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Company Voluntary Arrangement

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Summary and implications
This note provides a short summary of company voluntary arrangements ("CVA") and covers some of the frequently asked questions. Each CVA is different and what follows is a general overview. Specific advice should be taken in individual cases.

A CVA is a rescue procedure for a company in financial difficulties. A CVA is defined as "a compromise or other arrangement" with creditors under Part I of the Insolvency Act 1986 (the "1986 Act").

A CVA is carried out under the supervision of an insolvency practitioner ("IP") known as the "nominee" before the proposal is implemented and as the "supervisor" afterwards. The arrangement will be binding on creditors (if the relevant majorities vote in favour of the proposal at meetings of creditors and shareholders of the company). A CVA does not affect the rights of secured or preferential creditors unless they agree to the proposal.

The limited amount of court involvement (restricted to filing various documents) means that a CVA is potentially a simpler, lower cost form of restructuring. Theoretically, this should mean that CVAs would be a popular, low-cost option.

On 1 January 2003 the Insolvency Act 2000 (the "2000 Act") introduced an optional 28-day moratorium for small companies to allow them to put a CVA proposal to their creditors.

Aim of a CVA
Prior to the 1986 Act, a company wishing to enter into an arrangement with its creditors would only have had recourse to the scheme of arrangement procedure now contained in Part 26 of the Companies Act 2006.

The aim of introducing the CVA procedure was to allow companies to avoid liquidation by coming to a binding agreement or compromise with the company's creditors with the minimum of court involvement. CVAs may be used to avoid or supplement other types of formal insolvency procedures, such as administration or liquidation.
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The CVA procedure may be used by solvent as well as insolvent companies in financial difficulties.

**Proposing a CVA**
The essence of a CVA is that the directors of a company (other than one which is in administration or being wound up) make a proposal under Part I of the 1986 Act to the company and to its creditors for a "composition in satisfaction of its debts" or a "scheme of arrangement of its affairs".

A proposal for a CVA may also be made, where the company is in administration, by the administrator and where the company is in liquidation, by the liquidator.

**Who may act as nominee?**
A proposal for a CVA should identify a person who will act as the nominee in relation to the CVA either as trustee or otherwise for the purpose of supervising its implementation.

Where an administrator or a liquidator makes a proposal for a CVA, the administrator or liquidator will normally act as the nominee.

Prior to the 2000 Act, the nominee of the CVA had to be a licensed insolvency practitioner.

**Setting up a CVA**
Nominee considers proposal and reports to court
Where the nominee is not a liquidator or an administrator, the nominee must, within 28 days (which can be extended by court order) of being given notice of the proposal for a voluntary arrangement, submit a report to the court stating whether, in his opinion, meetings of the company and of its creditors should be called to consider the proposal.

This effectively gives the nominee a period of time to consider the proposal and its viability. If the administrator or liquidator is the nominee, he may simply summon a meeting of shareholders and creditors without the prior need to report to the court.

Statement of the company's affairs
To enable the nominee to prepare his report, the persons making the proposal, usually the directors, must give him a document setting out the terms of the proposed voluntary arrangement and a statement of the company's affairs containing details of the company's creditors, debts, liabilities and assets.

The meetings
Where the nominee recommends to the court that meetings should be held, he may call the meetings at the time and place recommended in his report to the court, unless the court orders otherwise.

Notice to the creditors
The person who calls the creditors' meeting must summon every creditor of the company of whose claim and address he is aware. Creditors must be given 14 days' notice of the meeting.

**Combining a CVA with administration**
For larger companies, the lack of a moratorium is a particular disadvantage of the CVA procedure. This can be overcome by combining the CVA procedure with administration, although inevitably increases the cost of the exercise and detracts from the original purpose of having a CVA as a cheap and informal alternative to administration.

**Authorising a CVA**

The creditors and members decide at their relevant meetings whether or not to approve the proposed CVA with or without changes. Where the decision of the creditors’ meeting differs from that of the members’ meeting, the decision of the creditors takes precedence.

Any proposal must allow for the payment of any preferential debts first in priority to other unsecured creditors. Otherwise, the proposal must be approved by a simple majority in value of the members and by more than 75 per cent in value of the company’s creditors present and voting.

However, the creditors’ meeting cannot approve any proposal or modification that affects the rights of a secured creditor to enforce its security without its consent.

**Binding creditors**

Before the 2000 Act came into force a CVA only bound those creditors who had notice of the proposal and were entitled to vote at the relevant meeting. This caused problems with creditors who could not be traced.

From 1 January 2003, an approved CVA will bind not only creditors who had notice of and were entitled to vote at the meeting but also creditors who would have been entitled if they had received notice of the meeting.

Other problems in practice include determining the voting rights of creditors in relation to disputed, unliquidated or unascertained debts. This can be a very difficult task for the insolvency practitioner but cases have shown that the court is unlikely to allow challenges to the insolvency practitioner’s estimates of the value of the creditors’ debts, if made in good faith.

**Operation of a CVA**

The approved CVA takes effect as if made by the company at the creditors’ meeting. The nominee becomes the supervisor of the CVA and is given the power to implement the proposal.

Implementation may involve the directors (or liquidator/administrator, if he is not the supervisor) handing over the assets of the company to the supervisor. The supervisor can petition for the winding-up or administration of the company.

The power of the supervisor derives from the terms of the CVA, but in carrying out this role the supervisor is entitled to apply to the court for directions.

If the supervisor considers that the CVA should cease, he may apply to the court for an administration or winding-up order.

The threat of administration or winding up may be instrumental in the supervisor securing the creditors’ consent to the CVA.
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If the CVA is successful, the supervisor must send a report on the implementation of the proposal to all members and creditors who are bound by the CVA within 28 days of its final completion.

A successful CVA typically results in the company being relieved of its entire pre-CVA debts and being able to trade uninterrupted throughout the CVA process.

**Challenges to a CVA**

A CVA can be challenged in court on the grounds of unfair prejudice or material irregularity within 28 days of the approval being reported to court.

**Binding the creditors**

As well as introducing an optional CVA moratorium for small companies, the 2000 Act also addressed the problem of binding creditors who may be difficult to trace.

**Position under 1986 Act**

Under the 1986 Act, an approved CVA was only binding on creditors who had notice of, and were entitled to vote at the creditors' meeting convened to consider a CVA proposal. It did not bind creditors who had no notice of the meeting.

**Position under 2000 Act**

The approved CVA will now bind creditors who were entitled to vote at the creditors' meeting and creditors who would have been entitled if they had had notice of the meeting. This means that CVAs are binding on both known and unknown creditors.

If a creditor (for example, an unknown creditor) is bound by a CVA without having received notice of the meeting and that creditor does not receive any payments under the CVA, the company will be liable to pay that creditor the amount he should have received under the CVA when the CVA comes to an end unless the CVA comes to an end prematurely.

As a deterrent against a director deliberately concealing known creditors, it is an offence for a director to make any false representations for the purpose of obtaining the approval of the creditors to a CVA.

**Applies to small and large companies**

These amendments apply to all CVAs and not simply CVAs in respect of companies that meet the eligibility requirements for a CVA moratorium.

The amendments are significant: a creditor could now find that a CVA has been approved, and all of the company's assets have been distributed according to that CVA, without his being aware of the CVA or receiving any payments under it.

**Advantages and disadvantages of a CVA**

**Advantages**

- A CVA is an informal insolvency procedure with limited court involvement. It is therefore cheaper than formal insolvency procedures, which may mean more money for creditors.
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- There is an optional moratorium available for small companies to protect the company from creditors’ actions whilst a proposal for a voluntary arrangement is being put into place.

- In the absence of the optional moratorium for small companies, it is possible to combine a CVA with an administration, which brings with it the benefit of a statutory moratorium. The administrator may be able to put together a suitable CVA proposal to persuade the creditors and save the company.

Disadvantages
- The main weakness of a CVA procedure is that there is no automatic statutory moratorium preventing creditors from taking action. The optional moratorium introduced by the 2000 Act only applies to small companies and even then is very much dependent on obtaining the consent of secured creditors to the moratorium for the moratorium to work in practice.

- CVAs are not binding on secured or preferential creditors.

- CVAs have proved difficult to implement and are rarely used in practice. Only a small percentage of corporate insolvencies involve voluntary arrangements because of the difficulties associated with them.