

## **LEGAL ALERT**

### **CVAs - are they an escape for tenants from unwanted leases?**

The recent spate of Company Voluntary Arrangements (CVAs) is concerning many landlords and rightly so given their potential impact on future rental income and investment value. It appears that a CVA is becoming recognised by retail tenants as a potentially convenient way to escape (or at least reduce) costs in respect of unwanted premises.

It has been recognised at least since the judgment in *Re Cancol Ltd* [1996] that a tenant in financial difficulties can seek to mitigate the costs of unwanted leases by providing that future rent should fall within the scope of a CVA, and therefore be payable at a reduced rate in accordance with the terms agreed by a 75% majority of creditors by value. If a landlord was unhappy with that he was obliged to exercise his right to forfeit the lease and relet (if he could) to a new, and hopefully financially stronger, tenant.

The usual battle grounds have become: (1) the value for voting purposes placed upon the landlord's claim and, in particular, whether it should include loss of future rent and, if so, how much. Clearly the higher the value placed upon the landlord's claim the stronger his prospect of defeating the proposals by voting against them and; (2) whether the arrangement is unfairly prejudicial to the landlord (for instance because it treats other similar creditors more favourably).

The electrical retailer PowerHouse went into a CVA in March 2006. Although there is limited information available in the public domain regarding the proposals in the CVA, it seems that the arrangement has resulted in the closure of 31 loss-making stores, with continued trading at the remaining profitable stores. Under the agreement it appears that landlords were offered 6 months rent on the affected stores equating to approximately 28p in every pound owed to them and it is also likely that the amount of future rent due to certain landlords has been reduced by the CVA. The terms of the CVA also apparently seek to limit the landlords' rights to sue for arrears of rent and other breaches of covenant and, most significantly, to pursue guarantors (including PowerHouse's parent company, Pacific Retail Group).

The position of PowerHouse's landlords has been complicated by recent changes in insolvency law which make it unclear whether or not a landlord can forfeit a lease once a CVA has been approved, although it is argued on behalf of landlords that a CVA cannot affect a landlord's right to re-enter, as it is incident to the estate granted and is not merely a remedy against a tenant. Certainly it would seem anomalous to bind a landlord to accept a lower rent against his will and to prevent him from forfeiting a lease.

Worryingly for landlords, two further retail tenants, QS and BeWise, have now secured permission to use a CVA, which could allow them to leave 133 of their loss-making properties whilst continuing to trade from their remaining properties. It is also feared that Silverscreen, a DVD retailer, may also use a CVA to avoid some of its rental liabilities, after it appointed an administrator in early April.

The PowerHouse landlords are seeking to challenge the CVA on the grounds that their claims have been wrongly valued and/or on the basis that the proposals unfairly prejudice them. In the light of the current lack of clarity about the full affect of CVAs on landlords the outcome of the claims is eagerly awaited, in the hope that it will provide much needed guidance in this area.

**For further information please contact our property litigation partner David Stevens on 020 7421 6453**