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English Court Crams Down Tax Authority in Prezzo's Restructuring Plan; Ability to Zero "Out of the Money" Classes

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At a Glance

The English court today handed down its [judgment](#) approving Prezzo's restructuring plan, notwithstanding a challenge from the tax authority, HMRC. This contrasts with the court declining to approve two recent midmarket restructuring plans following opposition from HMRC (namely *Nasmyth* and *GAS* – see our [Alert](#)).

In *Prezzo*, the court was satisfied that:

- the payment to be provided to HMRC under the plan (33.5% in respect of its preferential claims; zero in respect of its smaller unsecured claims) meant it would receive most, if not all, of the "restructuring surplus" generated by the plan;
- the allocation of benefits under the plan was fair;
- the plan was not being used by the company as an "instrument of abuse"; and
- approving the plan would not give a "green light" to companies to use restructuring plans to "cram down" their unpaid tax bills.

In contrast to HMRC's opposition on *Prezzo*, HMRC voted in favour of Fitness First's restructuring plan, which involved a five-month instalment plan for a historic VAT liability. The court approved Fitness First's plan on 29 June, binding dissenting landlord classes and despite opposition from certain landlords; judgment is awaited.

More generally: for the first time, the court in *Prezzo* held that it has jurisdiction to sanction a plan in which certain classes would receive no distribution under the plan

(because they would be completely “out of the money” in the relevant alternative and were “no worse off” under the plan).

Background

The principal terms of the restructuring plan were as follows.

<i>Class</i>	<i>Treatment under plan</i>	<i>Vote</i>
1. Senior secured loan noteholders (£24 million)	Principal and accrued interest to remain whole, with maturity date extended	Approved (100%)
2. HMRC, in its capacity as preferential creditor (c.£10 million)	To receive a cash payment equal to the value of the floating charge assets in the relevant alternative (namely, insolvent pre-packaged administration), less the estimated costs of the administration process, plus (following an amendment to the plan) an additional payment of £2 million	Rejected (100%)
3. Local authorities in respect of business rates and council tax for sustainable sites ¹	Payments due in May and June 2023 compromised in full (for no consideration), but no compromise in respect of payments from July 2023 onwards	Approved (80%)
4. Other unsecured creditors ²	Liabilities compromised/released in full for no consideration	Rejected (82%)

The current shareholders will remain, with no variation to their rights. The secured loan noteholders largely coincided with the shareholders; they had made substantial

contributions to the group including interim emergency funding and the additional £2 million to be paid to HMRC.

Judgment

The court found (and HMRC had accepted) that the statutory conditions to bind a dissenting class were satisfied – namely, no member of a dissenting class would be any worse off under the plan than in the relevant alternative, and an “in the money” class (here, the secured noteholders) had approved the plan.

Accordingly, the judgment principally focussed on whether the court should sanction the plan as a matter of its discretion.

Binding HMRC:

- The court paid “due regard to the fact that HMRC has objected to the Plan, and done so in strong terms, the fact that it is an involuntary creditor and the need for caution generally in considering the ‘cram-down’ of HMRC debts, as well as the preferential status afforded to the majority of those debts”. However, it was nevertheless satisfied that the allocation of benefits under the plan was fair.
- The court distinguished other cases in which the court had refused to bind HMRC as a dissenting class (namely, *Nasmyth* and *GAS*) on various bases, including that:
 - the proposed return to HMRC was higher in *Prezzo*, at 33.5% compared to 4.8% in *Nasmyth* and 9.1% in *GAS*;
 - the payment to be provided to HMRC meant it would receive most, if not all, of the “restructuring surplus” generated by the plan;
 - HMRC would be repaid quicker in *Prezzo* – within 30 days of the effective date, whilst in *GAS* payments would be made over two years;
 - *Prezzo* had procured a significant improvement for HMRC – an additional £2 million – from its secured loan noteholders/shareholders;
 - HMRC’s debt in *Prezzo* related to a much shorter and more recent period (April-June 2023) than in *Nasmyth*;
 - unlike *Nasmyth* and *GAS*, *Prezzo* had no history of broken time to pay arrangements with HMRC; and
 - certain creditors that *Prezzo* had continued to pay were truly critical to the preservation of its business, in contrast to the position in *Nasmyth*.

Jurisdiction to “zero” out-of-the-money classes:

The court held that the legislative requirement for a “compromise or arrangement” does not require out-of-the-money classes to be given any valuable compensation for the release or cancellation of their rights under the plan. Whilst some element of “give and take” is required in a conventional scheme of arrangement, the court held that this requirement does not apply in the context of a restructuring plan, owing to the court’s ability to approve a plan under which no member of a dissenting class is “worse off” than if the plan had not been sanctioned.

1. Namely, restaurants considered to be profitable and critical to the future operation of the business. ↩

2. Namely, landlords of loss-making sites, creditors in respect of deferred and exit consideration, local authorities in respect of loss-making sites and other unsecured creditors, including HMRC in respect of its non-preferential claims. ↩

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- 05 July 2023 Award Bankruptcy Tax Specialists in the Nation's Major Law Firms 2023
- 27 June 2023 Kirkland Alert UK Insolvency Service’s “Post-Implementation Review” of Restructuring Plans and Other Measures; Possible Refinements Ahead

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