Neutral Citation Number: [2020] EWHC 2860 (Ch)

Case No: CR-2020-003942

IN THE HIGH COURT OF JUSTICE
BUSINESS AND PROPERTY COURTS OF ENGLAND & WALES
INSOLVENCY AND COMPANIES LIST (ChD)

Rolls Building,
Fetter Lane,
London, EC4A 1NL

Date: Wednesday 28 October 2020

Before :

MR JUSTICE SNOWDEN

- -

Between :

IN THE MATTER OF SUNBIRD BUSINESS SERVICES LIMITED

AND IN THE MATTER OF PART 26 OF THE COMPANIES ACT 2006

- -

Andrew Thornton QC (instructed by **CMS Cameron McKenna Nabarro Olswang LLP**) for the **Company**
Henry Phillips and **Lauren Kreamer** (instructed by **Shoosmiths LLP**) for the **Opposing Creditors**

Hearing date: 19 October 2020

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Approved Judgment

COVID-19: This judgment was handed down remotely by circulation to the parties' representatives by email. It will also be released for publication on BAILII and other websites. The date and time for hand-down is deemed to be 10.00 a.m. on 28 October 2020.

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MR JUSTICE SNOWDEN

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Introduction

1. This is a renewed application by Sunbird Business Services Limited (the "Company") seeking an order convening a single meeting of its financial (non-trade) creditors (the "Scheme Creditors") for the purposes of considering and, if thought fit, approving, a proposed scheme of arrangement (the "New Scheme") between the Company and the Scheme Creditors pursuant to Part 26 of the Companies Act 2006. The Company also seeks directions as to how the court meeting should be convened.

2. I refer to this matter as "the New Scheme" because on 18 September 2020 I dismissed the Company's application for sanction of a scheme in near identical terms (the "Original Scheme"). My reasons for doing so were set out in a written judgment: [2020] EWHC 2493 (Ch) (the "Judgment"). Unless otherwise indicated, I shall use the same abbreviations herein as in the Judgment.

3. As was the case with the Original Scheme, the New Scheme provides for a debt to equity conversion of the debts of the Scheme Creditors (amounting to about US$15.9 million plus accrued interest) into A1 Ordinary Shares in the Company at a conversion rate of one A1 Ordinary Share for each US$0.33 of debt (the "Debt to Equity Conversion").

4. The Debt to Equity Conversion under the Scheme would not provide the necessary working capital for the continued operations of the Company's group of subsidiaries. Accordingly, as was the case with the Original Scheme, conditional upon the New Scheme becoming effective, the Company proposes to raise working capital for the group by a fully underwritten rights issue of further A1 Ordinary Shares in the Company (the "Rights Issue"). The Rights Issue will apply to all of the Company's existing shareholders, including the Scheme Creditors in respect of their converted debt, and will raise a further US$3 million at a subscription price of US$0.20 for each new A1 Ordinary Share.

5. In the Judgment I held that the information provided by the Company to the Scheme Creditors in relation to the Original Scheme was inaccurate, incomplete and, in certain respects, misleading. I also criticised the manner in which the Company had approached the scheme process. It had not, for example, provided Scheme Creditors with a letter complying with the Practice Statement (Companies: Schemes of Arrangement) [2002] 1 WLR 1345; and had engaged individually and informally to enter into "lock-up" agreements with those creditors who it thought would be supportive of its proposals, whilst seeking to keep creditors who were opposed to the Original Scheme at arm's length and in the dark about the convening hearing.

6. In putting forward a renewed application in respect of the New Scheme, the Company contends that it has sought to rectify the defects that I identified in the Judgment. So, for example, I have been told that it has released Scheme Creditors who had previously entered into lock-up agreements in relation to the Original Scheme from any obligations in that regard, and it sent a letter to the Scheme Creditors in accordance with the new Practice Statement (Companies: Schemes of Arrangement under Part 26 and Part 26A of the Companies Act 2006) (the "Practice Statement") by email on 5 October 2020.

7. Further, the draft scheme document and explanatory statement (the "Scheme Document") which was produced by the Company shortly prior to the convening hearing on 19 October 2020, has been significantly revised. It now includes, in particular, an analysis of the estimated returns to Scheme Creditors if there were to be a formal insolvency of the Company and each of its subsidiary companies (the "Insolvency Analysis"), and detail in relation to the Rights Issue. The Scheme Document also includes a report which purports to relate to the underlying methodology and justification for the decision of the board of the Company in setting the conversion ratio for the Debt to Equity Conversion and the pricing of the Rights Issue (the "Valuation Report").

8. According to the Scheme Document, the Insolvency Analysis and Valuation Report have been provided for the information and benefit of the board by two insolvency practitioners and the corporate finance arm of James Cowper Kreston LLP ("JCK"). It is, however, stated that the Insolvency Analysis has been prepared primarily on the basis of information provided by the management of the Company, and that JCK has not sought to verify the reliability of that information (except by reference to certain information at Companies House). JCK also states that it assumes no responsibility to any other party for either document.

The Issues

9. The Original Scheme was opposed by a group of creditors to which I referred in the Judgment as the "Opposing Creditors". The same creditors appeared by counsel at this convening hearing. At this stage they have not indicated their position on the merits of the New Scheme, but for ease of reference I shall continue to refer to them as the Opposing Creditors.

10. The Opposing Creditors have raised three points concerning the convening order sought by the Company.

11. First, they raise a question of class composition for the purposes of voting at the court meeting(s). They contend that one of the other Scheme Creditors, 21st Century Group Holdings Limited ("21st Century") should not be included in the same class as all other Scheme Creditors but should constitute a separate class on its own. That contention arises from the fact that in addition to being a Scheme Creditor owed about US$1.75 million plus interest by the Company (about 11% of the total New Scheme debt), 21st Century is owed a debt of US$890,000 (US$750,000 principal plus interest of US$140,000) by the Company's wholly owned subsidiary, Sunbird Business Services Africa Limited ("SBSAL"). SBSAL is a holding company which sits in the group structure immediately below the Company and owns the shares in all of the group's operating subsidiaries, together with some inter-company debts.

12. The Company has entered into a separate consensual agreement with 21st Century (the "Deed of Novation") under which, conditional upon the New Scheme being sanctioned, the debt owed by SBSAL to 21st Century will be novated and assumed by the Company and converted into new A1 Ordinary Shares in the Company at the same conversion rate as offered to Scheme Creditors under the New Scheme. 21st Century will then also be entitled to participate in the Rights Issue in respect of those new shares *pari passu* with all other shareholders in the Company (including the Scheme Creditors).

13. The Opposing Creditors contend that the effect of the Deed of Novation is that, pursuant to the wider restructuring, 21st Century is going to be given valuable additional rights by the Company that are not being given to other Scheme Creditors. They have calculated that under the New Scheme, 21st Century will receive 708,929 A1 Ordinary Shares (if accrued interest to 19 October 2020 is included) in return for a discharge of its Scheme Claim. This is in line with the deal offered to other Scheme Creditors. In addition, the Opposing Creditors contend that 21st Century will have a near-worthless loan against a different entity treated as a liability of the Company and will thereby qualify to receive a further 298,051 A1 Ordinary Shares (if accrued interest to 12 June 2020 is included), which will themselves carry a further right to subscribe under the Rights Issue for a pro-rated entitlement to A1 and A2 Ordinary Shares in the Company.

14. Although this arrangement brought about by the Deed of Novation is outside the New Scheme and therefore does not serve to increase the votes which 21st Century will be entitled to cast at the court meeting to consider the New Scheme, the Opposing Creditors contend that these are valuable additional rights offered to 21st Century under the broader restructuring of which the New Scheme forms the central part, they are collateral to and conditional upon the New Scheme being sanctioned, and they are not available to other Scheme Creditors. The Opposing Creditors contend that the conferring of such rights means that 21st Century is in effect being offered a materially different and more advantageous deal than the other Scheme Creditors and hence should not be permitted to form part of the same class when voting on the New Scheme.

15. Secondly, the Opposing Creditors raise a number of concerns about the form and content of the Scheme Document. In particular, they contend that because the Insolvency Analysis has been provided by JCK on the basis that JCK assumes no responsibility to any party other than the board of the Company, it cannot properly form the basis for any class analysis by the Court (referring to House of Fraser (Funding) Limited [2018] EWHC 1906 (Ch) at [28]-[33]).

16. The Opposing Creditors also criticise the manner in which both the Insolvency Analysis and Valuation Report are presented to Scheme Creditors in the document. The Opposing Creditors submit that, especially when considered against the background of the scheme document for the Original Scheme which expressly stated that the board's decisions were supported by a (then unidentified) independent review, the latest Scheme Document does not make sufficiently clear (i) that Scheme Creditors cannot rely upon the Valuation Report in assessing the merits of the New Scheme, (ii) that in certain material respects JCK adopted a different methodology to that of the board, and (iii) that if JCK's approach had been followed by the board, a different result would have been arrived at in terms of the ratio for the Debt to Equity Conversion. The Opposing Creditors also criticised the lack of transparency in the Scheme Document as to whether, and if so, to what extent, the board had exercised subjective judgment in favouring the existing shareholders of the Company when deciding upon the subscription price for the Rights Issue.

17. Thirdly, the Opposing Creditors contend that at least 28 days ought to be allowed between the circulation of the Scheme Document and the court meeting to consider the New Scheme, rather than the 14 days proposed by the Company.

Class composition

18. The basic legal principles relevant to class constitution under Part 26 were not in dispute between the parties and are well-known. I summarised them in Re Noble Group Limited (convening) [2018] EWHC 2911 (Ch) at [82]-[90].

19. In short, the question of class constitution is primarily answered by reference to an analysis of creditors' rights rather than their individual interests. It requires a comparison of the existing rights of the creditors which are to be released or varied under the scheme, and the new rights to which creditors will become entitled under the scheme. The test is then whether any differences in such existing and new rights of groups of creditors make it impossible for them to consult together with a view to their common interest as creditors. See in particular Sovereign Life Assurance Co v Dodd [1892] 2 QB 573 per Bowen LJ at page 583, Re Hawk Insurance Co Limited [2001] 2 BCLC 48 ("Hawk") per Chadwick LJ at [30], and Re UDL Holding Ltd [2002] 1 HKC 172 (HKCFA) per Lord Millett NPJ at page 179B.

20. Under Part 26 the courts have emphasised that the mere fact that there are differences, or even material differences, between the rights of creditors does not mean that they must be placed in separate classes for the purposes of considering a scheme. Whether any such differences in existing and new rights make it impossible for creditors to consult together with a view to their common interest requires an evaluation by the court of the economic and business impact of the proposals.

21. It does not follow, however, that simply because a scheme company is insolvent and seeking to restructure to avoid liquidation, that all creditors should simply be placed into a single class on the basis of an argument that the scheme will provide a better economic outcome for everyone than the financial Armageddon of a liquidation. As Hildyard J pithily remarked in the second APCOA case, Re APCOA Parking Holdings GmbH (No.2) [2015] Bus LR 374 at [117],

> "the risk of imminent insolvency is not to be used as a solvent for all class differences."

22. By the same token, many judges have sounded warnings that the court should not be overzealous in identifying differences for fear of creating too many small classes carrying an inappropriate right of veto; and have reiterated that an important safeguard against minority oppression is that the court is not bound by the decision of the class meeting, but retains a discretion to refuse to sanction the scheme: see e.g. Hawk at [33], Re BTR plc [2000] 1 BCLC 740 at 747, and Re Telewest Communications plc [2005] 1 BCLC 752 at [37].

23. Finally, and relevantly for the instant case, modern authorities have emphasised that, in assessing how creditor classes should be constituted for the purposes of a scheme, the Court should not adopt a narrow approach and look at a scheme in isolation. The scheme should be looked at in the context of the restructuring as a whole, including, in particular, any rights conferred in other agreements that are provided for under the terms of the scheme, or which are conditional upon it: see e.g. per David Richards J in Re Telewest Communications plc [2004] BCC 342 at paragraph [54]; my own observations to that effect in Re Baltic Exchange Ltd [2016] EWHC 3391 at [17],

citing Re Stemcor Trade Finance Ltd [2016] BCC 194 at [17]-[18]; and the recent discussion of this approach by Falk J in Re Codere Finance 2 (UK) Limited [2020] EWHC 2441 (Ch) at [49] et seq..

24. Applying these principles to the facts of the instant case, it seems to me self-evident, first, that the New Scheme and Rights Issue, which are legally and commercially inter-dependent, must be taken together for the purpose of applying the class test. It is also necessary to take into account the existing rights which 21st Century has against SBSAL and the conversion of those rights into shares in the Company which is envisaged by the Deed of Novation. That agreement is plainly part of the overall restructuring and is legally and commercially conditional upon the New Scheme becoming effective.

25. In that regard, I accept the submissions of Mr. Phillips that there is a material difference between the treatment of the rights of 21st Century and the treatment of the rights of the other Scheme Creditors. In addition to the conversion of the debt which it is owed by the Company into shares in the Company, 21st Century stands to receive an extra tranche of shares in the Company in exchange for its (different) rights against SBSAL. Although Mr. Thornton QC initially sought to persuade me that there was no real difference between the rights of a creditor in respect of debts owed by the Company and those in respect of the debts owed by SBSAL, the analysis of rights at the first stage of the class test must be carried out in accordance with legal principle and respecting separate corporate personalities.

26. The key issue, however, is whether that difference in rights makes it impossible for 21st Century to consult together with the other Scheme Creditors with a view to their "common interest" in the New Scheme. At this stage of the analysis it is important to have regard to the commercial factors relevant to the decision facing the Scheme Creditors and the effect on that commercial evaluation of the additional deal which applies solely to 21st Century.

27. In this regard, Mr. Phillips pointed out that on the Company's own case, based upon the estimated outcome statements in the Insolvency Analysis, SBSAL's only assets were its shares in, and loans to, the operating companies, which would realise nothing in an insolvency once the costs of the liquidation exercise were taken into account. Thus the unsecured creditors of SBSAL stood to receive no distribution at all in a winding-up of SBSAL. Mr. Phillips therefore sought to characterise the Deed of Novation as giving 21st Century an extra tranche of shares in the Company in exchange for the surrender of a worthless claim against SBSAL; and he pointed out that those extra shares would serve to dilute the shareholdings offered to the other Scheme Creditors in exchange for their debt under the new Scheme. The result, Mr. Phillips submitted, was that the commercial interests of 21st Century and the other Scheme Creditors were not aligned, but were in conflict.

28. Mr. Thornton QC had an answer to that submission. He pointed out that the potential value of the A1 Ordinary Shares to be issued to the Scheme Creditors under the New Scheme essentially depends upon the Company being able to derive value from the continuation of the business of the group which is conducted by the operating subsidiaries. This continuation depends upon the ability of the Company to lend the working capital to be provided by the Rights Issue directly or indirectly down to the

operating subsidiaries, and for the Company then to benefit from dividends declared by those operating companies, or from a sale of their shares in due course.

29. But, submitted Mr. Thornton QC, since SBSAL sits in the group structure between the Company and the operating subsidiaries, this underlying commercial rationale for the restructuring would be frustrated if 21st Century were to press for full repayment of its US$890,000 debt from SBSAL, or seek to wind up SBSAL which has no assets with which to pay that debt. In effect, submitted Mr. Thornton QC, the structure of the group and its debts gives 21st Century the commercial leverage to undermine the restructuring by seeking to divert a substantial proportion of the proceeds of the Rights Issue to itself in full repayment of its debt, by threating to wind up SBSAL and thereby sever the link between the Company and its operating subsidiaries.

30. Mr. Thornton QC therefore disputed Mr. Phillips' contention that the arrangement under the Deed of Novation amounted to 21st Century seeking an additional benefit to the detriment of other Scheme Creditors. Rather, he submitted, 21st Century was agreeing to assist the restructuring process by giving up valuable commercial leverage resulting from its right to seek full repayment of its debt by SBSAL after the New Scheme and Rights Issue had become effective. Mr. Thornton QC characterised this as 21st Century "seeking to stand closer to the Scheme Creditors rather than further apart from them".

31. I accept Mr. Thornton QC's submissions. When the effect of the difference in rights provided to 21st Century under the New Scheme, the Rights Issue and the Deed of Novation, and to the other Scheme Creditors under the New Scheme and the Rights Issue is analysed in a commercial way, it does seem that 21st Century is willing to forgo a strategic advantage which it has by being owed money by SBSAL, and instead to throw its lot in with the other Scheme Creditors who are only owed money by the Company, in order to give the overall restructuring the chance to succeed.

32. On that basis, in my judgment there is no reason why 21st Century cannot consult together with other Scheme Creditors on the commercial merits (or otherwise) of the proposal put forward for the survival of the group. In particular, I see no reason why 21st Century cannot consult with other Scheme Creditors on the common interest that they all have of evaluating whether the Company's proposals for the future operations of the group are viable, or whether they are in effect being asked to throw good money after bad; together with evaluating whether the relative proportions of the shares in the restructured group which are being offered to the Scheme Creditors and to the existing shareholders provide a suitable division of the ownership of the restructured group.

33. I should, for the avoidance of doubt, add that in reaching this conclusion on class composition I am not expressing any view as to whether the court should ultimately give effect to an affirmative vote in such class having regard to the various different interests that some of the Scheme Creditors have in other capacities (e.g. as existing shareholders, directors and underwriters of the Rights Issue). Such factors go to the exercise of the court's discretion at the sanction stage (see Hawk above).

34. Further, given that my class analysis (above) essentially turns on a commercial point arising from the basic structure of the group, rather than upon any fine distinctions between the precise level of the estimated outcome in a liquidation for creditors of the

Company and SBSAL, I do not consider that the fact that JCK has indicated that it accepts no responsibility to any third party for the Insolvency Analysis should prevent me from determining the class issue at this stage.

35. Moreover, in House of Fraser (Funding) (above), Birss J was ultimately prepared to convene the court meeting on the basis that the expert accountants in that case had accepted responsibility to the scheme company which was then able to put the relevant evidence before him (see paragraph [31]). It would seem that the question of reliance had arisen because initially there was no evidence to support the liquidation analysis from the board at all. In the instant case a director has provided some evidence of the financial position of the individual companies in the group by reference to a series of balance sheets, and has also exhibited the Insolvency Analysis, so a similar position has been reached as regards reliance as that which satisfied Birss J.

36. I also note that there was no specific challenge to the accuracy of JCK's Insolvency Analysis at this stage. In saying that I have well in mind that the Opposing Creditors only had a relatively short time to consider the materials prior to the convening hearing, but I nevertheless consider that the correct course to adopt is to determine the class question and convene the court meeting without further delay. If the Insolvency Analysis could be shown to be inaccurate in a material way at sanction, the class question (which goes to jurisdiction) could then be re-opened.

37. I shall therefore convene a single meeting of the Scheme Creditors as requested by the Company.

The draft Scheme Document

38. After Mr. Phillips had raised the Opposing Creditors' concerns over the draft provided at the convening hearing, the Company reconsidered its draft and made a number of revisions to it, which it circulated on 23 October 2020.

39. In response, the Opposing Creditors have provided one further suggestion for inclusion in the document at this stage. Subject to that and to a number of points on the form of order (see below) the Opposing Creditors have indicated that they are content for me to proceed to convene the court meeting. They have, however, reserved their position on the adequacy of the Scheme Document and their right to challenge its accuracy and adequacy at the sanction stage.

40. In my view, the process that has been followed on this occasion (as distinct from that deployed in relation to the Original Scheme that failed for want of proper information being supplied to Scheme Creditors) well illustrates the utility of the opportunity provided for by the Practice Statement for interested creditors and the court to take a broad overview of a scheme document at the convening hearing before it is circulated more generally. Some obvious points have been made by the Opposing Creditors and taken on board by the Company, the overall process has not been materially delayed, and rights have been reserved to challenge the detail of the document at the appropriate occasion i.e. sanction.

41. On that basis, and assuming that the further point raised by the Opposing Creditors can be accommodated, I propose to say no more at this stage as to the adequacy and accuracy of the Scheme Document.

Timing

42. After the convening hearing had concluded, and together with proposing a revised Scheme Document, the Company indicated that it would be prepared for me to order that no less than 21 days should elapse between the circulation of the Scheme Document and the court meeting. That corresponds with the view that I had formed at the hearing, which was that even though Scheme Creditors were familiar with the general shape of the New Scheme because of the earlier proposal in relation to the Original Scheme, they should nevertheless be given more time to read and digest the additional (and materially different) information now provided by the Company.

43. I will also indicate that the sanction hearing should be listed for a date no less than one week after the holding of the court meeting. This will provide an adequate period in which the parties can consider the outcome of voting and prepare submissions in advance of the sanction hearing.

Conclusion

44. I shall make a convening order for a single meeting of Scheme Creditors. I invite counsel to agree a draft order. I should also be provided with short written submissions if there is a dispute over the request by the Opposing Creditors that they be paid their costs of the convening hearing by the Company.