SLAUGHTER AND MAY/

CINEWORLD: RESTRUCTURING GOES TO HOLLYWOOD

ACROSS BORDERS
Part of the Horizon Scanning series

Following its acquisition of the Regal cinema chain in the US in 2018, Cineworld, with its English-incorporated parent company, London premium listing and status as a household name in the UK cinema industry, became a truly transatlantic business. Add that to its businesses in Central and Eastern Europe and Israel, and Cineworld is one of the largest cinema chains in the world, operating in 10 countries with 672 sites and 8,181 screens. It is easy to see how the Cineworld restructuring, which kicked off following its chapter 11 filing in September 2022 and concluded in July 2023, became a blockbuster transaction.

For Slaughter and May, it was the latest significant cross-border chapter 11 case over recent years in which we have acted for the debtor (following the Seadrill chapter 11 cases between 2018 and 2022 and the 2021 Valaris restructuring under chapter 11), but the first where the company had a significant UK operating business and a London listing.

One of the fascinating aspects of this transaction was the interaction between the US chapter 11 process and the legal framework applicable to listed UK PLCs. And with the seemingly ever-increasing trend of UK and European companies looking to the US market for debt and equity financing, as well as the ongoing debate around the implementation of the UNCITRAL Model Laws, the international recognition of cross-border restructuring procedures and the application of the rule in Gibbs[1], the lessons learned about the interaction between the English and US regimes will likely serve as a guiding light for similar transactions in the future.

This piece provides an overview of the main takeaways and themes that we think will be relevant for any future transatlantic restructuring of this nature.

Overview of the Cineworld restructuring

On 7 September 2022, Cineworld, one of the largest cinema chains in the world, announced that group companies comprising its US, UK and Jersey businesses had commenced chapter 11 cases in the United States Bankruptcy Court for the Southern District of Texas, Houston Division. This paved the way for a comprehensive restructuring transaction that provided for, among other things, a significant deleveraging through the release of approximately $4.53 billion of funded debt and the injection of new liquidity through: (i) an $800 million capital raise; and (ii) new debt financing in the aggregate amount of approximately $1.71 billion. The restructuring completed, and Cineworld emerged from chapter 11, on 31 July 2023.

As part of the steps to implement the restructuring, Simon Appell, Catherine Williamson and Ian Partridge of AlixPartners UK LLP were appointed as joint administrators of Cineworld's ultimate parent company, Cineworld Group plc, and its business and assets were sold pursuant to a pre-packaged sale to a newly incorporated parent company owned and controlled by certain of Cineworld's lenders. Following the appointment of the joint administrators, Cineworld Group plc was delisted from the London Stock Exchange on 1 August 2023.

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[1] A rule based on English case law case that established that, under English law, where a contract specifies that it is governed by a particular country's law, it cannot be compromised or discharged by insolvency proceedings under a different law without the relevant creditor's consent.

Key takeaways and themes from the Cineworld restructuring

1. Chapter 11 is a more "inclusive" process than equivalent English processes, which requires extra consideration when managing relationships with UK counterparties

English restructurings implemented through a scheme of arrangement or a restructuring plan under Part 26 or Part 26A of the Companies Act 2006 tend to be focussed on particular categories of liability, such as financial liabilities or lease liabilities. English law also remains relatively permissive about leaving certain creditors unimpaired in a restructuring where it is commercially rational to exclude them. As a result, these tend to be targeted processes rather than collective proceedings that attempt to deal with all of the liabilities of a debtor company.

In contrast, the US Bankruptcy Code places broad restrictions on the payment of pre-chapter 11 petition debts without some kind of US Bankruptcy Court approval. To address this, it is typical to obtain initial US court approval for extensive "first day orders" that allow for the payment of pre-petition liabilities critical to the basic function of the debtor company's business. These orders usually apply to certain types of trade creditors only, and pre-petition lease liabilities will almost always be excluded (given that the US Bankruptcy Code has a separate process for addressing lease liabilities). The orders will also often impose additional procedural requirements that must be complied with before the creditor can be paid, such as the entry into a new trade agreement in a specified form.

In practice, while US counterparties may be familiar with these procedural hurdles, equivalent UK-based counterparties will likely require extra attention. This is especially the case given the propensity (particularly in the UK media) to compare chapter 11 with administration in the UK, the latter of which is often perceived as a "terminal" insolvency process or representing corporate failure rather than a restructuring procedure that results in the survival of the business. This can lead to confusion and, in extreme cases, counterparties taking adverse action, such as filing winding-up petitions in England, in the misapprehension that doing so is necessary to protect their position. We found that a clear communications strategy was key to helping counterparties understand that, notwithstanding the need to jump through some extra hoops, it was still business as usual for Cineworld during the chapter 11 cases. These considerations will also feed into the strategy with respect to proactive or reactive recognition and parallel implementation of the US process in England (as to which, see further below).

2. The ability to raise rescue finance in the US through a court approved "debtor in possession facility" is a powerful tool for distressed companies

In the English law financing market, the contract is king. It is generally impossible to override key terms like negative pledge clauses or to subordinate a pre-existing secured creditor without creditors' consent or the use of a formal restructuring procedure, such as a Part 26A restructuring plan. This means that companies with significant liquidity constraints will be at the mercy of their existing creditors when seeking to put in place new financing as a bridge towards a more comprehensive restructuring transaction. As such, there will often be a risk that there may not be time to obtain the consents, or to develop and implement a Part 26A restructuring plan, in order to allow new debt financing to come in before the company is forecast to run out of cash. Accordingly, the ability under chapter 11 to put in place a new secured facility ranking ahead of existing secured debt with US court approval can (together with the chapter 11 automatic stay) be the difference between providing a period of stability to lead to a successful restructuring and one that fails to get off the ground in the first place. In Cineworld's case, the approximately $1.94 billion debtor in possession financing facility provided in connection with its chapter 11 filing was key to ensuring that it had sufficient liquidity to negotiate and implement its restructuring as well as to continue operating its global business as usual throughout its chapter 11 cases.

3. Chapter 11 requires extensive disclosure by the debtor company, which has to be followed alongside UK disclosure regimes

Chapter 11 has its own transparency and disclosure framework that is designed to ensure that all stakeholders are aware of the key terms and milestones in relation to the restructuring process. Nevertheless, UK laws and regulations, such as under the Companies Act 2006, the Listing Rules and the UK Market Abuse Regulation, will continue to apply to

English companies falling within the purview of those regimes that are pursuing a restructuring through chapter 11. This means that disclosure through RNS announcements and the publication of financial statements may still be required alongside disclosure through the chapter 11 process. This will likely require careful management to ensure compliance with both regimes, particularly given their differing requirements and the contrasting style and content of US and UK disclosures. This can also lead to uncommon situations, such as where Cineworld's Board was required under section 656 of the Companies Act 2006 (which applies where a company has experienced a serious loss of capital) to call a general meeting to consider any steps required to address its situation, even after it had disclosed to the market already that there was not expected to be any recovery for shareholders.

4. Parallel implementation processes are likely to be required since chapter 11 does not override UK corporate law and regulation

When it comes to implementing a restructuring transaction, the US Bankruptcy Code allows for a chapter 11 plan of reorganisation to supersede all other consents and process requirements that would otherwise apply under US law. However, for an English public company, due to the requirements pursuant to the Companies Act 2006 and (where applicable) the Listing Rules, an issuance of shares to lenders as part of a debt for equity swap will require either shareholder consent or some other legal process to be implemented in parallel with the chapter 11 case, such as a Part 26A restructuring plan or a pre-pack administration.

As the legislation is presently drafted, a Part 26A restructuring plan cannot override Listing Rule 9.3.11R, which requires any issue of shares for cash to be made on a pre-emptive basis. In practice, this means that shareholder consent will almost always be required in respect of the issuance of shares to creditors of LSE-listed companies as part of a debt for equity transaction (unless the company can satisfy the FCA that it meets the conditions in Listing Rule 5.2.7R in relation to a cancellation of its listing due to severe financial difficulty, which is a high bar).

As other similar cases in the market have shown, it may not be commercially feasible to obtain shareholder consent to a debt for equity restructuring, particularly if shareholders are to make minimal or no recovery (the latter of which was the case with Cineworld). It was these sorts of considerations that led Cineworld and Valaris, another group with an English-incorporated parent advised by Slaughter and May that pursued a chapter 11 restructuring, to implement their restructurings in England through pre-pack administration processes.

The need to undertake a parallel process in England may also provide the opportunity to address other English law arrangements, such as leases and other operational liabilities. Detailed consideration of the choreography, and timing, of the effectiveness of the chapter 11 plan and any parallel English process will be key to ensuring the smooth implementation of the transaction.

Slaughter and May worked as part of an integrated team with Cineworld's in-house legal team, led by Nigel Kravitz, and Kirkland & Ellis LLP. PJT Partners, Inc. acted as financial adviser to Cineworld in connection with the restructuring and AlixPartners LLP acted as restructuring adviser. Ashurst LLP and Kramer Levin Naftalis & Frankel LLP acted as independent counsel to the Board of Cineworld Group plc (in relation to English and US law respectively).

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