Neutral Citation Number: [2021] EWHC 1209 (Ch)

**Case No: CR-2020-003558**

**IN THE HIGH COURT OF JUSTICE**
**BUSINESS AND PROPERTY COURTS OF ENGLAND AND WALES**
**INSOLVENCY AND COMPANIES LIST (ChD)**

7 Rolls Building
Fetter Lane
London EC4A 1NL

Date: 10th May 2021

**Before**:

**MR JUSTICE ZACAROLI**

**Between:**

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| **(1) LAZARI PROPERTIES 2 LIMITED**<br>**(2) THE TRAFFORD CENTRE LIMITED**<br>**(3) LS BRACKNELL LIMITED AND 10 OTHERS**<br>**(4) FORT KINNAIRD NOMINEE LIMITED AND 20 OTHERS** | **Applicants** |
| **- and -** | |
| **(1) NEW LOOK RETAILERS LIMITED**<br>**(2) DANIEL FRANCIS BUTTERS**<br>**(3) ROBERT SCOTT FISHMAN** | **Respondents** |

**Peter Arden QC and Ben Shaw** (instructed by **Hogan Lovells International LLP**) for the **Applicants**
**Tom Smith QC and Adam Al-Attar** (instructed by **Latham & Watkins (London) LLP**) for the **Respondents**

Hearing dates: 17, 18, 19, 22, 23 & 24 March 2021

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**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 10.00 am on 10 May 2021.

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MR JUSTICE ZACAROLI

**Mr Justice Zacaroli:**

A: Introduction

1. This case concerns a company voluntary arrangement ("CVA") under Part 1 of the Insolvency Act 1986 ("IA 1986") which, among other things, seeks to impose rent reductions on landlords of a company operating in the retail sector.

2. There have been a number of CVAs in recent years of companies operating in the retail sector seeking to do the same, but only one in which a challenge by landlords to the CVA has reached a conclusion in court: *Discovery (Northampton Limited) v Debenhams Retail Limited* [2019] EWHC 2441 (Ch) ("*Debenhams*").

3. The trial in this case took place a week after a trial in respect of the challenge by landlords to a CVA for another retail company, Regis UK Limited ("Regis"). The same solicitors and counsel appeared for the landlords in the Regis case as in this one. Counsel for the respondents in each case were permitted to attend and observe the trial in the other matter. Although all parties were content for a single judgment to be produced covering both cases, in the event I have decided not to delay judgment in this case (where the CVA is continuing) while completing my consideration of the Regis case (where the CVA has long ago terminated). A judgment in the Regis case will follow shortly.

B: Background

4. New Look Retailers Limited ("New Look") is the principal operating company in the New Look group (the "Group"), which operates a retail, clothing, footwear and accessories business. As at August 2020 New Look operated from over 400 stores in the UK and employed over 10,000 people.

5. Like many businesses in the retail sector, New Look has suffered enormously as a result of the COVID-19 pandemic. During March 2020, the Group experienced a decline in like for like sales compared to the prior year of 32%. On 23 March 2020, the start of the first national lockdown, the Group's revenue from its stores fell to nil. The Group continued to trade through its e-commerce channels, and began a phased re-opening of stores on 1 June 2020. Stores were closed again as a result of the second and third national lockdowns.

6. At the start of the pandemic it ceased to pay rent and service charge to its many landlords. Upon the re-opening of its stores it paid a contribution to the rent payments due on a turnover basis.

7. By August 2020 it was clear that the Group could not continue to trade without a major restructuring of its liabilities. New Look's principal liabilities were as follows:

(1) It was borrower under a £100 million revolving credit facility ("RCF") which was fully drawn;

(2) It was borrower under a £65 million trade finance facility agreement ("TFFA"), under which £54 million was outstanding;

(3) It was guarantor of two series of senior secured notes due 3 May 2024 (the "SSN") issued by another group company, New Look Financing Plc ("NLF"), under which £441 million was owing;

(4) The liabilities under the RCF, TFFA and SSN were secured by a debenture over the assets and business of New Look. Under an intercreditor deed, the RCF and TFFA had priority over the SSN;

(5) Apart from its liabilities to suppliers, employees and ongoing trade creditors, New Look's other significant liabilities were its obligations to pay rent, service charge and other amounts under numerous long-term leases of its stores.

8. The directors believed that the effect of the pandemic on the retail sector would be long lasting. They concluded that New Look could not survive without a restructuring which addressed both its financial obligations and reduced its long-term rent obligations.

9. New Look's immediate problem was that it was projected to run out of cash by October 2020. It is common ground that in the absence of a restructuring it would be forced into administration, the most likely scenario being a short period of marketing the business with a "pre-pack" sale upon the appointment of administrators. In that event, there would have been no assets available for distribution to the unsecured creditors other than the prescribed part under section 176A IA 1986, which is set at a maximum sum of £600,000. This would have resulted in a dividend to unsecured creditors of 0.1p/£.

10. The restructuring involved the following elements:

(1) An extension of the term of the RCF and TFFA from 25 June 2021 to 30 June 2024, and certain amendments to the terms of the RCF, by agreement with the relevant creditors;

(2) A scheme of arrangement (the "Scheme") between NLF and the holders of the SSN (the "SSN Holders"), under which:

(a) the SSN Holders released all claims against NLF and against New Look (as guarantor) in return for participation rights in (i) 20% of the equity of New Look Retail Holdings Limited (the "Parent") and (ii) a subordinated shareholder £40 million loan to an intermediate holding company ("Midco") on a cashless basis; and

(b) SSN Holders were entitled to participate pro rata in a new £40 million term loan to Midco (the "New Money Loan") in return for a pro rata share in 80% of the equity in the Parent.

(3) a CVA of New Look (the details of which are set out below) principally in order to amend the terms of leases with those landlords who did not opt to terminate their lease(s) with New Look, so as to provide for reduced rental payments going forward and other amendments to the leases.

11. The proposal for the CVA was dated 26 August 2020 (the "Proposal"). It was sent to all creditors of New Look. The meeting of creditors took place on 15 September 2020, at which the CVA was approved by a majority of 81.6% by value of those attending and voting.

12. On 13 August 2020 New Look, NLF and various other companies in the Group entered into a lock up agreement (the "LUA") with the majority of the Group's secured lenders (including the creditors under the RCF, TFFA and many of the SSN Holders). By the time of the CVA meeting in excess of 93% of the SSN Holders had acceded to the LUA. This obliged them to support the wider restructuring, including the CVA.

13. The Scheme procedure was commenced by the sending of a letter to Scheme creditors pursuant to the Practice Statement issued by the Chancellor of the High Court dated 26 June 2020. On 23 September 2020 Miles J ordered that a single meeting of SSN Holders be convened to consider the Scheme. That meeting took place on 16 October 2020. It was attended (in person or by proxy) by SSN Holders holding 98.27% by value of the SSN, who all voted in favour of the Scheme. I sanctioned the Scheme at a hearing on 23 October 2020.

14. Although the CVA (which came first) and the Scheme were separate processes, they were closely linked. It was a condition to the extension of the RCF and TFFA and a condition to the provision of the New Money Loan that the CVA was approved and had not been challenged within the time required by the Insolvency Rules 2016 ("IR 2016") (although that condition was subsequently waived). More importantly, it is quite clear that had the CVA not been approved the Scheme would not have gone ahead. The amount of the New Money Loan had been calculated by reference to the cash needs of New Look on the basis of the reduced rent burden which the CVA was designed to achieve. Without that reduction, there would have been no reason for the RCF and TFFA lenders to agree to an extension of the facilities, or for the New Money Loan to be advanced. Conversely, reflecting the fact that if the facilities were not extended, or the New Money Loan not provided, clause 45.1(a) of the Proposal provided that if there was a challenge to the CVA that had not been dismissed, or if the wider restructuring was not completed by 31 January 2021, the Supervisors of the CVA had the power to terminate the CVA.

C: The terms of the CVA

15. The Proposal divides New Look's creditors into numerous different categories, as follows.

*Category A (Landlords)*

16. Category A comprises two landlords of New Look's distribution centre at Newcastle under Lyme. The directors considered the leases of the distribution centre to be critical to the Group's continued operations.

17. The Category A landlords' rights are unimpaired by the CVA except that: (1) the timing of payments of rent is changed from quarterly to monthly; and (2) the Category A landlords waived and release any claims resulting either from New Look's failure to pay amounts due before the "Effective Date" (meaning the date on which the CVA was approved) or from a "CVA Related Event" (in essence, the promotion and coming into effect of the CVA and any cross-default arising in consequence).

*Category B (Landlords)*

18. Category B comprises landlords of stores described (at paragraphs 6.4 to 6.12 of section 2 of the Proposal) as stores where the property costs were above market or were moving to a rent based on a percentage of turnover was necessary to assist cash-flow and make these stores viable following the COVID-19 Pandemic, and to appropriately share risk and rewards between New Look and the relevant landlords.

19. For all Category B landlords, all claims for rent arrears were released in full. They were entitled to receive, however, payment of arrears of service charge and insurance in full, payment in respect of dilapidations claims at 2% of the "Dilapidations Allowance", defined as a fixed amount per square foot of the premises (if termination occurred during the Rent Concession Period, but not thereafter), and a pro rata share of a fund of £600,000 set aside to meet claims which closely mirrored the claim a landlord would have upon disclaimer of the lease by a liquidator ("Disclaimer Damages", by reference to a formula set out in Schedule 2 to the Proposal).

20. Going forward, New Look's contractual obligation to pay rent was replaced with an obligation to pay turnover rent (monthly in arrears) based on a fixed percentage of net sales during the "Rent Concession Period", defined as the earlier of three years from the Effective Date, or the termination of the lease (the "CVA Turnover Rent").

21. Each landlord had the option, however, to terminate the relevant lease(s) on or before an Initial Break Date (150 days after the Effective Date), by giving not less than 60 days' prior notice. They had further termination rights exercisable on the first or second anniversary of the Initial Break Date and on the Final Break Date (the day before the third anniversary of the Effective Date).

22. The fixed percentage of net sales by which CVA Turnover Rent is calculated varies as between nine sub-categories of Category B landlords, ranging from 12% for Category B1 to 2% for Category B9.

23. In the second year of the Rent Concession Period, the landlords are entitled to a minimum of 85% of the CVA Turnover Rent paid in the first year. A similar minimum rent for the third year is set by reference to the CVA Turnover Rent in the second year.

24. After the end of the Rent Concession Period, all Category B landlords are entitled to receive the higher of the CVA Turnover Rent and market rent (either agreed or determined by an expert) until the termination of the relevant lease.

25. New Look was itself provided with a new "termination right" by giving notice not more than 90 days and not less than 60 days before the Final Break Date, if net sales for the premises have not returned to 85% of the net sales in the year immediately before the Pandemic or the market rent has not been agreed or determined for the remainder of the lease. The effect of such a termination notice would be that New Look offers to relinquish any right of occupation (though the relevant landlord is not obliged to accept that offer) and New Look is released from all liabilities in respect of rent, service charge, insurance and all other covenants under the lease.

*Category C (Landlords)*

26. Category C comprises landlords of stores described as those which New Look has already vacated, or would be vacating, because they were significantly underperforming and were considered to have no prospect of being restored to viability.

27. For Category C landlords, arrears of rent were compromised in full. After the Effective Date, they were entitled to receive rent, service charge and insurance payments at the contractual rate for two months, after which they ceased to be entitled to any rent or service charge. The landlords are entitled to contractual amounts due in respect of insurance for such period as New Look remains in occupation of the premises, and are entitled to a pro rata share, alongside the Category B landlords, in the fund of £600,000 for a Disclaimer Damages claim.

28. Category C landlords are granted a new right to terminate the lease at any time after the Effective Date by giving not less than 60 days' notice. New Look is also granted a new right to terminate the lease on 60 days' notice provided that the notice period expires within the Rent Concession Period. The effect of such a notice is the same as for the termination notice served by New Look upon Category B landlords.

29. I shall refer to the Category B and C Landlords as the "Compromised Landlords".

*Category D (Agreement for a lease)*

30. Category D comprises an agreement for a lease relating to a store that was under development. The landlord would become a Category B landlord upon either New Look taking possession or signing the lease.

*Categories E, F, G, H, I and J*

31. The claims of all creditors in Categories E, F, G, H, I and J are released in return for an entitlement to a distribution of 2% on Allowed CVA Claims.

32. Category E comprises creditors in respect of guarantees given by New Look in respect of leases entered into by other entities. Category F comprises creditors with claims (totalling £1.1 million) deemed to be non-critical to the success of the CVA. Category G consists of intra-group claims. Category H comprises certain contingent liabilities under, for example, previous or terminated leases. Category I comprises rates due to certain (but not all) rating authorities. Category J comprises historic dilapidations claims.

*Category K (SSN Holders)*

33. Category K comprises the SSN Holders. Clause 21.2 of the Proposal provides that they will be compromised by the Scheme and that, aside from the fact that they are prevented from exercising any termination and other rights triggered by a CVA Related Event, the CVA shall not affect their rights.

*Category L (Former employees)*

34. Category L comprises former employees of New Look. Their claims are released in exchange for a distribution of 2% on CVA Allowed Claims (except that certain redundancy claims were paid in full).

*Ordinary Unsecured Creditors*

35. Ordinary Unsecured Creditors (defined as any creditor to whom a liability is owed other than a secured creditor, a preferential creditor, a Category A Landlord, a Compromised CVA Creditor or a Contingent Property Creditor) are unaffected by the CVA, save that they are prevented from (if they otherwise could) exercising termination rights triggered by a CVA Related Event.

36. The Ordinary Unsecured Creditors are listed at Schedule 19 to the Proposal. The aggregate amount of their claims was stated to be approximately £72.7 million.

37. Included within Ordinary Unsecured Creditors are claims of current employees, with a value of £10,682,978.

38. At paragraph 3.20 of the Summary of the Proposal, it is stated that "certain" of the Ordinary Unsecured Creditors (including suppliers), as well as the Hedge Creditors and certain employees will not have their claims compromised "…as the Directors consider them 'critical creditors' and it is necessary to pay them in full in order to keep the business operating. This is necessary for the successful implementation of the Proposal, which is in the interests of all of the CVA Creditors." New Look accepts that the reference to "certain" of the Ordinary Unsecured Creditors is a mistake, since (as is clear from the CVA terms themselves) all of them were to be paid in full.

*Secured Creditors*

39. As I have noted above, the creditors under the RCF and TFFA as well as the SSN Holders, had security over all of New Look's assets and undertaking. A secured creditor may vote in a CVA only in respect of the unsecured portion of its debt.

40. The value of the security was estimated, for voting purposes, at £250 million. That meant that the RCF and TFFA were fully secured, and that the unsecured portion of the SSN Holders' claim was £273.4 million.

D: Summary of votes cast at the meeting of creditors for the CVA

41. Of those creditors who voted at the meeting, the votes in favour of the CVA included:

    (1) 100% of the Category A landlords (approximately £6.5 million);

    (2) Virtually 100% of the Ordinary Unsecured Creditors and employees (together approximately £72 million) (trade creditors owed £1,595, and employees owed £51,172 voted against the CVA);

    (3) 100% of the SSN Holders (approximately £273.4 million)

42. Of the Category B Landlords who voted, 58.27% with claims aggregating approximately £119 million voted in favour of the CVA, and 41.2% with claims aggregating £85 million voted against. Of the nine sub-categories, landlords in only one group (B8) voted in favour by the requisite 75% majority. Landlords in all other sub-groups, other than B3, voted in favour by more than 50% but less than 75%. A majority (61.9%) of landlords in sub-category B3 voted against the CVA.

43. Of the category C landlords who voted, 70% with claims aggregating approximately £34 million voted *against* the CVA, and 30% with claims aggregating £14.4 million voted in favour.

44. Of the non-critical creditors, a majority of 55% (with claims aggregating £2.3 million) voted *against* the CVA.

45. The turnout among landlords as a whole was high. 88.9% engaged with the CVA by voting or abstaining at the meeting. Excluding abstentions, the turnout was 81.4%.

E: The statutory provisions

46. The following are the relevant parts of IA 1986 and IR 2016, where the proposal is made by directors (as opposed to a liquidator or administrator of the company) and where there is no moratorium in place.

47. By section 1(1), the directors of a company may make a proposal for a CVA, defined as "a composition in satisfaction of [the company's] debts or a scheme of arrangement of its affairs".

48. The proposal must provide for a person (the "nominee") to act as trustee or otherwise for the purposes of implementing the CVA. The nominee must be qualified as an insolvency practitioner: section 1(1). The directors are required to provide to the nominee a document setting out the terms of the proposed arrangement, a statement of affairs and such other information as is prescribed: section 2(3).

49. The nominee is obliged, within 28 days after being given notice of the proposal (or such longer period as the court may allow), to file a report with the court stating whether, in his opinion, (a) the proposed CVA has a reasonable prospect of being approved and implemented, and (b) the proposal should be considered by a meeting of the company and its creditors (and, if so, stating the time and place for the meeting of the company): section 2(2).

50. It is for the nominee (where he has reported that the proposal should be considered by the company and its creditors) to summon a meeting of the company and to seek a decision from the company's creditors (by a qualifying decision procedure, which may include a physical meeting, a virtual meeting, electronic voting or correspondence): section 3(1) and (3).

51. Notice of the qualifying decision procedure shall be given to "every creditor of the company of whose claim and address the person seeking the decision is aware": section 3(4). The decision date must be not less than 14 days from the date of the delivery of the notice of the qualifying decision procedure and not more than 28 days from the date the nominee's report was filed with the court: Rule 2.27.

52. The company and its creditors may approve the proposed CVA with or without modifications: section 4(1A). Neither the company nor its creditors, however, may approve a proposal or modification:

(1) which affects the right of a secured creditor of the company to enforce its security (without the concurrence of the creditor concerned): section 4(3); or

(2) under which (in summary) the rights of preferential creditors to the priority they are entitled to under the Act and Rules are not respected (unless the relevant preferential creditor agrees otherwise): section 4(4).

53. Every creditor (secured or unsecured) who has been given notice of the qualifying decision procedure is entitled to vote: Rule 15.28(5). Secured creditors, however, are entitled to vote only in relation to the unsecured part (if any) of their debt: Rules 15.31(4) and (5).

54. In relation to decision procedures generally, where a debt is of an unliquidated or unascertained amount, the creditor may vote only where the convener or chair decides to put upon it an estimated minimum value for the purpose of entitlement to vote and admits the claim for that purpose: Rule 5.31(2). In the case of a CVA, however, "a debt of an unliquidated or unascertained amount is to be valued at £1 for the purposes of voting unless the convenor or chair or an appointed person decides to put a higher value on it."

55. A decision to approve a proposal or modification for a CVA is made when three-quarters or more (in value) of those responding vote in favour of it: Rule 15.34(3). A decision is not made, however, if more than half of the total value of the unconnected creditors vote against it: Rule 15.34(4).

56. By section 5, the CVA takes effect as if made by the company at the time the creditors decided to approve it, and it binds: "every person who in accordance with the rules (i) was entitled to vote in the qualifying decision procedure by which the creditors' decision to approve the voluntary arrangement was made, or (ii) would have been so entitled if he had had notice of it, as if he were a party to the voluntary arrangement.

57. By section 6(1), a creditor (among certain others) may apply to the court, not later than 28 days after the chairman of the meeting has reported the result to the court, on either or both of the following grounds:

> "(a) that a voluntary arrangement … unfairly prejudices the interests of a creditor, member or contributory of the company;
>
> (b) that there has been some material irregularity at or in relation to the meeting of the company or in relation to the relevant qualifying decision procedure."

58. If the court is satisfied as to either of the grounds mentioned, then by section 6(4) it may, among other things, revoke or suspend the decision approving the CVA and, by section 6(5), it may give supplemental directions as it thinks fit.

F: Future rent and voluntary arrangements

59. Certain aspects of the treatment of landlords' claims in voluntary arrangements are not in dispute.

60. First, a landlord is a creditor, for the purposes of a voluntary arrangement, in respect of the tenant's liability for rent falling due in the future. Such rent would not be provable in a liquidation; a landlord would be restricted to proving for instalments of rent as they fell due after the commencement of the liquidation. It is nevertheless a pecuniary liability to which the company may become subject by reason of the covenant to pay rent in the existing lease. The authorities on this point were extensively reviewed, and the point confirmed, by Norris J in *Debenhams* (above) at [23] to [61].

61. Second, although future rent is typically fixed by the lease in a particular amount, the landlord's claim is treated, for voting purposes, as unliquidated and unascertained: *Doorbar v Alltime Securities Ltd (No.2)* [1995] BCC 728, at 738; *Re Newlands (Seaford) Education Trust* [2006] EWHC 1511 (Ch), per Sir Andrew Morritt C. at [24]. Accordingly, the claim is to be valued at £1 unless the convener or chair decides to put a higher value on it: Rule 15.31(3) IR 2016. In *Newlands*, the task of the convener or chair in this regard was explained as follows:

> "The chairman should not speculate. Nor is he obliged to investigate the creditor's claim. But he must examine such evidence, and I do not use that word in any technical sense, as the creditor puts forward and any relevant evidence provided by any other creditor or the debtor. If the totality of that evidence leads him to the conclusion that he can safely attribute to the claim a minimum value higher than £1 then he should do so."

62. Third, the possibility that a CVA may compromise the claim of a landlord in respect of its right to future rent has long been recognised: see, for example, *Doorbar (No2)* in which Knox J's reasoning at p.739 (in support of the conclusion that there was no material irregularity in the chairman valuing the landlord's claim in respect of future rent at an amount equal to one year's rent) was reached in circumstances where the landlord was entitled, under the CVA, to receive "only a small dividend in respect of every gale of rent for the rest of the term".

63. The question whether it is permissible for a CVA to compromise a claim for future rent, yet entitling the company to remain in possession, was answered in the affirmative in *Debenhams*. Norris J there rejected (at [62] to [82]) the argument that there was no jurisdiction to do so and rejected the argument that it was inherently unfair to do so. This is not an issue of common ground in this case, however, as Mr Arden QC invited me to depart from this part of Norris J's decision. This is addressed below at [203] to [212].

<u>G: The issues</u>

64. The Applicants' challenge to the New Look CVA, by the close of the hearing, was put on three broad bases:

    (1) The Proposal, or aspects of it, did not constitute a composition or arrangement within the meaning of section 1(1) IA 1986 (the "Jurisdiction Challenge"), specifically because:

        (a) it did not constitute a composition in satisfaction of the company's debts or a scheme of arrangement of its affairs, by reason of the fact that on a true analysis it involved separate arrangements (on fundamentally different terms) with different groups of creditors;

        (b) there was insufficient "give and take" as between New Look and various of the creditor groups; and

        (c) the new termination right granted to New Look in respect of leases with Category B and Category C landlords improperly sought to interfere with property rights of those landlords;

    (2) There were material irregularities (the "Material Irregularity Challenge"), specifically:

(a) in relation to the calculation of the landlords' claims for voting purposes; and

(b) by reason of omissions and inaccuracies in the Proposal; and

(3) The Applicants were unfairly prejudiced (the "Unfair Prejudice Challenge"), because:

(a) the requisite majorities at the creditors meeting were secured with the votes of creditors whose claims against New Look were unimpaired by the CVA;

(b) creditors whose claims were compromised received differential treatment from those that were not; and

(c) various of the modifications to the terms of leases were unfair.

G: The Applicants' core contentions

65. At the heart of the Jurisdiction and Unfair Prejudice Challenges lie the following contentions. First, a CVA cannot be used to effect two or more deals on substantively different terms with different groups of creditors, either because there is no jurisdiction to do so, or because to do so is inherently unfairly prejudicial. Second, even if it can, it is inherently unfairly prejudicial for a CVA to compromise the claims of a sub-group of creditors where the requisite statutory majority at the creditors' meeting is achieved by the votes of other creditors who are unimpaired by the CVA, or who receive substantially different treatment.

66. Applied to the facts of this case, the Applicants contend that:

(1) the CVA comprises at least three substantially different deals: (a) with the SSN Holders (who are unimpaired by the CVA and were instead offered a materially different deal via the Scheme); (b) with the Compromised Landlords in categories B and C; and (c) with the Ordinary Unsecured Creditors and the Category A landlords who are entitled to receive payment in full; and

(2) the CVA was imposed upon Compromised Landlords by virtue of the votes cast at the meeting by the SSN Holders, the Ordinary Unsecured Creditors and Category A Landlords who were wholly or substantially unimpaired by the CVA, or alternatively (as regards the SSN Holders) received fundamentally different treatment.

67. In support of this root and branch attack on the use of CVAs, the Applicants' submissions ranged over wide areas of relevant law, both before and after IA 1986. These can be distilled into the following four broad points. First, Part 1 IA 1986 must be construed in the light of principles established in the context of previous statutory provisions relating to arrangements with creditors. Mr Arden QC referred me to the various pre-1986 regimes for compositions and arrangements with creditors (both of individuals and of companies) and to a

substantial body of cases decided under them. Those cases, he submitted, established basic principles of good faith and equality among creditors which equally underpin Part 1 of IA 1986 and which support the Applicants' core contentions at [65] above. Second, he referred me to the legislative history of IA 1986, in particular the report of the committee under the chairmanship of Sir Kenneth Cork ("the Cork Report"), which he submitted indicates that voluntary arrangements were intended to be used only in simple cases, where substantially the same treatment is offered to all creditors. Third, he cited a trilogy of Court of Appeal cases, each of which was concerned with an individual voluntary arrangement ("IVA"), which established that the principles of good faith and equality continued to apply in shaping the concept of material irregularity in section 6(1)(b) IA 1986. Fourth, he referred to the development of the concept of unfair prejudice in section 6(1)(a) in authorities since 1986, which he submitted also supported the Applicants' core contention.

*(1) Compositions and arrangements prior to 1986; basic principles of good faith and equality*

*Individuals*

68. A statutory power of a majority within the general body of an insolvent debtor's creditors to bind the remaining creditors has existed in one form or another for many years.

69. For example, the Bankruptcy Act 1861, by sections 192 to 200, provided for a deed entered into between a debtor and his creditors, or any of them, "relating to the debts and liabilities of the debtor, and his release therefrom, or the distribution, inspection, management, and winding-up of his estate, or any of such matters" to be binding on all of his creditors, where the deed was approved by a majority of creditors (in number) representing 75% in value (whose debts amounted to £10 and upwards).

70. As noted in the Cork Report, at [362], these provisions quickly fell into disrepute because of dishonesty and malpractice. They were replaced by section 18 of the Bankruptcy Act 1883. This included a requirement that in order for a composition or scheme to be binding on creditors it must be sanctioned by the court. In *Reed v Bowen* (1886) 17 QBD 244, Lord Esher (at p.251) said that these provisions were enacted "…for the purpose of preventing a majority of creditors from dealing thus recklessly, not only with their own property, but with that of the minority, and of enforcing, so far as the legislature could, a more careful and moral conduct on the part of debtors."

71. The 1883 Act introduced the language now found in IA 1986 (sections 1 and 253, relating to CVAs and IVAs respectively) of "composition in satisfaction of [the debtor's debts]" and "a proposal for a scheme of arrangement of the debtor's affairs". It applied, however, only in the context of existing proceedings for bankruptcy, after the making of a receiving order.

72. The 1883 Act provisions were re-enacted in the Bankruptcy Act 1914 (section 16). In addition, the Deeds of Arrangement Act 1914 contained provisions for

an arrangement, which was void unless assented to by a majority in number and value of creditors, by way of an assignment of property or agreement for a composition. Such a deed constituted an act of bankruptcy, however, and did not prevent a dissenting creditor from obtaining a bankruptcy order.

73. In relation to these statutory provisions, the courts recognised that there were limitations on the power of the majority to bind the minority, by virtue of the application of principles of good faith and equality of treatment between creditors. The 19th century authorities were extensively reviewed at first instance in *Somji v Cadbury Schweppes plc* [2001] 1 WLR 615 ("*Somji*) (see below at [88]). For present purposes, it is sufficient to refer to just two of them.

74. *McKewan v Sanderson* (1875) LR 20 Eq 65 was typical of many of the cases, in that it concerned an attempt by one creditor to obtain an advantage outside of the arrangement not available to others. Malins V-C said, at p.72:

> "Now I take it to be thoroughly settled, both in Courts of Law and Equity, that where there is a bankruptcy, or an arrangement with creditors by composition or insolvency, when insolvency exists as contradistinguished from bankruptcy, it is the duty of all creditors who have once taken part in the proceedings of bankruptcy or composition to stand to share and share alike. Equality is the only principle that can be applied, and if one creditor, unknown to the other creditors--not unknown to one or two, but to the general body--enters into an arrangement by which he gets for himself from the debtor, or from any one on behalf of the debtor, any collateral advantage whatever, that is a fraud upon the other creditors ..."

75. In *Thompson v Knight* (1866-67) LR 2 Ex 42, however, the principle of equality was applied to outlaw a provision in the arrangement itself. A deed entered into under section 192 of the 1861 Act provided that creditors' debts were to be compromised by payment of 10s/£, payable in instalments. The trustee was given discretion, however, to pay any creditor, whose debt was less than £20, the full amount of its composition at such time or times as he thought fit. The deed was held to be invalid. Kelly CB, at p.44, said:

> "Now I think it absolutely essential that all the creditors should be placed on an equal footing, especially when I remember that, generally, a great number of them are in these cases bound by an instrument to which they are not parties and to which they have not assented. Under such circumstances, it is only when the provisions of the deed are just and equal that the deed ought to be held binding upon all."

*Companies*

76. The Companies Act 1862 introduced two procedures by which arrangements might be made between a company and its members and creditors.

77. The first, by section 136, applied to a company either about to be, or in the course of being, wound up voluntarily. An arrangement would be binding on the company and its creditors if sanctioned by an extraordinary resolution and acceded to by three-quarters in number and value of the creditors. This provision was rarely used. In the only reported case on its application, *Re Contal Radio Limited* [1932] Ch 66, Maugham J held that a composition intended to make the company solvent, and thus avoid winding-up, was not within the meaning of the section.

78. The second, by sections 159 and 160, gave the liquidator extensive powers to pay any classes of creditors in full, or make compromises with creditors, debtors and contributories. If there was any power to bind minorities at all, it was very restricted: *Re Alabama, New Orleans, Texas and Pacific Junction Railway Co* [1891] 1 Ch 213, per Lindley LJ at [235]. The power was enlarged by section 2 of the Joint Stock Companies Arrangement Act 1870, which provided that an arrangement or compromise between a company and its creditors, or any class of them, was binding on all creditors if approved by a majority in number representing three-quarters in value of the creditors, or any class of them, and sanctioned by the court. This provision, once extended to an arrangement with members (by section 24 of the Companies Act 1900) and extended to companies not in the course of being wound up (by section 38 of the Companies Act 1907), subsists in materially the same terms in Part 26 of the Companies Act 2006 ("CA 2006").

79. It was soon established that a class is made up of those creditors whose rights (both their pre-existing rights and the rights conferred by the scheme) were "not so dissimilar as to make it impossible for them to consult together with a view to their common interest": *Sovereign Life Assurance Company v Dodd* [1892] 2 QB 573, per Bowen LJ at p.583. This interpretation of "class" was to "prevent the section being so worked as to result in confiscation and injustice".

80. It was also established from an early date that one of the key functions of the court in considering whether to sanction a scheme was to "see that the minority is not being overridden by a majority having interests of its own clashing with those of the minority whom they seek to coerce": *Alabama, New Orleans, Texas and Pacific Junction Railway* (above), per Lindley LJ at p.239. Bowen LJ, at p.243, identified the purpose of the section as being to enable compromises for the "common benefit" of the creditors or some class of creditors. At p.244, he said that, although it was perfectly fair for each creditor to do that which seemed best for itself, the court had to have regard to the interests of the whole class, and it would be "certainly be very much influenced in its decision, if it turned out that the majority was composed of persons who had not really the interests of that class at stake."

81. Although the procedure introduced by section 136 of the Companies Act 1862 was rarely used (see above), the Australian equivalent of section 136 (section 510 of the Corporations Act 2001) has been held not to be subject to the same limitation that Maugham J imposed on the English statute in *Re Contal Radio*. Mr Arden QC relied on Australian authorities which have emphasised the need for an arrangement under this provision to provide for *pari passu*

treatment of creditors: see for example *Re Farmers' Freehold Land Co Ltd* (1892) 3 BC (NSW) 39 (Manning J); *Re Switch Telecommunications PTY Ltd* (2000) 35 ACSR 172 at [34] – [35]. In the latter case, Santow J held that to be binding on non-voting or dissentient creditors, they must be paid *pari passu* with the voting creditors.

82. In *Kassem v Sentinel Properties Limited* [2005] NSWSC 403, Barrett J said (at [17]) that it was understandable that section 510 should be subject to such limitations because, unlike the provisions in the Australian legislation concerned with schemes of arrangement, it contained no mechanism for the recognition and protection of classes of creditors "according to community of interest in relation to the particular proposal". He considered that any case where a majority sought to dispossess or otherwise prejudice a minority should be dealt with under the scheme of arrangement provisions.

*(2) The Cork Report*

83. In chapter 7 of the Cork Report, the committee, having noted the deficiencies in the existing law relating to compositions and arrangements for individuals, recommended a new statutory procedure to enable an insolvent debtor to enter into a voluntary arrangement for the discharge of his debts. This formed the basis of IVAs, first enacted in the Insolvency Act 1985 and then in IA 1986.

84. It also recommended, in a few short paragraphs, adapting the same new statutory procedure for use by companies.

85. The Applicants' contention that the committee intended CVAs to be used only for small companies and for relatively simple cases is based in particular on the following passage (at [430]) in which the committee said that a voluntary arrangement for a company was:

> "…only likely to be used, first, where for some reason it is not appropriate to appoint an Administrator and, secondly, where the scheme is a simple one involving a composition or moratorium or both for the general body of creditors which can be formulated and presented speedily. However, we are convinced that the facility to promote such arrangements without the obligation to go to the Court will prove of value to small companies urgently seeking a straightforward composition or moratorium."

*(3) Three Court of Appeal cases applying principles of good faith and equality*

86. The three Court of Appeal cases, all of which concerned IVAs, are: *Somji*; *National Westminster Bank plc v Kapoor* [2011] EWCA Civ 1083 ("*Kapoor*"); and *Gertner v CFL Finance Ltd* [2018] EWCA Civ 1781 ("*Gertner*").

87. The first two cases were considered at length in *Gertner*: *Somji* at [65] to [69] and *Kapoor* at [70] to [72], and I will therefore deal with them here only briefly.

88. *Somji* involved a secret side deal (to the debtor's knowledge) whereby a friend of the debtor agreed to buy up the debt of certain banks who were opposed to the IVA. The Court of Appeal concluded that the failure to disclose the side-deal was a material omission which justified the making of a bankruptcy order under section 276(1)(b). The deputy judge at first instance had conducted a review of the 19th century cases establishing principles of good faith and equality. In the Court of Appeal (although it was found that the deputy judge had been wrong to conclude, in reliance on these principles, that the IVA was void), Robert Walker J considered that it would be "no great surprise" to find that the "intellectual freight", in particular the basic principles such as "proportionate treatment of unsecured creditors" were to be found in the regime under IA 1986.

89. *Kapoor* concerned an assignment from a creditor who was connected with the debtor, to an unconnected third party for the sole purpose of circumventing the requirement that debts of connected creditors are left out of account under Rule 5.23(4) of IR 1986 (which rendered an IVA invalid if more than half in value of creditors who were not connected with the debtor voted against it). The Court of Appeal concluded that this was a material irregularity. Etherton LJ said (at [69]) that the expression "material irregularity" was coloured by the well-established principle of good faith articulated in the authorities considered by the deputy judge in *Somji.* It was not restricted to cases concerning non-disclosure of a side-deal (the assignment in *Kapoor* having been disclosed to creditors).

90. As to the principles to be derived from the pre-1986 law, Etherton LJ cited *Dauglish v Tennent* (1866) LR 2 QB 49 for the proposition that in order that a deed should be binding on creditors it was essential that there should be the "most perfect good faith between the debtor and all his creditors" and he cited *Mare v Sandford* (1859) 1 Giff 288, for the proposition that the court interferes in transactions of this kind on the ground of public policy, recognising that the object of the bankrupt laws was "to secure an equal distribution of property among the creditors, so that none shall have any advantage over another."

91. An important consideration in *Kapoor* (at [67]) was that an IVA enabled an insolvent debtor to escape the full and rigorous consequences of bankruptcy and, conversely, had potentially severe disadvantages for creditors, particularly where there were doubts as to whether the debtor had been full and frank in the information provided as to his assets. Etherton LJ held, at [68] to [69] that the assignment was patently intended solely to subvert a critical principle of legislative policy as to the conditions for approval of an IVA and, as such, was "…an uncommercial arrangement inconsistent with any notion of good faith between Mr Kapoor and his independent creditors."

92. In *Gertner*, the debtor's proposal for an IVA disclosed that he had no assets, that his unsecured creditors totalled approximately £583 million, and that a third party was willing to provide a sum of £487,500 which would, after payment of expenses and preferential claims, enable a distribution of 0.07p/£ to be paid to unsecured creditors, as opposed to a nil return in bankruptcy.

93. The largest of Mr Gertner's creditors, Kaupthing Bank hf, was owed approximately £547 million. Kaupthing had entered into a settlement agreement with Mr Gertner, his brother and a trust established by the provider of third-party funds for the IVA (the "KSA"). Pursuant to the KSA, Kaupthing received a payment of US$6 million, certain other consideration and the benefit of a profit-sharing agreement.

94. After the IVA was approved, with the benefit of Kaupthing's vote in favour, one of Mr Gertner's creditors ("CFL") issued an application to revoke the IVA under section 262 IA 1986 on the grounds of unfair prejudice and/or material irregularity.

95. Although one of the grounds of complaint was inadequate disclosure of the KSA, at [63] Patten LJ noted that the real thrust of CFL's argument did not depend on non-disclosure. The objection was that it provided (and was intended to provide) a significant inducement to Kaupthing to vote in favour of the IVA and that this denied the other creditors the ability to secure, through a trustee in bankruptcy, any further investigation into the assets of Mr Gertner: "The creditors are not therefore on an equal footing in the consideration of the merits of the IVA proposal over a bankruptcy or in relation to the benefits which they obtained from the approval of the proposal."

96. Having endorsed the statement of principle by Malins V-C in *McKewan v Sanderson* (above, at [74]), Patten LJ at [65] stated that the principle was not merely a re-iteration of the *pari passu* principle, but could be breached if a creditor received a collateral advantage from a third party in return for entering into the arrangement. At [80] he said that where the policy considerations referred to by Etherton LJ at [67] of *Kapoor* were very much in issue the good faith principle was required to be strictly applied. He concluded that there was a breach of the good faith principle because Kaupthing had been provided with a collateral advantage not available to other creditors, which placed it in a position of conflict with the interests of those other creditors. He said that the good faith principle was not confined to "vote buying of the kind exemplified by *Somji*" and that revocation of the IVA on grounds of material irregularity did not depend on whether disclosure of the arrangement could have made a difference to the outcome. The consequence of the finding of material irregularity was that Kaupthing was disqualified from voting on the proposal.

97. Mr Gertner relied on two cases concerned with voluntary arrangements of football clubs, (*IRC v Wimbledon Football Club Ltd* [2004] EWCA Civ 635 and *HMRC v Portsmouth City Football Club Ltd* [2010] EWHC 2013 (Ch), both of which I consider in more detail below, in which "football creditors" would be paid in full (from sources other than the company) but had been allowed to vote at the meeting of creditors.

98. Patten LJ accepted, at [79], that the mere fact that some (but not all) creditors would receive preferential treatment in the form of payment by a third party did not in itself constitute a material irregularity. The problem with the KSA, however, was that "looked at objectively, the additional consideration was intended to act and must be presumed to have acted as an inducement to

Kaupthing to support an arrangement which would avoid Mr Gertner's bankruptcy." The football cases were distinguishable because the provision made for football creditors was carried out in conformity with rules which pre-dated the insolvency of the clubs in question:

> "It was a standard published requirement, protecting a defined class of creditors, and applied to all clubs in the event of insolvency. It was not an *ad hoc* private arrangement designed to give the largest and most influential creditor an additional financial advantage not made available to any other creditor in the IVA."

99. I agree with Mr Arden QC that these cases establish that although the route to challenging a CVA or IVA is via the statutory provisions in Part I or Part VIII IA 1986 respectively, the basic principles of good faith and equal treatment, which underpinned the pre-1986 bankruptcy law assist in shaping those provisions.

100. In fact, in each case, the court was concerned only with challenges based on material irregularity and it was unnecessary to consider an alternative basis of challenge based on unfair prejudice. In part that might be explained by the fact that they each involved a separate deal with one or more creditors outside the terms of the arrangement, and in a line of first instance authority (which Robert Walker LJ in *Somji*, at [37], said he was "by no means convinced" was wrong) it was established that to establish unfair prejudice the unfairness must stem from the terms of the arrangement: see for example *Re a debtor (No 259 of 1990)* [1992] 1 WLR 226, per Hoffmann J at p.228H.

101. As a matter of principle, however, the basic principles are applicable as much to shaping the meaning of unfair prejudice as they are to shaping the meaning of material irregularity.

102. It is clear from, in particular, *Gertner*, that notwithstanding IA 1986 and IR 2016 expressly provide that notice is to be given to all creditors of the debtor and all such creditors are entitled to vote, where a material irregularity occurs as a result of a breach of the good faith principle, its consequence may be to disallow a creditor's vote altogether.

103. It is also clear from these cases that the principle of good faith is rooted in part in the concept of equal treatment of creditors. Hence, an inducement offered to one or more creditors, not offered to all, to ensure their support constituted a material irregularity, whether or not that inducement was disclosed to the creditors as a whole. Although, as I have noted, the cases were all concerned with an inducement that took effect outside the terms of the arrangement, Mr Smith QC accepted that had the inducement been contained within a term of the arrangement, it would have been equally objectionable (albeit, in that case I consider the challenge would be better framed on the grounds of unfair prejudice).

104. On the facts of each of the three cases, however, there was something in the arrangement, beyond mere preferential treatment, to make it objectionable.

*Somji* involved a secret side-deal. In *Kapoor* the purpose of the arrangement was to subvert the statutory policy that a resolution approving an arrangement was invalid if more than half in value of the independent creditors voted against it. In *Gertner* the KSA provided and was intended to provide a significant inducement to Kaupthing to vote in favour of the IVA. Moreover, in both *Kapoor* and *Gertner*, the Court of Appeal stressed the importance of the policy consideration that an IVA potentially disadvantaged creditors by depriving them of the benefit of greater scrutiny into a debtor's affairs that bankruptcy offered.

105. Notwithstanding Patten LJ's comment (see [96] above) that the good faith principle is not confined to cases of vote buying, therefore, these cases do not go so far as to say that an arrangement that is approved by virtue of votes of creditors receiving materially different treatment (without the different treatment being offered as an inducement to vote in favour) is invalid, in the way that (for example) the arrangement in *Thompson v Knight* (above) was invalid simply because it provided for unequal treatment of creditors by enabling the trustee to pay some creditors in one go rather than in instalments.

*(4) The meaning of unfair prejudice in section 6 IA 1986*

106. Prejudice to a creditor, in the context of a CVA, is likely to be readily identifiable and readily established, for example if the amount owing to it is reduced (without receiving payment) or if it loses a benefit relating to the debt, for example if its security is impaired. More difficult to pin down are the circumstances that render the prejudice "unfair".

107. In considering whether an arrangement is unfairly prejudicial, while recognising that it is necessary to have regard to all the circumstances of the case, the courts have developed two helpful tests, labelled the "vertical" and "horizontal" comparators: see *Prudential Assurance Co Ltd v PRG Powerhouse Ltd* [2007] EWHC 1002 (Ch) ("*Powerhouse*"), at [75].

108. The vertical comparator, described by Henderson J in *Mourant & Co Trustees ltd v Sixty UK Ltd* [2010] EWHC 1890 (Ch) ("*Sixty*") at [67] as the "irreducible minimum" below which the return in a CVA cannot go, is a comparison with what the creditors' position would have been in the event that the CVA was not approved, typically therefore their position in a winding up or bankruptcy: see the Cork Report (at [378]) and *Re T&N Limited* [2004] EWHC 2361 (Ch), per David Richards J at [82], where he considered it difficult to envisage a court *not* interfering with a CVA which was "…likely to result in creditors, or some of them, receiving less than they would in a winding up of the company, assuming that the return in a winding up would in reality be achieved and within an acceptable time-scale".

109. It is emphatically not enough, to preclude a finding of unfair prejudice, that the vertical comparator test is satisfied in respect of objecting creditors. It is also necessary to consider the position as between creditors – the horizontal comparator. Indeed, it was established relatively early on that unfairness in the context of section 6(1)(a) stems from differential treatment as between creditors: see, for example, *Re a Debtor (No.222 of 1990), ex p the Bank of*

*Ireland* [1992] BCLC 137, per Harman J at p.145d-e. In *Doorbar v Alltime Securities Limited (No.2)* [1995] BCC 728, Knox J, put it this way:

> "Unfair prejudice, therefore, is a reference to a degree of prejudice to one creditor or class of creditors as compared with other creditors or class of creditors. It involves an assessment of any imbalance between possible prejudices to one or the other.."

110. Knox J's conclusion on the question of unfair prejudice was upheld on appeal: [1996] 1 WLR 456, per Peter Gibson LJ at pp.467-468.

*The consequences of differential treatment*

111. The mere fact that there is differential treatment does not, however, establish unfair prejudice: see *Re a Debtor (No.10 of 1999)* [2001] 1 BCLC 54. At p.63c, Ferris J held that it gave cause for inquiry, but might turn out to be justified.

112. Lightman J in *IRC v Wimbledon Football Club Ltd* [2004] EWHC 1020 (Ch), at [18] summarised the effect of the authorities to that date as follows: (1) the unfairness must be caused by the terms of the arrangement; (2) unequal or differential treatment of creditors of the same class will not of itself constitute unfairness, but may give cause for inquiry and require an explanation; (3) it is necessary to consider all the circumstances including, as alternatives to the arrangement proposed, not only liquidation but the possibility of a different fairer scheme; (4) differential treatment might, in some circumstances, be required to ensure fairness (citing, as an example, *Sea Voyager Maritime Inc v. Bielecki* [1999] 1 All ER 628). Further, he noted that differential treatment may be justified where necessary to ensure the continuation of the business that underlies the arrangement: see also, *Powerhouse*, at [90], *Sixty* at [67], and *Debenhams*, at [110].

113. Differential treatment is also justified where it is required by section 4 IA 1986 (relating to secured and preferential creditors, see [52] above). There is no inconsistency, however, between such differential treatment and the basic principles of good faith and equality, because "equality" in this context does not mean equal treatment in the abstract, but equal treatment in the context of the established insolvency principle of *pari passu*. The *pari passu* principle is not an absolute rule, but is subject to important exceptions. For example, secured creditors are entitled to rely on their security outside of bankruptcy or liquidation (and the assets of the debtor subject to security have been treated as excluded from the bankruptcy estate) and for policy reasons preferential creditors have for a long time ranked ahead of other unsecured creditors upon insolvency (although the precise definition of a preferential debt has changed over time).

114. The *pari passu* principle also recognises that some creditors may have additional rights which they are entitled to retain in an insolvency, for example a right in some circumstances to pursue third parties for the debt owed to them by the insolvent debtor. There is no inconsistency with the principles of good

faith and equality if a voluntary arrangement affords different treatment to a creditor in order to preserve those rights.

115. That is what happened in *Bielecki* (above). A creditor (SVM) with a negligence claim against the debtor potentially had the right to be indemnified by the debtor's insurer, pursuant to the Third Party (Rights Against Insurers) Act 1930. Such a right depended, however, on first establishing liability as against the debtor. There was an implied term in the arrangement which prevented all creditors from taking proceedings against the debtor. Richard McCombe QC sitting as a deputy High Court Judge, concluded that SVM was, by reason of its rights under the 1930 Act, a creditor of a different type ("one may say a different class") to the others bound by the arrangement, and its interests as a creditor were unfairly prejudiced by being denied, albeit along with other creditors, the right to pursue proceedings against the debtor.

*A compromise imposed by virtue of the votes of unimpaired or differently treated creditors*

116. There is an undoubted tension between the principles of good faith and equality and a compromise which is imposed on a minority by the exercise of a statutory power conferred on the majority, where the majority is either unimpaired or receives materially different treatment. Mr Arden QC pointed to a number of cases where this resulted – or at least contributed to – a finding of unfair prejudice.

117. In *Re a Debtor (No.101 of 1999)* (above), for example, although Ferris J held that differential treatment was not in itself proof of unfair prejudice, he did in fact conclude that the arrangement was unfairly prejudicial. In that case, the debtor had three groups of creditors: (1) friends to whom £541,000 was owed in aggregate; (2) the Crown, to whom £77,000 was owed, and (3) household creditors of £20,000. He proposed a voluntary arrangement under which: (1) his friends would receive nothing but would retain the right to pursue him in full for the debts; (2) third party funds would be used to pay the expenses of the arrangement and to make payments totalling £15,000 to the Crown in satisfaction of its debts; and (3) the household expenses would be paid by his wife.

118. In considering all the circumstances, Ferris J took particular account of the fact that the friends of the debtor had exercised their majority vote in a way which "forces the Crown creditors to accept a reduced payment in satisfaction of their debts while leaving their own position unchanged or even improved (by the elimination of competing debt)" (p.63i). That could not be justified merely on the basis that HMRC would have done better under the IVA than if the debtor had gone into bankruptcy because the alternatives to the IVA included "the ability to press for a more satisfactory arrangement in which there would be no differential treatment of creditors" (p.63h).

119. In support of its contention that allowing creditors with differential treatment to vote as one with all other creditors cannot be inherently unfairly prejudicial, New Look points to the fact that IA 1986 and IR 2016 positively require all creditors to be given notice of the meeting and be permitted to vote, including preferential and secured creditors.

120. So far as preferential creditors are concerned, since there is nothing which excludes them from being entitled to receive notice of, and vote at, the meeting, the legislation expressly envisages that they are entitled to preferential treatment (i.e. payment in full in so far as their debts would be preferential upon insolvency) <u>and</u> have their vote included within the statutory majority. As Mr Smith QC pointed out, that had also been the case under section 18 of the 1883 Act, subsection (14) of which prevented the court from approving a composition or scheme which did not respect the priority which preferential creditors would have had in bankruptcy. It is unlikely however, although not impossible in a case where the vote was close, that the vote of preferential creditors would have been material, in the sense of being necessary to secure the requisite majority. No case was cited to me where that had occurred.

121. The position is less straightforward so far as secured creditors are concerned, because a distinction is drawn for voting purposes between the secured and unsecured parts of their debt. By IR 2016 Rule 15.31(4)&(5), if they are wholly secured, then they are excluded from voting altogether (so the situation of which the Applicants complain could not arise), and where they are partly secured, they are permitted to vote only in respect of the unsecured part of their debt. That reflects the expectation that in respect of the unsecured part of their debt they stand together with the ordinary unsecured creditors, entitled to share in a distribution of the assets that fall within the insolvency estate.

122. One way of expressing the argument of the Applicants is that the horizontal comparator test is failed where the Compromised Landlords would have formed a separate class for the purposes of a scheme of arrangement, which they could have blocked.

123. The relevance of the comparison with a scheme of arrangement has been the subject of some debate, in particular in *Sisu Capital Fund Ltd v Tucker* ("*Sisu*") and *Powerhouse*.

124. In *Sisu*, Warren J referred to the "helpful summary" of the differences between schemes of arrangement and CVAs provided in *Re T&N Ltd* [2004] EWHC 2361 (Ch). At [81], in that case, David Richards J considered that there is no difference in the substance of the underlying test of fairness to be applied when sanctioning a scheme of arrangement or considering a challenge to a CVA on the basis of unfair prejudice. The test was deliberately broad and was best summarised as follows, in the scheme context, in Buckley on the Companies Acts:

> "In exercising its power of sanction the court will see, first, that the provisions of the statute have been complied with, second that the class was fairly represented by those who

> attended the meeting and that the statutory majority are acting bona fide and are not coercing the minority in order to promote interests adverse to those of the class whom they purport to represent, and thirdly, that the arrangement is such as an intelligent and honest man, a member of the class concerned and acting in respect of his interest, might reasonably approve.
>
> The court does not sit merely to see that the majority are acting bona fide and thereupon to register the decision of the meeting, but, at the same time, the court will be slow to differ from the meeting, unless either the class has not been properly consulted, or the meeting has not considered the matter with a view to the interests of the class which it is empowered to bind, or some blot is found in the scheme."

125. David Richards J pointed out the crucial difference with a CVA is that it involves just one meeting of creditors. Necessarily, therefore, there may be sub-groups within a CVA who would constitute separate classes for a scheme. In such a case, in considering unfair prejudice, the court would have regard to the different position of different groups of creditors. He noted that this was also the case in a scheme of arrangement where a voting class of creditors contains a sub-group of creditors with different interests, or even rights. I note that the latter might occur if the court had concluded that the differences in rights were not such as to prevent the different sub-groups consulting together with a view to their common interest.

126. Warren J went on at [76] of *Sisu* to refer to the "reasonable and honest man" also being a "welcome guest" at the home of the CVA. In particular, he considered that if the reasonable and honest man in the same position as the applicants might reasonably have approved the CVA, then the applicants would fail.

127. It had been submitted to Warren J that the applicant creditors would – had there been a scheme of arrangement instead of a CVA – have been in a position to block the scheme as they would have formed a separate class within which the requisite statutory majority was not achieved. As to that, Warren J said (at [133] to [134]) that even if it were true that they would have formed a different class for the purposes of a scheme (which he did not need to decide), the mere fact that they would be able to block it as a separate class in a hypothetical scheme did not mean that they were necessarily unfairly prejudiced because the vote in the CVA went against them.

128. It is important to see this comment in context. *Sisu* was a complex case, but that was because it involved numerous interlocking CVAs for different companies in the same group, pursuant to which the settlement of various potential claims between group companies were approved. The alleged unfairness related primarily to the terms of those inter-company settlements, it being said they favoured companies other than those whose CVA was challenged by the applicants. The particular complaint was that some of the bondholders of company A, whose CVA was challenged, were also creditors

of other companies in the group which were on the other side of the issues to be settled. In their capacity as creditors of the other companies, they were in a position of potential conflict with those who were creditors of company A alone. It was not a case, therefore, where the alleged unfairness arose from the allocation of the CVA company's assets as between different groups of creditors of that company.

129. In a subsequent passage, Warren J did consider the hypothetical case of a creditor of a company using its majority position to insist on receiving a better return as a creditor of that company (at [425] and [573]), concluding:

> "a majority creditor of a company cannot, without causing unfair prejudice, insist on receiving *qua* creditor of that company more than his *pro rata* share of assets as a condition of approving a CVA: the office-holder should not, in the first place, present such a proposal."

130. Warren J's judgment was cited with approval by Etherton J in *Powerhouse*, at [74]. In fact, the arrangement in *Powerhouse* was objectionable on the simple ground that it failed the vertical comparator. The CVA purported to affect the rights of landlords of premises from which the company had traded, but were now closed. It provided for the release of all claims of the relevant landlords against the company and, pursuant to guarantees, against the company's solvent parent. The relevant landlords would receive only a dividend of 28p/£ under the CVA. Meanwhile, all other creditors would be paid in full. This reversed the position in a liquidation of the company, under which all other creditors would receive nothing, but the relevant landlords would retain the valuable rights under the guarantee given by the parent. The relevant landlords clearly fared much worse under the CVA than under the vertical comparator.

131. It was not on this basis alone that Etherton J upheld the landlords' objection, however. His decision was based on a consideration of all the circumstances and one of the points he considered was the utility of comparison with a scheme of arrangement.

132. On the one hand, at [92], he noted that it was not envisaged by the authors of the Cork Report that its proposals would enable a CVA to be imposed in circumstances in which a scheme of arrangement could have been successfully challenged on the grounds of "unfair prejudice" (by which I understand him to have been referring to the test of fairness adopted in determining whether to sanction a scheme). On the other hand, at [95], while he considered that a comparison with what the position would have been in a scheme of arrangement may be of assistance, caution was necessary in carrying out the comparison exercise, citing Warren J's comment at [134] of *Sisu* that the mere fact that creditors objecting to a CVA would have been in a different class able to block a scheme of arrangement does not entail that they are unfairly prejudiced when the CVA vote goes against them.

133. In reaching his conclusion on the facts, at [108], Etherton J nevertheless placed considerable reliance on the fact that such an "illogical and seemingly unfair" result could *not* have been achieved via a scheme of arrangement. In a scheme, the guaranteed landlords would have formed their own class and the creditors who were to be paid in full would not have been included in the scheme at all. The only reason the guaranteed landlords were not able to veto the arrangement, therefore, was that under a CVA all creditors form one class, and that class includes every creditor entitled to be given notice of the meeting, including those that were to be paid in full: "In effect, the votes of those unsecured creditors who stood to lose nothing from the CVA, and everything to gain from it, inevitably swamped those of the guaranteed landlords who were significantly disadvantaged by it."

134. At [109], Etherton J thought it was obvious that such a result was "wholly outside" the contemplation and intention of the authors of the Cork Report.

135. As to the application of the "reasonable and honest man" test, at [96] Etherton J said that while he agreed with Warren J in *Sisu* that if a reasonable and honest man in the same position as the claimants might reasonably have approved the CVA, that was a powerful "and probably conclusive" factor against the claimants on the issue of unfair prejudice, he also accepted that the fact that no reasonable and honest man in the same position as the claimants would have approved the CVA is not necessarily conclusive in their favour.

136. Mr Arden QC next referred to *Sixty*, in which similar considerations to those in *Powerhouse* arose. The CVA provided for payment in full of most of the company's creditors but sought to compromise the claims of landlords of various closed stores both as against the company and as against the parent as guarantor of the leases. The leases had many years to run, but the CVA compromised the landlords' claims by purporting to pay 100% of the estimated liability to the landlords on surrender of the leases.

137. Henderson J concluded (at [70]) that the CVA was unfairly prejudicial for similar reasons to those of Etherton J in *Powerhouse*: the guaranteed landlords would have been better off in a liquidation; they would have formed a separate class for the purposes of a scheme of arrangement, which they clearly would have vetoed; and the CVA was passed by the votes of the unsecured creditors, who stood to lose nothing from the CVA and whose votes inevitably swamped those of the guaranteed landlords.

138. It also failed the horizontal comparator because in at least two instances there was no proper justification for the differential treatment of other creditors. In particular, the debt payable to two entities associated with the company was unimpaired by the CVA (albeit one was deferred). At [81] Henderson J concluded that, although the dividend of 28p/£ to the compromised landlords was justified as being higher than they would receive *from the company* in a liquidation, that still left unanswered the question why the landlords of closed stores suffered the burden of their claims being compromised when the associated companies retained their right to payment in full.

139. It is not often that a court is required to consider, when sanctioning a scheme, circumstances where (1) a sub-group of creditors within a class has a special interest not shared by other members of the class; (2) that special interest was the dominant cause for that sub-group voting in favour of the scheme; and (3) the vote of that sub-group was material in obtaining the requisite majority at the class meeting.

140. This situation did arise, however, in *Re Lehman Brothers International (Europe)* [2019] EWHC 1980 (Ch). Hildyard J concluded that it was appropriate to sanction the scheme. At [109] he noted that the choice for the court was between (a) discounting the weight given to the majority vote and considering the fairness of the scheme without adopting any particular presumption in favour of the majority or (b) altogether disregarding the relevant votes of the special interest creditors, so that they do not count towards the majority (in which case if the votes of other creditors were insufficient to reach the required statutory majority, the scheme must fail, c.f. *Gertner* (above) in the CVA context). Having reviewed the authorities in which the distinction between discounting and disregarding votes was drawn, he rejected the argument of the administrators in that case that the court should only disregard votes as a last resort. If anything, he preferred the reverse approach, saying:

> "The court has always been, and should always be, especially disposed to guard against coercion of a minority by a self-interested majority. I would prefer to leave it that the discretion is to be exercised according to all the circumstances of the case, including (often most importantly) the level of support from unconnected creditors and the court's view of the balance of benefit offered by the scheme."

141. Mr Smith QC contended that the exercise of the court, in a case where the requisite majority at a meeting of creditors for a CVA had been achieved by reason of the votes of creditors who received different treatment from those who were objecting to the CVA, was essentially the same.

142. He submitted that this had always been the case, but that it is particularly so since the enactment of the Corporate Governance and Insolvency Act 2020 ("CIGA") and its insertion into CA 2006 of Part 26A, relating to the plan of reorganisation, and the "cross-class cram-down" power in section 901G. Under that section, the court has a power to sanction a plan (which shares most of the features of a scheme of arrangement under Part 26 of CA 2006) even where one or more classes of creditors has not approved the plan by the requisite majority, provided two conditions are met. The first condition is that none of the members of the dissenting class would be worse off under the plan than they would be in the "relevant alternative" (being the most likely alternative if the plan were not sanctioned). The second condition is that at least one class, who would receive a payment or have a genuine economic interest in the company in the event of the relevant alternative, has approved the plan.

143. The test for class composition in a plan is the same as for that in a scheme: see, for example, *Re Virgin Atlantic Airways Ltd* [2020] EWHC 2191 (Ch), per Trower J at [45] to [48]. Part 26A is thus important because it permits the court to approve a plan notwithstanding there are (for example) two sub-groups of creditors with rights so dissimilar that they *cannot* consult together in their common interest, and the requisite majority is obtained by the votes of only one of those sub-groups.

144. The Part 26A jurisdiction is relatively new, and there is so far only one case which has explored in any depth the circumstances in which the discretion to cram down a dissenting class should be exercised: see *Re Deep Ocean 1 UK Ltd* [2021] EWHC 138 (Ch). That case involved three linked restructuring plans for three companies in the Deep Ocean Group. In respect of two of the companies, the statutory majorities were achieved in each of the meetings summoned by the court. In relation to the third company, DSC, two meetings were summoned, one for secured creditors and the other for unsecured creditors. The meeting of secured creditors approved the plan by the requisite majority, but the meeting of unsecured creditors approved the plan by a majority representing only 64.6% of the class. The threshold conditions were both met. As to the first condition, Trower J considered (at [35]) that whether a creditor would be "worse off" than in the relevant alternative was to be assessed more broadly than merely by reference to financial return. It was necessary to take into account the impact of the restructuring plan on "all incidents of the liability to the creditor concerned".

145. In sanctioning the plan, and applying the cross-class cram-down under s.901G of the 2006 Act, Trower J (at [44] to [66]) identified the appropriate starting point as the approach adopted by the court in deciding whether to sanction a scheme of arrangement, but without the court's reluctance to differ from the meeting in a scheme context (because by its very nature the power under that section contemplates the court overriding the wishes of a class meeting). He considered the court should focus on the negative question, whether it was appropriate to refuse to sanction the plan because it was not just and equitable and that an applicant would have a fair wind behind it if the two threshold conditions were satisfied. Of particular relevance to his decision to sanction the plan in that case were:

(1) The dissenting class were out of the money in the relevant alternative (such that they could have been excluded from a Part 26 scheme by virtue of the principle in *Re Tea Corp* [1904] Ch 12), so their receipt of any benefits under the plan meant that they were unlikely to have been treated in a manner that was not just and equitable;

(2) The benefits under the plan were to be provided by a third party, which was a powerful pointer in favour of exercising the cram-down power; and

(3) The overall support among creditors for the three companies' proposals and, in particular, the substantial support of creditors of the other companies who were in essentially the same position as the dissenting class of DSC creditors.

146. By analogy with the horizontal comparator test applied in a challenge to a CVA, Trower J said that the court would be particularly concerned "…to ascertain whether there had been a fair distribution of the benefits of the restructuring (what some commentators have called the "restructuring surplus") between those classes who have agreed the restructuring plan and those who have not." As to this, (a) the difference between the treatment of the secured creditors and those in the dissenting class was readily explained because of the secured nature of the former's claims; (b) the horizontal comparison test was less significant where the benefits under the plan are derived from sources other than the plan company and the dissenting class are out of the money in the relevant comparator; and (c) so far as some creditors had been excluded altogether from the plan, that was justified on commercial grounds.

147. One feature of the scheme fairness test is that the court is concerned only with the terms of the scheme actually proposed; it does not enquire whether a different scheme might have been better for particular groups of creditors: see, for example, *Re Co-operative Bank PLC* [2017] EWHC 2269 (Ch), per Snowden J at [37]. In both *Sisu* (at [73]) and *Powerhouse* (at [82]), it was said that the same approach applies in the context of a CVA. There is a tension, however, with Ferris J's comment in *Re a debtor* (above, in a passage that was also cited with approval by Etherton J in *Powerhouse* at [88]) that in considering whether an arrangement creates unfair prejudice for a creditor it is necessary to look beyond a comparison with that creditor's position in bankruptcy because, among other things, the alternatives to the arrangement included the ability to press for a more satisfactory arrangement. There is similarly a tension with the approach suggested by Trower J in the context of the exercise of the cross-class cram-down power under Part 26A 2006 Act (with which I respectfully agree), that it is necessary to consider whether the plan involves a fair allocation of the "restructuring surplus" between different sub-groups of creditors.

148. In each of the cases referred to above, in which the fact that the CVA was approved by reason of the votes of creditors of the company who were unimpaired by the CVA, there was a finding of unfair prejudice. Mr Smith QC, however, pointed to *Re Portsmouth City Football Club Ltd* [2010] EWHC 2013 (Ch), where the challenge to the CVA failed. In that case, the football club was in administration. As a result, the Football League had the right to transfer the club's share in the Football League to another person, and under the rules of the Football League the administrator could only sell the club's undertaking if under the sale contract the purchaser agreed to pay certain non-preferential creditors (the "football creditors") in full and if the exit from the administration was a CVA.

149. A CVA was proposed under which the unsecured creditors (principally HMRC) would receive a dividend of 20p/£, but the football creditors would be paid in full by the Football League (as a deduction from payments that would otherwise be made to the football club).

150. In considering whether the CVA was unfairly prejudicial to HMRC, Mann J first noted, at [67], that it was not entirely clear that the CVA provided for the football creditors to be paid in full, as opposed to acknowledging that they would be dealt with elsewhere. At [68], however, insofar as the CVA provided for football creditors to be paid in full, he held that it was not unfair because it did not do so at the expense of other creditors at all. They were not paid out of assets that would otherwise fall into the CVA. Subject to an attack on the rule of the Football League requiring football creditors to be paid in full, the money out of which football creditors were to be paid in full would not otherwise come into the CVA or the football club in the events which had happened or were likely to happen. None of the possible alternatives to a CVA presented a picture that was more favourable to the unsecured creditors such as HMRC.

151. At [72] to [74], Mann J addressed the argument that the HMRC was unfairly prejudiced because it had been voted down by the football creditors who had no interest in the outcome, because they were going to be paid in full. Approaching this point on the assumption that if the relevant votes were taken out of account the statutory majority would not have been reached, he nevertheless concluded that there was no unfair prejudice. Though he found the argument troubling, he rejected it because the football creditors *were* creditors of the company and did have an interest in the outcome of the CVA because it would enable the balance of their contracts to be honoured, whereas in a liquidation their employment would come to an end. Furthermore, he thought that it was not unfair that HMRC were left financially better off by the CVA than a liquidation.

152. The same Football League rule was also the subject of the *Wimbledon* case (above). In that case, the CVA purported to compromise the preferential debts of HMRC. Football creditors were to be paid in full. The principal issue, there, however, was whether there had been a material irregularity, being the failure to comply with section 4(4)(a) IA 1986 (which provides that no arrangement may be approved under which any preferential debt is paid otherwise than in priority to the non-preferential debts of the company). Lightman J and the Court of Appeal concluded that there was no material irregularity, because section 4(4)(a) applied only to payments out of the assets of the company, and the payments to football creditors were to be made out of third-party funds.

153. Lightman J (but not the Court of Appeal) dealt also with the issue of unfair prejudice. Having summarised the law (as set out above at [112]), he concluded (at [23]) that the only practicable course available to the administrators was to enter into the agreement and proceed with the CVA: "The alternative advocated by the Revenue, in their single-minded pursuit of their principled objection to the payment in full of the priority debts, can only bring down the whole edifice and secure a nil return for all concerned." The possibility of unfair prejudice arising from the fact that the statutory majority was reached by the votes of the football creditors was not raised in that case.

154. The facts in *Portsmouth* were extreme. As I have pointed out above, the decision was distinguished in *Gertner* (in considering whether allowing a creditor with preferential treatment to vote was a material irregularity). That was on the basis that the football creditor rule was a standard published requirement which pre-dated the insolvency of the clubs in question, and which protected a defined class of creditors and applied to all clubs in the event of insolvency. Moreover, I consider it to have been critical to the conclusion in *Portsmouth* that the money to pay football creditors could never have been available to pay the ordinary unsecured creditors.

*Conclusions*

155. As a preliminary point, Mr Smith QC pointed out that the Applicants' case, that a CVA cannot encompass different deals with different groups of creditors, runs counter to the result in at least some of the cases under IA 1986 referred to above. That undoubtedly provides a difficult starting point for the Applicants' argument, but since the point on jurisdiction was not taken in any of those cases, this fact alone is not fatal to the Applicants' case.

156. Nevertheless, for the reasons I set out below, I consider: (1) that a CVA that provides for different treatment of different sub-groups of creditors is not for that reason outside the jurisdictional scope of section 1(1) or necessarily unfairly prejudicial; and (2) that it is not necessarily unfairly prejudicial to a sub-group of compromised creditors that the statutory majority is achieved, in respect of such a CVA, by the votes of unimpaired creditors or those who receive substantially different treatment. That, however, will be a highly relevant factor in determining whether, in any given case, there is unfair prejudice.

157. I deal, first, with a short point of construction on section 1(1). Mr Arden QC submitted that a proposal for a CVA can only constitute a "composition" or an "arrangement" within section 1(1) if, having regard to the existing rights of creditors and the rights conferred by the proposal, all of the creditors are able to consult together in relation to the proposal with a view to their common interest; in other words if all of the creditors would fall into a single class if the terms of the proposal had been contained in a scheme of arrangement under the Companies Acts.

158. It is common ground that, if this was an accurate statement of the law, the Proposal would fail that test, since it involves at least three separate deals with different groups of creditors as summarised in [66] above.

159. The Applicants' argument is based principally on the reasoning of Chadwick LJ in *Re Hawk Insurance* [2001] EWCA Civ 241, addressing the test for class composition established in *Sovereign Life Assurance Co v Dodd* (see above at [79]) based on a sufficient similarity in rights.

160. In *Hawk*, Chadwick LJ, at [13] to [16], said that the basis upon which the decision whether to summon more than one meeting was to be made was, self-evidently, to ask the question: "between whom is the proposed compromise or arrangement to be made?". Where, applying Bowen LJ's test, there were

distinct groups of creditors, the creditors in each of which were able to consult together with a view to the common interest of that distinct group, but were unable to consult together with a view to a common interest with creditors in the other groups, then the true analysis was that there were separate, but linked, arrangements with each distinct group.

161. Mr Arden QC submitted that the same meaning should be ascribed to the term "arrangement" in section 1(1). Since the legislation mandated only one meeting at which all creditors of the company were permitted to vote, it followed that a CVA could only be used where the rights of all creditors were such that they would form only one class under Bowen LJ's test.

162. Mr Arden QC referred to a number of other cases which have applied the reasoning in *Hawk*. None of them, however, adds anything to the short point he seeks to derive from Chadwick LJ's judgment in *Hawk*.

163. I do not accept that "arrangement" in section 1(1) IA 1986 is to be construed in the same way as in section 895(1) CA 2006, so as to limit a CVA to an arrangement in which the rights of all creditors are such that they can consult together with a view to their common interest.

164. What falls to be construed is not the word "arrangement" alone, but the following different phrases:

(1) In section 895(1) CA 2006, "a compromise or arrangement … between a company and … its creditors or any class of them"; and

(2) In section 1(1) IA 1986, "a composition in satisfaction of its [the company's] debts or a scheme of arrangement of its affairs".

165. Under section 899(1) the court has jurisdiction to sanction a scheme only where it is approved by a meeting or meetings of a class or classes of creditors. The section creates (self-evidently, as Chadwick LJ said) a distinction between different types of scheme: those which involve a single arrangement between the company and all its creditors; and those which involve distinct arrangements between the company and two or more classes of creditors. These are mutually exclusive alternatives.

166. Chadwick LJ's reasoning is thus premised on the fact that section 895(1) requires an analysis of whether there is a single arrangement with all of the creditors or a number of separate arrangements with different classes of creditors. The reasoning is simply inapplicable to section 1(1), where there is no such requirement. Section 1(1) contains no reference to, let alone a jurisdictional requirement for, an arrangement between the company and a class or classes of its creditors. I do not think, therefore, that the analysis in *Hawk* requires the meaning of "arrangement" in section 1(1) to be read down in the way the Applicants contend.

167. Turning to the broader points advanced by the Applicants, although I accept that the principles of good faith and equality developed in the 19th century continue to shape the meaning of both material irregularity and unfair prejudice, they do not lead to the conclusions advocated by the Applicants.

168. First, it is significant that parliament implemented a procedure, with greater flexibility in mind than was available under the existing law, where *all* creditors were to be included and were to have the right to vote, notwithstanding that some creditors were positively required to be given a different treatment.

169. In particular, as I have noted above, section 4 IA 1986 acknowledges that the single arrangement may involve different treatment of secured creditors and preferential creditors. It is implicit in section 4(3) (which provides that no proposal can be approved which affects the right of a secured creditor to enforce its security, without the concurrence of that creditor) that the concurrence of the secured creditors may be obtained on terms (for example as to the way in which the secured assets will be dealt with as part of the CVA) that differ from the terms that are offered to the general body of unsecured creditors. For reasons which I develop below (at [249 to 254]), I consider that to be the proper analysis of what happened in this case so far as the SSN Holders are concerned. The legislation nevertheless mandates that both secured and preferential creditors are given notice of the meeting and are entitled to vote at it (in the case of secured creditors, in respect of the unsecured portion of their debt).

170. Second, the Applicants accept that a CVA may provide for different treatment of creditors in other ways, particularly where it is necessary for reasons of business continuity to do so (as in *Debenhams*) or where the existing rights of creditors in the context of the insolvency of the company mean that it would be unfair to impose the same treatment on them (as in *Sea Voyager Maritime Inc v. Bielecki* [1999] 1 All ER 4 628, see above at [112]). It has been firmly established that although differential treatment of different groups of creditors is a cause for enquiry (see, for example, Ferris J in *Re A Debtor*, below, at p.63c), which needs to be justified (see, for example, Henderson J in *Sixty*, below, at [67]), it is not inherently unfairly prejudicial.

171. These first two points are significant because, if a CVA was necessarily outlawed where the requisite majority was obtained with the votes of unimpaired or differently treated creditors, that might well be the case even though only a small proportion of the creditors were unimpaired or received different treatment. The only workable method for calculating whether the statutory majority had been achieved by reason of such votes would be to determine whether the majority would have been achieved without their votes. That would, in effect, involve a re-writing of the Rules, to impose an additional threshold condition, alongside that in Rule 15.34(4) relating to unconnected creditors. The fact that the Rules contain a specific provision to deal with connected creditors, but nothing in relation to other possible sub-groups of creditors, militates against implying the threshold condition which the Applicants' case would require.

172. In addition, the consequence would be the same whether, for example, the compromised creditors voted 20% in favour of the CVA (being swamped by a large proportion of unimpaired creditors) or the compromised creditors voted 74.9% in favour of the CVA (so that a very small amount of unimpaired creditors pushed the vote above the requisite majority). This points towards a more flexible approach where the fact that the statutory majority was achieved by virtue of the votes of unimpaired creditors is no more than a factor, albeit an important one, the strength of which varies with the extent to which it can be said the vote of the compromised creditors is 'swamped'.

173. Third, so far as the pre-1986 position is concerned, I accept that the researches of Counsel were not able to unearth any case prior to 1986 in which a composition or arrangement had been made, whether by an individual or by a company, which involved substantially different deals with separate groups of creditors, other than through the use of a scheme of arrangement under the Companies Acts. I also accept that the principles of good faith and equality, as developed in the 19th century cases referred to above, point against a compromise being imposed upon a creditor or sub-group of creditors by virtue of the votes of a "self-interested majority" where, for example, the majority of creditors are offered substantially better terms.

174. It is not surprising, however, that there is no example of such a pre-1986 case involving a company in light of the fact that the only legislative provision for an arrangement with creditors other than a scheme of arrangement was rarely used and rendered mostly redundant by Maugham J's decision in *Re Contal Radio* that it had to be followed by a winding-up.

175. More broadly, IA 1986 marked a significant departure in corporate insolvency law in providing frameworks for rescuing companies that, although insolvent or likely to become insolvent, had a viable business. The administration procedure, also introduced by IA 1986, is one such framework, but the CVA (whether or not preceded by an administration) is another. It is no coincidence that, aside from secured and preferential debts, the type of differential treatment of creditors that has consistently been permitted in CVAs is that which is essential to the rescue of the business, i.e. where payment in full of, e.g., suppliers, is needed to ensure business continuity.

176. The same issue does not appear to have arisen in any of the composition or arrangement cases involving individual debtors prior to 1986. As noted above, the arrangement introduced by the 1883 Bankruptcy Act applied only after a receiving order had been made. Mr Smith QC pointed out that, while debtors had used that procedure to avoid a bankruptcy order, the arrangements were generally straightforward in providing a distribution which mirrored the rights of creditors in bankruptcy. A debtor generally survives bankruptcy, in contrast to winding-up which marks the death of the company. In none of the cases cited to me under the pre-1986 legislation involving an individual debtor, therefore, was there a need to fashion an arrangement so as to differentiate between ordinary creditors and those whose continued support was necessary for the continuation of the debtor's business.

177. Although the Australian equivalent to the provision introduced by section 136 of the Companies Act 1862 has been interpreted as requiring equal treatment of creditors, none of the Australian cases cited to me involved an arrangement to enable the survival of a company's business, but were concerned with arrangements to enable the assets of more than one insolvent company to be pooled for the purposes of distribution. (Mr Smith QC also submitted that the reliance placed in *Kassem* on the English authority of *Re Trix Ltd* must be seen in the light of the fact that in the subsequent English case of *Re Bank of Credit and Commerce International SA (No.3)* [1993] BCLC 1490, Sir Donald Nicholls VC declined to follow *Re Trix*. He permitted a pooling arrangement in respect of two companies in the BCCI group to be undertaken using the compromise powers of a liquidator under schedule 4 IA 1986. I do not think this takes his argument any further, however, particularly as Sir Donald Nicholls VC himself noted that any departure from the *pari passu* principle ought to be undertaken via a scheme of arrangement and that the reason that was not done in *BCCI* was because it was simply not feasible to call a meeting of BCCI's creditors.)

178. In light of these factors, the absence of pre-1986 cases where an arrangement had been approved notwithstanding it contained different treatment for different groups of creditors is of limited relevance to the construction of section 1(1) IA 1986, even though its language is similar to that in the 1883 Bankruptcy Act.

179. Fourth, the approach taken in *Kapoor* and *Gertner*, of disallowing altogether the votes of a creditor offered preferential treatment, is not necessarily to be followed where a creditor or sub-group of creditors is given preferential treatment by the terms of the CVA. As I have noted when dealing with those cases, there was something more, in each of them, than the mere fact of preferential treatment which constituted a breach of good faith. Moreover, in each case the court stressed the public policy considerations that apply in bankruptcy, which do not have a direct corollary in corporate insolvency: see Etherton LJ at [67] in *Kapoor* and Patten LJ at [80] of *Gertner*.

180. Fifth, in light of the cross-class cram-down power introduced by CIGA, it cannot (now, at least) be said that there is an incontrovertible principle that creditors should not have their debts compromised by a statutory majority unless the majority and minority shared sufficiently similar rights that they could consult together on the proposal with a view to their common interest.

181. Sixth, as to Mr Arden QC's submission based on the Cork Report, I accept the contention that the report's authors envisaged that CVAs would be used for relatively simple cases. That is insufficient, however, to read down the wording of section 1(1) so as to exclude either a CVA for large companies or arrangements where different creditors or classes of creditors are treated differently.

182. It is impossible to imply any limitation to "small" companies. "Company" is defined by section 1(4) without any such limitation. Moreover, parliament has expressly carved out special treatment for "small companies" in Schedule A1, including the entitlement to obtain a moratorium in conjunction with a CVA

(see section 1A), but has not chosen to limit CVAs altogether to such companies..

183. As for the limitation to relatively simple cases, I accept Mr Smith QC's submission that it is difficult to see what legislative relevance the Cork committee's view has in this respect. That is particularly so when a key part of their recommendations was not adopted in the legislation. The committee envisaged that a voluntary arrangement might affect and be made with some only of the debtor's creditors (see paragraphs 373-375), but the legislation, as enacted, provides for a single arrangement with all creditors. This meant that the committee did not need to grapple with the question as to how the underlying principle of equal treatment between creditors might apply to an arrangement that must include all the company's creditors. The parties have been unable to identify anything in the White Paper or the passage of the bill (for the Insolvency Act 1985) through the Houses of Parliament which sheds light on Parliament's intention in not adopting that particular aspect of the proposal in the Cork Report.

184. Moreover, other parts of the Cork Report stressed the intended flexibility of the new procedure, including that a basis of distribution other than *pari passu* might be adopted, so as to enable advantages accruing to creditors from the provision of third-party money or after-acquired property: see paragraph 364(2) of the Cork Report; *IRC v Wimbledon Football Club Limited* [2004] EWCA Civ 655 at [52], per Neuberger LJ, stressing the flexibility of the CVA procedure.

185. Seventh, while it is true that in each of *re a Debtor*, *Powerhouse* and *Sixty,* the fact that the requisite majority was achieved by the votes of unimpaired creditors led to a finding of unfair prejudice, in none of those cases was it said to be determinative by itself. The court in each case emphasised the need to have regard to all the circumstances. Further, both Warren J (in *Sisu*) and Etherton J (in *Powerhouse*) said that the fact that compromised creditors formed a sub-group that could have blocked a scheme was not enough by itself to constitute unfair prejudice.

186. Accordingly, while I accept that, taking into account the basic principles of good faith and equality, the fact that a statutory majority for a CVA is achieved by the votes of unimpaired or differently treated creditors will be an important consideration in determining whether unfair prejudice exists, I do not accept that those principle necessarily lead to a finding that a CVA achieved in those circumstances is unfairly prejudicial.

187. As against this, Mr Smith QC submitted, based on the authorities I have reviewed extensively above, that a CVA approved in such circumstances would not be unfairly prejudicial provided that: (1) any differential treatment was objectively justified; (2) the vertical comparator was satisfied; and (3) a reasonable and honest person in the position of the applicant could have approved the CVA. He submitted that these criteria were clearly satisfied in this case.

188. I do not accept that the position is as straightforward as Mr Smith QC's submission suggests. His analysis does not pay sufficient regard to the basic principle of equality and, in particular, the importance (as demonstrated in the pre-1986 cases cited above at [73] to [80]) of ensuring that a statutory majority shares sufficiently similar rights with the minority it seeks to bind.

189. On Mr Smith QC's case, provided that the vertical comparator is satisfied and any differential treatment is justified, then the only other requirement is that an honest and reasonable person in the position of the applicant could have approved the CVA. Unless the honest and reasonable person test is just a proxy for the court having to take into account all the circumstances, however, it is difficult to see what it adds to the vertical comparator test: it would invariably be possible to posit an honest and reasonable person who could conclude that it was better to approve a CVA because it offered a better outcome to it than a liquidation.

190. Put another way, where a sub-group of creditors is compromised by a CVA and their vote was swamped at the creditors' meeting by the votes of those who were unimpaired by the CVA, I do not think that it is necessarily enough to avoid a finding of unfair prejudice that the differential treatment of others was objectively justified (e.g. because they were critical creditors), and the compromised creditors are treated more favourably than they would be in the relevant vertical comparator.

191. Whether unfair prejudice exists depends on all the circumstances, including those that would be taken into account in exercising the discretion to sanction a Scheme, per Hildyard in *Lehman* (above), and in exercising the discretion to cram-down a class in a part 26A plan.

192. Without attempting to define what all the circumstances in any case might be, I make the following four points which are of particular relevance on the facts of this case.

193. First, an important consideration is whether there is a fair allocation of the assets available within the CVA between the compromised creditors and other sub-groups of creditors. That will include considering the source of the assets from which the treatment of the different sub-groups derives, and whether they would or could have been made available to all creditors in the relevant alternative.

194. For example, if secured creditors receive favourable treatment solely by reference to the existence of their security so that, insofar as they are unsecured creditors and thus vote at the creditors meeting they are treated no better than other creditors, then the fact that their vote was decisive in approving the CVA is unlikely to be unfair.

195. In contrast, if assets that would, in the relevant alternative, have been available for all unsecured creditors are allocated in a greater proportion to other creditors (e.g. where critical creditors are paid in full), then the fact that the requisite majority was reached by reason of the votes of those creditors may

point towards the CVA being unfairly prejudicial, even if there was an objective justification for their payment in full.

196. For the reasons I have expressed at [147] above, in considering whether the allocation of assets is fair, the court is necessarily required to consider whether a different allocation would have been possible, so the principle adopted in scheme cases, against considering whether an alternative arrangement would have been fairer, needs to be modified.

197. A second important consideration will be the nature and extent of the different treatment, the justification for that treatment, and its impact on the outcome of the meeting. There would be strong grounds to conclude it was unfairly prejudicial where a CVA, which compromises the claims of a sub-group of creditors, is achieved only because of the votes of a large swathe of creditors who are unaffected by the CVA, even if there was an objective justification for those creditors being unaffected by the CVA. As was pointed out in *Powerhouse*, that could *not* have been achieved in a scheme, not because the unaffected creditors would have formed a separate class, but because they would not have been included in the scheme at all: see *Sea Assets Ltd v Perusahaan Perseroan (Persero) PT Perusahaan Penerbangan Garuda Indonesia* [2001] EWCA Civ 1696. On the other hand, if CVA creditors are impaired, but in different ways, or where the creditors who were (justifiably) unimpaired, though sufficient on the numbers to tip the scales at the meeting, were small in number and value, then that is less likely to constitute unfair prejudice.

198. Third, it is also relevant to have regard to the extent to which others in the same position as the objecting creditors approved the CVA: c.f. *Lehman* (above), at [129] to [130]), in the case of a scheme; and *Deep Ocean*, (above) at [59], in the case of a Part 26A plan.

199. Fourth, a finding of unfair prejudice ought not to be precluded merely because the same result might have been achieved in a part 26A plan. As Mr Arden QC pointed out, the process under part 26A contains important safeguards for creditors that are absent from the CVA process. Most importantly, there is significant court oversight *before* the scheme becomes effective. In particular, the court is closely involved with identifying whether the class meetings are properly constituted before they are convened. Creditors know at the outset, therefore, with whom they are to consult and are able to negotiate with the company and other groups of creditors with clarity as to the strength of their position. In addition, creditors are likely to have significantly more time to consider the plan, and to consult with other creditors, before the plan meeting: all creditors are required to be sent a "practice statement letter" sufficiently in advance of the convening hearing so as to enable creditors to have an effective opportunity to appear at and take part in the hearing; and the court will direct that the period of notice for the class meetings is sufficient in all the circumstances, including the complexity of the plan. In contrast, in a CVA creditors are entitled to receive only one notice within a much tighter timetable: not less than 14 days before the decision date, but not more than 28 days from the date the nominee's report was filed at court: IR 2016, Rule 2.27.

H: Were the Compromised Landlords unfairly prejudiced in this case?

200. I turn to consider the Applicants' contention that the Compromised Landlords were unfairly prejudiced on the facts of this case. The Applicants point to three broad elements which, individually or collectively, are said to have given rise to unfair prejudice: (1) the inherent unfairness in numerous modifications to the terms of the leases, in particular the permanent reduction in rent; (2) the differential treatment, *per se*, afforded to (a) the SSN Holders and (b) the Ordinary Unsecured Creditors; and (3) the fact that the requisite majority at the creditors' meeting was secured with the votes of those groups of creditors.

201. As a preliminary point, it is common ground that, aside from questions relating to the payment of future rent where New Look remains in possession of the relevant premises, Compromised Landlords receive more under the CVA than they would have done in the event of an administration of New Look. To that extent, the vertical comparator is satisfied in this case.

*The modifications to the terms of the leases of Compromised Landlords*

202. The Applicants' main objection under this head is to the reduction in rent and other modifications to the leases. They object in particular to the change to turnover rent, which is said to be unfair in principle because "it involves the fundamental reallocation of commercial risk and deprives such landlords of their bargain". They also object to: the continued reduction in rent for Category B Landlords beyond the expiry of the Rent Concession Period; the move to payment of rent in arrears; the release of "keep open" covenants (which impact on the extent to which turnover rent would be paid); the limitation on New Look's obligations to pay rent by reference to amounts in fact received from sub-tenants; and the release of New Look's obligation to enter into an 'authorised guarantee agreement' upon an assignment of a lease.

203. The first way in which this objection is framed is that a CVA *cannot* operate to reduce future rent (or make other adjustments to the terms affecting the ongoing rights and obligations under the lease) while permitting the tenant company to remain in possession, because it is inherently unfair on the landlords. Mr Arden QC acknowledged that this point had been decided against him by Norris J in *Debenhams* (at [62] to [82]), but invited me to depart from this part of Norris J's decision.

204. In *Debenhams* the CVA placed landlords into a number of categories, depending on the extent to which (among other things) future rent was to be reduced.

205. As in this case, the compromised landlords had the option to terminate their leases. It was accepted that the right to terminate the leases would in principle eliminate any unfairness: see [69] of Norris J's judgment.

206. The argument that a CVA could not impose a reduced rent while the company remained in possession of the premises related, therefore, only to the termination notice period. By analogy with the "expenses principle" applicable in liquidation or administration, it was said that basic fairness

required that a company which made beneficial use of premises let to it must pay contractual rent referable to that period of occupation.

207. Norris J rejected that argument. He accepted (at [66]) that, normally, it would seem wrong that a tenant should be able to trade under a CVA for the benefit of past creditors at the present and future expense of its landlords (citing *Thomas v Ken Thomas Ltd* [2007] Bus LR 429, per Neuberger LJ at [34]), but that it was not necessarily so. In particular, he considered that, in a case where short-term creditors charged prices that reflected current market prices but lease liabilities were set at amounts that far exceeded current market value, it was not *necessarily* unfair for landlords to receive less than their contracted-for rent.

208. At [71], he concluded that "basic fairness" did not require a choice between full rent as an expense or a dividend at the rate paid on unsecured debts generally, but in the context of a jurisdiction which permits the modification of obligations it did require two things. First, that a landlord should receive at least the market value of the property it was providing and, second, that contractual rent should be interfered with to the minimum extent necessary in the circumstances, "the modification being limited to what is necessary to achieve the purpose of the CVA."

209. As to whether the reduction in future rent was unfair on the facts, Norris J referred to *Powerhouse* for the relevant principles, noting (at [12] to [13]) that it was necessary to consider all the circumstances, including the vertical and horizontal comparators and the justification offered for any differential treatment. At [75] he accepted that satisfaction of the vertical comparator did not in itself mean the CVA was fair, because fairness must be considered in the round. The critical feature of the CVA that rendered the reduction in rent fair was the ability of the landlords to bring to an end the varied relationship: see [76].

210. In their skeleton argument Mr Arden QC and Mr Shaw contended that Norris J erred "…in concluding that market rent is all that is required in order for a retail CVA to satisfy the requirement of fairness".

211. I do not accept that this is an accurate characterisation of what Norris J decided in *Debenhams*, for the following reasons. First, as I have noted, in concluding that the reduction in rent was not unfairly prejudicial to the landlords he applied the test derived from *Powerhouse*, emphasising that it is necessary to take into account all the circumstances. At [71], Norris J was doing no more than considering what was sufficient to preclude a CVA being <u>necessarily</u> unfair. Second, in that respect he did not say that market rent alone was sufficient; the interference also had to be no more than necessary to achieve the purposes of the CVA. Third, this conclusion in any event only related to the rent falling due during the termination notice period (see the last sentence of [71]), it being common ground that the termination right was an answer to the objection that the longer-term reduction in rent was unfairly prejudicial.

212. Mr Arden QC acknowledged that, although I am not bound by Norris J's decision, I am constrained in departing from it. In fact, Mr Arden QC did not specifically seek to persuade me that the decision was "plainly wrong", which is the applicable test. In any event, I am not persuaded that Norris J was wrong to conclude that a CVA which provides for a reduction in future rent during a notice period before which the landlord can terminate the lease is necessarily unfairly prejudicial.

213. Reading Norris J's judgment as a whole, even in relation to the allegation relating to the reduction of rent in the termination notice period, I do not understand him to have laid down a rigid test that the CVA could only escape a finding of unfair prejudice if at least market rent was paid and the interference was the minimum necessary to achieve the purposes of the CVA. If he did, then I respectfully disagree that there is such a rigid test. Whether it is in fact unfairly prejudicial can only be answered by reference to all the circumstances. While that includes both of the points referred to by Norris J, it also includes what the position would have been (so far as entitlement to, and likely recovery of rent, are concerned) in the relevant vertical comparator.

214. I can see considerable force in the contention that a permanent or long-term reduction in rent imposed on landlords without the option to terminate would be inherently unfairly prejudicial, certainly if achieved by the votes of other creditors who did not suffer the same treatment, but that is not the case here (and was not the case in *Debenhams*).

215. The second way in which this objection is framed is that the rent reductions and related modifications to the leases were "unfair" on the facts. As I understood this aspect of the Applicants' argument, it is separate from the contention that the modifications to the leases were unfairly prejudicial by reference to the differential treatment between different groups of creditors.

216. The difficulty with this argument is identifying any objective criteria by which it can be assessed whether modifications to a lease are, *per se*, "unfair". For example, by what criteria is the nature or extent of a reduction in rent to be evaluated? Is it inherently unfair to change to a turnover rent? Is it unfair to do so for the remainder of the term, but not for a specified period? Moreover, the fairness of the same modification may be different as between the company and one landlord, taking into account all the commercial circumstances between them, and as between the company and another landlord.

217. The answer suggested by Mr Arden QC was that the court is required to assess the modifications against the test (derived from *Debenhams*) that they must interfere with the landlords' rights only to the minimum extent necessary to achieve the objectives of the CVA. For the reasons given above, however, I do not accept that Norris J intended to set any new such "test" in the *Debenhams* case, even in relation to rent reductions during a termination notice period. He was certainly not laying down any general principle that modifications to leases, which landlords had the option to get out of, were necessarily unfair unless they were the minimum necessary.

218. I address below at [232] to [237] the question whether the modifications to the leases in this case, during the termination notice period, were unfairly prejudicial. In relation to the broader argument that the long-term modifications were unfair, I consider (in agreement with the concession in *Debenhams*) that the answer is provided in the landlords' right to terminate, provided that the terms offered to landlords upon exercise of that termination right are at least as beneficial as in the relevant vertical comparator.

219. This can be tested by reference to a simple case, where the vertical comparator is a liquidation, in which leases would be disclaimed and there would be only a very small return to landlords (in respect of the Disclaimer Damages Claim and any arrears) and to all other creditors in respect of their unsecured claims. It would be difficult to find unfair prejudice in a CVA, against that background, which compromised the claims of landlords to future rent, for a percentage return which, though small, was better than the return in a liquidation, and which gave all other unsecured creditors the same percentage return. It would be no different if the comparator was administration where, although there would be no power of disclaimer, there would be a similarly small return to all creditors and no prospect of the company being able to pay future rent.

220. In either case, the loss of future rent is not forced upon the landlords by the CVA, but is the consequence of the company's insolvency.

221. The key difference between those examples and this case (so far as the treatment of the Compromised Landlords is concerned) is that, while the comparator is an administration in which there would be no material financial return to unsecured creditors, there is a core business which is viable, albeit only if operated from fewer stores. Accordingly, the CVA offers all Compromised Landlords the choice between (1) terminating their lease and accepting a financial return that was better than in the relevant comparator or (2) continuing the lease but on reduced rent and modified terms. Again, the reduction in rent and modified terms are not forced on Compromised Landlord: the inability to pay full rent is the consequence of New Look's insolvency and the reduction in rent and other modifications only apply if the relevant Compromised Landlord does not opt to terminate its lease.

222. Provided, therefore (as it is in this case), the vertical comparator test is satisfied in relation to the returns offered to those landlords who opt to terminate their lease, I consider that it is not unfairly prejudicial to offer landlords that choice. The *fact* that the landlords are offered that choice, and the nature and extent of the proposed lease modifications, are matters to take into account when considering the differential treatment between landlords and other creditors. Differences in the terms offered as between different sub-groups of landlords may also be relevant (but no complaint is made in that respect in this case). As a practical matter, any company proposing such a CVA will need to ensure that the reduction in rent and other modifications to the leases are as fair to landlords as possible, because it will need a sufficient number of the landlords to opt to continue the leases if it is to have premises from which to trade. That, however, is a purely commercial question, the answer to which is provided by the number of landlords that opt to continue

their leases. The "fairness" of the modifications, *per se*, is not something which falls to be evaluated by the court as part of the unfair prejudice challenge.

223. The Applicants nevertheless object to the termination rights offered by the CVA to Compromised Landlords. They contend that they do not mitigate the unfairness of which they complain, for four reasons.

224. First, they contend that the "new" termination rights are incapable of mitigating unfairness where the Compromised Landlords already have termination rights. I do not accept this. The existing rights enable the landlords to terminate for non-payment of the reserved rent. The new right performs a different function - enabling the landlords to, as Mr Arden QC neatly put it, "get off the bus" altogether rather than submitting to the modifications imposed by the CVA.

225. Second, they contend that the CVA fails the vertical comparator test, because a liquidator or administrator could never unilaterally reduce rents while remaining in occupation of the premises: if the company remained in occupation of the premises in liquidation or administration, it would have to pay contractual rent as an expense. Insofar as this relates to the long-term position, it is answered by the termination right. In any event, I do not think that it is an accurate characterisation of the CVA to say that it unilaterally reduces rents. As I have already noted, the inability to pay future rents is caused by New Look's insolvency. That inability exists whether or not New Look goes into administration. Without the CVA, New Look would have no ability to pay anything in respect of future rent. The CVA thus offers landlords the option to continue to be paid *some* future rent, albeit at reduced rates, or to accept a slightly better financial return on their debt claims than they would get if New Look went into administration.

226. The Applicants nevertheless say that this does not adequately respect the negotiating rights of landlords who, given the expenses principle in administration, would have a strong bargaining position in terms of the rent to be paid in return for continued occupation. In contrast, the CVA removes the bargaining power of the landlords altogether. That, however, assumes a tenant company that was in a financial position, in administration, to continue to pay rent to the landlords. In the context of New Look's pre-pack administration, the most that landlords could expect was the possibility that the purchaser of the business (if one was found) would negotiate an assignment of the lease and be willing to fund the payment of rent as an expense in the administration pending that assignment. Mr Arden QC suggested that this was a more favourable position for a landlord to be in, than being able to re-let the premises in the market. That is inherently speculative, as it depends on who the purchaser is, the situation of the particular store, and the market for alternative tenants in that area, and it is not an assumption I can fairly make.

227. Third, the Applicants object to the absence of a rolling termination right, and contend that New Look's justification for this (the need for certainty from year to year as to the stores that will remain within its possession) is insufficient. The extent to which the landlord may – in the future – exercise a right of

termination in the event that it opts, at the outset of the CVA, to continue the lease is simply an aspect of the modification to the lease that it has opted to continue. For the reasons set out above (at [216] to [222]) the fairness of such a term is not something which it is for the court to evaluate, but a factor which each landlord can assess in exercising the choice the CVA presents to it.

228. Fourth, the Applicants object to the fact that the exercise of a termination right is in full and final satisfaction of the Compromised Landlords' claims. Since it is accepted by the Applicants that the return on Compromised Landlords' debt claims in the CVA (including the right to share in a fund of £600,000 for a Disclaimer Damages Claim) represents a better return than they would achieve in the relevant vertical comparator, I do not think this point gives rise to unfair prejudice.

229. More generally, the Applicants object to the lack of mitigating factors in the CVA, such as a profit share fund, which they contend exists in other CVAs and provides a potential "upside" to the Compromised Landlords. Without such potential upside, it is contended that the CVA is wholly unfair, because it obliged Compromised Landlords to fund the turnaround of the company's business following the disruption caused by Covid-19, but it is future equity that will alone reap the benefit of such turnaround. A comparison with what has happened in other CVAs is of no assistance (particularly where the other CVAs have not been the subject of any court decision). I consider (and dismiss) at [242 to 264] below the possibility that the differential treatment of the SSN Holders, who became entitled to participate in equity under the Scheme, unfairly prejudiced the Compromised Landlords. It is important to note that the current holder of equity in New Look lost out altogether in the restructuring. This is not a case, therefore, where creditors' rights are being compromised in order to benefit existing equity holders. In those circumstances, I do not think that the absence of a profit share fund, or other mitigating feature, was unfairly prejudicial to the Compromised Landlords in this case.

230. The Applicants also object to the termination rights granted <u>to New Look</u> on fairness grounds (in addition to the jurisdictional objection which I address below at [278 to 282]). So far as Category B Leases are concerned, New Look has the right to terminate at the end of the Rent Concession Period. That is, therefore, one of the modifications to the leases in the event that Category B Landlords opt to continue them. Again, for the reasons set out above (at [216 to 222]) the fairness or reasonableness of such a term is not something which it is for the court to evaluate.

231. As to Category C Leases, the Applicants contend that New Look's purported justification (that it was necessary to include such a term because the wider restructuring required it) is not made out. In the absence of any other justification, there is no "need" for the termination right and it therefore fails the *Debenhams* "minimum necessary" test. For the reasons I have set out above, I do not accept that *Debenhams* established such a new test. In fact, although called a "termination right", the CVA does not permit New Look to terminate the lease. The lease remains on foot, but New Look's obligations under it are released. There is no question of New Look retaining possession

of the Category C premises (since these relate to stores that were, or were about to be, closed). In substance, the Company's right of termination adds nothing (in terms of fairness) to the fact that the Category C Landlords' recovery in the CVA is limited to recovering two months' rent, service charge and insurance in full and a distribution of a small percentage in respect of dilapidations claims and Disclaimer Damages (which it is accepted is a greater return than they would receive in the vertical comparator).

232. I turn next to consider any alleged unfairness by reason of the fact that New Look was entitled to remain in occupation of the relevant premises during the notice period if a landlord had exercised its right to serve a termination notice. The Applicants did not focus specifically on this period (in contrast to the applicants in *Debenhams*), but it seems to me that it is necessary to deal with the point, because the CVA did impose on Compromised Landlords a reduction in rent for that period, from which they could not escape by an immediate termination of the lease.

233. This relates only to Category B Landlords, who were entitled to receive only turnover rent during the relevant period. Category C Landlords, in contrast, were entitled to receive rent at the contractual rate for the same period.

234. The answer to this point lies, in my judgment, in considering the likely circumstances of a pre-pack administration as the vertical comparator. That would have involved a short period of trading, during which New Look would have marketed the business for sale, followed by the appointment of administrators who would, immediately following their appointment, have executed a sale contract with the purchaser, if one had been found. In that event, Category B Landlords would have had the following principal rights: (1) to continue to receive rent at the contractual rate; and (2) to forfeit the lease in the event of non-payment of such rent.

235. As to the former, however, there was no realistic prospect of New Look being able to pay rent at the contractual rate to Category B Landlords. It had not done so since March 2020. The most that it had paid was a form of turnover rent as and when stores had been open. The prospects of receiving any payment at all in respect of rent in circumstances where the CVA had failed were worse, as the Group was forecast to run out of cash in October.

236. The right to forfeit, at the time of this CVA, was complicated by the Coronavirus Act 2020, which would have precluded the Category B Landlords from exercising a right of forfeiture based on the non-payment of rent, although would have permitted them to forfeit because of the promotion of the CVA. It is highly unlikely, however, that a Category B Landlord would have been able to instal a tenant paying rent in any of the premises before the end of the two-month notice period.

237. In short, therefore, if the CVA had not been approved, the most that the Category B Landlords could have hope for during the next two months was a remote prospect of recovering turnover rent for that period. That is no better, and probably significantly worse, than their rights under the CVA in that same period. Accordingly (and leaving aside the impact of the different treatment

of other creditors, and the extent to which the CVA was forced on Compromised Landlords through the votes of other creditors), I find that the reductions in rent for Category B Landlords during the notice period for termination of the leases was not unfairly prejudicial to them.

238. Finally, I should deal with the contention that in certain respects, the reduced rent under the CVA was below market rates. At an earlier stage in the proceedings, the Applicants sought to argue that this was true of turnover rent payable generally to Category B Landlords. In the absence of any expert evidence as to market value, however, that was abandoned save in respect of a very small sub-category of Category B1 Landlords (in which a cap is placed on the turnover rent). In relation to Category C Landlords, it is accepted that the reduction of rent to nil, after the notice period, must have the effect of reducing it below market rates.

239. In relation to rent falling due after the date the landlords could have terminated, however, the answer to the alleged unfairness lies – for the reasons given above – in the right to terminate. For the reasons already given, I do not accept that Norris J in *Debenhams* laid down a principle that modifications to a lease could not reduce the rent below market rates, certainly insofar as the period after the lease could have been terminated is concerned.

240. During the notice period, the rent payable to Category C Landlords was not reduced at all. As to the small sub-category of Category B Landlords (where there was a cap on turnover rent), the Applicant's argument fails due to lack of evidence as to market value. The most the Applicants could point to was that the proposed rent is less than New Look's own assessment of estimated rental value used for categorising the various leases. That falls far short of evidencing that the turnover rents for these premises is less than market value, certainly during the notice period of 60 days from the Effective Date. That is because the estimated rental values were prepared on the basis of a post-pandemic world, which was clearly not the case in September/October 2020.

241. The Applicants separately objected in their skeleton argument to the treatment of Category E CVA Creditors (who had guarantee claims against New Look) and to the different treatment in relation to premises in the Republic of Ireland. The latter point was abandoned (given that the leases were held by companies in the Group other than New Look). While the former point was not formally abandoned, in circumstances where none of the Applicants fall into this category, and there was a 70% turnout of Category E creditors, all of whom voted for the CVA, the point was not seriously pursued in argument and I reject it. Insofar as the Applicants relied on the point made by Henderson J in *Sixty*, that it is unfair for a CVA to re-write the fundamental bargain of guarantee by providing for a one-off payment, that is distinguishable here, where it is New Look that has the guarantee liability (not a solvent third party as in *Sixty*) and a guarantee liability would, in the relevant comparator, be subject to the same valuation and divided procedure as any other liability.

*Differential treatment of the SSN Holders*

242. In this section, I address the Applicants' contentions that there was no adequate justification for the differential treatment of the SSN Holders and that the Compromised Landlords were unfairly prejudiced because their rights were impaired, in the ways considered in the previous section, in circumstances where the statutory majority at the creditors' meeting was achieved by the votes of the SSN Holders.

243. It is correct to say that the SSN Holders' vote was critical in ensuring the statutory majority was obtained since, without it, the vote in favour of the CVA would have amounted to less than 75% by value of the creditors who voted at the meeting.

244. The Applicants put this argument primarily on the basis that the SSN Holders were wholly unimpaired by the CVA and it was unfair for the statutory majority to be obtained by the votes of wholly unimpaired creditors. While it is true that there is no term of the CVA which released either the debt or the security of the SSN Holders, I do not accept this argument, for two reasons.

245. First, it is necessary to see the CVA as an integral part of the wider restructuring which included the Scheme. There is no doubt that under the restructuring as a whole the SSN Holders' rights were impaired: they exchanged secured debt for a minority equity interest in New Look.

246. In *Re Uniq Plc* [2011] EWHC 749 (Ch), a scheme of arrangement was proposed, the end result of which was that shareholders would give up 90.2% of their equity in exchange for the company being discharged from its obligations under a pension scheme, thus leaving them with one-tenth of their original shareholding but in a company unencumbered by its liability to the pension fund. It was contended that this did not constitute a compromise or arrangement. In rejecting this argument, David Richards J said, at [24]:

> "If regard is had only to the terms of the scheme itself, the existing members see their 100% equity interest diluted to 9.8%, without any benefit to Uniq or themselves unless the restructuring as a whole is completed. If the restructuring is completed, a very substantial benefit is conferred on Uniq and, while the existing members' interests are reduced to 9.8%, they retain an interest in a viable company. It would, in my judgment, be artificial to confine the analysis to the terms of the scheme itself when the scheme forms an integral part of a restructuring which confers substantial benefit on the members bound by the scheme."

247. That was so, even though it was possible for the scheme to come into effect without the rest of the restructuring occurring, since that was neither intended nor likely.

248. In the present case, although the Scheme followed the CVA, and although the CVA was not formally dependent upon the Scheme, each of the elements of the wider restructuring (including the bi-lateral arrangements with RCF and TFFA creditors, the Scheme and the CVA) were as a practical matter interdependent, for the reasons I have set out above at [14]. In particular, the injection of new money under the Scheme and the extension of the RCF and TFFA were premised upon the reduction in New Look's overall rent burden, achieved by the CVA.

249. Second, given that a CVA cannot affect the right of a secured creditor to enforce its security without their agreement (section 4(3) IA 1986), it is axiomatic that the source of any impairment in their rights in this respect is the agreement between them. Since that agreement is part and parcel of the CVA process, the impairment can properly be regarded as a consequence of the CVA whether or not it is a term of the proposal itself.

250. In the absence of the CVA, all of the assets of New Look would have been covered by the security in favour of the creditors under the RCF and the TFFA (who would have recovered in full) and the SSN (who would have recovered only in part, leaving nothing for the unsecured creditors other than the prescribed part).

251. Assume, first, that the release of the SSN Holders' rights against New Look had been achieved by bi-lateral agreement between New Look and each of them. The source of their right to the equity would have been the terms of their agreement to forego enforcement of their security pursuant to section 4(3).

252. In practice, it was not possible to obtain the agreement of all SSN Holders. The Scheme was necessary to bind the few SSN Holders whose express consent could not be obtained. The fact that the Scheme was the means by which the consent of *all* SSN Holders was obtained does not alter the analysis: the impairment in their rights is a consequence of the CVA notwithstanding it is not the consequence of a particular term in the Proposal.

253. The Applicants nevertheless object that the SSN Holders received *different* treatment by virtue of the CVA and Scheme combined. In my judgment, that different treatment is explained and justified by the fact that the SSN Holders were secured. It is true that the SSN Holders were not wholly secured, but that is only because the value of the assets of New Look was insufficient to satisfy the whole of the debt owed to them. In those circumstances where, but for the CVA, the entirety of New Look's assets would have been taken upon enforcement of the SSN Holders' security, there can be no serious objection to viewing the equity and subordinated debt which was granted to the SSN Holders under the Scheme as the *quid pro quo* for the release of their security.

254. That leaves the SSN Holders' unsecured debt. If, as I think it is appropriate to do, the grant of equity and subordinated debt under the Scheme is regarded as the quid pro quo for the release of the secured part of their debt, then the SSN Holders received nothing in exchange for the release of the unsecured portion of their debt. While that is undoubtedly different to the terms offered to the

Compromised Landlords, it cannot have unfairly prejudiced them: a creditor who receives *something* under a CVA (and, a fortiori, where it receives more than it would have done in the relevant comparator) is not unfairly prejudiced if another creditor or group of creditors receives *nothing* in respect of their unsecured debt.

255. Finally, the Applicants contend that they were unfairly prejudiced by reason of the fact that the statutory majority was reached by virtue of the votes of the SSN Holders who (even if not impaired) received substantially different treatment. It is true that the SSN Holders were incentivised to vote the unsecured portion of their debt in favour of the CVA for reasons that they did not share with the Compromised Landlords. They were incentivised to vote in favour because the CVA was essential to the success of the Scheme, under which they would receive their equity and subordinated debt interests. The amount of new money to be injected as a consequence of the Scheme was calculated by reference to the reduced rent burden, and the CVA was essential in order to reduce the rental liabilities of the restructured business going forward.

256. As a preliminary point, in a CVA designed to rescue a viable business it will invariably be the case that the survival of the business as a going concern will protect or increase the value of security held over that business. A partially secured creditor will in such a case always have an incentive (the improvement of its position as secured creditor) to vote in favour of a CVA, which would not be shared with ordinary unsecured creditors. That cannot in itself be an indication of unfair prejudice, however, because IR 2016 expressly permit the secured creditor to vote in respect of the unsecured portion of its debt.

257. I am satisfied that the fact that the rights of the Compromised Landlords were impaired in the various ways referred to in the previous section of this judgment as a result of the votes of the SSN Holders did not constitute unfair prejudice, for the following reasons.

258. First, there is no question of the SSN Holders receiving any benefit from any assets of New Look which were or should have been available for unsecured creditors. The benefits they received were referable to their security interest. This is not a case where (to paraphrase Warren J at [573] of *Sisu*) a creditor used its voting influence to extract a greater share of assets (i.e. the assets that are otherwise to be shared between unsecured creditors).

259. Second, it is precisely because of the terms on which the SSN Holders agreed not to enforce their security that any assets were made available (other than the *de minimis* prescribed part) for other creditors, including the Compromised Landlords, so as to permit New Look to continue trading. The benefits conferred on the Compromised Landlords by the CVA, including the option to continue letting their premises to New Look, albeit at a reduced rent, and the dividend paid out in the event that they chose to terminate their leases, were only available as a result of the SSN Holders' consent to release their security. Further, the <u>amount</u> of the dividend to unsecured creditors was increased

because the available assets did not have to be shared with the SSN Holders as a result of the release of their unsecured debt.

260. Third, as I have noted above, the treatment of the SSN Holders' unsecured claim was materially worse than the treatment of the Compromised Landlords.

261. Fourth, even taking the benefits conferred on the SSN Holders as a whole, it cannot be said that they are materially better than those conferred on the Compromised Landlords. The SSN Holders went from holding an interest at the top of the priority waterfall in an insolvency of New Look (being secured creditors with security sufficient to cover at least a substantial part of their debt) to holding an interest at the bottom of the priority waterfall (as holders of equity and subordinated debt in the Parent). At best, the value of their post-restructuring interest is speculative, as it is dependent on the performance of the restructured business in a trading environment that continues to be highly challenging.

262. Fifth, while the statutory majority would not have been achieved without the SSN Holders' vote, the court can take comfort in concluding that the allocation of assets within the CVA was reasonable, from the fact that a majority of Compromised Landlords nevertheless voted in favour of it. More than 80% by value of Compromised Landlords voted at the meeting and, of these, more than 57% voted in favour.

263. Taking into account all the circumstances, while the SSN Holders undoubtedly had incentives to vote in favour of the CVA that the Compromised Landlords did not share, I do not think that the differences were such as to mean that the Compromised Landlords were unfairly prejudiced by reason of the SSN Holders' vote securing the statutory majority at the meeting. Albeit in different ways, both the SSN Holders and the Compromised Landlords were substantially impaired by the CVA, and there was more to unite than divide them in ensuring that New Look avoided a formal insolvency process which would have resulted in a significantly worse recovery for the SSN Holders and virtually no recovery for the Compromised Landlords.

264. Finally, in response to an argument that was pressed in opening on behalf of the Applicants, the fact that a large majority of SSN Holders had committed under the LUA to vote for the Scheme (under which they would become holders of equity in the restructured group) does *not* mean that they are to be treated as equity holders when considering the fairness of the CVA. They would only become equity holders if the Scheme went ahead and, as I have pointed out above, that would not have been the case in the absence of approval of the CVA.

*The Ordinary Unsecured Creditors and Category A Landlords*

265. All of the Ordinary Unsecured Creditors and Category A Landlords were substantially unimpaired by the CVA. It is true that their claims were subject to *some* modification: any termination right based upon a CVA-related event was waived, and the Category A Landlords were required to accept payment of rent monthly rather than quarterly. In comparison to the compromise

imposed on the Compromised Landlords, however, these were *de minimis* modifications.

266. For the following reasons, however, neither the differential treatment afforded to them nor the fact that they were permitted to vote notwithstanding they were not materially impaired by the CVA constitutes unfair prejudice.

267. As to the differential treatment itself, although there was some exploration during the trial of the adequacy of the justification for paying in full at least some of them, the Applicants accepted in closing submissions that payment in full of the Ordinary Unsecured Creditors and the Category A Landlords was justified on the basis that it was necessary for reasons of business continuity. The success of the CVA, and thus the payment of anything to unsecured creditors, was dependent on payment in full of the relevant creditors.

268. The Applicants did not maintain, therefore, an objection that the differential treatment *per se* was unfairly prejudicial.

269. As to the fact that their vote counted towards the statutory majority, although the size of the vote cast by the Ordinary Unsecured Creditors and Category A Landlords was substantial, it was not enough in aggregate to have had a material effect on the outcome of the meeting. The CVA would still have been approved even if their vote had been altogether discounted. Accordingly, in this respect the arrangement was not imposed on a minority by a self-interested majority.

*Conclusion on Unfair Prejudice Challenge*

270. For the above reasons, I reject the Applicants Unfair Prejudice Challenge.

<u>I: Other jurisdiction points</u>

*(1) Is there give and take between New Look and (1) the Compromised Landlords; (2) the Ordinary Unsecured Creditors; and (3) the SSN Holders?*

271. It is common ground that *some* element of give and take is necessary for a proposal to constitute an "arrangement" (by analogy with the position in relation to schemes of arrangement): see *Re NFU Development Trust Ltd* [1973] 1 All ER 135 per Brightman J (at p.140):

> "…the word "arrangement" in this section implies some element of give and take. Confiscation is not my idea of an arrangement. A member whose rights are expropriated without any compensating advantage is not, in my view, having his rights rearranged in any legitimate sense of that expression."

272. It is also common ground that a composition can include an agreement to pay some or all of the debtor's creditors less than the full amount they are owed: see *Commissioners of Inland Revenue v Adam & Partners Ltd* [2001] 1 BCLC 222, per Mummery LJ at [52].

273. So far as the Compromised Landlords are concerned, the Applicants contend that there is no sufficient "give" by New Look, because the rights given by the CVA are *de minimis*, and New Look was in any event already obliged to give the Compromised Landlords everything which the CVA offered. For example, the right conferred on landlords to terminate the leases was not a "give" at all, because they already have termination rights.

274. I reject this contention. Wherever a CVA involves a composition by offering a dividend on debts, the company is necessarily already obliged to give that which the CVA offers. There is nevertheless sufficient give and take in an arrangement which "takes" from the creditors their contractual rights and "gives" them a return which is at least as good as that which the company could give in the relevant comparator, e.g. a liquidation of the company. Since it is common ground that the CVA offers the Compromised Landlords a better return than they would achieve in the relevant alternative, it follows that there is sufficient to satisfy the relatively low jurisdictional hurdle of give and take.

275. As for the termination right, while it is true that the Compromised Landlords already have the right to forfeit the leases on grounds of non-payment of the reserved rent, the new termination right is properly seen as part of the package of new rights granted by the CVA. Without it, the reduction in rent imposed by the CVA would preclude the Compromised Landlords from terminating the leases unless the new, reduced, rent was not paid. The new termination right thus counterbalances that by enabling Compromised Landlords to terminate notwithstanding that the reduced rent continues to be paid.

276. As to the Ordinary Unsecured Creditors, the fact that a CVA may legitimately provide for payment of some creditors in full where that is commercially justified on business continuity grounds (as the Applicants accept) means that this cannot cause a CVA to fail the requirement for sufficient give and take.

277. So far as the SSN Holders are concerned, for the reasons I have set out above at [248], the CVA has to be seen in the context of the wider restructuring, including the Scheme. In that context, there is clearly give and take as between New Look and the SSN Holders.

*(2) Do the termination rights given to New Look in relation to Category B and C Leases purport to interfere with the proprietary rights of landlords?*

278. New Look accepts that a CVA cannot interfere with the proprietary rights of landlords. In *Re Instant Cash Loans Ltd* [2019] EWHC 2795 (Ch), a provision in a scheme of arrangement that purported to surrender the company's leases was held to fall foul of this rule.

279. In this case, the Proposal provides New Look with the termination rights summarised at [25] and [28] above.

280. The Applicants point out that in *Instant Cash Loans* at [19], reference was made to passages in Megarry and Wade on the Law of Real Property and Woodfall on Landlord and Tenant which demonstrated that a tenancy might be

surrendered by operation of law if the contractual relationship between the parties ceased to have the minimum necessary requisites of a lease, for example if the contract ceased to provide for the tenant to have exclusive occupation. The Applicants contend that the release of all liability to pay rent and other sums due under a Category C Lease has the same effect: it operates in substance as a surrender binding on the parties, with the proprietary consequences that follow from that.

281. I disagree. It is not an essential requirement of a lease that the tenant is obliged to pay rent: see for example section 205(1)(xxvii) of the Law of Property Act 1925 which defines a "term of years absolute" as a term of years "…whether or not at a rent…".

282. The Proposal in this case offers the Category B and C landlords the opportunity to agree to a surrender of the lease, but does not require them to do so. Unless and until they do so, it is accepted by New Look that the lease remains on foot with, for example, the consequence that liability for rates remains that of New Look.

J: Material Irregularity

*(1) Voting Issues*

283. The Applicants' case, as originally formulated, was that there was a material irregularity in that the vote at the CVA meeting was not representative, because the statutory majority was achieved with the votes of unimpaired creditors. At the hearing, however, Mr Arden QC realistically accepted that these points were better dealt with under the heading of unfair prejudice and that if he could not succeed under that heading, there was nothing to add under the heading of material irregularity.

284. The principal remaining contention of material irregularity in respect of voting issues, therefore, is the argument that the 25% discount applied to the claim of all landlords for voting purposes was not justified. The Applicants also contend that the approach to the valuation of dilapidations claims and to break premiums was also a material irregularity.

285. Schedule 2 to the Proposal sets out a valuation methodology for calculating the claims of landlords for voting purposes.

286. The Applicants contend that this was a material irregularity, because:

(1) It fettered the chair's duty to put an estimated minimum value on the claims for voting purposes;

(2) It involved double counting to the prejudice of the landlords, because the formula in Schedule 2 already contained a deduction to reflect the landlords' re-letting ability;

(3) It created a "one-way bet", because it did not allow for the possibility that the estimate arrived at as a result of following the formula in Schedule 2 might result in an *under*-estimate of the claim;

(4) It was arbitrary and the justification offered for it (that it was a substantially reduced discount relative to the discount used in other CVAs) was insufficient; and

(5) It was particularly unfair because no similar discount was applied to the votes of SSN Holders, notwithstanding that they too were contingent claims.

287. The starting point is that (as noted above at [61]) under Rule 15.31(3) a claim of an unliquidated or unascertained amount is to be valued at £1 unless the chair decides to put upon it an estimated minimum value for voting purposes. I accept that it is the duty of the chair of the meeting to consider the available evidence and, if that evidence leads to the conclusion that he can safely attribute to the claim an estimated minimum value, he must do so: see *Doorbar* (above), at 738F-H; *Re Newlands (Seaford) Educational Trust* (above), at [27]-[28].

288. In this case, the evidence of the chair (Mr Butters) was that he reviewed Schedule 2 and agreed with the formula for calculating the claims of landlords for voting purposes. If a landlord had put forward evidence in support of a different conclusion, he said that he would have considered it. In fact, no landlord did so. Schedule 2 was not, therefore, a fetter on his discretion, but ensured transparency to all landlords in the calculation of their claims.

289. As to the remainder of the Applicants' objections, it is important to take account of two points. First, that the calculation of the likely shortfall between the net present value of a landlord's contractual right to future rent for the remainder of the lease and the net present value of the likely rent that the landlord could recover in the market over the same period in the future is inherently uncertain. Second, the chair's duty is to place an estimated *minimum* value on the claim.

290. In this case the prospects of re-letting and the likely rent that could be achieved in the market had been estimated separately for each landlord. That had been done with the benefit of advice from experts. Had that advice elicited a range of valuations and a valuation at the lower end of the range adopted, then a further discount to reflect uncertainty may well have involved double counting. The advice, however, identified a single value without identifying the possible range. In those circumstances, the single value may reasonably be taken as the mid-point within a range. The discount of 25% is therefore a proxy for identifying the lower end of the range. That is, in my judgment, consistent with the duty to place an estimated minimum value on the claim and does not involve double counting. Nor is it objectionable as being a "one-way bet": the obligation to place an estimated *minimum* value on the claim requires such a one-way adjustment.

291. While there was no particular science behind the adoption of a discount of 25%, as opposed to 10% or 20%, I do not regard that as a material irregularity. The number and range of uncertainties involved in estimating the quantum of future liabilities is such that identifying the appropriate discount is not an exact science.

292. In any event, since the discount was applied equally to landlords who voted in favour of the CVA and those who voted against, and since the aggregate claims of those voting in favour was greater than the aggregate claims of those voting against, the application of the 25% discount had no impact at all on the outcome of the meeting. For that reason, even if there had been an irregularity, it was not material. Mr Arden QC contended that materiality is to be assessed more broadly than by reference only to the impact on the result. He submitted that the application of the 25% discount may have had the effect of dissuading landlords from engaging with the CVA because they felt that the "cards were stacked against them". I do not accept this: there is no evidence that any landlord was dissuaded from voting because of the 25% discount and (as I have noted above) the turnout among landlords was high (over 80% by value).

293. Finally, I do not accept that there is any irregularity arising from the fact that the claim of the SSN Holders was not subjected to the same discount. The Applicants accept that the SSN Holders' claim, being for a certain sum contingent only on non-payment by the Issuer, was a liquidated one (see *McGuinness v Norwich and Peterborough Building Society* [2011] EWCA Civ 1286). While the claim was contingent, being dependent upon default by the Issuer, there was no doubt that the Issuer was not in a position to pay. Accordingly, there was no reason to discount the claim at all.

294. That leaves the question whether the value of the unsecured portion of the debt should have been discounted to take account of the possibility that the assets and undertaking of the company (over which the SSN Holders had security) had been undervalued. There is no fair comparison with the valuation of landlords' claims in this respect, because the requirement to place an estimated minimum value on the claim under Rule 15.31(3) is not engaged. Instead, Rule 15.31(5) merely provides that where a debt is partly secured, for voting purposes its value is "the unsecured part".

295. In any event, the value placed upon the unsecured part of the SSN Holders' debt did in fact equate to an estimated minimum value. New Look had instructed independent valuers to produce an enterprise value for its assets and undertaking. This produced a range of values, from £190 million to £250 million. For voting purposes, the upper end of this range had been taken. This meant that the valuation of the unsecured portion of the SSN Holders' claim was arrived at by taking the *lower* end of a range of possible values. In those circumstances, even if Rule 15.31(3) was engaged, in contrast to the valuation of landlords' claims, the valuation of the unsecured element of the SSN Holders' claim already had built into it a discount for uncertainty and there was no need to apply a further discount.

296. For these reasons, which reflect the submissions of Mr Smith QC, I reject the contention that there was any material irregularity by reason of the 25% discount applied to the claims of landlords for voting purposes.

297. The objection in relation to dilapidations allowances is that they were calculated on a broad-brush basis, as a fixed amount per square foot based on the type of premises. This was done on the basis of advice from CBRE following a survey of a sample of representative stores. It is true, as the Applicants contended, that this would not have precisely represented the actual dilapidations claim for each individual landlord. I accept New Look's contention, however, that this was no material irregularity given (1) the absence of any evidence that there would have been any material impact on the outcome of the meetings, had dilapidations claims been calculated separately for each lease, and (2) the cost of such an exercise would have been disproportionate, particularly in light of the first point.

298. The objection in relation to break premiums is that New Look failed to take them into account at all in valuing landlords' claims. While I reject New Look's contention that this was justified on the basis of consistency between landlords (because it cannot be right that all landlords are treated the same when some of them did, but most did not, have the contractual right to a break premium), I accept that it would have had no impact on the outcome of the meeting if the claims of landlords with the benefit of a right to a break premium had been valued with the inclusion of that right. Accordingly, this too gave rise to no material irregularity.

*(2) Non-disclosure*

299. The contents of a proposal for a CVA are prescribed by Rule 2.3(1) IR 2016. Among other things, it must state the nature and amount of the company's liabilities, how they will be met, modified, postponed or otherwise dealt with by means of the CVA. The overarching obligation of disclosure is reflected in the last item in the list set out in Rule 2.3:

> "(x) any other matter that the proposer considers appropriate to enable members and creditors to reach an informed decision on the proposal".

300. Unsurprisingly, since CVAs and schemes of arrangement share in common the fact that creditors are invited to vote upon a compromise or arrangement affecting their rights, this overarching obligation is materially the same as that which exists in the scheme jurisdiction. In *Re Indah Kiat International Finance Co BV* [2016] EWHC 246 (Ch), for example, Snowden J said (at [41]):

> "it is well-established that the scheme company has a duty to place before members or creditors sufficient information for them to make a reasonable judgment as to whether the scheme is in their commercial interest or not."

301. What amounts to sufficient information to enable creditors to reach an informed decision on the proposal is highly fact specific and will differ from case to case.

302. If a company fails to provide sufficient disclosure in a proposal for a CVA, it is only if that failure constitutes a material irregularity that the court can grant relief under section 6 IA 1986. It will only constitute a material irregularity if, "…had the truth been told, it would be likely to have made a material difference to the way in which the creditors would have considered and assessed the terms of the proposed [CVA]": see *Somji v Cadbury Schweppes plc* [2001] 1 BCLC 498, per Robert Walker LJ at [35], approving a passage in the judgment of Rimer J in *Apton New Homes Ltd v Tack* (unreported, 19 June 1998).

303. In *Trident Fashions (No2)* [2004] 2 BCLC 35, Lewison LJ, at [46], considered what was meant by "likely" in this context, saying:

> "The word "likely" is used in a variety of different ways. It does not necessarily mean that there is more than 50% chance. It seems to me, therefore, that the right test is whether there was a substantial chance that the creditors would not have approved the CVA in the form in which it was presented."

304. It is accepted that this raises an objective question. The subjective view of particular creditors may in some circumstances be relevant – if, for example, it is clear that particular creditors would not have voted differently even if the disclosure had been made: see *Golstein v Bishop* [2016] EWHC 2187 (Ch), per Warren J at [68]. That is not the case here.

305. The list of agreed issues identified seven instances in which the Proposal was alleged to contain inaccuracies and omissions. At the hearing, however, Mr Arden QC pursued the claim only in relation to the following: (1) inadequate disclosure of aspects of the wider restructuring, namely (a) the failure to disclose the identity of the parties to the LUA and the fact that they had committed to vote in favour of the CVA; (b) the failure to disclose the value of the equity interests which the SSN Holders would receive under the Scheme; and (c) the failure to disclose anything about the "exit process" for the SSN Holders, as set out at schedule 9 to the LUA; and (2) the failure to disclose the existence and terms of a management incentive plan.

306. As to the remainder of the matters identified in the list of issues, Mr Arden QC frankly accepted that the Applicants would struggle to say that they would have had a material effect on the voting outcome. I will address, therefore, only the issues identified in the preceding paragraph.

*The parties to the LUA.*

307. The existence of the LUA was revealed at paragraph 9.2 of the summary of the Proposal, which stated that "certain of the Secured Lenders" had entered into the LUA, pursuant to which they had agreed to support and implement the

"2020 Restructuring on the following terms…". The "2020 Restructuring" is defined in the Proposal as the balance of the restructuring other than the CVA.

308. It is correct to say, therefore, that the Proposal neither disclosed that SSN Holders who had signed the LUA were bound to vote in favour of the CVA nor disclosed the number of SSN Holders who had locked up. By the time the Proposal was issued, in fact, 90% of SSN Holders had acceded to the LUA.

309. The first point to note about this alleged non-disclosure is that it is not a matter that goes to the terms or nature of the arrangement, or any other related deal, between New Look and its creditors. The Applicants nevertheless contend that it was material for them to have been told these matters because they needed to know which "camp" other creditors sat in, in advance of the CVA meeting, so that they could know who they could approach in order to consult on the arrangement. I do not accept that this. There is no evidence that any creditor was interested to know which camp the SSN Holders were in, and the only prejudice a creditor would suffer by not knowing in advance was that they would have wasted their time in making contact with a SSN Holder who was already committed to voting in favour. This gets nowhere near the threshold for materiality: I do not see how it could be suggested that had this information been made known it was likely to have caused any other creditor to change the way it assessed the Proposal.

*The value of the equity interests*

310. The Proposal revealed that the SSN Holders would receive under the wider restructuring, in exchange for the discharge in full of the SSNs, a pro rata share in 20% of the equity in the Parent, and a subordinated loan to Midco. It also disclosed that those SSN Holders that participated in the New Money Facility would be entitled to share pro rata in the other 80% of the equity in the Parent.

311. The Applicants contend, however, that the Proposal should also have provided a valuation, or at least an estimated valuation, of those equity interests. They point to the fact that in a report prepared by KPMG to establish that the consideration to be received by the SSN Holders under the Scheme was fair and reasonable, the estimated value of the equity in New Look (assuming that the Scheme was approved) ranged from nil to £229.1 million.

312. I accept that the likely value of the equity interest to be received by the SSN Holders as part of the overall restructuring was relevant information for all creditors in assessing the Proposal. A reasonable creditor would be interested in knowing how the assets of the company were to be allocated between different groups of creditors. Since (as I have concluded) it is necessary to view the CVA in the context of the wider restructuring, it is no answer to this that the SSN Holders received their equity interests via the Scheme and not the CVA.

313. I do not, however, think that the failure to disclose the information in the circumstances of this case was a material irregularity, for the following reasons.

314. First, the non-disclosure needs to be seen in the context of what was disclosed about the SSN Holders. The Proposal identified the SSN Holders as holding security over the assets of New Look. It disclosed (in the estimated outcome statement) that on the assumption that the assets of New Look realised £250 million, there would be a shortfall to the SSN Holders of £272 million – which implied that they might expect to recover in excess of £160m from their security, leaving nothing other than the prescribed part for unsecured creditors. The CVA creditors were informed, therefore, that as a consequence of the restructuring the SSN Holders' position would change from being entitled, under their security, to all remaining assets of New Look after satisfaction of the RCF and TFFA liabilities, to holding an indirect minority stake in the equity of the company.

315. Second, the value of that minority equity interest was highly uncertain. As I have pointed out above, in KPMG's fairness opinion in connection with the Scheme, the value of the entirety of the equity was estimated to be within a range from nil to £229.1 million. The range of valuation of the minority interest to be acquired by the SSN Holders would have been between nil and at most 20% of £229.1 million.

316. Although the CVA did not identify an estimated value for the post-restructuring equity interest, the estimated outcome statement included, in addition to the range of values for the assets and undertaking, the amount of post-restructuring debt (which, after deduction of available cash, totalled some £152.9 million). This implied the possibility that there would be at least some equity value. On the figures presented, it implied a possible value between approximately £37 million and £97 million, although this was as speculative as the estimate in the KPMG fairness opinion, as it was dependent on the enterprise value of the assets and business.

317. Notwithstanding that the CVA indicated that the possibility of there being some value in the equity post-restructuring, and that SSN Holders would receive a share of that equity as a result of the Scheme, there is no evidence that any creditor made any enquiry of the position. I do not accept, as suggested by the Applicants, that it is an answer to this to say that creditors cannot enquire about matters of which they are unaware. They were told enough to enable them to make further enquiry if they thought it relevant to their decision.

318. Third, the equity interest to be acquired by the SSN Holders was the *quid pro quo* of the release of their security right. Its value was of less relevance to other creditors than if, for example, it was part of the allocation of the company's assets available to all creditors.

319. Fourth, whereas any benefit that a CVA provided to existing shareholders of a company would be a matter of considerable interest to creditors who were being asked to compromise their claims, that is not the case here. As I have already noted, the existing shareholders were wholly wiped out by the restructuring, and the SSN Holders were receiving new equity in exchange for the discharge of secured debt.

320. In all the circumstances, I do not think that, had creditors been informed of the range of estimated equity values in the KPMG fairness report, it would have been likely to make any difference to their assessment of, or vote in respect of, the CVA.

*Exit process for equity holders*

321. Schedule 9 to the LUA sets out the terms on which the new equity was issued to SSN Holders. It includes a timetable for a planned exit (by sale or other disposal) to be completed within four years.

322. The Applicants contend that this was material information which should have been disclosed to CVA creditors, because it demonstrates that the reduction of rent payable under leases with Compromised Landlords for longer than the three-year Rent Concession Period was part of an overall strategy to maximise the value of the Group so as to enable equity holders to achieve an exit.

323. I do not accept that the fact that the SSN Holders negotiated an exit process provides any evidence that the motivation of the restructuring, or that part of it which extended the reduction in rent beyond the Rent Concession Period, was the maximisation of equity value. There is no reason to doubt the genuineness of the view expressed in the Proposal that the purpose of the CVA was to rescue New Look from the financial distress in which it found itself.

324. As Mr Smith QC submitted, it is not surprising that SSN Holders, who initially invested by way of debt, were keen to negotiate an exit route when required to take equity as part of the Scheme, rather than being locked in indefinitely as minority shareholders.

*The management incentive plan*

325. Under the management incentive plan, the Group's management was entitled to 5% of the ordinary share capital of the post-restructuring holding company, together with D Ordinary Shares giving them 2% of the equity value on any exit for a consideration above £300 million. This was disclosed to Scheme creditors, but not to CVA creditors.

326. The Applicants contend that its omission from the Proposal was material because it gave the management a significant financial interest in the successful implementation of the CVA as well as the Scheme. As it was relevant to disclose to Scheme creditors, it was also relevant to disclose to CVA creditors.

327. New Look points to the fact that its disclosure to Scheme Creditors was because there is a specific requirement to disclose any material interests of the directors (section 897(2) CA 2006), but there is no similar requirement in IR 2016 relating to CVAs.

328. It seems to me that any benefit in a proposed scheme or CVA which directors of a company promoting have in it is a matter which creditors are entitled to

be told about, since it will always be relevant to know whether those promoting the scheme or CVA have a particular incentive to do so.

329. Nevertheless, I do not think that the failure to disclose the incentive plan to CVA creditors amounted to a material irregularity. There already existed an incentive plan of a similar nature for the benefit of the same individuals, and I infer that the replacement plan was necessitated by the restructuring of the equity interests in the Group as a result of the Scheme. Even if it provided enhanced benefits for the directors, I do not see how knowledge of that would have caused any creditor to change its vote on the CVA. It did not involve CVA creditors giving up any entitlement to any assets of New Look, as the subordinated equity provided under the incentive plan was never an asset of New Look for distribution to its creditors. Insofar as it provided an incentive to directors, it was one that was exactly aligned with the interests of creditors, in that it would have incentivised them to work to make a success of the restructured business.

K: Conclusion

330. For the above reasons, I reject each of the Jurisdictional Challenge, the Material Irregularity Challenge and the Unfair Prejudice Challenge.