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In this edition of **Restructuring Watch**, we reflect on:

- The first restructuring plan to cram down HMRC.
- Recent government reports on certain UK restructuring processes and learnings from the first six-months of the National Security and Investment Act 2021.
- Government consultations on a crypto special administration regime and prospective additions to the cross-border recognition and insolvency framework.
- A reminder of the recent important milestone in the Galapagos cross-border insolvency battle.

RECENT DEVELOPMENTS

Houst's Restructuring Plan: The First Cram Down of HMRC

The first restructuring plan cramming down HMRC as a secondary preferential creditor has been sanctioned.

On 22 July 2022, the court handed down its judgment sanctioning the plan proposed by Houst Limited (Houst), an SME offering property management services for short-term holiday lets. Six classes of stakeholders voted on the plan, including a (single) secured creditor and HMRC in its capacity as a (secondary) preferential creditor.

The terms of the plan include a reduction in the amount owed to the secured creditor and a requirement for Houst to make monthly contributions to a fund from which payment to HMRC will be made. The valuation evidence provided by the company showed that absent the plan—in the "relevant alternative"—the secured creditor and HMRC would be the only "in-the-money" stakeholders. The relevant alternative was an accelerated marketing process followed by a pre-pack administration sale, which would likely see a recovery of 7p/£ for the secured creditor (from the sale of assets subject to a fixed charge) and 15p/£ for HMRC. Under the plan, it was likely that the secured creditor would recover 27p/£ and HMRC, 20p/£.

HMRC voted against the plan and, in doing so, was the only dissenting class. In sanctioning the plan, the court considered that the two conditions to cross-class cram down were satisfied. HMRC, as the dissenting class, was no worse off under the plan than in the relevant alternative (satisfying "Condition A" or the "no worse off" test) and the secured creditor, which had a genuine economic interest in the company in the event of the relevant alternative, had voted in favour of the plan (satisfying "Condition B"). The court also considered it appropriate in the circumstances to exercise its discretion to sanction the plan. Interestingly, the treatment of stakeholders under the plan departed from the priority that they would have received in the relevant alternative. In considering this point—and sanctioning the plan—the court highlighted that while the treatment of stakeholders in the alternative scenario is a relevant reference point, departure from that priority is not fatal to the success of a plan.

In the face of its inaugural cram down through a restructuring plan, the UK tax authority did not appear before the court to oppose or challenge sanction. The court interpreted HMRC's decision to vote against the plan reflective of a general policy, rather than one based on the specific circumstances of the Houst plan (HMRC had reportedly not sought to engage with the company on the terms of the plan or sought to negotiate an alternative deal). If it is indeed the case that HMRC has, as a matter of policy, opted to refrain from engagement in restructuring processes, they may face future cram downs under restructuring plans. HMRC's position as preferential creditor in a company voluntary arrangement (CVA) should, however, be contrasted. In a CVA, if HMRC is a preferential creditor, it cannot be subject to cram down in respect of amounts owed to it in that capacity, as a CVA cannot compromise preferential (or secured) creditors without their consent.

The Houst plan is an important addition to the learnings on restructuring plans. It also serves as a reminder that restructuring plans can work for smaller companies (the first restructuring plan proposed by an SME in administration, *Amicus Finance*, was sanctioned in August 2021) and reiterates that if a stakeholder wishes to oppose a plan on the basis that the company's valuation evidence misstates recoveries in the relevant alternative, they will be expected to produce their own evidence to, and appear before, the court (a point first made in the judgment sanctioning the second *Smile Telecoms* plan in March 2022).

Reflections on UK Restructuring Processes: Two Insolvency Service Reports

The last few weeks of June were busy for the UK Insolvency Service. On 21 June, an interim report was published on the three permanent reforms introduced by the Corporate Insolvency and Governance Act 2020 (CIGA) in June 2020—the restructuring plan, the moratorium and the restriction on contractual insolvency termination clauses (*ipso facto* clauses) (the CIGA Report)—followed seven days later by a research report on CVAs (the CVA Report).

The CIGA Report was based on feedback received from insolvency practitioners, legal professionals and trade associations. The overall conclusion was that the restructuring plan is a success—generally and with respect to the use of cross-class cram down. However, the process is seen as too costly and time-consuming for SMEs (although the Houst plan, discussed above, is perhaps a step towards allying those concerns). In a similar vein, the costs of challenging plans are seen as excessive. The standalone moratorium process is also considered to be a success, but with its use to date limited to the SME market (primarily because the eligibility criteria broadly operates to exclude larger companies). In this earlier edition of *Restructuring Watch*, we considered the Corbin & King moratoria and the key takeaways from the first judicial consideration of the process earlier this year.

Finally, the restrictions on *ipso facto* clauses are also perceived as positive additions to the UK restructuring toolbox, although it is considered too early to fully assess how this measure will operate (particularly because the temporary pandemic-relation protections—such as the restrictions on winding-up petitions—allowed certain companies to avoid formal insolvency for a period of time).

In light of a number of CVA challenges in recent years (*New Look*, *Regis*, *Debenhams*, to name a few), the Insolvency Service commissioned RSM to conduct the research which underlies the CVA Report. The report broadly finds that, under the 59 CVA proposal documents reviewed, landlords were equitably treated. It is suggested in the report that CVA proposals could be shortened and written with better clarity, plus consultation with landlords enhanced. Otherwise, it is likely to be seen as a (further) blow to landlords who, in their recent challenges, have been largely unsuccessful.

National Security and Investment Act 2021 Clarifications

In January, the National Security and Investment Act 2021 (NSIA) came into force. Focusing on changes in ownership and control of entities and assets in the UK where that change could impact UK national security, NSIA establishes a regime through which the government's ability to scrutinise relevant transactions is enhanced. Our international trade colleagues consider the approach taken to screening in this briefing and we reflected on the implications of the regime for the restructuring world in this prior edition of *Restructuring Watch*.

In late July, the government published market guidance notes, reflecting on the first six months of the NSIA's operation. The following clarifications are relevant to restructurings:

- **Liquidator and receiver appointments**: While the NSIA is clear that the appointment of administrators does not trigger notification or other requirements under the act, the position was less clear with respect to liquidators. In the guidance notes, it is clarified that an appointment of a liquidator or receiver may, depending on the circumstances, trigger the NSIA regime and, in certain cases, require mandatory notification. For example, where the entity in liquidation has shares in a solvent entity, during the insolvency process, and prior to these shares being sold, the liquidator or receiver may have voting rights over these shares. This would be an acquisition of control and, if relevant tests are met – including if the solvent entity carries on activities specified in the notifiable acquisition regulations – could require mandatory notification.
- **Taking share security:** It is common for English law-governed share pledge agreements to provide that the security agent can exercise voting rights in respect of the pledged shares upon enforcement. The guidance notes clarify that simply granting share security does not constitute a notifiable acquisition within the NSIA regime and as a result, will not require mandatory notification. The position, and analysis, will of course differ post-enforcement, and the person/entity that will be acquiring control of an entity carrying on activities specified in the notifiable acquisition regulations would need to make a notification and obtain approval prior to completion.

Consultation: Crypto Special Administration Regime

May saw the government introduce a new consultation entitled "*Managing the failure of systemic digital settlement asset (including stablecoin) firms*".

Seemingly one of the first steps in the government's attempt to put the UK financial services sector at the forefront of crypto asset innovation, the Treasury was seeking views on applying the existing Financial Market Infrastructure Special Administration Regime (and aspects of the Payment and E-Money Special Administration Regime) to systemic digital settlement asset (DSA) firms. A "systemic DSA firm" is considered to be one which provides DSA payment systems or a DSA service provider of systemic importance, so it does not appear that it is intended that this regime will apply to all DSA platforms that fail: just the largest. The consultation closed earlier this week.

Consultation: Cross-Border Recognition and Group Insolvency

In July, the government launched another consultation, this time focusing on the implementation in England and Wales of (i) (part of) the UNCITRAL Model Law on Recognition and Enforcement of Insolvency-Related Judgments (the Judgment Model Law) and (all of) the UNCITRAL Model Law on Enterprise Group Insolvency (the Group Model Law).

The UNCITRAL Model Law on Cross-Border Insolvency (the Original Model Law) was published in 1997 and implemented in England under the Cross-Border Insolvency Regulations 2006. The Original Model Law provides a template for implementing states to, within the parameters of their domestic legal systems, subscribe to a common framework for recognising and enforcing foreign insolvency proceedings.

Since developing the Original Model Law, UNCITRAL has continued to work on insolvency-related initiatives and recently adopted the Judgment Model Law (in 2018) and the Group Model Law (in 2019). The new Model Laws are separate to, but expand on, the framework of the Original Model Law. The UK is reportedly one of the first countries to consult on their implementation.

The main focus of the Judgment Model Law is (as the name suggests) to set out a framework under which foreign insolvency-related judgments can be recognised and enforced in an implementing country. The Insolvency Service does not propose to implement the Judgment Model Law in its entirety in England. Instead, it proposes to give effect in English law to a specific provision which clarifies that, alongside judgments **opening** insolvency proceedings, recognition can be sought in England of judgments that are "*issued on or after the commencement of insolvency proceedings, that arise as a consequence of, or are 'materially associated' with, the proceedings*".

The Group Model Law seeks to provide a framework to enable cross-border cooperation to manage group insolvencies. Key here is the suggestion of a group plan or insolvency solution, which would be developed and coordinated by a "group representative". The Insolvency Service proposes that this law be implemented in full.

The consultation is open until 29 September 2022.

Galapagos: The Long and Winding Road to Winding-Up

In late June, the court made a winding-up order in respect of Galapagos S.A., representing an important milestone in a three-year cross-border insolvency battle involving the English, German and European courts. In this briefing, we reflect on the judgment handed down in connection with the order and the helpful guidance it provides on pre- and post-Brexit recognition of insolvency proceedings.

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