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Cross-Border Case Study: Resolving Inter Company Claims between Corporate Group Companies in Insolvency Proceedings in Different Jurisdictions



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however, that the company was no longer able to meet its payment obligations and that it would be necessary to file an insolvency petition in Germany. On that same day, the German Court appointed Mr. Volker Böhm of Schultze & Braun GmbH, as the preliminary insolvency administrator. After his appointment, Mr. Böhm continued the business operations of the insolvent company with an aim of selling the debtor's assets. On February 28, 2012, the German Court formally opened the insolvency proceedings for SMAG and appointed Mr. Böhm permanent Insolvency Administrator.

Introduction

Solar Millennium, A.G. ("SMAG"), was a global solar company registered in Erlangen, Germany, founded in 1998, and listed on the Munich Stock Exchange. SMAG owned subsidiaries in Germany, Spain, the United States, China, and other locations and focused on large scale project development of solar power plants based on CSP technology. SMAG successfully developed power plants in Spain and Egypt and had begun to develop or had investigated developing plants in the United States, Asia, Africa, and the Middle East.

As of April 30, 2011, SMAG had total assets of approximately €477.8 million (mostly its subsidiaries' project rights) and liabilities of about €394.5 million, of which over €210 million or over 53%, was due on account of outstanding bonds. These bonds were sold to over 16,000 mostly-German individual investors. SMAG also has some minor bank debt and general unsecured claims held by vendors and other suppliers in Germany.

The Federal Republic of Germany was one of the first leading industrial nations to promote renewable energy sources, which reportedly created many jobs in Germany. In the last few years, however, several major German solar companies have gone bankrupt due to a reduction of government subsidies and global competition, most notably from China.

SMAG also faced delays, technological problems in various countries, and reduced support from its strategic partner in the development of SMAG's US power plants. As a result, SMAG began to evaluate strategic options including the sale of solar projects. SMAG's Executive and Supervisory Boards determined on December 21, 2011,

As SMAG's US-based subsidiary, Solar Trust of America, LLC ("STA"), represented by professional and independent management, ran out of liquidity, it filed voluntary petitions for relief under Chapter 11 of the Bankruptcy Code in Wilmington, Delaware, obtained post-petition financing and moved to sell their assets. With the possibility of a sale, Mr. Böhm filed a Chapter 15 Petition in Delaware with respect to SMAG. The Delaware Court entered an order granting Mr. Böhm relief and recognition under Chapter 15. One of the main reasons Mr. Böhm filed a Chapter 15 was to ensure he could participate in the auction of STA's assets and ensure SMAG's creditors were not harmed by that sale. Another important reason was that the former CEO of SMAG had filed a lawsuit in the state court in California seeking over US\$250 million from SMAG, STA, and certain other parties. Volker Böhm believed it necessary to extend the automatic stay of the German insolvency proceeding to the US in order to protect SMAG's assets in the US.

Sale of the US Entities' Assets and Disputes Regarding Letters of Credit

In its Chapter 11 auction process, STA sought to sell the rights to develop its solar farms (referred to as the Blythe and Palen Projects) in the southwestern part of the United States. SMAG had loaned STA over \$100 million and had arranged for the issuance of letters of credit on STA's behalf to allow STA to pursue its solar development projects. Mr. Böhm asserted that SMAG caused at least 16 letters of credit, totaling approximately \$14.2 million of which about \$9.8 million was outstanding, to be issued on behalf of several of STA's subsidiaries for the benefit of third party creditors of those entities. SMAG had

¹ Messrs. Martin and Esser were legal counsel to Mr. Böhm for his Chapter 15 case in Delaware and with respect to the STA Chapter 11 cases also in Delaware. The views presented in this article are those of the authors and have not been endorsed by or authorized by Mr. Böhm.

collateralized these letters of credit with cash and if the L/Cs could be replaced or released as part of the STA sale, those funds would be available for SMAG's German creditors. Since SMAG issued some of these letters of credit with respect to the Palen and Blythe Projects, Mr. Böhm filed a limited objection to STA's sale to ensure the letters of credit were not sold or used to benefit STA's creditors to the detriment of SMAG's creditors.

Recognizing that his presence at the auction might enable him to negotiate a resolution to his Objection, Mr. Böhm, travelled to Wilmington to be present at the auction. This proved worthwhile because at the all-day auction, Mr. Böhm was able to negotiate with the STA and its US Creditors' Committee (the "STA Committee") for the replacement of the letters of credit in a way that allowed the cash collateral supporting them to be released to SMAG. In exchange for this, SMAG agreed that it would subordinate a portion of its intercompany claims to the general unsecured creditors of STA. This agreement was approved by the Delaware Bankruptcy Court as part of the approval of the sale of the Blythe and Palen Projects.

The Parent Company Claims and the Plan of Liquidation

Having resolved issues related to the letters of credit, Mr. Böhm (on behalf of SMAG and certain of its German affiliated companies) also filed proofs of claim in the STA case in an aggregate, non-duplicative amount of approximately \$118 million. STA then filed a Plan of Liquidation and a Disclosure Statement that described that plan, including provisions that sought to substantively consolidate the entire USA corporate group and subordinate all of SMAG's claims to the claims of STA's creditors. Mr. Böhm objected to the Disclosure Statement.

The STA Committee then filed a Complaint against Mr. Böhm and SMAG, alleging that the loans made by the SMAG entities should be recharacterized as debt, contractually or equitably subordinated, or avoided. The Committee also asserted a claim for alter ego against SMAG and claimed that SMAG should be liable for all of STA's debts. Mr. Böhm considered this Complaint a violation of the Chapter 15 automatic stay and demanded that the Complaint be withdrawn.

The STA Committee did not withdraw the Complaint and all parties were faced with potentially extensive and very costly legal proceedings further reducing STA's available and limited cash resources. However, the STA Committee, STA, and Mr. Böhm were able to resolve Mr. Böhm's Disclosure Statement Objection when the Debtors and the STA Committee agreed to a meeting to discuss all open issues and to share information regarding substantive consolidation. The Delaware Bankruptcy Court approved this agreement and ordered that Mr. Böhm could visit the United States but could not be served with process of the STA Committee's complaint. After this formal resolution, the parties then agreed to mediation in Wilmington, Delaware to be conducted by former Delaware Judge Joseph A. Farnan, III.

Resolution through Mediation

In preparation for the mediation, the parties submitted

confidential mediation statements to the mediator and provided him with documents and exhibits in support of their positions. Mr. Böhm again travelled to Wilmington, Delaware for the mediation, this time bringing with him an accountant he hired to provide him with professional advice, his German legal counsel, and former SMAG employees that could provide factual background during the mediation.

The mediation lasted an entire day with the parties engaged in intense discussions over the merits of SMAG's claims, the issues related to the plan of liquidation STA had proposed, and other economic and legal issues. At the end of the day, while the parties had exchanged some offers, they were not able to negotiate a resolution, and so SMAG left the mediation. Overnight and the next morning, with the help of the mediator, the parties decided to try again on a second day before Mr. Böhm and his professionals had to return to Germany. In a tense, all hands on meeting, the parties stated their positions, and then with the guidance of the mediator, the parties structured a framework that they thought might form the basis for a resolution. As part of this structure, the creditors of STA and SMAG would agree to share proceeds from the liquidation of STA in a weighted fashion that would initially favor STA's creditors but would favor SMAG at later stages. The parties were not able to bridge the gap, however, and the mediation concluded without a resolution.

The parties did not give up and after the mediation, continued to negotiate and exchange ideas and offers for a resolution. They ultimately were only within a few hundred thousand dollars of each other and a final hearing on the liquidation plan was looming. In a final effort, the parties requested a status conference with the Delaware Judge presiding over STA's Chapter 11 and SMAG's Chapter 15 cases, after which the parties participated in a final round of negotiations in chambers with the presiding Judge. As a result of this meeting, the parties were able to agree to a resolution consistent with the structure they had outlined at the mediation but that was economically acceptable to all parties. Thereafter, the Delaware Bankruptcy Court approved the settlement on SMAG's claims, confirmed the Plan of Liquidation, and SMAG and the former STA creditors are now on a liquidation advisory board working with a liquidation trustee to collect remaining assets for the benefit of STA's and SMAG's creditors.

Conclusion

The lessons from the SMAG Chapter 15 case and the Chapter 11 cases of its US subsidiaries are that when there are multiple insolvency proceedings in different jurisdictions there are certain to be cultural and legal impediments to an easy resolution. It is likely that parties will enter the cases with complete distrust, dispute ownership of assets and dispute whether claims between companies in the same corporate group are legitimate. At the end, however, it is possible to cooperate in order to reach efficient outcomes that mutually benefit all parties. In order to resolve the issues and reach positive results, professionals must work to bridge cultural gaps and think creatively in a way that permits maximization of value of the corporate group for all creditors. 🌐