Irish examinership: post-eircom A look at Ireland's fastest and largest restructuring through examinership and the implications for the process*

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The Irish telecommunications company eircom recently successfully concluded its restructuring through the Irish examinership process. This examinership is both the largest in terms of the overall quantum of debt that was restructured and also the largest successful restructuring through examinership in Ireland to date. The speed with which the restructuring of this strategically important company was concluded was due in large part to the degree of pre-negotiation between the company and its lenders before the process commenced. The eircom examinership demonstrated the degree to which an element of pre-negotiation can compliment the process. The advantages of the process, having been highlighted through the eircom examinership, might attract distressed companies from other EU jurisdictions to undertake a COMI shift to Ireland in order to avail of this process.

The eircom examinership was notable for both the size of this debt restructuring and the speed in which the process was successfully concluded. In all, €1.4bn of a total debt of approximately €4bn was written off the balance sheets of the eircom operating companies. The restructuring was confirmed by the Irish High Court just 54 days after the companies entered examinership.

This restructuring also demonstrates the advantages of examinership as a 'one-stop shop': a flexible process that allows for both the write-off of debt and the change in control of ownership. The eircom examinership resulted in the senior lenders becoming the new owners of the business.

Below we set out an overview of the key features of the process and look at its capability to implement a restructuring that has been negotiated in advance. We also consider whether the success of the eircom examinership will reinvigorate this restructuring process that is currently underused, relative to the number of corporate insolvencies in Ireland in the current economic climate. There is the possibility that this process might attract certain over-leveraged distressed European companies to consider a COMI shift to Ireland in order to avail of this process.

Key features of the examinership process

Irish examinership is perhaps the closest restructuring process in Europe to US chapter 11. The purpose of the process is to rescue all or part of an ailing business. When an examinership petition is granted by the court, the court appoints an insolvency practitioner, typically nominated by the petitioner, to be the examiner to the company. The examiner's role is to investigate the affairs of the company, with a view to putting together a rescue plan for its business. This is typically achieved through a process of attracting new investment into the company and often involves the writing down of debt. The company in examinership will have extensive protection from creditor actions, from the time of presentation of the examinership petition through to the end of the process.

The examinership petition is normally presented by the company itself, although the applicable statute, the Companies (Amendment) Act 1990 (as amended) (the 'Examinership Act') also gives other stakeholders, such as shareholders, directors and creditors the standing to petition the court to place the company into the process.

During examinership, the company's management typically retain control of day-to-day business, akin to the debtor-in-possession concept in US chapter 11. The examiner's role is to formulate proposals that provide for the rescue of the company, part of which can be through seeking new investment for the company. The examiner then puts these proposals to the vote of each class of the company's shareholders and creditors. If the examiner's proposals meet the creditor approval test set out below, the examiner can then ask the court to confirm the proposals. The effect of confirmation by the court is that the proposals become binding on the company, its shareholders and its creditors, even those that have voted against the examiner's proposals.

The creditor approval threshold (for approval of an examiner's scheme of arrangement) is relatively low, being at least one class of impaired creditors voting (by majority in number and value) to accept those proposals. If the examiner's proposals meet this threshold, the remaining hurdle for the examiner to meet is that their proposals are not 'unfairly prejudicial' to any interested party. To date, in practice, this has been ascertained by comparing what a creditor could receive under the proposals to what he would have received in an alternative insolvency process (typically liquidation or receivership). The burden of proving that no interested party is unfairly prejudiced by the proposals lies with the examiner.

The examiner is subject to strict statutory milestones throughout the process, described in more detail below, with an outside date for presentation of his/her proposals to the court of 100 days after the presentation of the examinership petition.

Examinership – a process that should be pre-negotiated?

The advantages of a pre-negotiated corporate rescue are obvious: a shorter and more certain process, limiting the degree of damage to the business that might otherwise be incurred. The eircom examinership demonstrated the extent to which an element of pre-negotiating can compliment the process. Proposals for a scheme of arrangement can be formulated by the company and its key creditors before the examinership commences. Thus, the examiner can come to the role with at least one restructuring proposal available offering them the certainty of some level of creditor support, a smoother path to implementation and a reduced risk of significant challenge at the confirmation hearing.

However, since the examiner is an independent court appointed officer, they are obliged to consider all reasonable offers of prospective investment and restructuring proposals for the company. A proposal that has buy-in from a number of the company's creditor groups almost inevitably becomes the 'stalking horse': the deal to beat.

A lock-up agreement is one method of documenting the pre-negotiated proposals, as well as delivering to the examiners the creditor support they will need if they decide to adopt that pre-negotiated plan.

There are indications that the intent behind the Examinership Act was to create a process that would have a pre-negotiated element and that would move to a speedy conclusion. The Act provides that draft proposals for the company's rescue can be presented with the petition at the very outset of the process. The maximum duration of the process, 100 days, is hardly generous to restructuring professionals. In fact, the initial deadline faced by an examiner is to have held meetings of creditors to vote on their proposals and presented those proposals to the court within 35 days of appointment. The fact that the Examinership Act provides that this timeline can be extended, first to 70 days and then to 100, in both instances at the discretion of the court, does not detract from the fact that the Act sets down 35 days as the default position, indicating a legislative imperative for expedition. In complex restructurings, that kind of expedition is only possible with a significant deal of negotiation and planning prior to the process.

The court in the eircom examinership noted that while there was a tendency to regard examinership as a 100-day process, the Examinership Act contemplates a much shorter process, with the court allowing the statutory extensions only where warranted by the circumstances of the case. The judge referred to the examiner's 'enthusiasm for carrying out his statutory duty', stating that it was 'highly desirable', while noting that the examiner's task had been made 'somewhat lighter' by the negotiations that had taken place between creditors before the examiner's appointment.

Interim examiner appointments – a collateral benefit to a pre-negotiated process

There was an indication in the eircom examinership that a company will have a greater chance of benefitting from the appointment of an 'interim examiner' where it can demonstrate to the court, at the initial ex parte hearing on the presentation of the petition papers, that negotiations with the company's key creditors are at an advanced stage.

An interim examiner will be in place between the presentation of the petition and the inter partes hearing on that petition, at which, if the court approves the petition, the interim examiner will become confirmed in the role of examiner. While a number of judges have taken the position that an interim examiner should be appointed in exceptional circumstances only, securing such an appointment is an important advantage for the company in examinership. Having an interim examiner not only lends a stability to the process that can provide comfort to critical stakeholders, such as the company's trade suppliers, but it also means that the restructuring process gets underway as soon as the clock starts ticking on the initial 35 day deadline discussed above.

Position of senior creditors

The relatively low creditor approval threshold in examinership can be advantageous to senior lenders where they have reached a pre-negotiated restructuring arrangement with the company. A majority in number and value of that class alone voting in favour of the proposals is sufficient for the court to confirm the proposals, subject to the examiner showing that no other class would be unfairly prejudiced were the proposals adopted. Even if every other class of creditor votes against the examiner's proposals, unless one such class can successfully challenge the proposals on unfair prejudice grounds, they are ultimately subject to cram-down. The unfair prejudice test is typically met by a showing that the class receives treatment that is at least equivalent to what that class would have received in an alternative insolvency process. The only alternative open to an out of the money unsecured creditor class is liquidation and the unfair prejudice test can therefore usually be met where that class receives even a nominal dividend.

While there is no express requirement in the Examinership Act that the examiner's proposals must have the support of the senior creditor class, the unfair prejudice test (arguably and unintentionally) favours senior secured creditors. This is because this class of creditors has a greater array of options outside of examinership. For example, in the 2010–2011 McInerney examinership, the senior lenders effectively won out in a court overseen challenge as to what level of return they would receive in a long-term receiver controlled work-out (over 11 years) versus their return under the examiner's scheme.

The position of secured creditors who have pre-negotiated a restructuring deal with the company is undermined somewhat by the degree of interloper risk that exists in examinership. Even where the senior lenders and the company have reached a consensual deal to restructure the company's debts, or where that class has otherwise established a plan for the enforcement of its security, the examiner will still be open to bids from third parties during the process. This raises the spectre of a lengthy valuation battle, in which the examiner is required to establish, over the objections of a dissatisfied senior creditor class, that the dividend paid to that class, from the proceeds of the third party investment, is higher than what that class would receive if it were to enforce its security outside of examinership.

Where to from here?

It is hoped that eircom's widely publicised successful exit from examinership will reinvigorate an insolvency process that has been underused in recent years in Ireland. Particularly in the current economic climate, a restructuring tool with the benefits of examinership should be welcomed by Irish businesses and their lenders. There were, however, a number of tail-winds behind the eircom examinership that might not prevail in the case of the majority of distressed companies in Ireland considering their restructuring options. For instance, eircom continued to have a strong cash-generative business, even as its balance sheet reached the tipping point. Also, the company has a strategic importance in Ireland that made its continued viability and prospect of survival almost beyond question: eircom owns and controls the primary infrastructure platform that provides the vast majority of access to fixed line telecommunications services throughout the country. In addition, eircom employs almost 6,000 people throughout Ireland, a fact that was referred to by the court several times in the course of the judgments handed down in the case.

One of the primary drawbacks to examinership is the limited access to liquidity for companies in the process. However, where a company has access to sufficient working capital and the support of its senior lenders, examinership has a number of advantages, highlighted by the *eircom* case, that might attract distressed companies from other EU jurisdictions to undertake a COMI shift (that is, a shift of their 'centre of main interests') to Ireland in order to avail of this process.

Note

* David Baxter and Tanya Sheridan of A&L Goodbody acted as Irish counsel to the Coordinating Committee of the First Lien Lender Group in eircom's recent restructuring.