

UK Restructuring Proceedings May Attract More Foreign Cos.

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In September 2019 the English High Court sanctioned two schemes of arrangement which were integral to the restructure of Syncreon International Group, a U.S.-headquartered global logistics business.

This appears to be the first time where a U.S.-headquartered group openly favored an English scheme of arrangement over Chapter 11 proceedings and the first time an English scheme was recognized in Canada under Part IV of the Companies' Creditors Arrangement Act RSC 1985.

This could lead to more U.S. and Canadian corporate groups seeking to use the English courts to restructure their financial liabilities as an alternative to Chapter 11 proceedings.

What Is a Scheme of Arrangement?

A scheme of arrangement is an English statutory procedure which enables a company to implement a compromise or arrangement with any of its members or creditors (or any class of the same). It requires a requisite number of affected members or creditors to vote in favor of the scheme and two court hearings.

Once approved, the scheme becomes effective and binding on all creditors and members. It is not, strictly speaking, an insolvency proceeding as the process emanates from the Companies Act 2006 (which is not within the U.K.'s insolvency legislation) but is commonly used by companies to restructure existing liabilities.

The advantages of the English scheme are that:

- It avoids the need to enter into formal insolvency proceedings and in turn avoids the potential stigma and negative impact that can arise from such proceedings;
- It is flexible — the objective of the scheme and the rights affected are not prescribed by the legislation;



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- The time from filing the application to approval of the scheme is relatively quick;
- The England and Wales court judges generally take a commercial view when deliberating over the applications;
- It can be used to cram down the rights of members or creditors (or a specific class of these) where unanimous consent is not possible (e.g. to remove minority shareholders);
- It is binding on all creditors and members of the company; and
- It is likely to be recognized in foreign jurisdictions such as the EU, the U.S. and Canada.

Background to the Scheme Applications

Syncreon was formed in 2007 when a leading logistics partner of several large technology companies merged with one of the world's biggest suppliers of supply chain services to the automotive industry. With help from private equity funds and debt finance, the combined business grew its operations and expanded into the retail, telecom and health care sectors.

The group's financial difficulties arose from the loss of its largest tech customer, a general downturn in the number of automotive customers, adverse consequences resulting from foreign currency movements, higher than anticipated launch costs and a loss of customer and supplier confidence.

To address their financial difficulties, Syncreon Group BV (a Dutch registered company) and Syncreon Automotive (UK) Ltd (an English registered company) filed scheme applications in the U.K. (together, the Syncreon schemes), even though the filing companies were part of the Syncreon group, a Michigan corporation with a majority of its operations and revenues based in North America.

Choice of English Scheme

The reasons given by the filing companies for the choice of an English schemes were:

- The anticipated higher costs associated with Chapter 11 proceedings;
- The avoidance of a formal insolvency proceeding and the related negative effects that an insolvency proceeding could have on the group; and
- The likelihood of recognition of the schemes in jurisdictions in which Syncreon BV and certain guarantors are incorporated.

The Syncreon Schemes

The Syncreon schemes concerned the following:

- A parent credit facility where Syncreon BV is the principal borrower and which is guaranteed by other members of the group including Syncreon U.K. This is secured and the principal outstanding was \$680 million; and

- A notes indenture issued by Syncreon BV pursuant to which \$225 million notes had been issued. These are also guaranteed by other members of the group including Syncreon UK. However, these are unsecured.

Under the Syncreon schemes, the group planned to reduce its approximately \$1.1 billion debt by \$625 million and provide the group with over \$250 million in additional liquidity:

- The parent credit facility debt would be released in exchange for restated debt of \$225 million owed by Syncreon BV and 80% equity (subject to dilution)[1] in a new Dutch parent company (Newco); and
- The notes would be cancelled in exchange for a 4.5% interest in the Newco together with warrants to acquire 10% of such equity (each, subject to dilution).

It is understood that other existing debts of the group would be restructured consensually and simultaneously with the implementation of the Syncreon schemes. A restructuring support agreement entered into in May 2019 provided for certain liquidity facilities to be restructured and new money to be provided. In return the lenders would receive equity in Newco.

In addition, the parent credit facility lenders and holders of notes who signed up to the restructuring support agreement before the stated deadline qualified for lock-up payments (which took the form of 5.5% equity in Newco for the parent credit facility lenders and 2.5% equity for the holders of the notes) in the event that the Syncreon schemes were implemented.

Unsecured trade creditors were not affected by the Syncreon schemes or corporate restructure. The majority equity holders of the group lost their interest in the Syncreon group as a result of the creation of Newco. Following implementation of the Syncreon schemes the anticipated return to the parent credit facility lenders is between 59% and 72% (with the benefit of the lock-up payment). The anticipated return to the holders of notes is between 7% and 10% (again with the benefit of the lock-up payment).

Court Sanction of the Syncreon Schemes

The first Syncreon scheme hearing was held on July 25, 2019. Judge Sarah Falk considered whether there was any major roadblock to the Syncreon schemes being approved, focusing on whether the jurisdiction of the English court was appropriate. Shortly before the applications were submitted, the governing law and jurisdiction of the parent credit facility and the notes were changed from New York law to English law with the express intention of improving the ability of the filing companies to apply for a scheme in England.

Such changes were made with the requisite majority consent and knowledge of the creditors. In addition, pursuant to the terms of the restructuring support agreement, 95% of both classes of creditors affected by the Syncreon schemes had agreed to submit to the jurisdiction of the English courts.

At the hearing, Judge Falk found that the change of the governing law to English law and the fact that the parties submitted to the jurisdiction of the English courts in the restructuring support agreement provided Syncreon BV with a sufficient connection with the English jurisdiction. As such, there was found to be no major roadblock to the Syncreon scheme applications.

Furthermore, after consideration of the composition of the classes affected by the proposed Syncreon schemes, Judge Falk ordered the summoning of meetings of the proposed classes of creditors to vote on the Syncreon schemes. The meetings of the classes of creditors affected by the Syncreon schemes was held on Sept. 3.

The scheme legislation requires the consent of 75% of creditors by value and 50% by number in each class in order for the vote to be passed by each class. The affected creditors at the convening meetings voted overwhelmingly in favor of the Syncreon schemes.

The second Syncreon schemes hearing was held on Sept. 10. At this hearing Judge Falk considered issues such as fairness and jurisdiction in order to determine whether the Syncreon schemes should be approved. The court's approval is required in order to ensure that the schemes proposals are fair, reasonable and represent a genuine attempt to reach agreement between a company and its creditors.

In order for a scheme to be approved it must compensate the affected creditors for the scheme's alteration of their rights. The Syncreon schemes granted equity in Newco to the parent credit facility and notes creditors as compensation for the reduction in their claims. Judge Falk also considered whether the lock-up payments (and certain other payments under the restructuring support agreement) would have caused creditors to support the restructuring where they would not otherwise have done so without the incentives.

Judge Falk took into account the likely dividend to the classes of creditors in the event that the Syncreon schemes and restructure were not implemented and the likely dividend to the creditors of the group in the event of either enforcement and an accelerated sale or a piece-meal wind down of the group. She found that the creditors of the group whose interests were affected by the Syncreon schemes were materially better off if the schemes are implemented than if they were not.

A scheme applicant must also satisfy the court that the scheme will be effective as regards the company's creditors. The court will not sanction a scheme which is unlikely to achieve its purpose. As such, when considering a scheme application the court will consider issues such as whether the scheme will be recognized in relevant foreign jurisdictions and whether such recognition is necessary for the scheme to achieve its purpose.

In reviewing this the court will usually rely on the evidence of foreign experts. With Syncreon BV being a foreign registered company, Judge Falk was satisfied, after reviewing evidence from legal experts, that the schemes would be recognized in the relevant foreign jurisdictions.

Foreign Recognition of the Syncreon Schemes

On Aug. 8, the Canadian court granted relief to the group's foreign representative and recognized the Syncreon scheme proceedings as foreign nonmain proceedings. The substantive recognition hearing in Canada took place on Sept. 19, at which the recognition was granted. This is considered to be the first time that CCAA recognition has been granted to a scheme.

On Sept. 11, the United States Bankruptcy Court for the District of Delaware, in an uncontested hearing, determined that the filing companies' center of main interest was in England, and granted an order recognizing the Syncreon UK scheme as a foreign main proceeding pursuant to Chapter 15 of the United States Bankruptcy Code and giving full force and effect in the U.S. to the English proceedings.

It is considered likely that the Syncreon schemes will be recognized in the Netherlands, Ireland and Germany as a result of an EU regulation.

The Future Popularity of English Schemes for Foreign Registered Companies

This could be the start of a new trend and a further advancement of the attractiveness of English restructuring proceedings to foreign corporates. Given the current Brexit headwinds it is important to recognize the significance of the approval of the schemes for foreign registered companies by the English court.

As the nature and timing for Britain's exit from the EU is still uncertain, there is no certainty that courts of EU member states will continue to recognize the English court proceedings in the manner in which they do now. This may impact upon the English court's continued ability to approve schemes for companies registered in the EU (as, among other requirements, the English court must be satisfied that the scheme will be effective in all relevant jurisdictions).

As in the Syncreon schemes, which required separate applications in the U.S. and Canada for recognition, it may well be that following Brexit the English court can be satisfied that such recognition can be obtained by individual applications in the relevant EU jurisdictions. If this "effectiveness and recognition" hurdle can be surmounted then it is likely that the English schemes shall continue to be an effective restructuring tool for international groups.

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[1] Dilution of equity in Newco is likely to occur as a result of equity being granted to the lenders and backstop lenders under the RSA.