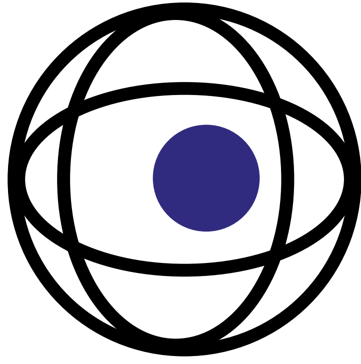

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INSOL Europe Guidance Note

on the Implementation of Preventive Restructuring Frameworks under EU Directive 2019/1023

Procedural features

Barry Cahir & Michael Quinn

November 2020

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Table of Contents

Foreword 5

Introduction by the authors 6

Defined Terms 7

I. PROCEDURAL FEATURES AND GOVERNANCE MATTERS 8

II. CONFIRMATION BY JUDICIAL OR ADMINISTRATIVE AUTHORITY 8

III. JUDICIAL OR ADMINISTRATIVE? 9

IV. MEASURES COMMON TO RESTRUCTURING AND INSOLVENCY 14

Foreword

It is with great pleasure that INSOL Europe presents the third in a series of Guidance Notes on the Implementation of Preventive Restructuring Frameworks under EU Directive 2019/1023 on Restructuring and Insolvency.

In March 2019, during Alastair Beveridge's presidency, the Council of INSOL Europe launched a "Directive Project" with the specific objective of preparing a helpful guide for legislators in the Members States who are in the process of turning the EU Directive into updated or brand new national legislation.

As you will be aware, the objectives of INSOL Europe are to take and maintain a leading role in European business recovery, turnaround and insolvency issues, to facilitate the exchange of information and ideas amongst its members and to discuss business recovery, turnaround and insolvency issues with official European and other international bodies who are affected by those procedures.

As the leading pan-European association of practitioners, academics and judiciary within the field of insolvency and restructuring, and whose members have between them thousands of years of experience, INSOL Europe is well-positioned to take a close look at and provide a pan-European perspective on those tools which would be beneficial in delivering successful restructurings and those tools which may be counter-productive.

The first Guidance Note deals with **Claims, Classes, Voting, Confirmation and the Cross-Class Cram-Down.** The main authors of the first Note are **Adrian Thery** and **Tomas Richter**.

The second Guidance Note deals with **Stay of Individual Enforcement Actions**. The main author of the second Note is **Ben Schuijling**.

This third Guidance Note deals with *"Procedural features"***.** The main authors of this Note are **Michael Quinn** and **Barry Cahir**.

It is our hope that this Guidance Note, will be considered to be a significant and useful contribution to enhancing the harmonization of the pre-insolvency restructuring regimes across the Member States. It is our sense that, in the wake of the unfolding Covid-19 pandemic, the restructuring frameworks envisaged by the Directive might need to be in place rather sooner than originally envisaged by the EU legislator. We hope that our Guidance Notes will assist in that.

November, 2020

On behalf of INSOL Europe

Piya Mukherjee	Marcel Groenewegen
Immediate Past President	President

Introduction by the authors

The Guidance Notes are written in order to provide assistance to legislative drafters in the 27 Member States of the European Union tasked with implementing into their national laws the restructuring frameworks envisaged in Title II of EU Directive 2019/1023 on restructuring and insolvency.

The First Guidance Note, which was written by Tomáš Richter & Adrian Thery dealt with claims, classes, voting, confirmation and the cross-class cram-down. The Second Guidance Note, which was written by Ben Schuijling treats the stay of individual enforcement actions as a fundamental instrument in the preparation of a restructuring plan.

This Third Guidance Note deals with *"Procedural features"*. In the context of the implementation of the Directive, Member States have considerable discretion in the supervision, negotiation and confirmation of the restructuring plan, including the choice of the competent authority, judicial or administrative, according to the expertise developed by relevant authorities and by specialist practitioners. In this regard, some key questions have arisen in the context of negotiating and confirming the reorganization plan before the judicial or specialized administrative authority; appointing an insolvency practitioner to assist the debtor and creditors in negotiating and drafting the plan; imposing a test of the debtor's viability under national law and the possibility for the competent authority to refuse to confirm restructuring plan where it has no reasonable prospect of preventing insolvency or ensuring the viability of the business.

As with the First and Second Guidance Notes, it is the purpose of this Third Guidance Note to identity some of the key issues that national legislators will want to consider in this particular context when implementing the restructuring frameworks prescribed by Title II of the Directive, and, at least at times, also to respectfully suggest which approaches might perhaps be explored more productively than others.

In Dublin, November 2020

Michael Quinn

Michael Quinn is judge of the High Court of Ireland and Co-Chair of the Judicial Wing of INSOL Europe.

Barry Cahir Email: b.cahir@beauchamps.ie

Barry Cahir is Head of Insolvency & Corporate Recovery at Beauchamps and Vice President of INSOL Europe.

Defined Terms

"**Directive**" means DIRECTIVE (EU) 2019/1023 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 20 June 2019 on preventive restructuring frameworks, on discharge of debt and disqualifications, and on measures to increase the efficiency of procedures concerning restructuring, insolvency and discharge of debt, and amending Directive (EU) 2017/1132 (Directive on restructuring and insolvency).

"**EU Restructuring Framework**" means one or more of the preventive restructuring frameworks to be implemented into Member States' laws pursuant to Title II of the Directive.

"**Member State**" means member states of the European Union.

“**Practitioner in the field of restructuring**” means any person or body appointed by a judicial or administrative authority who assists the debtor and creditors in negotiation and drafting the plan pursuant to Article 5 of the Directive.

“**Restructuring**” means measures aimed at restructuring a debtor’s business that include changing the composition, conditions or structure of a debtor’s assets and liabilities or any other part of the debtor’s capital structure.

“**Stay**” means a temporary suspension, granted by a judicial or administrative authority or applied by operation of law, of the right of a creditor to enforce a claim against a debtor.

When this Note refers to "**Articles**" it is referring to Articles of the Directive, unless indicated otherwise.

I. PROCEDURAL FEATURES AND GOVERNANCE MATTERS

Intra Member State competence and jurisdiction. Member States should consider:

What authority will be competent to supervise the process and confirm the restructuring plan?

1. The Directive envisages that supervision and confirmation of important decisions may be by a judicial or an administrative authority. The specifics and technicalities of the process, like the assessment of valuations, can be a reason to concentrate the procedure at a specialized judicial or administrative authority. This way, its members may build up the necessary expertise and experience. It may also enhance predictability of outcome. On the other hand, a single specialized authority may hamper access to restructuring proceedings for small and medium enterprises ("SMEs") located at a distance from such a central authority.

In which courts or other authorities should jurisdiction over the EU Restructuring Framework be vested?

2. Member States with specialized and well-functioning insolvency courts will most likely find it opportune to vest jurisdiction in those courts in order to capitalize on the experience of their judges and staff as well as their processes, including in particular electronic registers and other infrastructure already in place. Where, on the other hand, the courts or other authorities that have jurisdiction over formal insolvency proceedings are perceived to carry a stigma, Member States may want to consider vesting intra-state jurisdiction over the EU Restructuring Framework elsewhere.

Principle of light-touch court involvement and streamlined procedure versus sufficient safeguards of parties' legitimate interests, including in constitutional terms (the right to fair trial).

3. The concept of "light touch" has different meanings in different jurisdictions. For the purposes of this Guide we have treated this as meaning the question for Member States to decide as to the extent to which their restructuring procedures will necessitate at each stage of the process, firstly, the engagement of a judicial or administrative authority, and secondly, the appointment by such authority of a practitioner in the field of restructuring.

4. The Directive expresses an aspiration to limit to defined circumstances the burden imposed by the requirements to engage with authorities and practitioners. Nonetheless, features such as automatic general stays and cross-class cramdown are significant tools in achieving the objectives of the Directive, and those benefits generally require the direct engagement of authorities and practitioners. The level of engagement required will vary by reference to the different stages of restructuring processes as required by the Directive

II. CONFIRMATION BY JUDICIAL OR ADMINISTRATIVE AUTHORITY

5. The objective of the Directive is that Member States shall ensure that effective preventive restructuring procedures are accessible to viable enterprises and debtors. Historically Member States experienced obstacles to such processes, such as delay, cost and the administrative burden of engaging with institutions such as judicial and

administrative authorities and the additional cost in certain cases of the appointment of independent expert insolvency practitioners, however controlled these interventions may be.

6. The Directive recognises (Recital 4) that in the context of procedures now available to debtors in certain Member States the degree of involvement of judicial and administrative authorities and of persons appointed by such authorities varies from no involvement or minimal involvement to mandatory full involvement. The Directive notes at Recital 30 that debtors should in principle be left in control of assets and day-to-day operations of the business and that the appointment of a practitioner in the field of restructuring should not be mandatory in every case.

7. The ultimate objective in restructuring processes is the confirmation and implementation of a plan for the restructuring to enable the debtor continue its operations with all the benefits this provides for stakeholders (including employees) and the community in general. The Directive recognises at Recital 48 that assessment of a restructuring plan by a judicial or administrative authority before confirmation of such a plan is necessary to ensure that the reduction of rights of creditors or of the interest of equity holders is proportionate to the benefits of the restructuring and that such parties, where aggrieved, have access to an effective remedy to ensure balance and fairness. At Article 10 the Directive provides that restructuring plans which affect the claims or interests of dissenting affected parties, and certain other forms of restructuring plans, can only be binding on such parties if they are confirmed by a judicial or administrative authority.

8. Articles 4.6, 9 and 15 of the Directive envisage that certain restructuring procedures may be or should be available without the invariable requirement for the intervention of judicial or administrative authorities or practitioners. Plans resulting from such procedures will only bind parties who have participated in their adoption. Therefore, plans not involving engagement with a judicial or administrative authority may be of limited benefit in terms of the objective of the Directive.

III. JUDICIAL OR ADMINISTRATIVE?

9. The next consideration is whether Member States should confer jurisdiction in these matters either on a judicial or an administrative authority.

10. In certain Member States agencies are already established which have well developed expertise in insolvency and restructuring matters. As between Member States expertise levels will vary between such agencies, as in the case of judicial authorities. The decision as to the nature of the body or authority on which Member States will decide to confer competence in measures implementing the Directive may depend on such questions as the following:

    (a) What existing expertise is available on the one hand in administrative agencies or on the other hand in judicial resources; or

    (b) The policy preference of the member state for vesting substantive decisions on such matters as the imposition of “cram down” in an administrative or a judicial authority.

11. Certain Member States have long established policy preferences, and in some cases constitutionally mandated preferences, to confer decision making such as confirmation of plans on bodies such as a court of law. Inasmuch as the Directive refers to "judicial or administrative authorities", it clearly envisages that Member States may now consider whether alternative specialist administrative bodies can be conferred with this competence.

12. In certain Member States the concept of imposing reductions on claims by cramdown or limitations on the enforcement of creditors' remedies, for example, by the imposition of a stay, is regarded as a breach of constitutionally protected property interests. Such impositions may not be fundamentally unsuitable or objectionable and the general ability to impose such cramdowns on certain conditions will now be a requirement of EU law pursuant to the Directive. However, it is recognised that the process by which such impositions can be made must be in accordance with strictly defined rules of law and in many states constitutional requirements will mandate that affected parties have the right on a case by case basis to be heard before such a plan can have effect. In certain Member States this principle can only be observed through a process of judicial adjudication which enjoys the protection of objectivity and independence.

13. There may also be cases where agencies which themselves are organs of the state such as revenue/tax collection authorities are affected by a plan and therefore it will be considered that only a judicial authority, acting independently of the state itself, will be seen to have sufficient objectivity and independence to determine the overall fairness of such a plan.

14. The Directive envisages the possibility of an entirely out of court process being available in certain circumstances. However, it is also clear from Recital 48 and Article 10 that if a plan is to affect dissenting or objecting parties then it will require confirmation by a judicial or administrative authority. Similarly, it is clear from Article 6.7 and Article 9 that only a judicial or administrative authority can make decisions in relation to such matters as an extension of the automatic stay or of lifting the stay in certain conditions.

15. Member States must also consider whether a process which does not engage formal decisions by a judicial or administrative authority will be recognised under EIR – R 2015/848. Article 1c of that Regulation suggests that if there is a stay of individual enforcement proceedings granted "by a court or by operation of law" and if such proceedings are notified under Annex A, they will enjoy such recognition.

A. Appeals

16. Article 16.1 provides that if any appeal is to be provided for under national law against a decision to confirm or reject a plan taken by a judicial authority such an appeal must be brought before a higher judicial authority. This does not mean that there must be a remedy of appeal available. It only means that where an appeal is provided for in a national law such appeal must be to a higher judicial authority. This would be common in most Member States in terms of the general jurisdiction of courts of law.

17. Article 16.1 also provides that decisions to confirm or reject a plan made by an administrative authority must be amenable to appeal to a judicial authority whose decision itself may be subject to further appeal. As with other administrative authorities and the concept of judicial review, this can lead to what would in effect be three layers of adjudication.

18. In certain jurisdictions a specialised government agency is available as a resource limited to the processing of filings, stay applications and plans, but decisions which affect third parties such as the grant of the stay and confirmation of a plan are made by a court of law.

B. Appointment of a practitioner

19. Article 5 provides that Member States shall ensure that debtors accessing preventive restructuring procedures remain totally, or at least partially, in control of their assets and the day to day operation of their business.

20. Article 5.2 provides that the appointment by a judicial or administrative authority of a practitioner shall be decided on a case by case basis "except in certain circumstances where Member States may require the mandatory appointment of such a practitioner in every case."

21. Article 5.3 provides for the appointment of a practitioner in the field of restructuring to assist the debtor and creditors in negotiating the drafting of a plan at least in certain cases. Those cases are:

   (a) where a general stay of enforcement actions is granted by the authority and the authority decides that the appointment of such a practitioner is necessary to safeguard the interests of the parties,

   (b) where the restructuring plan needs to be confirmed by a judicial or administrative authority by means of a cross class cramdown in accordance with Article 11, or

   (c) where it (i.e. such an appointment) is requested by the debtor or by a majority of the creditors, provided that in the latter case the cost of the practitioner is borne by the creditors.

22. In the majority of cases, and certainly in cases where it is considered likely that there will be a necessity for the plan to involve a cross class cramdown, then the provisions of Article 5.3 would appear to envisage the appointment of a practitioner. This being the case, the question is one of degree as to the extent of the powers and functions of the practitioner[1]. There are a wide range of options which include conferring on the practitioner any selection of the following powers:

   (a) To monitor the conduct of the debtor's affairs, with reference to scrutiny for any abuse or potential abuse of a stay;

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[1] In examinership in Ireland the Examiner is conferred with certain mandatory functions which respect the concept of debtor in possession and only on the occurrence of certain events will he acquire additional powers over the debtors assets and affairs, and even then only after an appropriate application to the court. His fundamental function is to submit the restructuring plan, and that he reports on continuing viability of the debtor, the court having also been satisfied as to viability when appointing him.

(b) To take control of limited aspects of the assets or affairs of the debtor;

(c) To investigate matters concerning integrity/honesty of the debtor and its officers;

(d) To report to an administrative or judicial authority on matters stipulated, which may include application of the viability test;

(e) To formulate the restructuring plan, whether or not considering proposals made to him by the debtor or creditors and present them to the required meetings of affected parties and ultimately to the judicial or administrative authority for confirmation.

23. As to whether the appointment of a practitioner is desirable, it is relevant to note the most important aspects of the role of a practitioner as follows:

24. Under Article 6.7 the practitioner may be one of the persons who has authority to apply for extensions of the stay or under Article 6.9 one of the persons entitled to request that the stay be lifted.

25. Under Article 8.1(h) the practitioner is one of the persons whom the Directive envisages that Member States may require could be requested to provide a statement of the reasons why a restructuring plan has a reasonable prospect of preventing the insolvency of the debtor and ensuring the viability of the business.

26. Article 9.1 provides that Member States may provide that practitioners have the right to submit the restructuring plan. In certain Member States the practitioner is central to the formulation and submission of the plan, although not to the exclusion of rights of the debtor and of creditors to submit a plan.

C. Committees of creditors

27. The operative text of the Directive contains no mandatory provisions regarding role of committees of creditors However, the recitals refer to committees in a number of contexts and Member States must decide whether certain measures of supervision and control are best effected through provisions for the appointment or election of committees of creditors. Examples of this would be the concept of ex ante control of interim financing or of transactions which are reasonable and necessary for the negotiations of the restructuring plan in accordance with Articles 17 or 18 of the Directive.

28. Similarly, the appointment of a creditors' committee may be of assistance in implementing the measures required by Article 26 and 27 which govern the nomination and appointment of practitioners and their supervision and remuneration.

29. Article 26.1 provides that debtors and creditors should have the opportunity to either object to the selection or appointment of a practitioner or request the replacement of practitioner and consideration should be given to whether such a mechanism could be achieved through the appointment of creditor’s committees.

30. Similarly, Article 27 requires the establishment of mechanisms to supervise and ensure accountability of practitioners. Those mechanisms may be better suited to an appropriate agency or authority. However, for individual cases Article 27.4 provides that remuneration of practitioners is to be governed by rules consistent with the

objective of an efficient resolution or procedures. Again, the remuneration of practitioners may be an appropriate matter for committees.

31. In certain jurisdictions Member States find that if there is court supervision associated with the process then this may be as efficient as the formation of creditors' committees. As against this, it may be considered desirable as a policy matter that those who have an economic stake or who represent stakeholders in the process should hold an important role in relation to the approval of such matters as the cost of the process.

D. Viability tests

32. Article 4.3 provides that Member States may impose a viability test under national law.

33. Article 10.3 provides that Member States shall ensure that judicial or administrative authorities are able to refuse to confirm restructuring plan where that plan would not have a reasonable prospect of preventing insolvency or ensuring the viability of the business.

34. It appears from these provisions that viability is intended to be a test at the confirmation of the plan stage but not necessarily at the opening of the proceedings. This gives rise to a number of questions. Member States will need to consider whether under Article 4.3 they should introduce a viability test at the outset of the process and if so, who is to determine this. It is suggested that if such a fundamental test is to be applied then this, as under Article 10.3, should be a matter for a judicial or administrative authority.

35. In certain Member States, the viability test must be complied with at the outset, supported by substantial evidence in the form of a report of an independent person. The policy underpinning such a requirement is that if a debtor is to avail of the very significant benefits of the procedure, including a stay which impairs the rights of third parties, then this will only be fair to affected stakeholders if the business can be shown to have satisfied a viability test (and that the process is not being availed of only to delay or avoid an otherwise inevitable insolvent liquidation, which would be considered a form of abuse).

E. Adoption of plans and confirmation of plans - classification of creditors

36. Article 9.5 provides for the examination by a judicial or administrative authority of voting rights and the formation of classes. In cases where a request for confirmation of the plan is submitted to such an authority, 9.5 also provides that Member States may require such an authority to examine and confirm the voting rights and formation of classes at an earlier stage.

37. This requires a decision by Member States as to whether to impose the requirement for submission of classes to such authorities at an earlier stage. In certain forms of restructuring the classification of creditors is examined and approved at an initial directions hearing. If such option is not exercised it will be a matter for the confirmation hearing to consider the validity of the classification as one potential ground of objection to the confirmation of a plan.

IV. MEASURES COMMON TO RESTRUCTURING & INSOLVENCY

F. Training and expertise

38. Title IV of the Directive addresses matters concerning the training and expertise, of members of judicial and administrative authorities, and the training, supervision and remuneration of insolvency practitioners. These provisions are not confined to appointments relating to restructuring procedures but apply also to insolvency and discharge of debt procedures generally.

39. Article 25 requires Member States to ensure that members of judicial and administrative authorities receive suitable training and have the necessary expertise for their responsibilities. This is stated to be without prejudice to judicial independence and to any differences in the organisation of the judiciary across the Union. This is a recognition that in most jurisdictions, matters concerning restructuring and insolvency are heard by judges whose expertise is not exclusively grounded in a specialisation in insolvency matters, but whose credentials are otherwise respected in terms of independence and general judicial skills. However, it will be incumbent on Member States to at least examine their existing training models and, if necessary, to introduce appropriate forms of training in the sphere of restructuring and insolvency matters.

40. Member States are required by Article 26 to ensure that persons appointed to restructuring and insolvency offices under national legislation receive suitable training and have the necessary expertise for their responsibilities. It provides also that the conditions for eligibility must be clear, transparent and fair.

41. In certain Member States, appointments to positions of "insolvency office holder" such as liquidator, administrator or trustee are regulated by national licencing systems. In others, there are general rules requiring appointees to be members of specified professional bodies, such as accountancy or legal professions. Member States must now consider whether the role of a practitioner in the field of restructuring can be adequately performed by members of those professions specialising in traditional insolvency practice, or whether a new expertise appropriate to achieving the goals of the Directive in terms of preventive restructuring must be developed and accredited.

42. The approach to this question will vary depending on the range of procedures already available in different Member States and the expertise developed by specialist practitioners. If the relevant Member State has no existing framework for preventive restructuring comparable to that required by the Directive, there is likely to be a need to develop and provide training in the fundamentals of such restructuring, and to control the appointment of practitioners by reference to such training, including continuing professional education and appropriate accreditation.

43. In Member States where there is a strong history and culture of restructuring as alternatives to liquidation procedures, it should not be assumed that existing training and accreditation meets the requirements of the Directive. This requires Member States firstly to assess objectively whether their existing conditions concerning training, eligibility and suitability of practitioners meet the requirements of expertise and secondly to ensure that those requirements are clear, transparent and fair.

44. Article 26 requires also that the authorities, whether judicial or administrative, making an appointment must give due consideration to the particular expertise required and

specific features of individual cases to which a nominee is being appointed. Although the Directive in Recital 88 envisages the existence of a "list" or "pool", preapproved by the relevant authorities, the emphasis on specific skills and expertise for particular assignments suggests that appointments should not be made by reference merely to a system of rotation within such a list or a pool.

45. Member States must afford the debtor and creditors the opportunity to object to a selected nominee or to request a replacement. Implementing this requirement means, of necessity, that appropriate advance notice, including publicity, should be given so that the debtor and creditors have the opportunity to make meaningful representations as to the identity of the nominee.

46. In cases where appointments are made on an urgent basis and such prior notice is not possible, this requirement could be met by making a provisional or interim appointment pending a public process.

47. An alternative would be that appointments are made subject to the rights of interested parties to apply to the relevant appointing authority within an appropriate deadline and to make any submissions regarding the appointment or replacement of a nominee.

48. Article 27 requires Member States to establish appropriate oversight and regulatory mechanisms to ensure that the work of practitioners is effectively supervised to ensure "that their services are delivered effectively, competently, impartially and independently."

49. Many Member States already have experienced government insolvency agencies which perform these functions on a proactive basis or which receive and consider complaints in relation to the conduct of insolvency assignments. In others, the practitioner is required to report to the court which has appointed him/her. The Directive requires that information about the system for such supervision and accountability is publicly available. This reflects the fact that the affected parties may not be limited to the debtor, creditors and other direct stakeholders, but may extend also to counterparties and other participants in the market in which the debtor trades.

50. Article 27 also provides that Member States may encourage the development of and adherence to codes of conduct by practitioners. In Member States where appointments are limited to members of certain professional bodies, such bodies will invariably have adopted codes of conduct. However, if new systems for training and accreditation are to be adopted, it is recommended that appropriate codes of conduct would form part of such systems.

G. Remuneration of practitioners

51. Article 27 provides that Member States must ensure that remuneration of practitioners is governed by rules which are consistent with the objective of an efficient resolution of procedures.

52. This Article requires that Member States appraise and if necessary update national rules regarding remuneration of practitioners and office holders. For example, in certain Member States there has been a historic preference for remuneration by reference to time expended on an assignment. Many such Member States have in recent years moved away from such formulae. Similarly, formulae which are based on

percentages of asset realisations, whilst attractive in certain contexts, may not always serve the objective of the procedures.

53. This requirement is linked to the requirements concerning transparency associated with the appointments. Whilst it may not always be possible for a nominee to predict or fix the level of remuneration which will be required, Member States may choose to provide that at the time of appointment the nominee present particulars of the basis upon which he will be remunerated, which would facilitate the measurement of remuneration ultimately sanctioned.

54. Article 27(4) requires that Member States ensure that appropriate procedures are in place to resolve disputes over remuneration. This may be achieved by a "tiered" approach whereby remuneration could be approved either by directly affected stakeholders such as creditors, or by a committee of creditors, with provision ultimately in appropriate cases for appeal to the relevant authority, whether judicial or administrative.

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