BANKING AND FINANCE

COVID-19 Restructuring Themes and Trends: Nordic Aviation Capital DAC (the "Scheme Company")

High Court Judgment Briefing

September 2020

EXECUTIVE SUMMARY

The scheme of arrangement entered into between the Scheme Company and certain of its creditors (the "**Irish Scheme**") demonstrates the usefulness and flexibility of using an Irish scheme of arrangement with sanction from the Irish High Court (the "**High Court**") as a tool for both Irish and foreign entities with a connection to Ireland to implement quick and efficient financial, covenant and enforcement waivers under US, English and German law governed finance documents, as well as deferrals of principal and interest payments. Together with the considerable use of the Examinership process to reorganise insolvent entities, it also highlights the viability and effectiveness of Ireland as a location for complex international restructurings.

The short timescale to the potential breaches combined with the requirement for access to sufficient liquidity to meet obligations and the high number of creditors necessitated the use of the Irish scheme of arrangement process. This non-insolvency process, which required the approval of a majority in number representing three quarters in value of the Scheme Company's creditors attending and voting at each scheme meeting implemented a series of arrangements to defer the payment of principal and interest and final maturity amounts under the financing, and to provide for fee/charge enhancements, equity investment, INED appointment, capex and cash regulation and collateral provisions in order to stabilise the financial position of the Scheme Company and its subsidiaries (the "**Group**"), where there was anticipated potential breaches, among other things, of certain financial covenants under existing finance arrangements, which are tested quarterly with the possible triggering of acceleration or prepayment events and consequent cross default.

KEY TAKEAWAYS

- ***Covenant waivers and payment deferrals*** *(where breach and cross default was anticipated in the short term with large number of creditors) were implemented by the Irish Scheme.*
- ***A non-insolvency[1], court sanctioned process****, namely the Irish Scheme, used to effect the appropriate waivers and deferrals.*
- ***Supplements Examinership, the existing go-to Irish restructuring process****, which is an insolvency procedure with a lower creditor approval threshold for court sanctioned cramdown.*
- ***The Scheme Company was a common guarantor and single point of entry*** *for purposes of the Irish Scheme across the appropriate financings of the Group which included not only the Scheme Creditor claims against the Scheme Company but also against all companies within the Group who are debtors under the facilities the subject of the Scheme and for certain finance leases (collectively "**Schemed Claims**").*
- ***Class composition*** *– Two classes of Scheme Creditors - secured and unsecured.*
- ***Approval Threshold*** *– the approval threshold for the Irish Scheme is a simple majority in number representing 75% in value of each class of creditors attending and voting at each scheme meeting.*
- ***Non Irish law debt schemed*** *- the Irish Scheme was used to implement waivers and deferrals of English, US and German law governed debt.*
- ***Ricochet Claims*** *- the Irish Scheme included debt owed by both the Scheme Company and other Group companies to third parties (contingent & contribution claims) within the Schemed Claims. Principle of sufficient nexus endorsed by the High Court.*
- ***Cross border recognition*** *– US (Chapter 15), England and Wales, Germany, Denmark, Malta (Brussels Recast Regulation ("**BRR**")[2]), Singapore, Japan, Cayman. With regard to the English law governed debt, the English common law principle known as "the rule in Gibbs," which prevents debt obligations governed by English law being discharged by foreign proceedings without consent, did not impact recognition.*
- ***Capetown Convention*** *(the "**CTC**") – high threshold of Scheme Creditor approval, High Court therefore deemed it unnecessary to determine whether Irish Scheme constitutes an "Insolvency Procedure" under Alternative A of the CTC.*
- ***No moratorium*** *– while the High Court has jurisdiction, on application, to stay or restrain all proceedings for such period as the courts sees fit, no such order was sought in this case.*

BACKGROUND

The Scheme, together with a series of bilateral arrangements, was implemented using the Scheme Company as a common guarantor and single point of entry across the appropriate financings of the Group. This innovative approach allowed for the Irish Scheme to be implemented in respect of approximately 90 separate debt facilities, which included a wide range of financing arrangements that were governed by a mixture of New York, English and German law. Following the sanction of the Irish Scheme and in order to ensure the valid implementation of the Irish Scheme, NAC has sought recognition of the Scheme under Chapter 15 of the US Bankruptcy Code. With regard to the English law governed debt, the Scheme represents a significant departure from the long-standing English common law principle known as "the rule in ***Gibbs***," which prevents debt obligations governed by English law being discharged by foreign restructuring proceedings without consent.

KEY ISSUES CONSIDERED

Jurisdiction – Irish Courts

The Irish Scheme process applies in the case of a "compromise or arrangement" which is proposed between a "company" and its creditors or a class of them or its members or a class of them. A "company" for these purposes is any company that is liable to be wound up under the Companies Act 2014 and therefore includes both Irish companies, and those deemed to have sufficient connection to Ireland.

The High Court determined that the Scheme Company is a company to which this process applies based off the fact pattern regarding the Irish nexus (see above). Further the High Court was satisfied it had jurisdiction to consider and, if appropriate, to sanction a proposed Irish Scheme.

Ricochet Claims included as Schemed Claims

A deed of indemnity and contribution (the "**Deed**") was entered into by the Scheme Company by deed poll to create an indemnity claim and contribution claim against the Scheme Company by third party lenders who were considered as Scheme Creditors. This was relevant, among other situations, for the finance lease financing structures and JOLCO finance lease structures ("**Finance Leases**") the Group had entered which involve an special purpose company outside the Group as borrower and lessor, and in the case of JOLCO structures included Japanese tax investors to whom part of the finance lease rentals are paid by the Group as lessee. Through the Deed, the lessor and the lender to the lessor received a direct right of contribution against the Scheme Company. The High Court in considering this dimension accepted evidence that, the Scheme Company in entering the Deed was not taking on any additional liability or was not taking on one which it did not have the ability to mitigate. The court referenced authority where similar arrangements were entered.[3] In so doing the High Court held it did not regard the Deed as presenting any bar, jurisdictional or other, to the court sanctioning the Irish Scheme. Further the High Court accepted that it was a reasonable and commercial arrangement for the Scheme Company to have entered and that it had reasonable commercial objectives both of which enhanced the Irish Scheme being sanctioned and recognised in the US.

IRISH NEXUS & JURISDICTION

- *The Group operations substantially run from Ireland with 65 active Irish incorporated subsidiaries.*
- *The Scheme Company is an Irish incorporated limited liability company whilst half of the board of directors of the Scheme Company are Irish nationals.*
- *Citibank Europe plc, a secured creditor holding a Scheme Claim of USD100M, is Irish incorporated.*
- *CEO appointed as foreign representative in any proceedings under Chapter 15 confirmed by the High Court.*
- *Certificate granted under Brussels Recast Regulation certifying the court had jurisdiction to hear and determine the Scheme Company's application pursuant to Art 1(1),4&8(1) of the Regulation.*

KEY FACTS (FROM THE JUDGMENT)

By numbers

- *75 lessees in 50 countries, 65 of whom had requested deferrals on lease payments*
- *23-34% of billed payments for April – June 2020 period paid*
- *423 leased aircraft regional aircraft, ATR turbo-props, Embraer regional jets and Bombardier aircraft*
- *138 subsidiaries in debtor group, 65 of which are Irish incorporated*
- *90 separate finance facilities*
- *85 different lenders*
- *USD5.923bn outstanding under facilities the subject of the Irish Scheme*
- *USD3.697bn outstanding to unsecured creditors*
- *USD2.226bn outstanding to secured creditors*
- *Approval at scheme meetings:*
  - *100% of those present and voting being 98% in value of total relevant unsecured debt*
  - *100% of those present and voting being 91% in value of total relevant secured debt*
- *Recognition in 8 countries, 3 continents North America, Europe and Asia*

Ancillary releases

The Irish Scheme included a waiver and deferral, binding not only on the Scheme Creditors as against the Scheme Company but also as against all NAC Group companies who are debtors under the relevant facilities and in relation to the Finance Leases as against the Finance Lessors and the JOLCO Lessors. The High Court considered this did not undermine the status of the Irish Scheme as a "compromise or arrangement".[4] The High Court noted that the releases in the cases cited were different to the present case, but indicated that there was no real difference in principle. The Judge indicated that the words "scheme or arrangement" are to be considered liberally and in a flexible manner. The High Court referred to a case of the Singaporean courts[5] quoting that "provided there is a sufficient nexus between a release and the relationship between the creditor and the scheme company, the Scheme can validly incorporate the release". On the limits of such a release the High Court cited with approval ***Opes***[6] and also ***Pathfinder***[7] where an Irish Scheme sought to compromise a debt between the creditor and a third party. The High Court rejected the requirement for a necessity test such that the release needed to be necessary for the compromise of the liabilities between the guarantor and its creditors. The High Court found no good reason to draw a distinction between a primary and secondary obligation in the context of a guarantee for the purpose of determining jurisdiction. The High Court endorsed and applied the Singaporean courts[8] observations and conclusions to releases in the Irish Scheme. Finally the High Court noted the recent Lecta Paper decision in UK[9] where reference was made to the necessary test but the High Court preferred to adopt the sufficient nexus test, noting in any event either test was satisfied in the context of the Irish Scheme.

Test to Sanction Scheme of Arrangement

The well-established test used by English and Irish courts was applied by the High Court in deciding whether to sanction

the Irish Scheme. In particular, the High Court noted that the judgement in the recent case of ***Re Ballantyne***[10] is the most relevant judgement in the case of schemes of arrangement of insolvent companies. The High Court was satisfied that the test set out in ***Colonia***[11] applied and involved the following five requirements, as well as being satisfied that the Scheme is not ultra vires:

1. **Sufficient steps to identify and notify interested parties**;
2. **Statutory requirements and directions** of the High Court have been complied with;
3. **Class of creditors has been properly constituted** – The High Court referenced the legal principles considered and applied the ***Allergan***[12], ***Xtrackers***[13] and ***Fundlogic***[14] cases. The key points being as follows:
   a. The meaning of the term "class" must be such as to prevent it resulting in confiscation and injustice and must be confined to "persons whose rights are not so dissimilar as to make it impossible for them to consult together with a view to their common interest"[15].
   b. The High Court also cited and agreed that it is a matter of judgement on the facts in each particular case and that the two stage test focused firstly on the rights of creditors and whether there is a difference both in absence of the Scheme and any new rights they get under the Scheme. In the second stage is focussed on whether in the court's assessment looking at the two groups in the round (and not having regarding to individual and special interest) the differences in their rights and their treatment under the scheme are such as to make it impossible for them to consult together with a view to their common interest.[16]
   c. This needs to be balanced with the risk of creating a new minority class with an effective veto right. The test should not be exercised as an oppression of the minority.
   d. The court in assessing class constitution the court considers if there is more that unites than divides in terms of the scheme at their proposed meeting.
   e. Finally a broad approach is to be taken and the differences may be material without leading to separate classes.
   f. The appropriate comparator is the treatment on a winding up in the case of an insolvent company i.e. what is the alternative if the scheme does not proceed. It was noted the Scheme Company in this case was insolvent so winding up is the appropriate comparator;
4. **No improper coercion of creditors concerned**; and
5. **An intelligent and honest person**, being a member of the class concerned, acting in his interest might reasonably approve of.

Recognition

The High Court considered the opinions provided and formed the view that the Irish Scheme was likely to have a substantial effect and was likely to be recognised in each of those jurisdictions. The High Court noted that the Irish Scheme has now been recognised under Chapter 15 of the US Bankruptcy Code.

The High Court decided that it had jurisdiction to hear and determine the Irish Scheme under BRR which provided for the recognition of the sanction order across participating members states of the EU and decided as follows:

1. The application for court sanction in respect of the Irish Scheme concerning an insolvent company falls within the BRR. In particular it is a "civil and commercial" matter for purposes of the Brussels Recast Regulation and not excluded expressly[17], and that it is not an insolvency proceeding under the Recast Insolvency Regulation; and
2. It had jurisdiction to sanction the Irish Scheme under the BRR where some of the Scheme Creditors are domiciled in other member states of EU by adopting the usual practice of the English courts of assuming (without deciding) that BRR applies and that Scheme Creditors are "defendants" who are being "sued" by the Scheme Company (noting the High Court believed in this case the assumptions were correct). The question is based off the assumption if jurisdiction can be found and the High Court could on the basis that one or more of the Scheme Creditors were domiciled in Ireland. Some UK cases look also to the number and size of such creditors and in others one is sufficient. The High Court preferred the latter view but noted in any event the creditor is not immaterial, namely Irish domiciled Citibank Ireland Limited as a secured creditor owed USD100M and the High Court was satisfied it was expedient to hear and determiner the application to sanction insofar as it applied to all EU domiciled Scheme Creditors.

Capetown Convention (the "CTC")

The Company produced expert evidence that the CTC and the Aircraft Protocol[18] do not apply to Irish schemes of arrangement and submitted that the Irish Scheme did not fall within the definition of "insolvency proceedings" for the CTC and "insolvency-related event" for the Aircraft Protocol. In the event that the Capetown Convention and the Aircraft Protocol had applied to the Irish Scheme, fundamental difficulties may have arisen as regards court sanction for the Irish Scheme. Ultimately, the High Court took the view that it was unnecessary to embark on a consideration of the potential issues under the CTC and the Aircraft Protocol in circumstances where none of the Scheme Creditors, and in particular none of the secured Scheme Creditors, were opposing the Irish Scheme or relying on their potential rights under the CTC or the Aircraft Protocol. Rather, there was overwhelming support for the Irish Scheme by the secured creditors who attended the Irish Scheme meetings. The High Court noted that a small number of secured Scheme Creditors (and small in value) did not vote and those creditors had been provided with extensive information on the Irish Scheme and had ample opportunity to participate in scheme meetings but did not, nor did they appear at the sanction hearing to oppose the sanctioning of the Irish Scheme. Those who did vote in favour did not oppose sanction and in these circumstances, the High Court did not make a determination on the applicability of the CTC.

CONCLUSION

The Irish Scheme demonstrates the usefulness and flexibility of an Irish scheme of arrangement (which largely mirrors the corresponding legislation in England and Australia) as a cross border tool for both Irish and foreign entities with a connection to Ireland to put in place creditor compromises/arrangements, with foreign recognition including in the US. Together with the considerable use of the Examinership process to reorganise insolvent entities, it also highlights the viability and effectiveness of Ireland as a location for complex cross-border restructurings.

The speed with which complex schemes of this nature can be completed in Ireland was evidenced in this instance, with the Irish Scheme coming to fruition in approximately 3 months.

COVID-19 Restructuring Themes and Trends: Nordic Aviation Capital DAC (the "Scheme Company") High Court Judgment Briefing

KEY CONTACTS

Kathleen Garrett led the Arthur Cox team advising creditors on the Nordic Aviation Capital Irish Scheme supported by Elizabeth Bothwell, Michael Coyle, Ryan Ferry, Ruth Lillis and Patrick Munnelly.

Kathleen Garrett
Partner
+353 1 920 1174
kathleen.garrett@arthurcox.com

Elizabeth Bothwell
Partner
+353 1 920 1670
elizabeth.bothwell@arthurcox.com

Michael Coyle
Partner
+353 1 920 1061
michael.coyle@arthurcox.com

Ryan Ferry
Partner
+353 1 920 1143
ryan.ferry@arthurcox.com

Ruth Lillis
Associate
+353 1 920 1244
ruth.lillis@arthurcox.com

Patrick Munnelly
Associate
+353 1 920 1367
patrick.munnelly@arthurcox.com

ENDNOTES

1 It is not an insolvency proceeding under *Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings* ("**Recast Insolvency Regulation**")

2 Regulation (EU) No 1215/2012 of the European Parliament and of the Council of 12 December 2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters

3 *Re A. I. Scheme Limited [2015] EWHC 1233 (Ch), Re Codere Finance (UK) Ltd [2015] EWHC 3778 (Ch)* and *Re Lecta Paper UK Ltd [2020] EWHC 382 (Ch).*

4 *Re Ballantyne Re: plc [2019] IEHC 407 and Re Opes Prime Stockbroking Ltd [2009] FCA 813 and the judgment of the Full Court of the Federal Court of Australia on appeal in the same case [2009] FCAFC 125* cited to support his view

5 Pathfinder Strategic Credit LP v. Empire Capital Resources PTE Ltd. [2019] SGCA 29

6 *Re Opes Prime Stockbroking Ltd [2009] FCA 813 and the judgment of the Full Court of the Federal Court of Australia on appeal in the same case [2009] FCAFC 125*

7 *Pathfinder Strategic Credit LP v. Empire Capital Resources PTE Ltd. [2019] SGCA 29*

8 *Pathfinder Strategic Credit LP v. Empire Capital Resources PTE Ltd. [2019] SGCA 29*

9 *Re Lecta Paper UK Ltd [2020] EWHC 382 (Ch)*

10 *Re Ballantyne Re: plc [2019] IEHC 407*

11 *Re Colonia Insurance (Ireland) Ltd [2005] 1 IR 497*

12 In *Re Allergan PLC [2020] IEHC 214*

13 In *Re Xtrackers (IE) public limited Company [2020] IEHC 330*

14 *FundLogic Alternatives PLC [2020] IEHC 428*

15 *Sovereign Life Assurance Company v Dodd [1892] 1 QB 405*

16 with Hillyard in *Re Stronghold Insurance Company Limited [2018] EWHC 2909 (Ch)*

17 *Re Rodenstock GmbH [2012] BCC 459* (regarding solvent schemes) and *Re Magyar Telecom BV [2014] BCC 448* (regarding insolvent schemes) cited

18 *Cape Town Convention and its accompanying Aircraft Protocol have force of law in Ireland pursuant to s. 4(1) of the International Interests in Mobile Equipment (Cape Town Convention) Act, 2005)*