



ICLG

The International Comparative Legal Guide to:

Corporate Recovery & Insolvency 2015

9th Edition

A practical cross-border insight into corporate recovery and insolvency work

Published by Global Legal Group, with contributions from:

Ali Budiardjo, Nugroho, Reksodiputro

Anastasios Antoniou LLC

Atlantik Legal Services

Baker & Partners

Bonelli Erede Pappalardo

Bredin Prat

Campbells

Clifford Chance LLC

Debarliev, Dameski & Kelesoska Attorneys at Law

Dhir & Dhir Associates

El-Borai & Partners

Fellner Wratzfeld & Partners Rechtsanwälte GmbH

Ferraiuoli LLC

Gall

Gilbert + Tobin

Gorrissen Federspiel

Hengeler Mueller

INFRALEX

Kvale Advokatfirma DA

Lenz & Staehelin

Nishimura & Asahi

Odvetniška družba Špec o.p. d.o.o.

Olswang LLP

Osler, Hoskin & Harcourt LLP

Pachiu & Associates

Paul, Weiss, Rifkind, Wharton & Garrison LLP

Pinheiro Neto Advogados

RESOR N.V.

Rivera Gaxiola y Carrasco

Sedgwick Chudleigh Ltd.

Slaughter and May

Tonucci & Partners

Uría Menéndez

Uría Menéndez – Proença de Carvalho

White & Case

Yonev Valkov Nenov

GLG

Global Legal Group

Contributing Editors

Tom Vickers, Partner, Slaughter and May, and Sarah Paterson, Senior Consultant to Slaughter and May and Assistant Professor in Law, LSE

Head of Business Development

Dror Levy

Sales Director

Florjan Osmani

Commercial Director

Antony Dine

Account Directors

Oliver Smith, Rory Smith

Senior Account Manager

Maria Lopez

Sales Support Manager

Toni Hayward

Sub Editor

Sam Friend

Senior Editor

Suzie Levy

Group Consulting Editor

Alan Falach

Group Publisher

Richard Firth

Published by

Global Legal Group Ltd.
59 Tanner Street
London SE1 3PL, UK
Tel: +44 20 7367 0720
Fax: +44 20 7407 5255
Email: info@glgroup.co.uk
URL: www.glgroup.co.uk

GLG Cover Design

F&F Studio Design

GLG Cover Image Source

iStockphoto

Printed by

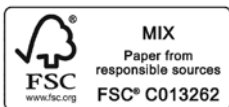
Information Press Ltd
June 2015

Copyright © 2015
Global Legal Group Ltd.
All rights reserved
No photocopying

ISBN 978-1-910083-50-5

ISSN 1754-0097

Strategic Partners



General Chapters:

1	Recast EC Insolvency Regulation – Progress So Far and Remaining Steps to Adoption – Tom Vickers & Lynda Elms, Slaughter and May	1
2	Restructuring Bonds: Legal Issues Under English Law – Alicia Videon & Julian Turner, Olswang LLP	5

Country Question and Answer Chapters:

3	Albania	Tonucci & Partners: Artur Asllani & Ervin Bano	11
4	Australia	Gilbert + Tobin: Dominic Emmett & Nicholas Edwards	17
5	Austria	Fellner Wratzfeld & Partners Rechtsanwälte GmbH: Markus Fellner & Florian Kranebitter	24
6	Bermuda	Sedgwick Chudleigh Ltd.: Alex Potts & Nick Miles	30
7	Brazil	Pinheiro Neto Advogados: Luiz Fernando Valente de Paiva & André Moraes Marques	40
8	Bulgaria	Yonev Valkov Nenov: Todor Nenov & Pavel Tsanov	46
9	Canada	Osler, Hoskin & Harcourt LLP: Tracy C. Sandler & Andrea Lockhart	52
10	Cayman Islands	Campbells: Ross McDonough & Guy Cowan	60
11	Cyprus	Anastasios Antoniou LLC: Anastasios A. Antoniou & Michalis Michaelides	66
12	Denmark	Gorrissen Federspiel: John Sommer Schmidt & Morten Nybom Bethe	74
13	Egypt	El-Borai & Partners: Dr. Ahmed El Borai & Dr. Ramy El Borai	80
14	England & Wales	Slaughter and May: Tom Vickers & Lynda Elms	86
15	France	Bredin Prat: Nicolas Laurent & Olivier Puech	98
16	Germany	Hengeler Mueller: Dr. Ulrich Blech	104
17	Hong Kong	Gall: Nick Gall & Anjelica Tang	112
18	Iceland	Atlantik Legal Services: Eiríkur Elís Þorláksson & Benedetto Valur Nardini	119
19	India	Dhir & Dhir Associates: Nilesh Sharma & Sandeep Kumar Gupta	124
20	Indonesia	Ali Budiardjo, Nugroho, Reksodiputro: Theodoor Bakker & Herry Kurniawan	130
21	Italy	Bonelli Erede Pappalardo: Vittorio Lupoli & Lucio Guttilla	135
22	Japan	Nishimura & Asahi: Yoshinori Ono & Hiroshi Mori	145
23	Jersey	Baker & Partners: William Redgrave & Ed Shorroch	152
24	Macedonia	Debarliev, Dameski & Kelesoska Attorneys at Law: Dragan Dameski & Jasmina Ilieva Jovanovikj	157
25	Mexico	Rivera Gaxiola y Carrasco: Fabián Bartolini Esparza & Carlos F. Chapela De Alvarado	163
26	Netherlands	RESOR N.V.: Lucas Kortmann & Tom Booms	172
27	Norway	Kvale Advokatfirma DA: Stine D. Snertingdalen & Ingrid E. S. Tronshaug	179
28	Portugal	Úria Menéndez – Proença de Carvalho: Pedro Ferreira Malaquias & David Sequeira Dinis	185
29	Puerto Rico	Ferraiuoli LLC: Sonia Colón	191
30	Romania	Pachiu & Associates: Ioana Iovanesc & Marius Nita	196
31	Russia	INFRALEX: Artem Kukin & Stanislav Petrov	203

Continued Overleaf ➡

Further copies of this book and others in the series can be ordered from the publisher. Please call +44 20 7367 0720

Disclaimer

This publication is for general information purposes only. It does not purport to provide comprehensive full legal or other advice. Global Legal Group Ltd. and the contributors accept no responsibility for losses that may arise from reliance upon information contained in this publication. This publication is intended to give an indication of legal issues upon which you may need advice. Full legal advice should be taken from a qualified professional when dealing with specific situations.

GLG

Global Legal Group

Country Question and Answer Chapters:

32	Slovenia	Odvetniška družba Špec o.p. d.o.o.: Boštjan Špec	209
33	Spain	Uria Menéndez: Alberto Núñez-Lagos Burguera & Ángel Alonso Hernández	215
34	Sweden	White & Case: Carl Hugo Parment & Michael Gentili	224
35	Switzerland	Lenz & Staehelin: David Ledermann & Tanja Luginbühl	230
36	Ukraine	Clifford Chance LLC: Olexiy Soshenko & Andrii Grebonkin	238
37	USA	Paul, Weiss, Rifkind, Wharton & Garrison LLP: Alan W. Kornberg & Elizabeth R. McColm	245

Restructuring Bonds: Legal Issues Under English Law

Olswang LLP



Alicia Videon



Julian Turner

Introduction

With the volume of European bond and note issuances continuing to climb, a focus is returning to the issues that arise in restructuring such debt. A significant body of English case law developed following the economic downturn in the early 2000s and again following 2008, which is directly relevant in this context. There have been recent legal developments both within and outside the high yield debt arena, including in the increasingly complex area of cross-border insolvency.

This article considers questions of English law relevant to issuers who may be subject to English insolvency law and to bonds or notes (described generically as bonds) governed by English law.

When bond issuers face a potentially distressed situation, two major issues are drawn into sharp focus. The first issue is, somewhat obviously, whether there may be a bond default. Investors and other parties may seek to put pressure on the issuer (or other creditors), often through the trustee, by using the potential to call events of default. There is a substantial body of case law in England concerning the interpretation of events of default and the trustee's powers and duties to bondholders in such circumstances.

The second aspect concerns the impact of implementing the restructuring on bondholder class rights. The English courts have continued to explore class rights in the context of restructuring, both through informal and formal processes. In the context of informal, consensual restructuring, one key issue is whether the majority of the class of bondholders can bind a minority through the mechanism set out in the trust deed.

If the restructuring requires a formal process, such as a scheme of arrangement, class rights remain paramount. If a class would receive nothing in insolvency then a scheme may be implemented which does not require the vote of that class. If bondholders' votes are required, they vote as one or more classes and the question of class membership is critical.

1 Events of Default and Trustee's Powers and Duties

Where a trustee has been appointed in a bond structure, it may need to determine whether a breach has occurred and, if one has, whether it would be in the best interests of the bondholders (whose interests it represents) to call an event of default based on that breach and, subsequently, accelerate the bonds.

In the high yield debt arena, bond documents tend to contain relatively few covenants. A trustee may have the discretion to decide whether

a breach has occurred in respect of defaults which are typically difficult to determine, such as insolvency. If the trustee's decision is challenged, the burden of proof will be on the trustee to show that the relevant event has occurred.

Despite a spate of recent case law on the "cash flow" and "balance sheet" insolvency tests under the Insolvency Act 1986,¹ it is often difficult to determine insolvency in a bond scenario, where maturity dates can be several years away and the markets are typically volatile. This difficulty was illustrated in *Colt Telecom*,² a pre-Enterprise Act 2002 case in which two corporate bondholders petitioned for the issuer's administration on the grounds that the issuer was, or was likely to become, both "cash-flow" and "balance sheet" insolvent and would not be able to repay the bonds when they matured (although there was not, at the time of the hearing, any default under the bonds). The court held that the bondholders had failed to prove the issuer's insolvency on a balance of probabilities.

In *Eurosail*,³ where loan notes were issued as part of a securitisation, the House of Lords held that establishing "balance sheet" insolvency on a balance of probabilities will be difficult where the company has long term prospective liabilities or liabilities which are contingent as to timing and/or quantum. In that case, the company's future prospects and financial position (and therefore its ability to pay its debts) were matters almost entirely outside of its officers' control and depended instead on three "imponderables", including future currency exchange rate and LIBOR movements. As the debt was not payable for a further 30 years, the court said that the "imponderables" were a matter of speculation rather than calculation and prediction on any scientific basis, and could not be finally determined until much closer to maturity. The court expressly approved an earlier case⁴ which held that once the court has to move beyond the reasonably near future (the length of which depends on the circumstances), any attempt to apply the "cash flow" test will become "completely speculative" and a comparison of present assets with present and future liabilities (discounted for contingencies and deferment) becomes the "only sensible test".

Implications of Getting it Wrong

Where a trust deed provides that a trustee has discretion to take (or omit from taking) any action, the deed will often state that the trustee can exercise such discretion absolutely. This will be subject to the trustee's fiduciary duty to act in good faith. The scope of a trustee's fiduciary duty was considered in *Elektrim SA*.⁵ The claimant acquired a substantial number of bonds from Everest Capital Limited ("Everest"). Suing as the assignee of claims held by Everest under the bonds, the claimant claimed, among other things, that the trustee was in breach of its fiduciary duties in failing

to advise the bondholders on the risks of accepting “tainted funds” from a guarantor of the bonds. The Court of Appeal held that the trustee was not under any fiduciary duty to advise the bondholders in this way and, even if it could be argued that it was, the fact that the trustee was told that the bondholders were receiving legal advice on this very point meant that it was “fanciful” to suggest that the trustee should have gone further and second-guessed that advice. The claimant also claimed that the trustee was in breach of the trust deed in failing to exercise due care in withdrawing Polish bankruptcy proceedings against the issuer. The trustee, in accordance with the instructions of a bondholders’ committee. The court dismissed the claimant’s claim, finding that the trustee was entitled and obliged to act on the committee’s instructions (subject to getting satisfactory indemnities) under the terms of the trust deed. The trustee argued that the bondholders were “expert investors who look after their own interests” and that market practice is that, when things go wrong, bondholders may organise committees, which the court accepted.

A trustee will also be mindful of the statutory duty of care it owes under the Trustee Act 2000. Whenever this applies, the trustee must exercise such care and skill as is reasonable in the circumstances, having regard in particular (a) to any special knowledge or experience that he has or holds himself out as having, and (b) if he acts as trustee in the course of a business or profession, to any special knowledge or experience that it is reasonable to expect of a person acting in the course of that kind of business or profession. Professional trustees will therefore be subject to a higher standard.

In practice, where a trustee has the discretion to declare an event of default, it will err on the side of caution. In difficult cases the trustee may prefer to refer the question to court and seek direction, which has time and cost implications, or act only on the instruction of a majority of the bondholders. The trustee may also request indemnification prior to taking any action. However, aside from the potential risk to a trustee’s reputation, to what extent is there any other risk for a trustee if they get it wrong?

Case law suggests that the risk is limited. In *Concord*,⁶ the necessary majority of bondholders requested the trustee certify that the suspension by the company’s board of the bondholders’ nominated board member constituted an event of default that was materially prejudicial to their interests. The trustee obtained directions and a declaration from the Chancery Division to that effect. The bondholders requested that the trustee issue a notice of acceleration. However, in response to the certificate, the company put the trustee on notice that in its view, there had been no event of default and threatened the trustee on the basis that a notice of acceleration would cause the company substantial loss because of the effect it would have on third parties with whom the company was dealing. The bondholders objected to providing the trustee with a substantial indemnity against the risk that the trustee would be liable for a damages claim for giving an invalid notice. While the House of Lords acknowledged the trustee’s contractual entitlement to demand an indemnity, it held that the indemnity could only be in respect of a risk which was “more than a merely fanciful one”. The House of Lords held that:

- A. It was not reasonably arguable that the giving by the trustee of a notice of acceleration could give rise to a cause of action against the trustee in either contract or tort.
- B. As a matter of contract, an unjustified assertion by the trustee of an event of default, or the giving of an invalid notice of acceleration, could not give rise to a liability for breach of contract. The various tests for the implication of terms into a contract (including to give business efficacy to the contract) were considered, and it was held that there was no contractual term, express or implied, that the trustee shall not serve an invalid notice of acceleration or default.

- C. As to whether any cause of action in tort could arise (negligence, conspiracy or unlawful interference), it was held not to be reasonably arguable that the giving of a notice of acceleration based on the event of default declared by the Chancery Division could give rise to a tortious cause of action in damages. Lord Scott found it very difficult to see that the trustee owed a tortious duty of care to the issuer, but did not explore the issue.

2 Class Issues in Informal Restructuring

Where the issuer faces a known potential bond default and seeks to amend the bond terms, the power to amend those terms becomes the critical issue.

Trust deeds under English law commonly incorporate modification provisions allowing relevant majorities the power to amend the bond terms. It has long been held that the power given to the majority to bind a minority may carry with it a requirement to act for the benefit of the class as a whole.⁷ This power can be used in conjunction with tender offers, where noteholders are offered consideration (cash or new debt securities) in exchange for their notes. The consenting noteholders may be asked to vote on amendments in relation to their original holding (known as an “exit consent”) which significantly devalues the existing bonds.

The legitimacy of exit consents was considered in *Assenagon*.⁸

The case considered the restructuring of unsecured subordinated floating rate notes issued by Anglo Irish Bank, following its nationalisation. The issuer proposed to exchange the old notes for new notes at an exchange ratio of 0.20 (close to the value at which the old notes were trading at the time); the new notes would not be subordinated. Any noteholder who offered to exchange their old notes for the new notes was obliged to appoint a proxy to vote in favour of a resolution put to the noteholders at a subsequent meeting. The resolution would give the issuer a right to redeem the old notes of those who did not exchange for a nominal amount. The deadline for offering up the old notes in exchange for the new notes was set as the day before the noteholders’ meeting, where the resolution would be put to the noteholders. Most of the noteholders by value offered their notes for exchange; the claimant did not.

The claimant argued that:

- A. The resolution was beyond the power of the majority under the trust deed, because it conferred a power on the issuer to expropriate the old notes for no more than a nominal amount.
- B. Contrary to the terms of the trust deed, at the time of the noteholders’ meeting all those noteholders who voted in support held their notes beneficially for the issuer. Such votes ought to be disregarded.
- C. The resolution constituted an abuse of power, conferring no conceivable benefit or advantage upon the noteholders as a class. By the time of the noteholders’ meeting, it only affected the notes of the minority which had not exchanged their old notes for new notes; it was thus oppressive and unfair against the minority.

Ultra Vires

The court held that the power of the majority to pass the resolution depended entirely on it falling within the power contained in the trust deed to sanction any abrogation in respect of the rights of the noteholders against the issuer.

However, Briggs J held that the *vires* of the action was rescued by the fact that the trust deed imposed a special quorum for the reduction or cancellation of the principal payable on the notes or

the minimum rate of interest payable thereon. Briggs J therefore concluded, assessing the trust instrument as a whole, that the noteholders must be taken to have assented to the exercise of a power by the majority to bind the minority by abrogating all rights of noteholders as against the issuer. The court found in favour of the defendant on this point.

Disentitlement of the Issuer to Vote

The purpose of the disentitlement of the issuer to vote contained in the trust deed was found by the court to be the prevention of a vote designed to serve the interests of the noteholders from being undermined by the exercise of votes cast in the interests of the issuer.

Briggs J held that this applied to any person holding the notes for the benefit or for the account of the issuer. At the relevant time, the notes were held for the benefit of the issuer. The applicability of the disentitlement was to be tested at the date of the meeting and not when the old notes were exchanged for new ones.

Briggs J went on to conclude that the issuer's interest in the shares at the time of the vote was a beneficial interest which ordinarily arises in favour of the contracting purchaser of shares and was an interest of the type contemplated by the prohibition.

The court found in favour of the claimant on this point.

Abuse of Power by Majority

Briggs J referred to a general principle of English law that applies to all authority conferred on the majority of a class when binding a minority, namely that this authority must be exercised *bona fide* and in the best interests of the class as a whole. Previously, as cited by Briggs J, it was held in *Redwood*⁹ (in the context of a syndicated loan facility) that this principle could only be implied for business efficacy purposes, if it was obviously intended to be inferred or if it was necessary to give effect to the reasonable expectations of the parties. Briggs J disapproved of this statement on the basis that it is a term generally implied by the law of contract in arrangements of particular types, on that basis it can still be overturned by evidence of contrary intention, thus the extent and content of the principle that the majority must act *bona fide* and in the best interests of the class is inevitably dependent on the context in which the principle operates.

Briggs J held that the coercive power of the exit consent is one which can only be wielded by the majority of the very class which the issuer wishes to coerce and not by the issuer itself, which lacks any power to bring about an expropriatory amendment of the terms of the security.

The question was whether the passing of the resolution was an abuse of power by the majority noteholders, i.e. was it capable of being regarded as beneficial to the class of noteholders.

Briggs J held that the resolution was used as a negative inducement to deter noteholders from refusing the exchange. He went on to say that there was not a single noteholder who can be said to have accepted it unaffected by the coercive effect of the exit consent.

While in some cases the resolutions are the substance of what the issuer wishes to achieve, the issuer's primary plan was to substitute the old notes for new notes.

The purpose of the resolution was to destroy rather than enhance the value of the original notes. The court drew a distinction between this situation and that occurring pursuant to a corporate restructuring where a compromise might conceivably increase the value of notes held by creditors by protecting the company from liquidation.

In short, Briggs J concluded, finding in favour of the claimant on this point, that it was not lawful for the majority to lend its aid to the coercion of a minority by voting for a resolution which expropriates the minority's rights under their notes for a nominal consideration.

The case was due to be appealed, but the issuer entered liquidation ahead of the appeal, which did not then proceed. However, the appeal of a related case was heard with a contrasting outcome. In *Azevedo*,¹⁰ the Court of Appeal upheld the legality under English law of consent solicitations and consent payments. The amendment involved postponing the payment of interest due under the notes.

The claimants were minority noteholders who did not vote in favour of the resolution. They argued that it was unlawful to offer to pay to some noteholders, but not to all of them, payments which were not part of the proposal being voted on. This was argued to be a bribe or a vote contrary to interest the class of noteholders.

Assenagon was mentioned only in passing; its facts being considered too far away to be of assistance.

Lloyd LJ noted with approval the proposition that a majority must exercise its power in the interests of the class as a whole; *British America*.¹¹ In that case, the support of a minority noteholder had been obtained by the undisclosed promise of a potentially valuable consideration.

His Lordship distinguished that case on the basis that here, consent payments were offered to all members of the class. Full disclosure of the details of the scheme had also been made to all noteholders. Accordingly, it was concluded that a resolution is not necessarily invalid if the result of it being passed is to treat different members of the class differently.

It was also distinguished from the situation where the dissenting minority could not obtain the same benefits as the majority. The court in *Azevedo* noted the relevance of authority on schemes of arrangement where class issues are highly material. It is interesting to compare this with the cases concerning schemes of arrangement. It is also useful to note that as between different classes of noteholder, there will be no duty to consider the interests of the separate class.¹²

3 Class Issues in Formal Processes: Schemes of Arrangement

Background

A scheme of arrangement ("**scheme**") is a statutory procedure pursuant to Part 26 of the Companies Act 2006 ("**Companies Act**") whereby a company can make a compromise or arrangement with its creditors (or members) or any class of them. Schemes are commonly used to affect the restructuring of a distressed company's debt.

Schemes can be used for companies incorporated under the Companies Act as well as for companies incorporated outside of England and Wales, provided such companies have a sufficient connection to the UK.

The fact that a scheme can be used by any overseas company, provided the sufficient connection test is satisfied, has led to a significant increase in their use for overseas companies. Indeed, the sanction of the APCOA scheme,¹³ where the governing law of the underlying documentation was changed to English law to ensure the sufficient connection test was satisfied, has increased the options to restructure a company's debt where the underlying documentation may currently be governed by, say, New York law.

Constitution of the Voting Classes

Part of the scheme procedure involves creditors voting on the proposal put forward by, usually, the company. Creditors vote in one or more classes and for a scheme to become effective, subject to the sanction of the Court, a majority in number of those present and voting in person or by proxy and representing 75% in value of each class must vote in favour of the scheme.

The issue of classes raises two separate but connected issues. First, which creditors must be afforded the opportunity to participate in and vote on the scheme. Secondly, how many classes of creditors should there be. These issues are key. Every class needs to vote in favour of the scheme for it to become effective. Should the classes be incorrectly constituted (and this includes where creditors have been excluded from the scheme process when they should not have been), then the Court will have no jurisdiction to sanction the scheme, even if no prejudice has been suffered and the scheme is fair.

How are the classes to be determined? The classic test is as stated in *Sovereign Life*,¹⁴ namely that a class must be confined to those persons whose rights are not so dissimilar as to make it impossible for them to consult together with a view to their common interest.

This was considered in detail in *Re Hawk*.¹⁵ Hawk was an insolvent insurance company which proposed a scheme with three types of insurance creditors. All were included in the same class for voting purposes. At the sanction hearing, at first instance, the Court refused to sanction the scheme holding more than one meeting of creditors should have been convened. The decision was appealed. The Court of Appeal held that the question to consider was whether the rights of those who are affected by the scheme proposed are such that the scheme can be seen as a single arrangement or ought the scheme to be regarded, on a true analysis, as a number of linked arrangements. The Court held that the answer to that question involved an analysis (i) of the rights which are to be released or varied under the scheme, and (ii) of the new rights (if any) which the scheme gives, by way of compromise or arrangement, to those whose rights are to be released or varied. The Court held that the rights of creditors to be varied did not fall into more than one class, nor did the new rights to be given to those creditors under the scheme. It was essential to have regard to the fact that Hawk was insolvent and that the scheme proposed was an alternative to a winding up. In a winding up, after contingencies had been valued, all claims would be treated in the same manner. The Court held that neither the existing nor new rights of the creditors were so dissimilar as to make it impossible for the persons entitled to those rights to consult together with a view to their common interest, as members of a single class. It was added that a broad view should be taken of the meaning of class.

This issue was considered further in the case of *Re Telewest*.¹⁶ Telewest applied for leave to convene meetings of creditors to consider proposals for a scheme. The main creditors were dollar and sterling bondholders. The scheme proposed a debt for equity swap, and in order to determine the number of shares to be transferred to each bondholder, all claims had to be expressed in a single currency. Sterling bondholders argued that if the scheme was to proceed, there should be separate meetings of the sterling and US dollar bondholders. The Court gave leave for the creditors' meetings to be convened to consider the scheme. In doing so, it held that:

A. Any issues as to whether creditors formed one or more classes would be a question of judgment based on the circumstances of each case. Whether the sterling bondholders formed a separate class of creditors from the US dollar bondholders would depend on the similarity or dissimilarity of the

bondholders' rights against the company, not on any interests deriving from such rights.

- B. Although the different series of bonds had different maturity dates and interest rates and were in different currencies, there was still a great deal more which united the bondholders than divided them. The bonds were all in default, were all unsecured and would all rank *pari passu* in a liquidation.
- C. Where a scheme is put forward as an alternative to an insolvent winding up, the rights which the Court should take into account when deciding any class issues were the rights which the creditors would be entitled to in a winding up. Although the provisions of a scheme can differ from the position in a liquidation, this may give rise to class issues if the difference produces a result which affects one group of creditors in a different way to other groups of creditors.
- D. However, the Court did not consider that the average exchange rate conversion method created a separate class of sterling bondholders. The sterling and US dollar bondholders formed a single class as there was insufficient dissimilarity to constitute separate classes and enough similarity to group both sets of bondholders in the same class. The average exchange rate may produce different financial results for the US dollar bondholders and the sterling bondholders but such a consequence was insufficient to create separate classes as their rights were still substantially the same.

A separate but related issue is who must be included in a scheme and be given the opportunity to vote on it.

If applicants are able to show that certain classes of creditor will not be affected by the scheme, can they ignore such creditors? This may be attractive where they are opposed to the scheme. If so, it would follow that only creditors who are affected by a proposed scheme need to be consulted. The issue was considered by the Court of Appeal in *Re MyTravel*.¹⁷

MyTravel was in financial difficulties and sought to enter into a consensual agreement with its creditors. A group of bondholders refused the original offer made to them. As a result, MyTravel proposed a scheme whereby its business and assets were to be transferred to a new company. The new company would assume some of the liabilities of MyTravel but the majority of the liabilities would be converted into equity in the new company. However, crucially, the bondholders' debt would not be transferred and would therefore remain as a claim against the old company. This was on the basis that MyTravel considered that if it went into liquidation, the bondholders would have no prospect of receiving anything (as their debt would be subordinated) and so had no economic interest in the company. They were therefore not included, and would be excluded for voting purposes.

The Court of Appeal considered this point, albeit only on an *obiter* basis. Whilst not technically a class issue, the question of whether MyTravel was obliged to consult with bondholders in respect of the scheme could, as mentioned, ultimately effect whether the Court had jurisdiction to sanction the scheme. The Court commented as follows:

- A. As a matter of principle, the jurisdiction of the Court to sanction the scheme could be exercised without regard to the wishes of a class of creditors who had no real interest in the assets of the company.
- B. When ascertaining the rights of a creditor, it was appropriate to see if those rights could realistically only be enforced in a winding up and, if so, to use a notional winding up as a method of assessing what those rights would be. This was particularly relevant where, on the facts, there were arguments to support the view that a liquidation was the only real alternative to restructuring through the scheme. The fact that the bonds may have some value in the market, or that the creditors may have been prepared to do a deal and so receive something in a consensual restructuring, was

irrelevant to the bondholders' actual economic interest in the company (assessed by reference to a winding up). Where the Court concludes that a creditor's prospect of recovery in a liquidation is merely a theoretical or fanciful possibility, that is sufficient to conclude that the creditor has no economic interest in the company.

- C. On the facts, it appeared that MyTravel would have a huge shortfall in relation to ordinary unsubordinated creditors and there would be no return to the bondholders or subordinated creditors, so the bondholders had no realistic economic interest in the company and therefore had no right to be consulted in relation to the scheme.

The issue was considered again in *Re Bluebrook Ltd*.¹⁸ Here a scheme was proposed to affect a debt restructuring. The company had both senior and mezzanine debt and pursuant to an intercreditor agreement the mezzanine debt was fully subordinated to the senior debt. The scheme proposed did not include the mezzanine lenders on the basis that the value of the group's assets was less than the senior debt and there was no realistic possibility of a return to the mezzanine lenders.

The case was interesting in that the mezzanine lenders looked to challenge the valuation that the senior lenders had produced to show that the value of the assets was less than the value of the senior debt as opposed to otherwise challenging their exclusion from the scheme. The mezzanine lenders sought to demonstrate that they did have an economic interest in the group and therefore should have been involved in the scheme as a class of creditor entitled to vote. The Court rejected the method of valuation put forward by the mezzanine lenders and instead emphasised that the aim of the valuation exercise was to answer the question of how much a buyer would pay for the group now, on a going concern basis. On that basis, the Court held that the mezzanine lenders did not have an economic interest in the company, would not be affected by the scheme and therefore they did not need to be included as a class of creditor entitled to vote.

Summary

The level of bond restructurings, especially in the high yield arena, is likely to increase in the short term. Understanding the tools available to restructure such bonds and the legal challenges that may be faced is key. This article has shown how the law has developed in recent years to support stakeholders in effecting such restructuring. The extent to which these tools can be used is likely to be tested as more restructurings come to the market. As a result, the law is likely to develop further.

Endnotes

1. Including the High Court's decision in *ARM Asset Backed Securities S.A. [2013] EWHC 3351*, which held that limited recourse provisions do not prevent issuers being insolvent on either a balance sheet or cash flow basis, and the Commercial Court's decision in *Bank of New York Mellon v GV Films Ltd [2009] EWHC 3315* that although the issuer was not insolvent, a proposed scheme of arrangement still fell within the provisions of the "Insolvency" clause, which the court found did not apply only in the context of insolvency.
2. In the matter of *Colt Telecom Group plc [2002] EWHC 2815*.
3. *BNY Corporate Trustee Services Ltd and others v Eurosail-UK 2007-3BL PLC and others [2013] UKSC 28*.
4. *Re Cheyne Finance (No. 2) [2008] Bus LR 1562*.
5. *Elektrim SA v Vivendi Holdings 1 Corp [2008] EWCA Civ 1178*.
6. *Concord Trust v The Law Debenture Trust Corporation plc [2005] 1 WLR 1591*.
7. *British America Nickel Corp v MJ O'Brien Ltd [1927] AC 369*.
8. *Assenagon Asset Management SA v Irish Bank Resolution Corporation Ltd [2012] EWHC 2090 (Ch)*.
9. *Redwood Master Fund Limited and Others v TD Bank Europe Limited and Others [2006] 1 BCLC 149*.
10. *Azevedo and another v Imcopa Importação, Exportação e Indústria de Óleos Ltda and others [2013] EWCA Civ 364*.
11. *British America Nickel Corp v MJ O'Brien Ltd [1927] AC 369*.
12. *Myers and another v Kestrel Acquisitions Ltd and others [2015] EWHC 916*.
13. *APCOA Parking Holdings GmbH [2014] EWHC 3849 (Ch)*.
14. *Sovereign Life Assurance Co v Dodd [1892] 2 QB 573*.
15. *Re Hawk Insurance Company Limited [2001] 2 BCLC 480*.
16. *Re Telewest Communications Plc [2004] EWHL 924(Ch)*.
17. *Re MyTravel Group plc [2004] EWHC 2741 (Ch)*.
18. *Re Bluebrook Ltd and others [2009] EWHC 2114*.

Acknowledgment

The authors would like to thank Emma Bardetti and Caroline Grant for their invaluable assistance in the preparation and finalisation of the chapter.

**Alicia Videon**

Olswang LLP
90 High Holborn
London, WC1V 6XX
United Kingdom

Tel: +44 20 7067 3640
Fax: +44 20 7067 3999
Email: alicia.videon@olswang.com
URL: www.olswang.com

Alicia is a Partner at Olswang and specialises in restructuring, insolvency and non-performing loan sales. She has significant experience representing lenders and special servicers, as well as other stakeholders, involved in local and multi-jurisdictional work-out assignments. Alicia has advised on a number of the most recent high profile insolvencies and restructurings involving commercial real estate.

**Julian Turner**

Olswang LLP
90 High Holborn
London, WC1V 6XX
United Kingdom

Tel: +44 20 7067 3552
Fax: +44 20 7067 3999
Email: julian.turner@olswang.com
URL: www.olswang.com

Julian is a Partner at Olswang and specialises in insolvency and restructuring matters, often with a cross-border element, as well as providing structuring advice on complex finance transactions. Julian also has financial services and banking experience and has acted on a number of companies act schemes of arrangement. Julian has undertaken transactions in a number of industry sectors including media, technology, financial services, insurance and leisure. Julian has significant Middle East experience having spent three years in Abu Dhabi.

OLSWANG

Olswang is a pioneering firm with a distinctive approach and a progressive culture. Thanks to our connected, committed and commercial people, we are the law firm of choice for leading entrepreneurs and innovators and have established a commanding reputation for truly changing the face of business. Headquartered in London, Olswang has an international presence spanning Belgium, France, Germany, Spain, the UK and Singapore.

We align our services to the way our clients think about the future and help our clients stay connected, informed and sharp within their fields. Our people are our business. Working with the very best companies calls for ingenuity, verve and judgment. Our clients rely on our capability, but they value our distinctive personality and culture. We know that if our people reach their potential, then our clients can, too.

Other titles in the ICLG series include:

- Alternative Investment Funds
- Aviation Law
- Business Crime
- Cartels & Leniency
- Class & Group Actions
- Competition Litigation
- Construction & Engineering Law
- Copyright
- Corporate Governance
- Corporate Immigration
- Corporate Tax
- Data Protection
- Employment & Labour Law
- Environment
- Franchise
- Gambling
- Insurance & Reinsurance
- International Arbitration
- Lending & Secured Finance
- Litigation & Dispute Resolution
- Merger Control
- Mergers & Acquisitions
- Mining Law
- Oil & Gas Regulation
- Patents
- Pharmaceutical Advertising
- Private Client
- Private Equity
- Product Liability
- Project Finance
- Public Procurement
- Real Estate
- Securitisation
- Shipping Law
- Telecoms, Media & Internet
- Trade Marks



59 Tanner Street, London SE1 3PL, United Kingdom
Tel: +44 20 7367 0720 / Fax: +44 20 7407 5255
Email: sales@glgroup.co.uk

www.iclg.co.uk