The next wave of restructurings

Latham & Watkins' three Global Restructuring and Special Situations chairs share their views on who will be doing the next wave of deals and how they will be doing them.

George Davis in New York,
Jeff Bjork in Los Angeles
and **Bruce Bell** in London

George Davis, Latham & Watkins

Jeff Bjork, Latham & Watkins

Bruce Bell, Latham & Watkins

Q Which stakeholders are going to be driving the next wave of international restructurings?

Bruce: Private equity sponsors will often be in the driver's seat, given the relative decline of public companies' share of the economy in recent years.

Private equity firms also drive the market in the sense of demand for, and terms of, financial debt. These incumbents' ability to drive strategy will in large part dictate how quickly the next wave of restructurings takes shape, especially with the absence of meaningful covenants in debt documents.

As a result, defaults will materialise more slowly, and there will likely be less of them than in previous cycles.

Jeff: While private equity will almost certainly be the primary driver, a number of companies who went public through a Special Purpose Investment Company or SPAC have foreign operations in various jurisdictions, which will create some need for cross-border restructurings.

Q Which marketplaces do you see becoming busier in terms of cross-border cases?

Jeff: The US judiciary may shape the cross-border landscape, as four appellate courts have cases before them that could affect non-obligated affiliates.

Legislation proposed in the US Senate could also limit a bankruptcy court's jurisdiction to grant injunctions in favor of non-debtor affiliates and raise questions on the relief a company could receive in the US from those affiliates.

These cases could significantly complicate cross-border restructurings because the level of oversight and interaction required of the company that has filed is less than ideal.

You try to limit the number of companies that file so that the court's involvement in daily operations stays limited as well, especially in foreign subsidiaries where Chapter 11 may not be viewed as a valid process. That places the non-debtor releases at a premium in cross-border cases.

Bruce: London will remain a critical market, although no doubt Brexit and related recognition issues between the UK and EU will add complexities.

For cross-border restructurings, Delaware may see more activity than New York where there is a Chapter 11 proceeding, given the difficulties with third party releases and the like in New York post-Purdue.

These restructurings may also involve concurrent procedures like a Scheme of Arrangement in the UK or an Examinership in Ireland to bind essentially non-US holders – Mallinckrodt was a good example of this.

Asia has some interesting considerations. Hong Kong remains the centre for China-facing matters, but other restructurings out of South East Asia may migrate to Singapore.

Q Looking back, what stood out in 2022?

Jeff: Large mass tort restructurings dominated throughout 2022, including our work with Mallinckrodt and Owens-Illinois.

Our approach to these two successful matters prioritised hard-fought negotiations in deals that cover current and future liability over litigating the legacy liability, allowing us to effectuate the overall restructurings.

For Mallinckrodt in particular, we used a funded debt restructuring with an international component, as the parent company was based in Ireland.

That's a good example of a complicated, cross-border restructuring that involved both funded debt and foreign issues, as well as a negotiated resolution with the public and private opioid claimants.

Bruce: Restructuring movement felt somewhat slow in the first two quarters of 2022 - you'd expect 2023 to be different given the increase in potential distressed situations though we'll have to see.

Nonetheless, several 2022 cross-border cases stand out from a European perspective for employing a scheme in England. Lowen Play, a German arcade business, launched an English Scheme of Arrangement for its refinancing and restructuring. We also advised the bondholders or Haya Real Estate, a Spanish market leader in managing real estate debt and property assets on its recapitalisation, which was also done through an English scheme.

And then there's HK Airlines, which we advised on its US$6.2 billion debt restructuring, marking the first time that a parallel Hong Kong scheme and UK restructuring plan were approved by the courts in both jurisdiction. The notorious Gibbs rule in the UK allowed us to bring the process into England and potentially cram down dissenting creditors.

George: One of our larger matters in 2022 was the prepackaged Chapter 11 of Lumileds Holdings B.V. and certain of its affiliates in the Southern District of New York.

Lumileds is a leading provider of lighting solutions based in the Netherlands, with 7,000 employees and operations in over 30 countries.

The international nature of the transaction was a key factor in the Chapter 11 restructuring because the company had guarantors in the United States, Germany, Netherlands, Poland, Hong Kong, Singapore, and South Korea, and yet the company and its advisors were able to effect a restructuring by only filing the United States and Netherlands entities, while using the credit agreement and confirmation order to effect the restructuring in the other countries.

Although this was a highly unique structure with a creative approach, I suspect that given the global macroeconomic trends and geopolitical turmoil, we will see more of these cross-border bespoke restructurings in the near future.

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Q For the year ahead, what do you expect to see in the restructurings space?

Bruce: In Europe, I suspect that most cases will stem from companies that have maturities due in late 2023 or early 2024 who for whatever reason missed the opportunity to refinance prior to interest rate rises and the invasion of Ukraine.

Those companies may find themselves requiring light to heavy restructurings to deal with those maturities, so I think you'll have a number of stuck capital markets issuers who can't get a bond refinancing away.

Jeff: The US has a lot of moving pieces that could affect the next year. I'm looking at retail's performance during the holiday season and the potential impact it may have on matters related to malls and shopping centers.

Also, keep an eye on deSPACs who lack the necessary revenue to host their operations, which I suspect we'll see pop up often given the number of SPACs from the last few years. Depending on how the appellate courts rule on the mass tort cases before them, the market will see larger defendants following the approach we took with Owens-Illinois, only submitting a subsidiary or moving the parent company into a subsidiary position.

Larger companies will also continue the trend of using Chapter 11 to neutralise litigation and resolve legacy liability.

George: The mass tort cases take time, but what I think we will also continue to see in the US are pre-arranged, pre-packaged bankruptcy sales to third parties.

> Debt holders are looking to equitize debt and limit the amount of time and duration in bankruptcy, and there's liquidity sitting on the sidelines as companies fail.

So I suspect we'll see buyers come in, seeing the acquisition as an opportunity to buy technology IP or goodwill in a brand they can revamp.

Those will be shorter cases, but much more transactional in nature.

Q Where does crypto fit into your market forecast?

Bruce: The 'crypto winter' continues to produce crypto insolvencies.

> There's obviously been something of a domino effect since the collapse of the TerraUSD and LUNA coins.

There are some interesting opportunities for restructuring professionals in the US and UK given the US has been the 'go to' jurisdiction for crypto businesses to seek bankruptcy protection and the fact that many of them are incorporated in English-derived offshore jurisdictions like the BVI and do business using English law terms.

George: Along with increased consumer skepticism, the crypto space has several coming vulnerabilities on the horizon.

We see the exchanges and brokerage services suffering from liquidity pressure and declining fee revenue, while lending and borrowing platforms have insufficient funds to service customer withdrawals.

Meanwhile, the rapid decline in crypto asset prices has affected the industry's startups, projects, and decentralised autonomous organisations.