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TENANT COMPANY VOLUNTARY ARRANGEMENTS - TEN KEY POINTS FOR LANDLORDS

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There has been a series of high profile tenant company voluntary arrangements (CVAs), particularly in the retail and casual dining sectors. Many landlords have been hit by closure of underperforming stores, and by rent cuts on those remaining open. Here we outline ten points for landlords on what CVAs are, how they are entered into and what landlords can do to protect themselves.

What is a CVA?

A CVA is a statutory process, supervised by an insolvency practitioner. It allows a company in financial difficulty to:

- settle its unsecured debts by only paying a proportion of the amount due; and
- to come to an arrangement with its creditors about the payments of its debts.

It can be used on its own, or in conjunction with another insolvency process, such as administration.

What is the purpose of a CVA?

To save businesses in financial difficulty from closing down by reducing their debt burden.

Who proposes a CVA?

The company's directors (or its administrators, where the company is in administration, or its liquidator, where the company is in liquidation).

Who approves a CVA?

A CVA goes ahead where:

- at least 75% by value of voting creditors vote in favour of it; unless
- more than 50% by value of creditors voting against the CVA are creditors "unconnected" with the company.

The value of a landlord's claims in relation to other unsecured creditors determines that landlord's voting power.

There is also a shareholder vote, but it is the creditor vote that determines whether or not the CVA goes ahead. CVAs do not bind secured creditors (for example a bank with a charge over freehold property) unless they agree.

Do tenants need their landlords' agreement before entering into a CVA?

No, if the required majorities vote in favour, the CVA is binding on all unsecured creditors entitled to vote, and those who would have been entitled to vote if they had notice. Therefore a landlord may be bound by a CVA even though it voted against and is strongly opposed to it.

Creditors, including landlords, have 28 days after a CVA has been agreed and filed at court in which to challenge the CVA. There are two grounds for challenge: unfair prejudice and material irregularity.

Why do tenants enter into CVAs instead of other insolvency arrangements?

Where a company in financial difficulties is a tenant, a CVA may allow the company to restructure its rent obligations and thereby improve its financial position.

CVAs are flexible in that they can provide for different categories of creditor to be paid on different terms. This contrasts with other insolvency procedures such as administration and liquidation where all unsecured creditors must be treated equally. The downside for landlords of this flexibility is that landlords may find themselves particularly adversely affected by the terms of a CVA, for example where future rents are cut significantly but

the landlord cannot terminate the lease early. Sometimes CVAs may leave landlords worse off than if the company had entered another insolvency process such as administration.

How does a tenant CVA affect landlords?

Once bound by a CVA, a landlord cannot take any step against the company to recover a debt that is within the scope of the CVA. The arrangement will catch rent arrears and will usually also cover other sums that are due or will become due under the lease, including future rent and dilapidations.

How about guarantees?

Most lease guarantees are worded so that the guarantor's liability is not automatically affected by a CVA. However:

- some guarantee wording may result in a lease guarantor being released automatically when a CVA is approved; and
- in principle, a CVA can expressly release a guarantor of the debtor company from its guarantee obligations, provided that the landlord is compensated for the loss of its rights. The good news for landlords is that the courts have not been quick to find that a CVA is effective to release a guarantor in this way.

What should landlords do when a tenant CVA is proposed?

Take legal advice, for example on:

- what steps the landlord can take before the CVA vote takes place, for example whether it wants to and can forfeit the lease at this stage. Whether the landlord can forfeit depends on the wording of the lease forfeiture clause and whether there is a moratorium on debt enforcement in place; and
- how the landlord's claims, such as for future rent, are being valued for voting purposes. This may be crucial in determining the relative weight of the landlord's vote in the CVA approval process. It may be possible to appeal the valuation, but it is vital to act quickly.

What can landlords do to protect themselves

against a tenant CVA?

There are a number of steps landlords can take, for example:

- before granting a lease, landlords should carefully consider the strength and types of security that the prospective tenant is offering, in view of the tenant's covenant strength and the risk of a tenant CVA or other insolvency process;
- if a CVA is proposed, landlords should consider taking early advice on the CVA process and proposed terms and on the valuation of their debt (which affects the weight of their vote in the CVA approval process). They may also take advice on whether they are able to forfeit the lease at this stage, if that would suit their plans for the property;
- once a CVA is approved, landlords may consider challenging it, on their own or together with other affected landlords.

What can we do to help?

We can advise you on how best to protect your position at all asset management stages and once a CVA is proposed. Please get in touch with your usual Gowling WLG contact if you would like us to help.

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