Neutral Citation Number: [2020] EWHC 2977 (Ch)

Claim No: CR-2020-003944

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

The Rolls Building
7 Rolls Buildings
Fetter Lane
London EC4A 1NL

Date: 05/11/2020

Before:
MR. JUSTICE SNOWDEN
- -

Between:

IN THE MATTER OF KCA DEUTAG UK FINANCE PLC

Applicant

- and -

IN THE MATTER OF THE COMPANIES ACT 2006

- -

MR. DAVID ALLISON QC and **MR. ADAM AL-ATTAR**
(instructed by **Allen & Overy LLP**) appeared for the **Applicant.**

- -

APPROVED JUDGMENT

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MR. JUSTICE SNOWDEN :

Introduction

1. This is the application by KCA Deutag UK Finance plc ("the Company"), for an order sanctioning a scheme of arrangement (the "Scheme") between the Company and its "Scheme Creditors" (as defined in the Scheme) pursuant to Part 26 of the Companies Act 2006. The Scheme has received overwhelming support of over 99% of Scheme Creditors and is not opposed by the only creditor who voted against the Scheme at the court meeting.

2. In those circumstances and without intending any disrespect to the very full and detailed submissions which I have received from Mr. Allison QC and Mr. Al-Attar, I shall be brief.

3. The background to the Scheme was set out in some detail in paragraphs 2 to 18 of the judgment of Mr Justice Trower following the convening hearing: see [2020] EWHC 2779 (Ch). I shall not repeat it at any length.

4. The Company is incorporated in England and Wales. It is a finance company in the KCA Deutag group which is a market-leading international drilling, engineering and technology group, serving both onshore and offshore drilling markets. The group operates in more than 15 countries, with a strong presence in Europe (including in the North Sea), Russia (including in the Caspian Sea), Africa and the Middle East.

5. The company has its centre of main interests (COMI) in England. A substantial number of the Scheme Creditors are domiciled in the UK. Following a change in accordance with the then governing law (New York law), the relevant

financing documents constituting the debt to be compromised under the Scheme (the "Scheme Debt") are now governed by English law and have choice of forum clauses in favour of this court.

6. The combined impact of the COVID-19 pandemic and the OPEC-related oil price reduction on the group and the wider market has meant that the group is unable to meet its ongoing liquidity requirements and to address a decline in its EBITDA without a material reduction in its debt. That is the purpose of the restructuring of which the Scheme forms the central part.

7. The Scheme relates to approximately $2 billion of financial indebtedness under a variety of instruments owed by the Company and its affiliates. That Scheme Debt will be released in exchange for $500 million of new senior secured notes ("New Notes") and what will initially be 100% of the ordinary shares to be issued by a new Jersey holding company ("Jersey newco"), which will become the ultimate holding company of the Company. The new debt and equity will be allotted to Scheme Creditors pro rata to the financial indebtedness owed to those Scheme Creditors.

8. That 100% equity ownership of Jersey newco by Scheme Creditors might be reduced in certain circumstances in the future by the issue of up to 5% of the equity under a management incentive scheme, or the issue of up to a further 10% of the equity following the exercise of warrants to be issued under the wider restructuring to certain "Participating Shareholders" of the Company's ultimate parent company. I will return to those matters in due course.

9. Following the restructuring, the group will have a strengthened balance sheet. Its total debt will be reduced by approximately $1.4 billion, meaning it will have

a net leverage of 1.4 times its asset value, compared to its current net leverage of 6.3 times its asset value.

10. In addition to the debts owed to the Scheme Creditors, there are two ancillary facilities of about $60 million, which are not to be compromised by the Scheme but will instead be restructured by bilateral arrangements. There are also certain other term loans and hedging arrangements which will not be compromised by the Scheme.

11. The evidence indicates that the alternatives to the Scheme and the proposed restructuring would either be a distressed, accelerated sale of the individual business units within the group; or a formal liquidation process of the whole or of those parts of the group that could not be easily sold.

12. Deloitte have modelled the likely realisations in these different scenarios and have concluded that Scheme Creditors would be likely to recover between 49% and 59% of the Scheme Debt owed to them in the event of a distressed, accelerated disposal of the business units of the group; and would be likely to recover only between 27% and 38% of the Scheme Debt owed in the event of a formal liquidation of the group's assets following a cessation of business.

13. Deloitte have also prepared a going concern valuation of the group, on the assumption that the business is no longer in financial distress. This indicates that an estimated enterprise value, on a cash-free and debt-free basis, is in the range of $1.2 billion to $1.5 billion. Based on this estimated enterprise value, the indicative post-restructuring value of the shares and New Notes in Jersey newco is estimated to be 69.7% of the Scheme Debt immediately after the

Scheme becomes effective, with the potential, as a result of a subsequent increase in the value of the equity, to rise to 100% or more thereafter.

14. In the convening judgment, Mr. Justice Trower ordered a single class meeting of Scheme Creditors. The evidence establishes, to my satisfaction, that the Company complied with the convening order. The court meeting was held on 30th October 2020, without any problem, by electronic means. The meeting was attended, in person or by proxy, by 189 creditors, representing 96.96% by value of the Scheme Creditors who were entitled to vote. Of those, as I have indicated, all but one Scheme Creditor voted in favour. That represented a vote of 99.47% in number and 98.97% by value to approve the Scheme.

The approach to sanction

15. Against that background, the Company now seeks the court's sanction for the Scheme. The relevant principles which are applied at this stage of the process were conveniently summarised by Mr. Justice David Richards, as he then was, in *Re Telewest Communications plc (No. 2)* [2005] 1 BCLC 772, at paragraphs [20] to [22] as follows,

> "20. The classic formulation of the principles which guide the court in considering whether to sanction a scheme was set out by Plowman J in *Re National Bank Ltd* [1966] 1 All ER 1006 at 1012, [1966] 1 WLR 819 at 829 by reference to a passage in Buckley on the Companies Acts (13th edn, 1957) p 409, which has been approved and applied by the courts on many subsequent occasions:
>
> > 'In exercising its power of sanction the court will see, first, that the provisions of the statute have been complied with; secondly, that the class was fairly represented by those who attended the meeting and that the statutory majority are acting bona fide and are not coercing the minority in order to promote interests adverse to those of the class whom they

> purport to represent, and thirdly, that the arrangement is such as an intelligent and honest man, a member of the class concerned and acting in respect of his interest, might reasonably approve.
>
> The court does not sit merely to see that the majority are acting bona fide and thereupon to register the decision of the meeting; but at the same time the court will be slow to differ from the meeting, unless either the class has not been properly consulted, or the meeting has not considered the matter with a view to the interests of the class which it is empowered to bind, or some blot is found in the scheme.'
>
> 21. This formulation in particular recognises and balances two important factors. First, in deciding to sanction a scheme under [Part 26], which has the effect of binding members or creditors who have voted against the scheme or abstained as well as those who voted in its favour, the court must be satisfied that it is a fair scheme. It must be a scheme that 'an intelligent and honest man, a member of the class concerned and acting in respect of his interest, might reasonably approve'. That test also makes clear that the scheme proposed need not be the only fair scheme or even, in the court's view, the best scheme. Necessarily there may be reasonable differences of view on these issues.
>
> 22. The second factor recognised by the above-cited passage is that in commercial matters members or creditors are much better judges of their own interests than the courts. Subject to the qualifications set out in the second paragraph, the court 'will be slow to differ from the meeting'. "

16. The relevant questions for the court at the sanction hearing can therefore be summarised as follows:

i) Has there been compliance with the statutory requirements?

ii) Was the class fairly represented and did the majority act in a *bona fide* manner and for proper purposes when voting at the class meeting?

iii) Is the scheme one that an intelligent and honest man, acting in respect of his interests, might reasonably approve?

iv) Is there some other 'blot' or defect in the scheme?

In the case of a scheme with international elements there is also the question of whether the court will be acting in vain if it sanctions the scheme. This requires some consideration of whether the scheme will be recognised and given effect in other relevant jurisdictions.

17. I therefore turn to consider those questions.

Compliance with the statute

18. The question of whether the provisions of the statute have been complied with can be subdivided as follows: (i) have the classes been properly constituted; (ii) was there compliance with the terms of the convening order (including in particular whether the scheme creditors received an adequate explanatory statement); and (iii) were the statutory majorities obtained?

19. Class Although the court is required to be satisfied at the sanction stage that the class(es) were properly constituted, the general expectation is that if notice has been given to scheme creditors in accordance with the Practice Statement (Companies: Scheme of Arrangement under Part 26 and Part 26A of the Companies Act 2006) and the court has determined the class question at the convening stage, the court should not generally revisit the class question of its own motion at sanction unless it can see that some material factor was not considered or there was some obvious error in the determination of the question at the convening stage.

20. In this case, due notice of the convening hearing was given to Scheme Creditors and Mr. Justice Trower considered the class question at some length at the convening stage. I have no reason to doubt or differ from his judgment.

21. The only issue which I raised at this sanction stage was in relation to the issue of warrants by the Jersey newco as part of the wider restructuring after the Scheme becomes effective. Mr. Allison QC has satisfied me that the issue of warrants by the Jersey newco will only take place to Participating Shareholders and not to any Scheme Creditors of the Company. As such, this feature of the restructuring will not give any additional benefit to any of the Scheme Creditors and accordingly does not affect the class question which Mr. Justice Trower decided.

22. The court meeting and explanatory statement As I have indicated, I am satisfied on the evidence that the court meeting was convened in accordance with the court's order, that it was attended by almost all of the Scheme Creditors and that it was properly held. The explanatory statement was also provided to Scheme Creditors in accordance with the convening order and is comprehensive and lengthy. No-one has suggested that it failed in any material respect to give Scheme Creditors the information that they reasonably required to form a view as to the merits of the Scheme.

23. In that regard I think it would be fair to say that the possibility of the 100% ownership of Jersey newco by the Scheme Creditors being reduced either by the subsequent issue of shares pursuant to the management incentive plan or by the exercise of the warrants issued to the Participating Shareholders was not full, front and centre of the explanatory statement. However, those possibilities were

discoverable from the detail included in the explanatory statement and were mentioned in a statement in the "Risk Factors" section that,

> "An additional issue of ordinary shares by Jersey Newco could dilute the proportionate ownership and voting interest of shareholders and could have an adverse effect on the price of Jersey Newco Shares. This will particularly be the case if and to the extent that such an issue of Jersey Newco Shares is not effected on a pre-emptive basis (including, but not limited to, any issue of ordinary shares in relation to the Management Equity Plan and/or exercise of Warrants) or shareholders do not take up their rights to subscribe for further Jersey Newco Shares structured as a pre-emptive offer or as an emergency securities issuance."

24. It is also apparent that the only circumstances in which, in particular, the warrants might be exercised would be if an exit event had occurred which resulted in a return to Scheme Creditors of at least 115% in respect of their Scheme Debt. Given that this situation would mean that Scheme Creditors would already be well ahead of the game in terms of recoveries, I do not think that highlighting more clearly the possible dilutive effect of exercise of such warrants on Scheme Creditors in the explanatory statement would be at all likely to have affected the way in which they voted.

25. The statutory majorities As I have already indicated, the statutory majorities were obtained with an overwhelming vote.

The majority vote

26. I have already indicated that the very high turnout at the court meeting means that almost all the class were present in person or by proxy. The meeting was therefore plainly representative of the class as a whole. I also have absolutely no basis to think that those attending and voting in favour were doing anything

other than voting in accordance with the interests of the class which the majority was empowered to bind.

27. In the convening judgment at paragraphs [38]-[44], Mr. Justice Trower specifically considered the potential impact of the payment of so-called "work fees" on the class question. He took the view on the basis of the Company's evidence that payment of this fee was most unlikely to have had any material influence on the recipients' consideration of the merits of the Scheme. As matters have turned out, this view appears to have been confirmed. Among those who approved the Scheme were 109 Scheme Creditors, holding 41% in value of the Scheme Debt voted, who did not receive any work fees. Moreover, the one creditor that voted against the Scheme was in fact a recipient of work fees. It can therefore be surmised that the payment of work fees did not influence the majority vote, and that it was achieved in the interests of the class as a whole.

The "fairness' of the Scheme

28. Although the third test which I outlined above is often, for shorthand, referred to as the question of whether the scheme is 'fair', it is apparent from paragraph [21] of the judgment of Mr. Justice David Richards in the *Telewest* case to which I have referred above, that 'fairness' in this context has a specific and limited meaning. The court simply has to be satisfied that the scheme is one that an intelligent and honest man, acting in respect of his interests, might reasonably approve. It does not mean that the court is required to form a view of whether the scheme is, in some general sense, or even in the court's own opinion, the 'fairest' or 'best' scheme.

29. Moreover, as Mr. Justice David Richards explained, provided that the scheme meeting was properly consulted (viz., by creditors having the necessary time to consider sufficient information in an adequate explanatory statement), that attendance at the meeting was representative of the class, and that the majority were not actuated by any form of improper motive or purpose, the court will generally take the view that in commercial matters the majority of scheme creditors are much the better judges of their own interests than the court. Accordingly, given satisfaction of the qualifications that I have mentioned, the court will be very slow to differ from the result of the meeting.

30. It seems to me that that approach is entirely appropriate in this case. The Scheme Creditors had the opportunity to consider the very full explanatory statement which contained an independent analysis of their options by Deloitte; this obviously provided a sensible basis for a Scheme Creditor to consider that the Scheme would be in its best interest; and the overwhelming majority of Scheme Creditors obviously did think that and voted in favour.

No ‘blot’ or defect

31. In the convening judgment, Mr. Justice Trower dealt with a number of technical points on how the Scheme is intended to operate. Again, I see absolutely no reason to doubt or differ from his conclusions. I also see no other blot or defect in the Scheme.

International effectiveness

32. The final point is that the court will wish to be satisfied that it is not acting in vain when it sanctions a scheme, especially one which has an international

aspect. The concern arises where a significant number of scheme creditors and assets of the scheme company are located in other jurisdictions. In such a case the court should be alert to ensure that there is at least a reasonable prospect that scheme will be recognised and given effect in other relevant jurisdictions so as not to be capable of being undermined by action by dissenting creditors (or indeed any creditors who participated under the scheme), who might fancy a second bite at the assets of the company.

33. In this case, two things give me that comfort. The first is that there was an overwhelming vote by Scheme Creditors in favour, and a very large number of such creditors entered into a lock-up agreement which bound them contractually to support the Scheme and not to do anything to undermine it. It is very difficult to see how such creditors who contractually agreed to support the Scheme and/or who voted in favour could possibly be allowed to take action contrary to the Scheme in any foreign jurisdiction, and the number and financial interests of those who did not vote in favour is comparatively very small indeed. That alone is sufficient to demonstrate to me that the Scheme is likely to have a substantial international effect and that I would not be acting in vain if I were to sanction it.

34. Secondly, however, and for good measure, the company has also produced independent expert evidence to satisfy me that in practice the scheme is likely to be recognised and given effect in those other jurisdictions in which creditors are located, or in which substantial assets of the group are located. Those jurisdictions are the United States, Germany, Norway, Russia and Oman. The experts' reports give me additional comfort in that respect.

Conclusion

35. Accordingly, this is a Scheme which I consider that it is appropriate to sanction, and I will do so on the terms of an order which I will now discuss with Mr. Allison QC.

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