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Legal Update

Developments in Restructuring Plans: Gategroup

On 26 March 2021, Mr Justice Zacaroli of the English High Court sanctioned a restructuring plan (the **Plan**) proposed by gategroup Guarantee Limited (**Gategroup**), following approval at two creditors' meetings convened pursuant to a judgment handed down by Mr Justice Zacaroli on 17 February 2021.

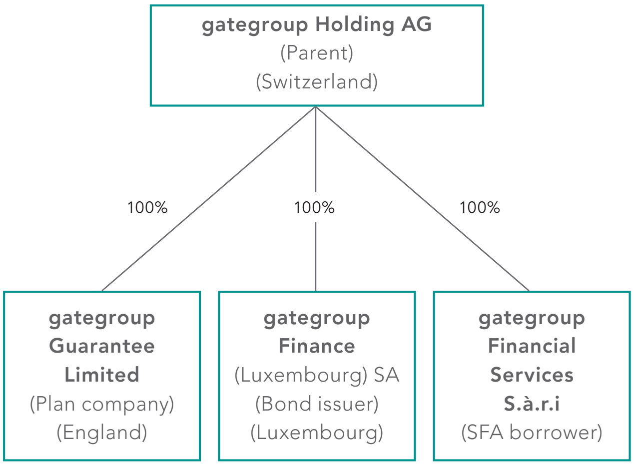
This latter judgment contained a detailed consideration of significant (albeit subsequently withdrawn) written objections from creditors on a number of grounds, and has provided unprecedented (and in some ways, surprising) insight into how the English courts are likely to approach a number of issues relating to the relatively new restructuring plan and where there may be divergence from the similar and much older scheme of arrangement.

Summary of the Plan

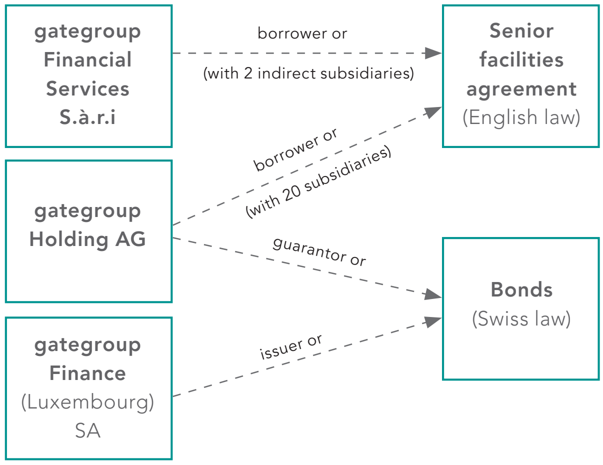
Gategroup is wholly owned by gategroup Holding AG (the **Parent**) which, together with its subsidiaries (the **Group**), is the world's largest provider of airline catering services. As a result of the reduction of flights globally due to the pandemic, the Group's business plummeted with the result that it experienced serious financial difficulties.

The Plan is part of a wider restructuring of the Group, each element of which (including the injection of CHF500m by the Group's ultimate shareholders) is inter-conditional. The Plan itself covers two of three of the Group's principal financing arrangements, being (i) a senior facilities agreement (the **SFA**) entered into by gategroup Financial Services S.à.r.l. (**Luxco II**, a wholly owned subsidiary of the Parent) and two of its indirect subsidiary companies (as borrowers), comprised of a EUR350m revolving facility and a EUR250m term loan facility (the lenders under the SFA being the **Senior Lenders**), and (ii) CHF350m of bonds (the **Bonds**, the holders of these being the **Bondholders**), issued by gategroup Finance (Luxembourg) SA (the **Issuer**, a wholly owned subsidiary of the Parent, and incorporated in Luxembourg). A diagram of this structure is set out below. The Plan amends the maturity of the SFA and the Bonds by five years and makes certain other amendments to the terms of the SFA and the Bonds.

Gategroup - Group Structure



Gategroup - Financing structure subject to the Part 26A restructuring plan



Artificial Structures and "Good" Forum Shopping

Without a restructuring plan, the Bonds' maturity could not be extended (due to the burdensome quorum requirement in the Bonds' terms for amendments and the fact that many of the holders were retail investors with small individual holdings), which ultimately would have led the Group into an insolvency process within weeks. The Issuer, although it had its centre of main interests (**COMI**) in England, was not in a position to propose a restructuring plan as to do so would have constituted an event of default under the Bonds leading to potential acceleration and enforcement action.

Consequently, Gategroup was incorporated in England and Wales and was interposed into the Group's borrowing arrangements through the execution of a deed of indemnity and contribution (the **Deed Poll**) in favour of the Senior Lenders and the Bondholders. Through this, Gategroup agreed to pay the liabilities outstanding under the SFA and the Bonds, whilst an accompanying contribution payment agreement required such payments to be made by the respective obligors under the SFA and the Bonds. The Deed Poll created liabilities (albeit artificial liabilities) for Gategroup to the Bondholders and the Senior Lenders, which it could rely on in order to propose a restructuring plan (continuing the trend identified in our PizzaExpress update).

This artificial structure was the only solution available to allow a restructuring of this sort to be effected given the quorum requirements of the Bonds. Although in the instant case such a structure was not necessary to give the English court jurisdiction (given that Gategroup was incorporated in England), the Court did go on to broadly endorse the use of such an artificial structure in order to engage the jurisdiction of the English Court, and that this could be seen as "good forum shopping" where such a structure was being used to achieve the best possible outcome for all parties. The Court was careful to note, however, that where an artificial structure is being used to override legitimate interests of creditors in a way which is wholly objectionable (such as where a primary obligor is seeking to avoid applicable principles of insolvency law under the laws that apply to it or where the attempt to compromise plan creditors' rights against third parties would not be recognised in any of the relevant foreign jurisdictions where it mattered), it remains open to an English court to use its discretion to refuse to sanction a plan (or even refuse to convene a meeting of the creditors).

Restructuring Plans are Insolvency Proceedings

Given that (i) the Bonds contained an exclusive jurisdiction clause in favour of the courts of Zurich, and (ii) Gategroup's application was filed in advance of the Brexit implementation date (1 January 2021), the question arose as to whether restructuring plans fall within the "bankruptcy exclusion" in the Convention on Jurisdiction and Enforcement of Judgments in Civil and Commercial Matters (the **Lugano Convention**). If restructuring plans did fall within the exclusion, the Lugano Convention would not have applied and the English court would not be bound to give effect to the jurisdiction clause in favour of the Zurich courts, ultimately allowing the Plan to proceed.

The Court found that the Plan did indeed fall within the "bankruptcy exclusion" as an insolvency proceeding, the Lugano Convention did not apply and the Court had jurisdiction to sanction the Plan.

In making this decision, the Court distinguished restructuring plans from schemes of arrangement primarily on the grounds that a restructuring plan is only available where two conditions are met, being that (i) there exists actual or potential financial difficulties which threaten the ability of the debtor to continue as a going concern, and (ii) the proposed plan must address those financial difficulties. This is in contrast to the position for schemes of arrangement, which may be proposed irrespective of the financial position of the company. Consequently, the Court considered that Part 26A of the Companies Act 2006 (under which restructuring plans may be initiated) is a law relating to insolvency as restructuring plans constitute proceedings designed to enable a company in financial difficulties to reach a composition or arrangement with its creditors, with the ultimate purpose of avoiding insolvency.

This particular element of the judgment comes as somewhat of a surprise and stands in contrast to a number of recent judgments on restructuring plans (including *PizzaExpress* and *Deep Ocean*), both of which proceeded on the basis that restructuring plans, like schemes of arrangement, were civil or commercial matters, rather than matters of insolvency. However, in each of those cases the point was neither determined, nor the subject of argument before the relevant court.

The outcome in Gategroup could significantly limit the recognition of restructuring plans in other jurisdictions (particularly European jurisdictions), diminishing their marketability at a time when such plans are starting to gain traction. In particular, the judgment may extinguish any possibility of being able to undertake significant airline restructurings in England using the restructuring plan where there are dissenting creditors, given the similarity of the bankruptcy provisions of the Lugano Convention and the Cape Town Convention. We previously explored this issue in greater detail in our February alert; in summary, should restructuring plans constitute an "insolvency-related event" for the purposes of the Cape Town Convention, it would not be possible to amend any obligations of a debtor and compromise any creditor whose interests are protected by the Cape Town Convention without the consent of that creditor, potentially rendering the cross-class cram down mechanism redundant in this context.

Similarly, the Gategroup judgment could also limit the use of the Hague Convention for matters involving restructuring plans due to the bankruptcy exclusion in the Hague Convention being expressed in broadly the same terms as that contained in the Lugano Convention. If restructuring plans were to fall within the bankruptcy exclusion in the Hague Convention, it would not be possible to rely on such convention to achieve international recognition and enforcement of a judgment relating to a restructuring plan.

Class Composition

Contrary to the proposal put forward by Gategroup, Mr Justice Zacaroli ordered that the Senior Lenders and the Bondholders be placed in separate classes of creditors for the purposes of voting on the Plan, finding that the Senior Lenders and the Bondholders did not satisfy the test for a single class due to the materially different rights that they each had under the SFA and the Bonds respectively, including that these rights were against different obligors (when looking behind the artificial structure). Gategroup's obligations to the Senior Lenders were satisfied by procuring that Luxco II (and the other obligors under the SFA) pay the Senior Lenders whereas Gategroup's obligations to the Bondholders were satisfied by paying the Issuer and Parent. Mr Justice Zacaroli stressed that this exposure to different obligors made it impossible for the Bondholders and Senior Lenders to consult together due to the entirely different credit risk.

The contention that the Plan gives all creditors "a real prospect of full recovery, over time", and that the Bondholders had a "greater incentive to approve the Plan than the Senior Lenders" (all of whom had already approved the Plan) was rejected and described by the Court as an argument which stretches the concept of "more to unite than to divide" to "breaking point", making it clear that it is not for the Court to assume the acceptance of a particular class of creditors.

Mr Justice Zacaroli also considered that there were key differences in the amendments being made to the SFA and the Bonds under the Plan (for example, the differences in interest rates and the removal of the event of default triggered by a change of control in the Bonds (there being no similar right to waive in the SFA)). Mr Justice Zacaroli noted that if all of these points had stood alone, a different view may have been taken.

This reasoning should be taken into account, when considering class composition and the potential use of the cross-class cram down mechanism.

Conclusion

Contrary to expectations (including comments in other recent judgments), the judgment in Gategroup has shown a readiness on the part of the courts to make a distinction between schemes and plans, particularly with respect to how certain international treaties apply to each of them. In some cases, this may ultimately lead to a company experiencing financial difficulties needing to make an undesirable choice between the greater international recognition that a scheme of arrangement may afford, against the golden tool of cross-class cram down offered by a restructuring plan. This choice is potentially made more difficult by the demonstration of the Court's willingness to look through an artificial structure and fracture a class, meaning that it will not always be possible to use a scheme comprising of a single class of creditors to structure around this choice.

If you'd like to find out more about other aspects of the restructuring plan and its use so far, please see our COVID-19 response blog and podcast and our alerts on the PizzaExpress and Deep Ocean restructuring plans.

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