

THE LATEST ON INSOLVENT SCHEMES AND RESTRUCTURING PLANS



CASE



FACTS



RULING

PROVIDENT Sanctioned

Scheme proposed to compromise consumer redress claims for inappropriately provided loans.

FCA “letter of concern” noted that the proposed compensation plan was detrimental to consumers as they would receive less than they were owed and it was feasible that funding could be increased. However, the FCA did not tender evidence to substantiate this at the sanction hearing. Sir Anthony Mann held that he may have ruled differently had the FCA argued their case in court.

HURRICANE ENERGY Not Sanctioned

The proposed RP envisioned a debt-for-equity swap, and would use the **cross-class cram-down** procedure against existing shareholders to substantially reduce their shareholding. RP was approved by 100% of voting bondholders but rejected by 92.35% of voting shareholders.

Mr Justice Zacaroli disagreed with the company’s relevant alternative (a controlled wind-down leading to liquidation). The judge held that the lack of a **burning platform** created a possibility of future profitability and potential for a better outcome for shareholders, whereas the plan would have “immediately and irrevocably” removed most of the shareholders’ equity in the company.

AMIGO LOANS Not Sanctioned

The proposed scheme would have seen the creditors take a 90% haircut while the shareholders were going to retain their full equity interest.

Mr Justice Miles held that there was no **burning platform**. The scheme was held to be unfair to creditors (as argued by the FCA) for multiple reasons, including: (i) the creditors were financially unsophisticated, (ii) insufficient information had been provided to them, (iii) guidance available to them was lacking, and (iv) there was a **low turnout of creditors** (9%) at the creditors’ meeting to approve the scheme.

VIRGIN ACTIVE Sanctioned

RPs were proposed to restructure the group’s leasehold portfolio. New money (£65 million) was to be provided. Various landlords and other creditors objected to the RPs, so **cross-class cram-downs** were proposed to sanction the plans despite the objections.

The court rejected objections from the dissenting landlords, concluding that the **“no worse off” test** was satisfied. They were not shown to have a genuine economic interest in the company’s relevant alternative because they were out of the money. The shareholders who provided new money were allowed to keep their shares, and the dissenting landlords had their leasehold obligations compromised. The dissenting landlords failed to bring their own valuation evidence to demonstrate interest.

GATEGROUP Sanctioned

An RP was proposed to amend bonds that were subject to the exclusive jurisdiction of Swiss courts. The English court was required to assess whether it had jurisdiction to review the plan under the Lugano Convention.

Mr Justice Zacaroli held that RPs are “insolvency proceedings” and so fall outside the scope of the Lugano Convention. Schemes have been treated as falling within the scope of the Brussels Regulation and the **Lugano Convention** for jurisdiction and recognition purposes. RPs and schemes are therefore on different paths to recognition. Private international law as well as foreign local law will now have an important role to play in relation to the recognition of RPs.

DEEPOCEAN Sanctioned

RPs proposed to facilitate a solvent wind-down rather than a rescue. They required the use of the **cross-class cram-down** mechanism to overcome the fact that only 64.6% by value of the unsecured creditor class had approved the plans.

The court sanctioned the RPs as it considered that they would have a mitigating effect on the severity of the losses that the creditors would otherwise sustain. This was held to be sufficient to satisfy the “requisite purpose” test, which provides that an RP must eliminate, reduce, prevent, or mitigate the effect of any of the company’s financial difficulties. It is now established that RPs need not seek to rescue a company as a going concern.

EMERGING THEMES



SUBSTANTIATING A RELEVANT ALTERNATIVE

- Parties proposing schemes and RPs should be careful not to exaggerate the gravity of a company’s position in their relevant alternative analysis.
- Relevant alternatives must be supported by robust evidence.



FAIRNESS – A KEY AREA OF FOCUS

- Where a **burning platform** is not present or sufficiently evidenced, the court has more room to flex its muscles in reviewing the fairness of a scheme or RP.
- Companies should be aware that the court will actively scrutinise the fairness of proposals with respect to any stakeholders that stand to lose out.



RESTRUCTURING PLANS & DEBT-FOR-EQUITY SWAPS

- First use of an RP to effect a debt-for-equity swap, contrary to the wishes of existing shareholders was in *Hurricane Energy*.
- Although in that case the RP was not sanctioned, this does not mean that a debt-for-equity swap would not work in the future.
- The key issue in *Hurricane Energy* was one of fairness as the permanent removal of the shareholders’ equity in the company was not justifiable.



INTERVENTION BY THE FCA

- Growing willingness of the FCA to voice its concerns where the interests of consumers are at stake.
- However, the regulator will not receive special treatment and will need to substantiate its claims.



NO ABSOLUTE PRIORITY RULE

- No **absolute priority rule** under English law – shareholders or junior creditors may, in certain circumstances, receive value before a more senior class of creditor.
- In *DeepOcean*, the court noted that an RP may provide different treatment for some (but not all) creditors who are out of the money, where this is justified.
- In *Virgin Active*, it was justified for shareholders to receive some value because they provided new money, while landlords had their leasehold obligations compromised and were **crammed-down**.



NO DEBTOR-IN-POSSESSION (“DIP”) FINANCING

- No statutory provision for **DIP financing** in the UK – new funding in a restructuring must fit within the framework of existing debt documentation.
- Participants have made good use of RPs to inject new money with over UK£1.1 billion having been provided in the 12 months leading up to June 2021.