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Chapter 15 Court Balances Competing Comity Concerns and Grants Conditional Approval of Croatian Restructuring Plan (*In re Agrokor*, 2018 WL 5298403 (Bankr. SDNY))

Scott C. Shelley, Counsel, Quinn Emanuel Urquhart & Sullivan LLP, New York, USA[1]

Synopsis

In a recent ruling, the US Bankruptcy Court of the Southern District of New York (the 'Bankruptcy Court') granted conditional recognition and approval of a restructuring plan for Agrokor d.d. ('Agrokor') and eight of its affiliates (collectively, with Agrokor, the 'Debtors') that had previously been approved in Croatian restructuring proceedings before the Commercial Court of Zagreb in Croatia.[2] In a case under chapter 15 of the US Bankruptcy Code,[3] the Bankruptcy Court ruled that the Debtors' restructuring plan or 'Settlement Agreement,' once finally approved in Croatia, would be enforceable within the territorial jurisdiction of the United States, despite apparent conflicts with English law, which governed approximately €1.66 billion of the Debtors' indebtedness. Specifically, the Bankruptcy Court held that comity should be granted to the Settlement Agreement in the US, despite that it purported to modify the terms of English-law governed indebtedness, in contravention of English law.[4]

In resolving these competing comity concerns, the Bankruptcy Court noted that comity is a broad concept that may require consideration of overlapping rights of multiple parties and nations. Because the Debtors satisfied the Bankruptcy Code criteria for recognition of the Settlement Agreement, the Bankruptcy Court held that the Settlement Agreement would be recognized in full within the territorial jurisdiction of the US; courts in other jurisdictions – including England – would retain the authority to determine the effect of the Settlement Agreement within their respective jurisdictions.[5] The *Agrokor* ruling thus illustrates how courts can reconcile conflicting comity interests that may arise in chapter 15 proceedings in the US.

Background

Agrokor and its affiliated companies (the 'Agrokor Group') are the largest private company (by revenue) in Croatia.[6] The Agrokor Group's business interests that include retail, food production, agriculture and related activities that collectively account for approximately fifteen percent of Croatia's gross domestic product.[7] By early 2017, the Agrokor Group was in financial distress, due to high leverage and a general downturn in marketplace conditions.

On 7 April 2018, apparently in response – at least in part – to the Agrokor Group's dire financial situation, Croatia enacted the 'Act on the Extraordinary Administration Proceedings in Companies of Systemic Importance of the Republic of Croatia' (the 'EA Law').[8] The purpose of the EA Law is to protect the sustainability of 'companies of systemic importance for the Republic of Croatia' where the operations of those companies 'affect the entire economic, social, and financial stability of the Republic of Croatia.'[9] On the same day the EA Law was adopted, Agrokor and certain of its affiliates commenced restructuring proceedings (the

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1 The views expressed in this article are those of the author and not necessarily those of his firm.
2 *In re Agrokor*, 2018 WL 5298403 (Bankr. SDNY). References to the Bankruptcy Court's ruling are cited herein as 'Opinion at *_'.
3 11 USC § 101, et seq. (the 'Bankruptcy Code'). Unless otherwise specified, references herein to a 'section' refer to the applicable section of the Bankruptcy Code.
4 Opinion at *23.
5 *Id.* at *26.
6 *Id.* at * 1. The Agrokor Group consists of a group of more than 220 companies, 77 of which maintained headquarters in the Republic of Croatia. *Id.*
7 *See* Verified Petition for (I) Recognition of Foreign Main Proceedings, (II) Recognition of Foreign Representative and (III) Related Relief Under Chapter 15 of the Bankruptcy Code [ECF 4], ¶ 1, US Bankruptcy Court for the Southern District of New York, Case No. 18-12104 (MG) (the 'Verified Petition').
8 Opinion at *1.
9 *Id.*

'EA Proceedings') in the Commercial Court of Zagreb in Croatia (the 'Commercial Court').[10]

The Commercial Court determined that the Agrokor Group was eligible to restructure under the EA Law, as it was insolvent and satisfied the debt and employee thresholds under the law, and issued a commencement order officially instituting the EA Proceedings on 10 April 2017. Subsequently, the Commercial Court issued supplemental orders on 21 April 2017, 5 July 2017 and 13 July 2017, extending the proceedings to additional affiliates and subsidiaries of Agrokor.[11] The entry of these orders prohibited creditors from enforcing security over assets of the debtors and their controlled or affiliated companies, and from instituting or continuing legal action against such entities.[12] The Commercial Court also appointed Fabris Perŭsko as extraordinary administrator and foreign representative (the 'Foreign Representative') of the Debtors.

In accordance with the EA Law, the Agrokor Group negotiated with its creditors and formulated the Settlement Agreement, to adjust the debt obligations of, and ownership interests in, the debtors. In particular, the Settlement Agreement proposed to modify the terms of substantial debt obligations, including unsecured loans governed by English law, as well as unsecured notes governed by New York law.[13] The Agrokor Group obtained approval of the Settlement Agreement from the requisite number of creditors, and the Commercial Court entered an order approving the Settlement Agreement on 6 July 2018.[14] More than 90 appeals were lodged in respect of that order; these appeals are being adjudicated by Croatia's High Commercial Court, which has authority to grant final approval of the Settlement Agreement.[15]

On 12 July 2018, the Foreign Representative filed a verified petition under chapter 15 of Title 11, United States Code (the 'Bankruptcy Code'), seeking recognition of the EA Proceedings as foreign main proceedings, recognition that the Foreign Representative satisfied the requirements of Bankruptcy Code section 101(24), and recognition and enforcement of the Settlement Agreement within the territorial jurisdiction of the United States.[16]

By order entered 21 September 2018, the Bankruptcy Court granted recognition to the EA Proceedings as foreign main proceedings and recognised the Foreign Representative as the representative of the Debtors, 'with full authority to administer the Debtors' assets and affairs in the United States.'[17] In that order, the Bankruptcy Court expressly reserved decision concerning the request for recognition and enforcement of the Settlement Agreement, noting that such request 'raised more challenging issues.'[18] The Bankruptcy Court resolved the remaining issues in its ruling issued 24 October 2018, holding that it would recognise and enforce the Settlement Agreement within the territorial jurisdiction of the United States.[19]

Bankruptcy Court's analysis

The Bankruptcy Court identified the key obstacle to enforcement of the Settlement Agreement in the US: the so-called *Gibbs* Rule, emanating from an 1890 ruling from the English Court of Appeal, where the court held that it was impermissible for a foreign court to discharge obligations under a contract governed by English law that were to be performed in England.[20] Under the *Gibbs* Rule, the modification of English law governed debt obligations of the Agrokor Group through the EA Proceedings would not be recognised in England.[21] The Bankruptcy Court queried whether the *Gibbs* Rule, which was good law in England but not necessarily in the United States, justified a refusal to grant comity to the EA Proceedings, where those proceedings satisfied US due process standards.[22] In other words, the Bankruptcy Court was tasked with determining whether the request for US recognition of the Settlement Agreement required the Bankruptcy Court to undertake a comity analysis that balanced the interests of Croatia and England.

The Bankruptcy Court ultimately answered that question in the negative. The Bankruptcy Court noted:

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10 *Id.*
11 Verified Petition, ¶ 22.
12 Verified Petition, ¶ 23 (citing EA Law Article 41).
13 Opinion at *2. Significantly, the Settlement Agreement released and discharged written guarantees provided by non-debtor affiliates of the Debtors with respect to both the New York and English law debt.
14 Verified Petition, ¶ 37.
15 Opinion at 1.
16 Verified Petition, ¶ 4.
17 Order Granting Petition for (I) Recognition as Foreign Main Proceedings, (II) Recognition of Foreign Representative, and (III) Related Relief Under Chapter 15 of the Bankruptcy Code, ECF 30.
18 Opinion at *2.
19 *Id.*
20 *Id.* at *3 (citing *Antony Gibbs & Sons v La Societe Industrielle et Commerciale des Metaux* (1890) 25 QBD 399 (hereinafter, 'Gibbs')).
21 *Id.* The Bankruptcy Court also noted that the continued vitality of the *Gibbs* Rule was currently the subject of an appeal before the Court of Appeal of England and Wales.
22 *Id.* at *2.

> 'From the record before this Court – particularly since no objections have been filed – the Court concludes that the Croatian Proceeding was procedurally fair, provided proper notice to all creditors and, through the Settlement Agreement, determined the rights of all creditors to property that was subject to the jurisdiction of the Croatian Court.'[23]

Accordingly, the Bankruptcy Court determined to grant comity and recognition to the Settlement Agreement.[24]

In reaching this conclusion, the Bankruptcy Court noted that '[c]omity takes into account the interests of the United States, the interests of the foreign state or states involved, and the mutual interests of the family of nations in just and efficiently functioning rules of international law.'[25] Because the restructuring of the Agrokor Group implicated the interests and laws of numerous countries, the Bankruptcy Court observed that the interests of those other nations, and the decisions emanating from those countries concerning recognition, could be viewed as impacting its own comity analysis.[26] The Bankruptcy Court concluded, however, that it did not need to analyse comity as to every country involved, because the effect of the Bankruptcy Court's ruling would be limited to the territorial jurisdiction of the United States.[27]

Turning to recognition of the Settlement Agreement, the Bankruptcy Court explained that Bankruptcy Code section 1521(a) gives the court broad discretion in granting relief beyond the automatic relief attendant to recognition of a foreign proceeding, and that a court may grant such relief where necessary to protect a debtor's assets provided that the interests of creditors are 'sufficiently protected.'[28] In exercising its discretion to grant such relief and recognise a foreign restructuring plan such as the Settlement Agreement, the Bankruptcy Court observed that it should consider 'whether the foreign proceeding provided a full and fair opportunity for creditors to be heard consistent with due process, and whether the plan was approved by the debtor's creditors and the foreign court.'[29]

The Bankruptcy Court further declared that courts should also look to circumstances in which recognition of foreign plans have been denied to assess whether denial of comity is warranted with respect to a particular plan. To that end, the Bankruptcy Court referenced *In re Vitro, S.A.B. de C.V.*, 701 F.3d 1031 (5th Cir. 2012), where recognition of a Mexican restructuring plan that provided third-party releases was denied because approval of the plan was achieved only by counting votes of insiders. In contrast, in its recent decision in *In re Avanti Commc'n Grp. PLC*, 582 B.R. 603, 617-18 (Bankr. SDNY 2018), the Bankruptcy Court recognized a UK scheme of arrangement that included the release of third-party guarantees, where the vote of insiders was not indispensable for satisfying the statutory voting requirements. The *Avanti* court concluded that creditors in that case 'had a full and fair opportunity to vote on, and be heard in connection with, the Scheme' and found that recognition was appropriate.[30]

Last, the Bankruptcy Court explained that comity decisions should be informed by a list of non-exclusive factors adopted by the Second Circuit Court of Appeals to assess whether a foreign proceeding was procedurally fair. These factors include (1) equality of treatment of creditors of the same class, (2) whether the liquidator is a fiduciary accountable to the foreign court, (3) whether creditors have the right to have the court adjudicate their claims, (4) whether notice to creditors is required, (5) whether creditors meetings are convened, (6) whether the insolvency laws favour local creditors, (7) whether assets are marshalled for centralised distribution, and (8) whether there is an automatic stay that may be lifted to aid in the centralisation of claims.[31]

Applying these factors, the Bankruptcy Court concluded that the EA Proceedings were procedurally fair. Creditors received adequate notice, the EA Law was consistent with 'broadly recognized principles for insolvency laws,' and the distribution waterfall was similar to that provided under the Bankruptcy Code.[32] As a result, the Bankruptcy Court declared that the Settlement Agreement should be granted comity, and recognised within the territorial jurisdiction of the United States.[33]

With respect to the *Gibbs* Rule, as noted above, the Bankruptcy Court held that the rule did not justify withholding recognition of the Settlement Agreement:

> 'The fact that England applies the Gibbs rule and refuses to recognise a discharge or modification

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23 *Id.* at *18.
24 *Id.*
25 *Id.* at *17 (quoting *In re Artimm, S.r.L.*, 335 B.R. 149, 161 (Bankr. C.D. Cal. 2005)).
26 *Id.* at *19.
27 *Id.* The Bankruptcy Court further explained that 'if a foreign creditor has a claim governed by English law that is modified by the Settlement Agreement and wants to challenge the Croatian modification of that claim, the creditor may still challenge enforcement of the claim in the English courts.' *Id.* The Bankruptcy Court's ruling thus would not adversely impact the rights of foreign creditors outside the United States.
28 *Id.* at *20 (citing 11 USC § 1522(a)).
29 *Id.* at *21 (citing *In re Metcalfe & Mansfield Alt. Invs.*, 421 B.R. 685, 698–99 (Bankr. SDNY 2010).
30 *Id.* at *21.
31 *Id.* at *22 (quoting *Finanz AG Zurich v Banco Economico S.A.*, 192 F.3d 240, 249 (2d Cir. 1999)).
32 *Id.* at *22.
33 *Id.* at *23.

> of English law debt approved by a court outside of England is not, in this Court's view, a basis for this Court to decline to recognise and enforce the Settlement Agreement within the territorial jurisdiction of the United States.'[34]

In response to the argument, raised by Agrokor's counsel, that all creditors had submitted to the jurisdiction of the Commercial Court and thus should be bound by the Settlement Agreement, the Bankruptcy Court opined that the evidence adduced was not sufficient to support that conclusion. That argument, the Bankruptcy Court declared, could be raised in further proceedings before an English court.[35]

Discussion

The *Agrokor* ruling addresses the issue of conflicting comity concerns in a pragmatic and thoughtful manner. Entry of an order recognising the Settlement Agreement could be viewed as antagonistic to the *Gibbs* Rule and the law of England. However, the Bankruptcy Court properly apprehended that it had not been asked to determine the enforceability of the *Gibbs* Rule, but rather merely to grant comity to a foreign plan that arguably was in conflict with it. The Bankruptcy Court's comity analysis thus appropriately focused on whether the EA Law and the Settlement Agreement satisfied the requirements for recognition under chapter 15 of the Bankruptcy Code, and concluded that they did.

Creditors displeased with the outcome of the Agrokor restructuring and the terms of the Settlement Agreement will not be without any avenue for recourse. As noted, more than 90 appeals were filed in the EA Proceeding, and creditors holding English law governed claims may be able to pursue their rights in English courts. In the event the Court of Appeal of England and Wales upholds the *Gibbs* Rule in case pending before it, those creditors may find recourse in England, though it is unclear how they ultimately may vindicate those rights.

Conclusion

The *Agrokor* ruling demonstrates how the doctrine of international comity can be flexibly applied in the context of an international restructuring to achieve a pragmatic result. The Bankruptcy Court ruling was narrowly tailored to the facts and disputes before the court, which deftly sidestepped issues that did not need to be addressed. As a result, parties dissatisfied with the ruling will have the opportunity to fight their battles in another, more appropriate forum, in the future.

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34 *Id.* at *24.

35 *Id.* at *24 (citing *Rubin v Eurofinance SA* (2012) UKSC 46 at ¶ 157-67 (Eng.) for the proposition that 'when a creditor submits to the jurisdiction of a foreign court, either by submitting its claims in the foreign insolvency proceeding or otherwise agreeing to be bound thereby, then the creditor will be bound in that proceeding and *Gibbs* will no longer apply').

International Corporate Rescue

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