The New Corporate Restructuring Plan: A Supplier's Perspective

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The Corporate Insolvency and Governance Act 2020 ("CIGA") has introduced a number of new measures designed to bolster the UK's restructuring toolkit. One of these new measures is the restructuring plan ("Plan"), something which Virgin Atlantic has recently successfully implemented to restructure its balance sheet. While great for businesses seeking to restructure, what does it mean for suppliers who might get caught up in it all?

Rebecca Walker, a partner in our Restructuring & Insolvency team, takes a closer look.

What is the new Plan and does it offer anything new?

The Plan is a procedure under the Companies Act 2006 which allows a company to make an arrangement or compromise with its members or creditors, or any class of them. The company must be encountering (or be likely to encounter) financial difficulties that affect its ability to carry on business as a going concern and the purpose of the Plan must be to address these financial difficulties.

When proposing a Plan, the company must group those affected by the Plan into classes. A class is made up of members or creditors having similar rights. To use a simple example, a company might put all of its ordinary shareholders into one class, its secured lenders into a second class and its unsecured creditors into a third class.

To be approved, at least 75% in value of each class must vote in favour of the Plan.

The Plan is similar to other existing restructuring procedures, such as the company voluntary arrangement ("CVA"), which is currently being used by retailers and restaurants such as New Look and Pizza Express. However, unlike a CVA, the Plan can bind secured creditors as well as unsecured creditors. Further, the Plan is the only UK restructuring procedure that provides for the ability of one class of members or creditors to out vote another class.

A Plan can be approved if only one class of members or creditors votes in favour of the Plan (even if all of the other classes vote against it). However, for a Plan to be approved in these circumstances, it must be shown that:

- the class(es) who voted against the Plan would not be worse off under the Plan when compared to the most likely alternative (for example an insolvency process); and

- the class(es) who voted in favour of the Plan would have received a payment or otherwise have a genuine economic interest in the company under the most likely alternative. So this would, for example, prevent shareholders pushing through a restructuring where the most likely alternative would be an insolvency process under which they would be completely out of the money.

The process of one class of members and/or creditors pushing through a restructuring despite other classes of members and/or creditors voting against is known as “cross class cram down”.

If you are a trade supplier, how will you first hear about one of your customers wanting to propose a Plan?

The company kicks off the process of proposing a Plan by making application to Court for permission to convene a meeting of members and/or creditors to vote on the terms of the Plan. This is known as the “convening hearing”. The company will give notice of the convening hearing to those whose rights are going to be affected by the Plan in order to give them a chance to attend the convening hearing.

It is unlikely that you will hear about a proposed Plan until this stage. While it is common for some creditors to be informed in advance, this will usually only occur in relation to creditors that are owed substantial sums of money and whose favourable vote is required in order for the Plan to succeed. In the case of suppliers, there will likely be many suppliers who are owed less significant amounts of money and it would therefore be impractical to secure each and every supplier’s support prior to formally proposing the Plan.

How will you know whether to vote in favour of the Plan?

Prior to being asked to vote on the Plan, the company must send all affected members and creditors an explanatory statement setting out the commercial impact of the Plan. The purpose of this document is to give you all the information you need to make an informed decision on whether to approve the Plan.

How long will you have to make a decision on how to vote?

This can vary depending on the circumstances, and there is no set time period. However, a period of several weeks is customary, as it is recognised that members and creditors need time to consider how to vote and take appropriate advice, although this does need to be balanced against the urgency of the financial difficulties facing the company. With Virgin Atlantic, creditors were given 21 days’ notice of the convening hearing.

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If you do not wish the restructuring to go ahead, what should you do?

Your options will depend on the circumstances, so you should seek expert legal advice as soon as you hear of the proposed Plan.

When does the Plan become effective?

Once the class meetings have been held, the company has to apply to Court again to sanction the Plan. This is known as a "sanction hearing". The Plan becomes effective when the Court makes an order sanctioning the Plan and a copy of the Court order is registered at Companies House.

What happened in Virgin Atlantic's Plan?

Virgin Atlantic divided its creditors into four classes:

1. Its bank lenders. Virgin Atlantic had a $280 million fully drawn secured revolving credit facility. Its Plan proposed that certain security was released and that the terms of the facility were amended and its maturity date extended.

2. Various operating lessor creditors. Virgin Atlantic had 24 aircraft on operating leases with an aggregate liability of c. $1.25 billion. The plan offered various options for dealing with these creditors including rent deferral, rent reduction and bullet repayment, and lease termination.

3. Connected party creditors, who had claims of up to £400 million. The Plan proposed that this debt be converted into shares in Virgin Atlantic's parent company.

4. Trade suppliers, who had aggregate claims of c. £55 million with respect to goods and/or services supplied. The Plan proposed to reduce the debts owed to these creditors by 20% with the balance payable in instalments over two years.

Prior to formally proposing the Plan, Virgin Atlantic had secured the support of its bank lenders, operating lessor creditors and connected party creditors and they had each signed an agreement to support the Plan. While Virgin Atlantic had not sought the written support of its trade suppliers, it had consulted with them by way of a webinar prior to proposing the Plan and had given them an opportunity to ask questions.

By engaging with all affected creditors in advance, Virgin Atlantic knew that the Plan would have a reasonable chance of success. If trade suppliers voted against the Plan, they would likely be crammed down under the "cross class cram down" rules, not least because an 80% recovery on a debt is probably far better than a trade

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supplier could expect to receive as an unsecured creditor in an insolvency. In fact, the trade suppliers voted overwhelmingly in support of the Plan and so it was not necessary to invoke the "cross class cram down" rules.

If your customer proposes a Plan, will you be prevented from exercising your contractual rights such as repossessing goods supplied subject to reservation of title terms or terminating the contract?

CIGA introduced restrictions on the ability of suppliers to terminate contracts or do any other thing on the grounds of insolvency (unless they have the permission of the customer, relevant insolvency office holder or court). These restrictions extend to companies proposing a Plan and are likely to prevent suppliers from both terminating the contract and repossessing their goods on the grounds of insolvency.

Importantly, the restrictions only kick in once the Court has made an order summoning the convening hearing, so you could terminate your contract or repossess goods before the convening hearing taking place.

The restrictions do not prevent the termination of contracts or the taking of any other action unrelated to the insolvency of the customer. So if you have a contractual right to, say, terminate for convenience, then you will still be able to do this.

Is there anything you can do now to protect your position in the event that one of your customers were to propose a Plan in the future?

It is generally accepted that as the country emerges from lock down, we will see an increase in restructurings and insolvencies. The Plan is likely to become a commonly used tool to effect restructurings, although probably only in respect of larger companies as the process itself can be complex and expensive.

It would be worth reviewing your contracts with key customers now to assess what your rights would be if that customer were to propose a Plan (or indeed enter some form of insolvency process) and to consider negotiating amendments into those contracts now. Below is a (non-exhaustive) list of questions you should consider:

- What are your termination rights? Do you have an ability to terminate for convenience or is it tied to insolvency?
- Are you able to vary the payment terms with your customer to require payment up front or payment in instalments?
- Do you have a right to claim interest and costs on top of the debt your customer owes you?
- Do you have a right to set off any sums that you owe to your customer (e.g. by way of rebate) against

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sums that your customer owes to you?

- Is it appropriate for you to ask for other protections such as reservation of title terms, a third party guarantee or a letter of credit?
- If you already have the above protections, are they exercisable pre-insolvency?

If you have any questions in relation to the content of this article or wish to discuss a matter relevant to you, please get in touch with Rebecca Walker on 023 8082 7427 or email online.enquiries@LA-law.com