Landmark scheme of arrangement in Ireland

Ruairi Rynn reports on the Irish High Court sanctioned scheme of arrangement to restructure US$1.65 billion of senior debt

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William Fry recently advised Ballantyne Re plc ("Ballantyne"), an Irish reinsurance SPV, on an Irish law scheme of arrangement to restructure its reinsurance obligations and outstanding New York law governed indebtedness, such that the residual value in the company could be distributed to its senior noteholders (the "Scheme").

The Scheme provided for, amongst other things, the restructuring of third party guaranteed senior debt, the commutation of the largest guarantor's obligations and the preservation of the second guarantor's obligations until the original maturity of Ballantyn's senior debt in 2036.

The sanction of the Scheme by the Irish High Court was opposed by a senior noteholder with a relatively minor holding. Following a contested hearing, Mr Justice Barniville delivered a detailed judgment rejecting all the grounds of objection and sanctioned the Scheme on 6 June 2019. Ballantyne subsequently sought and obtained recognition of the Scheme under Chapter 15 of the US Bankruptcy Code on 11 June 2019.

What is a scheme of arrangement under Irish law?

Part 9 of the Irish Companies Act 2014 (the "2014 Act"") provides for a "company" to enter into a compromise or arrangement with (a) its creditors or any class of them or (b) its members or any class of them.

In order for a scheme of arrangement under Part 9 of the 2014 Act to take effect:

(1) the scheme of arrangement must be approved by a special majority (a majority in number representing 75% or more in value of the creditors/members of each class present and voting) at the required meetings of classes of creditors/members;

(2) the publication of notices of the passing of such resolutions at the scheme meeting(s) and that an application will be made to the High Court to sanction the scheme of arrangement; and

(3) The High Court must sanction the scheme of arrangement.

A "company" in this context means any company liable to be wound-up under the 2014 Act and therefore includes any company, Irish or non-Irish, with a sufficient connection to Ireland.

The legislation and jurisdiction of the Irish High Court is broadly similar to the English legislation and jurisdiction re schemes of arrangement.

Background

Ballantyne was incorporated for the purpose of entering into and performing an indemnity reinsurance agreement (the "Reinsurance Agreement") relating to a defined block of life insurance policies. In order to fund its obligations under the Agreement, Ballantyne issued senior notes and junior notes in the total amount of c. US$ 1.92 billion and engaged a third party as investment manager (the "Investment Manager") for the funds raised from the issuance of the notes.

The scheduled interest and principal of certain senior notes was guaranteed by Ambac Assurance UK Limited ("Ambac") (par value US$ 900 million) and Assured Guaranty (UK) plc (and ultimately other Assured Guaranty group entities) ("Assured") (par value US$ 500 million).

Approximately 95% of these funds were invested in subprime and Alt-A securities which experienced c. US$ 1 billion of losses between May 2006 and October 2008. Following the settlement of litigation against the Investment Manager and discussions with certain senior noteholders, Ballantyne considered a restructuring proposal presented by Ambac and concluded that the proposed restructuring was in the best interests of Ballantyne's creditors in their entirety and determined to proceed with the Scheme.

Proposed restructuring of Ballantyne

The key elements of the proposed restructuring included:

(1) the novation of the Reinsurance Agreement to Swiss Re Life and Health America Inc.;

(2) the disbursement of residual assets following the novation to pay a dividend to senior noteholders (US$ 0.512 per US$ 1.00 of senior debt);

(3) the commutation of the guarantee obligations of Ambac in return for a commutation payment;

(4) the releases of any claims of the senior noteholders against the various released parties (including Ambac as financial guarantor); and

(5) the subsequent solvent liquidation of Ballantyne.

The sanction hearing

Resolutions to approve the Scheme were passed overwhelmingly by senior noteholders at two scheme meetings and Ballantyne subsequently issued an application to the Irish High Court for an order sanctioning the Scheme. That application was opposed by

a single senior noteholder, ESM Fund I, LP ("ESM") who held US$ 5 million of the Ambac guaranteed senior notes, on the grounds set out below; each was rejected by The Irish High Court.

Judgment approving the Scheme

In the judgment approving the Scheme, Barniville J. reflected on longstanding Irish and international precedents applicable to schemes of arrangement. In particular, he noted that the judgment of Mr Justice Parker in *Re Ocean Rig UDW Inc* (18 September 2017, Grand Court of the Cayman Islands, Parker J) was of "considerable assistance".

The Court also cited with approval the leading Irish decision of Mr Justice Kelly in *Re Colonia Insurance (Ireland) Ltd* [2005] 1 IR 497 ("Colonia") which set out the following criteria to be satisfied when sanctioning a scheme:

(1) Sufficient steps have been taken to identify and notify all interested parties.
(2) The statutory requirements and all directions of the court have been complied with.
(3) The classes of creditors are properly constituted.
(4) No issue of coercion must arise.
(5) The scheme of arrangement is such that an intelligent and honest man, a member of the class concerned, acting in respect of his interest, might reasonably approve it.

Barniville J. noted that it would be extremely rare for a court to refuse to sanction a Scheme where it has been approved by the required special majority of correctly constituted classes and there is no suggestion that the majority did not represent the views of the class.

Grounds for objection

The court found that the real issue in this case concerned the fifth criterion and Barniville J. then went on to consider and reject each of the following objections put forward by ESM in that context.

Alleged material deficiencies

ESM alleged that the scheme circular was materially deficient, particularly with respect to Ambac's financial position. Whilst Barniville J. accepted that the financial position of Ambac was clearly of significance to the Scheme, he was not satisfied that there was any material deficiency in the information provided in the scheme circular and concluded that Ambac was clearly in a difficult or distressed financial position.

Third party releases

ESM argued that the applicable legislation could not be interpreted to enable the provision of third party releases in a scheme and that the court had no jurisdiction to sanction a scheme of arrangement providing for the release of claims. ESM argued that strict construction should be given to the relevant statutory provision insofar as it could interfere with an Irish constitutional right.

Barniville J. noted that third party releases are "fairly common" inclusions in such schemes in other jurisdictions. He accepted that the releases were necessary under the Scheme to give effect to the commutation of the Ambac guarantee and bring finality to the affairs of Ballantyne.

As to the constitutional point the Court (whilst not determining whether ESM as a non-Irish body corporate had the benefit of Irish constitutional rights) concluded that the involvement of the court in sanctioning a scheme of arrangement provided the appropriate protection and balance of any constitutional rights involved.

New York dimension

Barniville J. rejected any contention that the restructuring should have been pursued before the US courts and did not accept that fiduciary duties applicable to Ballantyne and its directors were governed by New York law. He accepted Ballantyne's submissions that an Irish scheme could be utilised to restructure New York law governed debt.

Finally, he concluded that ESM had not demonstrated any good reason for him not to sanction the Scheme based on the existence of a recently issued federal complaint against Ambac by ESM, that ESM asserted would have been compromised by the Scheme (in particular the third party release).

Decision

Barniville J. ultimately sanctioned the Scheme on the basis that:

1. the pre-conditions set out in Section 453 of the 2014 Act were satisfied;
2. the criterion set out in Colonia, that there was no coercion of the minority at the relevant scheme meetings, was met; and
3. an honest and intelligent person acting reasonably in his or her own interest would have supported the Scheme.

Chapter 15

An application was subsequently made to the US Bankruptcy Court to recognise the Scheme as a "foreign main proceedings" under Chapter 15 of the US Bankruptcy Code. Whilst that application was initially contested by ESM, that objection was not pursued at the hearing and an order was made on 11 June 2019 recognising the Scheme.

Key Points

This case demonstrates the effectiveness of an Irish law scheme of arrangement as a tool to implement complex international debt restructurings and it highlights the effectiveness and robustness of Ireland as a jurisdiction in which to pursue such restructurings. It also demonstrated the willingness of the Irish courts to consider the well-developed jurisprudence of other jurisdictions in evaluating and ultimately sanctioning a scheme of arrangement. ■

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