that a litigant cannot impliedly waive its right to be heard by an Article III court, and thereby be deemed to have impliedly consented to final adjudication by a bankruptcy judge.[32] The Ninth Circuit concluded, however, that notwithstanding these rules, a litigant could impliedly waive such a right and thereby be deemed to have consented to final adjudication.

In doing so, the Ninth Circuit did not attempt to formulate a rule by which to determine implied waiver/consent. It concluded, however, that based on the facts of the case, the defendants "fully litigated the fraudulent conveyance action before the bankruptcy court and the district court, without so much as a peep about Article III." To allow a litigant to argue for the first time on appeal that the bankruptcy judge had no authority to finally adjudicate the matter would be to allow litigants to improperly sandbag the court.

Many other courts also have concluded that litigants may impliedly consent to final adjudication of fraudulent transfer actions.[33] However, the U.S. Court of Appeals for the Sixth Circuit has suggested otherwise.[34] In an effort to bring clarity to the issue of consent, certain courts have entered standing orders requiring that parties to bankruptcy adversary proceedings state explicitly whether or not they consent to final adjudication to the various claims asserted in the proceeding or, alternatively, whether they will seek withdrawal of the claims to the district court.[35]

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[30] *See, e.g., Retired Partners of Coudert Bros. Trust v. Baker & Mackenzie LLP* (*In re Coudert Brothers LLP*) No, 11-2785(cm) 2011 U.S. Dist. LEXIS 110425 (S.D.N.Y. Sept. 23, 2011); *In re Crescent Resources*, 2011 WL 3022554 (Bankr. W.D. Tex. July 22, 2011); *Sanders v. Muhs* (*In re Muhs*), No. 09-10564, 2011 WL 3421546 (Bankr. S.D. Tex. Aug. 2, 2011); *Paloain v. Am. Express Co.*, No. 11 C5360, 2011 U.S. Dist. LEXIS 99804 (N.D. Ill. Sept. 1, 2011).

[31] *In re Ortiz v. Aurora Health Care, Inc.*, 665 F.3d 906 (7th Cir. 2001).

[32] *See* Fed. R. Bankr. P. 7008 and 7012(b).

[33] *See In re Coudert Bros. LLP*, No. 11-2785, 2011 WL 5593147 *9 (S.D.N.Y. Sept. 23, 2011) ("There is an alternative basis on which Judge Drain might have possessed final adjudicative authority over the Claims, based on the parties' consent."); *In re Am. Hous. Found.*, No. 09-20232, 2012 WL 443967 *11 (Bankr. N.D. Tex. 2012); *Ardi Ltd. Partnership v. River Entertainment Co.*, 467 B.R. 808, 822–24 (Bankr. W.D. Pa. 2012); *cf. Burtch v. Huston (In re USDigital, Inc.)*, 461 B.R. 276, 279 (Bankr. D. Del. 2011) (noting lack of clarity).

[34] *Waldman v. Stone*, 698 F.3d 910, 918 (6th Cir. 2012) ("Waldman's [constitutional] objection … implicates not only his personal rights, but also the structural principle advanced by Article III. And that principle is not Waldman's to waive.").

[35] *See, e.g.*, Bankr. S.D.N.Y. R. 7008-1 (effective Apr. 16, 2012).

The Ninth Circuit's decision is important because it is the first appellate court ruling on fraudulent transfer issues since *Stern*. In many respects, however, it is not a surprise, since all arrows were pointing in this direction.

The notion still is something of a shock to the system, however, as bankruptcy practitioners have long understood fraudulent transfer actions to be the proper domain of bankruptcy judges in all respects. They still will be, so long as parties consent. Yet there is little question that many more fraudulent transfer actions will now become the province of the district courts; that litigants may face strategic choices that may lead to charges of forum shopping; and that absent clear rules regarding consent, parties can be expected to engage in litigation posturing if rulings do not go their way.

Forewarned Is Forearmed: Adapting for Business in a Eurozone Crisis

CONTRIBUTING PARTNERS

Chris Mallon / London

Dominic McCahill / London

The financial difficulties in the eurozone have been widely reported, in particular the weak position of peripheral sovereigns such as Greece, Spain, Portugal and Italy. While discussion of these issues may have taken on a less urgent tone, the risk remains that the eurozone may experience catastrophic events, potentially including one or more member states leaving the currency zone.

In addition to the extreme stress on sovereigns, a severe corporate credit crunch likely will affect the eurozone in the next few years. It has been estimated that between 2012 and 2015, $1.3 trillion of eurozone corporate debt will need to be refinanced, including $325 billion of speculative-grade, nonfinancial corporate debt. Moreover, a recent IMF report predicted that European financial institutions will experience deleveraging of between €2 trillion and €4 trillion before the end of 2013.

Legal Risk

Redenomination risk arising from the possible departure of one or more states from the eurozone, or the breakup of the currency union, remains the foremost legal issue.

The *lex monetae* principle provides that when a debt is expressed in a particular currency, there is an implicit choice that the law of that currency's country will determine what that money is. As the euro is a multinational currency, there is no one jurisdiction to which the *lex monetae* can refer. However, if a eurozone state were to leave the single currency, it is likely that contracts governed by its domestic laws, as well as domestic obligations of that state's government and accounts with domestic banks, would be redenominated by emergency legislation to a new legal tender. In response, it is likely that other eurozone states also would enact emergency legislation relating to currency and payment obligations.

Currency Risk

If a periphery state were to leave the euro, its new currency likely would devalue rapidly against the euro, which over time may strengthen considerably against other currencies,

including the U.S. dollar. As the international obligations of the government of the periphery state leaving the euro probably would be unaffected by any redenomination, such a periphery state is likely to undergo a default caused by currency devaluation.

Business Risk

The business consequences of a departing state are hard to predict and could range from manageable to disastrous. If a eurozone state were to leave, its government likely would enact oppressive controls on the movement of currency and goods. Such measures may be met by equivalent measures in other EU states and likely would lead to further negative impacts of currency changes. Businesses can take practical steps to reduce potential risks, including:

- Considering the governing law of significant contracts in light of redenomination risk. For example, assuming that contractual obligations governed by English law and denominated in euros will continue to be payable in that form despite the departure of a state, drafting or amending contracts so they are governed by English law may mitigate redenomination risk.
- Achieving greater certainty for euro-denominated contracts by defining euro with reference to the currency in circulation and accepted as legal tender in a specific eurozone state. For example, a U.S. company contracting with a Greek company may wish to avoid receiving payment in a devalued currency following a Greek exit from the euro — and this may be achieved by defining euro as the currency in circulation and accepted as legal tender in Germany.
- Identifying and evaluating other contractual clauses that may be implicated as a result of events in the eurozone. Particular care should be taken when drafting clauses governing matters such as place of payment, material adverse change, *force majeure*, the impact of rating downgrades, and the impact of market disruption on pricing, termination rights, cross-default, netting and setoff.
- Examining supply chains as far back as possible to identify any potential vulnerabilities. If a state leaves the eurozone, there is a likelihood of supply chain disruption, and this risk can be addressed by building up precautionary inventories of supplies and establishing or identifying alternative sources.
- Assessing the health of business-critical banks both within and outside the eurozone. Severe stress in the eurozone may put banks at risk and diminish their ability and willingness to lend.
- Sweeping cash held in eurozone bank accounts on a regular basis, in particular accounts in those states most at risk of leaving.
- Matching assets and liabilities on a national basis within the eurozone also may mitigate the effects of a redenomination.
- Considering the effect of a redenomination on a business' treasury functions, cash management systems, invoicing and billing, cash reserves and financial management policy also should be focuses of euro risk reduction efforts.

> "The eurozone's shifting political context and continuing legal uncertainty are factors that must be considered in all transactions."

The eurozone's shifting political context and continuing legal uncertainty are factors that must be considered in all transactions. Companies should weigh practical measures to mitigate what could be extraordinary consequences resulting from any potential breakup of the eurozone. An ounce of prevention may have more worth than ever.

Negative Outlook for Exit Consents Under English Law

CONTRIBUTING PARTNER

Dominic McCahill / London

An exit consent is a fairly standard tool in bond restructurings in the United States. An issuer makes offers to bondholders to exchange their bonds for new bonds on different terms, which provide that holders who accept the offer (exiting bondholders) agree to vote in favor of (consent to) changing the terms of the existing bonds. Incorporating such "exit consents" into an exchange offer incentivizes bondholders to accept the exchange offer because, if a sufficient majority of acceptances are received, the exchange offer will be consummated and any minority of nonaccepting bondholders will be left with significantly diminished rights under the modified terms of the pre-existing bonds that they continue to hold.

The use of exit consents in the restructuring of bonds governed by English law has been the subject of recent critical analysis by the English court in *Assénagon Asset Management S.A. v. Irish Bank Resolution Corporation (formerly Anglo Irish Bank Corporation Limited)* [2012] EWHC 2090 (Ch). This case involved the Anglo Irish Bank, formerly Ireland's third-largest bank, which focused on commercial property lending. As a result of the financial crisis, it required very significant support by the Irish state and was nationalized in January 2009. In the months that followed, the Irish government provided nearly €23 billion in capital. Assénagon, a hedge fund, held €17 million in subordinated floating rate notes, which were due to mature in 2017.

The Anglo Irish Bank proposed an exchange offer to the holders of its notes. Under the terms of the exchange offer, the holder of a subordinated note would receive a new unsubordinated note with a face value of 20 cents for every one euro under the original note. The exchange offer provided that the terms of existing notes that were not exchanged would be altered by exiting noteholder consents to an extraordinary resolution of the rights and value of the pre-existing notes. Under the proposal, a note with a face value of €1,000 subsequently would have a value of only €0.01. Assénagon did not participate in the proposed exchange offer, and its €17 million of notes were converted to a new note with a face value of only €170. For Assénagon and other holders who did not participate in the exchange, the value in their notes was destroyed.[36]

Assénagon sought a declaration in the English court that the resolution reducing the value of its nonexchanged notes was invalid. The issue of most interest addressed in the *Anglo Irish Bank* case is whether the resolution of nonexchanging noteholder rights constituted an abuse of the power of the voting majority or, in other words, whether

[36] In the U.S. there is a general prohibition on the modification of payment terms without unanimous consent of all holders under Section 316 of the Trust Indenture Act of 1939.

it can be lawful for the majority to lend its aid to the coercion of a minority by voting for a resolution that expropriates the minority's rights under their bonds for a nominal consideration. Mr. Justice Briggs answered in the negative. The judge described the exit consent as:

> quite simply, a coercive threat which the issuer invites the majority to levy against the minority, based upon the fear of any individual member of the class that, by rejecting the exchange and voting against the resolution, he (or it) will be left out in the cold. … Putting it as succinctly as I can, oppression of a minority is of the essence of exit consents of this kind.

While the facts of the *Anglo Irish Bank* case are extreme and may well be distinguishable in future cases, the judge expressed strongly critical views on the use of exit consents as a restructuring tool. The *Anglo Irish Bank* decision is under appeal, and the outcome will be eagerly awaited by restructuring professionals in Europe and elsewhere where English law is deployed in corporate finance.