The Banking Law Journal

Established 1889

An A.S. Pratt™ PUBLICATION **MAY 2022**

LexisNexis

THE BANKING LAW JOURNAL

VOLUME 139 **NUMBER 5** **May 2022**

LexisNexis®

QUESTIONS ABOUT THIS PUBLICATION?

For questions about the **Editorial Content** appearing in these volumes or reprint permission, please call:

Matthew T. Burke at ..... (800) 252-9257
Email: ..... matthew.t.burke@lexisnexis.com
Outside the United States and Canada, please call . . . . . (973) 820-2000

For assistance with replacement pages, shipments, billing or other customer service matters, please call:

Customer Services Department at . . . . . (800) 833-9844
Outside the United States and Canada, please call . . . . . (518) 487-3385
Fax Number . . . . . (800) 828-8341
Customer Service Website . . . . . http://www.lexisnexis.com/custserv/

For information on other Matthew Bender publications, please call

Your account manager or . . . . . (800) 223-1940
Outside the United States and Canada, please call . . . . . (937) 247-0293

ISBN: 978-0-7698-7878-2 (print)
ISSN: 0005-5506 (Print)

Cite this publication as:

The Banking Law Journal (LexisNexis A.S. Pratt)

Because the section you are citing may be revised in a later release, you may wish to photocopy or print out the section for convenient future reference.

Editorial Office
230 Park Ave., 7th Floor, New York, NY 10169 (800) 543-6862
www.lexisnexis.com

MATTHEW BENDER

(2022–Pub.4815)

Editor-in-Chief, Editor & Board of Editors

THE BANKING LAW JOURNAL (ISBN 978-0-76987-878-2) (USPS 003-160) is published ten times a year by Matthew Bender & Company, Inc. Periodicals Postage Paid at Washington, D.C., and at additional mailing offices. For customer support, please contact LexisNexis Matthew Bender, 1275 Broadway, Albany, NY 12204 or e-mail Customer.Support@lexisnexis.com. Direct any editorial inquiries and send any material for publication to Steven A. Meyerowitz, Editor-in-Chief, Meyerowitz Communications Inc., 26910 Grand Central Parkway, #18R, Floral Park, NY 11005, smeyerowitz@meyerowitzcommunications.com, 631.291.5541. Material for publication is welcomed—articles, decisions, or other items of interest to bankers, officers of financial institutions, and their attorneys. This publication is designed to be accurate and authoritative, but neither the publisher nor the authors are rendering legal, accounting, or other professional services in this publication. If legal or other expert advice is desired, retain the services of an appropriate professional. The articles and columns reflect only the present considerations and views of the authors and do not necessarily reflect those of the firms or organizations with which they are affiliated, any of the former or present clients of the authors or their firms or organizations, or the editors or publisher.

POSTMASTER: Send address changes to THE BANKING LAW JOURNAL, LexisNexis Matthew Bender, 230 Park Ave, 7th Floor, New York, NY 10169.

POSTMASTER: Send address changes to THE BANKING LAW JOURNAL, A.S. Pratt & Sons, 805 Fifteenth Street, NW, Third Floor, Washington, DC 20005-2207.

Part 26A Restructuring Plan Proposed by a Non-English Company for the First Time Excludes "Out of the Money" Creditors and Shareholders from Voting

By Phillip D. Taylor and Anna Nolan*

The authors of this article discuss Smile Telecoms Holdings Limited's second restructuring plan, which excludes "out of the money" creditors and shareholders from voting on a Part 26A restructuring plan.

Smile Telecoms Holdings Limited, which is a Mauritius-incorporated company (with an establishment registered with Companies House in England) and the holding company of a group operating an internet and telecommunications business in Tanzania, Nigeria, Uganda, and the DRC, has recently proposed its second Part 26A restructuring plan. On March 30, 2022, the UK High Court judge sanctioned the Smile Telecoms restructuring plan and handed down a written judgment.

The Smile Telecoms second restructuring plan is significant because:

- For the first time, the court has exercised its power under Section 901C(4) of the Companies Act 2006 to exclude "out of the money" creditors and shareholders from voting on a Part 26A restructuring plan on the basis that they have no genuine economic interest in the plan company.
- It has been proposed by a non-English company in order to change the capital structure, including the shareholder structure, of that non-English company through an English restructuring tool.

---

* Phillip D. Taylor is a partner at Alston & Bird LLP handling both contentious and non-contentious matters, in-court and out-of-court restructurings, and contingency planning and advisory mandates for multinational corporations, private capital funds, banks, insurance companies, and restructuring office holders. Anna Nolan is counsel at the firm assisting a wide range of clients including hedge funds, special situations investors, trustees, providers of rescue and exit finance, issuers, sponsors, bondholder committees, administrators, and debtors with distressed transactions, conducting corporate, and financial restructurings and general insolvency matters. Resident in the firm's office in London, the authors may be reached at phillip.taylor@alston.com and anna.nolan@alston.com, respectively.

BACKGROUND

The Smile Telecoms group suffered financial difficulties, and in March 2021 a first restructuring plan, which facilitated the injection of additional secured debt by the company's super senior lender, 966 CO. S.à r.l., was sanctioned by the English courts.

However, the company has faced liquidity constraints (insufficient funds to pay trade creditors or the existing super senior facility which matured on December 31, 2021) and engaged in further discussions with its lenders to complete certain asset disposals on a solvent basis and avoid going into an immediate administration.

The company proposed, among other things:

- An additional liquidity injection from the super senior lender, 966.
- The acquisition of control of the company by 966 through the issuance of 100 percent of the company's new ordinary share capital to 966.
- The conversion of the ordinary shares and the preference shares into redeemable deferred shares which may be redeemed for nominal consideration.
- The discharge of the company's financial debt ranking after the super senior liabilities in return for certain ex gratia payments.
- The issuance of a contingent value rights instrument by the company to the super senior lender and to the senior lenders, which would allocate any value realised above certain new money and super senior debt repayment thresholds to the lenders.

The company has a number of existing creditors. It is a borrower under a super senior facility entered into between the company and 966, which is governed by English law. There are also a number of senior facilities which are owed to a number of banks. To establish the rights of the creditors as between themselves, a number of parties entered into an English-law-governed intercreditor agreement. The enforcement waterfall in the intercreditor agreement provides for recoveries to be paid to the super senior lender ahead of payments to the senior lenders.

EXCLUSION OF CLASSES THAT HAVE NO GENUINE ECONOMIC INTEREST IN THE COMPANY

At the Smile Telecoms convening hearing, the court, for the first time, exercised its power under Section 901C(4) to exclude the company's sharehold-

ers and out-of-the-money creditors from voting on the plan. The court was satisfied that only one creditor class had a genuine economic interest in the plan company and based on the evidence this was not "a marginal case."

The general rule under English law is that every creditor or shareholder of the plan company whose rights are affected by the plan must be permitted to vote on the plan by participating in a meeting convened by the plan company (with the approval of the court granted at the convening hearing).

Section 901C(4) provides for an exemption from the general rule in circumstances where the court "is satisfied that none of the members of [a] class [whose rights are affected by the compromise or arrangement] has a genuine economic interest in the company."

The court's power under Section 901C(4) to exclude its out-of-the-money creditors and shareholders from voting is very different to the "no worse off" test for the cross-class cramdown power under Section 901G of the Companies Act 2006. The power under Section 901C(4) to exclude a class from voting requires the company to satisfy the court (on the balance of probabilities) that none of the members of the classes to be excluded have a "genuine economic interest" in the company by reference to the relevant alternative. In other words, the court has to be satisfied that the excluded out-of-the-money classes do not have any economic interest (in a real, as opposed to a theoretical or merely fanciful, sense);[1] in the relevant alternative (in this case, the administration of the plan company). By contrast, a class may be crammed down whether or not its members have a genuine economic interest, provided that at least one in the money class voted in favor of the plan and the dissenting class is no worse off than it would be in the relevant alternative.

SUFFICIENT NOTICE AND OPPORTUNITY TO FORMULATE A CHALLENGE

If the company intends to rely on Section 901C(4), it will need to ensure that sufficient, comprehensive information is shared with interested parties ahead of the convening hearing because the court will want to ensure that all parties, in particular those who are to be excluded from voting, have had sufficient time and information to examine and challenge the evidence.

In this case, the company provided creditors with draft financial documentation and information about the sales process in mid-November 2021 and therefore creditors had almost two months to consider the documentation. The substantial evidence was also uploaded to the information agent's portal on

[1] *See Re Virgin Active* paras 247 to 249.

December 15, 2021. As a result, the court was satisfied that creditors had adequate time to formulate a challenge.

IMPORTANCE OF THE VALUATION EVIDENCE

Exclusion on grounds of "no economic interest" is a high bar, and the court may refuse to exercise its discretion for a range of reasons. Examples of factors that might influence the court's discretion are:

- The valuation evidence is insufficient.
- There is a tight timetable to complete the restructuring.
- Inadequate notice has been given to excluded creditors so that they do not have sufficient time to consider and prepare for a proper challenge.

In "marginal" cases or if there is some uncertainty, the court may require meetings of each relevant class and then the relevant out-of-the-money classes will be ultimately subject to a cross-class cramdown.

In this case:

- The senior lenders, who were valued as being out of the money, had accepted the valuation, which was provided to all interested parties that signed a non-disclosure agreement, with the exception of one senior lender who has decided not to appear at the convening hearing.
- The valuation had been carefully examined by the senior lenders and their advisors.

COMPROMISE OF RIGHTS OF SHAREHOLDERS OF A NON-ENGLISH COMPANY (CONVENING HEARING)

It is a well-established principle that the law of incorporation of a company will typically regulate the rights of shareholders (in this case—the law of Mauritius). In line with this principle, a senior creditor contended that the court would not have jurisdiction over the proposed restructuring plan because it also affected the rights of shareholders (and the company is incorporated abroad) and relied on the following passage in *Re Drax Holdings*: "It is almost impossible to envisage circumstances in which the English court could properly exercise jurisdiction in relation to a scheme of arrangement between a foreign company and its members which would essentially be a matter for the courts of the place of incorporation."

At the convening hearing, the High Court was not satisfied that the point expressed in *Drax* was a roadblock to the court exercising jurisdiction for a number of reasons:

- The passage in Drax concerned a scheme between a solvent company and its members. The High Court stated that the same considerations may not apply to a restructuring plan concerning a company threatened with insolvency where the shareholders do not have a realistic economic interest.
- While the position of the shareholders as shareholders of a non-English company may be a factor to be taken into account, it may not be decisive if the connections between the creditors and UK jurisdiction are sufficiently strong.
- The company's center of main interests is in the UK. The High Court stated that Mauritian expert evidence will be relevant as to the effectiveness of the plan in the place of the company's incorporation (which will be further considered at the sanction hearing).
- The shareholders have not objected to an order being made convening a meeting of super senior lenders as the only class.

CHALLENGE

Shortly before the sanction hearing, an "out of the money" creditor (a senior lender to the company excluded from the plan meetings by the High Court) contested the company's valuation evidence and raised issues about recognition of the plan in Mauritius.

The relevant comparator report provided by Grant Thornton before the sanction hearing sets out a range of indicative financial outcomes for the various plan participants in each operating company of the group on a consolidated basis. Under the low case and high case scenarios, value would break in the super senior facility with a 54.9 per cent and 72.6 per cent return to the super senior lenders, respectively. There would be no return in either scenario to the senior lenders or any other stakeholder. After the sanction hearing, an out of the money creditor presented its own rival report with a valuation range showing that the value of the company breaks below the super senior level and therefore indicates some repayment to senior creditors. The out-of-the-money creditor argued that the plan is inherently unfair.

SANCTION HEARING (VALUATION CHALLENGE AND COMPROMISE OF RIGHTS OF SHAREHOLDERS)

At the sanction hearing, two other senior lenders (who had been excluded from voting by the High Court at the convening hearing) also opposed the restructuring plan. This is the first time the UK High Court has considered the issue of how or whether excluded out-of-the-money creditors should have a role at the sanction hearing.

The senior lenders' valuation challenge in this case was unsuccessful. The High Court judge said that the appropriate time to object would have been at the convening hearing (absent some good reason) if a plan company has given proper notice of the convening hearing and of its intention to seek an order under Section 901C(4), if those affected have had a proper opportunity to adduce evidence, if the court has been satisfied by the evidence adduced at the convening stage and if there has been no material change of circumstances.

The High Court considered whether it is appropriate for the English court to sanction a plan that will lead to the alteration of the constitution and share capital of an overseas company incorporated in Mauritius. The High Court confirmed that as a matter of concept, the jurisdiction exists for the English court to sanction such a plan.

The proposed amendments to the constitution of the plan company and the issue of new shares were to be achieved using a power of attorney granted to the plan company under the UK restructuring plan. The power of attorney would be used by the plan company to pass special resolutions in accordance with the companies law of Mauritius. The High Court was satisfied (on the basis of expert evidence provided by Mauritian local counsel) that the power of attorney could be used and would be effective in Mauritius to achieve the proposed amendments to the constitution of the plan company and its share capital as envisaged in the restructuring plan.

The High Court was also satisfied (on the basis of expert evidence provided to it) that the restructuring plan would be likely to be recognized and given effect against plan creditors in Mauritius, Nigeria (where the main operating company is based) and South Africa. While the company did not intend to seek local recognition of the plan or to open parallel local proceedings, the High Court was satisfied that if any dissenting creditor or shareholder tried to challenge the plan in the abovementioned jurisdictions, given the likelihood of recognition being provided in such jurisdictions, it was unlikely that sanction of the plan would be made in vain. Accordingly, the High Court has sanctioned the Smile Telecoms restructuring plan.

KEY TAKEAWAYS

Cross-Class Cramdown Versus Exclusion of Out-of-The-Money Classes

The High Court held at the Smile Telecoms convening hearing that the court may conclude that in assessing matters under Section 901C(4), the evidence is not sufficiently complete or satisfactory to enable the court to reach a concluded view because (1) an inadequate notice has been given, or (2) creditors or shareholders have raised objections which the court considers need further

evidence or investigation. On the other hand, if the court is satisfied by the evidence at the convening stage that none of the members of the relevant class has a genuine economic interest in the company, then the court may properly conclude that there is no purpose to be gained from requiring any meeting of that class.

As a result, the companies will need to decide if, depending on the facts of each case, it is better to (1) seek the exclusion of relevant out-of-the-money classes from voting, or (2) ask the court to use its cross-class cramdown power against those classes voting against the plan. So far, the cross-class cramdown power has been used successfully four times and the Section 901C(4) power has been used once in this case.

Are Out-of-The-Money Classes Deprived the Opportunity to Vote Under Section 901C(4)?

Yes—the out-of-the-money classes will not vote on the plan if the company wishes to exclude them and the court is prepared to exercise its discretion to do so. It would be interesting to see how case law on restructuring plans evolves in the future. Especially, it remains to be seen if the courts will be prepared to convene meetings of multiple classes of creditors at the request of the plan company when an interested party argues that the other classes are out of the money.

Although it is a new feature of Part 26A restructuring plans, the court has long been able to approve a scheme of arrangement without requiring approval from out-of-the-money classes. For example, in *Re Tea Corporation CA*,[2] the contributories were divided into two classes, preference shareholders and ordinary shareholders (who had no economic interest in the assets). The court of appeal held that the High Court could sanction the scheme despite the objections of the out of the money ordinary shareholders. However, the application of this rule may depend on the precise nature of the arrangement and of the rights that the company seeks to compromise.

Valuation Evidence

The court has considered the valuation evidence very carefully and was satisfied that the senior lenders and those below them in the waterfall of payments were out of the money. The valuation evidence is very important, as well as giving anyone who is proposed to be excluded from voting time to consider the evidence.

In this case, a valuation has been prepared by FBN. As mentioned above, it is worth pointing out that this was not a marginal case and that FBN's

[2] [1904] 1 Ch. 12.

appointment was accepted by the senior lenders and the super senior lender. FBN's efforts in selling the assets were reviewed by PwC, and the valuation has been provided to all the interested parties who have been prepared to give appropriate confidentiality undertakings. The valuation has been interrogated and explored by the senior lenders and their advisers at length. In addition, FBN has provided answers to detailed questions raised by the senior lenders. On the relevant comparator report, the senior lenders were clearly out of the money. Earlier versions of excerpts of the report prepared by Grant Thornton were provided to the senior lenders in November and December 2021, and the senior lenders have had ample time to consider them.

Valuation Challenge

The High Court made it clear that a creditor or shareholder wishing to oppose a plan must "stop shouting from the spectators' seats and step up to the plate." This means that creditors and shareholders must act quickly and engage in the restructuring plan process if they intend to present a successful challenge. In order to challenge the company's valuation evidence, it is recommended that a person challenging it: (i) obtains financial information from the company (either on a voluntary basis or by making a timely disclosure application), (ii) files its own expert evidence in accordance with the UK Civil Procedure Rules 1998, Part 35, and instructs the expert to engage in the production of a joint report in the normal manner, (iii) makes its expert available for cross-examination, and (iv) attends the hearing to address any arguments for the assistance of the court at the appropriate stage (the convening stage in the case of Section 901C(4) application, or the sanction hearing in the case of the cross-class cram-down power under Section 901G).

Disclosure

The plan companies need to keep in mind that if an order under Section 901C(4) is sought, disclosure of financial and other relevant evidence will need to take place at an earlier stage than might otherwise be the case (as described above).

Court's Discretion

When the valuation evidence is more marginal, the affected classes may have a better chance of arguing against their exclusion from voting, and the court may be reticent to exercise its discretion to exclude them.