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US CORNER

UK Order Granting Non-Consensual Third-Party Releases Is Enforced in US Chapter 15 Case[1]

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Synopsis

In *In re Avanti Communications Group PLC*, Judge Martin Glenn of the United States Bankruptcy Court for the Southern District of New York enforced a UK court order granting non-consensual third-party releases. Despite these releases remain problematic for courts in U.S. chapter 11 cases, Judge Glenn reasoned that principles of comity and consistency with due process standards of the U.S. justified enforcement of the UK scheme of arrangement containing such releases. Albeit this may appear an opportunity to avoid the uncertainty of non-consensual third-party releases in chapter 11, *Avanti*'s scope is rather limited and does not open the door to approval of just any kind of non-consensual third-party releases through chapter 15.

Background

Avanti Communications Group ('Avanti') is an international satellite operator offering services throughout Europe, Africa, and the Middle East.[2] It is incorporated in England and Wales, and has multiple subsidiaries incorporated throughout Europe and Africa.[3] Avanti utilizes its fleet of satellites to collect and sell data communication services to various service providers, who in turn, supply to broadband, government, enterprise and backhaul markets.[4] Of the four satellites in Avanti's fleet, two satellites experienced delayed launches due to construction and manufacturing issues.[5] However, once launched, both satellites were expected to have a promising effect on Avanti's business for the foreseeable future.[6]

As of 2017, Avanti's capital structure consisted of senior secured notes maturing in 2021, with an outstanding principal of approximately USD 323.3 million (the '2021 Notes') and senior secured notes maturing in 2023 (the '2023 Notes'), with an outstanding principal of approximately USD 557 million, as well as indebtedness under a super-senior term loan with approximately USD 118 million outstanding.[7] As a result of the delayed launches, Avanti was forced to convene with a group of its creditors to create a detailed restructuring plan pursuant to a Scheme of Arrangement under UK law (the 'Scheme') to alleviate financial hardship and generate a suitable capital structure moving forward.[8] The Scheme proposed an exchange of the outstanding 2023 Notes for 92.5% of Avanti's then issued share capital, on a pro-rata basis, effectively relieving Avanti of approximately USD 81 million in annual interest on the 2023 Notes. The Scheme also amended the indenture governing the 2021 Notes, extending the maturity date and adjusting the interest rate payable to the 2021 Notes holders.[9] Ultimately, the Scheme called for releases from the 2023 Notes holders, including releases of guarantees that were provided by Avanti's affiliates, for any claim or liability arising from or in connection with the 2023 Notes.[10]

In February 2018, the UK Court granted Avanti permission to convene a meeting of its creditors to approve of the proposed restructuring agreement.[11] The Convening Order required a meeting of the 2023 Notes holders, the only class of creditors effected by the restructuring. Additionally, a notice of the restructuring

Notes

1 The views expressed herein are solely those of the author, and not necessarily the views of Proskauer Rose LLP or any of its attorneys.
2 *In re Avanti Communs. Grp. PLC*, 582 B.R. 603, 607 (Bankr. S.D.N.Y. 2018).
3 *Id.*
4 *Id.* at 608.
5 *Id.*
6 *Id.*
7 *Id.*
8 *Id.*
9 *Id.* at 609.
10 *Id.*
11 *Id.* at 610.

and proxy materials were required to be made available to the creditors to vote.[12] At the meeting, the restructuring agreement was approved, without dissenters, by creditors representing over 98% of the outstanding value of the 2023 Notes.[13] The UK Court subsequently sanctioned the restructuring agreement because Avanti had complied with statutory requirements, the voters were fairly represented and acted in a *bona fide* manner, and the restructuring agreement was 'one that an intelligent and honest man, acting in respect of his interest as a creditor, might reasonably approve'.[14] In turn, Avanti sought recognition and enforcement of the Scheme in the U.S. by commencing a chapter 15 case in the United States Bankruptcy Court for the Southern District of New York ('Bankruptcy Court').

The unsettled law on third-party releases

In U.S. chapter 11 cases, non-consensual third-party releases are unsettled at best. While third-party releases are routinely granted upon consent, contentions arise when consent is not unanimous.[15] The inconsistency surrounding non-consensual third-party releases has resulted in a circuit split: the Fifth, Ninth, Tenth, and the District of Columbia Circuits currently hold that the Bankruptcy Code restricts courts from granting non-consensual third-party releases, while the Second, Fourth, Sixth, Seventh, and Eleventh Circuits hold that non-consensual third-party releases may be granted in limited circumstances.[16]

For example, the Fifth Circuit took a restrictive approach to granting non-consensual third-party releases in *Bank of N.Y. Trust Co. v Official Unsecured Creditors' Comm. (In re Pacific Lumber Co.)*.[17] Approval of the plan was not consensual and 'crammed down' dissenting classes.[18] Proponents of the plan insisted the releases were essential to the restructuring – that it was 'part of their bargain' – as otherwise they would not have contributed to the plan's financing.[19]

The court perceived the releases as serving no other purpose than to protect non-debtors from negligence occurring throughout the restructuring process, which the court found to be inequitable.[20] In justifying striking the non-debtor release, the court reasoned that Bankruptcy Code section 524(e) only releases the debtor, and not co-liable third parties, indicating that non-consensual third-party releases may be improper under the Bankruptcy Code.[21] Further, the court failed to entertain a request to adopt a 'more lenient approach to non-debtor releases taken by other courts,' and held that precedent cases in the circuit 'seem broadly to foreclose non-consensual non-debtor releases'.[22]

Contrarily to the Fifth Circuit, the Second Circuit in *In re Metromedia Fiber Network, Inc.*, held that non-consensual third party releases may be granted, albeit in extraordinary circumstances.[23] The court held it permissible to enjoin a creditor from bringing claims against a non-debtor, provided that the release was critical to the restructuring process, but cautioned that 'such a release is proper only in rare cases'.[24] In recognizing that Bankruptcy Code section 105(a) provides the bankruptcy court 'necessary or appropriate' authority to act in furtherance of the Bankruptcy Code,[25] the *Metromedia* court emphasized that such authority cannot be created and must originate from the Bankruptcy Code itself.[26]

The factors set forth in *Metromedia* have continued to guide courts throughout the Second Circuit. Despite noting that the issue does not turn on satisfying

Notes

12 *Id.*
13 *Id.*
14 *Id.*
15 *Id.* at 606.
16 *Id.*
17 *Bank of New York Trust Co., NA v Official Unsecured Creditors' Comm. (In re Pacific Lumber Co.)*, 584 F.3d 229 (5th Cir. 2009), hereinafter *In re Pacific Lumber Co.*
18 *Id.* at 238.
19 *Id.* at 251-52.
20 *Id.* at 252.
21 *Id.*
22 *Id.* at 252.
23 *Deutsche Bank AG, London Branch v Metromedia Fiber Network, Inc. (In re Metromedia Fiber Network, Inc.)*, 416 F.3d 136, 141 (2nd Cir. 2005), hereinafter *In re Metromedia Fiber Network, Inc.* While ultimately holding the bankruptcy court erred in granting the release because there was insufficient evidence proving the release was essential to reorganization efforts, the court upheld the bankruptcy's release on the doctrine of equitable mootness. *Id.*
24 *Id.*
25 Bankruptcy Code section 105(a) provides:

> 'The court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title. No provision of this title providing for the raising of an issue by a party in interest shall be construed to preclude the court from, sua sponte, taking any action or making any determination necessary or appropriate to enforce or implement court orders or rules, or to prevent an abuse of process.'

26 *In re Metromedia Fiber Network, Inc.* 416 F.3d at 141.

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certain 'factors or prongs,' the court illustrated certain instances where third-party releases have been permitted.[27] Such circumstances include whether substantial consideration has been received by the estate, whether the enjoined claims were directed towards a settlement fund as opposed to being extinguished, whether the enjoined claims would alter reorganization through indemnity or contribution claims, whether the plan otherwise accounted for full payment of the enjoined claims, or if the releases were consented to by affected creditors.[28]

Third-party releases in chapter 15

Despite the uncertainty surrounding non-consensual third-party releases in chapter 11 cases, third-party releases granted in foreign orders have previously been enforced in the U.S. through chapter 15 cases. A main objective of chapter 15 is to foster cooperation between courts in the U.S. and competent foreign authorities involved in cross-border insolvency cases.[29] If enforcement of a foreign court's order is not contrary to U.S. public policy, courts often will wield the power granted to them in Bankruptcy Code section 1507 as they see fit.[30] 'Additional assistance,' such as enforcing a foreign court's order, however, must importantly be 'consistent with the principles of comity' to be provided by the court.[31]

For example, in *In re Metcalfe & Mansfield Alternative Invs.*, the Bankruptcy Court was faced with the question of whether to enforce a Canadian order sanctioning and implementing a restructuring plan which included extensive non-debtor releases.[32] The restructuring plan, a by-product of the world-wide financial crisis in 2007, was approved by 96% of the Asset Backed Commercial Paper ('ABCP') Noteholders and was subsequently approved by the Ontario Court and affirmed on appeal.[33]

The Bankruptcy Court held that '[p]rinciples of comity in chapter 15 cases support enforcement of the Canadian Orders in the United States *whether or not the same relief could be ordered in a plenary case under chapter 11*'.[34] The court emphasized that the relief granted in a foreign proceeding does not need to mirror relief available in the U.S, and that the court must determine whether the foreign procedures 'meet our fundamental standards of fairness'.[35] Further, the court relied on the comity factors set forth by the Supreme Court in *Hilton v Guyot* to support the decision, which provided, in part, that a foreign proceeding should be enforced if it offers 'a full and fair trial abroad before a court of competent jurisdiction…under a system of jurisprudence likely to secure an impartial administration of justice…and there is nothing to show either prejudice in the court, or in the system of laws under which it is sitting'.[36] Since the Canadian justice system operated in a manner consistent with U.S. due process standards, enforcing the restructuring plan, despite its broad non-debtor releases, was consistent with the principles of comity.[37] Therefore, the court enforced the restructuring plan despite the possibility the third-party releases would not have been be available in a U.S. chapter 11.[38]

The *Avanti* decision

In *Avanti*, the Bankruptcy Court granted the unopposed request for recognition of the Scheme, including the third-party releases, which would be binding against the small number of non-voting impaired creditors. The court in *Avanti* found comfort in the UK proceeding because the affected creditors had a 'full and fair opportunity to vote on, and be heard in connection with, the Scheme'.[39] Consistency with due process standards of the U.S. also favored enforcement of the order.[40] Further, UK law governing consent of the arrangement offers robust protection of creditors. For example, UK law does not provide a mechanism forcing a plan on dissenting creditors as a chapter 11 allows through 'cramdown'.[41] For these reasons, the Bankruptcy Court was able to justify recognizing and enforcing the Scheme under principles of comity.[42]

Notes

27 *Id.*
28 *Id.*
29 11 U.S.C. §1501(a) (2018).
30 11 U.S.C. §1506 (2018).
31 11 U.S.C. §1507(b) (2018).
32 *In re Metcalfe & Mansfield Alternative Invs.*, 421 B.R. 685, 687 (Bankr. S.D.N.Y. January 5, 2010).
33 *Id.*
34 *Id.* at 700 (emphasis added).
35 *Id.* at 697.
36 *Hilton v Guyot*, 159 U.S. 113, 202-03 (1895).
37 *In re Metcalfe & Mansfield Alternative Invs.*, 421 B.R. at 700.
38 *Id.*
39 *In re Avanti Communs. Grp. PLC*, 582 B.R. at 618.
40 *Id.*
41 *Id.*
42 *Id.*

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Ramifications of the *Avanti* decision may be more limited than it impresses. *Metcalfe* recognized that 'the relief available in a U.S. proceeding need not be identical,' but the foreign procedures need to meet the U.S. 'fundamental standards of fairness'. The *Metcalfe* court noted, approvingly, that the foreign court's decision approving non-consensual third-party releases reflected a 'sensitivity to the circumstances justifying approving such provisions' similar to that in the relevant U.S. courts.[43] Similarly, in *Avanti*, the consistency in due process standards was a factor in favor of enforcement of the order.

Also, there were no public policy concerns that sometimes arise with recognition of foreign proceedings. Bankruptcy Code section 1506 provides the court with ultimate discretion in chapter 15 to refuse to take an action if it would be 'manifestly contrary to the public policy of the United States'.[44] In *Avanti*, the Scheme was far from being contrary to U.S. public policy, as it was 'overwhelmingly approved by 98% of the only creditor class' whose rights were affected by the Scheme, the approval consisted of no insider votes in favor of the plan, and significantly, there were no dissenters to the plan.[45] Also, there were no objections filed in opposition to the recognition and enforcement of the Scheme.[46]

Indeed, courts have not shied away from declining to enforce foreign court orders that implicate non-debtor third-party releases. The Fifth Circuit in *In re Vitro S.A.B. de C.V.*, affirmed the bankruptcy court's decision not to extend comity or enforce a Mexican court order releasing non-debtor affiliates' guarantees in light of concerning facts. While declining to address the public policy exception in Bankruptcy Code section 1506, the court determined that comity should not be extended to the Mexican proceeding because the restructuring plan precluded non-consenting creditors from recovery, and was only approved by including insider votes.[47] Tellingly, Vitro's attempt to have the Mexican order enforced in chapter 15 faced multiple objections from creditors, a fact absent in *Avanti*.[48]

Avanti should give foreign representatives seeking to enforce non-consensual third-party releases in a broadly supported UK scheme of arrangement some peace of mind – but only in the foregoing circumstances. Given the unsettled law on non-consensual third-party releases, it would be imprudent to assume that any foreign order approving such releases would be enforced in the U.S.

Notes

43 *See In re Metcalfe & Mansfield Alternative Invs.*, 421 B.R. at 697.
44 11 U.S.C. §1506 (2018).
45 *In re Avanti Communs. Grp. PLC*, 582 B.R. at 606.
46 *Id.* at 607.
47 *Ad Hoc Group of Vitro Noteholders v Vitro SAB De CV (In re Vitro SAB De CV)*, 701 F.3d 1031, 1052 (5th Cir. 2012).
48 *Id.* at 1041.

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