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NEWS

African Minerals Limited: using a scheme to unlock value for all creditors

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Partner **Richard Hornshaw** and counsel **Tom Laidler** from Akin Gump Strauss Hauer & Feld's London litigation team discuss how a Cayman litigation trust and an English scheme were used to get around creditor differences on pursuing significant litigation, in the context of the administration of an iron ore miner in Sierra Leone.

It is not uncommon that insolvency practitioners (IPs) are faced with a situation in which one of the assets within the estate is a litigation claim which, while potentially valuable, will also be expensive to pursue. Third party litigation funding is of course one obvious avenue for the IPs to consider in those circumstances. But there can be challenges where the

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views of all creditors are not aligned, or cannot be ascertained. This article considers the recent use of a Cayman litigation trust vehicle, and an English scheme of arrangement, as an alternative approach to resolving this issue.

Background

Prior to its entry into administration in 2015, African Minerals Limited (AML) was the parent company of a mineral exploration and development group which held significant interests in an iron ore mine and related infrastructure projects in Sierra Leone, West Africa.

In February 2015, Shandong Iron & Steel Group (one of the world's largest steel producers and an existing equity investor in the projects) acquired the rights under a finance facility that was in default and made an immediate demand for repayment. The finance facility had been guaranteed by AML and secured by way of a charge over AML's shares in the Sierra Leone operating companies. In early March that year, Shandong instructed the security agent to commence a security enforcement sale process over the charged shares.

In mid-March 2015, AML and certain other group companies were put into administration. The administrators were immediately concerned that the sale process was not being run in a way which would realise the best price reasonably obtainable for the charged shares. An application to the Hong Kong court to halt the sales process was refused and, accordingly, the sales process continued to its conclusion, resulting in the charged shares being sold to a Shandong group company for a price believed to be equivalent to the amount then outstanding under the finance facility (approximately US$170 million).

The claims, and the challenge for the administrators

At the time of the sale, the administrators were in possession of valuations indicating that the charged shares may be worth substantially more than the price paid by Shandong. Accordingly, the administrators began considering the claims which AML may have for the loss incurred by virtue of the defective sales process. In doing so, it quickly became clear that, leaving

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aside the merits of the claim, there were a number of factors which meant it was likely that any proceedings would be lengthy, complicated and expensive.

AML had a fairly significant amount of cash in its bank account, principally as a result of an unrelated England and Wales Court of Appeal decision in its favour, shortly after the appointment of the administrators *(African Minerals Limited v Renaissance Capital Ltd*). However, it was unclear whether there was sufficient cash to fund the proceedings in their entirety; and there was of course also a risk that, if the claims were unsuccessful, there would be no further dividend for creditors. This gave rise to a divergence of views among creditors as to whether or not the claims should be pursued. Some preferred to take an immediate cash distribution of substantially all of the remaining cash; others wanted to pursue the litigation (potentially with the backing of a litigation funder).

The solution

A number of different structures were considered, including: a public sales process, a company voluntary arrangement (CVA), and third party litigation funding and a transfer of the claim pursuant to the administrators' powers under paragraph 69 of Schedule B1 to the Insolvency Act 1986. However, each of these approaches in isolation raised difficult issues on the facts of the case, including potential tax and other liabilities for the estate, or even the administrators personally.

Accordingly, in conjunction with the major creditors, the administrators designed a structure whereby the claims would be assigned to a litigation trust vehicle (known as a STAR Trust) established in the Cayman Islands. STAR Trusts lend themselves to litigation trusts because, among other things, they are managed by certain nominated "enforcers", rather than the beneficiaries, reducing the scope for costly conflict amongst beneficiaries as to how litigation is to be pursued, and additional beneficiaries can be named with relative ease, assisting with the raising of litigation finance.

This assignment would be accompanied by a scheme of arrangement which would allow the divergent wishes of the creditors to be respected.

The principal features of the scheme were that: (i) a further interim dividend would be paid to creditors, distributing substantially all of the remaining assets in the estate; and (ii) creditors would have the option to direct their dividend to the litigation trust in return for interests in the trust, with the intention that the trust would pursue the claims and distribute any proceeds among electing creditors.

The scheme therefore posed a binary question to creditors: take your share of the available cash, or take the chance of a greater recovery in the future via the litigation trust.

At the creditors' meeting, the scheme was approved by 86% of the creditors by value and, on 27 July 2020, it was duly sanctioned by the English court. The claim has now been assigned to the litigation trust, and those creditors who wished to take the cash have received their distribution. In this way, the structure successfully enabled the administrators to satisfy, to the greatest extent possible, the wishes of all creditors.

The scheme itself raised a number of issues, some of which are related to the covid-19 pandemic, and others of which are points that often need to be considered when structuring schemes, particularly where the company's liabilities include bond debt, held by a trustee on behalf of the bondholders. The remainder of this article briefly summarises certain of those issues.

One class of creditors, fairly represented at the meeting

The court agreed that the fact that creditors would ultimately end up with different forms of consideration was irrelevant given that they all had the same choice and that, accordingly, it was appropriate for there to be a single class of scheme creditor.

As set out above, the statutory thresholds for approving the scheme were met. However, given the low turn-out of creditors at the scheme meeting (less than 7% by number), the court gave particular consideration as to whether the single class of creditors was fairly represented at the scheme meeting.

In holding that the class was properly represented, the judge relied on the following: (i) AML had been in administration for over five years and, bar one proof of debt submitted in 2020, no proof had been submitted since 2017; (ii) the administrators' progress reports had kept creditors updated; (iii) the number of creditors voting was depressed by the fact that none of the bondholders were enfranchised to vote on the scheme (as explained below); (iv) it was public knowledge that well over 75% (by value) of creditors had locked up in favour of the scheme, which may well have dis-incentivised creditors to vote; and (v) and the scheme was unopposed.

Guidance on remote scheme meetings

Given the Covid-19 pandemic, the administrators proposed that the scheme meeting take place via telephone and video. At the convening hearing, after giving it detailed consideration, the judge confirmed it was appropriate for the scheme meeting to take place remotely on the express basis that the evidence at the sanction hearing should demonstrate that *"the* [remote scheme meeting] *technology works sufficiently to enable creditors to hear, to speak, to ask questions and to consult together adequately."*

Bond trustee voting on behalf of bondholders

One of AML's largest creditors was Wilmington Trust (London) Limited, as trustee of US$400 million of convertible bonds issued by AML. Where bonds are held through the clearing systems, underlying beneficial bondholders can be permitted to vote on the basis that they are contingent creditors of the issuer. To avoid double counting, the trustee in such cases usually undertakes not to vote at the scheme meeting (see: *Re Noble Group*). In AML's case, however, following a resolution of AML's bondholders in November 2018, the trustee undertook to vote in favour of the scheme on behalf of all bondholders.

Theoretically, this approach could have led to a fairness issue. However, the trustee pre-emptively addressed this point in its evidence for the sanction hearing, confirming that: (i) there appeared to have been minimal trading in the bonds since the resolution such that the current bondholders were substantially the same as the bondholders that had voted on the resolution;

(ii) it had not been notified of opposition to the scheme from any bondholders; and (iii) over 95% of bondholders who had voted had elected to subscribe for trust interests.

Conclusion

Litigation trust structures are reasonably common in the US, particularly in Chapter 11 bankruptcies. However, they are rare in the UK context.

The structure used here was an elegant solution to the problem of how to reconcile the divergent views amongst creditors as to the approach which the administrators should take to the proposed claim. Clearly, given its cost and complexity, a scheme of arrangement is not going to be a suitable structure for all IPs to adopt but, for the administrators and creditors of AML, the scheme provided an effective and robust mechanism, as well as providing another example of the flexibility of the English court's jurisdiction in relation to schemes. It will be interesting to see the extent to which IPs acting in other insolvencies choose to use this mechanism to resolve similar issues within their own estate.

Case references

African Minerals Limited v Renaissance Capital Ltd [2015] EWCA Civ 448
Re Noble Group Ltd [2018] EWHC 2911 (Ch)

Richard Hornshaw and Tom Laidler have acted for AML's administrators since their appointment.

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