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gategroup: Part 26A Restructuring Plans are insolvency proceedings for the purposes of the Lugano

In a significant judgment handed down by Mr Justice Zacaroli on 17 February 2021, the High Court held that Part 26A restructuring plans are insolvency proceedings falling outside the scope of the Lugano Convention[1]. This marks a clear departure from the case law on schemes of arrangement, where the established approach of the court has been to treat schemes of arrangement as falling *within* the scope of the Brussels Regulation[2] and, by extension, the Lugano Convention for jurisdiction and recognition purposes.

The judgment is also interesting as it confirms that a Part 26A restructuring plan can be used by a newco SPV which unilaterally assumes group liabilities for the sole purpose of proposing a restructuring plan for the benefit of the wider group. This structure is not novel and has been used in schemes before but there had been some concern from parts of the market that it could be susceptible to challenge. The judge carried out a detailed analysis of the legal effect of this structure which may go some way to address concerns about the use of a newco restructuring plan (or scheme of arrangement) to effect third party releases.

In this briefing, we summarise the reasoning behind the conclusion that restructuring plans are insolvency proceedings for the purposes of the Lugano Convention and consider the impact that this is likely to have in practice.

What is a Restructuring Plan?

A restructuring plan is a new restructuring tool, introduced in 2020 by the Corporate Insolvency and Governance Act 2020 ("**CIGA**"). It provides a company encountering financial difficulties which, as a minimum, could impact its ability to continue business as a going concern with the ability to propose a compromise or arrangement with its creditors and members to restructure its affairs. The framework of the new restructuring plan is based very much on the scheme of arrangement procedure (which still remains available to companies wishing to restructure), but with some key differences. Of particular relevance to this case, there are no

financial difficulty threshold conditions for a scheme of arrangement. Additionally, the new restructuring plan allows courts to sanction a plan by applying cross-class cram-down, which binds dissenting classes of creditors and members (rather than just minorities within a class).

Click here for a more detailed analysis of the restructuring plan tool.

The gategroup Plan

gategroup is the world's largest provider of airline catering services, and has suffered a massive decline in its business as a result of the Covid-19 pandemic. As part of a wider debt restructuring and recapitalisation exercise, the group launched a restructuring plan on 30 December 2020 to amend and extend its senior debt and bond liabilities in order to give it breathing space to trade through the pandemic.

The bonds contain an exclusive jurisdiction clause in favour of the Zurich courts. This gave rise to a difficult question at the gategroup convening hearing as to whether the English court had jurisdiction under the Lugano Convention. While the UK is no longer party to the Lugano Convention from 1 January 2021, as the restructuring plan was issued prior to this date, the Lugano Convention continues to apply. If the Lugano Convention was construed as applying to restructuring plans, it was accepted that the English court's jurisdiction would be ousted by the Swiss exclusive jurisdiction clause.

In order to determine the applicability of the Lugano Convention, it was necessary for the judge to decide whether restructuring plans constitute "civil and commercial matters", which would bring them within the scope of the Convention, or are outside the scope of the Convention because they fall within the exclusion applicable to "bankruptcy, proceedings relating to the winding-up of insolvent companies or other legal persons, *judicial arrangements, compositions and analogous proceedings*" (the "**Bankruptcy Exclusion**").

Part 26A restructuring plans are insolvency proceedings for the purposes of the Lugano Convention

Given the legislative history of the Lugano Convention and the fact that the Bankruptcy Exclusion is identical to that contained in the Brussels Regulation, the dovetailing principle was key to the judge's approach to the construction of the Bankruptcy Exclusion. The dovetailing principle reflects the legislative intention that the Brussels Regulation and the Insolvency Regulation[3] should be interpreted in such a way to avoid any overlap or vacuum between the two instruments, meaning that proceedings which fall within the Bankruptcy Exclusion should be covered by the Insolvency Regulation.

Therefore, in reaching his decision, the judge focused on whether restructuring plans would be covered by the Insolvency Regulation (if the UK were still a party to it). He found the elements of insolvency proceedings as defined by Article 1(1) of the Insolvency Regulation to be as follows:

1. they must be collective proceedings;
2. they must be based on laws relating to insolvency and have as their purpose rescue, adjustment of debt, reorganisation or liquidation; and

3. they must encompass at least one of the following:
    - the debtor is partially or totally divested of its assets;
    - the assets and affairs of the debtor are subject to control or supervision of a court; or
    - 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.

The judge found that these elements were satisfied for Part 26A restructuring plans:

Collective Proceedings

The Insolvency Regulation defines collective proceedings as including "all or a significant part of a debtor's creditors", and this can cover proceedings which involve only the financial creditors of a debtor where those proceedings are aimed at rescuing the debtor. The judge found that this was broad enough to be satisfied by creditor restructuring plans used to restructure financial debt for the purposes of rescue.

Laws relating to insolvency for the purpose of rescue, adjustment of debt, reorganisation or liquidation of the debtor

The judge found that the presence of the financial difficulty threshold conditions for a Part 26A restructuring plan meant that Part 26A is a law relating to insolvency for the purposes of the Insolvency Regulation, notwithstanding that it sits within the Companies Act 2006. These threshold conditions require a company proposing a restructuring plan to be facing actual or likely financial difficulties which threaten the ability of the company to continue as a going concern, and that the purpose of the plan is to eliminate, reduce or prevent, or mitigate the effect of these financial difficulties. The judge drew a distinction here with schemes of arrangement for which there are no financial difficulty threshold conditions and which can be used by solvent companies.

Assets and affairs of the debtor are subject to control or supervision by a court

The judge noted that "*there is undoubtedly significant court involvement*" in the approval of a restructuring plan and that the Insolvency Regulation does not exclude debtor in possession proceedings, such as those under Part 26A. In such a case, "*the supervision of the court may nevertheless be said to be over the debtor's affairs and assets in the sense that…the plan devised by the debtor can only come into effect if the court considers it appropriate to convene meetings of creditors and subsequently to approve it*". This element was therefore satisfied.

As a result, the judge found that restructuring plans were insolvency proceedings falling within the Insolvency Regulation and consequently the Bankruptcy Exclusion under the Lugano Convention. This enabled the judge to be satisfied that the English court had jurisdiction in respect of the restructuring plan, and the judge went on to convene meetings of creditors under the restructuring plan.

Comment

The conclusion that the restructuring plan is an insolvency proceeding for the purposes of the Lugano Convention is understandably causing some ripples in the market, in part due to the contrast with the approach to schemes of arrangement where judges had managed to avoid

taking a definitive view on the application of the Brussels Regulation for so long. But what will this mean in practice?

While the industry had been hoping that the Lugano Convention would, in due course, act as a reasonable alternative to Brussels Regulation for the recognition of schemes of arrangement and restructuring plans in the EU post-Brexit, it is still unclear whether the UK will be permitted by the EU to accede to the Lugano Convention. If the UK is permitted to accede, as a matter of English jurisprudence, Lugano will now not assist with the recognition of restructuring plans; having noted that, recognition in a foreign jurisdiction is in its pure sense a matter for the relevant foreign court and their interpretation of the Lugano Convention. This judgment is nevertheless significant and draws a clear distinction between schemes of arrangement and restructuring plans, despite their similarities and the fact that they sit in successive parts of the Companies Act. It is in this regard helpful, as it may allow further arbitrage between the two procedures for borrowers depending on whether the Bankruptcy Exclusion route can prove more helpful to recognition.

For the recognition of restructuring plans in EU member states, private international law will have a bigger role to play. As a general rule, the prospects of successful recognition under private international law will be greater where the restructuring plan company's COMI is in the UK, and the finance documents contain an exclusive English jurisdiction clause and an English governing law clause. This is likely to be the case whether the restructuring plan is characterised as an insolvency proceeding or not, and in this context, the question whether the restructuring plan is an insolvency proceeding will be a matter for foreign local law (which is not addressed by this judgment). Comfort can be taken from the fact the expert evidence adduced in the gategroup case is that the restructuring plan will be recognised and enforced in Switzerland and Luxembourg, notwithstanding that it is regarded as an insolvency proceeding for the purposes of the Lugano Convention.

1. The Convention on Jurisdiction and Enforcement of Judgments in Civil and Commercial matters signed in Lugano on 30 October 2007

2. EU Regulation on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters (1215/2012)

3. EU Regulation on Insolvency Proceedings 2015 (848/2015)

Key Contacts

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