Corporate Reorganization
Law and Forces of Change (OUP 2020)

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Motivation

- ABI Commission vs LSTA debate framed in similar terms to 1980s economic vs progressive debate
- But 1980s debate was a product of ‘firms, capital structures and players’ that existed at the time (Jackson 2018)
- Forces of change from proximate fields have dramatically changed the landscape and multiple types of reorganization case for large corporates have emerged as a result
- Different approach to these different types of case in the US and England
Controlling argument

- Using conceptual framework developed in a different context to analyse these adaptations leads to wrong turns
Comparative approach

- US Chapter 11 rooted in full financial and operational reorganizations and difficulties arise in applying existing conceptual framework to reorganizations limited to financial creditors
- English corporate reorganization rooted in financial reorganizations and has a well-adapted conceptual framework for this type of case
- But adaption needed in England for full financial and operational reorganizations
- And new adaptations of corporate reorganization law require flexibility in both jurisdictions
# The concepts

| Concept                        | Economic | Progressive | England                                                        |
|-------------------------------|----------|-------------|                                                               |
| Unsecured creditor protection | Market-based approach | Protect weakly adjusting creditors | London Approach and reorganizations limited to financial creditors |
| Collective action problem     | Broad agreement on role of corporate reorganization law in preventing the ‘grab race’ | | London Approach and principles of cooperation |
| Secured creditor control      | Respect secured creditor control rights | Shift bargaining power towards debtor | Long history of ‘blanket lien’ |
| Debtor control                | Sceptical of debtor control rights | Endorse debtor control rights to promote reorg. | Out-of-court nature of London Approach. Different experience of deregulation, mass tort, and class action litigation |
| Bargaining and litigation     | Concern with complex valuation | Support higher valuations for unsecured creditors | Role of Bank of England and fear of exclusion from primary syndication market |
| Transparency and disclosure   | Broad agreement on t&d | | Confidential London Approach negotiations |
## The forces of changes

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<th>Force of change</th>
<th>Concept</th>
<th>New or reformulated concept</th>
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<td>Rise of leverage</td>
<td>Informed, strongly adjusting, unsecured financial creditor: reduced importance of unsecured creditor protection</td>
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<td>Rise of trading</td>
<td>Rise of market for distressed debt and reduced importance of collective action problems</td>
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<td>Rise of secured credit</td>
<td>Incentives of secured creditors to promote corporate reorganization and reduced significance of secured creditor liquidation bias</td>
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<td>Fall of lifetime manager</td>
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<td>Fall of gentleman banker</td>
<td>New attitudes to risk of litigation and implications of complex mechanisms (Hart and Moore 2008)</td>
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<td>Fall of honest broker</td>
<td>Risks of transparency and disclosure</td>
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Practice: US

- Exchange offer
  - Reduce transaction costs
  - Contain holdout threat
  - Avoid litigation over valuation

- Connected party's 363
  - Reduce transaction costs
  - Contain holdout threat
  - Avoid litigation over valuation: current market price in prevailing market conditions

- Prepackaged plans
  - Reduce transaction costs
  - Signal 'business as usual'

- Contractual control rights
  - Reduce transaction costs
  - Contain holdout threat
  - Importance of control rights in reducing liquidation bias
Practice: England

- DIP to signal business as usual
- Reduce holdout problem and litigation risk: majority rule and counterfactual

Part 26A restructuring plan
- DIP to signal business as usual
- Reduce holdout problem: cross-class cram down power
- Reduce litigation risk: role of relevant alternative

Contractual control rights
- LMA intercreditor agreement
- Scope of intercreditor agreement and court
- Lock-up agreements and rights vs interests
Theory and practice

**Economic lens**
- Solve bargaining failure
- ‘Mimic’ results market would have produced if bargaining had been possible
- Reduce transaction costs

**Progressive lens**
- Prevent distress spreading to operations and to weakly adjusting trade creditors, employees, and community
New forces of change

- COVID-19
- Covenant-lite and covenant loose lending
  - Becomes more difficult to contain restructuring in financial debt
  - Cases compromising both financial and operational creditors
- Theory and practice
  - Greater distance between economically-minded and progressively-minded scholars
- Comparative analysis
  - US (still) has better tools to stabilize operations and create liquidity
New forces of change

- Modern strategic reorganization cases
  - Landlords
  - Pensions
- Theory and practice
  - New questions of equitable pain sharing
- Comparative analysis
  - Counterfactual/relevant alternative and non-financial creditors
New forces of change

- Fragmented capital structure reorganizations (Ayotte 2019)
  - Disagreement about the appropriate transaction in distress
  - Living will? (Jackson and Skeel 2013)
Future forces of change?

- Actors move from being iconoclasts to becoming part of establishment
  - Public reputation?
  - Attitudes of investors
- Willingness of market to discipline itself
  - Net short lender disenfranchisement provisions
  - Permitted transfer lists
Conclusion

- Identify type of corporate reorganization case
- How does dominant theoretical concern manifest itself in that type of case:
  - Allocation of assets to highest and best use
  - Preserve company for weakly adjusting trade creditors, employees, and community in which debtor is embedded
- Implications for reform agenda
References

- Oliver Hart and John Moore, ‘Contracts as Reference Points’ (2008) 123(1) Q J Econ 1
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