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FEBRUARY 2021 | FRAUD & INSOLVENCY

CROSS-CLASS CRAM DOWN AFTER DEEPOCEAN: WHAT CREDITORS NEED TO KNOW ABOUT THE NEW UK REGIME

The UK's new "restructuring plan" was enacted in June 2020.[1] This highly-anticipated regime introduced (for the first time into English law) a tongue twisting "cross-class cram down" (CCCD) mechanism by which a restructuring plan can (at the court's discretion) be imposed on an entire class of dissenting creditors or members.

1 Part 26A of the Companies Act 2006.

“The decision in *DeepOcean* will... also act as a reminder that dissenting creditors should provide reasons for their dissent to ensure that any concerns over a restructuring plan are brought to the court’s attention.”

Until recently, only two companies had successfully used the restructuring plan regime.[2] In both instances, CCCD was not considered as the required voting thresholds (i.e. 75%) were met.

However, on 13 January 2021, the English High Court implemented CCCD for the first time in *Re DeepOcean [2021]*[3] (in which HFW acted for a creditor of one of the plan companies). The comments of the judge at the hearing, as well as the subsequent judgment published on 28 January 2021, provide important guidance for creditors on how the court will exercise its CCCD discretion. We provide tips for creditors at the end of this article.

The facts

In December 2020, three UK subsidiaries of DeepOcean Group, namely DeepOcean 1 UK Limited (DO1), DeepOcean Subsea Cables Limited (DSC) and Enshore Subsea Limited (ES) proposed three inter-conditional restructuring plans to the court in order to effect a solvent winding-down of the companies. Approval to hold creditor meetings was provided by the court on 15 December 2020.

At the meetings on 6 January 2021, the majority of DO1 and ES creditors voted in favour of the DO1 and ES restructuring plans. However, DSC’s class of unsecured creditors failed to reach the requisite majority for sanction of the DSC plan with only 64.6% in favour.

Nevertheless, at the sanction hearing on 13 January 2021, Trower J approved all three restructuring plans using the CCCD mechanism.

The CCCD mechanism

Section 901F(1) of the Companies Act 2006 (the **Act**) sets out the requirement for the sanction of a restructuring plan: at least 75% in value of the creditors or class of creditors or members or class of members (as the case may be), present and voting either in person or by proxy must vote in favour of it.

However, under section 901G of the Act (i.e. the CCCD provision), the court has jurisdiction to sanction a restructuring plan which fails to obtain this 75% threshold if:

1. the court is satisfied that, if the plan were to be sanctioned, none of the members of the dissenting class would be any worse off than they would be in the event of the “relevant alternative” **(Condition A)**; and
2. at least one class of creditor who would receive a payment or have a genuine economic interest in the company in the event of the “relevant alternative” voted in favour of the plan by the requisite statutory majority (i.e. 75%) **(Condition B)**.

Identifying the “relevant alternative”

Section 901G(4) of the Act states that the “relevant alternative” is *“whatever the court considers would be most likely to occur in relation to the company if the compromise or arrangement were not sanctioned...”* In *DeepOcean*, Trower J confirmed that identifying the relevant alternative is a similar exercise to the appropriate comparator test in a scheme of arrangement (i.e. the likely alternative if the scheme was not sanctioned). To that extent, and as expected, case law in respect of schemes of arrangement can be applied to restructuring plans (at least for the foreseeable future).

In most instances, the relevant alternative will be the administration or liquidation of the company. However, Trower J noted that there may be cases in which identification of the relevant alternative is difficult. This will, in turn, make it harder to determine the financial impact on plan creditors and properly assess whether section 901G is satisfied. While this was not a particular issue

2 See *Virgin Atlantic Airways Limited [2020] EWHC 2191 (Ch) and Re Pizza Express Financing 2 Ltd [2020] EWHC 2873 (Ch).*

3 *Re DeepOcean [2021] EWHC 138 (Ch)*

in *DeepOcean* (where liquidation of the plan companies was quickly deemed the most relevant alternative), the court's approach in such cases will be something to watch out for.

Condition A – "any worse off"

At the sanction hearing, Trower J noted the ambiguity of the phrase "any worse off" under Condition A and questioned whether it should go beyond pure economic recovery. Ultimately, Trower J took the view that "any worse off" contemplates the impact of a restructuring plan on *all* aspects of the liability to the creditor concerned (including, for example, the speed of recovery and the security of any covenant to pay). While the primary question and starting point for any assessment under Condition A will be a comparison of the likely financial return under the relevant alternative (or the amount of any discount to the part value of each creditor's debt), the court must be satisfied that the dissenting class is not worse off *all things considered*.

Condition B – evidence of economic interest

In order to satisfy Condition B, it is necessary to show that a class of creditor (who voted in favour of the plan by the requisite majority) would receive a payment from, or have a genuine economic interest in, the plan company in the event of the relevant alternative. This is an evidence-based exercise. However, it is notable from the *DeepOcean* judgment that economic recovery in the relevant alternative need not be substantial. In *DeepOcean*, the recovery for the secured lenders (who voted in favour of the plan) was small in a liquidation scenario, but sufficient for the purposes of satisfying Condition B.

Condition B – artificiality in class constitution

When considering Condition B, Trower J confirmed that the court may revisit the conclusion reached on classes at the convening hearing if it appears that there has been some sort of artificiality (i.e. if it appears that the classes were created in such a way as to ensure that Condition B would be satisfied in any event).

The court's absolute discretion

The overarching point to note from the wording of section 901F and 901G of the Act, and indeed the *DeepOcean* judgment itself, is that the court *may* sanction a plan. While compliance with sections 901A to 901F (or section 901G, where applicable) is a prerequisite for approval, paragraphs 190 and 192 of the Explanatory Notes to the Corporate Insolvency and Governance Act 2020 (through which the restructuring plan regime was enacted) makes clear that the court has *"an **absolute discretion** over whether or not to sanction a restructuring plan"*. The court may refuse to sanction a plan on the basis that it would not be "just and equitable" to do so.

Notwithstanding this, Trower J indicated that a plan company will have a *"fair wind behind it"* if the statutory voting requirements for sanction (or Conditions A and B, where applicable) are satisfied. When deciding whether to apply CCCD in particular, the court will focus on the negative question of whether a refusal to sanction is appropriate because the restructuring plan is not just and equitable.

Just and equitable – when will the court refuse to sanction?

In *DeepOcean*, Trower J was satisfied that there was nothing unjust or inequitable about the proposed plans. However, in his judgment, he indicated that the following are material considerations for the court when deciding whether to refuse to sanction:

1. **The overall support for the restructuring plans** – the level of support for the restructuring plan is indicative of the weight to be given to the views of the class meetings which agreed the plan and the views of the dissenting class.
2. **Whether the dissenting class are fairly represented** – a low turnout at a class meeting is capable of undermining the conclusion that the vote was representative. Where turnout figures are low, the court will consider whether there were any procedural barriers to engagement at the creditors meeting, or whether the creditors' failure to engage simply signifies an unwillingness to do so.

   Composition of the class will also be important here. In *DeepOcean*, the turnout for unsecured creditors was low (25% to 32%), but unsurprising as the unsecured classes were largely made up of trade creditors with claims worth £5,000 or less. Trade creditors may be less sophisticated companies and/or less invested in the outcome of voting than, for example, finance creditors (whose turnout is usually 100%) and therefore less likely to vote.
3. **The existence of any collateral interest or "blot" in the plan** – if voters have been influenced by a collateral interest, or otherwise have not acted honestly when voting, the court may refuse to sanction a plan on the grounds that it is not just and equitable. Likewise, the existence of any issues with the plan itself (for example, the distribution model), will be cause for concern.
4. **The relative treatment of creditors** – as a class right of veto is removed by section 901G, the court may consider questions of *"horizontal comparability"* to see whether a plan provides for differences in the treatment of creditors and whether those differences are justified. In particular, the court will want to know whether there has been a fair distribution of the benefits of the restructuring across the approving and dissenting classes.

Looking ahead

The decision in *DeepOcean* will no doubt provide clarity to debtor companies looking to use the new restructuring regime under Part 26A of the Companies Act 2006.

It will also act as a reminder that dissenting creditors should provide reasons for their dissent to ensure that any concerns over a restructuring plan are brought to the court's attention. This is because one of the key issues in *DeepOcean* was that creditors in the dissenting class failed to provide reasons or make any submissions as to why they did not vote in favour of the plan.

It will be interesting to see how the court approaches CCCD in future cases, particularly those with more complex fact patterns and/or vocal dissenting creditors. In the meantime, we have set out below practical steps to assist creditors in the restructuring plan process:

1. **Promptly review the plan company's explanatory statement and any additional information provided** – consider seeking legal advice early. Creditors may have limited time to assess their position under the plan before the creditors meetings are held (in *DeepOcean* it was three weeks from publication of the explanatory statement). Explanatory statements can also be lengthy, making it difficult to ascertain a plan's likely impact on certain classes of creditors and/or identify relevant issues.
2. **Make sure to raise any objections to the restructuring plan and/or make further information requests (ideally) *before* the creditors meetings** – this will put the plan company on notice and (hopefully) give the parties time to resolve any problems before voting, or otherwise flag issues of which the court ought to be aware.
3. **Make sure to attend (or instruct a proxy to attend) the creditors meeting and vote** – in light of the court's comments about low turnout and fair representation, attendance and voting at creditors meetings is particularly important where a creditor (or class) is not in favour of the plan. It is also a good opportunity to seek clarifications and/or raise further objections.
4. **If voting against a plan, provide reasons to the plan company and the court** – the views of dissenting creditors are an important consideration for the court when deciding whether to sanction a plan. Do not go unheard.

If you have any questions relating to the restructuring plan, CCCD or any other matters covered in the briefing, please contact HFW's contentious insolvency team.

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