IN THE SUPREME COURT OF BERMUDA

COMPANIES (WINDING-UP)

2003: No. 274

IN THE MATTER OF LORAL SPACE & COMMUNICATIONS LTD.

AND IN THE MATTER OF THE COMPANIES ACT 1981

REASONS FOR DECISION

Date of hearing: April 5, 2007
Date of Reasons: April 18, 2007

Mr. Larry Mussenden, Attride-Stirling & Woloniecki, for the Joint Provisional Liquidators

Introductory

1. On April 5 2007, I made an Order, *inter alia*, appointing the Joint Provisional Liquidators, Michael Morrison and Charles Thresh ("the JPLs"), as Liquidators of the Company without a Committee of Inspection. This was done in the absence of a vote at the first statutory meetings of either creditors or contributories, which meetings are traditionally viewed as a precondition for the appointment of permanent liquidators by virtue of the provisions of section 171 of the Companies Act 1981 prescribe.

2. The affairs of the Company have already been wound-up, or will (if any matters are outstanding) be wound-up pursuant to the Plan made in the Chapter 11 proceedings the company commenced[1] in tandem with the present winding-up proceedings. The JPLs merely sought a permanent appointment in order to apply for a release and, one presumes, to apply for the dissolution of the Company.

3. While there were compelling commercial and logistical reasons for making the order sought, as Counsel pointed out, to give effect to the Chapter 11 Plan pursuant to which the Company's affairs have been reorganised, it seemed to me that the legal issues raised by the application were sufficiently novel to require the provision of short reasons. It is entirely possible that similar orders have in the past been made in other cases, but that the rationale for the approach adopted has not been set out in a reasoned decision.

4. Having considered the implications of the Chapter 11 Plan on the procedure for winding-up the Company at an earlier stage of these proceedings and immediately prior to the present application, however, the legal justification for the appointment of the JPLs as permanent liquidators were sufficiently compelling for

[1] In the United States Bankruptcy Court for the Southern District of New York.

me to decline Mr. Mussenden's offer to seek an adjournment in order to tender further legal submissions in this regard.

The statutory power to appoint permanent liquidators

5. In the ordinary liquidation, it is generally accepted that (a) provisional liquidators must convene first meetings of creditors and contributories within a month after a winding-up order has been made (or such further time as the Court may direct), (b) that the first meetings must resolve whether or not an application should be made to the court to appoint a permanent liquidator, with or without a committee of inspection, and (c) that where neither meeting passes a resolution for an application to be made to the Court to appoint a permanent liquidator, the Official Receiver becomes permanent liquidator by operation of law.

6. These principles are primarily[2] derived from section 171 of the Companies Act 1981:

> **"Appointment of liquidators**
> *171 The following provisions with respect to liquidators shall have effect on a winding-up order being made —*
>
> *(a) if the Court has appointed no other provisional liquidator prior to the winding-up order being made the Official Receiver shall become the provisional liquidator and he or the provisional liquidator appointed by the Court shall continue to act as provisional liquidator until another person becomes liquidator and is capable of acting as such;*
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> *(b) the provisional liquidator shall summon separate meetings of the creditors and contributories of the company for the purpose of determining whether or not an application is to be made to the Court for appointing a liquidator in the place of the provisional liquidator;*
>
> *(c) the Court may make any appointment and order required to give effect to any such determination and, if there is a difference between the determinations of the meetings of the creditors and contributories in respect of the matter aforesaid, the Court shall decide the difference and make such order thereon as it thinks fit;*
>
> *(d) in a case where a liquidator is not appointed by the Court, the Official Receiver shall be the liquidator of the company;*
>
> *(e) the Official Receiver shall be the liquidator during any vacancy;*
>
> *(f) a liquidator shall be described when a person other than the Official Receiver is liquidator, by the style of "the liquidator", and, where the Official Receiver is liquidator, by the style of "the Official Receiver and liquidator", of the particular company in respect of which he is appointed and not by his individual name."*

7. The Court is only empowered to decide any difference between the first meetings of contributories and creditors as to who the permanent liquidator should be. The choice of the liquidator is a power vested in the contributories and creditors, it being implicit that the creditors' views will prevail in an insolvent winding-up because shareholders have no economic interest in the liquidation. Where the Court makes no appointment to give effect to a resolution passed at a statutory meeting, section 171(d) of the Act provides that the Official Receiver "*shall be the liquidator of the company.*"

[2] Section 181 confers the power to decide on the appointment of a committee of inspection, on the first meetings, and confirms the provisions of section 171 in respect of the decision on the appointment of a liquidator other than the Official Receiver. Rule 85(1) prescribes the time within which the first meetings must be convened.

The commercial and pragmatic case against the application of the normal rules

8. The statutory scheme contemplates the Official Receiver becoming liquidator of a company, the affairs of which have not been wound up. Typically, where insufficient liquid assets exist to support the fees of a private liquidator, the first meetings will be unable to vote for a private liquidator, and the Official Liquidator assumes office by operation of law. In such cases, he will likely have become provisional liquidator by operation of law on the making of the winding-up order.

9. Since the affairs of the Company have been wound-up, and the JPLs have been in office for many years, the most cost-effective means of concluding the winding-up is obviously to allow the JPLs to assume permanent office and bring these proceedings to an orderly end. The Official Receiver would be given a burden without being required to satisfy any corresponding public need for oversight on his part. As Mr. Mussenden validly pointed out, as a practical matter the Official Receiver would most likely appoint the JPLs as his agents if he was required to assume office.

10. The only likely practical and commercial result from concluding that the JPLs could not be appointed appears to be that (a) the Official Receiver will be burdened with additional administrative responsibilities distracting him from other necessary public duties and (b) additional costs will be incurred because the JPLs as the Official Receiver's agents would have to additionally liaise with him over and above the limited functions it is contemplated they will carry out under the Plan.

Does the Plan purport to expressly or impliedly modify the operation of section 171 of the Companies Act?

11. On July 11, 2005, Wade-Miller J ordered that "*subject to confirmation by the US Bankruptcy Court of the …Plan….the JPLs be and are hereby authorised to exercise…their powers, for the purpose of implementing the Plan…*" The US Court approved the Plan on August 1, 2005.

12. The Disclosure Statement which accompanied the Plan observes in salient part as follows:

> " *The Bermudian court granted the JPLs the power to oversee the continuation and reorganization of the Bermudian Debtors' businesses under the control of their boards of directors and under the supervision of the Bankruptcy Court and the Bermuda Court…All claims will be dealt with in accordance with the procedure under the Plan. The Bermudian debtors will be put into liquidation as soon as practicable after the occurrence of the Effective Date of the Plan…*"

13. Clause 4.6 of the Plan provides in relation to the Company that: "*all…Equity Interests shall be cancelled and extinguished.*" Clause 4.4 provides that each unsecured creditor of the Company shall receive, in full satisfaction of its claim, its "*Pro Rata Share of the New Loral Common Stock Balance.*" Clause 5.2 (a) provides for, on the Effective Date, all assets of the Company to be transferred to New Loral. Clause 5(2)(d) provides for the dissolution of any Debtor, subject to the consent of the Creditors Committee, without further order of the Bankruptcy Court. It is clear on the face of the Plan that the Company's affairs are to be fully wound-up, and that all liabilities to creditors and shareholders are to be extinguished by the time the provisional liquidation comes to an end. The JPLs are given releases under the Plan.

14. On July 16, 2006 I ordered that the Company be wound up and that the then JPLs should be appointed with unlimited powers, thus ending any role for the board of directors. This was consistent with the fact that the Plan became effective on November 21, 2005, the shareholders' interests had been extinguished and the restructuring process was substantially complete.

15. The Plan explicitly contemplates that the JPLs or other liquidators in their place will complete the winding-up process, in language that implicitly suggests that the JPLs are authorised to conclude the winding-up process after a winding-up order is made. Clause 6.6(e) is headed "*Costs of Liquidation*." It establishes a "*Bermuda Liquidation Fund*". The clause goes on to state as follows:

> "*The Bermuda liquidation Fund will… be used to fund the liquidation of the Bermudian Debtors, provided, however, that* **any provisional liquidators and, subsequently, liquidators** *of the Bermudian Debtors will be required to carry out only their statutory obligations under Bermuda law.* **In the event that , following the making of the winding up orders in respect of the Bermudian Debtors, the JPLs do not act as provisional liquidators (and, subsequently, liquidators)***, of the Bermudian Debtors, the JPLs shall, upon the making of the winding up orders, transfer to* **such other person(s) so acting as provisional liquidators (and, subsequently, liquidators)**…" [emphasis added]

16. In my view, the Plan clearly contemplated that (a) the Company would have no shareholders or creditors by the time the winding-up order was made, and (b) that the provisional liquidators appointed when the winding-up order was made, in the event the present JPLs, would in due course be appointed permanent liquidators to complete the winding-up process. The creditors of the Company, in approving the Plan, effectively agreed that the JPLs should be appointed as liquidators, even though the subtle modifications of the statutory Bermudian insolvency regime were not explicitly spelt out. This is because the Plan explicitly contemplated that whoever became provisional liquidator on the making of the winding-up order would subsequently become permanent liquidators.

Can section 171 of the Companies Act 1981 be contracted out of by the creditors of an insolvent Bermudian company through a Chapter 11 plan or a scheme of arrangement?

17. The Judicial Committee of the Privy Council has recently confirmed that a scheme of arrangement under the law of the place of incorporation of a company whose shareholder rights have been extinguished under a Chapter 11 plan or reorganisation is not necessary in order for the plan to be given effect to under local law: *Cambridge Gas Transport Corp-v- The Official Committee of Unsecured Creditors (of Navigator Holdings PLC and others)* [2006]3 WLR 689 at 696-697. So this Court possessed the jurisdiction to assist the US Bankruptcy Court by giving effect to the Plan. As Lord Hoffman observed:

> "*At common law….the domestic court must at least be able to provide assistance by doing what it could have done in the case of a domestic insolvency.*"[3]

18. Although the central question in the *Cambridge Gas Transport Corp.* case was the effect of a Plan on the shareholders of an insolvent company, the reasoning seems to apply with equal force to this Court's jurisdiction to assist a US Court by giving effect to the Plan in general terms. This should not be taken as suggesting that it may not be desirable in other cases for schemes of arrangement to be formally implemented under Bermuda law to either (a) meet the contingency that certain creditors may not be bound by the US Plan[4] or (b) to deal in appropriate detail with unique Bermuda law issues which cannot appropriately be dealt with under the Plan.

[3] At pages 696-697.

[4] The requisite majorities in terms of value of claims for approving a scheme is three-quarters, higher than the two-thirds which I understand is required under US bankruptcy law.

19. So the crucial question becomes whether, in a Bermudian liquidation, this Court could approve a scheme of arrangement under section 99 of the Companies Act 1981 providing for the JPLs to serve as permanent liquidators in circumstances where it was impossible to convene the first meetings of creditors and contributories, post-winding-up, to approve their appointment at that stage. In the present circumstances it is clear that the Court would have ample grounds for exercising its discretion in favour of sanctioning a scheme modifying the effect of section 171 of the Companies Act 1981 assuming the jurisdiction to do so exists.

20. It is well settled that even statutory insolvency rights as fundamental of the *pari passu* principle of distribution can be varied through a scheme of arrangement. This point may be illustrated by reference to the judgment of Sir Richard Scott V-C in *Re BCCI (No. 10)* [1997] Ch 213. When dealing with the question of whether English statutory insolvency rules should be modified in the context of English ancillary liquidation proceedings in relation to a foreign incorporated company the Vice-Chancellor observed:

> "*One of the features of the contribution agreement, as it then stood, was that it contained a provision barring from participation in the funds being provided by the Abu Dhabi majority shareholders, any creditors who declined to release the majority shareholders from damages claims. To that extent, therefore, the contribution agreement effected a variation in the pari passu scheme established in this jurisdiction by the Insolvency Act 1986 and its statutory predecessors. It was contended by a group of creditors who objected to the contribution agreement that, inter alia, the court had no power, save by a formal scheme of arrangement under section 425 of the Companies Act 1985, to authorise a distribution of assets in a winding up otherwise than in accordance with the statutory pari passu scheme. Sir Donald Nicholls V.-C. said, simply:*
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> > *'I do not agree. The liquidators' powers under, paragraphs 2 and 3 of Schedule 4 to the Insolvency Act 1986, exercisable with the approval of the court, are wide and they are wide enough to cover this case.'*
> >
> > *The objectors took this ultra vires point (with other points) to the Court of Appeal*[5]*. The appeal was dismissed on 17 July 1992. As to the ultra vires point, Dillon L.J. said:*
> >
> > *'As I see it, in a liquidation there can be a departure from the pari passu rule by a scheme of arrangement under section 425; but, equally, there can be a departure from the pari passu rule if it is merely ancillary to an exercise of any of the powers which are exercisable with the sanction of the court under Part I of Schedule 4 to the Insolvency Act 1986.'"*

21. Part 1 of Schedule 4 of the 1986 lists powers that liquidators may exercise with the sanction of the Court or the liquidation committee and is the counterpart of section 175(1) of the local Companies Act 1981. The Vice-Chancellor goes on to point out that the relevant variation of the pari passu principle was held contrary to Luxembourg law and that the agreement approved by the Court of Appeal was subsequently withdrawn. This does not, however, undermine the principle that statutory insolvency rules may be modified either (a) through a scheme of arrangement or (b) through the exercise of those powers of a liquidator which require sanction of the court.

22. It is true that the substantive decision in *Re BCCI (No.10)* does suggest that if the Bermuda liquidation were to be characterised as an ancillary liquidation, then no power to modify the statutory regime absent a scheme of arrangement would exist. This view is apparent from the conclusions reached by the Vice-Chancellor on the central question before him:

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[5] *Bank of Credit and Commerce International S.A. (No. 3), In re* [1993] B.C.L.C. 106; [1993] B.C.L.C. 1490, C.A.

> *"I have already observed that the source of the discretionary power to disapply at discretion parts of the statutory insolvency scheme can be found neither in statute nor in any inherent common law power of the courts. There is, however, another way in which powers can become vested in the courts, namely, by accretion of judicial decisions. In the early decisions in which the English liquidations were described as "ancillary," no attempt was made to spell out the effect of placing that description on the winding up in question or to analyse the source of the dispensing power that the court was exercising. Without, apparently, any such analysis, the situation seems simply to have come to be accepted that in an appropriate case, of which the paradigm would be a company in liquidation in its country of incorporation but against which a winding up order had been made in this country, the court could direct that the winding up in this country be treated as "ancillary." The implication of this direction was that at some stage in the liquidation the court would authorise the English liquidators to transmit the assets they had got in to the principal liquidators. Mr. Geering and Mr. Brisby emphasised that, without that implication, the description of the liquidation as ancillary becomes fairly meaningless. I agree and consequently accept that the implication to which I have referred should be read into the numerous judicial dicta in which the concept of an ancillary liquidator has been endorsed. In Sir Donald Nicholls V.-C.'s order of 12 June 1992 in this liquidation, the direction to be implied in the earlier cases was spelled out in express terms. And his order was approved by the Court of Appeal.*
>
> *The accumulation of judicial endorsements of the concept of ancillary liquidations have, in my judgment, produced a situation in which it has become established that in an "ancillary" liquidation the courts do have power to direct liquidators to transmit funds to the principal liquidators in order to enable a pari passu distribution to worldwide creditors to be achieved. The House of Lords could declare such a direction to be ultra vires. But a first instance judge could not do so and I doubt whether the Court of Appeal could now do so.*
>
> *But the judicial authority which has established the power of the court to give, in general terms, the direction to which I have referred has certainly not established the power of the court to disapply rule 4.90 or any other substantive rule forming part of the statutory scheme under the Act and Rules of 1986.."*

23. This analysis would be a potential impediment to the modification of Bermuda's insolvency regime in ancillary liquidation proceedings commenced in respect of an overseas company, but in my view need not be considered in the context of parallel proceedings where the crucial question is whether provisions of a Chapter 11 Plan should be given effect to in relation to a Bermudian company. In this context it is now clear in light of the *Cambridge Gas Corp.* decision of the Privy Council which binds this Court, that foreign orders can be recognised and enforced particularly in circumstances where the same result could be achieved through a scheme of arrangement under Bermudian law. As Lord Hoffman observed [6]:

> *"In the present case it is clear that the New York creditors, by starting proceedings to wind up the Navigator companies and then proposing a scheme of arrangement under section 152 of the Companies Act 1931, could have achieved exactly the same result as the Chapter 11 plan… The jurisdiction is extremely wide. All that is necessary is that the proposed scheme should be a "compromise or arrangement" and that it should be approved by the appropriate majority. Why, therefore, should the Manx court not provide assistance by giving effect to the plan*

[6] [2006] 3 WLR 689 at 697.

without requiring the creditors to go to the trouble of parallel insolvency proceedings in the Isle of Man?"

24. The instant case for giving effect to the Plan is even stronger because parallel insolvency proceedings have been commenced in Bermuda the missing ingredient being a Bermudian scheme of arrangement to mirror the Plan. The only obvious potential argument that might be raised against modifying the application of section 171 of the Companies Act is that this is not a provision relating to creditors' rights in relation to which section 175 of the Act would potentially apply. This argument would be germane because the Court of Appeal decision in *Re BCCI (No. 3)* arguably implies that the sort of insolvency rules which may be modified pursuant to a scheme are those which the liquidator could modify with court sanction under section 175(1). Section 175 provides:

> "*(1) The liquidator in a winding-up by the Court shall have power, with the sanction either of the Court or of the committee of inspection —*
>
> *(a) to bring or defend any action or other legal proceeding in the name and on behalf of the company;*
>
> *(b) to carry on the business of the company so far as may be necessary for the beneficial winding up thereof;*
>
> *(c) to appoint an attorney to assist him in the performance of his duties;*
>
> *(d) to pay any classes of creditors in full;*
>
> *(e) to make any compromise or arrangement with creditors or persons claiming to be creditors or having or alleging themselves to have any claim, present or future, certain or contingent ascertained or sounding only in damages against the company, or whereby the company may be rendered liable;*
>
> *(f) to compromise all calls and liabilities to calls, debts and liabilities capable of resulting in debts, and all claims, present or future, certain or contingent, ascertained or sounding only in damages, subsisting or supposed to subsist between the company and a contributory or alleged contributory or other debtor or person apprehending liability to the company, and all questions in any way relating to or affecting the assets or the winding up of the company, on such terms as may be agreed, and take any security for the discharge of any such call, debt, liability or claim and give a complete discharge in respect thereof.*"

25. If there is a linkage between the scope of the power to make compromises under section 175(10) and the power to vary the usual insolvency regime under a scheme sanctioned under section 99 in respect of an insolvent company, the potential scope of compromises under an insolvent scheme is extremely wide. This is because section 175(1)(f) permits compromises with the requisite sanction in respect of "*all questions in any way relating to or affecting … the winding up of the company*". Having regard to these broad provisions, it is to my mind beyond serious argument that creditors of a Bermudian company could validly, under a scheme of arrangement entered into while the company was in provisional liquidation, agree as follows.

26. In circumstances where the affairs of the insolvent company were to be substantially wound up save for administrative formalities by the JPLs before a winding-up order was made, creditors could agree that their statutory right to choose the permanent liquidators at a first statutory meeting under section 171 would be modified by the creditors exercising this right at an earlier stage, namely at the meeting to vote on the scheme. This right would be exercised earlier because under the scheme all creditors' rights would be extinguished by the time a winding-up order was made. The choice made would essentially be that (a) the

JPLs would be *de facto* permanent liquidators and (b) either the JPLs or such other provisional liquidators as the court might appoint would become *de jure* permanent liquidators for the largely formal purposes of concluding the winding-up and dissolution of the company.

Conclusion

27. For the above reasons I appointed the JPLs as permanent liquidators of the Company without the vote of a first meeting of creditors convened under section 171of the Companies Act 1981, thereby giving further effect to the relevant provisions of the Chapter 11 Plan approved by the company's creditors in accordance with US Bankruptcy law.

Dated this 18th day of April, 2007

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KAWALEY J.