gategroup: UK court rules Restructuring Plans are insolvency proceedings

The ruling in gategroup may significantly impair international recognition of UK Plans post Brexit. Restructuring Plans were only introduced last June under the CIGA reforms.

The Court's decision arose out of an application by gategroup Guarantee Limited for the Court's permission to convene meetings of its creditors to vote on and, if thought fit, approve a Restructuring Plan that would amend certain debt instruments issued by members of the gategroup group.

The group is the world's largest provider of airline catering services, with a global network spanning approximately 60 countries and territories on six continents.

Comment

Mark Fennessy, partner at law firm McDermott Will & Emery, said the gategroup ruling had far-reaching implications:

"The decision in gategroup may have signalled a high-water mark for the utility of the new UK Restructuring Plan for debtors and debt issuers especially when it began to show such promise following decisions in the Virgin Atlantic, Pizza Express and the Deep Ocean restructurings.

> "The decision in gategroup to class the Restructuring Plan as an insolvency proceeding may significantly impair the means to have such a plan recognised internationally especially post-Brexit when it has lost the automatic recognition mechanisms under European regulations."

"Post Brexit the Lugano Convention and the Hague Conventions formed the foundation of a likely path to recognition and assistance for UK Restructuring Plans.

"There was a hope and expectation that the Restructuring Plan would not fall into the bankruptcy exception under either of the Lugano or the Hague Conventions and therefore, like its sibling the UK Scheme of Arrangement, would benefit from these recognition mechanisms," said Fennessy.

"It looks like a door has been shut on this possibility at such a formative stage of the Restructuring Plan, which only came into force in late June last year as a part of the Corporate Insolvency & Governance Act 2020 (CIGA).

"Where a door shuts another would need to be opened for debtors and we at McDermott are already exploring alternative ways of bypassing this decision in relation to future UK restructuring options which are now very likely to be needed," Fennessy concluded.

The judgment explained

Clifford Chance acts for gategroup, led by restructuring head Philip Hertz. They were represented in court by Felicity Toube QC and Riz Mokal of South Square.

In its judgment, the Court determined that Restructuring Plans were insolvency proceedings, so were not covered by the Lugano Convention on the recognition of civil and commercial judgments between the EU, Norway, Iceland, Switzerland and Denmark

The UK is currently applying to become a member of the Lugano Convention, following its automatic withdrawal on 31 December 2020, at the end of the Brexit transition period

This decision does not directly affect Schemes of Arrangement.

The Lugano Convention

According to a note by Clifford Chance, over the course of a two day hearing, the UK Supreme Court considered whether the Convention on Jurisdiction and Enforcement of Judgments in Civil and Commercial matters between the EU, Switzerland, Iceland, Norway and Denmark (the Lugano Convention) applied to UK Restructuring Plans.

If it did, then it was accepted that the Court would not have jurisdiction to sanction the Plan.

If, however, Restructuring Plans fell outside the scope of the Lugano Convention because they constitute "proceedings relating to the winding-up of insolvent companies or other legal persons, judicial arrangements, compositions and analogous proceedings " (the "bankruptcy exclusion"), then the Court would have jurisdiction to sanction the Plan.

This issue arose because one of the debt instruments subject to the Restructuring Plan contains an exclusive Swiss law jurisdiction clause.

Under the Lugano Convention, proceedings relating to "civil and commercial matters" must be brought (subject to certain exemptions) in the jurisdiction benefiting from the exclusive jurisdiction clause.

The Court's decision

The Court held that Restructuring Plans fell within the bankruptcy exclusion and were not, therefore, civil and commercial matters. In reaching this decision, the Court held that:

- The Lugano Convention should, to the extent possible, dovetail with the recast EU Regulation (2015/848) on Insolvency Proceedings (the EUIR) such that, if a proceeding fell within the EUIR, then it should not fall within the Lugano Convention;
- The Court needed to examine the substance of the Restructuring Plan procedure to determine whether it was an insolvency procedure or not;
- To be an insolvency proceeding, the Court held that:
  - The proceedings must be collective proceedings;
  - They must be based on laws relating to insolvency and have as their purpose rescue, adjustment of debt, reorganisation or liquidation; and
  - They must encompass at least one of the following:
    - (a) The debtor is partially or totally divested of its assets;
    - (b) The assets and affairs of the debtor are subject to control or supervision by a court; or
    - (c) A temporary stay is imposed, by a court or by operation of law, on individual enforcement proceedings to enable negotiations to take place between the debtor and its creditors.

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Restructuring Plans had all of the hallmarks of insolvency proceedings. In particular:

– Collective proceedings: To be collective, the proceedings need to affect (or have the potential to affect) a "significant part of the creditors to whom a debtor owes all or a substantial proportion of the debtor's outstanding debts provided that the claims of those creditors who are not involved in such proceedings remain unaffected". The Restructuring Plan met this criteria as it affected all of the Plan Company's financial creditors;

– Law relating to insolvency: While the legislation enacting Schemes and Restructuring Plans is contained in the Companies Act (and not the Insolvency Act), this was not determinative. Unlike Schemes which, as explained above, are available to all companies (whether solvent or not), Restructuring Plans are available only to companies facing actual or anticipated financial difficulties. Furthermore, the purpose of the Restructuring Plan must be to eliminate, reduce, prevent or mitigate, these difficulties. The fact that Article 1(1) of the EUIR made clear that proceedings which had as their purpose the "avoid[ance of] the debtor's insolvency or the cessation of the debtor's business activities" could be considered insolvency proceedings even if they "may be commenced in situations where there is only a likelihood of insolvency", meant that Restructuring Plans represented a "law relating to insolvency";

– Subject to the supervision of the Court: Finally, the Court considered that Restructuring Plans met the third requirement set out above, as the Court had supervision of the procedure. As the Court noted: "There is undoubtedly significant court involvement. No plan meeting may be convened without the court's order. The composition of the classes must be approved by the court. No plan can become effective until sanctioned by the court. At all stages the court is required to reach a judgment based on established principles and all interested stakeholders are entitled to be heard by the court."

European bankruptcies fell and then slightly rose last year

Eurostat, the EU's statistics body, has prepared some ground-breaking tables based on 'experimental statistics' gathered on a voluntary basis from around 20 EU and EFTA member states.

As such these figures are incomplete and only go up to the third quarter of last year. On the other hand they provide a uniquely broad illustration of the process of 'creative destruction' in modern Western economies, and the initial impact of the Covid-19 crisis.

Seeing Eurostat's statistics for the end of last year and for 2021 when they come out will be fascinating, especially when Government support schemes for businesses start to be wound down.

Bankruptcy numbers continue to fall

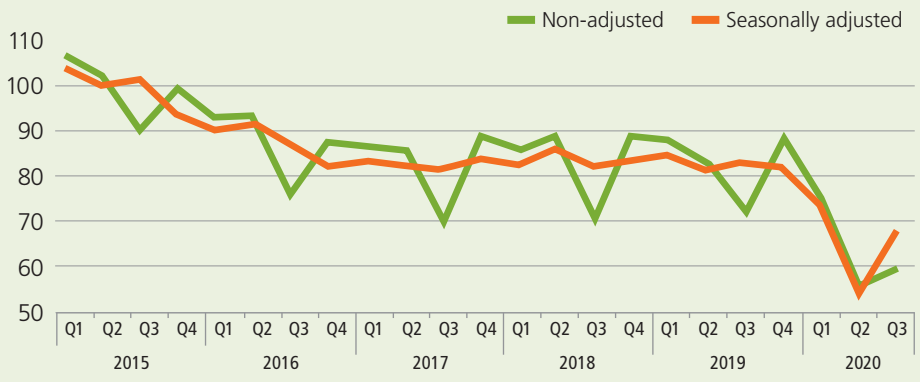
In further Eurostat research not shown in these particular tables, the number of bankruptcy declarations continued to decrease in the third quarter of 2020 compared with the same quarter of 2019, by 17.7 per cent in the EU and 19.8 per cent in the euro area.

> The largest decreases in the number of declarations of bankruptcies were found in Lithuania (-0.9 per cent), France (-34.9 per cent) and Belgium (-32.3 per cent).

The highest increases of bankruptcy declarations were observed in Estonia (+83.5 per cent), Portugal (+40.3 per cent) and Spain (+6.3 per cent).

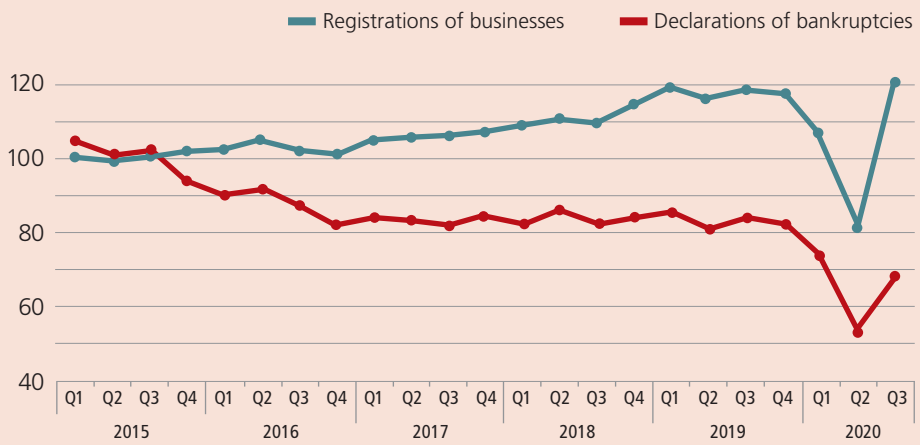
Eurostat observed: "The relatively low number of bankruptcies in many countries may be explained by the government measures supporting businesses during the crisis that may have allowed businesses that would otherwise have filed for bankruptcy to continue their activities."

EU (available countries), declarations of bankruptcies
Q1 2015 to Q3 2020 (2015=-100)



Source: Eurostat

Registrations of businesses and declarations of bankruptcies in the EU
Q1 2015 - Q3 2020, seasonally adjusted (2015=-100)



Source: Eurostat