By Gerald C. Bender, Giorgio Bovenzi and Oscar N. Pinkas[1]

Scheme of Arrangement Confirming Nonconsensual Third-Party Releases Approved in Chapter 15s

Gerald C. Bender
Dentons US LLP
New York

Giorgio Bovenzi
Dentons US LLP
New York

Oscar N. Pinkas
Dentons US LLP
New York

Gerry Bender, Giorgio Bovenzi and Oscar Pinkas are partners in the Restructuring, Insolvency and Bankruptcy Group of Dentons US LLP in New York. Mr. Pinkas is also a 2017 ABI "40 Under 40" honoree.

Third-party releases are a hot-button issue in the U.S., where the circuit courts are split on whether they have the power to grant such releases, when such a grant is appropriate, whether such releases are ever permissible without consent and, in those circuits that permit them, what constitutes such consent.[2] However, as Hon. **Martin Glenn** of the U.S. Bankruptcy Court for the Southern District of New York points out in his recent decision in the *Avanti* case,[3] such handwringing might not be necessary or even relevant in the chapter 15 context. In *Avanti*, Judge Glenn issued a decision explaining why such releases were permissible in a chapter 15 case involving a U.K. scheme of arrangement.

Despite the fact that no objections to recognition of the U.K. scheme of arrangement or enforcement of the releases had been lodged, the court issued a well-reasoned opinion. Indeed, the *Avanti* opinion clearly articulates the rationale and provides helpful comparisons between third-party releases in chapter 11 and chapter 15 cases.

At the time of its U.K. restructuring, Avanti Communications Group plc was a public, U.K.-based satellite services provider with a significantly overleveraged capital structure. Avanti owed (1) approximately $118 million under its super-senior term loan facility (the "term loan facility"), (2) approximately $323 million under its 10 percent/15 percent senior secured notes due in 2021 (the "2021 notes"), and (3) approximately $557 million under its 12 percent/17.5 percent senior secured notes due in 2023 (the "2023 notes").[4]

After experiencing delays related to the manufacture, procurement and launch of two of its satellites, Avanti entered into restructuring negotiations with its significant creditors that ultimately resulted in an agreement to, among other things, equitize the 2023 notes and amend the 2021 notes. Avanti then commenced a proceeding under Part 26 of the Companies Act 2006 before the High Court of Justice of England and Wales (the "U.K. Court") in which it sought to convene a meeting of the holders of the 2023 notes (the only group of creditors affected) to approve a scheme of arrangement embodying its restructuring. The scheme of arrangement provided for the release of guarantees from affiliates of Avanti in order to prevent any dissenting holders from seeking relief outside the scheme of arrangement. It was overwhelmingly approved by holders of more than 98 percent of the 2023 notes.

The U.K. Court also authorized the appointment of a foreign representative to file a chapter 15 case in the U.S. in order to recognize and enforce the scheme of arrangement and releases. The foreign representative sought (1) recognition of the U.K. proceeding as a "foreign main proceeding" under chapter 15; (2) relief afforded to foreign main proceedings under § 1520 of the Bankruptcy Code; (3) an order recognizing, granting comity to, and giving full force and effect in the U.S. to, among other things, the U.K. proceeding and the scheme of arrangement; and (4) an order enjoining parties from taking any action inconsistent with the scheme of arrangement, including certain releases given in favor of certain of the debtor's direct and indirect subsidiaries (the "subsidiary guarantors") that guaranteed the 2023 notes.[5]

In his decision, Judge Glenn pointed out that the analysis applicable to the approval of third-party releases in chapter 15 cases is different from that in chapter 11 cases. In a chapter 15, the focus is on whether the foreign court had proper authority to grant the releases, and thus whether the chapter 15

1 The views expressed in this article do not reflect the views of Dentons or any of its clients.

2 Courts in the Fifth, Ninth, Tenth and District of Columbia Circuits have held that the Bankruptcy Code only allows the bankruptcy court to grant releases against a debtor and prohibits releases of nondebtors or injunctions protecting such nondebtors unless specific consent is provided. The Second, Fourth, Sixth, Seventh and Eleventh Circuits have held that such third-party releases might be given consensually and, in certain circumstances, nonconsensually. *Id.* at 2-3 and cases cited therein. Courts still struggle with the nature of such consent, as well as the extent to which disclosure of such release provisions in a plan is sufficient. More recently, the U.S. District Court for the District of Delaware held that bankruptcy courts have constitutional authority to provide third-party releases in a reorganization plan, even where such releases are nonconsensual. *Opt-Out Lenders v. Millennium Lab Holdings II LLC (In re Millennium Lab Holdings II LLC)*, Civ. No. 17-1461, No. 15-12284 (LSS) (D. Del. Sept. 21, 2018).

3 *Avanti Commc'ns Grp. PLC*, 582 B.R. 603 (Bankr. S.D.N.Y.).

4 Under an intercreditor agreement, the term loan facility ranked above the 2021 and 2023 notes. *Id.* at 5.

5 While the *Avanti* decision is most notable for its analysis of third-party releases arising under chapter 15, the bankruptcy court also dealt with the preliminary issue regarding eligibility to file under § 109 of the Bankruptcy Code. While noting that the applicability of § 109 to a chapter 15 case results from the controversial ruling in *Drawbridge Special Opportunities Fund LP v. Barnet (In re Barnet)*, 737 F.3d 238 247 (2d Cir. 2013), the court concluded that the retainer paid to the New York law firm representing the foreign representative, as well as the fact that the indenture relating to one of Avanti's debt issuances was governed by New York law, each constituted property in the U.S. for purposes of § 109. *Id.* at 9. The decision reflects the case law trend that a retainer held by a U.S. law firm or contract rights under a New York law-governed indenture are sufficient to satisfy the "property in the [U.S.]" eligibility requirement under § 109(a). Revisions to chapter 15 that have been proposed to the U.S. Congress by the National Bankruptcy Conference on Aug. 20, 2018, include a proposal to render § 109(a) not applicable to a case under chapter 15 on the basis that *Barnet* was wrongly decided and that the same *Barnet* decision invited Congress to revisit the drafting of § 109(a).

court should recognize and enforce the foreign court's grant based on principles of comity.[6] Judge Glenn focused his attention on two provisions of chapter 15: Section 1521(a), which authorizes the court to grant "any appropriate relief" to a foreign representative "where necessary to effectuate the purposes of [chapter 15] and to protect the assets of the debtor or the interests of the creditors,"[7] and § 1507(a) and (b), which allows the court to "provide additional assistance to a foreign representative" if, "consistent with principles of comity," such assistance will, among other things, ensure the "just treatment of all holders of claims," "protection of claim holders in the [U.S.] against prejudice" and "distribution of proceeds of the debtor's property substantially in accordance with the order prescribed by this title."[8]

Focusing in particular on the "principles of comity and cooperation with foreign courts" language of § 1507, Judge Glenn noted that "third-party nondebtor releases are common in schemes sanctioned under [U.K.] law, particularly for releases of affiliate Guarantees."[9] He then looked at the extent to which creditors in the U.K. had been given a full and fair opportunity to vote on — and be heard in connection with — the restructuring. He noted that the scheme of arrangement had received 98 percent approval by the one class being affected, and creditors therein had been afforded a right to be heard consistent with U.S. due-process standards. Accordingly, Judge Glenn granted the request for recognition and enforcement of the scheme of arrangement and related sanctions order.

The court distinguished the *Vitro* decision,[10] where the Fifth Circuit affirmed the bankruptcy court's decision in a chapter 15 case not to grant comity to and enforce an order of a Mexican court approving a restructuring that involved the releases of guarantees provided by U.S.-based nondebtor affiliates of the Mexican debtor. As noted by Judge Glenn, in the *Vitro* case, there were very troubling facts and circumstances that led the Fifth Circuit, in an exercise of discretion to refuse to recognize and enforce the Mexican restructuring plan. Most significantly, approval of the hotly contested plan from the one voting class of creditors was only achieved through the counting of votes from "insiders" (*i.e.*, 50 percent of all voting claims were held by intercompany debtholders), and the threshold for approval in Mexico was (at the time) lower (50 percent — a bare majority).[11] In contrast, the court noted that a U.K. scheme of arrangement requires a majority of creditors representing not less than 75 percent in value in each creditor class, and the *Avanti* scheme of arrangement had near-unanimous noninsider support.[12]

Avanti follows in the steps of two earlier chapter 15 decisions by Judge Glenn. In *Sino-Forest*,[13] he granted the recognition and enforcement of third-party releases approved in the debtor's Canadian insolvency proceeding in conjunction with the settlement of securities class-action litigation. In that case, Judge Glenn reiterated the principle that he had previously articulated in his opinion in *Metcalfe*, namely that under chapter 15's comity standard, the court's task is not "to make an independent determination about the propriety of individual acts of a foreign court" but to determine whether the foreign procedures "meet our fundamental standards of fairness."[14]

Sino-Forest dealt with a scenario similar to the one in *Vitro* (and *Avanti*) — the implementation of third-party releases approved by a foreign court — but it was particularly interesting as it was the first chapter 15 ruling to address such a request since *Vitro*. Armed with his deep familiarity with the *Metcalfe* facts, Judge Glenn used the same factors that the *Vitro* court had used to distinguish *Metcalfe*, including the near-unanimous support for the plan, the absence of insider votes, the Canadian court's evaluation of the sensitivities involved with the approval of third-party releases, and the lack of objections to the requested relief, but it reached a conclusion opposite to the one reached in *Vitro*. In this respect, the *Avanti* rationale reflects the deliberate, consistent and analytical approach taken by the U.S. Bankruptcy Court for the Southern District of New York in connection with chapter 15 recognition and the enforcement of third-party releases that have been sanctioned in foreign proceedings.

The granting of the relief requested in *Avanti* — recognition of the scheme of arrangement and enforcement of the releases — seems to have been an easy call. The facts of *Avanti* (98 percent approval, no objecting creditors and draconian results if not approved) favored the relief. Judge Glenn noted that third-party releases under U.K. schemes of arrangement are relatively common, particularly releases of affiliate guarantees of the debt being adjusted by the scheme of arrangement.[15] Accordingly, the court concluded that schemes of arrangement sanctioned under U.K. law that provide for third-party releases should be recognized and enforced under chapter 15 of the Bankruptcy Code.[16] Since the case was brought in the Second Circuit, where third-party releases are not prohibited, the granting of the relief was also not contrary to public policy and thus consistent with principles of comity.

Conclusion

In cross-border insolvency practice, it is always interesting to see how — even after chapter 15 recognition of a foreign proceeding is granted — bankruptcy courts resolve the inherent tensions between different rules and legal systems.

While the approval of a noncontroversial restructuring scheme of arrangement that includes third-party releases from a jurisdiction in which such releases are commonplace, seems consistent with chapter 15 jurisprudence, it will be interesting to see whether other courts in circuits that take a dim view of third-party releases in chapter 11 plans would favor — in a chapter 15 context — the same approach taken in *Avanti*, emphasizing the comity mandate as set forth in chapter 15. It will be equally interesting to see

6 *Id.* at 3.
7 *Id.* (Ex. 10). *See also* 11 U.S.C. § 1521(a).
8 *Id. See also* 11 U.S.C. § 1507(a) and (b).
9 *Id.* at 3.
10 *In re Vitro S.A.B. de C.V.*, 701 F.3d 1031 (5th Cir. 2012).
11 *Id.* at 12. Insider votes are not counted under the Bankruptcy Code. 11 U.S.C. § 1129(a)(10).
12 *Id.*
13 *In re Sino-Forest Corp.*, No. 13-10361 (Bankr. S.D.N.Y. Nov. 25, 2013).
14 *In re Metcalfe & Mansfield Alternative Invest.*, 421 B.R. 685 (Bankr. S.D.N.Y. 2010), distinguishing *In re Vitro S.A.B. de C.V.*, 701 F3d 1031 (5th Cir. 2010). Notably, a portion of the *Sino-Forest* opinion was devoted to distinguishing the *Vitro* decision, and the *Sino-Forest* court declined to apply *Vitro*'s three-step framework for determining the appropriateness of post-recognition relief, focusing instead on the propriety of the relief as "additional assistance" and comity under § 1507.
15 *Avanti* at 12.
16 *Id.* at 13.

continued on page 112

from page 35

how courts deal with future cases from other jurisdictions with facts that are not so tidy, especially those where third-party releases are rare. Nevertheless, by making extensive use of the principles of comity that permeate chapter 15, *Avanti* potentially opens a strategic option for foreign companies that (1) need or desire third-party releases and (2) are considering whether filing a plenary proceeding outside the U.S. with an ancillary chapter 15 case — instead of a plenary chapter 11 case — might offer a higher probability of a successful restructuring. abi