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“Virgin Territory”
Restructuring Plans under Part 26A of the Companies Act 2006

Camilla Lamont

What is a Restructuring Plan?

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- New restructuring procedure introduced by CIGA 2020 as a new Part 26A of the Companies Act 2006. Also see the relevant new Practice Statement issued by the former Chancellor on 26.6.2020.

- Similar to schemes of arrangement under CA 2006 but Part 26A only applies to companies in financial distress and also includes a power of cross class cram down

- Part 26A facilitates broader restructuring than CVAs involving not only unsecured creditors (including landlords) but also secured creditors and shareholders

- As with CVAs, Part 26A does not permit interference with landlord's property rights

The Threshold Conditions – s.901A

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That 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 ("Threshold Condition A")

That a compromise or arrangement is proposed between the company and its creditors or members (or any class of them), the purpose of which is to eliminate, reduce, prevent or mitigate the effect of, any of the financial difficulties so mentioned ("Threshold Condition B")

Part 26A Procedure

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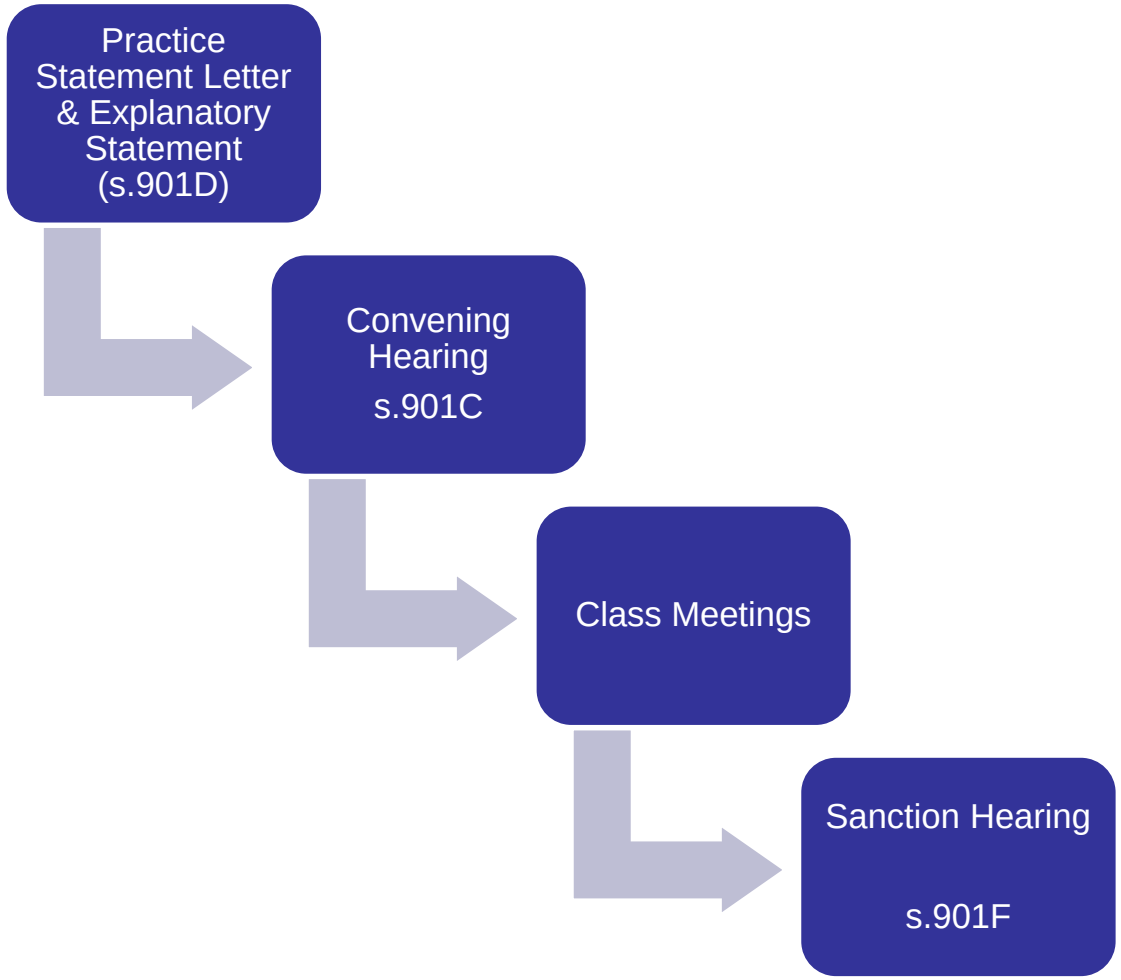

Court's power to Sanction Plan – s. 901F

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If each class votes in favour of Plan by 75% in value of creditors/ members voting

Court then decides whether to exercise its discretion to sanction Plan at the Sanction Hearing

Where Plan is sanctioned by the court, it is binding on all creditors, members and the company

Cross Class Cram Down – s.901G

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If at least one of the classes does not achieve a 75% majority

Do the Cross Class Cram Down Conditions A & B in s.901G apply?

If Yes, the court can (but is not obliged to) exercise its discretion to sanction the Plan

The Cross Class Cram Down Conditions

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Condition A is that the court is satisfied that, if the compromise or arrangement were to be sanctioned under section 901F, none of the members of the dissenting class would be any worse off than they would be in the event of "the relevant alternative" ("the No Worse Off Test")

The "relevant alternative" is whatever the court considers would be most likely to occur in relation to the company if the compromise or arrangement were not sanctioned under section 901F

Condition B is that the compromise or arrangement has been agreed by a number representing 75% in value of a class of creditors or (as the case may be) of members, present and voting either in person or by proxy at the meeting summoned under section 901C, who would receive a payment, or have a genuine economic interest in the company, in the event of the relevant alternative

Virgin Active Restructuring Plans

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- On 12 May 2021 Snowden J sanctioned Plans proposed by three companies in the Virgin Active Group - [2021] EWHC 1246 (Ch)

- First case in which the High Court has considered an application to sanction a Plan under Part 26A CA 2016 compromising landlords' existing and future claims under leases

- Striking example of the cross class cram down being exercised against dissenting landlords, so as to achieve a compromise that could not have been effected by a CVA

Plan Creditors

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Included Creditors

- Secured Creditors under a Senior Facilities Agreement of over £200 million
- Landlords in Classes A – E of 45 properties with unpaid rent claims of circa £30 million
- General Property Creditors

Excluded Creditors

- 9 categories of excluded creditors, deemed essential to day to day running of the Group, including trade creditors

The Convening Hearing & Meetings

- Snowden J made a “Meetings Order” convening 21 meetings of various classes on 16.4.21 (see [2021] EWHC 814 (Ch))

- Secured Creditors and Class A Landlords voted overwhelmingly in favour.

- 75% majority not achieved in relation to Class B to E Landlords and General Property Creditors

Sanction Hearing – [2021] EWHC 1246 (Ch)

- Cross class cram down conditions were held to be satisfied as:
  - Secured Creditors and Class A Landlords had voted in favour by requisite majority ("Condition B"); and
  - the court was satisfied on the evidence that the dissenting classes of creditor would be "no worse off in the relevant alternative"("Condition A")

- Judge exercised his discretion to sanction the Plans:
  - As the dissenting classes of creditors were "out of the money" in the relevant alternative, their objections to the Plan carried no weight
  - In any event it was not unfair for the shareholders to retain their equity as they had provided substantial "new money" on market terms which would rank junior to the SFA

Cross Class Cram Down - Key Points

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- Court does not need to be satisfied that relevant alternative will occur on balance of probabilities. It only needs to decide what is most likely to occur at the date of the hearing
- Plan Companies would otherwise have entered a trading administration involving an accelerated sale of the profitable parts of the UK businesses
- Plan Companies' valuation evidence showed that in administration the "value would break" with the secured creditors and unsecured creditors would be "out of the money". Dissenting classes would be paid 120% of the Estimated Administration Return under the Plans.
- No competing valuation evidence offered by the Landlords who "did not act with the urgency to be expected" in seeking additional disclosure. Procedure held not unfair to Landlords

Discretion – Key points

- Court should not have the usual reluctance (as is the case for schemes under Part 26) to differ from the vote where cram down powers are used under Part 26A

- Satisfaction of cross class cram down conditions not in itself sufficient reason to sanction and it was not appropriate to read in a principle that Plans should be approved unless court considered them not just and equitable

- Court must consider all the relevant factors and circumstances that it would ordinarily take in account in considering whether to sanction a scheme

The “out of the money” principle

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- A key principle is that it is for the company and the creditors who are “in the money” to decide, as against a dissenting class who is “out of the money” how the value and assets of the company should be divided. “Out of the money” creditors can, on application, be excluded from the vote altogether under s.901C(4)

- Court will however need to be satisfied that any restructuring surplus is fairly distributed between “in the money” creditors

- Differences in treatment between unsecured creditors will be justified if there are good commercial reasons for such differential treatment but a plan should not discriminate arbitrarily or capriciously between different classes of unsecured creditors even if they are all equally out of the money.

The importance of valuation evidence

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- The outcome of any individual case will be highly fact sensitive
- Valuation evidence will be critical both in respect of the "no worse off test" and in determining whether landlords are "in or out" of the money
- Landlords must act quickly to seek necessary disclosure and to obtain expert valuation evidence. Plan companies are expected to co-operate in the timely provision of information that may be relevant to the efficient resolution of genuine valuation disputes
- Landlords will need to consider costs implications of challenging

CVAs v Restructuring Plans

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- Plans likely to be favoured for larger and more complex restructuring involving secured creditors and reorganisation of share capital

- Plans are expensive and require court sanction but provide greater certainty

- Cross class cram down under a Plan is a potent tool where landlords' voting power would defeat a CVA – so a Plan is likely to be useful where the company wants to write off substantial arrears built up during the pandemic.

- The CVA jurisdiction is effective and well understood and, subject to the outcome of the New Look appeal, is likely to continue to be popular with companies looking to restructure over rented leasehold portfolios

Thank you for listening

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