UK stay on legal proceedings available to debtors without filing insolvency while creditors consider a scheme of arrangement

Schemes of arrangement (“schemes”) have become the restructuring tool of choice for English companies or overseas companies that have English law-governed debts.

However, the use of schemes for non-English companies has generally been limited to cases where the company is able to restructure without the threat of creditors taking individual action. This is because a scheme does not provide an automatic stay unless the company also goes into an insolvency (administration) proceeding. Although sometimes appropriate, an administration may be undesirable for a number of reasons, including that an overseas company would need to move its center of main interests to the UK, the directors would be displaced by an administrator, and there may be additional cost and business disruption.

Recent case law

A recent case has confirmed that, although a scheme carries no automatic stay, a company proposing a scheme may apply for a stay on action by creditors on a case by case basis, provided, among other things, that the scheme is reasonably likely to succeed.

In Bluecrest Mercantile NV v. Vietnam Shipbuilding Industry Group [2013] EWHC 1146 (Comm) the court used its case management jurisdiction under the UK’s Civil Procedure Rules to stay claims brought by certain creditors while the company’s creditors considered a scheme. The court reasoned that because the company was insolvent, the interests of its creditors generally took precedence over the rights of individual creditors. It was the court’s view that it would not therefore be right for dissentient creditors to proceed with their claims without first giving the company’s creditors as a whole the opportunity to vote on the company’s scheme.

The principles

The following principles can be taken from the court’s decision:

1. The company must be insolvent, although need not be in an insolvency proceeding;
2. The scheme must be reasonably advanced, for example in “term sheet” stage, even if definitive documents have not yet been prepared;
3. There must be a real prospect of the scheme being approved by a majority in number holding 75 per cent. in value of each class of scheme creditors, for example a reasonable proportion of creditors should be “locked up” or expressing support;
4. There must be a benefit to creditors generally in conducting the scheme which outweighs the interests of the dissentient creditors in pursuing their claims, for example that the scheme would produce a significantly better return for creditors generally than the company going into a local insolvency process; and
5. There must be some likelihood that the action to be stayed would disrupt the scheme.

**The consequences**

This decision further improves the array of tools available to implement restructuring of English law governed obligations. It confirms that an English scheme can be an effective implementation mechanism for English and overseas companies not only where there is little or no pressure from dissentient claimants, but also where the debtor is being aggressively pursued by one or more creditors. This can in appropriate circumstances be accomplished without combining the scheme with an administration.

**Background - the English law scheme of arrangement**

The English scheme is a flexible and efficient restructuring tool. It has been used by both English and overseas companies to restructure obligations governed by English law. For example, Sidley Austin LLP recently advised GRAND plc, an Irish company, on the use of a scheme to restructure the largest European CMBS transaction by value. Other companies which have used English schemes include those incorporated in BVI, Bulgaria, Canada, Cayman Islands, Dutch Antilles, Germany, Greece, Guernsey, Indonesia, Ireland, Italy, Jersey, Kuwait, Luxembourg, the Netherlands, Russia, Spain, Vietnam and the United States of America.

The process usually takes 6-8 weeks and often does not involve an insolvency proceeding. The scheme is a feature of English company law, and is used frequently by both solvent and insolvent companies. It involves two court hearings, one to convene meetings of creditors, and another to sanction the scheme after the creditors have voted.

Creditors vote as classes and a majority in number comprising 75 per cent in value of each class must approve the scheme. Dissenting classes cannot be crammed down, although classes with no economic interest do not necessarily need to be consulted. Once approved by the relevant majority, sanctioned and effective, it also binds the minority.

A scheme can restructure both secured and unsecured obligations, it can be used among other things to restructure public bonds (such as in Deutsche Annington/ GRAND plc, mentioned above) or syndicated loans (for example in TI Automotive, where Sidley Austin LLP advised the first lien lenders).

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