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How Do the Recent Company Voluntary Arrangement (CVA) Challenge Decisions in New Look and Regis Impact UK Insolvency Practitioners?

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For the most part, the outcome of the *New Look* and *Regis* CVA challenge cases impact the company subject to the CVA and the creditors bound by it, far more than they impact the insolvency practitioners (IPs) acting as nominee or supervisor.

However, given that part of the recent challenge cases has involved claims that might see the IP having to repay their nominee and/or supervisor fees, and claims against them for breach of duty, both the outcome in *New Look*, but more so *Regis*, give some comfort and guidance to IPs acting in that role about what their responsibilities are and whether, if a CVA is challenged, they will have to repay their fees.

This alert sets out the points of note from those decisions, including how the findings in the cases might influence the drafting of future proposals.

Post-pandemic CVA Terms

The findings in *New Look* and *Regis* highlight that the key to mitigating the (un)fairness of modified lease terms will be the ability of the landlord to terminate the lease.

The following are the key drafting points to note from the cases:

- **Modification of lease terms** – it is not inherently unfair to modify any (non-proprietary) lease terms and it is for a landlord to assess at the outset whether it thinks the modified term is acceptable to it, not the court. That is, assuming that the CVA gives the landlord a right to terminate the lease and, therefore, a choice as to whether to continue the lease or terminate it.
- **Market rent** – it is not inherently unfair if a CVA reduces rent below market rent, including during the notice termination period provided the vertical comparator test is met.
- **Turnover rent** – switching contractual rent to turnover rent is likely to be increasingly more common. It is not inherently unfair for a CVA to propose turnover rents, provided, again, that the vertical comparator test is met and the landlord is given a right to terminate.
- **Nil rent provisions** – an option to terminate is also key here. If a landlord has the option to terminate (and, therefore, a choice whether to accept this modification) a provision that releases the company from all of its obligations, including an obligation to pay rent, is not inherently unfair.
- **Company's right to terminate** – if the company is granted a new right to terminate, the effect of which (usually) reduces rent to nil, then again, if the landlord has a right to terminate, such a provision is not inherently unfair.
- **90 days' notice periods** – even if a landlord cannot find a new tenant or re-let within the initial termination period that is not to say that a landlord should be given longer or this period is unfair if what is offered to a landlord meets the vertical comparator test.
- **Rolling right to terminate** – when offering a right to terminate, it does not need to be a rolling right. There may be reason not to do so, such as business continuity. A landlord has to assess at the outset whether it is willing to continue the lease in the absence of such a provision.
- **Multiple leases** – given the focus on the importance of termination rights, we would expect future CVAs to give landlords the option of selecting which of its properties it wishes to take back, rather than, as has been the case, and option to terminate all or none.
- **Profit share fund** – there is not a requirement to include one, but it may address the question of fairness when considering the horizontal comparator test.
- **Termination rights** – for the most part, giving a landlord the opportunity and choice to decide whether to terminate the lease balances the perceived unfairness of the proposed rent reductions and lease modifications, provided that, on exercising the right to terminate, the landlord would be no worse off than in the relevant comparator.

Voting

Discounting of Landlord Claims for Voting Purposes

It is usual for a landlord's claim for voting to be valued based on a formula that applies certain assumptions, for example, in relation to re-letting and void periods. It is also usual for a discount to be applied to the claim, usually between 25-75%, to arrive at the "estimated minimum value" of the landlord's claim.

In *New Look,* a 25% blanket discount was justified, in *Regis* a 75% discount was not. The primary difference was that in *New Look,* each of the landlord's claims had been estimated according to the specific circumstances of the lease before the discount was applied, unlike in *Regis*. Therefore, what we could expect to see in the future (which has been the approach in 'newer' CVAs) is a move away from a broad brush formula to a more focused one, to justify the percentage discount.

New Look confirms there is not a hard and fast rule when it comes to what an appropriate discount is, save that, the bigger the discount, the more that it will need to be justified. The fact that the same discount has been used in other CVAs is irrelevant. It is also likely to be irrelevant, as it was in *Regis,* that the British Property Federation did not object to the discount or that the chair's decision was not appealed.

That said, if a different discount is applied, it will apply to all claims and therefore make no material difference to the outcome of the meeting. Similarly, if, despite applying a different formula there would have been no impact on the outcome of the meeting, any irregularity in the way that the landlords' claims have been valued is unlikely to be a material irregularity or unfairly prejudicial.

What is clear is this:

- A landlord's claim is treated for voting purposes as unliquidated and unascertained
- The starting point is that the claim for future rent is valued at £1 unless the chair decides to put a higher value on it
- The duty of the chair is to consider the available evidence and, if that evidence leads to the conclusion that they can safely attribute to the claim an estimated minimum value, they must do so

Using a formula to calculate claims is acceptable, provided that if a landlord thinks their claim should be valued at a higher amount and produces evidence to support their position, the chair should consider that and value the landlord's claim accordingly.

Counting the Unimpaired Creditor Votes

One of the primary grounds of challenge in *New Look*, was that unimpaired creditor claims should not be counted towards the vote. The decision confirms that unimpaired creditor claims should be counted, but if the CVA is approved as a consequence of the votes of unimpaired creditors voting in favour, that will be a highly relevant factor in determining whether there is unfair prejudice.

For IPs, they should count unimpaired creditor votes and those from creditors who are treated differently under the terms of the CVA, but if the CVA is approved because "a large swathe" of unimpaired creditors vote in favour, this may give rise to a challenge based on unfair prejudice.

If the CVA is approved by the votes of unimpaired creditors, the court will consider all of the circumstances to determine whether there is unfair prejudice (it is not enough that differential treatment is justified and the vertical comparator test met), including (but not limited to):

- The circumstances that would be taken into account in exercising the discretion to sanction a scheme
- The circumstances that would be taken into account when exercising the discretion to cram-down a class in a Part 26A plan
- Whether there is a fair allocation of the assets available within the CVA between the compromised creditors and other sub-groups of creditors
- The nature and extent of any different treatment, the justification for that treatment and its impact on the outcome of the meeting
- The extent to which others in the same position as the objecting creditors approved the CVA]

The Position of the IP

Nominee's Duties

An IP is required to exercise professional independent judgment in deciding whether a proposal is feasible, and should make such enquiries as they deem necessary to satisfy themselves that the proposal should be put to creditors.

The Judge in *Regis* commented that for CVAs involving small companies and uncomplicated arrangements, cost and time constraints will be important factors in limiting the work of a nominee. But, where a CVA is used by a large company to implement a complex arrangement of the kind typically implemented via a scheme of arrangement, then more should be expected of the nominee.

It is often the case that an IP will have advised a company pre-CVA and it is important that the nominee retains clear independence when reporting to the court on the proposal and their duties as nominee will be viewed in the context of their prior engagement with the company.

It is fair to say that the more complex the restructuring the more that is expected of the nominee in complying with their duties.

Risk To Fees

There is no statutory control over a nominee or supervisors' fees, which are agreed with the company. In both *New Look* and *Regis*, the landlords sought an order (consequential upon a finding of material irregularity or unfair prejudice) that the IP should repay their nominee and/or supervisor fees.

The Judge in *Regis* commented, *"that one would not expect a professional person acting in the course of their professional duties to be charged with the costs arising out of that exercise"*.

Although, not ruling out the possibility that there may be situations where a nominee should repay their fees, and noting that the court has power to make such an order, IPs can take comfort from *Regis* that it is extremely unlikely that they will be ordered to repay fees where the IP has acted in good faith (and absent any fraud).

Disclosure

Both *New Look* and *Regis* asserted that there was material irregularity because the proposal failed to provide adequate disclosure, neither challenge succeeded.

Non-disclosure will constitute a material irregularity only if there is a substantial chance that the non-disclosed material would have made a difference to the way in which creditors voted at the meeting.

How much is sufficient information? Although the answer to this is fact specific and will depend on the case an IP should consider, are the creditors being told enough to make an informed decision? They should be given enough detail to allow them to make a further enquiry if they think that the answer is relevant to their decision, whether to support the CVA or not. There are some additional pointers in *New Look* about disclosure:

- Where there is a wider restructuring, it is necessary to view the CVA and the information provided in the CVA in that context
- The position of equity stakeholders is a matter of considerable interest to compromised creditors
- It will always be relevant to know whether anyone promoting a CVA has a particular incentive to do so

Signing the Report

An interesting observation from *Regis* is that the judge made no findings in respect of the joint nominee, noting that they had *"played no active role in the preparation for the CVA"* and that although the report was signed on behalf of both nominees, it was only signed by one.

It is quite usual on a joint appointment for one office holder to play a more active role, but given the Judge's comments in *Regis,* IPs might wish to consider whether, where liability is joint and several, both IPs should sign the report?

Summary

There are some helpful observations in both *New Look* and *Regis* about the role and conduct of an IP and we can expect the shape of future CVAs to be moulded around the findings in those cases. It should be noted that *New Look* is subject to appeal and IPs should be mindful that the observations and comments above may alter if the court of appeal comes to any different conclusions.

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