

Consent Fees and Noteholder Meetings

Earlier this week, the Court of Appeal upheld the first instance decision of Mr Justice Hamblen in *Azevedo v Imcopa Importacao and others*, confirming that payments of consent fees in exchange for votes in favour of amendments to the terms of debt securities were neither unlawful, nor in breach of a contractual obligation to distribute any payments *pari passu*. Nevertheless the withdrawal of the conjoined appeal in *Assenagon Asset Management S.A. v Irish Bank Resolution Corporation* [2012] EWHC 2090 (Ch) has left certain important principles untested before the higher Courts.

Consent Fees and Noteholder Meetings

In the Summer of last year, the closely sequenced decisions of the High Court in *Azevedo v Imcopa Importacao and others* and *Assenagon Asset Management S.A. v Irish Bank Resolution Corporation* turned the spotlight on Noteholder Meetings, consent fees and the so-called "exit consent". Though both were appealed to the higher courts, the subsequent liquidation of Irish Bank Resolution Corporation Ltd. (formerly Anglo Irish Bank) has meant that only the *Azevedo* litigation has proceeded to further judgment. Whilst this has endorsed the view set out in our earlier paper (*Noteholder Meetings: Paying the Price for Change – May 2012*), it has also left unresolved some of the more detailed issues highlighted in that briefing, and our related paper on the *Assenagon* judgment (*Liability Management: Exit Consents and Oppression of the Minority – July 2012*).

Background – The First Instance Decision

The facts of the *Azevedo* case are already addressed in our earlier briefing. In the first instance decision, following the reasoning in *Goodfellow v Nelson Line (Liverpool) Ltd* and *British American Nickel Corp Ltd v MJ O'Brien Ltd* Mr Justice Hamblen concluded that consent fee payments were not bribes when made openly and where no noteholders were prevented from exercising their voting rights.

The Court also confirmed that the payments were not inconsistent with the *pari passu* requirements in the contractual documentation governing the relevant debt securities.

The Issues on Appeal

The two key elements of the first instance decision were revisited by the Court of Appeal. The first issue was a narrow point of contractual interpretation, as to whether payments of a consent fee in this particular case violated the *pari passu* provisions of the debt securities

Key issues

- Court of Appeal upholds payment of consent fees in connection with Noteholder Meetings
- Fees can be paid only to holders who vote in favour of a resolution
- Open disclosure of fee arrangements required
- Care should be taken over routing of any consent payments via a Trustee
- Coercive and oppressive structures may still be liable to challenge.

and the related trust deed. The second issue was a more general question as to "whether English law permits a company to solicit and procure votes...by offering and making cash payments to those members of the relevant class who vote in favour of the proposal but excluding from the payment those who vote against it..."

The Pari Passu Principle

On the narrower point, the Court of Appeal unanimously concluded that the *pari passu* provisions of the documents only applied to payments that passed through the hands of the Trustee. In this particular case, the consent fees were an additional payment made by the relevant company outside of the terms of the contractual documentation, and did not form part of the property that was held on trust for the benefit of Noteholders.

Although this may seem a relatively straightforward proposition, and one that accords with market practice, it is worth noting that this was a very narrow basis for the Court's decision, and the Court did not have to address the question of what ought to have happened if the payments had been routed via the Trustee. Care should therefore be taken to ensure that these sorts of payments are not inadvertently placed in the hands of a Trustee or other party who has an over-riding contractual obligations to apply those funds in a particular manner.

Consent Fees in General

Insofar as the general issue of consent fees was concerned, Lloyd LJ was comfortable that, as a basic principle, an offer to pay a consent fee could give rise to a collateral contract between the Issuer (or Offeror) who is promising the fee and the voting Noteholder who accepts such an offer by delivering a positive vote in favour of the proposals.

Moreover he was robust in his support of Mr Justice Hamblen's view that there was nothing inherently unlawful in the practice of offering consent fees:

"I can see nothing wrong or unlawful, in general terms, in a process of putting to

all members of a class a proposal which offers benefits open to all who vote in favour...but not to others. No member of the class is thereby excluded from participation in the offered benefits except by his own choice as to whether, and if so how, to vote."

Although this seems to be a fairly sweeping endorsement of consent fees, there are certain limitations to the scope of the Court's sanction, not least because the terms of the underlying resolution were not alleged to be in any way unfair or oppressive.

W(h)ither the Exit Consent?

As noted above, the Court specifically did not have to consider the issues raised in *Assenagon* and Lord Justice Lloyd, in his leading judgment, was at pains to point out: *"Accordingly, the issues raised in that case...remain open to be tested at appellate level"*.

Accordingly whilst the *Azevedo* appeal has confirmed that consent fees are not inherently unlawful, it has not provided any meaningful clarity to the debate regarding exit consents and resolutions that are (or may be argued to be) oppressive or unfair as between one group of Noteholders and another. The payment of a consent fee does not inevitably make a resolution unfair, but nor does the decision in *Azevedo* serve to whitewash every structure in which such fee payments appear.

As a result, care should still be taken in circumstances where resolutions or modifications are proposed which are clearly detrimental to a holder's rights, (e.g. compulsory redemption or squeeze out provisions), as the payment of a consent fee would not necessarily remove any concerns as to the fairness

of the underlying proposals. Lloyd LJ's judgment in *Azevedo* reaffirmed the central tenet of Viscount Haldane's judgment in *British American Nickel Corp Ltd v MJ O'Brien Ltd*, that *"the power given must be exercised for the purpose of benefiting the class as a whole, and nor merely individual members only..."*

It seems clear from the judgment that the Court of Appeal is not yet ready to abandon the long-standing principle that voting powers must be exercised *"bona fide in the interests of the class as a whole"*, and that therefore the challenge of ensuring that consent fees do not offend this principle will remain an important one.

Although the *Assenagon* appeal did not proceed to judgment, the first instance decision of the High Court nevertheless provided some welcome guidance on this issue. In distinguishing the facts of *Assenagon* from those at issue in *Azevedo*, Mr Justice Briggs confirmed that the facts in the latter case were such that *"it was not irrational to conclude that the proposal, ignoring the benefit of the inducement, was nonetheless itself capable of being regarded as beneficial to the class"*.

By contrast, in circumstances where the resolution could not credibly be viewed as beneficial to the Noteholders as a class, the Court would have grounds to intervene when disproportionate consideration was available to one group of noteholders as opposed to another. In the authors' view, this remains a crucial principle for determining whether incentive fees will or will not be permissible.

Useful Links

Clifford Chance Briefing: Noteholder Meetings: Paying the Price for Change?

http://www.cliffordchance.com/publications/publications/2012/05/noteholder_meetingspayingthepriceforchange.html

Clifford Chance Briefing: Liability Management: Exit Consents and Oppression of the Minority

http://www.cliffordchance.com/publications/publications/2012/07/liability_managementexitconsentsan.html

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