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Re Regis UK Limited [2021] EWHC 1294 (Ch) – Landlords fail in their attempt to force Nominees to return their fees and in their bid to establish a meaningful precedent in their ongoing fight against CVAs

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Matthew Weaver

Call: 2002

Barrister

Matthew has an impressive commercial practice with a particular specialism in insolvency and company law. He is ranked as a leading junior for restructuring/insolvency by Chambers UK Bar 2021 and for company and insolvency by The Legal 500 UK Bar. His practice covers all areas of contentious and non-contentious corporate and personal insolvency and he is regularly instructed to advise and appear on behalf of liquidators, administrators, administrative receivers, LPA receivers, supervisors and trustees in bankruptcy.

In a judgment handed down on Monday 17th May 2021 in ***Re Regis UK Limited*** [2021] EWHC 1294 (Ch), Zacaroli J revoked an already long-since terminated CVA, but refused to order the former Nominees and Supervisors of the CVA to repay their fees and dismissed all but one of the applicant landlords' claims of unfair prejudice and/or material irregularity; thereby thwarting their primary motive to create a meaningful precedent to inhibit the future use of retail CVAs. Matthew Weaver, who acted for the Respondent Nominees, provides a brief overview of the judgment.

The Background

Regis UK Limited operated its salon and beauty business under the Regis and Supercuts brands. It entered into a CVA in October 2018, the terms of which compromised the claims of certain landlords of the premises from which it operated as well as other non-landlord creditor claims.

In November 2018, 19 landlords issued an application to revoke the CVA based on various allegations of unfair prejudice and material irregularity pursuant to section 6 of the Insolvency Act 1986 ("IA 1986"). Somewhat unusually, the application also included allegations against the former Nominees and Supervisors, and sought relief against them, namely an order that they repay the fees received by them pursuant to section 6(6) of IA 1986.

The Company entered administration in October 2019, terminating the CVA. Shortly after, the Nominees attempted to strike out the application in circumstances where they asserted that it no longer served any useful purpose and where relief against the Nominees was unlikely to be ordered. In December 2019, the landlords were refused permission to amend the application to increase the grounds of criticism of the CVA. The landlords also sought to amend the application again during the trial but this application was also refused.

The trial of the challenge lasted 6.5 days and included evidence from four expert witnesses.

The criticisms of the CVA advanced by the landlords can be summarised as follows:

- a failure to adequately disclose to creditors details of certain transactions entered into by the Company in 2017 and 2018 which might have been subject to possible challenge by a liquidator or administrator;
- the alleged inaccuracy of the Statement of Affairs and/or Estimated Outcome Statement in (i) wrongly treating debts to two creditors and a debenture granted in favour of one of the creditors as valid; (ii) wrongly identifying a shut-down administration as the realistic alternative to a CVA; and (iii) failing to include any value for recoveries in respect of possible Antecedent Transactions;
- the admission for voting of two creditors of the Company whose debts were challenged as being unlawful distributions, unlawful returns of capital or arising from transactions which amounted to a breach of duty on the part of the Company's directors;
- unfair modifications to leases;
- the inappropriate application of a 75% discount to the landlords claims for voting purposes; and
- incorrect treatment of two creditors as being critical creditors.

As against the Nominees, it was alleged that each and every complaint of unfair prejudice and material irregularity gave rise to a breach of duty on their part. At trial, the landlords conceded that their case against the Nominees in fact focussed on the failures in respect of disclosure and the treatment of critical creditors. The landlords sought an order that the Nominees be compelled to repay their fees by reason of their alleged breach of duty.

The Decision

The Court:

- declined to order relief against the Nominees;
- revoked the CVA on the basis that the treatment of one creditor as critical was unfairly prejudicial; and
- dismissed all other grounds of unfair prejudice or material irregularity advanced by the landlords

At trial, the application was contested by reference to 21 issues (excluding issues relevant only to relief). The Court found against the landlords on the vast majority of these. In finding one example of unfair prejudice within the CVA, the Court applied long-standing and uncontroversial case law in respect of the equal treatment of creditors and dismissed all other grounds of challenge; resulting in a decision which is not the wide-reaching authority limiting the application of retail CVAs which the landlords had hoped it would be.

In reaching his decision, Zacaroli J accepted the Nominees' long-standing assertions that the application lacked any practical utility. Further, he observed that the landlords' desire to obtain a ruling from the court on the issues raised in the context of the wider retail CVA market had fallen away in light of the challenge in New Look Retailers Limited. As a result, the Judge agreed with the Nominees that determining the merits of claims advanced by the landlords against the Company's directors and third parties (in respect of the validity of the debts owed by the Company to two creditors and the validity of a debenture) was inappropriate in circumstances where those parties were playing no role in the proceedings.

<u>Disclosure</u>

Zacaroli J dismissed the landlords' criticisms of the disclosure within the CVA proposal of possible antecedent transactions in 2017 and 2018 involving the Company.

The 2017 claims were not sustainable given the Company's solvency at that time; any further disclosure would have had to include disclosure that the claims lacked obvious merit. The purpose of requiring disclosure of such transactions was to inform creditors of claims which would be lost by virtue of a CVA. Here, the 2017 transactions did not give rise to sustainable claims. Further, whilst the specific sections of IA 1986 were not cross-referenced to the individual transactions, this was not required where the substance rather than the form of the disclosure was the key issue.

As for the 2018 transactions, the Judge determined that any failure to identify challenges under IA 1986 to these transactions did not amount to a material irregularity where the facts of the case presented a viable defence to such claims and therefore rendered the possible claims of doubtful merit, a matter which would have had to have been disclosed to the creditors. The Judge was also content that the CVA proposal provided sufficient disclosure as to the Company's trading history and the various transactions to allow the creditors to form a view as to whether to support the proposal.

Statement of Affairs/Estimated Outcome Statement

The Judge dismissed the landlords' criticism of the Statement of Affairs and Estimated Outcome Statement.

The nature of the allegations against the Company's directors and the third parties and the lack of practical utility of the challenge to the CVA made it inappropriate to determine the validity of the debts owed to two creditors. Zacaroli J agreed with the Nominees that a Statement of Affairs ought not to refer to antecedent transaction claims given that they are not assets of a company pre-CVA and concluded that in circumstances where neither insolvency expert witness considered that values could properly be attributed to such claims, the reference to the same in the Estimated Outcome Statement was not materially irregular.

The Judge preferred the conclusions of the Nominees' expert, who supported the view taken by the Nominees at the time, that a shut-down administration was the most realistic alternative to a CVA. In doing so, he rejected the landlords' suggestions (i) that the subsequent administration (which, in any event, will almost certainly result in no distribution to unsecured creditors) was relevant; (ii) that the directors could or would have traded the business after rejection of the CVA; (iii) that a trading administration was possible (given the need for significant funding which was unlikely be obtained); and (iv) that the court ought to consider the realistic alternative to a CVA as if a marketing exercise had been carried out in parallel by the Company in the build up to the creditors' vote when, in fact, no such exercise was undertaken.

Voting

The Judge declined to make findings on the challenges advanced by the landlords to the validity of the debts due to the two creditors. However, he did find, on balance, that the landlords' assertions that one of the debts was a new debt created at the time of the CVA was incorrect in light of the evidence before the Court.

Modifications of Leases

Zacaroli J dismissed the landlords' criticism of the modifications to the leases.

The Judge relied on his recent decision in ***Re New Look Retailers Ltd*** [2021] EWHC 1209 (Ch) and confirmed that in circumstances where landlords are provided with an option to terminate their leases or accept the modifications under the CVA proposal and this option provided a more favourable outcome than the realistic alternative, there was no unfair prejudice. The failure by the landlords to adduce expert evidence of market rent prevented a finding that the modifications took the rent below market rent. The Judge also rejected the landlords' assertion that the 90-day termination window was insufficient so as to undermine the fairness of the termination option.

In addition, Zacaroli J rejected the landlords' claim that a modification letter issued by the Company altering some of the modifications to the leases (to address concerns raised by landlords) was ineffective. The Judge concluded that the letter was a valid modification of the CVA in circumstances where, as per the terms of the CVA, it did not materially alter the effect or economic substance of the CVA.

75% Voting Discount

The Judge dismissed the landlords' criticism of the 75% voting discount as being a material irregularity.

Fundamentally, as was explained in ***Re New Look Retailers Ltd***, a voting discount that applied to all landlord creditors, even if irregular, had no impact on the outcome of the creditors meeting, as it applied to all voting landlords equally, and, as such, was not material.

The Judge considered that a blanket discount across all categories of landlord was not justified in this CVA and a 75% discount could not be justified by reference to similar treatment in previous retail CVAs. However, given the lack of materiality, the landlords' complaints could not give rise to a material irregularity.

Treatment of critical creditors

Zacaroli J dismissed the landlords' complaints that the single largest connected creditor had been wrongly treated as critical. The Company's basis for doing so was objectively justifiable and, as such, no unfair prejudice resulted.

However, the Judge considered that there was insufficient evidence to objectively justify treatment of a second creditor as critical, rendering the treatment of that creditor unfairly prejudicial to the remaining unsecured creditors. As a result, the Judge revoked the CVA. In addition, he considered that in recommending in the report that the

CVA proposal be put to a meeting of creditors, the Nominee's conduct, "in this one limited respect" fell below the standard required of a nominee, given the unfairly prejudicial treatment of the second creditor as a critical creditor.

Relief

Having found one incident of unfair prejudice, whilst Zacaroli J identified the lack of practical utility of the CVA challenge, he accepted that an order revoking the CVA was relevant to the costs of the challenge as between the landlords and the Company and as a possible gateway to an order under s6(6) of IA 1986 that the Nominees repay all fees.

The Judge was prepared to revoke the CVA but declined to order any relief against the Nominees. Whilst not ruling out the possibility that the Court might have jurisdiction to make such an order if the circumstances were appropriate, it was plainly not appropriate to make such an order here in the absence of bad faith or fraud (which had not been alleged) and in circumstances where the services provided by the Nominees could not be (and were not) described as being without value.

The application for relief against the Nominees therefore failed.

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