CVAS
KEY CASES OF 2021

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With the commercial property market being crippled by the effects of the pandemic, coupled with the pre-pandemic pressures already facing retailers, 'landlord only' CVAs have become (and look set to continue to be) an increasingly popular method of restructuring distressed retail businesses. Conjunctively, impaired landlords have galvanised to challenge such CVAs.

In this article we explore the three high-profile retail tenant cases of 2021, providing long-awaited guidance on the legality and fairness of their use by distressed retailers.

NEW LOOK

The challenge:

- The CVA was not an "arrangement" as envisaged under the Insolvency Act 1986 (the Act) because it involved separate arrangements on substantially different terms with different creditor groups and the termination right granted to New Look improperly interfered with the landlords' proprietary rights.
- It is unfairly prejudicial to compromise the claims of sub-groups of creditors where the CVA is approved by the votes of unimpaired creditors (including secured creditors). Moving to turnover rents, the 3-year rent concession period and the release of 'keep-open' covenants was unfairly prejudicial.
- There were inaccuracies in the CVA proposal and the calculation of landlords' claims for voting purposes was disputed.

The finding (in dismissing the challenge):

- Differential creditor treatment is within the scope of the Act and is not necessarily unfairly prejudicial.
- The CVA did not compromise proprietary rights; landlords were given the opportunity to surrender the lease but were not required to do so.
- Although relevant when assessing unfair prejudice, a CVA approved by the votes of unimpaired creditors is not necessarily unfairly prejudicial.
- Where a CVA reduces rent payable to landlords to below market rent, this will not necessarily lead to a finding of unfair prejudice. No rigid test exists requiring rent reductions to be to the minimum extent possible, particularly where landlords can terminate the lease under the CVA.
- Fairness is fact-specific. Assuming the 'vertical' test of fairness is satisfied (i.e. the CVA will achieve a better outcome for creditors than the relevant alternatives), without setting an all-encompassing test, the judge noted some relevant factors such as (i) whether there is a fair allocation of assets between compromised

creditors and other sub-groups and (ii) the nature and extent of, and justification for, differential treatment, and its impact on the outcome of the meeting.

- The 25% discount applied to landlords' claims for voting purposes was justified, being a reasonable method of estimating a minimum value.
- Non-disclosure will constitute a material irregularity if there was a substantial chance that the undisclosed material would have affected how creditors voted. On the facts, there had been sufficient disclosure.

REGIS

The CVA was approved in October 2018, relying partly on votes from Regis' parent company (IBL) and former parent company (Corp) whose claims were unimpaired under the CVA.

The challenge:

- Preferential treatment of IBL and Corp was unfairly prejudicial.
- Material irregularity on the basis that antecedent transactions were insufficiently disclosed, rent claims were discounted by 75% for voting purposes and the proposal incorrectly identified the relevant vertical comparator as a Regis shut-down (rather than the sale of the business through an administration process).
- Considering the above, the Nominees breached their duties by promoting the CVA and should repay their fees.

The finding (in upholding the challenge based on a single limited ground):

- Based on contemporaneous evidence, no evidence justified classifying IBL as a "critical creditor" and its preferential treatment unfairly prejudiced impaired creditors. But for the CVA, IBL would have recovered nothing.
- Applying principles established in previous case law and New Look to the particular facts, the judge rejected the remaining grounds.
- Although the Nominees fell below the required standard by failing to objectively ascertain the treatment of critical creditors, the Nominees did not have to repay his fees (an order which the judge held should be limited to egregious conduct).

CAFFÉ NERO

The day before the CVA voting deadline, EG Group (EG) offered to acquire Caffé Nero's parent company and pay all landlords' rent arrears in full provided the CVA's terms were modified and the meeting postponed.

The offer was rejected. However, the CVA was modified to include a provision that if the company was sold to EG within 6 months, the company would use its best endeavours to procure that landlords receive rent arrears in full.

The challenge (by a single landlord funded by EG):

- The above events constituted material irregularities and unfairly prejudiced his interests.
- The CVA vote should have been postponed to allow for proper consideration of the offer.
- The last-minute CVA modification was invalid as most creditors had already cast their votes.
- The offer meant that the relevant comparator shifted from an administration to a transaction where landlords would receive payment of rent arrears in full.

The finding (in dismissing the challenge):

- The Act provides no clear route to postpone the electronic decision procedure and, given the timing, there was no time to apply to the court for relief.
- The Nominees complied with their duties; EG's offer was speculative, uncertain and did not justify a delay which would increase risk of administration.
- Where CVA modifications are proposed before the end of the electronic voting period, votes already received in favour may, in certain circumstances, be counted in favour of the proposal as modified.

KEY TAKEAWAYS

Whilst positive news for retail tenants seeking much needed restructuring to their premises portfolios following the pandemic, the recent cases tell a disappointing story for landlord applicants. Although fact-specific, recent judgments clarify the parameters for bringing a challenge, the courts' approach to assessing "fairness" and give some indication of what may constitute a material irregularity. It is clear that CVAs can treat different categories of creditors differently to deliver a sustainable outcome for the CVA company.

With corporate insolvencies rising and the retail sector continuing to face revenue pressure, the use of 'landlord only' CVAs shows no sign of slowing and may pick up pace as we near March 2022 when the moratorium on enforcing rent arrears comes to an end.

Case Citations:

(1) Lazari Properties 2 Limited, (2) The Trafford Centre Limited, (3) LS Bracknell Limited and 10 Others and (4) Fort Kinnaird Nominee Limited and 20 Others v (1) New Look Retailers Limited, (2) Daniel Francis Butters and (3) Robert Scott Fishman [2021] EWHC 1209 (Ch)

Carroway Guildford (Nominee A) Limited and 18 others and (1) Regis UK Limited, (2) Edward Williams (as Joint Supervisor of Regis UK Ltd) and (3) Christine Mary Laverty (as Joint Supervisor of Regis UK Ltd) [2021] EWHC 1294 (Ch)

Young v Nero Holdings Ltd [2021] EWHC 2600 (Ch)