Neutral Citation Number: [2021] EWHC 1759 (Ch)

Case No: CR-2021-000852

IN THE HIGH COURT OF JUSTICE
BUSINESS AND PROPERTY COURTS OF ENGLAND AND WALES
INSOLVENCY AND COMPANIES LIST (ChD)

IN THE MATTER OF HURRICANE ENERGY PLC

AND IN THE MATTER OF THE COMPANIES ACT 2006

7 Rolls Building, Fetter Lane
London EC4A 1NL

Date: 28 June 2021

Before :

MR JUSTICE ZACAROLI

Tom Smith QC, Matthew Abraham and Ryan Perkins (instructed by **Dentons UK and Middle East LLP**) for the **Company**
Stephen Robins (instructed by **Akin Gump LLP**) for the **Ad Hoc Committee of Bondholders**
Andrew Thornton QC and Ben Shaw (instructed by **Rosenblatt Limited**) for **Crystal Amber Fund Limited**
Mr Paul Steward, Mr Peter Baker and Mr Derek French, shareholders in the Company, appeared in person
Hearing dates: 21, 22 and 23 June 2021
Further written submissions and evidence received: 24 and 25 June 2021

APPROVED JUDGMENT

COVID-19: This judgment was handed down remotely by circulation to the parties' representatives by email. It will also be released for publication on BAILII and other websites. The date and time for hand-down is deemed to be 12.00 noon on 28 June 2021.

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MR JUSTICE ZACAROLI

MR JUSTICE ZACAROLI:

1. This is an application to sanction a restructuring plan (the "Plan") in respect of Hurricane Energy PLC (the "Company") under section 901F of the Companies Act 2006 ("CA 2006").

2. The hearing took place over Monday to Wednesday, 21-23 June 2021 at the end of which the parties indicated that – for reasons which I explain below – a decision was required at the latest by first thing on Monday 28 June 2021. Given the real possibility of an urgent application for permission to appeal, the parties required reasons to accompany the decision. While I have considered all of the submissions made by the parties and those shareholders who wrote to the Court or appeared (remotely) at the hearing, given the pressure of time this judgment does not expressly deal with each and every point advanced by them. It addresses what I consider to be the central issues raised by the application.

3. The Company, which is listed on the Alternative Investment Market ("AIM"), was incorporated in September 2004 as part of a group of companies whose business is extracting oil stored within fractures in solid rock beneath the sea, known as fractured basement reservoirs. It is the parent company of Hurricane Holdings Limited, which in turn is the intermediate holding company for two subsidiaries: Hurricane GLA Limited ("GLA") and Hurricane GWA Limited ("GWA"). These hold the following licences from the Oil and Gas Authority ("OGA"), of which the Company is the operator, covering an area to the west of Shetland:

   P1368 comprising two areas, Lancaster and Lincoln. Lancaster is owned by GLA, and Lincoln is owned by a joint venture between GWA and Spirit Energy Resources Limited ("Spirit Energy"). The term of this licence expires in December 2024.

   P2294, compromising the Warwick area, owned by GWA. The term of this licence expires in August 2023.

   P2308, comprising the Halifax area, owned by GLA. The term of this licence expires in November 2024.

The Lancaster area

4. Initial investigations led to the discovery of oil in the Lancaster area. In 2017, the Company announced the results of its initial work, which indicated there was producible oil in the Lancaster area, with a deep oil water contact. An independent report, known as a Competent Persons Report ("CPR"), was produced by RPS Energy in May 2017 which indicated that there were material reserves in the Lancaster area.

5. On the back of this information, the Company raised US$300 million via an equity placing and US$230 million via the issue of convertible bonds, in order to embark on extracting the oil.

6. Oil production commenced from the Lancaster area in May 2019. Two wells were operational: P6 and P7Z, the latter being drilled to a greater depth. From the outset, small amounts of water were produced, known as "water cut". The water cut steadily increased throughout 2019 but the Company considered this (as reported to the market in a regulatory news service announcement – "RNS" – in December 2019) to be the result of "perched water" (pockets of water trapped by buoyancy in a dead-end fracture or pore space) and thus of less concern.

7. Water cut increased during 2020, mostly from the P7Z well (reaching 46% by April 2020). In early May 2020, the decision was made to suspend production from P7Z because the flow had become unstable and it was believed that it was interfering with production from the P6 well. The P6 well remains the Company's only well with any current or planned oil production.

8. In June 2020 the Company announced a technical review of Lancaster. The preliminary results were presented in an RNS dated 11 September 2020. This concluded that – contrary to the perched water explanation previously given – the more likely explanation for the water cut was a shallower oil water contact. This led to a significant reduction in the estimate of proven probable oil reserves from 37 million barrels to 16 million barrels, and a reduction in the estimate of remaining proven probable reserves (that is, what remains in the well) to 9.4 million barrels. The Company indicated an intention to engage with all key stakeholders.

9. A further CPR produced in April 2021 by ERC Equipoise Ltd ("ERCE") broadly confirmed the Company's analysis. The difference in outlook, as between the 2017 CPR and the CPR prepared by ERCE in April 2021, is principally explained by the fact that the latter is prepared with the benefit of 18 months' production data.

10. It is currently estimated that production from the P6 well will reach the point where it is no longer economic to extract the remaining oil in the first quarter of 2024 (based on current predictions of production profiles and the future price of oil).

The Lincoln, Halifax and Warwick areas

11. Wells were drilled by the Company in each of the other areas, but there is no current or planned production from any of them. Three wells were drilled in the Greater Warwick area (which consists of Lincoln and Warwick). Two were plugged and abandoned in 2019. A third, relating to the Lincoln area (which successfully tested at commercial flow rates, confirmed to contain light, 43° API oil) is currently required (by the OGA) to be plugged and abandoned by 31 October 2021.

12. The wells drilled in the Halifax area have also been plugged and abandoned.

The FPSO bareboat charter

13. The extraction and transportation of oil from the Lancaster area is dependent upon the use of a floating production storage and offloading vessel ("FPSO"). GLA leases a FPSO from Bluewater (Aoka Mizu) B.V. ("Bluewater") pursuant to a bareboat charter (the "Charter"). The initial term of the Charter expires in June 2022. GLA had an option to extend for a further three years, exercisable no later than 4 June 2021, but that has not been exercised. The Company is currently in negotiation with Bluewater for a shorter extension.

The Company's financial position

14. The Company's creditors consist primarily of the bondholders under the bonds issued in 2017 (the "Bondholders" and the "Bonds"). The aggregate amount due under the Bonds is US$230 million. The maturity date is 24 July 2022. The Bonds are unsecured and do not have the benefit of any guarantees from other group companies.

15. The Company is currently meeting its obligations to pay interest under the Bonds and is predicted to be able to continue to do so until maturity. The Company predicts, however, that it will be unable to repay the Bonds in full at the maturity date.

16. The Company commissioned PwC to report on the anticipated outcome in the event that the Plan is not sanctioned. PwC's updated report is dated 14 June 2021. The following is a summary of the principal conclusions in the report:

    (1) Aside from the licences, the principal asset of the Company is cash and cash equivalents. This currently stands at US$168.5 million. Of this US$61.8 million is restricted. This consists of amounts held in escrow (and additional amounts) to meet decommissioning liabilities. It also includes a sum of US$20.3 million to meet a termination fee under the Charter with Bluewater. Since it is not intended to terminate the Charter early, however, this sum is likely to be released to the Company.

    (2) The report considers two possible scenarios if the Plan is not sanctioned. The first is an immediate uncontrolled liquidation. The second is a controlled wind-down in which the Company continues to extract oil from the P6 well until shortly before termination of the Charter, followed by a decommissioning process, paying all unsecured debts (save for the Bonds) in full, leading to a liquidation in about April 2023. In circumstances where an uncontrolled liquidation is in the interests of none of the stakeholders of the Company and there is no external pressure which would prevent a controlled wind-down, I exclude the uncontrolled liquidation as a realistic alternative scenario.

    (3) The report provides an estimate of the cash position between now and March 2023 in a controlled wind-down. It is anticipated that net cash generated from trading operations up until the end of May 2022 will be US$115.5 million. From this amount is then deducted capital expenditure, wind-down costs, fees and Bond interest associated with the

decommissioning process, leading to an unrestricted cash balance of US$176.6 million in March 2023.

(4) The two key variables for the anticipated outcome in the controlled wind-down are production rates from the P6 well and the future price of oil.

(5) The production rates in the report are based upon the projections in the April 2021 CPR from ERCE. ERCE provided both a high and low case for the forecasted production. The high case represents a figure which there is only a 10% chance of exceeding. The low case represents a figure which there is a 90% chance of exceeding.

(6) The future oil prices in the report are based upon the Brent forward curve. This represents the price, today, at which oil may be bought and sold upon various dates in the future. It is widely used as a proxy for the predicted future price of oil on those dates. PwC have applied a sensitivity analysis by refence to information from Consensus Economics (which aggregates estimates from 29 brokers) and from a consulting firm, Wood McKenzie.

(7) If the anticipated production levels adopted in the PwC report turn out to be accurate, then in order to generate sufficient cash from operations by May 2022 to repay the Bonds in full, the oil price would need to be at an *average* of US$85 per barrel throughout the period. The prospect of that happening must be seen in light of the fact that: (1) the price has not reached US$85 per barrel at any point in the last five years; and (2) it is not forecast to reach that price at any point over the next year, even applying a sensitivity analysis of +$10 per barrel.

(8) Even on the basis of the high case for production forecasts, if combined with the high case for the anticipated future oil price, the increase of US$20.3 million in cash generated by the end of May 2022 would be insufficient to repay the Bonds in full by July 2022.

<u>The restructuring pursuant to the Plan</u>

17. The restructuring envisaged by the Plan is relatively straightforward and involves the following elements:

(1) An extension of the maturity date of the Bonds to 31 December 2024;

(2) A reduction of US$50 million in the capital amount due under the Bonds;

(3) An increase in the cash coupon under the Bonds from 7.5 per cent to 9.4 per cent per annum, and the introduction of an additional payment in kind ("PIK") coupon of 5 per cent per annum;

(4) A cash sweep provision, so that if on any interest repayment date there is surplus cash, it will be used to make partial capital repayment of the Bonds;

(5) Provision of security and guarantees from the Company and two subsidiaries;

(6) Certain other amendments to the terms of the Bonds;

(7) The issue of shares in the Company to the Bondholders, with the effect that the Bondholders will hold 95% of the diluted equity, with the existing shareholders retaining only 5% of the diluted equity.

18. The Company will undertake an extended wind-down, with a view to continuing oil production from the Lancaster area until it reaches its economic limit (currently projected to be in the first quarter of 2024). Subject to the possibility of further investment, the Lancaster area would then be decommissioned, followed by the settlement of all third-party claims and a liquidation.

19. The Company projects that if the Plan is sanctioned, there is at least a possibility that sufficient cash would be generated over the period to the first quarter of 2024 to enable the restructured Bonds to be paid in full with a small surplus to generate at least some value in the equity (although this is described in the Company's evidence as less than "a meaningful return"). Aside from a high-level forecast in the April 2017 CPR as to the likely rate of decline in production in the P6 well, the Company's evidence does not address the likely rate of production over the period of extended wind-down.

20. It is important to note that the Company's evidence of there being any return to shareholders under the extended wind-down is premised on the Bonds being restructured. This is achieved through a combination of the Bondholders giving up US$50 million of principal (which is offset partially by the increase in cash interest and an additional US$15 million in PIK interest) and the cash sweep arrangement, which means that interest will be paid from time to time on a lower total amount of Bond debt. The Company's evidence indicates that the difference between the anticipated return for the Bondholders under the extended wind-down (US$215.6 million) and the total contractual entitlement under the existing terms of the Bonds (US$251.6 million) is US$36 million.

21. The extended wind-down is contingent on an extension of the Charter. The Company believes that there is a reasonable prospect of negotiating an extension of the Charter on acceptable terms. I will return to this below.

<u>The position of the shareholders</u>

22. The Plan is opposed by one of the two largest shareholders of the Company, Crystal Amber Fund Limited ("Crystal Amber"), who instructed counsel (Mr Thornton QC and Mr Shaw) to appear at the sanction hearing. It is also opposed by a large number of individual shareholders. I received emails from just under 50 shareholders urging me not to sanction the Plan. Three shareholders (Mr Paul Steward, Mr Peter Baker and Mr Derek French) spoke at the hearing in opposition to the Plan.

23. There is considerable discontent among the shareholders with the current board who, it is said, have failed to engage as promised with the shareholders and have instead agreed a deal with Bondholders which will see the shareholders' interest in the equity reduced from 100% to a mere 5%.

24. Shortly after the Practice Statement Letter was sent to Bondholders and posted on the Company's website (on 30 April 2021), Crystal Amber served a requisition notice under section 303 CA 2006 requiring the Company to convene a general meeting for the purpose of considering resolutions to remove five directors and replace them with two nominated by Crystal Amber.

25. The Company's current board gave notice convening a general meeting for 5 July 2021. In addition, the last date for holding the Company's annual general meeting, at which four directors are up for re-election, is 30 June 2021.

26. Accordingly, it is accepted on all sides that it is likely that by 5 July 2021 the entire board will have been replaced. It is also accepted on all sides that in that event it is highly likely that the Company would withdraw the Plan.

27. It is in those circumstances that the Company contends the Plan needs to be sanctioned prior to the general meetings being held because, if that happens, the existing shareholders will be prevented (as a result of the heavy dilution of their shares) from voting out the current board.

The position of the Bondholders

28. Approximately 66% of the Bonds are held by the members of an *ad hoc* committee (the "AHC"). By letter dated 14 June 2021 from Akin Gump LLP, representing the AHC, the Company was informed that the AHC indicated that it opposed the changes to the board proposed by Crystal Amber and that if the new board (if voted in) were to indicate an intention to incur new liabilities or obligations or otherwise take steps which are inconsistent with the implementation of the controlled wind-down, the AHC would need to reconsider whether the immediate appointment of an independent liquidator would be required to protect creditors' interests. The letter went on to state:

> "To be clear, the AHC would not be prepared to grant a material extension to the term of the Bonds or agree to a write-down of principal amount of the debt unless the Bondholders were able to take control of the Group as part of the proposed restructuring to ensure that minority activist and out-of-the-money shareholders could not take steps to derail the legitimate strategy formulated by the Company in the best interests of its in-the-money stakeholders."

The Convening Judgment

29. The Company sought an order convening a meeting of a single class consisting of just the Bondholders. In a judgment dated 25 May 2021 (the "Convening Judgment") I directed that two meetings be convened: one for the Bondholders and one for the shareholders. That was because I concluded (for the reasons set out at [27] to [34] of the Convening Judgment) that the rights of shareholders were "affected by" the Plan within the meaning of that phrase in section 901C(3) CA 2006. The Company did not at that stage contend that section 901C(3) was disapplied by section 901C(4) on the basis that the shareholders did not have a genuine economic interest in the Company.

The Plan meetings

30. The Plan meetings were held virtually, in light of the continuing restrictions due to the coronavirus pandemic, on 11 June 2021. The Bondholders' meeting approved the Plan with 100% of those attending (representing 84.89% of the Bondholders) voting in favour. The shareholders' meeting rejected the Plan with 92.34% voting against and 7.66% voting in favour. Overall, 32.8% of the issued share capital of the Company voted at the meeting.

The matters to be considered at a hearing to sanction a restructuring plan under Part 26A

31. In the few cases decided so far under Part 26A, the court has adopted as a starting point the approach taken when sanctioning a scheme of arrangement under Part 26. As Snowden J explained in *Virgin Atlantic Airways Ltd* [2020] EWHC 2376 (Ch), at [45], this reflects the fact that it is clear from the legislative background, and the Explanatory Notes, to Part 26A that it was envisaged that the authorities under Part 26 may, where appropriate, assist the court in deciding how to exercise its discretion under Part 26A.

32. The matters to be determined at a hearing to sanction a scheme under Part 26 were summarised by Snowden J in *Re Noble Group Ltd* [2018] EWHC 3092 (Ch) as follows:

> "i) the court must consider whether the provisions of the statute have been complied with;
>
> ii) the court must consider whether the class was fairly represented by the meeting, and whether the majority was coercing the minority in order to promote interests which are adverse to the class that they purported to represent;
>
> iii) the court must consider whether the scheme was a fair scheme which a creditor could reasonably approve; and
>
> iv) the court must consider whether there is any "blot" or defect in the scheme."

33. There is, however, an important difference between a scheme under Part 26 and a plan under Part 26A where not all of the relevant classes of creditors and/or members have approved the plan. Section 901G CA 2006 provides the court with a discretion to sanction a plan notwithstanding that one or more of the classes has not approved the plan by the requisite majority (termed a cross-class cram-down).

34. Where that is the case, as here, the plan may be sanctioned provided that two threshold conditions are met (section 901G(2)-(5)):

> Condition A: "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"
>
> Condition B: "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) 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".

35. The "relevant alternative" is defined by section 901G(4) as "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."

36. Condition A involves three steps: (1) identifying what would be most likely to occur in relation to the Company if the Plan is not sanctioned; (2) determining what would be the outcome or consequences of that for the shareholders; (3) comparing that outcome with the outcome and consequences for the shareholders if the Plan is sanctioned: *Re Virgin Active Holdings Ltd* [2021] EWHC 1246 (Ch) ("*Virgin Active*"), per Snowden J at [106].

37. As to the first step, the court is not required to be satisfied that a particular alternative would definitely occur, merely (where there are possible alternatives) which one is *most likely* to occur: *Virgin Active* at [107].

38. As to the second step, the outcome or consequences for the shareholders is to be assessed primarily, but not exclusively, in terms of the anticipated returns on their claims: *Virgin Active*, at [106]. In *Re Deep Ocean 1 UK Ltd* [2021] EWHC 38 (Ch), Trower J said of the phrase "any worse off" that it is "...a broad concept and appears to contemplate the need to take into account the impact of the restructuring plan on all incidents of the liability to the creditor concerned, including matters such as timing and the security of any covenant to pay." I consider a similarly broad approach is required in determining whether shareholders are "any worse off" as a result of the Plan: it is necessary to take into account all incidents of their rights as shareholders.

39. As Snowden J pointed out in *Virgin Active* the exercise at the second stage is inherently uncertain, "because it involves the Court in considering a hypothetical counterfactual which may be subject to contingencies and which will, inevitably, be based upon assumptions which are themselves uncertain". *Virgin Active* was a case where the relevant alternative involved an immediate insolvency process. In such a case (which is more typical in restructurings generally) disputes between stakeholders will often focus on the appropriate value to ascribe to assets and liabilities in that insolvency process. That is not the case here where (as I will develop below) the relevant alternative is the continuation of trading for at least a further year.

40. Where the threshold conditions are satisfied, although the starting point is the approach to the exercise of discretion adopted in relation to schemes under Part 26, the fact that the case involves the application of the cross-class cram-down power in section 901G requires important modifications to that approach: see *Deep Ocean* (above), per Trower J at [44] to [46]. In particular, the reluctance of a court to depart from the outcome of a properly convened meeting of a class of creditors cannot have the same place in the court's approach to sanctioning a restructuring plan to which section 901G applies.

41. Mr Thornton put the point more forcefully. He submitted that there is a fundamentally different test under section 901G. Whereas, under a Part 26 scheme, the court is asked to sanction a scheme where the requisite majority of creditors in each affected class has approved it, under section 901G the court is being asked to sanction a plan where there has been no approval by the relevant class. Indeed, in this case, the relevant class has, by an overwhelming majority, opposed the Plan. He pointed out that the arrangement proposed in this case could have been done with the Bondholders via a Part 26 scheme, but would have required the approval of the shareholders. It is being done via the Plan, therefore, so as to override the rights of the shareholders, in particular their rights to approve an allotment of shares under section 551 CA 2006.

42. He submitted that care should accordingly be taken before overriding rights of a dissenting class. That is particularly so where the consequences of the Plan would be to remove, immediately and irrevocably, virtually the whole of the shareholders' interest in the Company. That should not be done, he submitted, in a rushed process where the shareholders did not have the proper opportunity to test the Company's evidence (with proper disclosure and the ability to cross-examine witnesses). Although Crystal Amber has provided a report from its own expert (see further below), that expert has not had the same time or access to information that has been afforded to those preparing the evidence adduced on behalf of the Company.

43. The Company's position (supported by the AHC) is that the shareholders do not have any genuine economic interest in the Company. In the two cases which have developed to any extent the principles to be applied, the fact that a dissenting class was out of the money was indeed considered to be a critical factor.

44. The history of the court's approach to out of the money creditors in the context of Part 26 schemes and the reasons why a similar approach is appropriate under Part 26A were considered by Snowden J in *Virgin Active*, at [226] to [249]. It was not suggested before me that the approach there set out is wrong, and I gratefully adopt it. As he noted at [249], the logic of the point that a meeting need not be convened of a class of creditors or members, even if their rights are affected by a restructuring plan, where none of the members of the class have a genuine economic interest in the company, is that:

> "if creditors who would be out of the money in the relevant alternative could be bound to a plan which effects a compromise or arrangement of their claims without even being given the opportunity to vote at a class meeting, the fact that

> they have participated in a meeting which votes against the plan should not weigh heavily or at all in the decision of the court as to whether to exercise the power to sanction the plan and cram them down. Nor is it easy to see on what basis they could complain that the plan was "unfair" or "not just and equitable" to them and should not be sanctioned."

45. The Company and the AHC rely in particular on [242] of Snowden J's judgment in *Virgin Active*, where he said:

> "That established approach in relation to scheme cases reflects the view that where the only alternative to a scheme is a formal insolvency in which the business and assets of the debtor company would be held on the statutory trusts for realisation and distribution to creditors, that business and assets in essence belongs to those creditors who would receive a distribution in the formal insolvency. The authorities take the view that it is for those creditors who are in the money to determine how to divide up any value or potential future benefits which use of such business and assets might generate following the restructuring (the restructuring surplus)."

46. Mr Robins, who appeared for the AHC, submitted that was the case here: it would have been open to the Bondholders to acquire 100% of the equity, and they had in fact been generous in permitting the shareholders to retain 5% of the diluted equity under the Plan.

47. The question whether the shareholders are out of the money is a critical element in determining whether they would be any worse off in the Plan than in the relevant alternative, and in the exercise of discretion.

48. I agree with Mr Thornton that particular care is needed in the application of the cross-class cram-down provision where, as here, the Plan would deprive the members of the dissenting class of all but a fraction of their interest in the Company.

49. In any given case, it is important to balance any potential unfairness to the dissenting class as a result of the speed at which the case has been brought on and the difficulties the dissenting class faces in adducing its own evidence and testing the evidence of the plan proponents, against the genuine urgency of the proceedings. As Snowden J pointed out in *Virgin Active*, at [129] to [130], the cross-class cram-down provisions may well give rise to difficult questions of valuation and it is important that the utility of Part 26A is not undermined by lengthy valuation disputes. That would be particularly so where the relevant alternative is imminent liquidation or administration.

<u>Jurisdiction, class composition and representation at the meetings</u>

50. I addressed the questions of jurisdiction and class composition in the Convening Judgment. It is not contended by any party that I should revisit the conclusions I then reached, and I need not do so.

51. I am satisfied that the meetings were held in accordance with the directions made at the convening hearing. The meetings were held remotely in view of continuing restrictions resulting from the Covid-19 pandemic, but those wishing to participate were given a fair opportunity to do so.

52. There is no reason to believe that the majority of either the Bondholders or the shareholders voting at their respective meetings did not represent, and act in good faith in the interests of, the class as a whole.

<u>The threshold conditions</u>

53. Of the two threshold conditions in section 901G, there is no doubt that Condition B is satisfied: the Plan was approved by the Bondholder class and they would clearly receive a payment in the event of the relevant alternative. The dispute in this case centres on Condition A, which involves the three-step approach outlined in *Virgin Active* (see [36] above).

54. The Company's case as presented in its skeleton is that the most likely alternative is a controlled wind-down, leading to the outcome described in the updated PwC report. There would be no extension to the Charter. The AHC would not countenance any extension of the Bonds, or allow the Company to use its resources otherwise than to continue trading until May 2022 in order to generate cash to fund partial repayment of the Bonds. The Company would therefore trade only until May 2022 and then commence a decommissioning process. According to the most recent evidence from the Company's Chief Financial Officer, Mr Richard Chaffe, this is anticipated to lead to the Company having free cash of US$213 million as at 31 May 2022. That cash would not, however, be available to repay the Bonds, because it would be required to fund the wind-down of the Company thereafter, including costs associated with decommissioning (in addition to the funds already held in escrow for that purpose). By March 2023, it is anticipated that there would be US$176.6 million of cash available for distribution to the Bondholders, resulting in a recovery of 76.4% of the total Bond debt.

55. It is on the back of this evidence that the Company and the AHC contend that the shareholders are clearly out of the money so that the fact that shareholders are provided with 5% of the diluted equity in the Plan means that they cannot be worse off than under the relevant alternative.

56. Mr Thornton submitted that the Company has adopted too blinkered an approach to the relevant alternative. It has posed one question: will the Company be able to repay the Bonds in full by July 2022 from cashflow generated from the P6 well? Having answered that question in the negative, it has concluded that the shareholders have no economic interest in the Company and that the board can take no alternative step without the consent of the AHC. He contended that the question the Company has posed itself rules out a number of alternative possibilities. These include that actual performance over the next year could be better than forecast; that the Company could trade on beyond May 2022 (it being common ground that the P6 well is likely to remain economically viable until long after that date); that even if there is insufficient cash generated from the P6 well by July 2022 the shortfall could

be refinanced; and that the Company might take steps in the meantime to reduce the Bond debt, for example by itself purchasing some of the Bonds at a heavily discounted price in the market.

57. It would be wrong, he submitted, to sanction a Plan which immediately and irrevocably deprived the existing shareholders of all but a tiny fraction of their equity in the Company, when there was no immediate insolvency crisis, the Company was forecast to continue trading profitably in the short and medium term, and there remained a realistic prospect of the Bond debt being removed by the maturity date. Importantly, he contended that the premise underlying the Company's projections – that trading ceased in May 2022 – was flawed, given that it is clearly in all stakeholders' interests to continue trading beyond that date and there are good reasons to believe that could be done.

58. There is, in my judgment, little doubt as to steps 1 and 3, such that the real debate is over step 2.

59. As to step 1 (what is most likely to happen if the Plan is not sanctioned) it is common ground that if the Plan is not sanctioned the Company will most likely, in the short to medium term, continue trading profitably. That is what the current board propose to do but, more importantly, is what would happen under the direction of the new board if, which is widely assumed to happen, new directors are voted in at the forthcoming general meetings.

60. This is not a case, therefore, where the relevant alternative involves any immediate insolvency process. Even if the Company is (as Mr Smith QC contended) currently insolvent on the cash flow test – taking into account its ability to repay indebtedness falling due in 13 months' time – it is in the interests of all stakeholders to continue producing oil from the P6 well. The Company is currently operating at a profit, and is forecast to continue to do so up to and beyond the maturity date of the Bonds (assuming an extension of the Charter – as to which see below).

61. In argument, however, Mr Smith submitted that if the new board is voted in then the relevant alternative would actually not be that described in his skeleton, but would be the following. He submitted that I can and should conclude that the actions of the new board will undoubtedly lead to the insolvent liquidation of the Company, sooner rather than later. Specifically, he contended that the new board would pursue strategies which involved using the Company's available cash resources to pursue costly and risky investment opportunities. None of those strategies have any prospect of generating additional income in time to enable the Bonds to be repaid, and all of them would require the extension of the maturity date of the Bonds. If the board was allowed to proceed along that route, they would deplete the cash resources available to the Company so that by July 2022 there would be significantly less cash available to repay the Bonds and the Company would be clearly insolvent. In fact, the AHC would not permit this to happen and would instigate early enforcement action, by seeking the appointment of a liquidator. Either way, there would be no possibility of any return to shareholders.

62. He further submitted that I can assume the new board would adopt this strategy because there would be no point in them merely continuing the strategy proposed by the existing board, given the shareholders' opposition to it, and given that it would not achieve anything other than a less than full repayment of the Bonds, thus leaving nothing for the shareholders.

63. Mr Robins supported that contention. As he put it, the AHC would not agree to extend the maturity date of the Bonds so as to allow the cash to be used on "pipe dreams". They would be better off taking a liquidation return of 35%.

64. I accept that, *if* the new board adopted the approach outlined by Mr Smith, the most likely consequence would be the insolvent liquidation of the Company.

65. I do not accept, however, that the most, or even a, likely outcome is that the board would adopt that approach. The Company's contention is based on the fact that the evidence submitted by Crystal Amber in opposition to the sanction application relies in numerous places on such alternative investment strategies. These include drilling a new well (P8), injecting water so as to increase the rate and amount of oil produced and exploiting the Lincoln area so as to extract the oil which it is known to contain. The additional capital expenditure that these investment strategies would require ranges from approximately US$60-80 million (for drilling a new well – with an additional US$96 million if water injection was to be undertaken) to US$700 million to US$1 billion in relation to developing the Lincoln area. That evidence, which demonstrates the potential upside for shareholders from exploiting the Company's assets if funding could be obtained to pursue the possible investment opportunities, does not in my view demonstrate that the new board would, or would be likely to, divert the cash generated from the P6 well, needed to repay the Bonds, towards those other opportunities. Mr Thornton disavowed the suggestion that the new directors nominated by his client would do any such thing.

66. This is supported by the fact that such a strategy, if pursued using either the existing free cash or revenue generated by continuing trading over the next few months, would be likely to constitute a breach of duty by the directors. As Mr Smith submitted, where directors know or ought to know that the company is or is likely (in the sense of 'probable') to become insolvent, then the duty under section 172(3) CA 2006, requiring directors to consider or act in the interests of creditors, is triggered: *BAT Industries plc v Sequana SA* [2019] EWCA Civ 112. The precise content of that duty is not entirely clear (and a decision from the Supreme Court on an appeal from the decision of the Court of Appeal is awaited). In *Sequana* David Richards LJ, at [222] declined to determine (as it did not arise for decision in that case) whether, once the creditors' interests duty was engaged, their interests are paramount or are to be considered without being decisive. He did say, however, that in a case of present, actual insolvency, "it is hard to see that the creditors' interests could be anything but paramount". I did not understand Mr Thornton to resist the proposition that, in this case, for the directors to divert cash which was essential in order to repay the Bonds at maturity in July 2022 on speculative investment projects, which would not generate income until after the maturity date of the Bonds, would be a breach of duty. He submitted, however, and I

agree, that I should not assume the new board of directors would act otherwise than in accordance with their duties.

67. As to Mr Smith's point that the directors would be bound to follow an alternative investment strategy because there would be no point in them following the same strategy as that decided upon by the current board, which they have rejected, this fails to take account of three points. First, the current board's strategy involves the certain and irrevocable depletion of the shareholders' interest to a mere 5% stake in the Company. That in itself sufficiently explains the shareholders' rejection of the Plan. Second, the shareholders do not accept that the *forecasts* as to likely revenues over the next year will prove to be accurate, in particular so far as the predictions as to oil price are concerned. If (as some commentators predict) the oil price is likely to rise substantially and it turns out that there is enough to repay the Bonds, then the current board's strategy will have irrevocably shut out the shareholders from participating in anything other than a 5% share in the potential upside. Third, the shareholders wish to explore options that would result in repayment of the Bonds at maturity, even if this cannot be achieved solely by the revenues from the P6 well over the next year.

68. Accordingly, I do not infer, from the references in Crystal Amber's evidence to the possible alternative investment strategies, that it is likely that the new board would deplete the existing cash balance or the revenue to be generated from the P6 well towards the cost of alternative investments. On this basis, I reject the contention that the relevant alternative would be the near-term insolvent liquidation of the Company.

69. As to the third step, it is common ground that the Plan is not anticipated to provide any "meaningful return" to shareholders and that, even in respect of such less-than-meaningful return that might be generated, the current shareholders' interest in it will be limited to 5%.

70. That means that the second step raises the following question: in the absence of the Plan would the shareholders be better off (taking into account all the incidents of their rights as shareholders) than having a 5% stake in equity which promised no meaningful return?

71. It is common ground that the burden lies on those propounding the Plan. It is for the Company, therefore, to demonstrate that the shareholders would not be any better off than receiving a less than meaningful return, if they retained their shares and the Company continued trading for at least the next year.

72. Mr Robins, for the AHC, advanced a more extreme position. In answer to Mr Thornton's submission (which I address further below) that there would be a number of possible steps the new board could take to address the repayment of the Bonds in July 2022, Mr Robins submitted that it is not a question of reaching a conclusion on the balance of probabilities, but is simply a question of selecting the most likely outcome. It was therefore not sufficient for Crystal Amber to list possible options that might be open to the new board without identifying that which was the *most* likely to happen.

73. I am not persuaded that the court is so constricted, at least in the circumstances of this case. Pursuant to 901G, the relevant alternative is to be identified by reference to that which is most likely to happen if the Plan is not sanctioned. But once that has been identified, the question is whether I can be satisfied that none of the shareholders would in that event be any better off.

74. If the relevant alternative was, for example, an immediate liquidation then the question would be whether the shareholders could expect some meaningful return in that liquidation, i.e. whether that was the most likely outcome from the liquidation. Where, as here, however, the relevant alternative is that the Company carries on trading for at least a further year, I do not think the analysis is the same. The Company may or may not go into an insolvency process in a year's time, and whether it does, and the resulting outcome for shareholders, will depend in part upon what happens in the intervening period. It cannot be right that, in addressing that question at this stage, the shareholders must identify the one strategy (or combinations of strategies) that the Company is most likely to adopt. Nor is it necessary, in my judgment, unless there is some other legitimate ground of urgency, to arrive at a definitive present value for the future income stream. Rather, the possible courses of action open to the Company over the next year, and beyond, are factors to be considered in determining whether there is a realistic possibility that the financial outcome for the shareholders in a year's time will be better than that offered by the Plan. If there is a realistic possibility of this, I consider that the shareholders would be better off in the relevant alternative than the less-than-meaningful return anticipated under the Plan.

75. In addressing the likely ability of the Company to repay the Bonds in full in July 2022, Mr Thornton identified two principal areas of uncertainty: first, as to the quantum of revenue that will actually be generated from the P6 well over that period; and, second, the steps that the new board might be able to take to assist in repayment of the Bonds.

Anticipated revenue from the P6 well

76. As to the first of these, as noted in the PwC report, there are two main variables: the rate of production of oil from the P6 well and the future price of oil.

77. The evidence as to the anticipated rate of production is based on the Company's own assessment, corroborated by the CPR from ERCE in April 2021.

78. Crystal Amber instructed their own expert, Mr Jonathan Fuller of Xodus Group Limited. Mr Fuller provided a report, albeit at speed and without access to full information. He considers that ERCE's conclusions are based on overly conservative assumptions. Mr Smith submitted that Mr Fuller's conclusions in this respect are premised on the ability to inject water into the P6 well (which is not a realistic possibility given the cost involved). At section 6.7 of his report, Mr Fuller suggests that ERCE has underestimated the actual fracture porosity, such that the oil originally in place ("STOIIP") is of a magnitude higher than that reported by ERCE. In his conclusion at section

6.8, however, he says that he believes that "the higher STOIIP makes the potential prize of incremental recoverable resource from water-flooding the Basement correspondingly higher, than that given by the ECE CPR." I agree with Mr Smith that this does suggest that the additional oil Mr Fuller believes may be present would be accessible only via water injection, which would involve considerable further capital expenditure.

79. Nevertheless, ERCE's (and the Company's own forecasts) are – necessarily – estimates. The CPR states, at p.35, "The recovery and estimates of Hurricane's oil Reserves are estimates only and there is no guarantee that the estimated Reserves will be recovered. Actual volumes recovered may be greater than or less than the estimates stated in this report." As demonstrated by the change in outlook between the 2017 and 2021 CPRs, actual performance can and does depart from projections.

80. As to the second variable, the future oil price, the estimates in the PwC report are based on the Brent forward curve. I accept that this is a widely used measure in the industry for numerous purposes including forecasting future revenue. As noted above, PwC have tested this by reference to forecasts provided by Consensus Economics and Wood Mackenzie. The Brent forward curve indicates an average price during the period to 31 May 2022 of US$69 per barrel. A lower average price is indicated by the other forecasts.

81. Again, however, these are estimates of future prices. The price of oil is well known to be sensitive to world events. The marked impact on the oil price of the Covid-19 pandemic is an obvious example. The extent to which the demand for oil will increase as the world (hopefully) emerges from that pandemic, and the consequent impact on the price of oil, is unknown. Mr Paul Steward, an individual shareholder who spoke in opposition to the Plan at the sanction hearing, referred to the fact that the price of oil has more than doubled since September 2020 and is continuing to rise. He referred to the conclusions very recently expressed by several large banks and oil experts that the price will continue to rise on the back of "incredible demand", inflation and pressure on the major oil companies to cut emissions. He referred in particular to the prediction from Bank of America, in the last 48 hours, that the price could well hit US$100 in the coming year.

82. The fact that these statements have been made was not challenged in reply by the Company or the AHC (and is easily verified by an internet search). They are not the same, of course, as the consensus among experts which feeds into the Brent forward curve and Consensus Economics' forecasts.

83. If it was necessary to reach a definitive conclusion, now, as to the present value of the future revenue stream from the P6 well between now and the end of May 2022 (for example, if the task was valuing the price that could be achieved on a sale today of the Company) then the decision would likely be based on ERCE's forecast as to production rates and the Brent forward curve, as representing the most reliable evidence.

84. For the reasons I have explained, however, that is not the case here, where the relevant alternative, on the Company's case, involves a year of further trading before the "wall of debt", as it is described in the Company's evidence, falls due for payment.

Alternative steps

85. Mr Thornton identified a number of possible options that could be open to the new board of directors in order to facilitate the repayment of the Bonds on the maturity date.

86. His starting point was to analyse the shortfall between free cash, as at July 2022, and the amount needed to repay the Bonds at maturity. He contended that the Company's own evidence (based on the PwC projections) indicated that there would be US$213 million of "free cash" as at 31 May 2022. If, as he contended it should, the Company traded for a further seven weeks beyond that date (to the maturity date of the Bonds) then it would generate significant further cash. In the absence of any evidence from the Company as to anticipated cashflow after the end of May 2022, but extrapolating on a straight-line basis from the expected cash generation during the year to May 2022 of US$97 million, the Company would be likely to generate a further US$13 million during that short period. On that basis, by the maturity date under the Bonds, on the Company's own mid-case estimates the Company would have cash which fell just US$4 million short of the sum required to repay the Bonds.

87. Mr Smith objected that Mr Thornton's analysis of these figures leaves out of account important qualifications in the Company's evidence.

88. First, a deduction for estimated creditors, accruals and prepayments. In PwC's report these are estimated to total US$21.7 million, although their starting figure of unrestricted cash as at 31 July 2022 is US$216.9 million, slightly higher than that referred to in Mr Chaffe's evidence. In either case, the deduction of these amounts is said to result in net free cash of US$195.2 million as at 31 July 2022. The figures for creditors, accruals and prepayments are based on the balances as at 30 April 2021. PwC notes that they will move over time and are likely to be different (most likely lower) by July 2022. Nevertheless, I accept that it is inherently likely that a substantial proportion of this sum is likely to represent liabilities of the Company as at that date (particularly as, on the shareholders' case, the Company would still be trading). Insofar as they consist of accruals and prepayments, however, I accept Mr Thornton's contention that they are unlikely all to be due and payable on 31 July 2022, such that – if the Company was in a position to continue trading – it is reasonable to assume that they might be met from revenues from that ongoing trading.

89. Second, PwC's report indicates that further sums need to be deducted to fund the wind-down of operations between July 2022 and May 2023. This results in the sum of US$176.6 million I have referred to above as being available to repay the Bonds. Mr Thornton submitted – again, rightly in my judgment – that if the Company was continuing to trade, these sums would not necessarily

represent actual liabilities as at July 2022. They would be incurred only when, at some point in the future, the Company ceased production from the P6 well and could (depending on the up-to-date financial forecasts at that time) reasonably be expected to be funded from revenues generated thereafter.

90. I consider below the reasonableness of the assumption that the Company could continue trading beyond May 2022 (which underlies Mr Thornton's analysis). On that assumption, however, I accept that, taking the Company's own projections, while there would likely be a shortfall between the cash available at 31 July 2022 and the $230 million required to repay the Bonds in full, that shortfall would likely be less than that indicated in PwC's report.

91. Mr Thornton then pointed to the options potentially, at least, open to the Company to ensure that the Bonds were repaid in full, including: raising money from a third party, such as the Company's bank or another lender, by way of short-term facility; raising money from one or more of the existing shareholders or via a rights issue in order to bridge the gap between available cash from trading and US$230 million; an asset sale or sale of the trading subsidiary; seeking a joint venture partner for other assets owned by the Company; buying back some of the Bonds; or offering an incentive of some kind to persuade the Bondholders to wait the (potentially short) period of time within which further cash was generated from trading to make up the balance.

92. These options were identified by Mr Thornton as being ones which could raise sufficient cash to repay the Bonds at maturity. It might be said that it is not enough (to satisfy the test in section 901G) to show that the Bonds could be repaid, because the shareholders are only not *worse off* if there would additionally be a material cash surplus for them. This, however, would be to ignore the wider interests of shareholders. As Mr Thornton pointed out, the interests of equity holders are fundamentally different to that of debt holders. In the absence of contractual terms conferring a right to share in profits, debt holders have priority over shareholders in respect of the amount due to them (principal and interest), but it is the shareholders alone that have the right to share in the potential upside from the development of the Company's assets.

93. The interest of the shareholders in this Company is inherently more precarious than in many other industries, because of the risky nature of its investments. Mr Thornton was able to point to two tangible investments which, if the Company was in a position to continue trading beyond July 2022 *and* could repay the Bondholders in full by or around that date, could be of real interest to the shareholders.

94. The first is the P6 well itself. As I have noted, the Company's evidence is that the well is likely to remain economically viable until the first quarter of 2024. The likely net revenue to be generated from further trading beyond the end of May 2022 has not been modelled by the Company or PwC. The only evidence consists of:

(1) A table in ERCE's CPR which forecasts the rate of oil production from 1 January 2021 until early 2024. This indicates a production rate of over 10

Mstb/d in January 2021 falling to 5 Mstb/d by mid to late 2023 and reducing to approximately 3 Mstb/d by early 2024; and

(2) A paragraph in Mr Chaffe's first witness statement, provided to illustrate the potential return to Bondholders from the extended trading period permitted under the Plan. At present day values this appears to show an increase in the total return to them of US$60 million.

95. The only other available source for the likely oil production beyond May 2022 is a presentation which the Company made to Bondholders dated 24 May 2021. This was referred to by Mr Peter Baker, a shareholder who spoke at the hearing in opposition to the Plan. On page 7 of this document, there is a projection of the monthly oil production profile from June 2021 to February 2024, which indicates a steady decline from 9.7 kbbl/d to 5.6 kbbl/d. Page 9 contains annual financial projections. This broadly supports Mr Chaffe's evidence as to the likely additional funds available to service the Bonds. The figures for 2022 are not broken down pre- and post- July, but for the full year it is estimated that 3,045.8 kbbls will be lifted, generating receipts from oil sales of US$185.4 million, leaving some US$43.7 million after operating and capital expenditure. In 2023, it is estimated that 2,875.1 kbbls will be lifted, generating receipts of US$167.6, leaving approximately US$38.1 million after operating and capital expenditure. (I have ignored the entries for interest and movements in escrow – which was not explained at the hearing – since these do not appear to impact on the projections as to revenues from the P6 well itself.)

96. I received further submissions from an opposing shareholder, Mr Peter Baker, after the conclusion of the hearing, and submissions in answer from the Company's solicitors. Mr Baker relied on the Company's presentation dated 24 May 2021 to submit that there was likely to be US$337.5 million of revenue generated from the P6 well which, taking historical contributions, after operating expenses would result in a profit of US$170 million. As the Company's solicitors pointed out, however (and as I have noted above), the presentation of 24 May 2021 contained considerably larger estimates of operating expenditure resulting in much smaller anticipated profits. I do not accept, as Mr Baker submitted, that I was misled, deliberately or otherwise, at the hearing by counsel for either the Company or the AHC.

97. I cannot on the information available (and in any event need not) determine the likely quantum of net revenue which continued trading after July 2022 would generate. The important point is that if the Company is able to trade beyond May 2022 and able to fund the shortfall in the amount due to repay the Bonds in one of the ways suggested by Mr Thornton, there is a realistic prospect that it will retain an income producing asset of at least some value to its shareholders.

98. The second tangible investment is the Company's interest in the Greater Warwick area, which includes Lincoln. Mr Chaffe's evidence is that this was carried in the Company's financial statements as at 31 December 2020 (signed off in May 2021) at a value of US$55.4 million. I reject Mr Thornton's suggestion that this represents a realisable asset likely to attract such a value.

Mr Chaffe's evidence is that a non-producing asset such as Lincoln with liabilities and a low chance of development, would attract a low, if any, value. It nevertheless represents a potentially valuable asset of interest to the holders of equity. There are four points to make in this respect:

(1) It is the Company's evidence that the value ascribed to it in the accounts represents an amount which might be realised by further development. Mr Chaffe said that the amount was not impaired or written off in the accounts "…as analysis undertaken showed that its carrying value had the potential to be recovered through successful development."

(2) Second, the existence of further investment opportunities (which must have included the Lincoln area) was identified as one of the benefits to Bondholders of the Plan (albeit emphasising their uncertain value). In his first witness statement, at paragraph 125, Mr Chaffe said:

> "In addition to higher recoveries in the Extended Wind Down, if the Restructuring is implemented, it is also possible that the Plan Company will be able to pursue further investment options, which could result in further increased value for Bondholders. However, the economic viability of these investment options is uncertain, and they cannot be pursued without Bondholder consent, and will require an extension of the Bareboat Charter on acceptable terms. For this reason, the Plan Company has not included these investment options in any valuation of recoveries under the Restructuring Plan."

(3) As I have noted above, one of the Lincoln wells previously achieved a commercial flow of "light" oil (which Mr Steward described as the "Rolls-Royce" of oil). Although it is required to be plugged and abandoned by 31 October 2021, this shows that the possibility of extracting oil is not a fanciful one.

(4) While it is true that this is an investment opportunity that would require very substantial capital expenditure, that does not detract from the conclusion that it represents something of value to shareholders. Assuming the Bond debt could be removed, the position of the shareholders would be not wholly unlike their position prior to investment in the Lancaster area: potentially valuable oil reserves had been identified, but very substantial investment was needed to extract the oil, the prospect of repaying which was subject to risks, including as to oil production and price. This encapsulates the essential interest of shareholders in a venture like this one.

99. Turning to the options Mr Thornton listed, I do not think it can be said that they are unrealistic or inherently unlikely (aside from the sale of the Company's interest in the Lincoln area, which I have addressed above).

100. As to the possibility of raising funds, whether from a bank or other lender or from some or all of the shareholders, the likelihood of being able to do so increases in inverse proportion to the amount of the gap between cash realised

from the P6 well and the sum needed to repay the Bonds in full. Taking into account the extent to which I have accepted Mr Thornton's points on the Company's projections and the uncertainties surrounding the Company's performance over the next year (particularly in relation to the oil price), it is a realistic possibility in my judgment that the amount required would be small enough to be raised from one or other source.

101. The Company points to the fact that there are only two substantial shareholders (most of the shares being held by retail investors) and that, of those, one (Kerogen Capital) has indicated that it is not willing to invest further money into the Company and the other (Crystal Amber) declined to become "wall-crossed" earlier this year so as to receive confidential information to enable it to decide whether to invest further sums. Mr Robins added that Crystal Amber is an "activist" fund (by its own admission) and was thus intent only in creating leverage to improve its position. I do not accept that Crystal Amber's self-description as an activist fund means that its intentions are as characterised by Mr Robins. It has previously responded to requests to provide further funding for the Company and its evidence is that it may be "willing to lead a funding round to bridge any equity gap required to repay or refinance the [loans]". While it is a relatively small fund, and therefore may be limited in the amount of funds that it could provide, there is a realistic prospect that the funding gap by July 2022 would be of a size that Crystal Amber could assist in bridging. As to the position of Kerogen Capital, the evidence is that, following a detailed presentation and discussion of the potential benefit of potential development options was made available to it, it indicated that it was not willing to provide additional financial support to the Company. That does not necessarily answer the different question whether, in a year's time, it would be willing to participate in funding a much smaller gap in order to free the Company of the Bond debt, prevent liquidation and preserve other investment options.

102. The possibility of the Company buying back the Bonds in the market is, on the face of it, an attractive one given that the Bonds have been trading at a substantial discount to face value for a long time. They are currently trading at approximately 50% of face value. At that price, for every $1 which the Company spent in acquiring the Bonds it would be relieved of $2 of debt. When this was previously proposed, in October 2020 when the Bonds were trading at US$0.30, the board declined to adopt a buy-back strategy. A principal reason was that approximately 70% of the Bonds were then held by the AHC, who had recently written to the Company warning it not to take steps involving significant financial outlay outside the ordinary course of business. It was felt that any significant buy-back programme would antagonise the AHC and risk negotiations with them. A smaller buy-back programme would leave the majority of the Bonds to be dealt with and would similarly risk damaging the negotiations with the AHC. At that time, a further factor was that the Company was considering investing in a water injection programme and it may need to use its free cash for that purpose rather than repurchasing Bonds.

103. If it remains the case that the members of the AHC would be unwilling to sell their Bonds, then a large buy-back programme is still unattainable. Most of the reasons for rejecting a smaller buy-back programme – principally the risk of upsetting relations with the AHC – would not apply in the context of the relevant alternative. It was suggested that the Company might be entering into a voidable preference if it went into the market to buy back the Bonds of only a few Bondholders. While nothing I say in this judgment could influence the conclusion of a court if a preference claim were to be brought in a subsequent liquidation, this seems to me to be an unlikely proposition if the purpose of the buy back is to facilitate avoiding insolvency proceedings and would be at a substantial discount to face value. For similar reasons, it is difficult to see that it would be contrary to the duty to act in the interests of all creditors, although as Mr Smith pointed out, the Company would need to be careful not to mislead the seller of a Bond at a discount where the Company's purpose was to promote the possibility of repaying the Bonds in full at maturity. These would be issues that the new board, in the relevant alternative, would need to consider, but the possibility of purchasing at least some of the Bonds from Bondholders who would prefer to cash-out now rather than wait to see what happens over the next year, is a realistic option as part of a menu of options designed to bridge the gap between available cash and $230 million as at July 2022.

104. Finally, the possibility that the Bondholders themselves might be persuaded to delay enforcement action if the shortfall is relatively small and the Company could continue to trade profitably is not, despite the AHC's stated opposition to it, to be discounted altogether. The AHC's current position is that its members are only prepared to countenance an extension of the maturity date if they acquire control of the Company to the exclusion of the current shareholders. If, however, as next July approaches it remains in the Bondholders' interests to permit the Company to continue trading so as to be able to generate further revenue which would be used to repay the Bonds, I should not assume they would act against their interests.

<u>The Charter</u>

105. It is an important element in most of the options suggested by Mr Thornton for seeking to achieve repayment of the Bonds in full at or around the maturity date, and for preserving potential value for the shareholders, that the Company could continue to trade beyond May 2022. For that, it is essential that there is an extension of the Charter.

106. In circumstances where the best estimate as to oil production from the P6 well indicates that it will remain economically viable until early 2024, it is undoubtedly in all stakeholders' interests that the Charter is extended. Bondholders need and want the extension since the extended wind-down, which on the Company's projections maximises their recovery, is dependent on it. Equally the shareholders need it, because it provides the best prospect of repaying the Bonds, which is essential if they are to retain any benefit in what remains of the Company's assets.

107. In addition, it is likely to be in Bluewater's own interests that the Charter be extended. Based on evidence provided by Mr Fuller, which the Company agrees reflects its assumptions concerning Bluewater, Bluewater is clearly incentivised to agree to an extension of the Charter.

108. It is important to appreciate the degree to which the FPSO is tailored to operating with the Lancaster area. The cost of fitting it out for such operation was US$299 million. Mr Smith relied on this to demonstrate why acquiring another vessel to replace it in June 2022 was not a realistic option. If that is right, then it is reasonable to infer that for the FPSO to be utilised by another oil company in another area it would likely require substantial fitting out costs. That alone provides a significant incentive to the owner of the vessel to negotiate an extension.

109. Mr Fuller identified numerous other factors which point to the same conclusion: Bluewater has five FPSOs in its fleet, of which only three are currently operational (suggesting that if there were other potential charters out there it already has capacity to meet demand); Bluewater has a US$200 million unsecured bond debt due to mature in 2023; the FPSO contributes 43% of the total revenue of Bluewater's FPSO business and 22% of its total business; those figures increase when the daily rate under the Charter is increased from US$25,000 to US$75,000; field deployments within the UK are limited, and redeployment may require further upgrades or modifications – in addition to the cost (see above in relation to the cost of fitting out for use by the Company) this would involve many months of delay, which would compromise Bluewater's position as regards the maturity of its own bond debt.

110. It is nevertheless the Company's case that an extension of the Charter is dependent upon the Plan being sanctioned. This breaks down into two questions: the likelihood of Bluewater agreeing to extend the Charter if the Plan fails; and the ability and willingness of the board to enter into an extension.

111. As to Bluewater's willingness to negotiate, Mr Smith pointed to the fact that Bluewater has – upon the option to extend the Charter for a further three years not being exercised – advertised the vessel, and he suggested that Bluewater may be less inclined to reach an agreement with the Company while it remains uncertain whether it could repay the Bonds on maturity.

112. I agree with Mr Thornton that the fact that Bluewater has advertised the vessel reveals nothing as to its willingness to agree an extension. Once the option to extend for a further three years was not exercised, Bluewater had no choice but to advertise the vessel.

113. I do not accept that Bluewater is unlikely to agree an extension in the absence of the Plan, particularly when set against the clear incentive for Bluewater referred to above. Mr Smith referred me to a passage in Mr Chaffe's third witness statement in which he linked the expectation of being able to agree an extension with the fact of the restructuring. Having noted that Bluewater had advertised the FPSO, he said "However, if the Restructuring is implemented within the envisaged timeframe, the Plan Company still considers there to be a

reasonable prospect of extending the Bareboat Charter on acceptable terms." This contrasts with a passage in his first statement, where he expressed the unqualified belief that there was a reasonable prospect of negotiating an extension of the Charter on acceptable terms. It is true that Mr Chaffe does refer, at paragraph 119 of his third statement, to the fact that the on-going restructuring process was hampering the Company's ability to negotiate with Bluewater, due to a lack of certainty around the Company's financial stability and whether the Company would be able to pursue the extended wind-down, which was dependent on the Plan being sanctioned. I do not read this evidence, however, as indicating that Bluewater is only prepared to extend the Charter if the Plan is sanctioned. If that were the Company's case it would require much more compelling evidence than that set out above.

114. Having reached this conclusion on the evidence before me at the hearing, I received a further witness statement from Mr Bernstein of Crystal Amber late in the evening of 24 June 2021. This exhibited an email to Mr Bernstein (which he described as unsolicited) from Mr Michael Bonte, the Vice President Business Development with Bluewater, with responsibility for all commercial activities within the Bluewater group. He said that he had been listening to feedback from the hearing with interest and wished to correct the impression given as to Bluewater's position by the Company and the AHC. In particular, he stated:

> "…we of course remain very keen to progress discussions and investigate solutions and proposals to extend the charter of the [FPSO] with any existing, or new, management of the Company. We would be keen to enter into conceptual discussions around such extension constructs/scenarios with [Crystal Amber] now if you feel that this may assist clarify to the court? Various constructs could be put in place such as rolling six or twelve month extensions. Such constructs are typical in the sector for FPSO's 'on station' if formal contractual lease extension options don't quite 'fit' - and to prolong field life and maximise economic recovery for the benefit of all stakeholders."

115. The Company filed a further witness statement from Mr Maris in response, dated 25 June 2021. Mr Maris indicates that he did not believe the Company had ever said that Bluewater's position was that it would not negotiate or enter into an agreement unless the Plan was approved. He said that the last communication with Bluewater had been a 25-minute conversation on 11 May 2021, when Bluewater had made an offer of a 12 month extension (at a fixed cost of $27.4 million) plus 8% of revenues, with the option for a further 6 months. Bluewater would also require $18.67 million to be placed into escrow to cover the impact of an early termination and any decommissioning costs Bluewater might face. Other conditions were also imposed. The Company's response was to say that any extension would need the financial support of the Bondholders, and that they further discussion would "be relevant" after the court hearing to sanction the Plan.

116. On the basis of this further evidence, it is clear that Bluewater are willing to negotiate with or without the sanction of the Plan, and that it is the current board's view that they are unable to proceed without Bondholder support that has meant negotiations have been put off until after the decision to sanction the Plan.

117. Mr Smith placed much more emphasis on the point that the directors would be unable to negotiate an extension in the absence of the restructuring. He contended that it would, or at least could, be a breach of the duty of directors to act in the interests of creditors (see *Sequana*, above) to cause the Company to assume a new liability to Bluewater when it is insolvent. That was not a risk they faced under the Plan because it is a term of the Plan that at the extended maturity date in respect of the Bonds, any amount outstanding would be converted into equity. The Plan therefore removed the insolvency risk.

118. He referred me to *Re Ralls Buildings Ltd* [2016] EWHC 243 (Ch). One of the issues in that case was whether directors accused of wrongful trading could rely upon the defence in section 214(3) of the Insolvency Act 1986, namely that (having passed the point that they knew or ought to have realised that there was no reasonable prospect that the company would avoid going into insolvent liquidation or administration) they took every step with a view to minimising the potential loss to creditors. Snowden J concluded that this defence was not open to directors where, although their actions were aimed at reducing the net deficit, they did so by paying certain existing creditors at the expense of new creditors who ended up not being paid. On the facts, no order was made against the directors, however, because their actions had not in fact caused an increase in the net deficiency of the company.

119. It was not suggested that the triggering point for wrongful trading has been reached in relation to the Company. I do not accept that the duty to take into account the interests of creditors is to be equated with the obligation to take every step with a view to minimising potential loss to creditors. Nor do I accept that the directors could not properly enter into an extension of the Charter while the Company's ability to repay the Bonds at maturity remains in doubt.

120. Whether they could do so would depend upon the terms of the extension and their assessment of the Company's financial position and the interests of the Company and its creditors as a whole at the time. As to the former, a fixed term of longer than the period the P6 well was likely to remain viable would no doubt be problematic (and was why the option to extend was not exercised). A shorter extension, or one for a rolling period or periods, would not. The email from Bluewater of 24 June 2021 indicates that this type of deal is both typical and a real possibility in this case. The terms of the extension offered in Bluewater's letter of 11 May 2021 confirms that this is possible. It is not reasonable to think the terms offered in that letter are the final word, in the absence of attempts to negotiate that offer since it was made six weeks ago.

121. As to the latter, I have already noted that, in principle, an extension to the Charter is clearly in the interests of all stakeholders. The benefits offered by the Plan are dependent upon it. Thus it is not only objectively in the Bondholders' interests, but it is something they support (albeit only if they are able to acquire control of the Company). There is no difference, so far as the objective interests of the Bondholders are concerned, between extending the Charter within, or outside, the Plan. The essential point is that in order to improve their chances of recovery under the Bonds the extension to the Charter is required, and that is so whether or not the Plan is sanctioned. While incurring capital expenditure on unconnected projects would likely be (for the reasons I have referred to above) a breach of duty by the directors, that is not so – depending on the extent of payment, the likely returns from further extraction of oil during the period of the extension and the terms of the deal – in the case of expenditure on an extension of the Charter which all parties recognise is for their benefit.

122. In the relevant alternative these would be matters which would fall to be decided by the new board.

123. Accordingly, I reject the contention that it is unlikely that an extension of the Charter could be negotiated and entered into without the Plan.

Conclusion as to the relevant alternative

124. I return to the essential question whether I can be satisfied that the shareholders would be no better off under the relevant alternative than having a 5% stake in equity in the Company which promised a less than meaningful return.

125. For the reasons I have set out above, given that the relevant alternative involves on each side's case the Company's continued profitable trading for at least a further year, I do not think this question requires me to be satisfied – in order to find against the Company – that the most likely outcome from the relevant alternative is that there will be a return to shareholders at some point in the future. In my judgment, the fact that there is a realistic prospect (based on one, other or a range of the possibilities outlined above, including through refinancing any shortfall) that the Company will be able to discharge its obligations to the Bondholders, leaving assets with at least potential for exploitation, is enough to refute the contention that the shareholders will be no better off under the relevant alternative than under the Plan.

126. In other words, to retain 100% of the equity in Company that is continuing to trade, with a realistic prospect of being able to repay the Bonds in due course, is to my mind a better position than immediately giving up 95% of the equity with a prospect of a less than meaningful return as to the remaining 5%.

127. I take into account, as was urged on me by Mr Smith and Mr Robins, that while the Company may outperform the projections on which the PwC report is based, it may also do much worse: there may be problems with the P6 well preventing it producing any oil without further major investment; the water-cut might increase dramatically; and the oil price might fall. This does not

detract, however, from the fact that the prospect of it either meeting the projections, but the Company being able to trade beyond May 2022 and thus opening up the possibilities identified by Mr Thornton for bridging the funding gap, or outperforming the projections, is a realistic one.

128. Accordingly, I find that threshold Condition A is not satisfied.

<u>Urgency</u>

129. Notwithstanding that the relevant alternative would see the Company continuing to trade, rather than an imminent liquidation, this application is made on the basis that sanction of the Plan is urgently required, for two reasons. The first is that it is urgently necessary to enter into commitments as to future expenditure, namely the extension of the Charter. I agree that it is necessary to maintain negotiations with Bluewater and to secure the extension as soon as practicable. For reasons already given, however, I do not see that the Plan is essential for that purpose. The fact that Bluewater has made contact directly with Crystal Amber reinforces that view.

130. The second is that unless the Plan is sanctioned in good time before the annual general meeting on 30 June 2021, the likelihood is that a new board will be appointed who will withdraw it. (In fact, as indicated at the end of the hearing, if the Plan were sanctioned, an order would be required by first thing on Monday 28 June 2021, to enable the requisite steps to be taken to issue the shares pursuant to the Plan to the Bondholders). The court has accommodated the Company's desire for urgency in respect of this hearing, and Crystal Amber sensibly did not pursue a separate application for an adjournment on procedural grounds, recognising that the adjournment question could not be divorced from the overall merits given that, *de facto*, an adjournment would mean that the Plan was not sanctioned.

131. In itself, however, the fact that the board is likely imminently to be replaced is not in my judgment a good ground of urgency (particularly as I have rejected the submission that the new directors would be likely to take precipitate action leading to an early insolvent liquidation). Unless and until a company goes into a formal insolvency process, the identity of those managing it is under the ultimate control of the general body of shareholders. It is their collective right to replace the board if they see fit. While actual or likely insolvency causes a change in the content of the duty of the directors (and, provided it can be shown that there is no economic value in the shares, entitles the creditors in a restructuring to determine allocation of value as between interested stakeholders – see [45] above), absent the intervention of a formal insolvency proceeding it does not remove the shareholders' rights under the articles of association, including to appoint and remove directors. The Bondholders contracted on terms which gave them rights as unsecured creditors only, without security and with no rights to control appointments to the board.

132. Accordingly, I do not think that the AHC's desire to avoid the replacement of the board is a legitimate ground for urgency, so as to justify taking any different approach to the assessment of the likely consequences in the relevant alternative to that I have taken above.

Discretion

133. In light of my conclusion that threshold Condition A is not satisfied, the discretion whether to sanction the Plan does not fall to be exercised. Had it been necessary to exercise that discretion, the points I have made above would have led me to the conclusion to refuse to sanction the Plan.

134. In short, the following circumstances in particular point against exercising the discretion to sanction the Plan:

(1) The Company is profitable, and anticipated to remain profitable for at least the next year;

(2) The Company's evidence is that the P6 well is likely to remain economically viable until early 2024;

(3) There are reasonable grounds to believe that the Company will be able to negotiate an extension of the Charter on terms which enable it to continue extracting oil from the P6 well beyond July 2022;

(4) It is in the interests of all the Company's stakeholders that this happens;

(5) Despite the fact that there is projected to be a shortfall between available cash and the sum required to redeem the Bonds at maturity (and the AHC have expressed the firm view that they are not prepared to extend the maturity date without the Plan being sanctioned so that they can acquire control of the Company) there is a reasonable possibility that the size of the shortfall might be such that measures could be taken, such as refinancing, so that it could be bridged;

(6) The question posed by the Company and the AHC, whether the Company can generate sufficient cash from trading alone to repay the Bonds in full at maturity is too narrow and ignores the possibility of such measures being taken;

(7) The Plan would remove, immediately and irrevocably, all but a fraction of the current shareholders' equity in the Company;

(8) In considering whether the Plan fairly allocates value between the different stakeholders, it is not sufficient to conclude that the current valuation of the future revenue stream from the P6 well (based on ERCE's estimates of production and the Brent forward curve) indicates that this will be insufficient to repay the Bonds in full. This would deprive the shareholders of any potential upside which could be generated from future trading combined with steps the new board might legitimately take to address the repayment of the Bonds in July 2022;

(9) Unless (which I have not accepted) the rejection of the Plan would be likely to prevent the Charter being extended, the option of continued trading beyond July 2022 would be preserved such that, if actual performance and the steps taken by the new board do not improve the

financial outlook over the coming months, it is reasonable to believe that a restructuring could be undertaken at a later stage, with the same aim of maximising revenues from the P6 well. This reinforces the conclusion that shareholders should not immediately be deprived of anything other than a de minimis interest in the equity;

(10) That is not to say that the relevant alternative would be a different deal. Mr Robins rightly pointed out that the possibility of a different deal is not a relevant alternative. It *is* to say, however, that given the relevant alternative in this case (continued trading) it is relevant, in considering what consequences may flow, to take account of the fact that the interests of the Company, the shareholders and the Bondholders are likely to be aligned in ensuring the Company continues to exploit the Lancaster area until the point it ceases to be economically viable.

(11) There is no other sufficient ground of urgency which means that it is imperative that the Bonds be restructured now. In particular, the AHC's desire to obtain control of the Company is not a good reason to deprive the shareholders, now, of all but a fraction of their equity in the Company rather than waiting to see if actual performance over the coming months improves the outlook for the shareholders.

Conclusion

135. For the reasons set out above, I decline to sanction the Plan.