Amicus Finance - Restructuring Plan sanctioned on the basis of cross-class cram down of secured creditors

Technical Bulletin 972

Case: In the Matter of Amicus Finance plc (In Administration) [2021] EWHC 2255 (Ch), Snowden J, 9 August 2021 (Convening); [2021] EWHC 2245N (Ch), Zacaroli J, 2 August 2021 (Specific disclosure before sanction); and [2021] EWHC 3036 (Ch), Sir Alastair Norris, 15 November 2021 (Sanction)

Synopsis: This is the first case where a restructuring plan has been promoted within the context of a formal administration. It is also the first case where opposing secured creditors have been the subject of a cram down under part 26A Companies Act 2006. The sanction judgment was made in August 2021, but was only published in the Autumn of 2021. The case also provides an example of the restructuring plan being used in a mid-market context, with the court's approach to disclosure cognisant of the circumstances of the company, its financial difficulties and ensuring a proportionate approach to the level of information required in the Explanatory Statement to enable creditors to make an informed decision when voting upon the plan.

Topics covered: **Restructuring Plan; Disclosure in Explanatory Statement; Section 901A conditions; class composition; Section 901G; cram down; exclusion of creditors.**

Comment

The convening hearing judgment (Snowden J) serves as a useful reminder of procedural formalities required to be followed by those promoting a restructuring plan, in particular the importance the court places on adequate notice to those affected by the plan and the need for adequate information to enable creditors to properly consider whether the plan is acceptable when compared to the relevant alternative. In this regard the administrators had sought to amend various aspects of the Explanatory Statement following observations by the judge and submissions by an opposing creditor.

The case also provides a reminder of the general legal principles applicable when approaching class composition. In this case the judge split the class in relation to the senior debt due to a different ranking which was attributable to part of the debt.

The decision is also interesting in terms of the court summarily assessing the costs of the opposing creditor, reducing the total by almost 50% to take into account the evidence setting out the background to a number of issues that did not arise or were not pursued. However, Snowden J acknowledged that it was right in principle that a cost order was made in the opposing creditor's favour to reflect its success on the challenge to the class formation and contribution to the dynamic of the convening hearing.

The specific disclosure application provides some useful practical guidance on the approach of the court to applications for specific disclosure in the context of a restructuring plan.

The sanction judgment (Sir Alistair Norris) is the first case which has allowed cram down in respect of secured creditors. The analysis focuses first on the statutory requirements being met before turning to the exercise of discretion as to whether the court ought to sanction the restructuring plan which will be fact sensitive in each case.

The Facts

Re Amicus Finance Plc [2021] EWHC 2255 (Ch) (Snowden J) 9 August 2021 – Convening decision

An order was made convening meetings of creditors to consider the administrators' proposed restructuring plan in respect of Amicus Finance PLC (the Company) a property finance company where the purpose of that plan was to enable the Company to exit administration and return to solvency to be operated as a going concern, and the court was satisfied that there was sufficient information, following certain amendments having been made during the course of the hearing, in the accompanying Explanatory Statement to enable creditors to take a view on the plan's merits.

In relation to class composition, although the same general principles of class composition applied to Pt 26A plans as applied to Pt 26 schemes, a rigid application of those principles might not always be appropriate in the different context of a Pt 26A plan. The starting point was to identify the substance of the relevant rights possessed by creditors; if those rights were very different pre-plan or in the relevant alternative, or if they would fall to be treated very differently pursuant to the terms of the plan, that would tend to point to a conclusion that the creditors could not consult together with a view to their common interest. In the present case, applying these principles, the court ordered that there be five meeting of creditors: (i) expense creditors; (ii) senior secured creditors; (iii) junior secured creditor; (iv) preferential creditors; and (v) unsecured creditors.

The Company had two secured creditors (C and H). There was an agreement between those secured creditors as to the ranking of their security, the effect of which was that C and H had a first equal ranking of debt and related security equal to the sum outstanding to C. Thereafter, H’s debt and security ranked junior to that of C. The court held that although C and H stood shoulder-to-shoulder in respect of their senior debt up to the amount owing to C, there was a clear distinction between their rights thereafter. The difference in existing rights and their treatment under the restructuring plan meant that there was little or no commonality of commercial interest as regarded the holders of those different rights in their capacity as such. To focus on the creditor’s identity, rather than the rights they possessed, was not the correct approach. It was, therefore, directed that C and H should form a single class in respect of their respective secured claims up to the value of C's senior debt, and that H should form a separate class as junior secured creditor in respect of the balance of its claim.

Re Amicus Finance Plc [2021] EWHC 2245N (Ch) (Zacaroli J) 2 August 2021 – Specific disclosure before sanction

In the context of the restructuring plan, one of the senior secured creditors, C, applied for specific disclosure of documents in advance of the sanction hearing.

The court held that the approach to a specific disclosure application in the context of a restructuring plan is to be informed by the purposes of the legislation. Restructuring plans are intended to provide a solution for distressed companies, meaning that first, this will often be against a time pressure, and secondly, the company is likely to have limited resources. Given those pressures, reaching a final determination on issues such as the merits of potential claims against third parties so as to bolster recoveries in the relevant alternative (in this case, a liquidation) by a full blown trial process, though clearly of relevance to the outcome in the relevant alternative, is likely in most cases to be incompatible with the legislative aims.

In those circumstances, the court held that the test to be applied is whether the disclosure sought is, in all the circumstances, proportionate, taking into account factors such as the urgency of the case, the disclosure that has already been provided, the extent to which further disclosure will assist in resolving issues that need to be determined at the sanction hearing, the burden on the company in terms of time and costs of providing that disclosure, and any delay in making the application.

Applying those principles, the court refused C's application for specific disclosure on the basis that, amongst things, it: (i) lacked precision; (ii) would require searches to made of a large number of documents; (iii) had been late in the day; and (iv) was likely to add little value to the issues the court was required to decide on the sanction hearing.

Re Amicus Finance Plc [2021] EWHC 3036 (Ch) (Sir Alistair Norris) 15 November 2021 – Sanction Judgment

The remainder of this bulletin focuses on the sanction judgment.

On 19 August 2021 (with full reasons given later), Sir Alastair Norris sanctioned the Company restructuring plan under Part 26A (the Plan) to "cram down" certain dissenting secured creditors of the Company.

The Company provided short-term property finance. It entered into a trading administration in December 2018 to run off its loan book. The purpose of the administration at this stage was to achieve a better realisation than would be achieved in a winding up. The Company’s secured creditors comprised of H which had provided funding in the administration, and C, an online peer-to-peer lending platform provider which had assisted in raising funds for the Company through its peer-to-business loan platform prior to its administration. As a result of the effects of Brexit and the pandemic, the ability to recover its property loans was impeded. The administrators arrived at the conclusion that the administration would not achieve a full repayment of the senior secured lenders, and that the trading administration was no longer financially viable. As such, the administrators at first considered compromising creditor claims by using a company voluntary arrangement (CVA), but C as a secured lender was not willing to support this and therefore without the secured creditors support a CVA could not be pursued. The administrators therefore decided to pursue a restructuring plan under Part 26A Companies Act 2016 with a view to compromising the Company’s claims and allowing control of the Company to be returned to its shareholders. The relevant alternative if the Plan was not approved, was a liquidation. The Plan envisaged (i) the release of all existing claims and security; (ii) the injection of approximately £3.7 million of new equity funding from the Company's minority shareholder; (iii) the use of the funding proceeds to provide lump sum payments to the expense and preferential creditors who would be paid in full, and a part payment to the senior creditors; and (iv) a further payment in a waterfall to the secured and certain other creditors from the proceeds of legacy loans recovered by the Company.

The Plan envisaged five classes of creditors, which were as follows:

- **Expense creditors:** creditors whose claims would be treated as an expense of the administration under para 99 Sched B1 IA 1986 and/or r3.51(2) IR 2016 (and ranking ahead of floating charge creditors)

- **Preferential creditors:** i.e. claims by employees

- **Senior Secured Creditors:** this included C/individual lenders who had lent money on the peer-to-peer lending platform and H

- **Junior Secured Creditor:** H

- **Unsecured creditors**

At the creditors' meetings, C voted against the Plan, which meant that the Plan had failed to gain the support of the required 75% in value of the senior secured creditor class, with only H (as well as one individual lender who lent to the Company using C's lending platform, and who sought to vote directly in respect of their loan) having voted in favour. The remaining creditor classes voted in favour of the Plan.

Key Issues

1. Whether there was adequate disclosure in relation to the Explanatory Statement.

2. Whether the court should sanction the proposed Plan and utilise the "cross-class cram down" mechanism, despite the objections of the senior secured creditor class.

3. In doing so, relying on *Re DeepOcean* (Technical Bulletin 924) *and Re Virgin Active* (Technical Bulletin 946), whether the court should exercise its discretionary jurisdiction to sanction the Plan if Conditions A and B were met.

4. Condition A states that none of the members of the dissenting class would be any worse off than they would be in the relevant alternative (the "no worse off test") (s901G(3) CA 2006).

5. C, citing *Re Hurricane Energy* (Technical Bulletin 942), argued that for the court to be "satisfied", the administrators had to demonstrate that there was "no real prospect" or "no realistic possibility" of a better outcome for C.

6. C argued that the Estimated Outcome Statement was fundamentally flawed and failed to provide a true estimate of likely return, as the administrators were not independent.

7. In addition, C contended that the Estimated Outcome Statement: (i) did not factor in claw back claims; (ii) did not attribute value to goodwill; (iii) did not consider the possibility that the shareholder might have contributed to funds in a liquidation; (iv) did not factor in the misconduct claims against the administrators; and (v) wrongly assumed that there was no funding available on liquidation to pursue litigation.

8. Condition B states that the compromise has been agreed by 75% in value of a class who would receive a payment in the event of an immediate liquidation, or otherwise have a genuine economic interest in the company (s. 901G(5) CA 2006). This was not in contention in this case as the administration expense creditors who ranked ahead of the secured creditors in the statutory order of priority, and were the only creditors in the relevant alternative of a liquidation to be likely to receive anything, had voted in favour in of the Plan.

Decision

The case serves as a reminder that the court when considering whether to sanction a restructuring plan, will first consider whether the statutory conditions under Part 26A Companies Act 2006 have been met, before then considering whether it should exercise its discretion to approve the scheme. The court's assessment will be fact sensitive. In this case there was no dispute that the relevant alternative to the restructuring plan was a liquidation.

Disclosure

I. In determining whether the Explanatory Statement could be safely relied upon, the court held that the touchstone is not whether the fullest specific information reasonably obtainable was included in the Explanatory Statement, but whether what was provided was sufficient to enable the creditors to make an informed decision whether to accept the risks inherent in the scheme in place of the risks inherent in a liquidation. Such comments are helpful in promoting the use of the restructuring plan in the mid-market which, prior to this case, had been reserved for much more significant enterprises. It was recognised in this case that the utility of the restructuring plan relies upon the court acting properly in safeguarding stakeholders interest, but also promptly and proportionately by recognising the circumstances in which businesses in need of restructuring operate.

II. As such, the court found that the Explanatory Statement was adequate for its purpose, and that the scheme creditors were sufficiently informed as to enable them to reach properly grounded decisions.

Fairness

III. On the "fairness" test, the court noted that fairness in does not operate in Part 26A cases in precisely the same way as in Part 26 cases, though it "*remains the divining rod by which special interests can be discerned".*

IV. The court affirmed the established principles that (i) creditors are the best judges of their own interests, though they are expected to act rationally; and importantly (ii) it is not the role of the court to consider whether the scheme submitted for sanction is the best scheme or the only fair scheme or could be improved in some respect, but rather to assure itself that it is one approved by the requisite majority of properly informed and consulted creditors acting in accordance with their ordinary class interests and not oppressively in pursuit of some special interest.

Cross-class cram down and the no worse off test

V. On the "no worse off test", the court (following *Re DeepOcean*) considered this to be a broad concept "*taking into account the impact of the restructuring plan on all incidents of the liability to the creditors, but primarily focused upon on anticipated recoveries based upon assumptions and projections: and comparing them with a counterfactual based upon the relevant alternative".*

VI. The court held that, drawing parallels with para 11(a) Sched B1 IA 1986, where the court is required to be "satisfied", in relation to the no worse off test it must be so satisfied on the "balance of probabilities" for which the administrator bears the burden to discharge. It was not necessary to demonstrate that there was "no real prospect" or "no realistic possibility" of a better outcome for the dissenting class.

Valuation

The valuation dispute in this case, focused on the main asset of the Company which comprised its loan book and potential recoveries from pursing litigation.

VII. The court was satisfied that the scheme should not be dismissed simply because of the allegations that the administrators were involved in the valuation process, despite them being proponents of the scheme.

VIII. In relation to the claw back claims, the court noted that it is the material "net recoveries" which affect returns to creditors, and that it will be reticent to conduct a "mini-trial" of clawback claims without disclosure or evidence - the sole purpose of examining such claims would be to see whether they affect the outcome of the "no worse off test".

IX. The court rejected the arguments in paragraph 7(iii) and (v) above on the grounds that C had failed to provide sufficiently convincing evidence.

X. In respect of goodwill, the court noted that a company in liquidation typically does not have marketable goodwill.

XI. As such, the court was satisfied that C would be no worse off under the scheme than it would be in an immediate liquidation (where the secured creditors would receive nothing).

XII. On Condition B, the expense creditors are the only class of creditor who would receive a dividend in an immediate liquidation (of approximately 52p in the £1) based on the analysis of the administrators.

Court's discretion

XIII. The court emphasised that, even if Conditions A and B were satisfied, it remains the court’s discretion to sanction the Plan (*Re DeepOcean*).

XIV. In exercising its discretion to sanction the Plan, the court took into account the fact that: (i) the administrators had been in office for some two years and had made their judgement as to the way forward having regard to the interests of the creditors as a whole; (ii) the scheme had the overwhelming support of the great majority of creditors; (iii) even within the class of senior secured creditors there was a majority (albeit minute in value terms) in favour of the scheme; and (iv) C would, on the figures contained in the Estimated Outcome Statement, not obtain any return in an immediate liquidation.

XV. Interestingly, given C's peer-to-business lending model, the court considered that C’s lack of a "genuine economic interest" in the event of a liquidation and its opposition to the Plan would instead prevent those with an actual economic interest in the Company from re-arranging its affairs (utilising injected resources) to benefit creditors generally.

XVI. The court considered that it was immaterial that returns under the "waterfall" were uncertain, as returns in an immediate liquidation would be even more uncertain.

XVII. The court also emphasised that the Plan was not "unfair" simply because it provided for the payment of expense creditors before there was a return to secured creditors, as this reflects the statutory scheme of priorities in an administration. There was no cram up of creditors.

XVIII. The Plan was one which an honest and intelligent creditor addressing its terms from the standpoint of ordinary class interests could rationally regard as "fair".