

Agenda Item 13

	REPORT TO AUDIT COMMITTEE TO BE HELD ON 23 FEBRUARY 2021
	Corporate Aims ALL

REPORT OF: DIRECTOR (RB) – 21/011

WARDS AFFECTED: All

SUBJECT: TRAVELDGE CVA UPDATE

RECOMMENDATION:

The committee is asked to take note of the following update.

- (i) By way of an Urgent Leader Report in June 2020 the Leader, on behalf of the Council, accepted that a Company Voluntary Arrangement (CVA) be approved for Travelodge Hotels Ltd in accordance with section 4 of the Insolvency Act 1986. This acceptance meant a variation of the rental terms of the existing occupational lease (for the property known as Travelodge Hotel, St Nicholas Cliff, Scarborough) to Travelodge Hotels Limited.

REASONS:

The ongoing global COVID-19 Pandemic has had a rapid and unprecedented impact on the UK hospitality industry. In order to secure affordability and provide some stability a CVA was agreed to temporarily reduce Travelodge's obligations by amending the terms of all of its contractual leases. This includes the Council owned hotel in St Nicholas Cliff, Scarborough.

HIGHLIGHTED RISKS:

It should be noted that the CVA agreed was in response to the first national lockdown over the spring of 2020. In terms of any further proposed variations to terms or new CVA that will depend on further continued COVID-19 restrictions and Travelodge's profitability going forward. Further independent legal and property advice will be sought should this become an issue.

1. INTRODUCTION

- 1.1 On 14 May 2018 Council approved (i) the adoption of the Commercial Property Investment Strategy ('the Strategy') and (ii) a capital fund of £30

million funded from Public Works Loan Board borrowing, plus a revenue budget of £100,000 funded from the Council's Investment Fund, to facilitate the purchase of properties and to pursue development opportunities meeting the criteria set out in the Strategy

- 1.2 On 17 April 2018 Cabinet approved the delegation of authority to the Commercial Director, following consultation with the Property Investment Governance Board ('PIGB'), to approve expenditure and to acquire and dispose of such legal estates and interests in land and to make such property investments as are within the overall limits and criteria of the Strategy, subject to the preparation of a Business Case and Risk Assessment in line with the Strategy
- 1.3 Following consultation with the PIGB the Commercial Director approved the purchase of the Travelodge hotel on 17th September 2018. The freehold purchase of the hotel was subsequently completed on the 10 October 2018.
- 1.4 In complying with the COVID-19 restrictions Travelodge was required to close almost all of its hotels from the 24 March 2020 causing significant disruption to its operations and financial performance.

2. CORPORATE AIMS

- 2.1 **Better Council:** The approval will help protect future income to allow the Council to continue to be an efficient and effective Council which is financially sustainable for the future.

3. BACKGROUND AND ISSUES

- 3.1 Following the purchase of the hotel in October 2018 the Council now own the freehold interest subject to an existing lease to Travelodge Hotels Limited who are the occupational tenant.
- 3.2 The existing Lease has an unexpired residue of circa. 23 years and a landlord's option to extend for a further 5 years at the end of the present term.
- 3.3 This property was purchased following Council's approval of the Commercial Property Investment Strategy and was funded from the £30m fund that had been made available.
- 3.4 At the time of purchase the tenant was regarded as having an excellent covenant strength with a very low risk of not being able to pay rent over the lease term. However the COVID-19 pandemic has had a considerable impact upon all commercial businesses even those who were previously considered financially robust. Actions were therefore taken to protect the council's financial position as best as possible and independent specialist legal and property advice was obtained.

- 3.5 Following early negotiations with Travelodge in the summer to try and agree to a suitable deferment of rent we were subsequently informed that Travelodge were not engaging in individual negotiations and were working on a final 'take it or leave it' offer with all Landlords. Travelodge then very quickly moved to a CVA and the Council had to move swiftly to take advice and make a decision in order to decide whether to vote to accept the CVA or not, hence why an Urgent Leaders report was deemed appropriate at the time.

4. CONSULTATION

- 4.1 No further consultation has been had at this time the purpose of this report is to update the committee on actions already taken.

5. ASSESSMENT

- 5.1 External advisors recommended that the Council vote to accept the CVA on the varied lease terms, proposed by Travelodge.

- 5.2 The main details of the varied terms are as follows;

- A monthly payment cycle (rather than quarterly) for rent until the 31 December 2021 to assist cash flow for Travelodge.
- Rent reductions of 75% for nine months and 30% for the following year as outlined below.
- An extension to the lease term of 36 months which will mean we get a more certain return for longer and therefore add value to the investment. *The Council already have the right under the current lease for an extension at the end of the lease (5 years). With this additional extension the revised expiry of the lease is now 2051.* It should be noted that there was an alternative option to the lease extension of breaking and ending the lease within 5 months from the date the CVA came into effect. However after once again taking professional advice this alternative option was not taken. This was due to the substantial value left in the remaining long lease and the substantial risk of breaking the lease and trying to secure a new operator on the same or better terms, in very uncertain economic times. It should be noted that the vast majority of Landlords took this stance.
- A share on any earnings of 50% above £200m in the next 3 years.

- 5.3 Despite the reductions in rent over 2020/2021 the ongoing lease still benefits from;

- No proposed effect on lease terms beyond 2021 with rents returning to previous contractually agreed amounts.
- A long unexpired lease term with substantial value.
- Upwards only rent reviews (to protect the landlord's income stream and the investment value of the lease); and

- Full repairing and insuring lease terms, meaning that all the repairing liabilities are borne by the tenant.

6. IMPLICATIONS

6.1 Policy

There are no direct policy implications arising from this report.

6.2 Legal

The varied lease terms were documented by the Council's Legal team.

A CVA is an arrangement that allows a company to come to an arrangement with its creditors. It is an alternative to other insolvency regimes such as administration or liquidation. The perceived benefit of a CVA is that it allows the company to continue to operate under an arrangement that is agreed with the company's creditors. The CVA sets out that Travelodge considers that, as a whole, creditors will receive a greater return on the amount owed to them than if Travelodge were to enter administration or liquidation.

The CVA was proposed and creditors had the opportunity to vote on it. In order for the CVA to be approved it required a vote in favour by at least 75% (by value) of the creditors who vote on it. The actual percentage agreed was 90.1% with the majority of Landlords agreeing with the CVA.

It should be noted that even if the Council had not voted in favour of the CVA, due to the majority of Landlords voting to accept, the Council would still have had to accept the majority decision and would have still been carried forward on the CVA's terms.

If the majority of landlords had voted against the CVA Travelodge could have fallen into receivership and the Council may have lost the current lease, income stream and substantial value.

6.3 Financial

As a result of the CVA the Council will have to fund a reduction in rent of £762k up to the end of 2021. Whilst this reduction is unwelcome news, the net return to the Council from the date of purchase (October 2018) until December 2021 will still be £349k and this has helped support the provision of priority services.

6.4 Planning

No implications at this time.

6.5 Equalities and Diversity

No implications