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# *Investigating and Recovering Assets When the Liquidator has Limited Financial Means*

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Liquidators will consider litigation funding where estate assets are limited. In offshore cases there are generally no 'bricks and mortar' or other assets located in the offshore jurisdiction. Other assets are generally located elsewhere and an extensive investigation might be required before their repatriation. Similarly, a Fund's books and records are often onshore with the Fund's investment manager, administrator or other service providers. These records are vital for a Liquidator to identify property, investigate the financial position and the circumstances leading to the failure of the company and then to identify potential causes of action to recover property, particularly in cases where fraud is evident.

If service providers are not co–operative, which is often the case, the offshore Liquidator will need to deploy significant resources, including seeking recognition of the liquidation onshore, in an effort to obtain the books and records, investigate and recover assets. These unique characteristics make it more difficult for an offshore liquidator to discharge his duties than is the case for an onshore officeholder with assets in hand.

In any case, onshore or offshore, a liquidator has several options to fund the making of claims where assets are scarce.

## What if there is Insufficient Property to Fund the Liquidation?

In the offshore environment assets may be identified early but recovery may be time consuming. Foreign recognition of the liquidation might be a necessary precursor to asset recovery. Additional expense might arise if a party objects or further action is necessary to enforce production of the books and records.

The Liquidator can opt to defer his fees until such time as any identified assets are realised. In other situations there may be insufficient assets at the outset of the liquidation and the Liquidator will need to decide how to fund proceedings to recover the books and records.

If the Liquidator has identified potential wrong-doing in his preliminary investigation, but lacks liquid assets to fund further work, such as a detailed forensic tracing exercise, the Liquidator may explore alternative sources of funding rather than bearing the risk of incurring irrecoverable fees and expenses.

## Alternative Funding Options

The Liquidator may consider turning to creditors or independent third party funders ("Funders").

These alternatives are broadly similar. The Funder advances the Liquidator a non–recourse loan to fund the investigation and in some cases, the general conduct of the liquidation. Such funding is high risk to the Funder as the outcome of the investigation cannot be guaranteed. The Funder will seek a risk based 'reward' for providing funding to investigate and pursue claims from any subsequent recoveries to offset that risk. The Funder may also require the Liquidator to bear some risk, for example making some fees contingent, to align their economic interests with the overall outcome. The Liquidator may require an uplift to his usual rates to reflect the risk he is bearing.

## Funding Agreements with Creditors and Third Parties

Funding agreements are dynamic. They can impose a range of rights and obligations on the Liquidator and Funder. Negotiating a funding agreement can be time consuming, particularly if creditors provide the funds. Creditors will usually not have had any prior experience of funding a liquidation. An independent third party funder will have developed expertise from previous cases. He is generally more able to move quickly to agree any funding proposal.

The Liquidator will need to manage the expectations of the Funder and align the proposed rate of return on monies advanced with Court precedent and expectations. Syndicated funding, particularly from creditors, will further complicate the process as these parties may have widely varying expectations and requirements.

## Seeking Court Approval of the Funding Agreement

It is prudent for the Liquidator to obtain court blessing of any funding agreement before formally adopting it. The Liquidator will need to consider a variety of issues when negotiating a funding agreement, including;

- the potential for adverse cost orders if unsuccessful;
- whether the return sought by the Funder on their advances is an appropriate reward for risk and is in the best interests of the Fund; and
- in the case of creditors providing funding, how their claims rank against their risk premium.

If litigation to pursue a cause of action starts, the Liquidator will need to consider if the proposed funding is sufficient to see the litigation through until completion. If not, he will need a mechanism to seek additional funds.

The Liquidator will be wary of entering into any proposed

agreement whereby the Funder seeks to exert control over the Liquidator's investigation or any litigation to protect its economic interest. A Liquidator will recognise his duties to the court and be unlikely to seek approval of any funding agreement that affords the Funder the ability to select which causes of action should be commenced, settled or discontinued. It will be necessary for the Liquidator to balance the Funder's competing interests with that of the Estate and his obligations as an officer of the Court. The terms of the funding agreement must be lawful and in accordance with public policy in both the offshore and onshore jurisdictions otherwise there is risk that the offshore Court will not sanction the agreement. Once the agreement is approved, it may also be scrutinised by the onshore Court.

### Contingency Fee Agreements

If the Liquidator has identified causes of action but has insufficient funding to proceed to litigation an alternative to a funding arrangement may be a Contingency Fee Agreement ("CFA") with legal counsel. CFAs have been prevalent in the United States and the United Kingdom for some time.

Recent legislation changes in the United Kingdom coming into effect on 1 April 2013 also allow for Damages Based Agreements.

In most circumstances, a Liquidator will only consider this option if he has assets available to meet his costs and any out of pocket expenses.

CFA's may also be considered where the Liquidator has sufficient assets to pursue causes of action, but the Liquidator looks to "hedge his bets", preserving at least part of the pool of assets for creditors and sharing the risk with contingency fee counsel.

### Nature of Contingency Fee Agreements

CFAs are characterised by counsel retaining an interest in any damages awarded if successful, usually a predetermined percentage. It aligns counsel's interests with that of the Liquidator and the Estate, to maximise recoveries. The Liquidator and counsel will want to address what impact, if any, potential indemnity claims may have on the assets of the estate including any recoveries.

Before a Liquidator retains counsel on a contingent fee basis, they may consider seeking the offshore Courts sanction on the proposed CFA. The Liquidator would need to demonstrate, *inter alia*, that he had legitimate, meritorious, causes of action that were likely to be successful.

The Liquidator must retain control of the litigation, including any right to accept settlement offers or discontinue proceedings. The Court will seek to be the ultimate adjudicator of any disputes that might arise between the Liquidator and counsel with respect to the CFA. The CFA must also abide by the public policy and legal principles of the jurisdiction.

### Conclusion

An offshore Liquidator might be willing to conduct his preliminary investigation into the financial affairs of a Fund and circumstances of fraud speculatively, if there appeared to be assets which might be readily available to cover the fees and expenses incurred in conducting these steps, and provide additional recoveries for the benefit of the estate.

If no such property exists and the Liquidator has identified potential claims which warrant further enquiry, he might approach creditors or third parties to fund either or both further enquiries or the entire liquidation. These creditors and third parties can also be approached to fund litigation of a cause of action. Engaging counsel on a CFA basis is an alternative to funding litigation, including in cases where the Liquidator wants to spread the risk of pursuing claims and to preserve the assets of the estate, with the prospect of sharing the upside in a successful claim with legal counsel and the estate. However in these circumstances the Liquidator will need assets to meet his reasonable costs and out of pocket expenses.

## *INSOL Fellows Participate at ARIL Conference in Montreal, Canada*

During lunch at our INSOL Fellowship Course of 2012 in Miami, a group of international Fellows, comprised of Jean Baron (France), Allan Nackan (Canada), Paul Keenan (USA) and Rodrigo Callejas (Guatemala) sat down with Dr. Janis P. Sarra to discuss the lecture just given by Evan D. Flaschen of Bracewell & Giuliani, regarding cultural matters in insolvency.

Evan started his lecture with a challenging question to the non-US Fellows who were part our very diverse group: "*What do you think of Americans (US nationals)? What is our stereotype?*" Silence invaded the room for 30 seconds until our intrepid Fellow from Nigeria weighed in. Thereafter, Fellows from Europe, Central and South America joined the conversation. It was a rich discussion and after ten minutes, Mr. Flaschen intervened, illustrating how our cultural roots influence the way countries approach insolvency and its legislation.

During the lunch break, Dr. Sarra proposed the wonderful idea that we collaborate on a research paper dealing with the impact of cultural matters on cross-border workouts. If successful, it could be included in the "*Annual Review of Insolvency Law*" compilation, and presented during the conference in February 2013.
Allan Nackan assumed the daunting task of defining the scope of the paper and chasing each of the participants to review, discuss, edit, reference and complete a paper that was approved by the editors and published in the *Annual Review of Insolvency Law 2012*. The entire group travelled to beautiful and extremely cold Montreal to present our paper.

The paper focuses on the collaboration, cooperation and the importance of culture factors in cross-border workouts and identifies distinguishing factors that might impact outcomes. We explore different examples from Canada, U.S., Mexico, Guatemala, Colombia and Europe… contrasting the different issues and experiences that demonstrate how our cultural baggage impacts restructuring and insolvency, and alerting as to how we may deal with those issues in advance.

We concluded: ***"… cross-border workouts ultimately require successful management of people. This reality necessarily requires that practitioners pay really close attention to unique personalities and motivations, which are all driven by cultural factors. Ignore these cultural differences at your own peril!"***

A copy of the paper can be obtained by contacting one of the writers.