Neutral Citation Number: [2018] EWHC 402 (Ch)

Case No: CR-2016-002220

IN THE HIGH COURT OF JUSTICE
IN THE BUSINESS AND PROPERTY COURTS
OF ENGLAND AND WALES
INSOLVENCY AND COMPANIES LIST
CHANCERY DIVISION

Royal Courts of Justice
Strand, London, WC2A 2LL

Date: Tuesday 6 March 2018

Before :

MR CHRISTOPHER PYMONT QC

- -

IN THE MATTER OF SHB REALISATIONS LIMITED (FORMERLY BHS LIMITED (IN LIQUIDATION))

AND IN THE MATTER OF THE INSOLVENCY ACT 1986

Between :

ANTHONY JOHN WRIGHT AND GEOFFREY PAUL ROWLEY as joint liquidators of SHB Realisations Limited (formerly BHS Limited) (in liquidation)	**Applicants**
- and -	
THE PRUDENTIAL ASSURANCE COMPANY LIMITED	**Respondent**

- -
- -

Stephen Robins (instructed by **Jones Day**) for the **Applicants**
Blair Leahy (instructed by **Hogan Lovells International LLP**) for the **Respondent**

- -

APPROVED JUDGMENT

Mr Christopher Pymont QC :

1. This is an application by the liquidators of SHB Realisations Limited ("the Company") for directions under section 112 of the Insolvency Act 1986. The Respondent ("Prudential") is the Company's landlord under two leases demising to the Company premises in, respectively, Chester and Southend. The liquidators are concerned to establish whether certain sums claimed by Prudential are (i) payable at all (ii) provable in the liquidation and (iii) payable as an administration expense (an administration having preceded the liquidation).

2. The issues arise in the following circumstances. The Company (under its former name of BHS Limited) was the principal trading company in the BHS group, the well-known retailer of clothing, household goods, furniture and lighting. Following several years of increasing losses, the Company proposed a company voluntary arrangement ("CVA") on 4 March 2016. The CVA was approved by separate meetings of the Company's creditors and members on 23 March 2016. The CVA left the management of the affairs, business, Assets (as defined) and properties of the Company in the hands of its Directors (clause 4.1), but it quickly became apparent that the Company had insufficient funds to continue to trade in the short to medium term and the Company went into administration on 25 April 2016. The CVA did not automatically terminate on the Company's administration and so, for a period, the CVA and the administration ran in parallel. Concurrent administrators (Mr Anthony Wright and Mr Geoffrey Rowley) were appointed on 22 July 2016 so as "*to commence additional investigatory work into the Company's affairs with the [original] Administrators remaining in office to conclude trading activities and assist realisations ahead of a creditors' voluntary liquidation*" (I quote from the filed Notice of Result of Meeting of Creditors dated 23 June 2016). Ultimately, however, the

Company was put into creditors' voluntary liquidation on 18 November 2016 and Mr Wright and Mr Rowley were appointed its joint liquidators.

3. The Company's liquidation led indirectly to the termination of the CVA. Clause 25.8 of the CVA entitled any landlord creditor to send a notice demanding payment within 14 days of sums due within the categories set out; if payment were not made, a further notice could bring about the termination of the CVA on receipt by the Company. One of the Company's landlords (not Prudential) served the relevant notices on the Company and the CVA accordingly terminated with effect from 16 December 2016.

4. As I will explain in greater detail below, the CVA provided for some of the landlords of the Company to receive less than the full amount of the rent falling due under the leases granted to the Company. While the CVA was in force, these landlords were paid the reduced rents and other sums due under the leases to the extent provided for in the CVA. However, on the termination of the CVA, clause 25.9 of the CVA took effect, which provided as follows:

> "*Upon a termination under this Clause 25 …, the compromises and releases effected under the terms of the CVA shall be deemed never to have happened, such that all Landlords and other compromised CVA Creditors shall have the claims against [the Company] that they would have had if the CVA Proposal had never been approved (less any payments made during the course of the CVA).*"

On the basis of this clause Prudential's submission is that (a) it is owed the full amount of the outstanding rent payable under the relevant leases (giving credit for the amounts actually received during the currency of the CVA) and (b) part of the outstanding balance is payable as an administration expense for the period during which the original administrators continued to trade from the premises the subject of

those leases in furtherance of the aims of the administration (the period being from 25 April 2016 to 3 August 2016 for each of the Chester and Southend premises).

5. The liquidators say that this raises the following issues, which they seek to have resolved on this application:

   i) The penalty issue. The liquidators ask the Court to determine whether the provisions of clause 25.8 and clause 25.9, which (it is said) require the Company to pay additional sums upon breach of the CVA, render Prudential's claims unenforceable as a penalty or penalties.

   ii) The pari passu issue. The liquidators ask the Court to determine whether the effect of these provisions, which are said to have substantially increased the Company's liabilities to Prudential after the commencement of the liquidation, is that Prudential's claims contravene the pari passu principle (that is, the principle which precludes a company from agreeing to distribute its property among its creditors other than pari passu on insolvency).

   iii) The administration expense issue. The liquidators ask the Court to determine whether Prudential can claim the additional sums as an administration expense when (if they are recoverable at all) they only fell due after the period during which the original administrators were trading from the relevant premises and were payable by virtue of clause 25.9 rather than the relevant leases.

6. To address these issues, I turn first to the CVA to set out what seem to me to be the relevant provisions in their proper context.

The CVA

7. The reasons for and objectives of the CVA were explained in a summary provided to creditors in advance of the meetings at which the CVA was approved. One commercial problem explained in the summary had been the extent of the Company's property costs. Many of the Company's stores were too big in the prevailing retail landscape and many of them were subject to upward-only rent reviews negotiated decades earlier, with the result that a significant proportion of the Company's properties were over-rented. The Company had been unable to sell or surrender a sufficient number of properties, or to re-negotiate the rent payable, to reduce its cost base. Without a reduction in its lease obligations of the order proposed by the CVA, the Company did not have the capability to meet its debts and working capital requirements beyond the next rent quarter date. The proposal was therefore to impose rent reductions on certain landlords through a CVA.

8. The proposed terms of the CVA would achieve this by dividing the Company's premises into three categories and imposing restrictions on the respective landlords' rights.

   i) The obligations arising on Category 1 premises were subject to the least interference, those being the premises considered currently viable.

   ii) The Category 2 premises were those considered viable if a reduction in rent could be achieved. The landlords of these premises were to receive 75% (Category 2A) or 50% (Category 2B) of the rent payable, and 100% of the contractual amounts payable in respect of insurance and service charge, for three years from the next date on which rent was payable .

iii) The Category 3 premises were those considered uneconomic. The landlords of those premises were to receive only 20% of the rent payable, a further 5% of the rent payable in lieu of dilapidations and 100% of the contractual amounts payable in respect of insurance and service charge for 10 months from the next date on which rent was payable, after which the Company would have no liability to the relevant landlords unless it elected to remain in occupation.

9. Prudential was a Category 2A Landlord, in respect of both of its leases to the Company.

10. The CVA terms were expressed (so far as relevant) as follows:

> "*9.1 During the Rent Concession Period, [the Company] shall not be obliged to pay Contractual Rent or Turnover Rent to the Category 2 Landlords in the amounts provided for in the Category 2 Leases. Instead, [the Company] shall be obliged to pay Amended Contractual Rent in accordance with Clauses 9.2, 9.3 and 9.4 below, and Clause 12 (Rent Concession Agreement).*
>
> *9.2 The amount payable to each Category 2A Landlord under each category 2A Lease shall be 75% (seventy-five per cent) of the Contractual Rent and of the Turnover Rent (if any) in the period from the Next Payment Date until expiry of the Rent Concession Period, plus all contractual amounts payable in respect of insurance and service charge.*"

(Clause 9.3 provided for Category 2B Landlords to be paid 50% of the rent; and clause 9.4 dealt with the dates upon which payments were to be made).

11. The Rent Concession Period was defined for each Category 2 Lease as

> "*the period commencing on the Next Payment Date and ending on the earlier of:*

> *(i) the date that the relevant Lease expires or is otherwise determined; or*
>
> *(ii) the Category 2 End Date*".

The Category 2 End Date was 24 March 2019 or, if later, such other date as would fall three years after the Next Payment Date for the relevant Lease. The Next Payment Date was 25 March 2016 or such later date as Contractual Rent was first payable after the creditors' meeting under the relevant Lease.

12. When the Rent Concession Period was over, the rent payable to Category 2 Landlords was to be restricted as follows:

> "*10.1 From the Category 2 End Date in respect of each category 2 Lease, until expiry or determination of the relevant Category 2 Lease, the rent payable and reserved in respect of such Category 2 Lease shall be the greater of:*
>
> *(a) the rent payable pursuant to Clause 9.2 above with respect to a Category 2A Lease … and*
>
> *(b) the Market Rent as determined from time to time in accordance with Clauses 10.2 to 10.6 below."*

13. Clause 9.5 provided for these reduced rents to be in settlement of the Company's liability to a Category 2 Landlord, as follows:

> *"[The Company]'s obligation to make the payments referred to in this Clause 9 and in Clause 10 … is in full and final satisfaction of any Liability to a Category 2 Landlord under or arising out of or in relation to the relevant Category 2 Lease, and whether in respect of the Contractual Rent, Turnover Rent, service charge, insurance, dilapidations, termination amount or otherwise*."

"*Liability*" was defined widely.

14. The CVA provided for the possibility of the Company assigning any relevant Lease in clause 12. Clause 12.1 specified some arrangements for invoicing and interest and the terms continued:

> "*12.2 The payment arrangements set out at Clause 9 … and this Clause 12 shall, in respect of future payments due under the relevant Lease, cease immediately upon the date on which [the Company] assigns the relevant Lease (any such date being a "Lease Assignment Date").*
>
> *12.3 With effect from the Lease Assignment Date, any future amounts due under a Lease in respect of which the Lease Assignment Date has occurred shall, from that date, be payable as specified in the relevant Lease as if Clause 9 … and this Clause 12 had never taken effect.*
>
> *12.4 It is agreed between [the Company] and each Landlord that the arrangements and agreements set out in this Clause 12*
>
> *(a) …*
>
> *(b) will bind both [the Company] and the Landlord's successors in title and assigns of the Leases; and*
>
> *(c) shall not, from the Lease Assignment Date, be deemed to have varied the terms of the relevant Leases, but shall be deemed to have waived them only insofar as is necessary to give effect to the terms of this Clause 12.*"

15. Clause 17 contained a full and final settlement clause in the following terms:

> "*17.1 Subject to [various clauses, including clause 25]*
>
> *(a) upon the Effective Date the provisions of this Part V [i.e. the terms of the CVA] shall constitute a compromise of all CVA Claims, and [the Company]'s obligation to make payments pursuant to the CVA (including pursuant to the Leases as modified or varied) to CVA Creditors shall be in full and final settlement of all CVA Claims; and*

> (b) *accordingly, upon the CVA coming into effect … each CVA Creditor accepts the compromise of CVA Claims as set out in this Part V of the CVA Proposal as full and final satisfaction of each and every CVA Liability*."

CVA Claims, CVA Liability and CVA Creditors were defined to include any claim or Liability (itself, as I have said, widely defined) to any person.

16. I have already set out the material terms of clause 25 (i.e. clause 25.9) at paragraph 4 above.

17. One other terms should be mentioned, namely clause 3.3. Clause 3 imposes a stay or moratorium on legal process and other remedies available to Landlords and others and clause 3.3 excepts from this provision the enforcement of rights under the terms of the CVA

> *"(including, for the avoidance of doubt, under the terms of the Leases as modified or varied by the CVA or which revert to their normal terms in accordance with the CVA)"* (emphasis added).

As will appear, some significance is attached by the liquidators to the language of the phrase which I have highlighted.

18. I therefore turn to consider the issues raised before me as to the effect of those provisions in the circumstances I have described.

(i) The penalty issue

19. The liquidators' application seeks the Court's determination as to whether or not the termination provisions of the CVA fall foul of the law on penalties. The submission is that the CVA operates as a contract; that the contract varies the terms of the Leases

so that only the Amended Contractual Rent is payable during the Rent Concession Period; that the termination provisions come into operation on breach of the terms of the CVA; that they create a liability which did not otherwise exist for the Company to pay additional sums on breach; and that this engages the law against penalties, rendering that obligation unenforceable.

20. For the proposition that the CVA operates as a contract, the liquidators cite a number of authorities starting with the decision in Johnson v Davies [1999] Ch 117. This was a case involving an individual voluntary arrangement ("IVA") but the reasoning of the Court of Appeal applies equally to a CVA (see, for example, Commissioners of Inland Revenue v Adam & Partners Ltd [2000] BCC 513 at para 18, per Nicholas Warren QC, then sitting as a deputy judge of the High Court). The statutory provision under consideration in Johnson v Davies was section 260(2) of the Insolvency Act 1986 which provided that

> "*The approval arrangement (a) takes effect as if made by the debtor at the meeting and (b) binds every person who in accordance with the rules had notice of, and was entitled to vote at, the meeting (whether or not he was present or represented at it) as if he were a party to the arrangement*."

This provision is in materially the same terms as section 5 of the Insolvency Act 1986 which applies to CVAs. Chadwick LJ observed that:

> "*The statutory hypothesis is that the person who had notice of and was entitled to vote at the meeting is party to an arrangement to which he has given his consent …" (pp.129H-130A).*
>
> *"Unlike the earlier legislation, section 260(2) of the Act of 1986 does not purport, directly, to impose the arrangement on a dissenting creditor whether or not he has agreed to its terms; rather, he is bound by the arrangements as the result of a statutory hypothesis. The statutory hypothesis requires him to be treated as if he had consented to the arrangement*."

Accordingly, questions as to the effect of the arrangement on sureties

> *"... were to be answered by treating the arrangement as consensual; that is to say, by construing its terms as if they were the terms of a consensual agreement between the debtor and all those creditors who, under the statutory hypothesis, must be treated as being consenting parties*."

Thus the arrangement has contractual effect (see further Lloyds Bank PLC v Elliott [2003] BPIR 632 at para 51 per Chadwick LJ). In Tanner v Everitt [2004] EWHC 1130, Mann J summarised the position thus:

> "*The arrangement is therefore contractually based, with the statute providing the consent or deemed consent of the otherwise dissenting parties*" (para 71).

21. As to the alleged variation, the liquidators say that the effect of the CVA was to replace the Company's obligation to pay the Contractual Rent reserved by the relevant Leases with the Amended Contractual Rent imposed by clause 9, with the consequence that the Landlords (here, the Prudential) thereafter had no claim for the difference between the Contractual Rent and the Amended Contractual Rent during the Rent Concession Period. Such indeed was the conclusion of Edwards-Stuart J in relation to a similar term in a similar CVA in Oakrock Ltd v Travelodge Hotels Ltd [2005] EWHC 30. The fact that the parties used the term "*Amended Contractual Rent*" shows (it is said) that they intended to vary the rental obligations in the Leases (as Lord Hoffmann said in Chartbrook Ltd v Persimmon Homes Ltd [2009] 1 AC 1101: "*words used as labels are seldom arbitrary*"); a variation is also contemplated by the references in clauses 3.3 and clause 17.1(a) to the leases being "*modified or varied*" by the CVA and, separately, by the terms of clause 12.4(c).

22. The liquidators say that it follows that, upon termination of the CVA, clause 25.9 imposes new obligations on the Company, creating new obligations where the original

obligations had been fully compromised. The fact that clause 25.9 proceeds by deeming the compromises never to have happened shows that they had in fact happened.

23. What is more, it is said, those new obligations arise (and have arisen on the facts here) upon breach of the CVA (i.e. upon failure to pay rent). It is irrelevant that the termination clause may also allow for termination in circumstances other than breach (see Cooden Engineering Co Ltd v Stanford [1953] 1 QB 86 at p 96 per Somerville LJ and at p. 110 per Hodson LJ; the decision in Cooden was approved by the House of Lords in Bridge v Campbell Discount Co Ltd [1962] AC 600). It is also irrelevant that the obligation is triggered by notices which have been served by a different Landlord from the Landlord seeking payment, as this is a multi-lateral contract which is binding on all parties. The law as to penalties is thus fully engaged.

24. The liquidators cite in support of their submissions the decision of the Supreme Court in Cavendish Square Holdings BV v Makdessi [2016] AC 1172 in which the law on penalties has been reviewed and authoritatively re-stated. The Supreme Court affirmed that a contractual term can be unenforceable as a penalty if it operates on a breach of contract and satisfies the relevant test, which was explained as follows:

> "*The true test is whether the impugned provision is a secondary obligation which imposes a detriment on the contract-breaker out of all proportion to any legitimate interest of the innocent party in the enforcement of the primary obligation*" (para 32, per Lord Neuberger of Abbotsbury PSC and Lord Sumption JSC, with whom Lord Carnwath JSC and Lord Clarke of Story-cum-Ebony JSC agreed) and
>
> "*What is necessary in each case is to consider, first, whether any (and, if so, what) legitimate business interest is served and protected by the clause, and, second, whether, assuming such an interest to exist, the provision made for the interest is nevertheless in the circumstances extravagant, exorbitant or*

> *unconscionable*" (para 152 per Lord Mance JSC, with whom Lord Clarke and Lord Toulson JSC agreed) and
>
> *"… the correct test for a penalty is whether the sum or remedy stipulated as a consequence of a breach of contract is exorbitant or unconscionable when regard is had to the innocent party's interest in the performance of the contract*" (para 255, per Lord Hodge JSC, with whom Lord Clarke and Lord Toulson agreed)."

25. Applying these principles, the liquidators say that the decision in Vivienne Westwood Ltd v Conduit Street Development Ltd [2017] L&TR 23 is instructive (a decision of Mr Timothy Fancourt QC, then sitting as a deputy judge of the High Court). There, premises were demised at an initial annual rent of £110,000 (subject to review) but, by a side letter, the landlord agreed to accept lesser sums if the tenant did not breach the terms agreed by the side letter or the lease. If the tenant did breach those terms, the landlord could terminate the agreement in the side letter and impose the full rent reserved by the lease. The side letter was expressed to be personal to the tenant and not to be a variation of the lease. Mr Fancourt QC nevertheless held that the lease and the side-letter had to be read together, with the consequence that the primary obligation on the tenant was to pay the lower rent provided for in the side-letter. On that basis, the obligation to pay a higher rent in the event of a breach of the terms of the side letter and lease was capable of being (and, on the facts, was) a penalty clause and thus unenforceable, applying the principles set out in Cavendish Square. In reaching that conclusion, Mr Fancourt QC was particularly persuaded by the circumstance that the clause operated to increase the rent by the same amount, however significant or insignificant the breach (see para 63).

26. The liquidators also rely upon the (obiter) comment of Lord Westbury in Thompson v Hudson (1869) LR 4 HL 1 at p 28:

> "*It is plain enough that if part of a debt has been duly and unconditionally remitted, the part so unconditionally remitted ceases. If it be revived it becomes a subject in respect of which there is no longer any contract in existence, and which therefore may properly be regarded as a penalty*."

So, here, the liquidators say that the imposition of the Amended Contractual Rent (clause 9.1) in full and final satisfaction settlement of the obligation to pay the Contractual Rent (clause 9.5) means that any obligation by virtue of clause 25.9 is a new obligation and thus capable of being a penalty.

27. Attractively though this analysis of the CVA was presented, I do not accept it. In my judgment, the analysis is flawed for (at least) the following three reasons.

28. First, the fact that the CVA has contractual effect does not mean that it has every attribute of a contract or that every principle of the law of contract applies to it. The Insolvency Act creates a "*statutory hypothesis*" (as Chadwick LJ described it in Johnson v Davies, above) or deeming provision (as Mann J characterised it in Tanner v Everitt, above) which enables, and compels, the court to apply a contractual analysis to issues such as the true construction of the CVA (as in, for example, Re Brelec Installations Ltd [2001] BCC 421 at p 423E to F per Blackburne J and Sea Voyager Maritime Inc v Bielecki [1999] BCC 924 at p 939B per Richard McCombe QC, then sitting as a deputy judge of the High Court) or the effect on co-debtors and sureties (as decided in Johnson v Davies itself). In so providing, however, the Act makes it unnecessary and inappropriate to consider any of the usual principles of contract formation (offer, acceptance, consideration, intention to create legal relations), all of which are irrelevant. Instead, the CVA takes effect "*as if made by the company at the time the creditors decided to approve the voluntary arrangement*" (section 5(2)(a) of the Act) and binds every person entitled to vote (or who would have been entitled had

the relevant notice been given) "*as if he were a party to the voluntary arrangement*" (section 5(2)(b)). The statutory hypothesis thus works to bind all those affected by the arrangement, including the company itself.

29. This, in my judgment, renders it impossible to apply the law as to penalties, which is not designed to apply to hypothetical contracts of this kind. The foundation of the law of penalties was described by Dickson J in the Supreme Court of Canada in Elsey v JG Collins Insurance Agencies Ltd (1978) 83 DLR (3rd) 1 as follows:

> "*It is now evident that the power to strike down a penalty clause is a blatant interference with freedom of contract and is designed for the sole purpose of providing relief against oppression for the party having to pay the stipulated sum. It has no place where there is no oppression."*

This passage was cited by the Privy Council with apparent approval in Phillips Hong Kong Ltd v AG of Hong Kong (1993) 61 BLR 41 (itself cited with apparent approval in Cavendish Square, above). Whether there is oppression is "*judged by reference to the circumstances at the time of contracting*" (para 243 of Cavendish Square per Lord Hodge) and is likely to involve considerations such as the respective bargaining power of the parties in their negotiations (ibid, para 35 per Lord Neuberger and Lord Sumption and para 152 per Lord Mance) and the legitimate commercial interests of the innocent party at the time of contracting (ibid, para 32 per Lord Neuberger and Lord Sumption, para 152 per Lord Mance, para 255 per Lord Hodge). It is impossible to see how such principles can be applied to a situation where there has been no negotiation and where there has been no actual contract between the parties but rather where the arrangement has been brought about by a statutory procedure and is binding on the company itself and its members and creditors (consenting or dissenting) by reason of a statutory hypothesis. It is equally impossible to see how a proposal put

forward by or on behalf of the company in the interests of itself, its members and creditors, approved by a statutory procedure and having effect by the statutory hypothesis, can somehow be said subsequently to have oppressed the company in some respect.

30. I note also that the Act provides for challenges to a CVA to be made within a tight timetable. The statutory grounds for a challenge under section 6 of the Act are unfair prejudice to the interests of a creditor, member or contributory of the company or a material irregularity at or in relation to the relevant meetings (the latter being given a broad meaning, as explained by Briggs LJ in relation to the equivalent provision for IVAs in Narandas-Girdhar v Bradstock [2016] BPIR 428). The applicants who may apply for relief are specified under the Act as the persons entitled to vote at either meeting (or who would have been entitled to vote if they had had notice of it), the nominee or his or her successor or, if the company is being wound up or in administration, the liquidator or administrator. The company has no voice in this process, save in so far as matters which could be said to affect its interests are taken up by the persons who are entitled to apply, who are persons either whose financial interests are affected by the CVA (members, creditors) or who are otherwise interested in implementation of the CVA (nominee or successor, liquidator, administrator). There is no apparent room here for the company to continue to have a separate ground of challenge (under the law as to penalties) which does not need to be brought forward within the same tight timetable. My conclusion is that that is because Parliament did not envisage any such principle continuing to apply.

31. Secondly, on the assumption that I am wrong on the first point and that there is still scope for the law as to penalties to apply, I reject the suggestion that, on the facts

before me, clause 25.9 imposes a penalty. I proceed here on the further assumption (but without deciding) that the liquidators are correct in their submission (a) that termination under clause 25.8 is a termination for breach and (b) that the clause would operate as a penalty as between the Company and all the affected Landlords even if it were triggered by notices served by only one of them.

32. Before the CVA was approved, the Company's Landlords (including Prudential) were entitled to the full rent reserved by the various Leases. The CVA proposal was, as I have summarised above, a proposal to reduce those rents, in the case of Category 2 and Category 3 Landlords, during the Rent Concession Period (clause 9), in the hope of achieving a more permanent solution in the form of a lower rent to the end of each relevant Lease (clause 10). If this could not be achieved, the Company's Landlords were to have the same claims against the Company as they would have had if the CVA Proposal had never been approved (clause 25.9). This was precisely the commercial outcome which the Landlords were promised in the proposal put before them for approval. Paragraph 3.21 of the Introduction read as follows:

> "*If the CVA Proposal were approved, but [the Company] was nevertheless unable to pay the sums due under the CVA in the first two years of operation, whether because the Financial Restructuring was not implemented or otherwise, the CVA would terminate and the compromises in the CVA Proposal would be undone. The effect of this would be that the Landlords and other compromised creditors would have their original contractual claims restored, and would be able to claim against [the Company] for whatever sums were due on their Leases or other contracts under their pre-CVA terms. As a result, following a termination, the Landlords and other compromised creditors should be in no worse position than if the CVA Proposal had never been approved*."

Given that this statement was Part I of the CVA Proposal submitted to creditors and members for approval along with the proposed CVA terms at Part V, it is, in my judgment, a legitimate aid to construction of the latter.

33. The liquidators' submission is, in effect, that one should ignore this kind of statement in considering whether clause 25.9 operates as a penalty. They say that the relevant considerations start with the agreement to replace the Contractual Rent with the Amended Contractual Rent (clause 9.1) and the compromise or settlement of any liability over and above the Amended Contractual Rent (clause 9.5). On that footing, there was no longer any continuing liability to pay the Contractual Rent and clause 25.9 must therefore create a new liability, arising on breach, where none had existed before. That analysis, in my judgment, fails to have proper regard to the fact that the CVA was proposed and approved as a single transaction – a transaction which contained both the terms of clause 9 and the terms of clause 25.9. These were not (as the liquidators' submissions would suggest) two separate transactions whereby the Contractual Rent was first replaced and compromised with new obligations being later imposed. The Company only obtained the benefit of the reduced rent because, at the same time, it agreed to unwind that concession in the event that the CVA did not achieve its objective and the Company could not pay its debts. For the purpose of the law of penalties, the Landlords (including Prudential) had a legitimate commercial interest in the CVA's success or failure and it could not be said to be an exorbitant, extravagant or unconscionable provision for them to be returned to their pre-CVA position if the CVA should fail. What is more, there was no question, at the time of the CVA, of the Company's negotiating position being weak, or any weaker than the Landlords'; they were both having to find a solution to the Company's impending insolvency. The proposal was one made by or on behalf of the Company and

intended ultimately to revive the Company's fortunes at the expense of the Landlords' legal rights (whatever they were then worth). There was no oppression involved in unwinding the CVA if that objective could not be fulfilled.

34. Thirdly, the liquidators' submission depends upon clause 9 effecting a variation of the relevant Leases (so as to enable the liquidators to contend that clause 25.9 imposed a new obligation). That reasoning is wrong.

35. As an initial consideration, I note that clause 9 does not, in terms, alter the rent reserved by the relevant Leases. Clause 10 does seek to vary "*the rent payable and reserved*" (i.e. when a more permanent solution is found) but that is not the language used in clause 9. If, as the liquidators submit, labels are important, it may be significant that clause 9 provides for what is to happen during a "*Rent Concession Period*", the obligation to pay the reduced rents being a "*Rent Concession Agreement*". I also note that, by the terms of clause 12.4(c), there might need to be some continuing or residual obligation to pay the full rent for the Landlord to be able to waive it in the event of an assignment of the Lease. Nonetheless, I am content to proceed on the basis that, as the liquidators contend, the effect of clause 9 is to replace the Contractual Rent with the Amended Contractual Rent during the period to which that provision applies and to compromise all liability which would otherwise have arisen during that period.

36. However I reject the liquidators' submissions at the point where they contend that clause 9 effects a variation of the Leases. At law, a variation of a lease granted by deed has to be by deed. Clause 9 cannot effect a variation of any of the Leases granted by deed (including the Leases to Prudential) as the CVA is not a deed. The CVA is, or operated as, a contract. This is important because the contract is a single

contract with a number of different terms, all of which are entitled to equal force and recognition. The Company cannot select one part of the contract and insist on its full effect whilst denying the proper effect of another. If the Leases had been varied at law, there may just conceivably be room for the liquidators' analysis (I say nothing about that as the operative terms would have to be different from those with which I am concerned) but where the parties' respective rights lie only in contract, the contract must be given effect as a whole.

37. In consequence, it seems to me that once termination has taken place in accordance with clause 25, the liquidators can no longer say that the rent reduction and compromise has any effect or has ever had any effect. Clause 25.9 expressly provides that the compromises are "*deemed never to have happened*" so that the Landlords have the same claims as they would have had absent the CVA. Accepting the liquidators' submission would involve giving effect to clauses 9 (and clause 17) while giving no effect to clause 25.9. This is to rewrite the terms which govern the Rent Concession Period. The Rent Concession Period was only ever a temporary regime; and the question whether the obligations and compromises arising while it was continuing would be of permanent contractual effect depended on whether the Leases were to be contractually varied to the end of the term (clause 10) or assigned (clause 12.2 to 12.4) or left in full effect following termination (clause 25.9). Reading the CVA as a whole, my conclusion is that clause 25.9 cannot be properly characterised as a penalty payable upon breach at all. Rather, it is one of a number of contractual terms that define the length of the Rent Concession Period and specify the basis upon which the reduced rent is to be payable (clause 25.9 being the term that provides for what is to happen to the rent concession if the CVA should be terminated). So understood, the contention that clause 25.9 creates a penalty must fail.

38. The Vivienne Westwood case is not in point because there, as the judge found, there was no "original" rent in the lease higher than the "concessionary" rent agreed by the side-letter: the "concessionary" rent was in fact the rent agreed at the outset. That was the reason why the side-letter created a penalty when it provided for the higher rent to apply if the tenant was in default. The higher rent had never been payable before and was only payable on breach. That is not the case here. The original rent was undoubtedly payable before the CVA: that was one of the reasons why the Company had got into difficulty. The reduced rent imposed by the CVA was a true concession by the Landlords.

39. To my mind, a better analogy is provided by the case of Re Smith and Hartogs (1895) 72 LT 221. There, a landlord agreed to a reduction of the rent payable for the time being, with the balance in effect being added to the rent payable later in the term. The tenant failed to pay the reduced rent. In those circumstances it was held that the landlord was entitled to distrain for the full amount of the rent. Vaughan Williams J said:

> "*To put the case in the manner most favourable to the trustee [i.e. the tenants' trustee in bankruptcy]; Here was an agreement that if the tenant paid the rent agreed upon by instalments, the landlord would not enforce his original remedy. Treating the agreement as being one for good consideration, it cannot be enforced by the tenant if he was in default ...*"

So, here, the CVA provided for a Rent Concession Period to enable the Company's finances to be re-structured; that objective was not achieved and the Company defaulted; in those circumstances, the Company must accept the consequences, which (by the terms of the CVA itself) were that the concession be unwound. In such circumstances, the position is as stated by Lord Westbury in Thompson v Hudson

above, "*if a man submits to receive, at some future time and on the default of his debtor, that which he is entitled to receive, it is impossible to understand how that can be regarded as a penalty*" (p 28).

(ii) The pari passu issue

40. The liquidators' next submission is that the effect of clause 25.9 is to increase substantially the claims which the Category 2 and 3 Landlords would have in the insolvency proceedings which were, for all practical purposes, bound to follow the failure to achieve the CVA's objective. This, it is said, infringes the principle (the "pari passu principle") that "*statutory provisions for pro rata distribution may not be excluded by a contract which gives one creditor more than its proper share*" (Belmont Park Investments Pty Ltd v BNY Corporate Trustee Services Ltd [2012] 1 AC 383 at para 1 per Lord Collins of Mapesbury). (A separate though related rule, the anti-deprivation rule, applies to prevent attempts to withdraw an asset on bankruptcy or liquidation or administration, thereby reducing the value of the insolvent estate to the detriment of creditors (ibid, para 1 per Lord Collins and paras 148-9 per Lord Mance) but it is the pari passu principle which the liquidators rely upon before me).

41. The liquidators' submission is that clause 25.9 effectively provides for a substantial increase in the Landlords' claims against the Company in the event of the Company's insolvent collapse. If the Company had survived as a going concern, the Landlords' claim would have been limited to the Amended Contractual Rents payable under the CVA. But, if the CVA's objectives were to fail and the CVA terminated (with inevitable consequences for the Company's solvency), the Landlords would be able to claim substantially greater sums in the administration or liquidation.

42. As I understand it, this submission is based (like the appeal to the law of penalties) upon the analysis that the CVA effected a variation of the Company's liabilities to its Landlords with the consequence that clause 25.9 created a new liability where none existed before. For the reasons I have already explained (in particular my third reason in relation to the penalty issue, above) I do not accept this analysis at all. In my judgment, the CVA created a Rent Concession Period during which reduced rents (and other sums) were payable to Category 2 Landlords like the Prudential, in full and final satisfaction of any liability under the relevant Leases. However the terms of that concession included clause 25.9, by which the concession was to be unwound in the event that the CVA were terminated. The express consequence would then be that the parties would be restored to their original positions and the reduced rent and other sums actually paid would not be taken to be in full and final satisfaction of the Company's obligations under the Leases. Thus the termination of the CVA cannot properly be said to have increased the Landlords' claims in the Company's administration or liquidation; the true position was that the rent concession which might have applied if the Company's finances had been re-structured was brought to an end and the original rent (and other sums) continued to have effect. The liquidators cannot pick one part of the CVA (clauses 9 and 17) and reject another (clause 25.9): all these terms governed the way the concession was to operate. The clear intention of the CVA was to ensure that Landlords were not to be disadvantaged if the CVA were terminated, by being forced to continue a concession which was expressly conditioned to apply only while the CVA remained in force. It is quite wrong therefore to characterise the rent concession as final and the provision unwinding it as somehow conferring upon the Landlords an advantage in the

Company's administration or liquidation. That is to turn the substance of the agreement on its head. I therefore reject the liquidators' submissions.

(iii) The administration expense issue

43. The final issue is whether any part of the outstanding rent payable as a result of the termination of the CVA and the terms of clause 25.9 is payable as an administration expense. Prudential claims that it is. While the CVA was in force, Prudential was entitled to receive the reduced rent and other sums payable to it as a Category 2 Landlord; but, it argues, the effect of clause 25.9 was to restore its full rights under the relevant Leases, with the consequence that it is now owed additional sums in respect of the Rent Concession Period. For some of that period, the (original) administrators were in possession of the premises for the benefit of the administration and the evidence is that they paid all the (reduced) rents and other sums due under the relevant Leases in accordance with the CVA (subject to certain disputes which I am not asked to resolve on this application). In doing so, they were apparently accepting that the rents and other sums were payable as an administration expense. The principle which applies here was summarised by James LJ in In re Lundy Granite Co, ex p Heavan (1871) LR 6 Ch App 462 at p 466 as follows:

> "*if the Company for its own purposes, and with a view to the realisation of the property to better advantage, remains in possession of the estate, which the lessor is therefore not able to obtain possession of, common sense and ordinary justice require the court to see that the landlord receives the full value of the property*."

A more recent summary of the principle is that of Lewison LJ in Jervis v Pillar Denton Ltd [2015] Ch 87 at para 101, as follows:

> "*The true extent of the principle, in my judgment, is that the office holder must make payments at the rate of the rent for the duration of any period during which he retains possession of the demised property for the benefit of the winding up or administration (as the case may be). The rent will be treated as accruing from day to day. Those payments are payable as expenses of the winding up or administration. The duration of the period is a question of fact and is not determined merely by reference to which rent days occur before, during or after that period.*"

(The issue in Jervis was whether a company in administration was liable to pay a quarter's rent as an administration expense even though the amount had fallen due for that quarter the day before the company had entered into administration; the Court of Appeal held that it was). Prudential contends that the principle requires that the amount paid as an expense of the administration is not just the concessionary amount payable while the CVA was in force but, now that the CVA has been terminated and the concession unwound, the full amount of rent due under the relevant Leases.

44. The liquidators resist this conclusion. They say that what needs to be paid is the rent which accrued due during the relevant period. "*Rent accrued*" or "*rent accruing*" is the phrase used in the authorities, such as Lundy Granite, above, at p 467 per James LJ, In re ABC Coupler and Engineering Co Ltd (No 3) [1970] 1 WLR 702 at p 709 per Plowman J, In re Downer Enterprises Ltd [1974] 1 WLR 1460 at p 1469 per Sir John Pennycuick V-C and In re HH Realisations Ltd (1975) 31 P&CR 249 at p 253 per Templeman J. Here the rent accruing during the period of possession for the purpose of the administration was that due under the CVA. That rent was indeed duly paid, and paid in full and final satisfaction of any liability under the relevant Leases, as provided by clause 9.5. Moreover, no other rent was payable as (the liquidators contend) clause 25.9 did not restore the rent payable under the original Leases: what it

did was to create a new liability, to be calculated by reference to the amounts which would have been payable under the Leases if the CVA had not been approved.

45. I would approach the matter in this way. The rent accruing or rent accrued in respect of any period must include all sums payable for the premises in respect of that period, even if they are only contingent or yet to be ascertained at that time. It is only in this way that the landlord will receive the "*full value of the property*" (In re Lundy Granite, above) or "*the rent in full*" (In re Silkstone and Dodworth Coal and Iron Co (1881) 17 ChD 158 at p 160 per Fry J), which is what the principle is intended to achieve. So, for example, the rent accruing would include any uplift yet to arise from a rent review which had not yet been implemented or resolved at the time of the administrators' beneficial use of the premises (assuming the reviewed rent would be retrospectively applied under the lease). Similarly, supplemental rents and other incidental payments due under the various leasing and hire-purchase agreements in question in Re Atlantic Computer Systems plc (No 2) BCC 454 were payable as administration expenses in addition to the ordinary periodic payments, even if they were as yet unascertained. Such payments were "*in truth attributable to the current use of the equipment in question*" (p 459H per Ferris J), which is the relevant consideration. On this basis, if clause 25.9 has the effect of restoring the rent payable under the relevant Leases with retrospective effect, then the full amount would be payable as an administration expense for the relevant period.

46. In my judgment, and for the reasons I have already given, that is precisely what clause 25.9 did achieve. By that clause, the compromises and releases are deemed (by agreement) never to have happened "*such that all Landlords ... shall have the claims against [the Company] that they would have had if the CVA Proposal had never been*

approved …" Those claims would be or include claims arising under and by virtue of the relevant Lease, which are deemed not to have been compromised or released. The liquidators sought to argue that the deeming provision was introduced purely to allow the calculation of the amount due but without making that amount contingently payable as rent due under the Leases. I cannot see any reason for drawing any such distinction on the terms of the clause. If the compromises and releases in the CVA are to be ignored (because deemed never to have happened), then "*the claims*" which remain to be made are those under the Leases. These are the claims that, the clause provides, the Landlords "*shall have*" on termination. That result is entirely consistent with the explanation given to the Landlords in paragraph 3.21 of the introduction to the CVA proposal which I have quoted above, namely that, on termination, "*the Landlords … would have their original contractual claims restored, and would be able to claim against [the Company] for whatever sums were due on their Leases or other contracts under their pre-CVA terms*".

47. Some argument was addressed to me as to the effect of a deeming provision of the kind set out in clause 25.9. Despite some academic criticism (notably in Wilken and Ghaly on The Law of Waiver, Variation, and Estoppel, paras 13.22-13.24), the Court of Appeal has decided that a provision of this kind can take effect as a contractual estoppel, preventing either party from denying the facts agreed: Peekay Intermark Ltd v Australian and New Zealand Banking Group Ltd [2006] 2 Lloyd's Rep 522. That authority is binding upon me, as is the decision of Aikens J in Trident Turboprop (Dublin) Ltd v First Flight Couriers Ltd [2008] 2 Lloyd's Rep 581 which specifically applied the decision in Peekay to a deeming provision. However, I also observe that the deeming provision is not central to the terms of clause 25.9. What is crucial is that clause 25.9 provides that, upon termination, the Landlords "*shall have the claims*

against [the Company] that they would have had if the CVA Proposal had never been approved". The deeming provision is simply a formula to clarify that this consequence is to take effect in priority to and notwithstanding the terms of the compromises and releases. I do not therefore regard the deeming provision, in context, as creating any difficulties of construction or application.

(iv) Conclusion

48. For those reasons, I would declare that the additional sums falling due to Prudential upon the termination of the CVA are payable as an administration expense or administration expenses for the period during which the (original) administrators were in possession of the premises for the purposes of the administration. If there is any dispute as to the amount of that liability on the facts, the parties before me should have liberty to apply to resolve it.