INSIGHT

Asia-Pacific Restructuring Review 2021

Edited by

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Preface

Welcome to the *Asia-Pacific Restructuring Review*, a *Global Restructuring Review* special report.

GRR is the online home for all professionals who specialise in high-stakes restructuring and insolvency. We tell them everything they need to know about all that matters.

Throughout the year, *GRR* delivers daily news, surveys and features; organises the liveliest events ('GRR Live') – covid-19 allowing; and provides our readers with innovative tools and know-how products.

In addition, assisted by external contributors, we curate a range of comprehensive regional reviews – online and in print – that go deeper into developments than the exigencies of journalism allow.

The *Asia-Pacific Restructuring Review 2021*, which you are reading, is part of that series.

It contains the insight and thought leadership of 21 pre-eminent figures in the region.

Across eight chapters and 120 pages, it can be described as a blend of invaluable retrospective, handy primer and crystal ball. All our contributors are vetted for their standing and knowledge before being invited to take part.

Together, they capture and interpret the most substantial recent international restructuring developments from the past 12 months, complete with footnotes and relevant statistics.

This edition covers Australia, China (for the first time), Hong Kong, India, Indonesia, Japan, Singapore and South Korea.

Among the gems it contains:

- a behind-the-scenes look at three recent Australian restructurings;
- the latest on China's insolvency regime – including an answer to the question of whether arbitration clauses remain valid after bankruptcy;
- helpful reviews of key recent cases in Hong Kong and India;
- a note of caution for foreign lenders in Indonesia – if certain debtor-friendly reforms go through (with helpful graphics); and
- news that Japan has yet to make any covid-specific adjustments to its insolvency regime.

And much, much more.

If you have any suggestions for future editions, or want to take part in this annual project, we would be delighted to hear from you. Please write to insight@globalrestructuringreview.com.

Our sincerest thanks to all our contributors, but particularly to the remarkable Look Chan Ho who edited this volume. Thank you all. It's a blue-ribbon edition.

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London
September 2020

Australian Restructuring: Legislation, Transactions and Cases

Paul Apáthy and Angus Dick
Herbert Smith Freehills

In summary

This article covers major legislative developments, restructuring transactions and case law in Australia since August 2019. Herbert Smith Freehills discusses these developments with a view to identifying key trends, such as the Court's commercial approach to both schemes of arrangement, and the challenges the pandemic has posed to insolvency processes in Australia.

Discussion points

- Covid-19 temporary law reforms
- New laws to address phoenixing activity
- Major restructuring transactions in the Australian market
- Cross-border cooperation
- The courts adapting to the challenges posed by the covid-19 pandemic
- Clarification regarding circulating security interests

Referenced in this article

- Coronavirus Economic Response Package Omnibus Act 2020 (Cth)
- Treasury Laws Amendment (Combating Illegal Phoenixing) Act 2019 (Cth)
- *Re Tiger Resources Limited*
- *Re Wollongong Coal Limited and Jindal Steel & Coal Australia Pty Ltd*
- *Re Halifax Investment Services Pty Ltd (in liq)*
- *Re CBCH Group Pty Ltd*
- *Re RCR Tomlinson Ltd*

Introduction

Restructuring activity in Australia over 2019 was relatively subdued given continued relatively benign economic conditions. However, the climate changed markedly in March 2020 with the onset of the global covid-19 crisis.

The severity of the economic impact of the covid-19 pandemic was ameliorated by various temporary measures introduced by the federal government, including:

- the 'job-keeper' government financial support provided to businesses, with the aim of encouraging them to keep workers;
- a mandatory code of conduct introduced to require landlords and tenants of small and medium-sized enterprises to negotiate in good faith a proportionate sharing of the financial impact of the crisis between them;
- encouragement of the major banks to grant deferrals and other support to customers impacted by the crisis; and
- various temporary changes to insolvency laws aimed at reducing the number of formal insolvencies triggered by the crisis.

The strength of these temporary measures is demonstrated by the fact that despite Australia suffering the largest negative economic shock since the great recession, to date 2020 has seen fewer formal insolvencies than in the same period of the previous year.[1]

While government support has been a lifeline for many Australian businesses during the pandemic, it is unclear how long this will continue; a number of measures are currently scheduled to end or wind back from 25 September 2020. Even with this support in place, the crisis has caused or further exacerbated the financial distress of a number of significant Australian companies. As a result, several major restructurings are ongoing at the time of writing, including those of Virgin Australia and Speedcast.

In this year's review, we discuss the key developments in the Australian restructuring and insolvency market over the past year, including:

- the temporary changes in response to the pandemic and the permanent anti-phoenixing legislative changes;
- the most notable restructurings completed in the last year; and
- a number of important case law developments during this period.

1 Australian Securities and Investments Commission, *Insolvency statistics – Series 1 Companies entering external administration* (report, August 2020): https://asic.gov.au/regulatory-resources/find-a-document/statistics/insolvency-statistics/insolvency-statistics-series-1-companies-entering-external-administration/.

Legislative reforms

Temporary covid-19 changes

Similarly to steps taken in other jurisdictions, the Australian government has passed various temporary amendments to Australian insolvency law, with the aim of protecting viable businesses from the stresses caused by the pandemic and associated lockdown. These amendments were part of the broad package of relief contained in the Coronavirus Economic Response Package Omnibus Act 2020 (Cth) (the Coronavirus Act).

The two main changes to corporate insolvency law in the Coronavirus Act came into effect on 25 March 2020 (the effective date), with the aim of preventing unnecessary insolvencies caused by temporary illiquidity.[2] These changes provided for the:

- increasing of the minimum debt amount and the time frame to respond where a creditor seeks to wind up a company pursuant to a statutory demand; and
- relieving of directors on insolvent trading liability in respect of debts incurred in the ordinary course of the company's business.

Both of these temporary changes were introduced for an initial period of six months commencing on the effective date, but the Australian government has recently announced their intention to extend this period until 31 December 2020 (the temporary period).[3]

Statutory demands

Statutory demands are used under Australian law to create a presumption of insolvency against a company that fails to respond to it. Creditors can issue a statutory demand to businesses who fail to pay their debts when they fall due. Once issued to a debtor, a statutory demand must be either complied with or successfully challenged by the company. If the statutory demand is not addressed, the company is presumed to be insolvent,[4] and a creditor can apply to have the company wound up.[5]

The Coronavirus Act increases the minimum threshold for debts capable of supporting a statutory demand from A$2,000 to A$20,000 during the temporary period. In addition, if a statutory demand is issued during the period, the company will have six months to respond to that demand, a significant increase from the current 21-day period.[6]

2 Explanatory Memoranda, Coronavirus Economic Response Package Omnibus Bill 2020 (Cth), [12.2].

3 Corporations Act 2001 (Cth), section 588GAA; Corporations Regulations 2001 (Cth), r 5.4.01AA; The Hon Josh Frydenberg MP and the Hon Christian Porter MP 'Extension of temporary relief for financially distressed businesses' (Media Release, 7 September 2020).

4 Corporations Act 2001 (n 3), section 459C(2)(a).

5 ibid, sections 459A and 459P.

6 ibid, section 459E.

Insolvent trading

The Coronavirus Act has introduced a new and additional temporary 'safe harbour', intended to supplement the existing safe harbour protections from insolvent trading liability for company directors.[7]

Under the temporary safe harbour, a company director will be exempt from liability for insolvent trading where a debt is incurred:

- in the ordinary course of the company's business;
- during the temporary period; and
- before any appointment of an administrator or liquidator during the new safe harbour period.

Where a subsidiary's debts are covered by this temporary safe harbour, a holding company of that subsidiary will also be eligible for a corresponding harbour in respect of the debts incurred by the insolvent subsidiary,[8] provided that the holding company takes reasonable steps to ensure that the temporary safe harbour applies to each director of the subsidiary and to the debts incurred.

While the temporary safe harbour is of broader application than the existing safe harbour regime under Australian law, the existing protections are of continued relevance. To attract the new safe harbour, a debt must be incurred within the ordinary course of business. The explanatory memorandum of the Coronavirus Act clarifies that a debt will be taken to have been incurred in the ordinary course of business if it is 'necessary to facilitate the continuation of the business during the six month period that begins on commencement of the subparagraph'. This could be an important gloss on the concept of the 'ordinary course of business' for exceptional transactions, such as rescue financings.

Phoenix amendments to the Corporations Act

The Australia chapter in the *Asia-Pacific Restructuring Review 2020* noted the introduction of the Treasury Laws Amendment (Combating Illegal Phoenixing) Bill 2019. The Bill was introduced to address 'phoenixing', a practice whereby company directors seek to avoid paying creditors by transferring a company's assets to a new company controlled by the same owners (with the first mentioned company then entering formal insolvency with no assets available to meet creditor claims).

7 Herbert Smith Freehills, 'Australia' in Global Restructuring Review, *Asia Pacific Restructuring Review 2019*, 13; Paul Apáthy et al, 'Australia's New Ipso Facto Regime is Now Live: Are Your Rights Affected?' Herbert Smith Freehills (Blog Post, 3 July 2018): https://www.herbertsmithfreehills.com/latest-thinking/australia%E2%80%99s-new-ipso-facto-regime-is-now-live-are-your-contractual-rights-affected.

8 In Australia, holding companies may in certain circumstances be liable for the insolvent trading of their subsidiaries (see the Corporations Act (n 3), section 588V).

The Treasury Laws Amendment (Combating Illegal Phoenixing) Act 2019 (Cth) (the Phoenixing Act) included a number of important modifications to the Corporations Act 2001 (Cth) (the Corporations Act) that came into effect on 18 February 2020, including:[9]

- the introduction of a new type of voidable transaction, known as a 'creditor-defeating disposition', together with various criminal and civil liability provisions applicable to those who engage in or facilitate those dispositions; and
- measures designed to prohibit backdating director resignations and prevent companies being left without directors.

Creditor-defeating dispositions

Under the new section 588FDB of the Corporations Act, a disposition of company property is a 'creditor-defeating disposition' if:

- the consideration payable to the company was less than the lesser of the market value of the property and the best price reasonably obtainable for the property having regard to the circumstances; and
- the disposition had the effect of preventing, hindering or significantly delaying the property becoming available to meet the claims of creditors in the winding up of the company.

A creditor-defeating disposition may be voidable in the winding up of a company if:[10]

- the transaction was entered into, or an act was done for the purposes of giving effect to it, during the 12 months prior to the administration or liquidation of the company; and
- the company was insolvent at the time of that transaction or act, the company became insolvent because of that transaction or act, or an external administration of the company occurs as a direct or indirect result of that transaction or act.

A creditor-defeating disposition may become voidable either upon a court order, or by an administrative order made by the Australian Securities and Investments Commission (ASIC), which is the Australian companies regulator.[11] There are certain exemptions and good faith defences available both to parties to the transaction and third parties.[12]

This is the first time that ASIC has been granted the ability to exercise avoidance powers without a court order. There has been debate on whether this is appropriate or even constitutional. The explanatory memorandum to the Phoenixing Act explains that the purpose of granting ASIC this power was to ensure that suspicious transactions can be investigated even where the liquidator has insufficient funds to cover the cost of court action or to allow ASIC

9 Explanatory Memorandum, Treasury Laws Amendment (Combating Illegal Phoenixing) Bill 2019 (Cth) [1.9] (the Phoenixing EM).

10 Corporations Act (n 3), section 588FE(6A). There are exceptions where the transaction was entered into or the act was done under a scheme or arrangement or a deed of company arrangement, or by an administrator, liquidator or provisional liquidator.

11 Corporations Act (n 3), section 588FGAA(3).

12 ibid, sections 588FE(6B)(c) and 588FG.

to intervene where the liquidator is not fulfilling its obligation to recover company property; for example, where the liquidator is complicit in the illegal phoenix activity of a company director.[13] Failing to comply with an administrative order made by ASIC is an offence.[14]

The Phoenixing Act also provides that it is both an offence, and a contravention giving rise to civil liability, for an officer of the company to engage in conduct that results in the company making a creditor-defeating disposition of property.[15] Furthermore, any person who procures, incites, induces or encourages a company to enter into a creditor-defeating disposition may also commit an offence and be liable for a civil penalty.[16] This latter provision is primarily aimed at 'unscrupulous facilitators and pre-insolvency advisors, and other entities that, while not formally responsible for the management of a particular company, are responsible for designing and implementing illegal phoenix schemes'.[17] It does, however, give rise to a potential risk for professional advisers and other participants engaged in restructuring activity who could, in theory, be at risk of liability where they facilitate a transaction that is later held to be a creditor-defeating disposition.

There are various defences to civil and criminal liability under these provisions, where the disposition was made under a scheme of arrangement, under a deed of company arrangement, by a liquidator or provisional liquidator or pursuant to a course of action that is subject to the pre-existing insolvent trading safe harbour provisions.[18] The provisions, therefore, appear to be designed to encourage parties to undertake restructuring activity under the auspices of one of these prescribed regimes.

Director accountability

In addition to combating creditor-defeating dispositions, the phoenix amendments to the Corporations Act aim to improve the accountability of directors for their role in any phoenix activity by establishing new rules regulating the ability of company directors to resign from their positions. These rules target the practice of backdating director resignations to avoid liability for the company's actions through fabricating a director's resignation date.[19]

Should a director resign from his or her position, the resignation must be reported to ASIC within 28 days. As a consequence of the phoenix amendments, if the resignation is not reported within the 28-day time frame, the resignation is taken to have occurred on the date that the resignation is reported to ASIC unless the court is satisfied that it would be just and

13 Phoenixing EM (n 9), [2.52].

14 Corporations Act (n 3) section 588FGAC.

15 ibid, section 588GAB. There are certain additional requirements as set out therein.

16 ibid, sections 588GAC(1)–(2).

17 Phoenixing EM (n 9), [2.81].

18 Corporations Act (n 3), sections 588GAB(3), 588GAC(3) and 588GA(1). Somewhat strangely, a disposition by an administrator (other than by a deed of company arrangement) does not appear to be a defence despite transactions made by an administrator being excluded from being voidable under section 588FE. There are certain additional defences available for the civil liability provisions.

19 Corporations Act (n 3), section 203A.

equitable for the resignation to be considered to have occurred before this date.[20] Additionally, a director may not resign if doing so would result in the company having no director (unless the company is being wound up).[21]

Key restructurings

Tiger Resources

Tiger Resources Limited (Tiger) undertook a novel and contested restructuring by way of an Australian scheme of arrangement, despite the group's facilities being governed by English law and the group's borrower, Société d'Exploitation de Kipoi SA (SEK), being incorporated (and operating copper projects) in the Democratic Republic of the Congo.

Tiger was the Australian Securities Exchange (ASX) listed and Australian incorporated head company of the Tiger group, and SEK was its (95 per cent owned) direct subsidiary.

SEK financed its mining operations with three major financiers, pursuant to the following English law governed secured facilities, which were guaranteed by Tiger at the time that the scheme of arrangement was launched:

- Tranche A debts (senior debt) of approximately US$221 million comprising:
  - US$20,306,000 owed to QMetco Limted (QMetco);
  - US$144,855,000 owed to Taurus Mining Finance Fund LP (Taurus); and
  - US$55,932,000 owed to the International Finance Corporation (IFC); and
- Tranche D and E debts (super senior debt) of approximately US$25.9 million owed to Taurus and Qmetco:
  - US$13,731,000 owed to Taurus; and
  - US$12,191,000 owed to QMetco.

In 2019, Tiger's copper production dropped to 50 per cent of the level achieved in previous years owing to operational issues, which compounded pressure from falling copper prices.[22] Tiger's strategic plan required capital works to deliver copper enhancing projects, but more funding was required to pursue these opportunities.[23] However, obtaining additional funding was impossible given the company's existing debt levels.[24] An independent expert's report indicated that unless the secured debt was compromised, Tiger would soon be insolvent owing to persistent cash deficits.[25]

20 ibid, section 203AA.

21 ibid, section 203AB.

22 King & Wood Mallesons, 'Taming the Tiger: The Restructuring of Tiger Resources' (Speech, Turnaround Management Association, 15 July 2020).

23 ibid.

24 *Tiger Resources Limited v International Finance Corporation* [2019] FCA 2186, [21].

25 ibid, [19]–[21].

Scheme of arrangement

Tiger had reached an agreement with QMetco and Taurus, related entities that planned to acquire majority interest in Tiger, but not IFC. The agreement involved a debt restructuring that would involve converting the majority of the senior debt to equity in Tiger (reducing the senior debt to US$70 million) and that would leave the super senior debt outstanding in full.

Being unable to compromise the IFC secured debt without its consent, Tiger proposed an Australian creditors' scheme of arrangement intended to achieve this outcome compulsorily. Given SEK was not a body corporate incorporated in Australia, or a foreign body corporate registered under the Corporations Act, as required to fall within the scheme jurisdiction of the Australian courts under section 411 of the Corporations Act,[26] the scheme was instead undertaken by Tiger as the scheme company. This involved a two-step process under the scheme:

- first, Tiger assumed the senior debt of SEK pursuant to a novation mechanic; and
- second, the senior debt assumed by Tiger was then partially compromised in exchange for newly issued equity in Tiger (and the term of both the senior debt and the super senior debt was extended).

Despite the apparent disparity of rights between the senior and super senior debt, both before and after the scheme, Tiger formulated the scheme on the basis that all the debt would form a single class and vote together. This was necessary to give Taurus and QMetco in excess of 75 per cent of the debt in the class and thereby pass the scheme resolution, notwithstanding any objection by IFC.

In addition, as a result of the facilities being governed by English law, the scheme contained a condition precedent that the scheme be recognised under the Cross-Border Insolvency Regulations 2006 (UK), or that an order otherwise be obtained to the effect that the compromise of English law governed creditor claims would be recognised and treated as effective as a matter of English law.

The scheme independent expert opined that if the scheme was not implemented, the Tiger group would enter insolvency, with a shortfall anticipated to the senior debt but with the super senior debt expected to recover in full.

IFC's challenge to the scheme

At the convening hearing, IFC challenged the proposed scheme, contending the following.

- Exclusive jurisdiction clause: the scheme proceedings should be permanently stayed because they were in contravention of the English law exclusive jurisdiction clauses in the loan documents, or alternatively on *forum non conveniens* grounds (on the basis that

26 It would appear that the English courts would have had jurisdiction to undertake an English scheme of arrangement (owing to the English law facility documents) in respect of SEK, but the Tiger group did not choose to take this approach.

the debt was governed by English law, and that the existence of the *Gibbs* rule would likely require an English scheme of arrangement to compromise the English law debt).[27]

- No compromise or arrangement: the scheme did not satisfy the requirements of section 411 of the Corporations Act that there be a compromise or arrangement between the scheme company and its creditors or a class thereof. IFC argued that no debt of Tiger (the scheme company) was being compromised; rather it was debt of SEK that was being extinguished (and assumed) by way of the novation in the first step. The second step involved compromise of the new debt of Tiger created in the first step (which did not exist prior to the scheme), which IFC argued could not be used as a 'bootstrap' justification to fall within the provision. While Tiger guaranteed the SEK debt, Tiger's guarantee obligation was not directly modified by the scheme terms (although it was indirectly modified by the reduction of the primary debt).
- Class formation: it was inappropriate for all scheme creditors to vote as a single class, given the differences between the senior debt and the super senior debt. In particular: the senior debt was in an inferior security position to the super senior debt; and the senior debt was having its debt significantly reduced by the scheme, whereas the super senior lenders were not.[28]

Convening hearing decision

The convening application was before Gleeson J of the Federal Court of Australia (FCA or the Court), who ultimately allowed the scheme meetings to be convened, responding to IFC's objections as follows.

- The Court was not convinced that the jurisdiction clause in the loan documents was intended to confer exclusive jurisdiction on the English courts in relation to a scheme of arrangement, as it did not appear to relate to the settlement of a dispute. Furthermore, it considered Australia was prima facie the most appropriate forum for resolving insolvency issues relating to Tiger as an Australian company.
- The Court considered that the scheme was an arrangement for the purposes of section 411 in that it involved an adjustment of Tiger's existing obligations under its guarantee by reducing the amount of that obligation.
- The Court reached the preliminary view that the senior lenders should form a separate class from the super senior lenders, given the significantly different impact of the schemes on them. However, the Court postponed reaching a final view on the issue until the second court hearing.

27 *Gibbs v Societe Industrielle* (1890) 25 QBD 399 (*Gibbs*). The *Gibbs* rule states that debts must be discharged pursuant to the law that governs the debt documents, as the parties have agreed to the application to the debt of all elements of the debt's proper law, including that governing discharge.

28 IFC argued that under the independent expert's evidence, the senior lenders were better off in an insolvency than under the scheme.

Traditionally, a court would not allow a meeting to be convened to vote on a scheme where the classes of creditors had not been resolved. However, the Court permitted the scheme to proceed to be voted upon, questions of class composition notwithstanding. The Court emphasised that the scheme creditors were a small group (not only were there only three scheme creditors, but QMetco was a related entity of Taurus) and that proceeding with a meeting would not produce significant additional costs.

Scheme amendments and scheme meeting

Following the Court's orders allowing the convening of the meeting to vote on the scheme, Tiger relied on the Court's power to vary a scheme under section 411(6) of the Corporations Act in order to vary its scheme proposal and issued a supplementary explanatory statement. The Court approved the issuance of this revised scheme and explanatory material to creditors ahead of the meeting.[29]

Under the revised scheme, Tranche D of the super senior debt would be converted to equity at the same rate as the senior debt, and Tranche E would no longer form part of the scheme. The change was targeted at remedying the divergent outcomes for senior and super senior debt under the original scheme, which gave rise to the class composition concerns at the convening hearing.

The revised scheme was approved by the requisite majorities at the scheme meeting, with Taurus and QMetco both voting in favour and IFC electing not to attend.[30]

Second court hearing

At the second court hearing, IFC continued to oppose the revised scheme on the basis it advanced at the convening hearing. However, IFC conceded that its opposition would fail based on the reasoning adopted by the Court in the convening hearing.

In the absence of any submission to the contrary from IFC, the Court accepted that the scheme was fair and reasonable, and approved it.[31]

English recognition and effectiveness

Following the second court hearing, IFC sold its debt to a third party who was supportive of the scheme. This allowed Tiger to successfully apply for an order from the High Court of England to recognise and give effect to the compromise of English law governed creditor claims as part of the scheme as a matter of English law, on the basis that IFC and the third

29 *Re Tiger Resources Limited (No 2)* [2020] FCA 266, [6].

30 ibid, [7]–[9].

31 ibid, [29].

party confirmed to the High Court their submission to the jurisdiction of the Australian courts.[32] The scheme satisfied all conditions precedent and became capable of implementation on 25 March 2020.[33]

Commentary

The Tiger restructuring is the second contested creditors' scheme of arrangement in recent years where the approach to class formation has been a key focus of the argument. In each case, the scheme company has taken a broad approach to class composition to seek to cram down minority lenders, despite there being significantly different treatment of lenders within the class.

When advocating this approach, Tiger pointed to the *Boart Longyear* decisions[34] as justification for taking a literal reading of the class composition test in *Sovereign Life*:[35] only where it is 'impossible' for creditors to consult together should they be placed in separate classes. Gleeson J rightly doubted the class construct initially advanced by *Tiger* in this case, although her willingness to entertain the argument beyond the convening hearing is surprising. It may be that the *Boart Longyear* decisions have created an Australian divergence from the traditional understanding of class formation under English law.

Other aspects of the decision are also open to debate. There appears to be some merit to IFC's argument that the Tiger scheme involved a compromise of SEK's, rather than Tiger's, debts. Unfortunately, there was little examination of this issue in the judgment.

Minority lenders may feel particularly threatened by cram-down attempts where they are not provided with an appropriate level of information about the scheme and class composition ahead of the convening hearing. In the United Kingdom, this issue is addressed by way of the Practice Statement (Companies: Schemes of Arrangement under Part 26 and Part 26A of the Companies Act 2006), which provides that it is the responsibility of the applicant to ensure that notification is given to all persons affected by a scheme in sufficient time to enable persons affected by the scheme to consider what is proposed, to take appropriate advice and to attend the convening hearing.[36]

32 Order of Davis-White J in *Re Tiger Resources Limited* (CR-2020-001845, 17 March 2020); King & Wood Mallesons, 'Taming the Tiger: The Restructuring of Tiger Resources (Speech, Turnaround Management Association, 15 July 2020). Submission to jurisdiction is a recognised exception to the *Gibbs* rule.

33 Caroline Keats, 'Update on Proposed Debt Restructure – Creditors' Scheme Becomes Effective': http://www.tigerresources.com.au/wp-content/uploads/2020/04/Update-On-Proposed-Debt-Restructure-Creditors-Scheme-Becomes-Effective.pdf.

34 *Re Boart Longyear Ltd* [2017] NSWSC 567; *First Pacific Advisors LLC v Boart Longyear Ltd* [2017] NSWCA 116.

35 *Sovereign Life Assurance Company v Dodd* [1892] 2 QB 573.

36 High Court of England and Wales, Practice Statement (Companies: Schemes of Arrangement under Part 26 and Part 26A of the Companies Act 2006), 25 July 2020, [8]. Evidence of steps taken to notify interested persons of these considerations should be introduced at the convening hearing.

Unfortunately, there is no equivalent to the Practice Statement in Australia, and therefore there is some variance in the level of disclosure to creditors ahead of the convening hearing. There has also been a recent trend towards last minute changes to the scheme terms. In the case of *Tiger*, changes were made to the scheme booklet up to 24 hours before the convening application.[37] It also appears that IFC needed to seek a court order to obtain the material that Tiger intended to rely upon in support of its application at the convening hearing (and then only obtained this material three days before the hearing).[38]

Wollongong Coal

The second major creditors' scheme of arrangement over the past year featured two Australian subsidiaries of India's Jindal Steel & Power group. As in the case of the Tiger scheme, the proponents of these schemes faced the challenge of compromising English law debt through Australian schemes of arrangement. However, in the case of *Wollongong Coal*, the borrower under these facilities was an Australian entity.

The schemes rescheduled the group's finance debt and allowed the company's lenders to choose which of two new facilities they would roll their exposures into (which offered significantly differing terms). The schemes also underwent a Lazarus-like revival, through the power of the court, after they terminated for failure to satisfy their conditions precedent in time.

Background to the schemes

Wollongong Coal Limited (Wollongong) and Jindal Steel & Power (Australia) Pty Ltd (Jindal) are Australian incorporated subsidiaries of the Jindal Steel & Power group, an Indian steel and energy company. Wollongong and its subsidiaries operated two Australian collieries: Russell Vale and Wongawilli, which suffered major operational disruptions for a number of years. This ultimately caused Jindal to default on its two English law governed loan facilities: the US$276.99 million Axis Facility and the US$70.05 million SBI Facility (both of which were guaranteed by Wollongong).[39]

Following defaults under each facility, Jindal and Wollongong each proposed a creditors' scheme of arrangement with the objective of, among other things, creating a sustainable capital structure, providing the companies with breathing room pending regulatory approvals to recommence their mining operations and curing defaults under the Axis and SBI Facilities to facilitate additional financial support from the Jindal Steel & Power group.[40]

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37 Transcript of Proceedings, *Tiger Resources Limited v International Finance Corporation* (Federal Court of Australia, NSD2043/2019, Gleeson J, 19 December 2019), [40].

38 Order of Gleeson J in *Tiger Resources Limited v International Finance Corporation* (Federal Court of Australia, NSD2043/2019, 13 December 2019).

39 Wollongong Coal Limited, 'Schemes of arrangement implemented' (ASX Announcement, 8 May 2020); *Re Wollongong Coal Limited and Jindal Steel & Coal Australia Pty Ltd* [2020] NSWSC 73, [11] (*Wollongong sanctioning hearing*).

40 *Wollongong sanctioning hearing* (n 39), [20].

Terms of the schemes

Wollongong and Jindal proposed schemes of arrangement under which the secured debt under the Axis and SBI Facilities were reallocated into one of two rescheduled facilities.

- Rescheduled Facility A contained various reductions of principal amounts of up to 29 per cent depending upon the company achieving certain milestones and an interest rate margin of 4.5 per cent. All outstanding amounts under Facility A were required to be repaid by 30 September 2022.
- Rescheduled Facility B was to be repaid in three equal instalments on 30 September each year in 2026, 2027 and 2028, with no principal reduction mechanic, but at a lower 3 per cent interest rate margin.

Facility B ranked equally with Facility A, but lenders under Facility B were prevented from exercising their security rights while principal amounts remained outstanding under Facility A.[41]

In addition to providing lenders with this option, the schemes also permitted the sale of certain non-mining assets (that were subject to security under the Axis and SBI Facilities) to generate capital, which was required to resume mining operations.[42]

Approval of the schemes

Under a restructuring support agreement signed in November 2019, all creditors under the SBI Facility and creditors representing 78.94 per cent by value under the Axis Facility agreed to support the schemes,[43] and they were comfortably passed at the scheme meetings held for the two classes of creditors bound by the scheme: lenders under the Axis Facility and lenders under the SBI Facility.[44]

Compromising English debt

Prior to implementing the scheme, the Axis and SBI Facilities were both governed by English law. This presented an issue for the proposed Australian schemes of arrangement: as discussed in respect of the Tiger scheme, under the rule in *Gibbs* as a matter of English law, debt arising under a contract governed by English law cannot be compromised or discharged by a foreign (ie, non-English) restructuring or insolvency process.[45]

The parties addressed this challenge by amending the facility documentation (with majority lender consent) to change the governing law to New South Wales law prior to proposing the schemes of arrangement. In a clever twist, the amendment provided that the governing law would revert to English law on 16 March 2020, allowing sufficient time for the

41 ibid, [17]–[18].

42 ibid, [19].

43 ibid, [14].

44 Order of Black J in *Wollongong Coal Limited and Jindal Steel & Coal Australia Pty Ltd* (Supreme Court of New South Wales, 2019/00384003, 20 December 2019).

45 *Gibbs* (n 27).

scheme to take effect while the facility was governed by New South Wales law (with the aim of circumventing the *Gibbs* rule), but ultimately allowing the lenders to continue to hold their debt under English law governed documentation over the longer term.

On the basis that the change of law was not arbitrary (the borrower being incorporated in New South Wales) and that no lender objected to the change, the Court did not have any difficulty with this manoeuvre (but also did not consider it necessary to decide whether the amendment did in fact successfully avoid the rule in *Gibbs*).[46]

Resurrection of the scheme

Somewhat unusually, the schemes contained a number of substantive conditions precedent to their implementation. Unfortunately, these conditions were satisfied one day after the expiry of the required time frame, resulting in the automatic termination of the schemes under their terms.[47]

The substantial majority of scheme creditors remained supportive of the schemes, notwithstanding the late satisfaction of the conditions. The companies therefore approached the Court seeking an order retrospectively amending the terms of the schemes to extend the deadline for achieving the required conditions.[48] The Court granted the orders,[49] noting that:

- the failure to satisfy the conditions precedent arose from a short delay that would have been avoided had the parties had the benefit of hindsight;
- the failure of the schemes owing to the short delay would deprive the companies and the consenting creditors of the benefits of the schemes, and expose the companies to the risk of external administration;
- both the schemes and the application for retrospective amendment had the support of the majority of creditors by number and value;[50]
- there would be no practical utility and considerable wasted costs in reconvening a meeting to consider new or revised schemes for the companies; and
- the potential for the difficulties in implementing the scheme to delay future payments to the companies' creditors was not sufficient reason to deprive interested parties of the benefit of the schemes.[51]

The effect of these orders was to bring the schemes back to life, and ultimately allow for their successful implementation.

46 *Wollongong sanctioning hearing* (n 39), [63].

47 ibid, [10].

48 ibid.

49 The Court relied upon the power under Rule 1.1 of the Uniform Civil Procedure Rules to extend or abridge any time fixed by an order of a court, as schemes of arrangement are enlivened by orders of the court: *Re AGL Gas Networds Ltd* [2001] NSWSC 165; *Re Wollongong Coal Limited*; *Re Jindal Steel & Power (Australia) Pty Limited* [2020] NSWSC 614, [17] (*Wollongong CP hearing*).

50 The only creditor who abstained from voting on the scheme, the Bank of Baroda, ultimately indicated via its solicitors that it did not object to the schemes, *Wollongong CP hearing* (n 49), [34].

51 *Wollongong CP hearing* (n 49), [18].

Retail Food Group

In 2019, Retail Food Group (RFG) achieved a consensual recapitalisation and balance sheet restructure while under regulatory investigation and public scrutiny in respect of its past business practices. RFG is an ASX listed franchiser, whose key brands include coffee chain Gloria Jeans and food franchises Donut King, Crust Pizza, Michel's Patisserie and Brumby's Bakery.

RFG had suffered several challenging years, culminating in a highly critical review of its business practices in the Parliamentary Joint Committee's Fairness in Franchising report that was released on 14 March 2019. This report recommended (among other things) that the Australian Competition and Consumer Commission, ASIC and the Australian Tax Office conduct investigations into the operations of RFG and its current and former directors and officers.

In addition, RFG was highly leveraged and faced the challenge of refinancing approximately A$260 million of bank debt that was due to mature in late 2019. RFG engaged with various capital providers during this time, including granting exclusivity to Soliton Capital in respect of a potential A$160 million recapitalisation proposal, which was unable to be agreed.

Ultimately, RFG implemented a A$190 million capital raising, combined with a consensual restructuring of its existing bank debt. The transaction involved:[52]

- a A$190 million equity raise, which was effected through a fully underwritten A$170 million placement with institutional investors and a non-underwritten A$20 million share purchase plan;
- RFG's lenders receiving a partial repayment of A$118.5 million on their outstanding bank debt, extinguishing A$71.8 million of their debt (reflecting a write-off of approximately 27 per cent); and
- RFG's lenders entering into a new A$75.5 million debt facility for a three-year term, which refinanced the remaining balance of the bank debt.

The share placement was approved by a resolution of RFG's shareholders at its general meeting.[53]

In addition to the recapitalisation, RFG also undertook a broader operational turnaround programme, which included making changes to its executive team, reducing payroll costs, upgrading and consolidating its systems, and selling or closing non-performing brands.[54]

The RFG transaction is notable in that it involved the bank lenders both agreeing a significant haircut and to roll a portion of their debt into a new facility, a relatively uncommon outcome in a high-profile situation of this type in Australia.

52 Retail Food Group, 'Capital raising launch and guidance' (ASX Announcement, 11 October 2020).

53 Retail Food Group, 'Results of General Meeting' (ASX Announcement, 19 November 2019).

54 Retail Food Group, *Annual Report 2019* (Report, 29 October 2019) ii, 5.

Recent noteworthy cases

Halifax: cross-border joint court hearings

In *Re Halifax*,[55] the FCA signalled its willingness to facilitate a joint hearing with a foreign court for the first time.

The Halifax group provided broking and investment services to clients in Australia and New Zealand. When the group became insolvent, the administrators discovered a A$19 million deficiency in the group's client funds. Furthermore, there had been substantial commingling of the client funds between the group's Australian and New Zealand entities, which were subject to liquidations in Australia and New Zealand respectively (although the same individuals were appointed liquidators in each process).

The liquidators formed the view that the most expeditious way of obtaining certainty on the relative entitlements of the clients to the commingled funds was to hold a joint hearing of the FCA and the High Court of New Zealand (HCNZ). Accordingly, the Australian liquidators approached the FCA and requested that the Court issue a letter of request for assistance to the HCNZ under section 581(4) of the Corporations Act, in which it would request a joint hearing on the treatment of the funds. It was hoped this would reduce the risk of inconsistency in the judicial advice or directions given by each court in respect of the same commingled pool of funds.

To issue the request, the Court must be satisfied that:

- it has the power to issue the letter of request;
- the foreign court receiving the request has the power to act on the request; and
- issuing the letter of request is consistent with considerations of utility and comity.

While the FCA was satisfied it had the power to issue the request and that the HCNZ could act on the request, it delayed making any order until representative clients of the Halifax group first identified who would respond to the application.[56] Case management hearings were subsequently held in the HCNZ on 12 December 2019 and the FCA on 13 December 2019, where the courts agreed to hold a joint procedural hearing, which took place on 18 December 2019 by videoconference.[57]

55 *Kelly, Halifax Investment Services Pty Ltd (in liq) (No 5)* (2019) 139 ACSR 56.

56 ibid, [78]–[80].

57 Order of Gleeson J in *Kelly, Halifax Investment Services Pty Ltd (in liq)* (NSD2191/2018, 19 February 2020); KPMG, *Update to Investors – 24 December 2019*.

Following these initial case management hearings a series of joint case management and directions hearings took place where interested parties were joined to the application.[58] The HCNZ and the FCA have also held a joint hearing to consider two applications regarding whether certain investments could be closed out ahead of the scheduled final hearing regarding the pooling of commingled funds.[59]

The *Halifax* decisions chart new territory in Australia's (and New Zealand's) cross-border jurisprudence. The approach is reminiscent of the joint hearings undertaken by US and Canadian courts in the *Nortel* bankruptcy.[60] The matter remains ongoing.

Colette group: extended rent-free periods in administration

Under section 443B of the Corporations Act, administrators have a week upon appointment to decide whether they intend to continue to exercise a company's rights in respect of leased property. Should they fail to notify a lessor that they intend to disclaim the lease, the administrator becomes personally liable for rent payable for the period commencing one week after the appointment of the administrators until the conclusion of the administration.[61]

Section 443B strikes a balance between the interests of the distressed company and its lessors; however, during the covid-19 lockdowns, administrators were faced with a dilemma: they could either risk sizeable personal liability under a company's leases or quickly elect to disclaim key leases under conditions of radical uncertainty. Administrators faced with this dilemma began to approach the courts for assistance, leading to a number of decisions that altered the operation of section 443B during the pandemic.

In *Strawbridge (Administrator), in the matter of CBCH Group Pty Ltd (admin apptd) (No 2)* [2020] FCA 472, the administrators of the Colette group obtained orders relieving them of personal liability for rent changed by the group's landlords during the covid-19 lockdown.[62] The administrators argued that relieving them of personal liability would allow them to pursue a strategy of maintaining the stores in a closed state or 'mothballing' until a managed

58 Order of Gleeson J in *Kelly, Halifax Investment Services Pty Ltd (in liq)* (NSD2191/2018, 19 February 2020); Order of Gleeson J in Kelly, *Halifax Investment Services Pty Ltd (in liq)* (NSD2191/2018, 3 April 2020); *Kelly, Halifax Investment Services Pty Ltd (in liq) (No 10)* [2020] FCA 1146; Order of Registrar Kumar in *Re Kelly in the matter of Halifax New Zealand Limited (in liq)* (High Court of New Zealand, CIV-2019-404-2049, 28 February 2020).

59 *Kelly, Halifax Investment Services Pty Ltd (in liq) (No 7)* [2020] FCA 248; *Kelly, in the matter of Halifax Investment Services Pty Ltd (in liq) (No 8)* [2020] FCA 533; Minutes of Venning J in *Re Kelly in the matter of Halifax New Zealand Limited (in liq)* (High Court of New Zealand, CIV-2019-404-2049, 21 February 2020); *Re Halifax New Zealand Limited (in liq)* [2020] NZHC 2020. It appears that the FCA and HCNZ have proceeded to hold these subsequent hearings without the letters of request actually being issued to date.

60 *In re Nortel Networks Inc*, No. 09-10138, (Bankr D Del, 12 May 2015); *Re Nortel Networks Corp*, 2015 ONSC 2987. For more information, see Paul Apáthy and Hongbei Li, 'Classic cross-border cooperation: joint court hearings in the Halifax insolvency' (2019) 20(4&5), *Insolvency Law Bulletin* 68.

61 Corporations Act (n 3), section 443B(2)(a).

62 The orders were made under Corporations Act, section 447A. This section gives the courts broad discretion to vary aspects of the administration process.

wind-down, sale or recapitalisation could be pursued once the lockdown ended. The administrator's modelling suggested that this strategy would produce the best outcome for the group's creditors as a whole.[63]

The Court acknowledged that the proposed course not to pay rent was an unusual one that would jeopardise the Colette group's tenancies. Ordinarily, administrators only have a week to consider whether to disclaim a lease once appointed; after a week, they are personally liable for any rent incurred by the company.[64] Nonetheless, it was ordered that the administrators were justified in causing the companies in the Colette group not to meet their obligations to pay rent pursuant to any of the leases that accrued up until 5pm on 14 April 2020.[65]

Similar orders have subsequently been made in a number of other administrations, such as those concerning Virgin Australia, Techfront and Miniso. In each case, it was held that it was in the best interests of the company's creditors as a whole that the administrators be given further time to disclaim or retain certain leases, though the reasoning in these cases was more focused on the administrator's inability to make an informed decision regarding the leases during the height of the first wave of the pandemic.[66]

While the courts have demonstrated a willingness to support administrators trying to maximise creditor value during this extraordinary period, the interests of landlords and other lessors have not been forgotten. In the administration of the PAS Group, the Federal Court held that rent that is incurred during the period where administrators have been protected from personal liability will be payable as a priority expense in the tenant's liquidation so long as the rent is properly incurred.[67] This gives rent incurred during this period first priority (together with other expenses of the administration) in any subsequent liquidation of the tenant company.

RCR Tomlinson: priority to circulating assets in administration

The *RCR Tomlinson* decision resolved a number of important issues regarding the relative priorities of secured creditors and employees to certain categories of assets where a company enters administration.

63 *Strawbridge, in the matter of CBCH Group Pty Ltd (No 2)* [2020] FCA 472, [25] (*CBCH*).

64 Corporations Act (n 3), section 443B(2).

65 *CBCH*, [2]. This order was made under section 90-15 of the Insolvency Practice Schedule to the Corporations Act (n 3).

66 *Eagle, in the matter of Techfront Australia Pty Limited (admin apptd)* [2020] FCA 542, [20]-[22]; *Strawbridge, in the matter of Virgin Australia Holdings Limited (admin apptd)* [2020] FCA 571, [48]-[52]; *Jahani, in the matter of Miniso Master Franchisee Pty Ltd (admin apptd)* [2020] FCA 1066.

67 *Ford (Administrator), in the matter of The PAS Group Limited (admin apptd) v Scentre Management Limited* [2020] FCA 1023, 10; Corporations Act (n 3), section 556(1)(a).

Various companies in the RCR Tomlinson group (a major Australian engineering firm) entered into administration in 2018, and then subsequently liquidation. During the liquidation, a question arose on whether the secured creditors or the employees (who are preferential creditors under Australian law) had priority to the proceeds of certain categories of assets of the RCR companies.[68]

The assets in question were:

- amounts paid under construction contracts that, as at the date of the administrators' appointment (the appointment date), were not yet contractually due and payable but could be attributable to work in progress undertaken by RCR prior to the appointment date (WIP);[69]
- amounts potentially payable by principals to RCR in circumstances where, following the appointment date, the principals called on bank guarantees provided by RCR but ultimately not all the funds so called were required to meet claims by those principals against RCR (surplus proceeds);[70] and
- any amounts received by RCR under bank guarantees provided by subcontractors to RCR to guarantee performance under a subcontract, should RCR call on those bank guarantees after the appointment date (subcontractor proceeds).[71]

Section 561 of the Corporations Act provides that in a liquidation of a company, employees have priority to a security holder to the extent that the security relates to 'circulating assets' as that term is defined in the Personal Property Securities Act 2009 (Cth) (PPSA). Circulating assets are a concept introduced by the PPSA essentially for the purposes of replicating the concept of a 'floating charge' that existed under the pre-PPSA law (and which section 561 referred to prior to the introduction of the PPSA).[72]

Prior to the *RCR Tomlinson* case, there was limited case law on how section 561 was to operate following the introduction of the PPSA and the new concept of a circulating asset.[73] The RCR Tomlinson liquidators therefore sought directions from the Court on whether the WIP, surplus proceeds and subcontractor proceeds were circulating assets for the purposes of these provisions.[74]

The first question to be determined by the Court was the date on which a court should determine whether an asset is circulating, described as the 'snapshot date'. Given that assets typically change their nature over the course of an insolvency process (for example, assets being realised and converted to cash), this timing question is critical. The Court decided that the appropriate point to determine the nature of the assets is the 'relevant date' as defined

68 *Re RCR Tomlinson Ltd (admin apptd)* [2020] NSWSC 735, [7] (*RCR Tomlinson*).

69 ibid, [84]–[98].

70 ibid, [64]–[83].

71 ibid, [99]–[110].

72 Explanatory Memoranda, Personal Property Securities Bill 2009 (Cth), [9.55]–[9.67].

73 Personal Property Securities Act 2009 (Cth), section 340.

74 *RCR Tomlinson* (n 68), [7].

in the Corporations Act. Where the liquidation is preceded by an administration (as was the case in the *RCR Tomlinson* case), the relevant date is the date the administrators are appointed (otherwise it is at the commencement of the liquidation).[75]

The Court held that the surplus proceeds and subcontractor proceeds were not circulating assets, and therefore that the secured creditors had priority to these amounts.[76]

The Court held that WIP was a circulating asset if it had (as at the appointment date) reached a point where all that was required for payment to be owing was for an invoice to be raised or certification to be completed. WIP that had not reached this point as at the appointment date (for example, WIP where not all the work had been completed to reach a progress payment milestone) was not a circulating asset. Therefore, there was split priority entitlement to the WIP between the secured creditors and the employees.[77]

The RCR case provides important guidance on the priority treatment of various categories of intangible assets in an insolvency – a matter that has previously given rise to significant debate in Australia.

Final remarks

It is difficult to forecast what will come of the present entanglement of health and economic policy. Government relief measures, temporary moratoriums from insolvency laws and support extended by Australia's major banks by way of repayment deferrals has obscured the true toll of the pandemic.

Current market expectation is that this support will roll off, and as a result, we will likely see an increase in financial distress (and related restructuring and insolvency activity), in the first quarter of 2021. Should there be a significant increase in distressed situations, it will be interesting to see whether Australia's recent shift towards debtor-led turnaround and restructuring will reverse as the downturn puts pressure on the balance sheets of major banks.

Another secondary effect of the pandemic could be further legislative changes to Australia's insolvency and restructuring law. The 'restructuring plan' (essentially a modified scheme of arrangement) introduced in the United Kingdom may provide a template for similar reforms in Australia. However, there is likely to be greater focus on what measures can be taken to improve turnaround prospects for small and medium-sized enterprises. Reforms targeted at this sector will likely take priority over reforms targeted at creditor schemes of arrangement, which in Australia tend to be utilised by larger companies. Whatever direction the government ultimately takes, reforms capable of producing better outcomes for both debtors and creditors will be welcome, as both groups will be facing difficult decisions in the year to come.

75 ibid, [25]; Corporations Act (n 3), section 513C.

76 ibid, [80] and [110].

77 ibid, [84]–[98].

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