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COMPANY VOLUNTARY ARRANGEMENTS [“CVAs”]

2019 has seen a large rise in the number of Company Voluntary Arrangements [“CVAs”] being proposed by struggling businesses prompting Landlords and suppliers to air concerns that the process may be being used inappropriately. This month’s commentary therefore explores CVAs to give a better understanding of the considerations increasingly affecting businesses.

A CVA is an insolvency process that allows a struggling business to continue operating whilst negotiating full or partial repayment of its debt with unsecured creditors.

An Arrangement would typically last for 3-5 years and is an attractive proposition to Company directors as they retain control of the Company which, if successful will survive the process. It provides relief from creditor pressure to allow the directors to implement the necessary restructuring changes to the business operation. The Company can terminate unprofitable contracts and can make staff redundant more easily making the process extremely attractive to Companies which are weighed down by unprofitable contracts or are over-staffed.

From a creditor perspective, CVAs often provide a significantly improved return compared to other insolvency processes. However, in proposing a CVA, the Company is not only asking creditors to wait a significant period for repayment, but often for some level of debt relief. As such, the proposed CVA would need to obtain the approval of 75% of voting creditors to be implemented.

Once approved, all unsecured creditors will be bound by the terms of the Arrangement, irrespective of whether they voted in favour of it. The Arrangement does not bind secured creditors and they will rely on their security, leaving Companies open to Administrators being called in, even when the agreement is adhered to.

CVAs also have their disadvantages that need to be considered by the Board before proceeding. For example, once a CVA proposal is issued, a Company’s credit score is all but eliminated restricting access to supplier credit and lending facilities.

During the period the CVA is in place, any profits generated will be subject to conditions imposed by the Arrangement and creditors to ensure they are firstly allocated to repaying the debts subject to the Arrangement. As such, it is often best used as part of a restructuring process suited to Companies with a long-term vision.

The recent case of House of Fraser saw Landlords raising genuine concern that the CVA process was not being used to restructure the business but merely to avoid onerous lease liabilities. A consequence of this position is that Companies subject to a CVA can obtain an unfair competitive advantage over its rivals by operating in the same location with significantly reduced property costs. As such, it has been reported that a major high street retailer is now looking to insert a ‘CVA clause’ into all its leases that entitles them to a rent reduction should a neighbouring retailer be granted rent reductions and/or holidays as part of a CVA.

Please note that should your clients require any confidential advice regarding insolvency matters they are welcome to contact one of our partners. Initial advice is provided free of charge and without obligation. Also, if you or any of your colleagues require any clarification regarding insolvency law or procedures please do not hesitate to contact us.