Neutral Citation Number: [2021] EWHC 379 (Ch)

Case No: CR-2021-000055

IN THE HIGH COURT OF JUSTICE
BUSINESS AND PROPERTY COURTS OF ENGLAND AND WALES
INSOLVENCY AND COMPANIES LIST

Rolls Building,
Fetter Lane,
London EC4A 1NL

Date: 23 February 2021

Before :

MR JUSTICE SNOWDEN

- -

IN THE MATTER OF MAB LEASING LIMITED

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

- -

Tom Smith QC and **Ryan Perkins** (instructed by **Freshfields Bruckhaus Deringer LLP**) for the **Company**
David Allison QC (instructed by **Clifford Chance LLP**) for a group of scheme creditors

Hearing date: 22 February 2021

- -

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 am on 23 February 2021.

MR JUSTICE SNOWDEN

MR JUSTICE SNOWDEN :

1. This is an application by MAB Leasing Limited (the "Company") for an order sanctioning a scheme of arrangement (the "Scheme") under Part 26 of the Companies Act 2006 (the "CA 2006") between the Company and certain of its creditors (the "Scheme Creditors").

2. The Company is incorporated in Malaysia. It is a wholly-owned subsidiary of Malaysia Aviation Group Berhad ("MAGB") (together with its subsidiaries, the "Group"). The Group is a global aviation organisation which, amongst other things, operates the national air carrier of Malaysia. The Group employs approximately 12,000 people. The ultimate shareholder of the Group is Khazanah Nasional Berhad ("KNB"), the sovereign wealth fund of Malaysia.

3. The Company leases a number of aircraft under a series of lease agreements. The Scheme Creditors are the lessors under 52 operating lease agreements (the "Operating Lease Agreements"), which are governed by English law and subject to the jurisdiction of the English Court. The purpose of the Scheme is to compromise the rights of the Scheme Creditors under the Operating Lease Agreements.

4. The COVID-19 pandemic has had a disastrous impact on the Group's operations and the aviation industry in general. The Group is now on the verge of collapse. The rents payable by the Company under the Operating Lease Agreements are no longer in line with the market rates for such aircraft, and are (in any event) unaffordable for the Company.

5. In those circumstances, the Group is seeking to implement a comprehensive financial restructuring (the "Restructuring"). As part of the Restructuring, the Company has proposed the Scheme. Under the terms of the Scheme, each Scheme Creditor will be given a menu of options from which it is entitled to make an election. Those options are broadly to:

    i) continue to lease the relevant aircraft to the Company at a revised rent adjusted to be in line with market rates (with additional optionality to receive a higher rent in return for a contingent deferral, and regarding lease extensions), with all other material terms of the Operating Lease Agreement remaining unchanged; or

    ii) terminate the relevant Operating Lease Agreement and take back the aircraft (and receive a one-off payment which exceeds the upper end of the expected return in a liquidation of the Company).

6. Although the Company has been given interim financial support by KNB, absent the Scheme and the Restructuring it is projected that the Company would run out of money in very short order and would have to enter insolvent liquidation.

7. The convening hearing was held on 20 January 2021 (the "Convening Hearing"). Mr Justice Zacaroli made an order convening a single meeting of the Scheme Creditors (the "Scheme Meeting") to consider and, if thought fit, approve the Scheme (the "Convening Order") and gave a judgment explaining his reasons for making the Convening Order: see [2021] EWHC 152 (Ch).

8. The Scheme Meeting was held on 10 February 2021. The Scheme was unanimously approved by those voting at the Scheme Meeting. The turnout was approximately 95.9% by value, with only one Scheme Creditor (out of 44) having failed to vote. Accordingly, there was overwhelming support for the Scheme.

9. In addition, shortly before the sanction hearing I received further evidence that the one Scheme Creditor which did not vote at the Scheme Meeting has been able to resolve the communication difficulties with its financiers that prevented it from participating in the Scheme process and has consented to the Scheme. That is an important point for the purposes of an issue relating to the Convention on International Interests in Mobile Equipment signed at Cape Town on 16 November 2021 (the "Cape Town Convention") to which I shall return below.

Background

The Operating Lease Agreements

10. The Company provides aircraft leasing services to operating airlines in the Group. The Company leases aircraft and engines under various operating and finance leases. The Scheme relates to the Company's liabilities to the lessors under operating lease agreements in respect of 52 aircraft (the "Operating Lease Agreements"). These aircraft (the "Operating Lease Aircraft") comprise:

    i) 44 Boeing 737-800 aircraft;

    ii) 3 Airbus A330-200 aircraft; and

    iii) 5 Airbus A330-300 aircraft.

11. Although the Operating Lease Agreements follow a common legal framework, the individual commercial terms (e.g. as to the term of the lease and the rent) obviously differ depending on the "vintage" (age) and type of the aircraft, as well as other factors. However, all of the Operating Lease Agreements are governed by English law and provide for the courts of England and Wales to have jurisdiction in respect of any disputes arising out of or in connection with them.

12. The Operating Lease Aircraft are sub-leased by the Company to Malaysia Airlines Berhad ("Malaysia Airlines"), which is the national air carrier of Malaysia.

13. The Scheme Creditors' rights and claims under the Operating Lease Agreements are secured by way of a security assignment with respect to the corresponding sub-lease from the Company as sublessor to Malaysia Airlines as sublessee. This "security" would have a very low value if Malaysia Airlines were to enter into liquidation. Thus, in commercial terms, the Operating Lease Agreements are effectively unsecured. The Operating Lease Agreements are, however, guaranteed by MAGB (the parent company of the Group).

14. In addition to the Operating Lease Agreements, the Company is a party to various other aircraft and engine lease agreements which are not subject to the Scheme. To the extent that bilateral deals have been done with such other lessors, details of those deals were disclosed to Scheme Creditors via a dedicated Scheme website.

The impact of the COVID-19 pandemic

15. The outbreak of the COVID-19 pandemic in early 2020 has had an unprecedented impact on the Group's operations and the aviation industry in general. Together with a number of other factors, the extensive flight and travel restrictions, border controls and quarantine arrangements implemented around the world resulted in a precipitous drop in passenger demand for air travel and a surge in refunds due to flight cancellations. This has severely affected the Group's ability to generate sufficient cash for its working capital.

16. The Group carried over 12 million fewer passengers in 2020 than in 2019 and incurred a combined loss in the region of MYR 3.24 billion (approximately US$808 million) in the financial year ended 31 December 2020. Within the Group, the effects of COVID-19 have been most keenly felt by Malaysia Airlines, whose bookings fell by 76% in 2020 (compared to 2019). The Company's main source of revenue is from leasing aircraft and spare engines to Malaysia Airlines. If Malaysia Airlines is unable to recover from the impact of COVID-19 and to remain financially viable, the Company will also be unable to survive.

17. Although the Group has implemented a number of cost savings measures, it determined during the summer of 2020 that it would be necessary to implement a comprehensive restructuring of its financial obligations. To that end, commencing in September 2020, the Company began to formally engage with the Scheme Creditors and their advisers. The Scheme is the product of these discussions.

18. The Company invited the Scheme Creditors to sign a lock-up agreement to support the Scheme and the restructuring (the "Lock-Up Agreement"). All but one of the 44 Scheme Creditors (representing 95.9% of the Scheme Creditors by value) signed the Lock-Up Agreement prior to the Scheme Meeting. No fees or other benefits were available to signatories of the Lock-Up Agreement. At the sanction hearing I was also told that the final Scheme Creditor which did not vote in favour of the Scheme at the Scheme Meeting has since signed the Lock-Up Agreement.

The comparator to the Scheme

19. The evidence satisfies me that if the Scheme is not sanctioned by the Court, then the Company will run out of money immediately and would have no choice but to enter into liquidation, as would a number of other entities within the Group, including Malaysia Airlines.

20. In a liquidation, each of the Operating Lease Agreements would be terminated by the relevant Scheme Creditor (or otherwise disclaimed by the liquidator). This would give rise to an unsecured claim for damages against the Company. The Company retained AlixPartners which produced a detailed analysis of the returns that the Scheme Creditors would be likely to receive in a liquidation. Those returns are extremely poor. It is estimated that a liquidation of the Company would result in a total distribution to the Scheme Creditors within a range of 0.9-1.4% on their liquidation claims, increasing to a range of 3.7-6.4% when combined with recoveries against other Group companies.

The Scheme

21. The Scheme is itself very simple. It confers a power of attorney on the Company to enter into an "Override Agreement" on behalf of the Scheme Creditors. The Override Agreement contains the essential commercial terms of the compromise. This is a well-recognised structure: see Re ColourOz Investment 2 LLC [2020] BCC 926 at [74]-[75].

22. Within three business days of the Scheme becoming effective, the Scheme Creditors will be required to make an election between four options. To the extent that the Scheme Creditors have already communicated their elections to the Company, those elections will be accepted, unless superseded by a different election.

23. One of the options is a termination option. That option allows a Scheme Creditor to terminate its Operating Lease Agreement, recover its aircraft and receive a one-off payment (the "Termination Payment"). The amount of the Termination Payment will be 115% of (i) the amount the relevant Scheme Creditor would be entitled to claim from the Company in the event of a liquidation; multiplied by (ii) the upper end of the range of percentage of recovery in a liquidation of the Company (as calculated in the Alix Partners' Report).

24. If a Scheme Creditor does not wish to terminate its lease, then a different regime will apply. As a temporary measure, all such Scheme Creditors will be paid rent on a "power by the hour" basis ("PBH") during the calendar year 2021. This means that the rent during 2021 will be calculated by reference to the amount of time that each aircraft is used, subject to a floor and a cap. Following the market position, the rates and the floors and caps differ depending on the category of aircraft. The PBH structure is designed to reflect the fact that, during 2021, passenger demand will likely remain very depressed, the usage of the fleet of aircraft may be very limited indeed and it would be unaffordable for the Company to pay the contractual rates of rent for aircraft which are not being used.

25. The PBH structure will come to an end on 1 January 2022. For the period from 1 January 2022, the basic commercial deal involves the rent payable under the relevant Operating Lease Agreement being re-set to market rent. There are then variants of this basic deal available under which an enhanced rent, with a lease extension mechanism, is available in return for the Company having an option in certain circumstances to defer rent and pay an enhanced rent available depending on the Company's performance. There are default provisions which apply if the Scheme Creditor fails to make an election by the deadline.

The wider restructuring

26. As noted above, the Scheme forms part of a broader Restructuring of the Group's financial indebtedness. In brief summary, the Restructuring involves: (i) arrangements to defer principal payments and reduce interest payments under certain of the Group's finance lease agreements, as well as certain Malaysian law credit facilities and hedging agreements entered into by Malaysia Airlines; (ii) arrangements to amend certain of the Company's aircraft lease agreements (on terms similar to those proposed under the Scheme, but which will be implemented bilaterally with the relevant lessors); (iii) arrangements to amend the Group's engine lease agreements and maintenance and service contracts to align with market rates, the Group's cashflow requirements and its

revised long-term business plan; (iv) various arrangements with entities related to the Government of Malaysia; and (v) a substantial equity injection by KNB and the capitalisation of existing shareholder loans advanced by KNB.

27. The Scheme is inter-conditional with the wider Restructuring, and the Override Agreement will only become effective once the wider Restructuring has become effective. There is a "long-stop date" of 31 May 2021 by which (unless the date is extended) this must occur, failing which the terms of the Scheme will lapse and the original obligations of Scheme Creditors under the Operating Leases will remain in full force and effect.

The Scheme Meeting

28. The evidence shows that the Scheme Meeting was duly held without any technical difficulties and in accordance with the Convening Order on 10 February 2021. The Scheme was unanimously approved by the 43 Scheme Creditors who attended and voted at the Scheme Meeting. As indicated above, the turnout and vote in favour represented approximately 95.9% by value, with only one Scheme Creditor not attending or voting.

The approach to sanction

29. The principles that the Court applies when deciding whether to sanction a scheme of arrangement under Part 26 are well known. They were set out by David Richards J in Re Telewest Communications plc (No. 2) [2005] BCC 36 at [20]-[22] and have been applied countless times since. The relevant questions for the court at the sanction hearing can 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 scheme 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 "blot" (i.e. defect) in the scheme?

30. In addition to these questions, in the case of a scheme with international elements, the court should ask whether there is a sufficient connection with England to justify exercising the jurisdiction of the court to sanction the scheme. Relevant factors will include whether the scheme company has its centre of main interests (COMI), an establishment or substantial assets in England; or whether the debts to be compromised under the scheme are governed by English law. As a related question, the court should also consider the international effectiveness of the scheme. Relevant factors will include the level of creditor support for the scheme and expert evidence to provide some level of reassurance that the scheme is likely to be recognised and given effect by the courts in other relevant jurisdictions.

Application to this case

31. It is entirely clear that in this case the answer to the first three questions posed above is "yes". There has been no challenge to the decision of Zacaroli J to order a single class meeting of all Scheme Creditors, the Scheme Creditors were supplied with an explanatory statement in accordance with the CA 2006, the Scheme Meeting was held in accordance with the Convening Order and the Scheme was approved by an overwhelming majority of Scheme Creditors, far in excess of that required both in terms of number and value.

32. Given the very high turnout at the Scheme Meeting it is also obvious that the meeting was fairly representative of the class and there is nothing to suggest that those who voted in favour of the Scheme were doing so other than in good faith in the interests of the class. As there has been no suggestion that the Scheme Creditors were not properly consulted and informed by the explanatory statement, the overwhelming support for the Scheme means that I can confidently take the view that given that the Scheme Creditors are likely to be much the best judges of their own commercial interests, this is a scheme that an honest and intelligent creditor might reasonably approve.

33. Further, subject to the point concerning The Cape Town Convention to which I refer below, there is no suggestion of any blot or defect in the Scheme.

34. So far as sufficient connection is concerned, the liabilities under the Operating Leases are governed by English law, which has generally been regarded as providing such a connection: see e.g. Re Rodenstock GmbH [2011] Bus LR 1245 at [64]-[72] per Briggs J and Re Vietnam Shipbuilding Industry Group [2014] BCC 433 at [6]-[9] per David Richards J.

35. In relation to international effectiveness, the first – and in my mind decisive - point to note is that an overwhelming majority of the Scheme Creditors contractually agreed to support the Scheme by signing the Lock-Up Agreement and voted in favour of it. This very high level of creditor support provides good evidence both of the appropriateness of the involvement of the English court and the likelihood that the Scheme will have a substantial effect abroad. As I noted in Re KCA Deutag UK Finance plc [2020] EWHC 2977 (Ch) at [33]:

> "… 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."

36. That point has been further strengthened by the evidence from the Company shortly before the sanction hearing that the sole remaining Scheme Creditor that had not

previously signed the Lock-up Agreement or voted in favour of the Scheme had indicated that it consented to the Scheme and had signed the Lock-up Agreement.

37. For good measure, the Company also obtained persuasive expert evidence from Yow Pit Pin Jack, a Malaysian lawyer, to the effect that the Scheme is likely to be recognised in Malaysia, which is the key jurisdiction in which the Company operates.

The Cape Town Convention

38. The only real issue which might have required detailed consideration in this case is whether there was a "blot" or defect in the Scheme by reason of the impact of the Cape Town Convention and associated Protocol to the Cape Town Convention on matters specific to Aircraft Equipment (the "Aircraft Protocol"). The Cape Town Convention and Aircraft Protocol were ratified by the UK on 27 July 2015 and are given effect in UK law by the International Interests in Aircraft Equipment (Cape Town Convention) Regulations 2015 (SI 2015/912) (the "2015 Regulations").

39. All of the Operating Lease Agreements provide for the creation and registration of international interests in respect of the Operating Aircraft under the Cape Town Convention. In addition, the Operating Lease Agreements fall within the definition of an "agreement" under the Cape Town Convention.

40. Amongst other things, the Aircraft Protocol deals with the effect of an "insolvency-related event" on the parties to an "agreement" and the rights and remedies available to a relevant creditor in those circumstances. The term "insolvency-related event" is defined in Article I(2)(m) of the Aircraft Protocol as meaning:

> "(i) the commencement of insolvency proceedings; or
>
> (ii) the declared intention to suspend or actual suspension of payments by the debtor where the creditor's right to institute insolvency proceedings against the debtor or to exercise remedies under the Convention is prevented or suspended by law or State action."

41. The term "commencement of the insolvency proceedings" is defined as "the time at which the insolvency proceedings are deemed to commence under the applicable insolvency law": see Article 1(d) of the Cape Town Convention. The term "insolvency proceedings" is defined in Article 1(i) of the Cape Town Convention as follows:

> "bankruptcy, liquidation or other collective judicial or administrative proceedings, including interim proceedings, in which the assets and affairs of the debtor are subject to control or supervision by a court for the purposes of reorganisation or liquidation."

42. Article XI of the Aircraft Protocol identifies two options that Contracting States can elect to adopt to govern the rights and remedies available to creditors in circumstances of the debtor's insolvency (known as Alternative A and Alternative B). Article XI identifies a number of consequences that flow from an "insolvency-related event"

(depending on whether Alternative A or Alternative B is selected). Both Malaysia and the UK have adopted Alternative A.

43. The consequences of an insolvency-related event under Alternative A are set out in Articles XI(2) to XI(13) of the Aircraft Protocol. One such consequence is that under Article XI(10),

> "No obligations of the debtor under the agreement may be modified without the consent of the creditor."

44. Regulation 37 of the 2015 Regulations gives effect to Alternative A in the UK. Regulation 37 is largely identical to Articles XI(2) to XI(13) of the Aircraft Protocol. In particular, Regulation 37(9) is identical to Article XI(10).

45. The 2015 Regulations and the Cape Town Convention also include the same definition of an "insolvency-related event". It should, however, be noted that the 2015 Regulations contain a slightly different definition of the term "insolvency proceedings". Regulation 5 defines "insolvency proceedings" as:

> "liquidation, bankruptcy, sequestration or other collective judicial or administrative insolvency proceedings, including interim proceedings, in which the assets and affairs of the debtor are subject to control or supervision by a court (or liquidation committee)."

46. Although no Scheme Creditor in fact advanced such an argument in this case, it could be argued that the Scheme is an "insolvency-related event" and that it therefore cannot modify the obligations of the Company under the Operating Lease Agreements without the consent of each Scheme Creditor: see Regulation 37(9) (giving effect to Article XI(10)).

47. Plainly, even if applicable to the Scheme, this restriction could cause no difficulty as regards the 43 Scheme Creditors who expressly consented to the Scheme by signing the Lock-Up Agreement and voting in favour of it. However, until the very recent clarification of its position, a potential issue arose in relation to the sole Scheme Creditor which had not acceded to the Lock-Up Agreement and did not vote at the Scheme Meeting.

48. In his written submissions, Mr. Smith QC argued that I could simply take the pragmatic view that since the Scheme would be effective as against the vast majority of Scheme Creditors, the court would not be acting in vain if it sanctioned the Scheme, and that I need not concern myself about its effect against the one non-consenting creditor. For my part, I do not think that would have been a satisfactory approach. By its terms, the Scheme purported to bind the non-assenting creditor, and I believe that the court should be concerned whether it was right to give its sanction to a scheme which might be thought to breach an international convention to which the UK is a party.

49. As it is, however, the belated (but welcome) consent of the last remaining Scheme Creditor to the Scheme means that I do not need to resolve the issue of whether the Scheme is an "insolvency-related event" within the meaning of the Aircraft Protocol or the 2015 Regulations. Even if the Scheme were to be such an event, all Scheme

Creditors have consented to the modification of their rights. I am therefore content to leave resolution of the issue of whether a scheme under Part 26 CA 2006 falls within the definition of an "insolvency-related event" under the Aircraft Protocol or the 2015 Regulations to a case in which it matters.

50. I also note in that regard, that whilst fully supporting the Scheme in this case, Mr. Allison QC expressly reserved the position of his clients, as lessors, to argue in a future case that a scheme was such an "insolvency-related event".

Unanimous consent

51. The final issue arises out of the fact that as events have turned out, the Scheme is now supported by and consented to by all of the Scheme Creditors. The issue is whether I have jurisdiction to sanction, and should exercise my discretion to sanction, a scheme in such a case.

52. In Re Virgin Atlantic Airways Limited [2020] EWHC 2376 (CH) at [48], I commented,

> "Under Part 26, the court would not ordinarily entertain an application to convene scheme meetings or sanction a scheme of arrangement where it was known in advance that all creditors have consented or would be prepared to consent to a variation of their rights against the company. As such, although very high majorities are sometimes locked up in advance to support a scheme, it is not normal practice to include classes in a Part 26 scheme where 100% of the relevant creditors are known to be willing to consent."

53. The instant case is not the type of case which I had in mind in Virgin Atlantic. In particular, it was not known at the time of the convening hearing, or indeed until very shortly before the commencement of the sanction hearing, that 100% consent could be, or had been, obtained.

54. The question of whether the court would be deprived of jurisdiction or for some other reason should not exercise its discretion to sanction the scheme where 100% consent had been obtained was addressed in Re Dundee Pikco Limited [2020] EWHC 1059 (Ch) at [2]-[5]. In factual circumstances that were not dissimilar to the instant case, Zacaroli J accepted a submission that the requirement in Part 26 CA 2006 for creditor approval at scheme meetings was merely a minimum jurisdictional threshold. He also took the view that provided there was sufficient practical purpose in having a scheme, the court could consider whether to exercise its discretion in favour of sanction. In that regard, he observed, at [4],

> "In this case consent from the remaining three creditors has been received extremely late in the day. All the documents have been drafted on the basis that the restructuring would be effected by way of the scheme. Various steps provided for hereafter are formulated by reference to the scheme and to its sanction. If the court were not to sanction the scheme at this stage, then that would involve further work, delay and expense, in giving consideration to the mechanical changes that need to be made."

55. The same considerations all apply in the instant case. In particular, although in theory all 44 Scheme Creditors could now be approached and asked individually to execute the Override Agreement, that would obviously be time-consuming, incur further expense and could result in administrative difficulties and delays.

56. Given that all parties have proceeded thus far on the basis that there would be a scheme, I see no good reason at this very late stage to put the Company and its advisers to such a new task, or risk further delays given the pressing nature of its financial difficulties.

Conclusion

57. Accordingly, I shall sanction the Scheme and make an order in the form provided to me by the Company.