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Schemes of Arrangement: Irish court-sanctioned $1.65bn cross border restructuring recognised by US Bankruptcy Court

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Executive Summary

The recent *ex tempore* judgment of Mr Justice Barniville delivered June 6, 2019 in Re Ballantyne Re plc[1] confirms the Irish High Court's jurisdiction to sanction a scheme of arrangement between a company and its creditors that provides for the release of third parties pursuant to Part 9 of the Companies Act 2014 (the "Act").

In reaching his decision, Mr Justice Barniville expressly approved of recent scheme case law in other common law jurisdictions, including the recent decision of the Grand Court of the Cayman Islands in Re Ocean Rig UDW Inc[2] ("Ocean Rig").

Furthermore, it was a pre-condition to the implementation of the restructuring (envisaged by the scheme) that the scheme be recognised as a foreign main proceeding under Chapter 15 of the US Bankruptcy Code and United States Bankruptcy Court for the Southern District of New York granted a Recognition Order in respect of the Irish scheme of arrangement on June 12, 2019.

What is a Part 9 Scheme of Arrangement?

A scheme of arrangement under Chapter 1, Part 9 of the Act is a court approved arrangement between a company and its shareholders and/or creditors that can be used to effect a solvent reorganisation of a company or group structure as well as to effect insolvent restructurings ("a Part 9 Scheme of Arrangement"). Part 9 Schemes of Arrangement can be utilised in many circumstances: the merger of two or more companies, the subdivision of a company into two or more companies, certain takeovers and other amalgamations. It can also be used by a company in financial difficulties to reach a binding agreement or compromise inter alia with its creditors. It is the latter context which arose in Ballantyne[3]. The Part 9 Schemes of Arrangement provisions are largely identical to the English scheme of arrangement provisions contained in Part 26 of the Companies Act 2006. When a company proposes to enter into a Part 9 Scheme of Arrangement with its creditors and/ or its members and it obtains the sanction of a special majority of the members and/or creditors affected by it, then, once the court approves it[4], the compromise or arrangement is binding on all the creditors and/or members.

In order for a scheme of arrangement to be binding, the following criteria must be met:

1. The proposed scheme must be approved by majority in number representing at least 75% in value of the creditors or class of creditors or members or both (as the case may be) present and voting at the scheme meeting (a "Special Majority");
2. Appropriate notice of the scheme meeting(s) must be given; and
3. The High Court must sanction the scheme of arrangement.

1 [2019] IEHC 407

2 18 September 2017, Grand Court of the Cayman Islands, Parker J.

3 Such creditors' schemes of arrangement should not be confused with a scheme of arrangement proposed by an examiner under Part 10 of the Act. While both involve court sanction and are binding on dissenting creditors, there are a great many differences which go beyond the ambit of this article. For an explanation of examinership, please see our previous advisory here.

4 Under section 453 of the Act

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Background to Application

Pursuant to section 453(2) of the Act, Ballantyne Re Plc ("Ballantyne") sought an order sanctioning a proposed scheme of arrangement between Ballantyne and certain of its creditors (the "Scheme").

The objective of the Scheme was to provide for a compromise of Ballantyne's obligations under the relevant notes and for the commutation of certain guarantees provided by the guarantors under those notes.

The meetings at which the Scheme was proposed (the "Scheme Meetings") were convened properly and due notice was given to the relevant creditors. The Scheme was approved by the overwhelming majority of Ballantyne's creditors (98.12% of those present and voting of one class of creditors had voted in favour of the Scheme and 100% of those present and voting of the other class of creditors also voted in favour of the Scheme).

Ballantyne's application to have the Scheme sanctioned by the Court was opposed by one creditor, ESM Fund ILP ("ESM"), the holder of some US$5m class A 3d notes, on three main grounds:-

1. That the Scheme Circular was materially deficient in terms of the information it provided to the noteholder / creditors and in terms of the impression it created concerning the financial position of Ambac;
2. The Court had no jurisdiction to sanction any scheme of arrangement that makes provision for third party releases; and
3. That the Scheme, if sanctioned, would extinguish a complaint that ESM had against Ambac in New York, which complaint was filed after the Scheme Meeting had taken place.

Court approval of the Part 9 Scheme of Arrangement

Mr Justice Barniville spent a considerable portion of his judgment addressing the test that has to be met before a Court will sanction a scheme of arrangement.

Mr Justice Barniville cited with approval the judgment of Mr Justice Kelly (as he then was) in *Re Colonia Insurance (Ireland) Ltd*[5] in which Mr Justice Kelly set out the five-part test that had to be met in order that the Court would sanction a scheme:

1. The Court must be satisfied that sufficient steps have been taken to identify and notify all interested parties;
2. The Court must be satisfied that the statutory requirements and all directions of the Court have been complied with;
3. The Court must be satisfied that the classes are properly constituted;
4. The issue of coercion is one that the Court must consider; and
5. The Court must be satisfied that the scheme of arrangement is such that an intelligent and honest man, a member of the class concerned, acting in respect of his interest might reasonably approve.

Mr Justice Barniville noted that the reference to coercion in the above test was intended to be interpreted as referring to improper coercion as all schemes involve an element of coercion vis-à-vis any dissenting creditor.

In assessing the fifth criterion above in the context of the Scheme, Mr Justice Barniville was of the view that the decision in Ocean Rig was of "*considerable assistance*". In *Ocean Rig*, the Grand Court of Cayman was of the view that the Court could only refuse to sanction a scheme if it was satisfied that an honest, intelligent and reasonable member of the class could not have voted for the scheme, "*and in that regard the Court's own views as to whether the scheme is reasonable or even the best scheme is not relevant*".

Mr Justice Barniville expressly endorsed the above position adopted in Ocean Rig. He stated that "*the court should be slow to differ from the vote at the relevant meeting. However, the court must be satisfied that the proposed Scheme is reasonable, viewed from the perspective of an honest, intelligent and experienced person of business who is familiar with the Scheme. The court should only differ from the majority if it is satisfied that an honest, intelligent and reasonable member of the class could not have voted for the Scheme. The onus is on the objecting [member or] creditor, .. to establish this and it must do so… to the standard of the balance of probabilities.*"[6]

5 [2005] 1 IR 497

6 Ibid at para 73

Accordingly, Mr Justice Barniville said the burden rested with ESM to establish that the court should not sanction the scheme and that it had to do so, on the balance of probabilities.

ESM's Opposition to Sanctioning of the Scheme

Mr Justice Barniville ultimately rejected all three grounds put forward by ESM in opposing the sanctioning of the Scheme.

ESM's complaints regarding the alleged information deficit contained in the Scheme Circular and its complaint regarding the impact of the Scheme on other proceedings it had instituted in New York were fact specific. Having assessed the evidence before the Court, Mr Justice Barniville dismissed these complaints.

ESM's complaint regarding the Court's alleged lack of jurisdiction to sanction a scheme that release third parties if proved, would have a potentially very significant impact on schemes of arrangement under Irish law.

Third Party Release

ESM argued that the Court did not have the necessary jurisdiction to sanction the Scheme in circumstances where the Scheme contained a release of its (and other creditors') recourse to Ambac.

In assessing ESM's objection under this heading, Mr Justice Barniville referred with approval to a number of decisions in other common law jurisdictions in which schemes of arrangement have been sanctioned notwithstanding that they included (a) release(s) of a third party, such as Ambac.

Having reviewed and approved of the "pro release" cases in other common law jurisdictions, Mr Justice Barniville noted that there was no attempt by Oireachtas when enacting Part 9 of the Act to exclude third party releases from schemes of arrangement.

Mr Justice Barniville stated that the fact that the scheme would not be sanctioned if it was unfair, inequitable, improperly coercive or unreasonable, combined with the requirement to obtain a Special Majority amounted to a fair, reasonable and proportionate balance by the Oireachtas of the various competing interests involved in a scheme of arrangement.

Mr Justice Barniville opined that the release of Ballantyne's creditors' recourse to Ambac pursuant to the Scheme was necessary for the Scheme to work having regard to the central involvement of Ambac as a guarantor for a number of the classes of notes.

Case significance & US Chapter 15 Recognition

Mr Justice Barniville's judgment in *Ballantyne Re plc* is extremely helpful in so far as it confirms that there is nothing in principle prohibiting the High Court from sanctioning a scheme of arrangement that makes provision for third party releases –in line with that of other common law jurisdictions with equivalent schemes of arrangement.

The judgment also highlights the similar considerations that will be taken into account by the Courts in Ireland and in other common law jurisdictions in deciding whether or not to sanction a proposed scheme of arrangement.

Finally, it is noteworthy that the Irish commercial court was in a position to turn around a lengthy, detailed and reasoned judgment in such a short period of time. The application seeking sanction of the scheme proposals was filed on Wednesday 22 May 2019. As ESM contested the application, 13 Affidavits were filed and exchanged between the parties along with legal submissions. Mr Justice Barniville heard the matter 14 days later on Wednesday 5 June 2019 and delivered judgment on the evening of Thursday 6 June 2019. This turnaround was to facilitate a pre-condition to the implementation of the restructuring (envisaged by the scheme) that the scheme be recognised as a foreign main proceeding under Chapter 15 of the US Bankruptcy Code by the United States Bankruptcy Court and which hearing was due to take place on 11 June 2019. The Chapter 15 Recognition Order was entered by the United States Bankruptcy Court for the Southern District of New York on 12 June 2019.

At a glance: Irish Part 9 Scheme of Arrangement as a cross border restructuring tool

In light of the legal uncertainty which Brexit has created, it is possible that Ireland will become a more popular legal jurisdiction for directors of international corporates in difficulties and their advisors to consider. As the decision in *Ballantyne Re* shows, Ireland, with its common law system, English speaking jurisdiction and practical commercial approach to restructuring and insolvency matters can provide an effective alternative to offer those looking for a substitute to the English scheme of arrangement.

A Part 9 Scheme of Arrangement has the following notable features: -

- Unlike examinership, there is no restricted time period within which the company must formulate or put into effect the scheme of arrangement. This can be useful in the context of large and complex cross-border restructurings.
- Unlike examinership, there is no requirement that the company be a going-concern. It can simply be a holding company which provides greater flexibility in the context of a group restructuring
- There is no restriction on including guaranteed debt as part of the scheme proposals
- An Irish Court order sanctioning a Part 9 Scheme of Arrangement is a Court order for the purposes of the Recast Judgments Regulation[7] and will be automatically recognisable and enforceable throughout the EU
- Part 9 Scheme of Arrangement is capable of recognition in the US under the Chapter 15 recognition process
- A Part 9 Scheme of Arrangement does not constitute an Insolvency Proceeding for the purposes of Annex A of Regulation (EU) 2015/848 of 20 May 2015 on Insolvency Proceedings (recast)

Walkers can provide company debtors, creditors and shareholders with advice and court representation in respect of Part 9 Schemes of Arrangement and also can advise on other suitable restructuring mechanisms such as examinership. We also have leading multi-jurisdictional expertise in several other common law jurisdictions where schemes of arrangement are available. For a useful discussion of how schemes of arrangement work in other common law jurisdictions, please refer to Walkers' recent advisories here and here.

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7 Regulation (EU) No 1215/2012 of the European Parliament and of the Council of 12 December 2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters

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