Restructuring Plans and Chapter 11

A Transatlantic Perspective

Akin℠

Key Takeaways

1.

The restructuring plan regime - including, for the first time under English law, cross-class cram down - was introduced in June 2020. Our experience with restructuring plans proposed to-date has been that the English courts have (for the most part) implemented this new tool flexibly, pragmatically and commercially.

2.

Prior to and at the time of its introduction, comparisons were inevitably made between the restructuring plan and the chapter 11 reorganization process. The initial concerns about the absence of certain tools found in chapter 11 (e.g., a statutory absolute priority rule, automatic stay, or provision for post-petition super priority debtor-in-possession (DIP) financing), do not seem to have prevented the restructuring plan from being utilized effectively by distressed businesses in England.

3.

Although certain restructuring plans have been challenged before the courts, restructuring plans have, to-date, been swifter and more predictable than a free-fall bankruptcy case in chapter 11. However, we have yet to see certain points play out before the English courts, including extensive challenges from subordinated financial creditors or valuation disputes in which challenging stakeholders put their own evidence before the court. In those circumstances, a further rise in in-court challenges and a lengthier process may follow.

© 2023 Akin Gump Strauss Hauer & Feld LLP

Introduction

When the Corporate Insolvency and Governance Act 2020 (CIGA) introduced the restructuring plan in England[1], comparisons with plans of reorganization under chapter 11 of the United States Bankruptcy Code (U.S. Bankruptcy Code) were inevitable.

A rundown of the similarities between the two processes is easy: both are court-sanctioned and based on classes, with the ability to compromise claims and/or interests held by secured creditors, unsecured creditors and equity holders (including through cross-class cram down). In addition, neither interferes with directors' powers of management (in the U.S., absent significant showings of mismanagement or fraud). Despite their similarities, there are some obvious differences: different voting thresholds, U.S. statutory authority to obtain debtor-in-possession (DIP) financing, the "absolute priority rule" in chapter 11, and the lack of a statutory automatic stay in England. For ease of reference, the table below compares the key features of the English restructuring plan regime and chapter 11. Now, with the benefit of more than two and a half years of learning on English restructuring plans, it is an opportune time to re-visit those initial comparisons. In this article, we will consider some of the key features of the English regime, including the experience from the case law to-date, how the developments in the English cases contrast with the position and approach under chapter 11, and the practical significance of those differences.

1 The restructuring plan regime introduced by CIGA applies across the U.K.. This article focuses on, and considers, the restructuring plans proposed in England to-date.

Key Comparison One

Cross-Class Cram Down

Before June 2020, only chapter 11 offered the ability to cram down a dissenting class (or classes) of creditors.

While the English scheme of arrangement allowed dissenting stakeholders to be forcibly bound *within* a class, no English restructuring process had a cross-class cram down mechanism. That changed with the restructuring plan. Now, the long-held ability of chapter 11 to bind dissenting classes has made its way into the English restructuring toolkit.

Conditions to Cram Down

In England, cross-class cram down will be permitted if the court is satisfied that (i) none of the members of a dissenting class would be any worse off under the restructuring plan than they would be in the event of the "relevant alternative" (Condition A or the "no worse off" test), (ii) at least one class that would receive a payment or would have a genuine economic interest in the company in the event of the relevant alternative has voted in favor of the restructuring plan (Condition B), and (iii) it is appropriate (usually by reference to considerations of fairness) for the court to exercise its discretion to sanction the plan.

The "relevant alternative" to the plan is whatever the court considers would be most likely to occur in relation to the company if the plan were not sanctioned. While English courts have traditionally been reluctant to second-guess a debtor's evidence on the alternative to a scheme of arrangement, we have seen courts more willing to probe what is before them for restructuring plans and, in *Hurricane Energy*, reject what was proposed by the company as the sequence of events in the "relevant alternative" and arrive at a different finding. In this case (concerning an oil and gas company), the "relevant alternative" was not an insolvency process, but a continuation of trade for one year, followed by a decommissioning process. The judge considered that, during that year, it was possible that events could unfold in a manner different to that contemplated by the company and, as a result, reached the conclusion that shareholders may not be better off under the plan than in the relevant alternative.

In chapter 11, section 1129 of the U.S. Bankruptcy Code governs confirmation of a plan of reorganization and expressly authorizes the bankruptcy court to approve a plan over the objection of creditors under certain circumstances. Specifically, provided that all other requirements for confirmation are met, including, for example, that at least one impaired class has voted to accept the plan and that each holder of a claim or interest in an impaired class has accepted the plan or will receive no less than the amount that such holder would receive if the debtor were liquidated under chapter 7 of the U.S. Bankruptcy Code (known as the "best interests of creditors" test), a bankruptcy court will confirm a chapter 11 plan with non-accepting classes if, with respect to any impaired non-accepting class, (i) the plan does not discriminate unfairly and (ii) the plan is fair and equitable.

In order to be "fair and equitable", a plan must satisfy the "absolute priority rule", which requires that no impaired non-accepting class of creditors or interest holders (i.e., stakeholders, including shareholders) receive less than 100 percent of its (pre-petition) claim or interest if a more junior creditor (or interest holder) receives anything under the plan on account of its claim or interest. For the absolute priority rule to be satisfied:

- Secured creditors must retain their collateral and receive a deferred cash payment equal to at least the value of that collateral or realize the "indubitable equivalent" of their claim (which broadly means that the plan provides (i) the secured creditor with the present value of its allowed secured claim and (ii) a collateral package that attempts to ensure the safety of the secured creditor's principal).

- Unsecured creditors must receive or retain property of a value (as of the effective date of the plan) equal to the allowed amount of such claim. If they do not, no value may be distributed to creditors or interest holders that are junior to the impaired non-accepting class.
- Interest holders must receive or retain property of a value (as of the effective date of the plan) equal to the greater of the allowed amount of any fixed liquidation preference to which such holder is entitled, any fixed redemption price to which such holder is entitled, or the value of such interest. If they do not, no value may be distributed to interest holders that are junior to the impaired non-accepting class unless that class is paid in full.

Practically, what does this mean?

Plan Supporters

In order to cram down a class under either regime, one or more classes must vote in favor of the plan. In the U.S., the accepting class(es) must be impaired (i.e., not receiving a 100 percent recovery on account of its claim under the plan). In England, there is no requirement that the accepting class(es) be impaired, but the restructuring plan requires that Condition B is satisfied. This would appear to be a relatively low threshold to reach.

The Alternative Outcome

Both regimes require valuation evidence to demonstrate recoveries in the alternatives and, in particular, require a debtor to demonstrate greater recoveries under the plan than under an alternative outcome(s). Under an English restructuring plan, the comparator, or "relevant alternative", will often (but not always) be an insolvency process. Where a cross-class cram down is proposed under an English restructuring plan, a comparative analysis is required under the "no worse off" test, which requires valuation evidence to prove greater (or not worse) recoveries for the dissenting classes under the plan than in the relevant alternative. As we discuss below, this is emerging as a key battleground in English restructuring plans. Under chapter 11, the comparator will always be a chapter 7 liquidation, which typically reflects a lower valuation when compared to a going-concern valuation. In chapter 11, satisfying the "best interests of creditors" test requires a comparison of creditor recoveries under the proposed plan and a hypothetical liquidation of each debtor. Given the suboptimal circumstances surrounding a chapter 7 liquidation, a debtor can typically succeed in demonstrating that creditors will do better under the plan than they would under a liquidation.

As noted above, the "best interests of creditors" test applies to all chapter 11 plans: it requires that each impaired creditor (not class) either accepts the plan or receives not less under the plan than such creditor would receive in a hypothetical chapter 7 liquidation (which is essentially the "floor" for plan recoveries). Importantly, this test applies irrespective of whether (i) a cross-class cram down is in fact proposed, or (ii) an individual dissenting impaired creditor forms part of an assenting or dissenting class. No equivalent "best interests of creditors" test exists for English restructuring plans (the "no worse off" test applies only to cram downs and solely in relation to members of dissenting classes, although the court will always be concerned to understand whether all creditors have a prospect of receiving a larger or faster return on their debts under the plan than they would in the alternative scenario).

Court Discretion

If certain statutory and other legal requirements are satisfied (which include, among others, that the plan was not proposed in bad faith and any settlements contained therein satisfy applicable legal standards), a U.S. bankruptcy court will confirm a chapter 11 plan. That is not the case for an English court, which has overriding discretion as to whether to sanction a plan, even where voting thresholds have been achieved and, for plans involving cram down, Conditions A and B are satisfied.

While the English courts have not yet exercised their discretion to decline sanctioning a restructuring plan that has come before it, one has come close. In *Hurricane Energy*, the judge did not sanction the plan as he did not consider that Condition A (the "no worse off" test) was satisfied. However, he indicated that if that condition *had* been satisfied, he would not have exercised his discretion to sanction the plan. The English court's overriding discretion is not new (the court has an equivalent discretion for schemes of arrangement), but where the court is empowered, through cram down, to override the vote at a class meeting, the exercise of that discretion is perhaps even more carefully considered. This brings an element of uncertainty which does not exist to the same extent in chapter 11 plans.

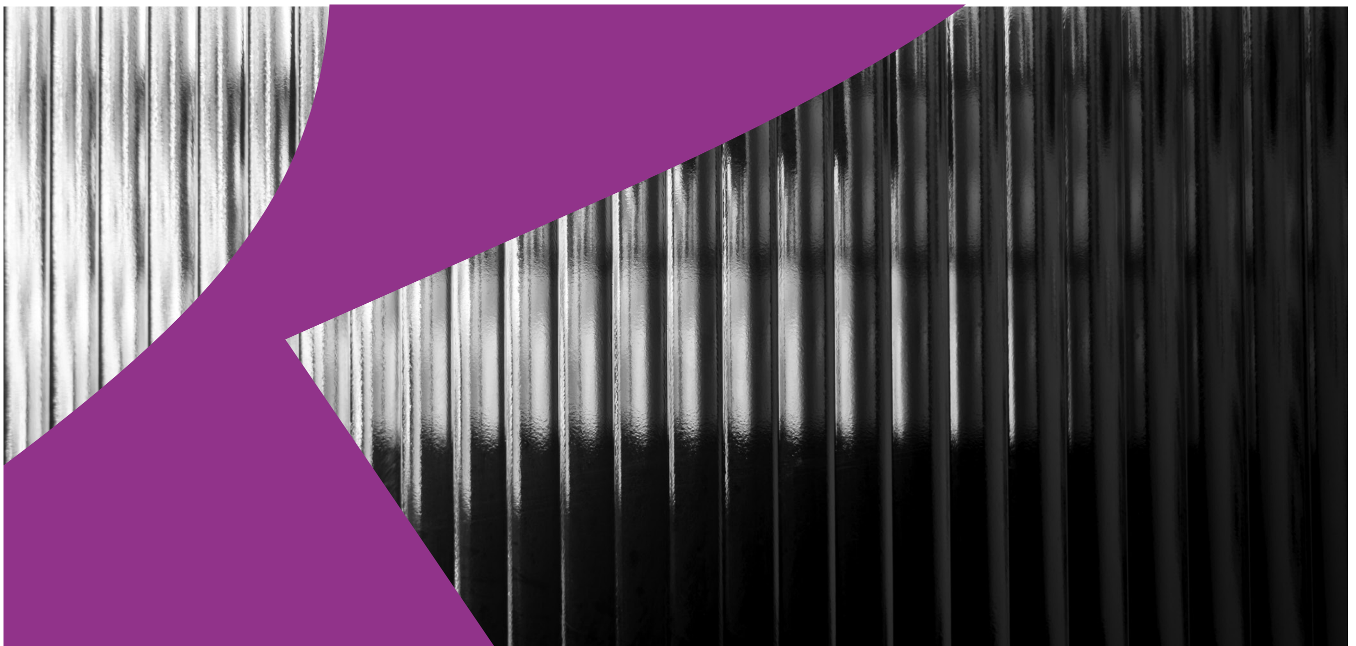
Absolute Priority Rule

Significantly, the absolute priority rule, described above and designed to protect impaired non-accepting classes of creditors or interest holders, does not have a home in the English framework. It was considered by legislators, but not adopted.

The restructuring plan therefore has the potential to allow junior creditors or shareholders to receive returns under the plan at the discretion of the in-the-money creditors. This is a flexibility which chapter 11 lacks. This was evidenced in the *Virgin Active* restructuring plan. Under that plan, existing shareholders retained their equity and, as a result, the benefit of any future upside in the plan companies. This was accepted by the court, even though, in the insolvency

© 2023 Akin Gump Strauss Hauer & Feld LLP

waterfall, the shareholders ranked lower in priority than certain unsecured dissenting creditors and the claims of those unsecured creditors were not to be satisfied in full under the plan. In a more express recognition of the flexibility provided by the English regime, when sanctioning the recent *Houst* plan, the judge noted that, in relation to restructuring plans,"a departure from the priority [in insolvency] is not in itself, unlike the position in...Chapter 11... fatal to the success of the plan".



© 2023 Akin Gump Strauss Hauer & Feld LLP

Key Comparison Two

Treatment of Out-of-the-Money Stakeholders

Determining where value breaks and identifying the fulcrum creditor class is critical in any restructuring. Where a class of creditors is to be crammed down, it becomes even more important: both for stakeholder treatment and the sway they hold in proceedings.

In England, all those whose rights are affected by a restructuring plan are entitled to vote on it, which the court has interpreted broadly to include creditors and, where a debt-for-equity swap is proposed, shareholders (*Hurricane Energy*). However, if out-of-the-money creditors or shareholders are "affected by" a plan, the debtor can apply to the court to *exclude* that class of stakeholders from voting on the plan, on the basis that none of the members of that class has a genuine economic interest in the company (a "901C(4) application"). In practice, what this means for stakeholders facing disenfranchisement is that they will need to challenge the application at the convening hearing (when the 901C(4) application is made), being an earlier point in the process than if a 901C(4) application were not made and the debtor sought cram down of dissenting classes (in which case, the challenge to cram down would be made at the sanction hearing). The challenging stakeholder would need to present evidence to rebut the company's suggestion that its class has no genuine economic interest in the company on a compressed timeframe, which is likely to prove challenging. From the debtor's perspective, the benefit of a 901C(4) application is that if a class is (or classes are) excluded from voting on the plan, there is certainty earlier in the process and no need to hold meetings of those excluded classes (or invoke cram down).

At the time of publication, only one company has sought to take advantage of this provision. Smile Telecoms applied to the court to convene a single meeting of creditors to vote on its (second) restructuring plan and in so doing, successfully excluded all other classes of creditors, and its shareholders, from voting on the plan. Relying on valuation evidence presented by the debtor, the court concluded that only the super senior lender class had any genuine economic interest in the company. While new ground was broken with this application, each case will differ on its facts and it will be interesting to see how this area develops, particularly if valuation evidence is produced to oppose a 901C(4) application in future.

In *Virgin Active*, the judge was clear that if a stakeholder group is out-of-the-money (but has not been excluded from voting on the basis that it has no genuine economic interest), the court will place little weight on that group's objections when deciding whether to sanction the plan. The judgment went further in noting that those creditors who were "in-the-money" should direct how the benefits of the restructuring (the so-called "restructuring surplus") should be distributed.

Chapter 11 takes a slightly different approach to out-of-the-money stakeholders. Significantly, an impaired class of stakeholders not entitled to any recovery under a plan may be deemed to reject such plan and thus, their vote will not be solicited. That class can still raise confirmation objections, including those based on violations of the absolute priority rule, valuation (which is common in the case of interest holders), unfair discrimination and the "best interests of creditors" test. Indeed, it is not uncommon for out-of-the-money creditors to insert themselves into the case at the outset and tactically threaten to raise objections or bring litigation in an attempt to gain bargaining leverage. So, while both processes provide a forum for challenges by out-of-the-money stakeholders, under an English restructuring plan the objections of out-of-the money stakeholders may carry less weight (both before a judge and in negotiations) compared to the practice under chapter 11.

© 2023 Akin Gump Strauss Hauer & Feld LLP

Key Comparison Three

Mounting a Challenge

The English court was well prepared for many aspects of the restructuring plan regime, given its similarity in many respects to the schemes of arrangement. It was arguably less prepared for challenges to a plan. Historically, English schemes of arrangement have seldom been contested. However, that trend is changing with the restructuring plan. Of the 15 plans proposed to-date in England, six have seen challenges before the court (with stakeholders expressing concern outside of the courtroom in a number more).

Bases of Challenge

In England, a stakeholder can challenge a restructuring plan at the convening or sanction hearing or both.

At the convening hearing, the plan proponent will seek the court's permission to convene meetings of the concerned stakeholders to vote on the restructuring plan. At this stage, a challenge is likely to be focused on class composition. Classes are composed by reference to the stakeholders' existing rights (prior to the plan) and proposed rights under the restructuring plan (similar to the approach in schemes of arrangement). In a few of the cases to-date, there has been suggestion that debtors may be tempted to propose an artificially large number of classes to more easily satisfy Condition B of the cross-class cram down test – the rationale being that if there are a greater number of classes, it is more likely that at least one of those classes will receive a payment or have a genuine economic interest and vote in favor of the plan. This is an interesting contrast to the often-expressed concern that, where a scheme of arrangement is proposed, debtors may seek to convene *fewer* classes (given that in a scheme of arrangement, each class essentially has a veto right in respect of the approval of the scheme of arrangement).

The U.S. Bankruptcy Code allows claims and/or interests to be classified together only if such claims and/or interests are substantially similar. Allegations of artificial impairment or allegedly improper classification of claims and accusations that a debtor has "gerrymandered" classes or "manufactured" an impaired, consenting class in order to more easily satisfy the cram-down requirements are often brought before the bankruptcy court. Courts typically defer to a debtor's proposed classification of claims and interests and thus require clear evidence of class manipulation to find in an objector's favor. In England, we are yet to see similar allegations made before the court in relation to restructuring plans, although future disputes on class manipulation are certainly possible and are likely to raise interesting questions as to how the court will approach considerations of fairness.

Separately, as we have explained above with regard to 901(C)(4) applications, a company may seek to exclude out-of-the-money classes of stakeholders whose rights are affected by a restructuring plan on the basis that the relevant class does not have a genuine economic interest in the company. No disenfranchised class appeared in person before the court to oppose the only 901(C)(4) application made to date (in the second *Smile Telecoms* restructuring plan). A more activist approach may be taken, however, in future cases, particularly where recoveries in the relevant alternative are disputed.

In England, the sanction hearing takes place after the meeting(s) to vote on the plan and it is at this stage that the court will consider whether it is appropriate to confirm the plan (with or without cram down, as applicable). In that respect, it is similar to a confirmation hearing in chapter 11. In practice, it is likely that only a stakeholder in a dissenting class would challenge cram down at the sanction hearing. A disgruntled stakeholder in a class which approved an English restructuring plan would not be prevented from raising objections at the sanction hearing, and may choose to do so by reference to procedural irregularities or on fairness grounds (perhaps suggesting that the plan offers less

than liquidation value or that other creditors will receive disproportionate fees in connection with the restructuring, which has influenced their vote). However, even in the face of a challenge of this type, if the court considers the restructuring plan to be fair and equitable (and provided that all other procedural aspects have been satisfied), it is unlikely to decline to sanction the plan simply because a dissenting stakeholder takes issue with the outcome of the meeting of the class of which it forms part. By contrast, certain challenges can be raised by stakeholders in accepting and rejecting (or deemed rejecting) classes in a U.S. chapter 11 case, which broadens the scope and likelihood of challenge. For example, as noted above, the "best interests of creditors" test (a confirmation requirement) establishes a "floor" recovery for creditors. Individual stakeholders (regardless of whether the class accepts or rejects the plan) have the right to raise objections based on this test, therefore assuring that they will receive at least what they would in a chapter 7 liquidation, even if the class to which they belong votes to accept the plan. Thus, *any* individual creditor or equity holder, regardless of the class to which it belongs, can raise a best interests objection. Additionally, the debtor always has an affirmative burden in connection with satisfying the plan confirmation requirements to show that in respect of every creditor the "best interests of creditors" test has been met.

The Importance of Valuation Evidence

In England, we have begun to see the question of recoveries in the relevant alternative emerge as a key battleground in the contested restructuring plans to date; e.g., *Virgin Active and Amicus Finance*, although a full valuation dispute with competing expert evidence has yet to play out before the English court.

In chapter 11, hotly contested valuation disputes are not uncommon. This is in part due to the significance of valuation in assessing the rights and recoveries of various stakeholders under the plan, but is also the natural consequence of the subjective nature of valuation. Proceedings to consider confirmation of a chapter 11 plan often involve the debtor and its supporting creditor groups, on the one hand, and the dissenting party (or parties), on the other, presenting competing valuation evidence to the bankruptcy court. In practice, financial advisers are involved at an early stage behind the scenes, advising on (among other things) the valuation of the debtor's business and the related debt or equity securities that will often form the basis of creditor recoveries. These financial advisors must address valuation issues and, if contested, present expert reports on their valuation conclusions and be subject to extensive questioning in depositions and cross-examination at trial. Experience suggests that U.S. bankruptcy courts will typically take a commercial approach to assessing the appropriateness of competing valuation methodologies, preferring valuations that are supported by market indicators of value, and disfavoring academic or "desk top" valuations that lack supporting market evidence.

Has the U.S. approach to valuations been mirrored in the English regime? It is notable that, during the legislative process in which the English restructuring plan was developed, the English judiciary expressed concern about the valuation evidence presented in chapter 11, describing it as "*contentious and often speculative*", enabling out-of-the-money stakeholders to claim an unwarranted benefit in restructuring negotiations. The judiciary specifically proposed the concept of the "relevant alternative" as a "*principled difference*" to the chapter 11 approach to valuation. In *Virgin Active*, the judge had cause to consider whether the debtor (and its advisers) should have conducted a market testing process to determine value. In concluding that a market test was not required and that a lack of market testing did not make a valuation report inherently unreliable, the judge referenced academic commentary which considered the chapter 11 approach to valuations, being one based on professional valuation opinions rather than current market prices established through an auction process. That may be a nod of approval for chapter 11 but may be limited to the basis of valuation, rather than the dynamics of (or considerations in) a valuation dispute.

Valuation Disputes as Drivers of Consensus

Strong valuation evidence is critical for the proposal of, and/or a challenge to, a plan in either jurisdiction. In the U.S., valuation evidence lends support to the position of each constituency but also, somewhat conversely, the prospect of valuation disputes can drive consensus and increase junior creditor recoveries, with parties pushed to negotiate creditor recoveries under a chapter 11 plan to avoid lengthy and costly court proceedings. These negotiations could occur either before or after the initial chapter 11 plan is filed. If, after the chapter 11 plan is filed, further negotiations result in an agreement among creditors for revised creditor recoveries, the debtor will file a revised chapter 11 plan to reflect the renegotiated (and hopefully consensual) deal.

It remains to be seen whether valuation disputes (or the threat of them) will have the same effect in England. There is arguably less scope in England, once the restructuring plan process has formally commenced, to amend the terms of a restructuring plan between the convening and sanction hearing as a result of valuation disputes (and certainly between the plan meetings and the sanction hearing). Debtors instead face the choice of either engaging in more extensive negotiations before the restructuring plan is filed (to avoid the need to re-start a restructuring plan if a deal is agreed down the line) or filing a plan that has the backing of fewer voting classes (with the possibility of staying or re-starting the restructuring plan proceedings if further negotiations result in amendments to the proposed deal).

Key Comparison Four

Disclosure and Discovery

In the U.S. and England, information (and lots of it) is key, both when proposing a plan and when challenging it. In chapter 11, a debtor is required to make certain information publically available, at the outset and throughout the process, filing a significant amount of financial information on day one in connection with its bankruptcy petition and throughout the case (including monthly operating reports and schedules of assets and liabilities).

In connection with confirmation, the debtor must file a disclosure statement that contains "adequate information." The U.S. Bankruptcy Code defines "adequate information" as "information of a kind, and in sufficient detail, as far as is reasonably practicable in light of the nature and history of the debtor...that would enable [a hypothetical investor typical of the holders of claims or interests in the case, that would enable such a hypothetical investor] of the relevant class to make an informed judgment about the plan." Disclosure statements typically include, among other things, information regarding the debtor and its go-forward business plan, reorganized enterprise value, creditor classification and recoveries, and liquidation value. Creditor groups that are actively involved in the process typically also enter into non-disclosure agreements, pursuant to which they may receive additional, non-public information related to the business plan and future projections of the reorganized debtor. Additionally, the U.S. Bankruptcy Code provides for the appointment of official committees of unsecured creditors (UCC) and, in certain instances, equity holders or other stakeholders, who have broad rights to information in order to undertake their statutory duties.

Although equally as focused on transparency, the English regime is less prescriptive. A debtor is required to send an explanatory statement to affected stakeholders in advance of the meeting(s) to vote on the plan which, similar to a disclosure statement, must include information sufficient to enable stakeholders to decide how to vote on the plan. The court will consider the explanatory statement in advance of the convening hearing and, if information is insufficient, the judge may require changes or even decline sanction (as was the case in the first *Sunbird* scheme of arrangement in 2020).

But how does access to information impact the mounting of a challenge? There is clearly an asymmetry between the debtor's access to its own documents on the one hand and the access it provides to stakeholders on the other. A natural consequence is that a disgruntled stakeholder wishing to challenge a restructuring plan must either present a challenge based on the information it has available to it or seek access to further information from the debtor. The English court has experienced both approaches in the last year. In *Virgin Active*, the dissenting landlords relied only on the company's evidence to challenge the plan's sanction. The creditor challenging the *Amicus Finance* restructuring plan made a (failed) disclosure request in the period between the convening and sanction hearings: the judge considered the scope of the disclosure request too broad and disproportionate in the circumstances. Thus, we have yet to see dissenting stakeholders put their own valuation evidence before the court. Until that time, the court has been clear that, absent competing evidence, criticisms about a debtor's valuation evidence are unlikely to bear much weight (*Virgin Active*).

© 2023 Akin Gump Strauss Hauer & Feld LLP

The English court has, however, made it clear that if a stakeholder wishes to oppose a plan on the basis that the company's valuation evidence shows an incorrect outcome in the relevant alternative, that stakeholder must appear before the court, file supporting expert evidence and the expert must be available for cross-examination. This would be the case for either a challenge of a 901C(4) application at the convening hearing or a challenge of cram down at the sanction hearing.[1]

In chapter 11, a relatively low bar exists for interested parties to obtain further information from the debtor. First, as noted above, the debtor is required to disclose a significant amount of financial and operational information about its business throughout the course of the chapter 11 case, and the debtor has statutory duties to provide certain additional information to the UCC or any other statutory committee if appointed. Further, the U.S. process generally provides for broad-ranging rights for creditors to receive "discovery" in connection with a contested plan confirmation process, including wide-ranging document production and deposition testimony of the debtor's management and its financial professionals. Additionally, even prior to the commencement of a formal plan process, the U.S. Bankruptcy Code provides powerful tools for creditors and other parties to obtain additional information about the debtor's business or financial condition through so-called "Rule 2004" discovery.

Procedurally and practically, England is a relatively long way from the lengthy disclosure disputes of chapter 11 and it remains to be seen how this will develop as more restructuring plans come to the fore and are contested, particularly in light of the clear direction from the court that future challenges will require evidence to be filed and information obtained. One thing we do know, however, is that the English judiciary is concerned to balance the need for stakeholders to have sufficient information to test the merits of the plan with ensuring that there are no unnecessary delays and costs, particularly when the plan company is faced with an impending liquidity crisis.

1 Put simply, if a creditor or member wishes to oppose a scheme or plan based upon a contention that the company's valuation evidence as to the outcome for creditors or members in the relevant alternative is wrong, they must stop shouting from the spectators' seats and step up to the plate."

[Per Snowden J at [53] in Smile Telecoms [2022] EWHC 387 (Ch)"]

Key Comparison Five

Operating During a Plan Process

Both the English restructuring plan and chapter 11 are debtor-in-possession processes, meaning that the debtor's management and board remain in control of the enterprise and continue the debtor's day-to-day operations (in the U.S., absent a significant showing of fraud or mismanagement). The framework for those continued operations is, however, a little different.

In the U.S., debtors are permitted to raise DIP financing (super-priority post-petition secured financing) during the pendency of their chapter 11 proceedings, in order to allow the operation of the business to continue uninterrupted and the costs of the process to be funded. With no provision to facilitate DIP financing during the English restructuring plan process, chapter 11 may have the edge if a company requires funding during, rather than after, a restructuring and it cannot readily be sourced from, or with the voluntary consents (which are often required) of, existing creditors.

Chapter 11 also affords an extra level of protection which is absent in the English restructuring process. When a chapter 11 petition is filed, a worldwide automatic stay comes into effect. That stay prevents any enforcement action or other legal proceedings being commenced or continued against the debtor or its assets, wherever located. At no stage in the English restructuring plan process is a stay imposed. An English plan could be proposed by the administrators of a company, in which case, the administration moratorium would continue (as was the case in *Amicus Finance*). Alternatively, a debtor could seek a specific stay of a certain action (as was the case in *Virgin Active*) or to commence a standalone moratorium under CIGA in parallel to launching a restructuring plan. In practice, only companies with low levels of public debt are eligible to apply for the moratorium, making its application quite limited. The lack of an automatic stay in England and the narrow circumstances in which a stay can be obtained mark a real limitation with the restructuring plan process, and one that in some circumstances may make chapter 11 a more attractive process.

© 2023 Akin Gump Strauss Hauer & Feld LLP

Key Comparison Six

Timing

While the exact timing for confirmation of a chapter 11 plan will depend almost entirely on all the specific circumstances of a particular case, broadly speaking the general timeframes for confirmation of chapter 11 plan constructs are: (i) 1-2 months for "pre-packaged" cases (i.e., where the debtor has solicited and secured acceptance of the plan pre-filing), though in recent years there has been a trend towards much shorter (i.e., a day or a week) "pre-pack" timeframes; (ii) 4-6 months for "pre-arranged" cases (i.e., where the debtor has negotiated proposed plan treatment with certain creditor groups pre-filing, often entering into a so-called restructuring support agreement (RSA) with such groups prior to filing); and (iii) 9-18 months on average for "free-fall" cases.

The English restructuring plan process has (so far) proved to be relatively swift. A restructuring plan is prepared ahead of the convening hearing and, ordinarily, hearings are limited to the two mandated by statute (convening and sanction). In England, there will typically be at least six weeks from the date of the application for a convening hearing (and the initial notice to stakeholders) to a sanction hearing and order. However, months of preparatory work may be required before filing an application. Further, additional hearings were held in the *Virgin Active* and *Amicus Finance* plans (in connection with costs and a stay of a landlord's claim and disclosure, respectively). In the case of pre-arranged or pre-packaged chapter 11 proceedings, each is typically preceded by many months, if not years, of planning and negotiations. Upon filing, pre-arranged cases can run the range from relatively fast (assuming wide-ranging pre-petition creditor support in the form of an RSA) to slow and litigious (where, for example, only some creditor groups have agreed to a pre-filing RSA and others oppose the recoveries contemplated in the RSA, or where a UCC or other statutory committee that is formed post-filing opposes the plan treatment contemplated in an RSA or the reorganized enterprise value of the debtor upon which such treatment is premised). So while the timeframes for an English restructuring plan process and pre-arranged or pre-packaged chapter 11 proceedings may, in theory, be relatively similar, it is worth bearing in mind that the English process may become more protracted in cases where the plan is contested.

Key Comparison Seven

Costs

Costs can be high when things go according to plan. They can be even higher when they don't.

In a chapter 11 case, while certain exceptions may exist if there is not sufficient creditor interest, the U.S. Bankruptcy Code otherwise requires that the United States Trustee appoint a UCC. The debtor's estate is responsible (subject to court review and approval) for payment of the UCC's professional fees which, in large and complex cases, typically include the fees and expenses of counsel, financial advisors, and investment bankers. As a result, UCCs are not constrained by the burden of expensive legal fees or other costs when challenging a plan (and recoveries under it), even if it appears that the unsecured creditors are substantially out-of-money.

The fees and expenses of informal creditor groups are often also paid by the debtor pursuant to contractual obligations in the underlying credit agreements or bond indentures. Therefore, like UCCs, creditors can (in certain circumstances) be entitled to have their professional fees reimbursed by the debtor's estate and may use their position in the capital structure to negotiate (or litigate) certain treatment under the plan. Separately, while an unimpaired class (the claims of which are not altered by the plan) is deemed to accept (and so does not vote on) a chapter 11 plan, members of that class can still raise objections in the lead-up to and in connection with the confirmation process. For example, such constituency may argue that they *are* impaired and so cannot be deemed to accept the plan, and may object to confirmation of the plan on that basis.

Thus, it is typically the debtor itself that shoulders the significant financial burden of paying for a contested plan confirmation process. Given these dynamics, chapter 11 can both facilitate baseless litigation from out-of-the-money creditors who can credibly threaten prolonged and expensive litigation, while also encouraging settlement in order to avoid that very outcome.

The English restructuring plan does not provide for the formation of any formal committees, nor does it lend financial support to potential challenge or scrutiny of the plan (whether through requiring the debtor to pay professional fees or DIP financing). Therefore, stakeholders wishing to challenge a restructuring plan (including on disputes over valuation and disclosure) are faced with the prospect of incurring significant out-of-pocket expenses, which may be unrecoverable. In some limited circumstances, they may also face an adverse costs award (requiring them to pay a significant part of the debtor's costs incurred in connection with the challenge).

This is because, in England, the question and amount of costs payable by one party to another is entirely within the courts' discretion. The courts will consider costs on a case-by-case basis and the overall justice of the allocation of costs. The general position is that an objecting stakeholder will be able to recover a portion of its costs of a successful challenge. That was the case in *Amicus Finance*: the judge at the convening hearing accepted part (although not all) of the merit in the challenge to class composition and ordered that the majority of the challenging creditor's costs be met as an expense of the administration. However, where a challenge is unsuccessful, the general principle under schemes of arrangement (which was adopted as a starting point to the question of costs in *Virgin Active*) is that where the challenge is not frivolous and is considered helpful to the court in scrutinizing the scheme of arrangement, the court will either make no adverse costs order or order the debtor to pay a portion of the costs of the objecting stakeholders' challenge. While these financial implications could disincentivize restructuring plan challenges, thus far that does not seem to be the direction in which the cases are going.

Members or creditors should not be deterred from raising genuine issues relating to the scheme in a timely and appropriate manner by concerns over exposure to adverse costs orders"

Conclusion

Same, But Different

Inevitable early comparisons with chapter 11 and concerns about missed opportunities for a statutory absolute priority rule have, to a certain extent, been allayed, as the English courts have demonstrated a robust ability to grapple with the allocation of the so-called restructuring surplus on tight, liquidity-driven timeframes. But the English restructuring plan is the (relatively) new kid on the block, and the extensive jurisprudence and prescriptive framework of chapter 11 (at odds with the limited detail in the restructuring plan legislation) cannot be disregarded. The lack of a statutory stay or provision for DIP financing under the English regime may mean, for example, that, for companies where those aspects are critical to implementation of a restructuring, chapter 11 may be more suitable. That said, each case will, of course, depend on the individual facts and circumstances and the process to be used in a specific situation will be determined on a restructuring-by-restructuring basis.

© 2023 Akin Gump Strauss Hauer & Feld LLP

Table Comparing Key Elements of the U.K. Restructuring Plan Regime and U.S. Chapter 11

	U.K. RESTRUCTURING PLAN REGIME	U.S. CHAPTER 11
Jurisdiction	Available to English companies and non-English companies that can establish a "sufficient connection" to the U.K.	Broad test with low jurisdictional threshold. Available to companies that have their principal place of business in the U.S. or (very limited) property in the U.S. (e.g., cash in a U.S. bank account).
Eligibility	**Two-part test:** **A**. The company has encountered, or is likely to encounter, financial difficulties that are affecting, or will or may affect, its ability to carry on business as a going concern; and **B.** A compromise or arrangement is proposed between the company and its creditors (or any class of them) or its members (or any class of them) and the purpose of the compromise or arrangement is to eliminate, reduce or prevent, or mitigate the effect of, the company's financial difficulties.	Filing may be for a number of reasons, including financial difficulties, to deal with contingent litigation liabilities and for operational restructurings. No insolvency requirement to commence chapter 11 and no financial difficulties threshold for voluntary bankruptcies. Case can be dismissed if filed in bad faith or without reasonable hope of success, but such dismissal is infrequent.
Court Process	Two mandatory court hearings: convening and sanction. Interim applications (i.e., for disclosure) may require further court hearings.	More extensive involvement and supervision by the U.S. court. Number of hearings will depend on length and complexity of the matter, but omnibus hearings are typically held on a monthly basis. A "first day" hearing takes place at the commencement of the process. A hearing to consider the adequacy of the disclosure statement and a confirmation hearing to approve or reject the plan presented by the company or any other party entitled to do so will also be convened. Various other hearings generally also take place throughout the process.

© 2023 Akin Gump Strauss Hauer & Feld LLP

	U.K. RESTRUCTURING PLAN REGIME	U.S. CHAPTER 11
Classes and Class Composition	Rights-based approach to class composition. **Key question:** Are the rights of creditors, both their existing rights and the rights conferred by the plan, not so dissimilar as to make it impossible for them to consult together with a view to their common interest? Meetings of stakeholders "affected by" the plan should be convened (which will likely include shareholders which are to be diluted as the result of a proposed debt for equity swap). Application can be made to exclude a class of stakeholders where "none of the members of that class has a genuine economic interest in the company" (a "901C(4) application").	Claim-based approach to class composition. Generally, a plan may place a claim or interest in a particular class only "if such claim or interest is substantially similar to the claims or interests of such class." This is determined according to the value and priority of the claim or interest, as well as the rights attached to it. A debtor has significant discretion in classifying claims. All classes of "impaired" claims and interests have the right to vote if such class is receiving a recovery under the plan. A claim is impaired unless (a) the plan leaves unaltered the legal, equitable and contractual rights of that claim, or (b) the plan cures any (non-bankruptcy) default, provides compensation for damages incurred and does not otherwise alter the stakeholder's rights. A class that is receiving 100 percent recovery may be deemed to accept the plan and a class that is receiving no recovery may be deemed to reject the plan.
Approval Thresholds	Seventy-five percent in value of the members of that class must vote in favor. No numerosity requirement.	At least two-thirds in amount and more than one-half in number of creditors voting in that class must vote in favor.
Cross-Class Cram Down	**Permitted if the court is satisfied that:** None of the members of a dissenting class would be any worse off under the plan than they would be in the event of the "relevant alternative" ("Condition A" or the "no worse off" test); At least one class that would receive a payment or would have a genuine economic interest in the company in the event of the relevant alternative has voted in favor of the plan ("Condition B"); and It is appropriate for the court to exercise its discretion to sanction the plan.	**Permitted if:** All other confirmation requirements have been satisfied. The plan does not discriminate unfairly against such class. The plan is fair and equitable with respect to such class.
Court Approval and Discretion	Court has ultimate discretion to sanction a plan.	U.S. bankruptcy courts also have wide discretion in interpreting and applying the requirements for confirmation set out in the U.S. Bankruptcy Code, but, when such requirements are satisfied, the plan must be confirmed.

© 2023 Akin Gump Strauss Hauer & Feld LLP

	U.K. RESTRUCTURING PLAN REGIME	U.S. CHAPTER 11
Certainty/Precedent	Legislation drafted in general terms. Limited plan case law available, but scheme of arrangement case law instructive on many issues.	Detailed legislative framework. Extensive and long-established case law.
Appeals	No appeals to date. Appeals are not common for schemes of arrangement. Appeals will only be possible in very narrow circumstances and the threshold will be extremely high (for example, the decision was a conclusion that no reasonable judge could have reached).	Appeals from plan confirmation orders occur with some frequency. However, it is relatively rare for such appeals to delay the implementation or "effective date" of a confirmed plan. Parties typically have 14 days following entry of the confirmation order to file an appeal.
Moratorium/ Automatic Stay	No automatic stay or moratorium.	Automatic worldwide stay comes into effect on the filing for chapter 11.
Timing/Control	Can be completed within 6-8 weeks. The plan and its terms are prepared in advance of the convening hearing.	Proceedings are highly variable in length depending on factors including whether the process is "pre-arranged" or "free-fall", as well as the size and complexity of the debtor's business but generally, chapter 11 proceedings will take significantly longer than U.K. restructuring plans. While some pre-arranged plans could be as short as just a few weeks (or even shorter), others cases may last years.
Cram-up	Cram-up possible.	Cram-up possible.
International Recognition	Principles of private international law or UNCITRAL Model Law. Automatic recognition in the U.S. under chapter 15 requires debtor's center of main interest "COMI" to be in the U.K.	Principles of private international law or UNCITRAL Model Law. Automatic stay purports to have worldwide effect.
Costs	Generally lower than schemes of arrangement, and much lower than chapter 11.	Generally very high (and much higher than a U.K. restructuring plan), due to the length of the process, the obligation of the debtor to pay professional fees of certain creditor groups and the adversarial nature of the in-court process.
Releases	Releases typically provided in favor of debtors and other guarantors under terms of plan. Releases in favor of finance parties can be included.	Typically provide for broad releases of major stakeholders by the debtors and third parties. Note, however, that third party non-consensual releases are often subject to challenge and increasingly narrowing in scope.

© 2023 Akin Gump Strauss Hauer & Feld LLP

Contributors

Tom Bannister
Partner
tom.bannister@akingump.com
London
T +44 20.7661.5319

Sam Brodie
Partner
sam.brodie@akingump.com
London
T +44 20.7661.5363

Richard Hornshaw
Partner
richard.hornshaw@akingump.com
London
T +44 20.7661.5489

Mouna Moussaoui
Associate
mouna.moussaoui@akingump.com
London
T +44 20.7012.9823

Joanna Newdeck
Senior Counsel
joanna.newdeck@akingump.com
London
T +44 20.7012.9622

Liz Osborne
Partner
liz.osborne@akingump.com
London
T +44 20.7661.5347

Lauren Pflueger
Knowledge Management Strategist
lauren.pflueger@akingump.com
Los Angeles
T +1 310.229.109

Abid Qureshi
Partner
aqureshi@akingump.com
New York
T +1 212.872.8027

Barry G. Russell
Partner
barry.russell@akingump.com
London
T +44 20.7661.5316

Emma Simmonds
Partner
emma.simmonds@akingump.com
London
T +44 20.7661.5420

James Terry
Partner
james.terry@akingump.com
London
T +44 20.7012.5310

© 2023 Akin Gump Strauss Hauer & Feld LLP

Akin is a leading global law firm providing innovative legal services and business solutions to individuals and institutions. Founded in 1945 by Richard Gump and Robert Strauss with the guiding vision that commitment, excellence and integrity would drive its success, the firm focuses on building lasting and mutually beneficial relationships with its clients. Our firm's clients range from individuals to corporations and nations. We offer clients a broad-spectrum approach, with over 85 practices that range from traditional strengths such as appellate, corporate and public policy to 21st century concentrations such as climate change, intellectual property litigation and national security.

akingump.com © 2023 Akin Gump Strauss Hauer & Feld LLP. All rights reserved. Attorney advertising. Prior results do not guarantee a similar outcome.