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Controversy over Company Voluntary Arrangement under the UK Insolvency Law, 1986 – A great winning goal, or a dubious dive in the penalty box?

In this article, the author looks into controversy over the Company Voluntary Arrangement under the UK Insolvency Law, 1986. He wonders whether arrangement is a great winning goal or it is a dubious dive into the penalty box.

Introduction

The Company Voluntary Arrangement (CVA) was first introduced into UK Insolvency Law in 1986, but relatively little used at first. Its counterpart for individuals, the Individual Voluntary Arrangement (IVA), has taken off in a big way, in terms of number of cases, and has become the most popular of formal insolvency processes in the country, period. But for most companies, the usual statutory processes are liquidation or administration, the latter largely replacing receivership as the process of choice when a company is looking at rescue options with court protection.

An administration invariably involves a sale of the viable parts of a company's business, sometimes through a pre-packaged disposal of assets (Pre-Pack), and is a process in which the directors lose control, as the administrator takes over and conducts a sale, and then accounts to creditors in accordance with approved proposals. Leaving aside the potential for directors to purchase those assets (through a Phoenix), a rescue of the *company* as such is rare.

Debtor in possession

The CVA is an American-style debtor-in-possession procedure, where the directors remain in charge of the day-to-day running of the business, and the Insolvency Practitioner supervises the arrangement and reports to creditors. The directors avoid some of the other potential pitfalls of more formal insolvencies, such as a liquidator's wide investigative powers and possible director disqualification. So there are good reasons for directors to consider a CVA if there is viable business at the company's core, but still they were not common until Richard Fleming, an IP and now European Head of Restructuring at Alvarez and Marsal, pioneered the 'retail CVA'. Richard's leading role in cases such as JJB Sports saw enterprises rescued with the support of their creditors, though some may question whether the CVAs were ultimately successful. More than half of those commenced five years ago were terminated without achieving their

objectives, though they may still have returned more money to creditors than would have been the case in administration according to research commissioned by R3. They paved the way however for increasing use of a process that has helped create a platform for recovery for retail traders, whose positions were otherwise precarious and likely to end in administration or liquidation.

The CVA is an insolvency process, so there is a starting assumption that the company is unable, or is likely to be unable, to pay its debts in full. One of the big advantages with a CVA is that creditors have a vote at the outset, and without the support of 75 percent the CVA cannot go ahead. The 75 percent voting majority is of all unsecured creditors, but calculated by reference to the value of the debts of those voting – so not necessarily three quarters of all creditors. The up-front vote provides an interesting contrast with the pre-pack administration, where creditors usually find out about a sale after the event.

Controversial CVAs

So what is the recent fuss about? The creditors making the most noise about the spate of retail CVAs, which this year include Carpet right, Jamie's Italian and House of Fraser, are the landlords. Some believe the CVA process is being abused for competitive purposes to permit companies to wriggle out of their rent liabilities – arguably to the disadvantage of profitable rivals. One retailer, Next, has suggested it might look for a CVA clause in its new leases to match competitors' rent cuts, and the landlords' concerns have been drawn to the attention of the government's Housing, Communities and Local Government select committee; its chair has confirmed that it will look into the matter, not least because of concern about the millions of square feet of vacated retail units this year.

The concerns were neatly summed up by one landlord's representative who likened some retailers' moves as a 'dive in the penalty box', implying that companies have cheated to gain an advantage through a process that has been described in the national press as a device that 'allows retailers to shut stores and cut rents'. Others go further and claim use of the CVA in this way is 'contrary to the legislation's intentions and the wider interests of society' – strong stuff!

Mathew Ditchburn is Vice Chair of the British Property Federation's (BPF) Insolvency Committee and the BPF's Lay Representative (and Chair) of the Joint Insolvency Committee, which sets standards for IPs. Mathew's take on this is that in some cases landlords are concerned CVAs are 'engineered to prevent them voting down the arrangements' by the way their claims are calculated, which might lead to legal challenges on grounds of material irregularity in the way voting is conducted. The BPF is calling on government to conduct an urgent review and would welcome a change to the practice guidance issued to IPs to raise minimum standards of practice in this area, and in particular around transparency and the provision of information at the pre-voting stage.

Inevitable correction

The alternative view might be that the retail sector is going through some inevitable and natural process of correction or adjustment in its business models as a consequence ofchanges in consumers' buying methods – more on-line purchases and less footfall in retail stores. IPs would argue that retail and other companies facing insolvency need to consider all options, and that for some a CVA is a sensible alternative to administration or liquidation.

It can also be beneficial to creditors, as evidenced by creditor support; 98percent supported the New Look arrangement, notwithstanding rent cuts of around 50percent on some units –thoughit should be noted that the adversely-affected landlord creditors may not have had sufficient voting power to affect the outcome.

Fleming is a keen advocate of the 'retail CVA' and supports its use in genuine insolvency situations. With some retailers in crises, he sees the present market correction as part of an accelerated model change for those belatedly recognising that the nature of their businesses has changed forever. That change has come about subsequent to many of the current leases being entered into and might

not reasonably have been for seen when those commitments were made, though he questions whether landlords have been sufficiently flexible in acknowledging the changing circumstances affected their tenants. He also points out, and the BPF accepts, that in some cases the supporting creditors have included the landlords, so (despite the noise and theoretical concerns) it seems many have been persuaded of the merits of the cases proposed to them. Fleming argues that the lifeline the CVA can provide, and the benefits of preserving businesses which can be revived with some restructuring, are plus factors which outweigh the downside for some landlords.

In his role helping company directors and distressed businesses he makes a strong case for the CVA as part of the IP's toolkit, and in response to the current controversy makes the general point that 'landlords are kept whole right until the bell is rung whereas all other stakeholders have taken pain prior to the CVA'. The commercial realities seem to lead many landlords, even those affected by rent cuts or surrenders, to vote in support of CVAs.

Regulatory safeguards

Formal insolvency processes including CVAs are subject to regulation. The courts can intervene, but there are protections through the regulation mechanisms too. IPs have to be licensed and monitored, so any abuse of process should be weeded out. The whole regime is overseen by the department for business, energy and industrial strategy, so there are government levers that can be pulled if necessary. Perhaps some changes will be made as part of the Government's insolvency and corporate governance agenda, as R3 has called for.

There do not appear to have been any specific suggestions of abuse of process. Some see the landlords' grumblings as a natural consequence of the hit they are taking on expensive leases, where perhaps there has been a lack of flexibility on terms in the past. While landlords and their representatives may push for better deals in future CVAs, there will doubtless be some compromise and an agreement reached when the alternatives become clear.

Nobody wants empty retail units and tenants in liquidation if there are viable ways to keep those businesess going, and the CVA it seems is here to stay to play its part in bringing that about. A winning goal is one that preserves ailing businesses through a process that encourages creditor engagement like no other, as the CVA does, and proposes fair compromises given the insolvency situation facing a corporate. These arrangements cannot proceed without creditor support, and as long as that is present it will be difficult to argue against them.

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IBC and Role of the Competition Commission

In certain matters where insolvency proceedings have commenced, the parties may have to take prior approval from the Competition Commission of India (Commission) established under the Competition Act, 2002. Only after getting such approval, the proposed acquisition of shares or management or control of the failing firm can take place. This article deals with the role of the Commission in light of the five orders that have been passed till now.

Introduction

The Competition Act, 2002 ('the Act') requires every combination exceeding the financial thresholds provided undersection 5 of the Act to be mandatorily approved by the Competition Commission of India (CCI / Commission). According to section 5, combination includes the acquisition of one or more enterprises by one or more persons or merger or amalgamation of enterprises. Section 5 also provides the modes of forming a combination which include acquisition of shares, assets, voting rights, control or mergers or amalgamation. Section 6 of the Act prohibits every combination which causes or is likely to cause an appreciable adverse effect on competition within relevant market in India and expressly declares such combination to be void. The Competition Commission of India (Procedure in regard to the Transaction of Business relating to Combinations) Regulations, 2011 ('Combination Regulations') regulate the procedure for taking approval from the Commission. Enterprises proposing to enter into a combination, are required to give a notice of such combination to the Commission by filing Form I or Form II, as the case may be.

Competition Assessment

On receipt of the notice in Form I or Form II, the Commission would inquire whether a combination referred to in the notice has caused or is likely to cause an appreciable adverse effect on competition in India.Section 20(4) provides that for the purposes of competition assessment, the Commission shall have due regard to all or any of the following factors:

- actual and potential level of competition through imports in the market
- extent of barriers to entry into the market
- level of combination in the market
- degree of countervailing power in the market
- likelihood that the combination would result in the parties to the

combination being able to significantly and sustainably increase prices or profit margin

- extent of effective competition likely to sustain in a market
- extent to which substitutes are available or arc likely to be available in the market
- market share, in the relevant market, of the persons or enterprise in a combination, individually and as a combination
- likelihood that the combination would result in the removal of a vigorous and effective competitor or competitors in the market
- nature and extent of vertical integration in the market
- possibility of a failing business
- nature and extent of innovation
- relative advantage, by way of the contribution to the economic development, by any combination having or likely to have appreciable adverse effect on competition
- whether the benefits of the combination outweigh the adverse impact of the combination, if any.

Failing business defense

Clause *(k)* of section 20(4) of the Act states that possibility of a failing business can be a ground for approving a proposed combination. If required, the Commission can apply this parameter also for assessing a proposed combination which is a part of insolvency proceedings. 'Recommended Practices for Merger Analysis' issued by the International Competition Network explicitly recommends such approach in the following words:

> "In assessing claims that a merger will not harm competition because one of the merging parties is failing, agencies should determine whether (a) the firm is unable to meet its financial obligations in the imminent future; (b) there would be no serious prospect of reorganizing the business; (c) there would be no credible less anticompetitive alternative outcome than the merger in question; and, (d) the firm and its assets would exit the market in the imminent future absent the merger."

Insolvency and Bankruptcy Code

A proposed combination dealing with an enterprise undergoing insolvency resolution proceedings initiated under the Insolvency and Bankruptcy Code, 2017 (IBC) also needs to be approved by the Commission if the monetary thresholds provided under the Competition Act are likely to be exceeded. The Commission would make the competition assessment of the proposed combination and would give its go ahead if the same is not likely to have appreciable adverse effect on competition within India. The Commission has already passed orders in five cases as detailed in Table A.

From the decided matters

Table A

Orders by CCI dealing with proposed combinations related to IBC

Combination Registration No.	Target	Enterprise giving the notice	Date of Order
C-2018/02/557	Binani Cement Limited	Rajputana Properties Pvt. Ltd.	07.03.2018
C-2018/02/558	Binani Cement Limited	UltraTech Cement Limited	27.03.2018
C-2018/03/562	Bhushan Steel Limited	Tata Steel Limited	25.04.2018
C-2018/03/561	Monnet Ispat and Energy Limited	Jointly by AION Investments Private II Limited and JSW Steel Limited	11.05.2018
C-2018/04/563	Electrosteel Steels Ltd.	Vedanta Limited	11.05.2018

As displayed by Table A, the Commission has passed orders under five matters, following interesting issues have emerged from the competition law perspective:

Order by the Commission: No AAEC and not the approval

Approval: In the normal course, if the Commission is of the opinion that the proposed combination is not likely to have any appreciable adverse effect on

competition in India, the Commission grants its approval to the same under sub-section (1) of section 31 of the Act.

AAEC: In case the proposed combination is subject matter of the proceedings initiated under the Insolvency and Bankruptcy Code, the Commission does not approve the combination under section 31(1). All that the Commission decides is that the proposed combination is not likely to have an appreciable adverse effect on competition inIndia.

Intimation of change

Rejected: Regulation 16 of the Combination Regulations requires the parties to give notice of any change in the information already provided to the Commission. Accordingly, in Combination Registration No. C-2018/02/558, the acquirer *i.e.,*UltraTech submitted that it has in-principle arrived at a commercial understanding with Binani Industries Ltd.(BIL) to purchase 98.43 per cent of the equity share capital of Binani Cement, subject to termination of the IBC proceedings (Alternate Proposed Transaction). UltraTech intimated the Commission that the alternate proposed transaction has amended the notice with respect to the mode in which the Proposed Combination would be undertaken if the IBC Proceedings stand terminated; and the consequential change in consideration payable by UltraTech to BIL. The Commission, however, did not accept the intimation of the change. The Commission observed that there is no definiteness vis-à-vis the alternate proposed transaction and, therefore, the submissions of the acquirer could not be accepted as intimation of change under Regulation 16 of the Combination Regulations.

Same target, different proposer

There is a possibility that more than one competing enterprise may approach the Commission for the same target and the Commission may have to pass order for competing enterprises though ultimately acquisition would be effected by only one acquirer to be finally decided according to the provisions under the IBC. Table B gives the details of one such target where two enterprises approached the Commission.

Target	**Binani Cement Ltd.**	
Combination Registration No.	C-2018/02/557	C-2018/02/558
Enterprise giving the notice	Rajputana Properties Pvt. Ltd.	UltraTech Cement Ltd.
Proposed transaction	Rajputana Properties Pvt. Ltd. to acquire 80 percent of the equity shares of Binani Cement Limited and 20% is proposed to be acquired by IDBI Bank Ltd. Following shall be carried out before the Proposed Combination: (i) the shareholding in the Acquirer is proposed to be divided among Dalmia, India Resurgence Fund and PiramalGlass Private Limited; (ii) Entity, managing the Fund, shall become a joint venture between Piramal Enterprise Limited and group entity of Bain Capital Credit, LP.	20 percent of the equity share capital of Binani Cement may be issued and allotted to certain unsecured financial creditors of Binani Cement and resultantly, UltraTech will hold 80 per cent of the equity share capital of Binani Cement.

Conclusion

The Commission commenced its powers to regulate the combinations since June 1, 2011. After seven years of the said operations, it is required to pass appropriate order by approving the different kind of combinations. Here its role is mainly to determine that the proposed combination is not likely to have appreciable adverse effect on the competition in India. The successful acquirer is to be determined according to the provisions under the Insolvency and Bankruptcy Code, 2016 only.

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