



## R3 STANDARD FORM COVID 19 CVA PROPOSAL

### EXPLANATORY NOTE FOR MEDIA

#### 1. R3

1.1. R3 is the association for the UK's insolvency, restructuring, advisory, and turnaround professionals. We represent licensed insolvency practitioners, lawyers, turnaround and restructuring experts, students, and others in the profession. Our members work across the spectrum of the profession, from global legal and accountancy firms through to smaller, local practices. Our members have direct experience of insolvencies and their impact on individuals and businesses across the UK.

#### 2. Introduction

2.1. Company Voluntary Arrangements ("**CVAs**") are a rescue process contained in the Insolvency Act 1986. They are the only consensual restructuring process contained in the Insolvency Act. As a basic summary, CVAs enable debtor companies to propose a way forward with their unsecured creditors, and if 75% or more by value of those creditors agree, the solution can bind a dissenting 25%. As an additional protection, the CVA is not approved if more than half of the company's unconnected creditors vote against it. (The terms of a proposal cannot bind a secured creditor unless it expressly agrees, and there are also protections for preferential creditors.) Usually the terms of a CVA allow the debtor company to pay a smaller sum in full and final satisfaction of its debts (a 'debt composition'), but their terms can be virtually anything. An unhappy creditor can challenge the terms of a CVA on the basis it is unfairly prejudicial or that there was a material irregularity in the proposal or approval decision procedure. Despite having been an option for over 30 years, CVAs are rare (see table below). They are usually bespoke documents and can be prohibitively costly. Recently, CVAs have come more into the public awareness due to their use by large (and well-known) retail companies.

*Source: The Insolvency Service*

Year	Total corporate insolvencies (England & Wales)	CVAs	CVAs as a % corporate insolvencies (E&W)
2010	19,603	757	3.9%
2011	20,381	758	3.7%
2012	19,485	829	4.3%
2013	17,708	569	3.2%
2014	16,292	559	3.4%
2015	14,587	372	2.6%
2016	16,420	345	2.1%
2017	17,316	307	1.8%
2018	17,454	355	2.0%
2019	17,225	351	2.0%

2.2. Research carried out on behalf of R3 and ICAEW in 2018 recommended the introduction of a standard form CVA for use by distressed SME companies.<sup>1</sup> The Covid 19 pandemic has made that need more urgent. The R3 Standard Form Covid 19 CVA Proposal ("**Standard Form**") and accompanying Covid 19 Standard Conditions for Company Voluntary Arrangements ("**Standard Conditions**") have been

<sup>1</sup> Professor Peter Walton, Chris Umfreville and Lézelle Jacobs *Company Voluntary Arrangements: Evaluating Success and Failure* (2018) (a research report commissioned by R3 and sponsored by ICAEW) at page 4 and section 9.8.



drafted by Stewart Perry and Professor Peter Walton, both members of R3's General Technical Committee together with the assistance and constructive criticism of other R3 members. Both documents are a free resource. R3 hopes these documents can be used by companies and their advisors, and form one of a number of tools available to the insolvency profession to help SME companies whose businesses have been affected by Covid 19.

- 2.3. Where its use is appropriate, the Standard Form is intended to save time and costs, and therefore make CVAs more accessible to the SME market. It is intended to encourage a responsible approach to the payment of corporate debts.

### **3. The potential users of the Standard Form**

- 3.1. It is impossible to create a template CVA to tackle all variation that may be necessary in a CVA. It is designed for use by companies whose businesses have been hit by the Covid 19 pandemic and which need some time to get their businesses fully operational. The terms provide for a (delayed) payment of 100% of the company's debts. It therefore creates a moratorium period when pre-CVA debts will not be paid and those creditors with pre-CVA debts are consequently prevented from enforcing their debts against the company whilst the CVA is in operation. Trading costs incurred during the CVA are to be paid out of new trading income. Continuation of the business will permit regular contributions to be made to the supervisor out of operational cash flow.
- 3.2. It is intended that the Standard Form will be amended to become fit for purpose for the various different companies that may employ it. Therefore, depending upon individual circumstances, a company may find it necessary to amend the proposal to allow for a debt composition, either immediately or as the CVA progresses and the company is more able to assess the impact of trading in the "new normal".
- 3.3. The Standard Form can also be used in conjunction with the new moratorium for businesses as introduced by the Corporate Insolvency and Governance Act 2020. The benefits of a moratorium are usually seen to be to enable a company sufficient time to put together a feasible rescue plan such as a CVA.<sup>2</sup> If the Standard Form is adopted, there may be no need to file first for a moratorium.

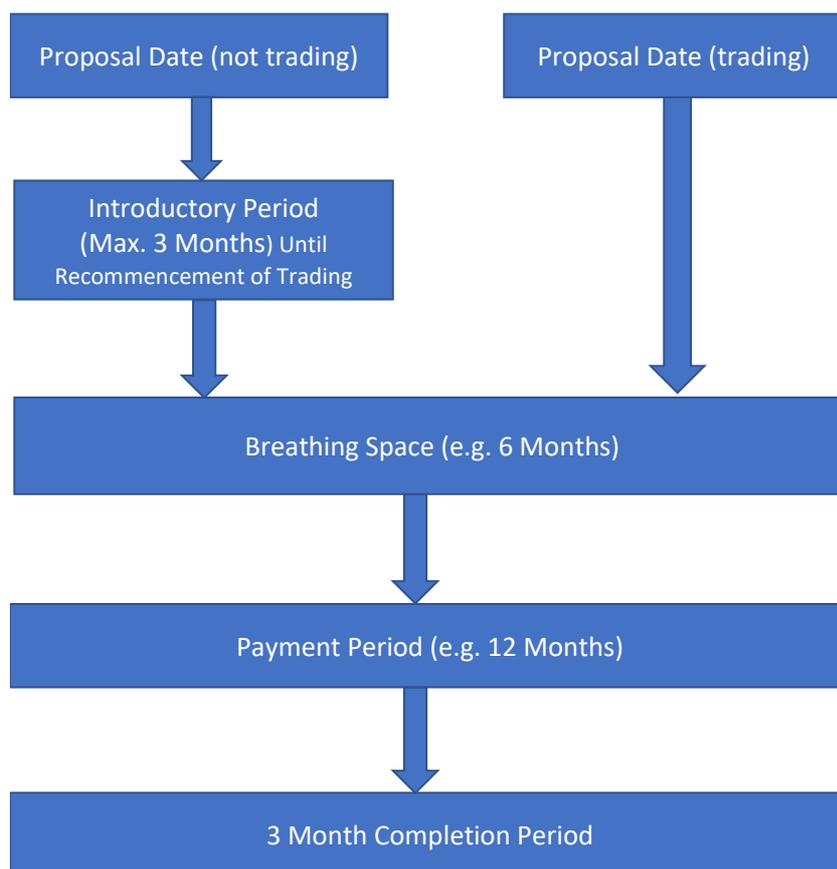
### **4. Timeline for a Standard Form Covid 19 CVA**

- 4.1. The flow chart below shows in outline the timeline for the Standard Form CVA (in unamended form).
- 4.2. The Standard Form recognises the inherent flexibility of a CVA with its inclusion of clauses on its first page with blanks which require completion. Not all of the clauses will be appropriate in each case. It recognises that businesses may or may not yet be operational following an interruption due to Covid 19. If the CVA proposal is made before the company's business has re-started, the Standard Form provides for an Introductory Period of up to 3 months during which the business remains inactive.
- 4.3. If no Introductory Period is required, or it has elapsed, the Standard Form contains a Breathing Space Period which provides a payment break in relation to debts owed prior to the approval of the CVA. The length of the Breathing Space Period is set by completing the blank on the first page. New debts incurred in the ordinary course of business during the CVA will be paid during the Breathing Space Period but CVA debts, those owed prior to the commencement of the CVA, will not be payable during the Breathing Space Period. The Breathing Space Period may last, for example, for 6 months during which time the company's business is intended to return to normal profitable day-to-day trading (and to the extent necessary to rebuild a working capital buffer).

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<sup>2</sup> Professor Peter Walton, Chris Umfreville and Lézelle Jacobs *Company Voluntary Arrangements: Evaluating Success and Failure* (2018) (a research report commissioned by R3 and sponsored by ICAEW) at Section 4.1.2.

- 4.4. Once the Breathing Space Period has elapsed, the company will begin to pay back its debts in the Payment Period. The Standard Form assumes that the company will be in a position to repay 100% of its debt but this may require amendment in a particular case. Such amendment may be needed either prior to commencement of the CVA or as a variation part way through the CVA. The Standard Form suggests an indicative Payment Period of 12 months but a longer or shorter period may be more appropriate on the facts of a particular case. Monthly payments will be made by the company to the Supervisor (a regulated insolvency practitioner overseeing the debtor company's compliance with the CVA) to distribute amongst the creditors according to their respective entitlements.
- 4.5. Once the Introductory Period, Breathing Space Period and Payment Period have elapsed, there will be a final Completion Period of three months to enable any final formalities and payments to be completed.
- 4.6. Research has shown that CVAs with proposed long durations, for example, up to 5 years, do not tend to lead to an optimum outcome and so the Standard Form envisages a total period for the CVA of between 18 months and 24 months using these indicative time periods.<sup>3</sup>



<sup>3</sup> Professor Peter Walton, Chris Umfreville and Lézelle Jacobs *Company Voluntary Arrangements: Evaluating Success and Failure* (2018) (a research report commissioned by R3 and sponsored by ICAEW) at page 4 and section 9.3 and 9.6.



## 5. Restrictions on companies (and powers of the Supervisor) during the CVA

- 5.1. During the CVA period, a number of restrictions apply to the company's operations. The (unamended) Standard Form provides that the company may not declare any dividends or increase directors' salaries. Borrowing or sales of the company's business or its assets (save in the ordinary course of business) may not be completed without the consent of the Supervisor or creditors. If the company's business is sold, the proceeds will be paid first to secured creditors, then to pay debts incurred during the CVA and finally to pay debts covered by the CVA.
- 5.2. The unamended terms also allow the Supervisor to extend the CVA period for up to 6 months and state that it will be a breach of the CVA if the company fails to meet its post-CVA trading liabilities or breaches the restrictions imposed under the CVA. Upon breach, the Supervisor may take steps to terminate the CVA and petition to wind up the company.

## 6. Standard Conditions

- 6.1. The Standard Form is supported by the Standard Conditions. These are based to a large extent upon the popular and well-used R3 Standard Conditions for Individual Voluntary Arrangements (used by consumers) with amendments appropriate for companies. They are incorporated into the Standard Form by inclusion in Appendix 1. Any agreed amendments to the Standard Conditions will appear in Appendix 2 to make it easier for creditors with multiple debtors to compare their proposals.

## 7. R3 Disclaimer

- 7.1. Led by Stewart Perry<sup>4</sup> and Professor Peter Walton<sup>5</sup>, the Standard Form and Standard Conditions have been produced by R3, with the assistance of its members and its [General Technical Committee](#) ('GTC'). R3, the Association of Business Recovery Professionals, is the leading professional association representing insolvency practitioners and professionals within the insolvency, restructuring and turnaround profession in the UK.
- 7.2. GTC deals with issues of general importance and significance to the profession, keeping under review all UK and EU legislation, prospective legislation and other matters relating to insolvency law and practice.
- 7.3. The Standard Form and Standard Conditions are not intended to be statements of law, will not be appropriate for any case until suitably modified, and are not a substitute for professional or legal advice. R3 and its contributing editors believe that both documents are accurate but accept no liability for any fault, error, negligence or omission howsoever caused, or for any loss or damage of any kind resulting from reliance on their contents.

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