Case note:

In the matter of Energy XXI Ltd [2016] SC (Bda) 79 Comm

Bermuda Supreme Court grants recognition by way of a permanent stay in case concerning parallel Bermuda and US insolvency proceedings

In a recent decision, Chief Justice Ian Kawaley granted recognition by way of a permanent stay in respect of a company in provisional liquidation in Bermuda and in Chapter 11 proceedings in the US. The stay was conditional upon the confirmation of a Plan in the Chapter 11 proceedings. Complex technical arguments concerning jurisdiction and the nature of primary and ancillary proceedings were considered. The Court also addressed the constraints on the forms of common law assistance available to the Court imposed by the Privy Council in *Singularis Holdings Ltd v PwC* [2015] AC 1675.

Facts

Energy XXI is a Bermuda exempt company ("the Company"). On 14 April 2016, the Company presented a Petition for its own winding-up. The Petition averred that the Company's ability to operate had been impaired by "liquidity issues" and sought, *inter alia*, the appointment of a provisional liquidator. On the same day, the Company and 25 other Group members commenced Chapter 11 proceedings in the Southern District of Texas, Houston Division ("the Texas Court"). Three days prior, a Restructuring Support Agreement ("the RSA") had been entered into by the Company with a representative group of note holders.

By an ex parte application on 15 April, a provisional liquidator ("the PL") was appointed with "soft touch powers" to review the financial position, monitor the continuation of business under the Company's Board of Directors, and to oversee and liaise with the Board, the Company's creditors and its shareholders in determining the most appropriate manner of effecting a re-organisation and/or refinancing of the Company. On the return date of the Petition, the Supreme Court determined that the Texas Court should be the primary forum for restructuring and that the Bermuda proceedings would be ancillary.

The PL subsequently issued an *inter partes* summons seeking an order that "*... recognition of a Plan of Reorganisation of the Company under Chapter 11 of the US Bankruptcy Code be granted by this Court by permanently staying all claims of creditors and shareholders brought in this jurisdiction against the Company, such recognition to be effective upon the confirmation of the Plan by the US Bankruptcy Court…*". This application was opposed by the Committee of Equity Security Holders ("the Committee"), which had earlier been appointed by the Texas Court on a limited basis and granted permission to instruct local counsel to advise on issues of Bermuda law.

At a contested hearing on 15 August 2016, the relief sought by the PL was granted. This order was made on a contingent basis; namely that the stay would not come into effect until such time as the Texas Court had approved a Chapter 11 Plan (the confirmation hearing having not taken place by this date). Written reasons were handed down on 18 August 2016.

Issues

The Committee opposed the application on a number of different bases. Firstly, the Committee argued that the Court had no jurisdiction to restructure an insolvent Bermuda company through provisional liquidation proceedings running in tandem with foreign restructuring proceedings in which the Bermuda company was also a party (in effect an abuse of process argument). Secondly, and against the orthodoxy of Bermuda authority, it argued that the Petition was defective, as the decision to wind-up the Company required the prior authorisation of its shareholders. Thirdly, that the Court had no jurisdiction to make a recognition order, and fourthly that the Court had no jurisdiction to order a permanent stay of claims against the Company. From the outset, the Court noted that from a Bermudian law perspective the Equity Committee appeared to have no tangible economic interest in the Company.

Ruling

In relation to the first argument, the Court observed that the jurisdiction to entertain a winding-up petition, presented by an insolvent company which proposed to pursue a restructuring through parallel provisional liquidation proceedings in Bermuda and Chapter 11 proceedings in the US, on the explicit basis that the US proceedings will be primary and those in Bermuda ancillary, had not been seriously questioned for more than 15 years, and in practice had been implemented extensively during that period. On this basis the Chief Justice determined that the use of provisional liquidation proceedings, in aid of insolvent restructuring, was too well established for a first instance Bermudian Court to question its propriety. Furthermore, that Section 170(3) of the Companies Act 1981 gave the Court wide powers to shape the needs of a provisional liquidation in each case. The Chief Justice, citing his

own earlier extra-judicial comments, described this longstanding practice thus:

"One important, usually unarticulated, legal factor which implicitly justifies the Bermuda court ceding primacy to the US Bankruptcy Court, in such cases, is the common scenario that the majority of unsecured creditors of the company involved in the restructuring are bondholders or noteholders under instruments governed by New York law. Under Bermuda conflict of laws rules, the validity and enforceability of the creditors' claims in a traditional liquidation would be governed by New York law as the proper law of the relevant contracts. In such a case, it is not incongruous for the US Bankruptcy Court to play a leading role in adjusting the creditors' rights, all other factors being equal. The creditors' expectations when contracting with the Bermudian company would have been that in the event of the company's insolvency, their contractual rights would fall to be determined under New York law, even if they were merely claimants in a Bermudian liquidation. This approach might not be followed where the US connecting factors are not so strong."

With respect to the second argument, the Company's Byelaws did not mandate shareholder approval for an insolvent winding-up, and lack of (board) authority was not being positively asserted. The Court held that it was well established in first instance decisions that the power to authorise a petition lay with the company's directors. As obiter, the Court commented that it would be questionable whether a company could lawfully contract with its shareholders to deprive management of the power to take steps to protect the interest of third party creditors when the shareholders' economic interest has been extinguished by insolvency.

As to the jurisdiction to make a recognition order, the Court considered in detail the decisions of the UK Supreme Court in *Rubin v Eurofinance SA* [2013] 1 AC 236 and the Privy Council in *Singularis* and noted that neither case directly considered recognition of an order approving a plan. Moreover, while accepting the principles established in those cases, the Court considered that the crucial differentiating factor was that the foreign court lacked *personal* jurisdiction over the shareholders whose rights were being extinguished, and lacked *in rem* jurisdiction to transfer title in shares located in another forum. By contrast, in the present case the Company had submitted to the jurisdiction of the Texas Court, as had all other material parties, and there was no doubt as to personal jurisdiction. Also, the Committee itself was a creature of the Texas Court and had not been appointed to challenge that Court's jurisdiction but to participate on the merits in the Chapter 11 proceedings.

As to the fourth argument that there was no jurisdiction to order a stay, this was soundly rejected. The Court had both an implied power to restrain abuses of process and/or to manage its own processes, and also statutory powers under the Supreme Court Act 1905 and the Companies Act 1981 to impose a stay where it was appropriate to do so. The stay was conditional upon a plan of restructuring being approved by the Texas Court and the effect of the stay would not go beyond the natural consequences of the confirmation order. In any event, the Court considered that if a material change in circumstances did arise, liberty to apply could be invoked.

David Kessaram, Head of Litigation, and Steven White, Senior Associate, represented John McKenna of Finance & Risk Services Ltd, the Provisional Liquidator, in the proceedings.

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