

Guide to Company Voluntary Arrangements (CVAs)

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February 2019

WHAT IS A CVA?

- Compromise between an English, Scottish or EEA company and all of its unsecured creditors
- Bespoke arrangement with contractual force (but not a true contract) given effect and challengeable by statute
- Insolvency Practitioner (IP) nominee/supervisor
- No moratorium on other claims prior to CVA implementation (except 28 day optional moratorium for “small” eligible companies)
- “Small” two or more of: £10.2m turnover or less; £5.1m balance sheet or less; 50 or fewer employees

WHAT DOES A CVA PROPOSAL COMPRISE?

- Statement of affairs, current financial position, compromise on debts, nomination of IP, IP comments
- IP submits report to court recommending consideration by creditors and shareholders
- IP then seeks decision
- 14 days' notice to all known creditors
- Permanent or temporary variation of lease terms?
- Historic and/or forward looking?

WHY WOULD A TENANT COMPANY WANT TO ENTER A CVA?

- Financial difficulty with unsecured creditors
- Avoid terminal insolvency
- Directors remain in office
- Opportunism
- Cheaper than other insolvency procedures
- Limited court involvement
- Alternative: “CVA clause” in leases e.g. Next
- Average 5 year term

WHAT SHOULD A LANDLORD DO IF FACED WITH A CVA PROPOSAL?

- Read proposal carefully and seek legal advice
- Consider all options promptly within 14 day notice period
- Repossession prior to CVA approval (unless moratorium)
- Calling rent guarantee
- Influence content of CVA proposal
- Maximise value of landlord claim to maximise influence in vote
- Talk to other landlords/creditors to coordinate approach
- Consider rights on eventual failure of CVA

WHAT IS THE APPROVAL PROCESS?

- Vote by creditors and shareholders
- Virtual or physical meeting
- Approval by at least 75% (by value of unsecured claims) of creditors who vote
- Unless more than 50% (by value of unsecured claims) of unconnected creditors vote against
- Approval by simply majority (by value) of shareholders
- Cannot affect right of secured creditors to enforce, except with their consent

WHAT IS THE EFFECT ON A LANDLORD AND OTHER CREDITORS?

- Binds all known and unknown creditors entitled to vote (including dissenting parties)
- Usual contractual formation principles do not apply
- Determining rights of creditors
- Categories of leases

WHAT IS THE EFFECT ON A RENT GUARANTEE?

- No effect provided guarantee is worded to be unaffected by debt compromise and CVA proposal is silent
- Otherwise could release guarantor if CVA amounts to debt satisfaction
- Some CVAs seek release of guarantee provided adequate compensation paid to landlord
- Court reaction

CAN A CVA BE CHALLENGED AFTER CREDITOR APPROVAL?

- Within 28 days of the CVA's approval by creditors and/or challenging creditor aware of CVA
- Unfair prejudice:
 - question of fact
 - treating of creditors in each category inconsistently (horizontal)
 - CVA is not materially better than likely alternative (vertical)
- Material irregularity:
 - conduct of the decision procedure / conflict of interest / non-disclosure
 - incorrect valuation of claims

WHAT IF A CVA IS NOT COMPLIED WITH AND/OR TERMINATES?

- 2013 CVAs:
 - 18.5% fully implemented
 - 16.5% ongoing
 - 65.0% terminated without achieving aims
- Average intended length of CVA is 5 years (too long?)
- 28 day pre-CVA moratorium reduced terminations to 20%
- Lack of standard terms; what happens for landlord on termination?

CAN A PROPERTY BE REPOSSESSED IF RENT PAYMENTS ARE SUBJECT TO CVA?

- Prior to CVA entry into force depends on:
 - no moratorium scenario
 - Moratorium scenario
- After CVA entry into force:
 - failure to pay future rent if CVA silent
 - scope of CVA agreement

MOTHERCARE CASE STUDY – JUNE 2018

Four categories of leases:

- **Category 1 Premises** (66 stores): performing adequately or core to future business – monthly rental payment for 3 years
- **Category 2 Premises** (21 stores): underperforming – marginally profitable and/or property costs are above market – rent reduced by 50%, paid monthly for 3 years and additional landlord right to terminate
- **Category 3 Premises** (50 stores): not of future strategic use – exit by June 2019 with rent reduced by 70% in meantime and additional landlord right to terminate
- **Category 4 Premises**: lease has expired – payment of 5% of final month's rent paid for release of dilapidations

THE LANDLORDS STRIKE BACK

- **BHS CVA March 2016** – landlord challenge to subsequent liquidators
 - Right to full rent after CVA termination is not a penalty
 - No permanent variation of leases (CVA not made by deed)
 - Full rent remained contingent liability (including any rent uplift)
- **House of Fraser CVA July 2018** – landlord challenge
 - Disproportionate effect on landlords
 - Alternative rescue possible
 - Challenge settled prior to administration
- **Regis CVA October 2018** – landlord challenge
 - “substantively unfair” CVA terms
 - Wide-ranging changes to lease terms
 - “questionable transactions” prior to business sale in October 2017