Maneuvering Through the Complex World of Cross-Border Distressed Transactions - By Michael Goodman and T.J. Haas, SSG Capital Advisors, L.P. - *Financier Worldwide*

Selling a company in distress or the subsidiary of a company in distress can be complicated even under the cleanest and most straightforward of circumstances. However, when assets or subsidiaries reside in more than one country, the level of complexity can soar, making the transaction more difficult for even the most savvy dealmaker. Buyers and sellers often have to quickly familiarise themselves with the nuances of bankruptcy or receivership proceedings that are unique to the country that the subsidiary or division is located.

As US-based investment bankers specialising in distressed situations, SSG Capital Advisors, L.P. ("SSG") is often referred into transactions in which a US parent company requires immediate liquidity through the sale of subsidiaries or divisions that are located both in the US and abroad. Usually, the driving force behind the structure of such transactions is the balance sheet of both the US parent and the non-US subsidiary. The following are three scenarios that underscore the varying circumstances and resultant options available for crossborder distressed divestitures.

In 2002, SSG was retained by a public company in the US that was operating under a forbearance agreement with its lenders that mandated a near term liquidity event to significantly reduce bank debt and free up working capital. The crown jewel of the business was a healthy French subsidiary, Terraillon Holdings, which sold bathroom and kitchen scales worldwide. It was determined that realisation of market value for the subsidiary would precipitate a paydown of the bank debt sufficient to preclude a bankruptcy proceeding in the US. By keeping the US company out of bankruptcy, and the fact that Terraillon was not itself overleveraged, we were able to divest Terraillon in a straightforward sale of shares to a strategic purchaser.

The situation becomes more complicated when the US parent is in bankruptcy. Such was the case with Country Home Bakers, a USbased commercial bakery that operated a UK-based subsidiary. The subsidiary, Readi-Bake Ltd., had maintained an impressive track record of growth and profitability over the last several years. Further, it was the capital structure of the parent rather than that of Readi-Bake which prompted the bankruptcy filing. Since the shares of Readi- Bake were an asset of the bankrupt US parent, the sale was transacted under Section 363 of the US Bankruptcy Code, whereby a buyer is identified and a definitive agreement is executed. However, the offer is still subject to higher and better bids during a Section 363 auction. A challenge for the investment banker in such a situation is educating foreign buyers of the complexities of the US bankruptcy process. Experience has shown that buyers who retain local bankruptcy counsel earlier in the process often have the best opportunity to position themselves as the ultimate purchaser.

The level of complexity multiplies significantly when circumstances warrant that both the parent and the foreign subsidiary are subject to some type of insolvency proceeding. This scenario is often impelled when it is likely that senior lenders will be impaired and they either lend directly to both the domestic and foreign companies or have debt that is cross-collateralised between the two entities. To maximise recovery, insolvency proceedings are often necessary to subordinate claims that would otherwise be assumed by a purchaser, including trade payables and pension liability.

Although concurrent insolvency proceedings serve to subordinate such claims, they also surface and mobilise additional stakeholders that can impede a preferred transaction. For example, the fiduciary responsibility of an administrative receiver in a receivership proceeding is to maximise value of that specific entity rather than that of the estate as a whole. The administrative receiver may not be inclined to support a sale of the assets in their entirety unless they are certain that this sale also maximises the value of the specific assets on a stand alone basis. To combat this conflict, a comprehensive marketing process is required.

If the seller can align all stakeholders behind a transaction, negotiate a reasonable purchase price allocation and warrant that the business has been adequately marketed, it is likely that a unified group of stakeholders can convince a bankruptcy judge, trustee or receiver that a certain transaction is the path to value maximisation. It is critical that the parties in a transaction resolve these issues early since contentiousness in a process can give judges, trustees or receivers pause in approving a deal. One potential negative outcome is that the distinct fiduciaries in separate countries stagger the timing of the sale of the different entities, which often leads to the suppression of value. Staggered timing can particularly adversely affect value when the two entities have an integrated operational relationship.

Ultimately, the only way to deal with issues arising from distressed sale transactions in multiple countries is to go into the process with your eyes wide open. A thorough marketing process coupled with the retention of professionals well versed in the insolvency rules of each local venue can help prevent errors that can drastically reduce recovery for all stakeholders.

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