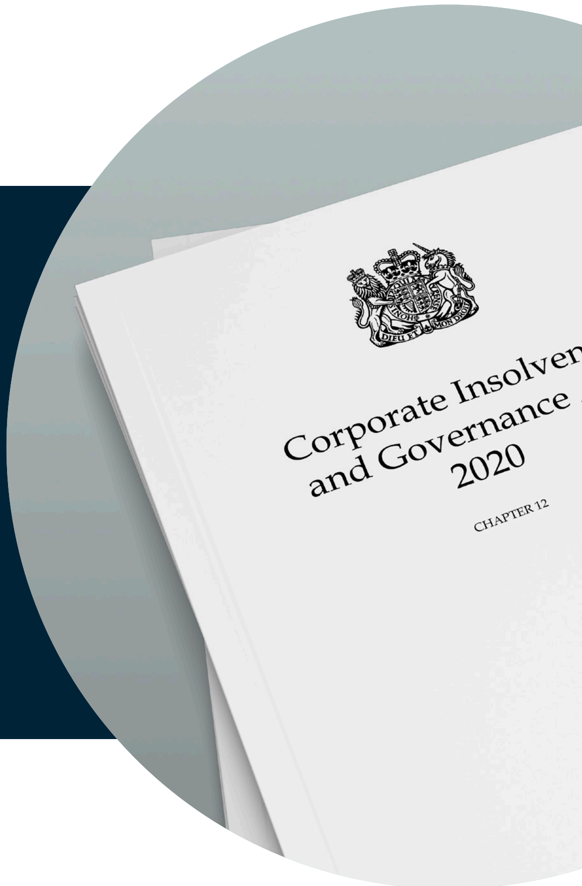
3 VERULAM BUILDINGS
BARRISTERS

On 25 June 2020 the Corporate Insolvency and Governance Act 2020 (“**CIGA**”) formally received Royal Assent and passed into law heralding the most significant changes in UK insolvency legislation since the 1986 reforms spearheaded by the Insolvency Act 1986 (“**IA 1986**”).



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Introduction and Overview

Jamie Riley QC and Philip Hinks

The Bill which ultimately became CIGA[1] was introduced to the House of Commons on 20 May 2020 and has cantered at pace over the legislative course in accordance with the fast-track procedure. This expedition of the Bill's progress through Parliament was in response to the economic crisis triggered by the COVID-19 pandemic and the sudden financial threat to many UK companies. According to the Explanatory Notes which accompany the Bill, the overarching objective of the new legislation is *"to provide businesses with the flexibility and breathing space they need to continue trading during this difficult time. The measures are designed to help UK companies and other similar entities by easing the burden on businesses and helping them avoid insolvency during this period of economic uncertainty"*.

In order to achieve this general goal, CIGA implements change in three main areas:

- The introduction of greater flexibility in the insolvency and restructuring regime to allow financially distressed companies to explore their options for their rescue and survival.
- The temporary suspension of rules in certain areas of insolvency law to support directors in continuing to trade through the period of the pandemic free of the threat of personal liability.
- The temporary lifting of requirements relating to company filings and meetings, including annual general meetings.

Specifically, CIGA has brought in five main insolvency reforms, namely:

(1) The introduction of a new form of moratorium;

(2) A new restructuring plan;

(3) Restrictions on the operation of termination clauses in contracts for the supply of goods and services;

(4) Restrictions in the use of winding-up petitions; and

(5) The suspension of liability for wrongful trading. The first three of these reforms are permanent; the latter two are temporary and have been introduced in response to the needs of business for support during the currency of the coronavirus crisis.

Although the economic shock and uncertainty caused by COVID-19 undoubtedly have hastened these legislative changes, the permanent reforms that have now been made were under consideration by HM Government for a number of years. In May 2016, the Department for Business, Energy and Industry Strategy ("**BEIS**") launched a "Review of the Corporate Insolvency Framework: a consultation on options for reform". It consulted on a package of insolvency reforms intended to assist businesses to continue to trade through a restructuring process. Subsequently, in March 2018, following the high profile collapse of BHS Ltd and Carillion plc, BEIS published its consultation document "Insolvency and Corporate Governance" in which it sought views on proposals to reduce the risk of corporate failures resulting from inadequacies of leadership. On 26 August 2018, the Government published its "Response to the Insolvency and Corporate Governance Consultation".[2] In respect of the broader aspects of insolvency law identified in the 2016 and 2018 consultations, the Response proposed specific reforms to include:

- The introduction of a new moratorium to shield financially distressed but viable companies from creditor action while preparing to restructure or seeking new investment.
- The creation of a new flexible restructuring plan procedure including the ability to bind dissenting classes of creditors who vote against it (so-called 'cross-class cram-down' provisions).
- The prohibition of enforcement by suppliers of insolvency event termination clauses (so-called 'ipso facto clauses') to enable companies to continue trading while they formulate a rescue plan.
- Action to improve the insolvency framework in cases of major failure.

These reforms were aimed at reinvigorating the UK's rescue culture by changing and expanding the restructuring options and helping businesses to continue trading through the restructuring while striking a fair balance between the interests of the company seeking rescue and the rights of creditors.

Until the outbreak of the COVID-19 pandemic, it had been anticipated that the insolvency reforms proposed in the Government's Response would be introduced after the completion of the Brexit negotiations. However, on 28 March 2020, the Business Secretary, Alok Sharma, announced that the Government would be making changes, including the reforms proposed in the 2018 Response, much earlier to assist companies hit by the coronavirus crisis.

1 Corporate Insolvency and Governance Bill (HC Bill 128)

2 Department for Business, Energy & Industrial Strategy "Insolvency and Corporate Governance – Government response", 26 August 2018

This guide

This guide identifies and provides commentary on the key reforms introduced by CIGA. Each of the key areas are addressed in separate, dedicated sections which follow. As the commentary in the sections highlights, some of the reforms introduce measures and concepts which are not clearly defined or which are likely to be contentious giving rise to disputes between companies and their creditors. As a result, it remains to be seen how the courts will interpret the new provisions and develop the concepts and principles which they introduce. Therefore, this guide necessarily provides an introductory assessment of the reforms only. It is intended that further commentary and updates will be provided by members of 3 Verulam Buildings as the reforms bed in and fall under the spotlight before the courts.

Overview of the reforms

By way of introduction, the key reforms of CIGA (which are the subject of more detailed commentary in the relevant sections of this guide) are summarised as follows.

Moratorium

At the forefront of the reforms is the introduction of a free-standing moratorium which represents an entirely new development in UK insolvency law. The policy is to afford a company in financial distress the breathing space to explore rescue and restructuring options free from creditor action. These include a company voluntary arrangement ("**CVA**"), a restructuring plan (another new development introduced by CIGA) or simply refinancing. The intention is that the moratorium will lead to a genuine and more effective rescue although there is no requirement to have a particular outcome when entering the moratorium.

The moratorium is a debtor-in-possession process analogous to that available under Chapter 11 of the US Bankruptcy Code. Once commenced, it will be overseen by an insolvency practitioner in the newly created office of "monitor", although the directors will retain control of the day-to-day running of the business. In order to limit the risk of the procedure being abused, there are various exclusions restricting the eligibility of a company to enter a moratorium and there are various procedural pre-requisites which must be satisfied such as formal statements by the directors and the monitor regarding the company's financial state and the prospects of a going concern rescue. There are also requirements to bring the moratorium to an end if it becomes clear that a rescue is unlikely. Some of these requirements have been temporarily relaxed in light of the COVID-19 crisis.

Restructuring plans

This reform allows companies, their creditors or members to propose a new restructuring plan as an alternative to a CVA or a scheme of arrangement under Part 26 of the Companies Act 2006. The new restructuring plan introduces a 'cross-class cram down' mechanism binding dissenting classes of creditors or members. The effect is that creditors or members who vote against the proposal but would be no worse off under the restructuring plan when compared with the most likely alternative outcome have no veto. However, cross-class cram down is subject to satisfying various conditions and requires the sanction of the court which, as with schemes of arrangement, retains absolute discretion and may refuse to sanction a plan if it is not just and equitable. In particular the restructuring plan may be used in tandem with the new moratorium process (subject to the eligibility and procedural requirements being satisfied) thereby streamlining the restructuring process free from creditor action.

Winding-up petitions

CIGA introduces a temporary prohibition on winding-up proceedings based on statutory demands where the grounds for the winding-up petition are attributable to the impact of COVID-19. In particular, there is a ban on the presentation of winding-up petitions on or after 27 April 2020 based on statutory demands served in the "relevant period" between 1 March 2020 and 30 September 2020. In addition, CIGA limits the ability of a creditor to present a winding-up petition and obtain a winding-up order on the grounds that the company is unable to pay its debts. During the relevant period of restriction, a creditor may only present a petition where there are reasonable grounds for believing that the company's inability to pay its debts was not caused by the coronavirus pandemic. Similarly, the court may only make a winding-up order where it is satisfied that the grounds relied upon in the petition are not attributable to coronavirus.

Wrongful trading

Ordinarily, the risk of directors facing wrongful trading proceedings and incurring personal liability for losses may act as something of a deterrent against continuing to trade under a threat of insolvency (although it is only right to acknowledge that the reported cases contain few examples of successful wrongful trading claims). As a result of the uncertainties caused by the COVID-19 crisis, many directors have had to make difficult decisions about the future viability of their companies and the justification for continued trading bearing in mind the risk of personal liability. On 28 March 2020 the Government announced that it would suspend the wrongful trading regime on a temporary basis in order to enable directors to make decisions about their companies free of the deterrent of a potential wrongful trading claim. However, as the commentary in this guide considers, the reforms amount not so much to a suspension as to a modification of the extent to which directors may be found liable. According to the changes introduced by CIGA, where the court hearing a wrongful trading application is considering whether to impose on the director liability to contribute to the company's assets and, if so, in what amount, it shall not take into account any losses incurred during a specified period i.e.1 March 2020 to 30 September 2020.

Insolvency termination clauses
A significant change introduced by CIGA is the prohibition of reliance on termination clauses in supply contracts which are triggered on the company's insolvency or based on breaches which predate the insolvency process. Consequently, subject to certain exclusions, suppliers will have to continue their supply notwithstanding the company's insolvency or arrears which accrued prior to the company's insolvency process.
This reform is part of the suite of permanent changes aimed at improving the environment for corporate rescue. There are provisions for those companies and contracts which are exempt from the prohibition: these predominantly relate to the financial services sector. In addition, "small entity" suppliers as defined are exempt from the prohibition for a limited period (until 30 September 2020) to mitigate the effects of COVID-19 on smaller businesses with a power for the period to be extended. However, where a company enters an insolvency process after the exemption has expired, suppliers of all sizes will be subject to the ban unless subsequent exemptions become applicable. A supplier can apply for relief from the prohibition on the grounds of "hardship" and there are express carve outs preserving the right to terminate a contract with the agreement of the company (if in a moratorium, restructuring plan or CVA in is force) or the office holder (where other insolvency procedures have commenced).

Amendment of corporate insolvency and governance legislation
This measure permits the Secretary of State on a time limited basis to use so-called Henry VIII powers to amend corporate insolvency legislation via Statutory Instruments. The policy underlying this reform is to ensure that the insolvency and restructuring regime is flexible and able to address any sudden and significant developments impacting business in the aftermath of the coronavirus pandemic. For example, temporary amendments may be made to protect and provide regulatory support for otherwise viable companies. However, the exercise of such power is regulated by the need to satisfy certain requirements: the impact of persons likely to be affected by the amendments must be considered; the amendments must be proportionate to the issues being addressed; the amendments are necessary to bring about the intended effect; and there are no other existing provisions which could be deployed to bring about the amendments.

Meetings and filing requirements
CIGA introduces new measures to enable companies to hold annual general meetings ("**AGMs**") and other meetings in a manner which is consistent with their constitutional arrangements and the requirement to limit the spread of COVID-19. During the temporary period commencing on 26 March 2020 and ending on 30 September 2020, companies can exercise greater flexibility in holding meetings, including by remote, electronic platforms. The measures also permit the extension, if required, of the period in which a company must hold its AGM.

CIGA provides the Secretary of State with a new, broad power to make regulations extending deadlines for maximum periods in respect of company filings such as accounts, annual confirmations and the registration of charges.

Territorial extent
The reforms set out in the provisions of CIGA are variously stated to apply to the whole of the United Kingdom; to England and Wales and Scotland; to England and Wales only; to Scotland only; or to Northern Ireland. The principal focus of this guide is the introduction of the new reforms that relate to England and Wales. While similar provisions have been enacted in relation to other parts of the United Kingdom, it is recommended that the reader consult the relevant sections of CIGA for their detail.

Moratorium

Jamie Riley QC and William Day

Introduction

Section 1 of CIGA introduces a new Part A1 to the Insolvency Act 1986 which sets out the provisions for the new, free-standing statutory moratorium ("**the Moratorium**"). The purpose of the Moratorium is to afford financially distressed companies protection from immediate creditor action and breathing space to consider its options for corporate rescue or restructuring.

The Moratorium is specifically aimed at bringing about a rescue of the company (including by a refinancing, pursuant to a CVA or via a restructuring plan (another new innovation introduced by the Act). The intention behind these reforms is to provide a more effective and efficient route to corporate rescue for the benefit of all interested parties than has hitherto been available via administration. All too often, administration has failed to achieve its corporate rescue aims. Instead it has become a preferred terminal route favoured by secured creditors with floating charges.

A significant feature contributing to this terminating effect of administration is that at the outset, the control of the business and affairs of the company is handed to the newly appointed administrator. A key aspect of the rescue aims of the Moratorium is that, unlike administration, the directors will remain in control of the company and the insolvency practitioner will merely have a 'monitoring' role to oversee the rescue attempt and protect creditor interests. As such, the Moratorium is a debtor-in-possession process akin to Chapter 11 in the United States.

Eligibility

The new Schedule ZA1 to the Insolvency Act 1986 which sets out those companies eligible for the moratorium. In general, all companies are "eligible" for the Moratorium unless they fall within the exceptions of "excluded" companies. The list of excluded companies is long and varied but includes:

(1) Companies in respect of which a Moratorium is already in force (the question then is one of extension: see below).[1]

(2) Companies which have been in a Moratorium in the 12 months preceding the filing date unless the court has ordered that the previous Moratorium is not to be taken into account in determining eligibility for a later Moratorium.[2]

(3) Companies which are already in an insolvency procedure or during the 12 months prior to the filing date have been subject to a CVA or administration.[3] For these purposes a company has been in an insolvency procedure includes where it has been subject to an interim moratorium for proposed administrations pursuant to paragraph 44 of Schedule B1 to the Insolvency Act 1986. As such, a floating charge holder or an unsecured creditor may pre-emptively seek to block a company's eligibility for the Moratorium by making an administration application or filing a notice of intention to appoint an administrator.

(4) Insurance companies, banks, and a number of other financial institutions (such as payment institutions, recognised investment exchanges, securitisation companies and public-private partnership companies) which are already subject to their own bespoke insolvency processes.[4]

(5) Companies which have a 'capital market arrangement'. This is widely defined to exclude a company which has entered into an arrangement under which it has incurred a debt of at least £10 million and which involves the grant of security to a person as trustee for investors and a guarantee or security for the performance of obligations by another party.[5]

These exclusions also apply to overseas companies with equivalent operations and which would be ineligible if registered in England and Wales or Scotland.[6]

1 Schedule ZA1, para 2(1).
2 Schedule ZA1, para 2(2). Although for a temporary period up to 30 September 2020 this restriction has been removed to mitigate the extraordinary impact of the COVID-19 pandemic: see Schedule 4, para 6.
3 Schedule ZA1, paras 2(2) – (4). Although this restriction has also been suspended up to 30 September 2020: see Schedule 4, para 6.
4 Schedule ZA1, paras 3 – 12.
5 Schedule ZA1, paras 13 – 14.
6 Schedule ZA1, para 18.

How to obtain a moratorium

Chapter 2 of the new Part A1 sets out the procedure for obtaining the Moratorium. Like administrations, depending on the particular circumstances, moratoriums can be obtained by an out of court process or by an application to court.

The out of court process is available for an English registered company which is not subject to an outstanding winding-up petition (i.e. a winding-up petition which has been presented but not yet withdrawn or determined).[7] Under this process, the Moratorium is triggered on the filing of the various "relevant documents" at court. The relevant documents are notices and statements which set out and confirm that: (i) the directors wish to obtain a moratorium; (ii) the proposed monitor or monitors are qualified and consent to act; (iii) the company is eligible; (iv) in the opinion of the directors, the company is or is likely to become unable to pay its debts (likely applying a balance of probabilities test); and (v) in the view of the proposed monitor or monitors, it is likely that the Moratorium would result in the rescue of the company as a going concern.[8] However, the notice does not need to specify precisely how a going concern rescue may be achieved (for example, via a CVA, restructuring plan or refinancing).

In an effort to mitigate insolvencies during the COVID-19 crisis, this latter requirement is modified by Schedule 4. Until 30 September 2020, the proposed monitor can still endorse a moratorium even if it appears that the company may not be rescued as a going concern so long as the only reason for that is the company's worsening financial position caused by the COVID-19 crisis (in other words, but for the COVID-19 crisis, the monitor considers the company could be rescued as a going concern).[9]

The out of court procedure will not be available in two cases and it will be necessary for the directors to make an application to court in those cases:

(1) English registered companies in respect of which there is an outstanding a winding-up petition.[10]

(2) Overseas companies that are not subject to outstanding winding-up petitions.[11] Such companies will only be eligible for a moratorium if they could be wound up under Part 5 of the Insolvency Act 1986. In considering whether to grant a moratorium to an overseas company, the court will apply the same test and principles as when considering the winding up of an overseas company: in essence, the court will at least have to be satisfied that the company has a sufficient connection with the UK. Whether a "COMI" (centre of main interests) test is applied to EU companies will depend on the terms on which the future relationship between the UK and the EU is fixed by the end of this year.

In these cases the application must be supported by the same documents as set out above and the court will need to be satisfied that the Moratorium will achieve a better outcome for creditors as a whole than would be likely in the event that the company were wound up without first being in a moratorium.[12] This test echoes the second part of the waterfall provisions of the statutory objective for administration in paragraph 3 (1) (b) of Schedule B1 to the Insolvency Act 1986.

Again, there is some relaxation of these rules to deal with the COVID-19 crisis. In particular, English companies currently facing a winding up petition can nonetheless seek a moratorium on an out-of-court basis until 30 September 2020.[13] However, there is no temporary suspension of the requirements in relation to overseas companies while the COVID-19 pandemic continues and it will still be necessary for an overseas company to apply to court for protection.[14]

Depending on which process is used, the Moratorium will come into force on the date and time that the relevant documents are filed at court or when the court makes an order granting a moratorium.[15] On the Moratorium coming into force the office of the "monitor" formally commences. As soon as reasonably practicable after the Moratorium comes into force, the directors must notify the monitor who, in turn, must then immediately notify (i) the registrar of companies, (ii) the company's creditors of whom the monitor is aware, (iii) the Pensions Regulator (where the company has set up an occupational pension for employees) and/or the Pension Protection Fund (where the pension scheme set up by the company is eligible for such protection). The notice from the monitor must specify when the Moratorium came into force and when it is due to end subject to any alterations or extensions.[16]

7 Part A1, section A3.
8 Part A1, section A6.
9 Schedule 4, para 7.
10 Part A1, section A3(1)(a).
11 Part A1, section A3(1)(b).
12 Part A1, section A4(5) for companies subject to winding up petitions. The same test is not expressed to apply to overseas companies but one would expect a similar comparison exercise against other available insolvency procedures.
13 Schedule 4, para 6(1).
14 Schedule 4, para 6(2).
15 Part A1, section A7.
16 Part A1, section A8. The directors and the monitor commit offences if they fail to make these notifications without reasonable excuse.

Length of the moratorium

The length of the Moratorium is addressed in Chapter 3 of Part A1. The Moratorium initially is set to last for a short period of time: 20 business days beginning with the business day after the day on which the moratorium comes into force, unless it is extended or terminated early.[17] In view of the short initial period, it is anticipated that many moratoriums will need to be extended if they are not simply to be a prelude to another insolvency process.

Moratoriums can be extended in a number of ways:

(1) ***By the directors without creditor consent.***[18] This is available if all moratorium and pre-moratorium debts have been paid other than those for which there is a payment holiday (see below). The directors may extend the moratorium for a further 20 business days subject to the requirement to file at court a notice that the directors wish to extend the Moratorium together with other documents. Those documents include: (i) a statement from the directors that all of the moratorium debts and pre-moratorium debts for which the company does not have a payment holiday that have fallen due have been paid or otherwise discharged; (ii) a statement from the directors that in their view the company is still or still likely to become unable to pay its pre-moratorium debts (see below); and (ii) a statement from the monitor that, in his or her view, it is likely that the moratorium will result in the rescue of the company as a going concern. The extension cannot happen until 15 business days have expired since the start of the Moratorium. Once the extension has been triggered, the revised period ends on the expiry of 20 business after the initial 20 business day period irrespective of when the extension documents are filed, thereby extending the period of the moratorium to 40 business days from commencement. This form of extension is only available once.

(2) ***By the directors with creditor consent.***[19] This also requires the same re-confirmations as for (1) above along with a statement from the directors that “creditor consent” has been obtained and specifying the revised end date for which consent was given. For these purposes “creditor consent” is defined as being the consent of pre-moratorium creditors (see below) obtained by a qualifying decision procedure.[20] As with the first method of extension (see (1) above), the requisite documents cannot be filed until 15 business days have elapsed since the commencement of the Moratorium although there is no restriction on engaging with creditors in the first 15 days with a view to obtaining consent. Once the relevant documents have been filed, the Moratorium is extended so that it expires on the new date agreed with the creditors even if that date is beyond the period of 40 days after the commencement of the moratorium. This form of extension can be used more than once but not so as to extend the overall moratorium period beyond a year. This is the only form of extension available where the company has defaulted on obligations for which there is no payment holiday (see next page).

(3) ***On an application to the court by the directors.*** The directors may also apply to the court for an extension beyond 40 business days but the application cannot be made until at least 15 business days have expired since the commencement of the Moratorium. The application must be supported by the same documents which are filed for the out of court process in (1) above along with a statement from the directors as to whether the pre-moratorium creditors have been consulted and, if not, why not. In determining the application, the court must balance the interests of (a) pre-moratorium creditors against whom the Moratorium will bite and (b) the likelihood of the extension leading to a rescue of the company as a going concern. The court can extend the moratorium to a date specified in the order or make such order as it thinks appropriate. In principle, there is no limit on the extension which can be ordered, but in practice it seems unlikely that the court would allow a moratorium to extend beyond a year save in exceptional circumstances. Where an application to extend is made but not determined before the end of the initial period of the Moratorium, the Moratorium does not come to an end until the time specified in any order or, if no such order is made, when the application is withdrawn or otherwise disposed of.[21]

(4) ***In conjunction with a pending CVA or (on the order the court) in conjunction with a scheme of arrangement or restructuring plan.*** In respect of a company for which a CVA has been proposed, the period of the Moratorium will extend pending the approval or alternative disposal of the CVA proposal. In cases involving an application for a scheme of arrangement or restructuring plan, the court may extend the Moratorium to any date which it may choose to specify although, obviously, the date in the order will be determined by reference to the meetings of creditors convened to consider a scheme of arrangement or an arrangement and reconstruction.[22]

Given the practical difficulties of marshalling any creditor consensus within a short period of time, applications to court for extensions under option (3) are likely to become a frequently used method of securing an extension. Consequently, even though most moratoriums should start out of court, it is anticipated that many will rapidly be drawn into a court process.

The directors must notify the monitor of any change to the end of the moratorium. In turn, the monitor must notify the registrar of companies and every creditor of the company of whose claim the monitor is aware.[23]

The Moratorium will end at any time at which the company enters an insolvency procedure including a CVA, administration or liquidation or an interim moratorium in respect of administration pursuant to paragraph 44 of Schedule B1 applies to the company. The Moratorium will also terminate upon an order sanctioning a compromise or arrangement under section 899 or 901F of the Companies Act 2006 coming into effect.[24]

17 Part A1, section A9.
18 Part A1, section A10.
19 Part A1, section A10.
20 Part A1, section A12. See Insolvency Rules 2016, Pts 15 – 16. as modified by Schedule 4, paras 23 – 28.
21 Part A1, section A13.
22 Part A1, section A14.
23 Part A1, section A17. The directors and the monitor commit offences if they fail to make these notifications without reasonable excuse.
24 Part A1, section A16.

Effect of the moratorium

The effects of the moratorium are addressed in Chapter 4 of Part A1. The principal object and effect of the Moratorium is to provide to the company temporary shelter in the form of a "payment holiday" restricting the enforcement or payment of certain debts classified as "pre-moratorium debts". Pre-moratorium debts are debts that have fallen due before the commencement of the Moratorium or that become due during the Moratorium pursuant to an obligation incurred prior to the Moratorium.[25] The explanatory notes to the Act state that these definitions are intended to replicate the distinction between provable debts and expenses in administration: see *Re Nortel GmbH*.[26]

There are various exceptions to the category of pre-moratorium debts. For these debts, the company must continue paying what is owed during the Moratorium, and will limit the company's ability to extend the Moratorium save by way of application. These exceptions include: (i) the monitor's remuneration and expenses (excluding in respect of anything done before the commencement of the moratorium); (ii) goods and services supplied during the moratorium (including the ongoing provision and usage of property owned by another such as leased equipment or licensed services e.g. software where the lease or licence obligation was incurred prior to the moratorium); (iii) rent falling due during the moratorium; (iv) wages, salaries or redundancy payments; and (v) debts or other liabilities arising under financial services contracts.[27]

By contrast, a "moratorium debt" is defined as: (i) a debt or other liability to which the company becomes subject during the Moratorium but not as a result of any obligation incurred prior to the Moratorium; or (ii) a debt or liability to which the company may become subject after the Moratorium has ended by reason of an obligation incurred during the Moratorium.[28]

Other significant effects of the Moratorium include:

- ***Restrictions on insolvency proceedings.***[29] The Moratorium generally prevents the commencement of insolvency proceedings (via both court and out of court processes) with limited exceptions: (i) a winding-up petition on the petition may be presented by the directors, or by the Secretary of State on grounds of public interest; (ii) a resolution for the voluntary winding up of the company may be passed but only on the recommendation of the directors; (iii) no order can be made for the winding-up of the company except on a petition by the directors; (iv) an administration application may be made but only by the directors. Accordingly, a qualifying floating charge holder is prevented from filing at court a notice of intention to appoint an administrator or a notice of appointment of an administrator under paragraph 14 of Schedule B1. Where the directors intend to commence any insolvency proceedings as permitted by these exceptions then they are obliged to notify the monitor.[30]
- ***Restrictions on enforcement and other legal proceedings.***[31] During the Moratorium, unless the court grants permission, no steps may be taken to enforce any security over the company's property (unless it is created under a financial collateral arrangement or a step to enforce a collateral security charge) or repossess any goods under a hire-purchase agreement. The Moratorium also protects against a landlord's forfeiture by peaceable re-entry under any lease of business premises without the court's permission.
- ***Floating charges.***[32] The moratorium prevents the crystallisation of any floating charge and the imposition of restrictions on the disposal of company property. However, the holder of a floating charge is permitted to give notice to crystallise the floating charge as soon as practicable after the end of the Moratorium or, if later, the date when the charge is notified of the end of the Moratorium. There are limited exceptions to this for collateral security; a market charge; security financial collateral arrangement; and a system charge.[33] However, other types of secured "financial service contracts" (for example, vanilla loans) are not exempted from this provision. That means that although debts due under such contracts must be paid during the Moratorium (see above), a default cannot be followed by enforcement of the charge. That may provide important breathing space to a company on the edge of insolvency.

These features of the Moratorium broadly track the administration moratorium provided for in paragraph 43 of Schedule B1, with the significant exception of the restriction on the crystallisation of the floating charge. This is a uniquely distinguishing aspect of the new procedure and likely to be one of its most attractive features.

The corollary of the Moratorium is that the company is subject to various restrictions and conditions during the time it is in force:

- ***Publicity.***[34] During the moratorium the company must display at its business premises a notice of the moratorium. It must also publicise the fact that it is subject to a moratorium on each and every website and business document issued by the company and display the name of the monitor.
- ***Restrictions on New Credit.***[35] The company may not obtain credit of £500 or more unless the person giving credit has been informed that a Moratorium is in force. This includes entering into conditional sale agreements or hire-purchase agreement under which goods are hired and where the company is paid in advance for the supply of goods or services. This obligation to inform may be satisfied by the company's compliance with the requirement to publicise the Moratorium referred to above.
- ***Restrictions on New Security.***[36] Security may only be granted over the company's property, and will only be enforceable, if the monitor consents. The monitor may only give consent if he or she considers that the grant of security will support the aim of rescuing the company as a going concern.

25 Part A1, section A18(3).
26 *Re Nortel GmbH* [2013] UKSC 52, [2014] AC 209.
27 Part A1, section A18(3)(a)-(f). Financial services contracts are defined very widely in a new Schedule ZA2 and include market contracts, qualifying collateral arrangements and property transfers, contracts secured by certain charges or arrangements, default arrangements and transfer orders, capital market arrangements, contracts forming part of a public-private partnership, derivatives, financial contracts, spot contracts, card-based payment transactions and securities financing transactions.
28 Part A1, section A53.
29 Part A1, section A20.
30 Part A1, section A24. Failure to notify the monitor without reasonable excuse is an offence.
31 Part A1, section A21.
32 Part A1, section A22.
33 Part A1, section A22(7) cross-referring to section A27 (addressed below) and the Financial Collateral Arrangements (No 2) Regulations 2003 (SI 2003/3226).
34 Part A1, section A19. Failure to provide the requisite publicity constitutes an offence by the company and (if there is no reasonable excuse) by the relevant officers of the company.
35 Part AI, section A25. Contravention by the company and the relevant officers (if they have no reasonable excuse) is an offence.
36 Part A1, section A26. Again, contravention by the company and the relevant officers (if they have no reasonable excuse) is an offence.

- ***Restrictions on New Financial Arrangements.***[37] The company is prohibited from: entering into a market contract or a financial collateral arrangement; giving a transfer order; granting a market charge or system-charge; providing collateral security.[38]
- ***Restrictions on Paying Old Debts.***[39] If the company wants to pay a pre-moratorium debt which is the greater of £5,000 and 1% of the value of the unsecured debts owed by the company at the start of the Moratorium, despite the payment holiday, either (i) the monitor's consent must be obtained or (ii) the permission of the court is obtained. The monitor may give consent only on the basis that he/she is of the view that the payment supports the company's rescue as a going concern.
- ***Restrictions on Disposal of Property.***[40] The company may dispose of property that is not subject to security if (i) the disposal is in the ordinary course of business (ii) the monitor consents (on the limited basis that the disposal will support a going concern rescue) or (iii) the court gives permission.
- ***Restrictions on Disposal of Secured Property.***[41] In respect of property that is subject to security or a hire-purchase agreement, the company may only make disposals with the permission of the court or in accordance with the terms of the security/agreement. This restriction also resembles the conditions for similar disposals applicable in administration. In particular, the court will grant permission if it considers that the disposal will support a going concern rescue and on the condition that the net sale proceeds (which the court may determine based on an open market valuation) are allocated to discharge or reduce the sums secured or payable under the hire-purchase agreement.

CIGA expressly states that a contravention by the company of any of these conditions and restrictions does not render a transaction void or unenforceable or affect the validity of anything else.[42] In light of that express provision, it is doubtful that such arrangements could be unenforceable at common law applying the test for illegality recently developed by the Supreme Court in *Patel v Mirza.*[43]

The monitor

Chapter 5 of Part A1 contains provisions regarding the newly created office of "monitor". On 26 June 2020, the Government published detailed guidance for monitors which emphasised that monitors are expected to act "with integrity and good faith" and "ensure creditor interests are protected". The key obligation on the monitor is to monitor the company's affairs for the purpose of forming the view as to whether it remains likely that the Moratorium will result in the rescue of the company as a going concern – and, if not, to end the Moratorium.[44]

Compared with other established insolvency processes, a distinguishing feature of the Moratorium is that it is a debtor-in-possession process with the control of the company remaining in the hands of the directors. This structure is closer to the model of Chapter 11 in the US and is in line with the European Restructuring Directive.[45] However, during the Moratorium the company's affairs will be supervised by "the monitor" (an insolvency practitioner) whose primary role is to verify whether there remains a likelihood of a rescue of the company as a going concern.[46] In doing so, the monitor can require the directors to provide information upon which the monitor may rely in forming a view save where there are reasons to doubt its accuracy.[47]

If at any stage the monitor concludes that: (i) the moratorium is no longer likely to lead to a going concern rescue; (ii) a going concern rescue has been achieved; (iii) the monitor is unable to carry out his/her functions due to a failure by the directors to provide required information; or (iv) the company is unable to pay its moratorium debts and pre-moratorium debts from which the company does not have a payment holiday, the monitor must bring the moratorium to end by filing a termination notice at court. In such circumstances, the moratorium comes to an end on the date the notice is formally filed at court.[48]

37 Part A1, section A27.
38 Within the respective definitions contained in the Companies Act 1989, the Financial Collateral Arrangements (No 2) Regulations 2003 (SI 2003/3226), the Financial Markets and Insolvency Regulations 1996 (SI 1996/1469) and the Financial Markets and Insolvency (Settlement Finality) Regulations 1999 (SI 1999/2979).
39 Part A1, section A28. Old debts paid in breach of the prohibition amounts to an offence by the company and the relevant officers (if they have no reasonable excuse).
40 Part A1, section A29. Property disposed of in breach of the prohibition amounts to an offence by the company and the relevant officers (if they have no reasonable excuse).
41 Part A1, sections A30 – A31. Property disposed of in breach of the prohibition amounts to an offence by the company and the relevant officers (if they have no reasonable excuse).
42 Part A1, section A33.
43 *Patel v Mirza* [2016] UKSC 42, [2017] AC 467.
44 Part A1, section A35.
45 EU Directive 2019/1023.
46 Part A1, section A35.
47 Part A1, section A36.
48 Part A1, section A38.

As with officeholders in other forms of insolvency procedures, the monitor may apply to court for directions as to the carrying out of his/her functions.[49] However, given the monitor has a less active role compared to administrators and liquidations, directions are likely to be sought less frequently.

The monitor can be removed and replaced by court order on the application of the directors or the monitor him/herself but not by the creditors or members.[50] That gives a monitor greater security of tenure compared to administrators and liquidators who can be removed on the application of creditors or (in an MVL) members. Removal applications are likely be successful in similar circumstances to removal applications in administrations and liquidations. Analogising from that case law, applications would fall broadly into three categories:

- Where there is justifiable criticism of the monitor's conduct.
- Where there is a conflict between the monitor's duties and his or her personal interests or other duties. In this regard, we note that the Government guidance to monitors emphasise that "it is vital that any conflicts of interests are avoided or managed appropriately to safeguard the interests of all stakeholders" and that monitors act in accordance with the Code of Ethics for insolvency practitioners.
- Where those directors who nominated the monitor are now considered to have interests adverse to creditors whose interests the monitor must uphold.

The replacement monitor must provide a notice of consent to act including a statement that they are qualified to act as monitor and, in the case of more than one monitor, details of which functions are to be carried out by which monitor or jointly. In addition, the monitor must notify the registrar of companies and the creditors of the removal of a monitor and the appointment of the new replacement.[51]

Challenges to moratoriums by creditors and members

Creditors and members, as interested parties, may be heard in supporting or opposing applications brought by directors to initiate a Moratorium. They may also attend subsequent applications to extend the Moratorium to make submissions in opposition to such an extension.

In addition, Chapter 6 of Part A1 contains provisions for making challenges to the acts, omissions or decisions of the monitor in the Moratorium. A creditor, member, director or any other person affected (including the Pension Protection Fund) also has standing to bring an application, either during the Moratorium or has ended, to challenge any act, omission or decision of the monitor on the basis of "unfair harm" to the applicant's interests. The court has a broad and flexible discretion to grant relief on such an application: it can confirm, reverse or modify a monitor's act or decision or give directions or make some other order as it thinks fit (including bringing the moratorium to an end). However, the court cannot order the monitor to pay compensation.[52]

This right to have recourse to the court resembles equivalent rights in respect of other, established insolvency procedures although it is important to bear in mind that the role of the monitor is not to manage the affairs of the company but to oversee the management by the directors. As such, any complaint about the monitor's conduct must be made in that limited context. Further, the "unfair harm" test echoes paragraph 74 of Schedule B1 in respect of administrators and we would expect the Courts to adopt the same "cautious" approach to interfering with the officeholder's exercise of discretion: see, e.g., *Lehman Brothers Australia Limited (in liquidation) v MacNamara*.[53]

The more striking feature of Chapter 6 is that, while directors remain in control of the company, they are subject to supervisory jurisdiction of the court. Creditors, members and the Pension Protection Fund can invoke that jurisdiction applying the "unfair harm" test and may bring an application not only during but also after the period of the Moratorium. The court has a wide discretion to make any order it thinks fit including: (i) an order to regulate the management of the company; (ii) an order requiring the directors to do or not do something in particular; (iii) an order which requires the sanction of creditors on a particular matter; or (iv) an order to bring the Moratorium to an end. It is noteworthy that, unlike in relation to challenges made in respect of the conduct of the monitor, there is no express exclusion preventing the court from ordering compensation against the directors.[54]

We consider it likely that the unfair harm jurisdiction is likely to be used more frequently for directors than monitors (given directors remain in control of the company during the Moratorium) and that, for directors, the test is likely to incorporate some of the principles that have been developed in the context of the unfair prejudice petition (as well as or instead of paragraph 74 of Schedule B1). Again, unfairness should be judged objectively, and not take into account motive or intention. Most (if not all) successful unfair prejudice petitions have as their foundations (i) breaches of the company's articles of association, (ii) breaches of fiduciary duty, and/or (iii) breaches of legitimate expectations arising from some formal or informal agreement as to the conduct of the company's affairs. We would expect the unfair harm test to have similar foundations.

The unfair harm jurisdiction also raises the prospect of compensation and damages claims being brought against directors both during and after the Moratorium. This stands in stark contrast to administration and liquidation in which the officeholders take over control of the company and assume duties the breach of which exposes them to misfeasance claims.

Given the inevitable existence of competing interests of the company and its various creditors and members and the direct supervision of the court, the challenge provisions are likely to be the most litigious area of the Moratorium. In view of its very short length of 20 business days, it seems unlikely that many challenges will be made during the initial period. Instead, the challenge provisions are more likely to come into their own after a company has secured an extended moratorium and, for example, a trade creditor faces the prospect of being kept out of its money for a significant length of time. It is also conceivable that the challenge provisions are used by creditors and members to attack the very decision to put the company into Moratorium in the first place.

49 Part A1, section A37.
50 Part A1, section A39.
51 Part A1, section A39.
52 Part IA, section A42.
53 *Lehman Brothers Australia Limited (in liquidation) v MacNamara* [2020] EWCA Civ 321 esp [84].
54 Part IA, section A44.

Conclusion

The introduction of new scheme of the Moratorium marks an important rebooting of insolvency policy back towards corporate rescue as originally envisaged in the Cork Report ahead of the 1986 reforms. The directors retain management control of the company making the Moratorium a debtor-in-possession process similar to US Chapter 11 proceedings. In theory, it offers financially distressed but ultimately viable companies an opportunity to get back on track rather than inexorably slip towards a de facto winding-up. These are laudable aims and the new process undoubtedly will be welcomed by those critical of administration as having strayed from its original aims and too often being a terminal procedure.

In practice, however, the picture may be very different and the implementation of corporate rescue may be far from straightforward or, in some cases, illusory. The new Moratorium is notionally available to companies which, in reality, are terminally insolvent and inevitably heading towards administration or liquidation. The harsh reality is that the Moratorium is not intended for such companies but, understandably, the temptation to make a final ditched attempt at a going concern rescue will be great. In more extreme and hopefully rare scenarios, the potential ease with which the Moratorium may be commenced and later extended may be open to abuse by moribund companies whose directors merely seek to keep creditors at bay while extending losses.

As a counterweight to these risks, the scope for eligibility has been made narrow: there are many categories of excluded companies, the most notable of which is the exclusion for companies with a "capital market arrangement" which bars the way for companies financed by issuing bonds of at least £10 million. That is going to exclude a number of the companies hit hardest by the COVID-19 lockdown (such as the retail, leisure and hospitality sectors).

Further, as noted above, the Moratorium is not available to companies which are already in an insolvency procedure. As a result, floating charge holders and other creditors may be more inclined to pre-empt the company's resort to a Moratorium by taking steps to put the company into administration at an earlier stage. In many cases there may be a race to fire the first shot between a company (seeking a Moratorium) and creditors (seeking an administration).

Where companies are eligible for Moratoriums, there are safeguards against inappropriate or abusive moratoriums built into the formal requirements to obtaining the Moratorium. In particular, the proposed monitor must certify that the Moratorium is "likely" to result in a rescue of the company as a going concern. This is a more definite and arguably stricter requirement than for an administrator appointed out of court to state an opinion that the administration is "reasonably likely" to achieve it purpose. It remains to be seen whether insolvency practitioners will feel comfortable to certify a likelihood of a corporate rescue particularly, as will often be the case, under the pressure of a short time frame. One notable factor which the proposed monitor will need to have in mind is the wide-ranging list of pre-moratorium debts for which the company does not have a payment holiday. As observed above, these include debts owed to lenders and finance providers which in some cases may be an immoveable obstacle to a corporate rescue.

There is therefore a risk that the availability of Moratoriums has been restricted to too few companies and, even for those companies, the bar has been set too high with the result that the Moratorium will only be available in practice to those limited number of companies for whom there is greater certainty and not merely an opportunity for a corporate rescue.

The Restructuring Plan

Jamie Riley QC and Anthony Pavlovich

Introduction

Section 7 and Schedule 9 of CIGA introduce a new Part 26A in the Companies Act 2006 entitled “Arrangements and reconstructions for companies in financial difficulty”. This sets out arrangements for a company to enter into a ‘restructuring plan’ with the approval of its creditors or members (“**the Restructuring Plan**”).

Section 8 of CIGA is another provision dealing with the restructuring of companies in financial difficulty. It revives paragraph 60A of Schedule B1 to the Insolvency Act 1986. That paragraph allowed the Secretary of State to make regulations for pre-pack administrations, that is, disposals by administrators of company assets to persons connected to the company. The old paragraph had expired in May 2020 without any such regulations having being issued. The revived paragraph extends the time to make such regulations until the end of June 2021. This section of the guide, however, focuses on the more innovative provisions for the Restructuring Plan.

The new Restructuring Plan is based on the existing scheme of arrangement under Part 26 of the Companies Act 2006 but differs in three important respects:

(1) A Restructuring Plan is only available in order to eliminate, reduce, prevent or mitigate the adverse effect on a company’s ability to carry on business as a going concern caused by serious “financial difficulties” that the company encounters or is likely to encounter.[1] No guidance is provided limiting the meaning or scope of “financial difficulties” which on the face of it can be given a broad interpretation. The only defining feature is that the financial difficulties will or may impact on the company’s ability to operate as a going concern.

(2) The requirement for approval of a Restructuring Plan is for a 75% majority in value without an additional simple majority in number required to approve a scheme.[2]

(3) Restructuring Plans benefit from a “cross-class cram down” provision that allows the court to sanction the plan as binding even if a dissenting group in a class of creditors or members results in the plan not being agreed by 75% in value.[3] This provision stops obstructive investors holding the company to ransom, but it only applies where those investors will be no worse off under the Restructuring Plan, and where some other class of investors with a “genuine economic interest” approves the plan.

The process

The first stage in the process is that the company, any creditors or member or any administrator or liquidator appointed over the company may apply to court for directions to summon a meeting of creditors or class of creditors, or the members or class of members in order to consider a Restructuring Plan.[4]

At the initial hearing of the application the court will consider the various proposed classes of creditors and members. As the Restructuring Plan is modelled on the existing schemes of arrangement, it is anticipated that, by analogy, the court will apply the same test in determining into which class creditors or members fall. On that basis creditors and members will vote in the same class where their rights are similarly tied to a common interest.

The general rule is that every creditor or member whose rights are affected by the proposed Restructuring Plan must be permitted to participate in the meeting. However, this mandatory right to participate in the meeting (and further stages in the process) may be removed if, on an application, the court is satisfied that, in relation to a particular class of creditors or members, none within that class has a “genuine economic interest” in the company.[5] This almost certainly will give rise to disputes as to the nature and value of an interest which certain creditors or members claim in respect of the company and will require the court to provide some clear guidance as to what constitutes a “genuine economic interest”. However, it presents the company, or those proposing a Restructuring Plan on its behalf, with the chance to remove from the equation troublesome creditors or members who are “out of the money”. This aligns Restructuring Plans with schemes of arrangements where it is established that it is unnecessary for the scheme company to consult any class of creditor or member that has no economic interest in the company.[6]

Where a meeting is directed, the notice sent to creditors and members summoning the meeting must include a statement explaining the effect of the Restructuring Plan and identifying any material interests of the company’s directors and stating how they are affected by the Restructuring Plan.[7] Where the notice summoning the meeting is given by an advertisement, the notice must include the explanatory statement or give details of how and where the creditors and members may obtain copies of the statement.

1 Section 901A Companies Act 2006.
2 Section 901F Companies Act 2006.
3 Section 901G Companies Act 2006.
4 Section 901C Companies Act 2006.
5 Section 901C(3)-(5) Companies Act 2006.
6 *Re Bluebrook Ltd* [2010] B.C.C. 209.
7 Section 901D Companies Act 2006.

If the requisite majorities are obtained at the meeting of creditors or members summoned pursuant to the initial order, at a hearing on a further application, the court may exercise its discretion to sanction the Restructuring Plan.[8] The requisite majority is the number representing 75% in value of the creditors/members or class of creditors/members (as the case may be) in attendance and voting in person or by proxy. In a departure from the procedure applicable for schemes, there is no additional requirement for a majority in number. Although there are no provisions which expressly set out how the discretion is to be exercised, it is likely that the court will draw on the principles applicable to schemes. For example, the court may refuse to grant sanction, notwithstanding if all the procedural requirements are met, if it considers that the Restructuring Plan is not just and equitable.

Where the court makes an order sanctioning the Restructuring Plan, if the company is in administration or liquidation, the court order may: (i) order a stay of the administration or liquidation; (ii) direct that the appointment of the administrator or liquidator should cease to have effect; or (iii) give directions for the conduct of the administration or liquidation which the court thinks necessary or appropriate to facilitate the Restructuring Plan.[9]

The order sanctioning the Restructuring Plan is binding on all affected creditors/members once notice is delivered to Companies House.[10]

Cross-class cram down

A Restructuring Plan may be sanctioned using a cross-class cram down notwithstanding that it has not been approved by 75% in value of a class of creditors or members ("**the dissenting class**").[11] In order for the court to grant sanction two conditions ("**Condition A**" and "**Condition B**") must be met:

- Condition A is that the court is satisfied that, if the Restructuring Plan were sanctioned, none of the members of the dissenting class would be any worse off than they would be in the event of "the relevant alternative". For these purposes, "the relevant alternative" is whatever the court considers would be most likely to occur in relation to the company if the Restructuring Plan were not sanctioned.
- Condition B is that the Restructuring Plan by a requisite majority (i.e. a number representing 75% in value) has been approved by at least one class of creditors or members who would receive payment or have a genuine economic interest in the company in the event of "the relevant alternative". These are described as 'impaired creditors' in the Government's consultation response on which CIGA is based, presumably because they give up some of their entitlements as a result of the restructuring.

As in cases where there is no dissenting class, the court will still have a broad discretion as to whether or not to sanction the Restructuring Plan and may refuse to do so if it is not considered just and equitable.

These provisions are likely to spawn a multitude of difficult and complex disputes involving competing valuations and comparisons between the estimated outcome of the Restructuring Plan and "the relevant alternative" which, given that the companies involved are in or on the verge of financial distress, may take the form of an administration, a liquidation or an alternative Restructuring Plan. A particularly contentious aspect of the cram down is likely to centre on the court's jurisdiction to sanction the Restructuring Plan on the approval of only one class of creditors or members. If the other creditors and members within the dissenting class would not be worse off in the relevant alternative then, if it is sanctioned by the court, they will be bound by the Restructuring Plan regardless of whether they rank as senior or junior to the approving class.

Overseas companies

As in the case of scheme of arrangement, the Restructuring Plan is available to a "company" within the meaning contained in the Companies Act 2006.[12] This includes overseas companies that would be subject to the UK courts' winding-up jurisdiction under Part 5 of the Insolvency Act 1986. Therefore, in order to qualify the overseas company must have "sufficient connection" with the United Kingdom although that is a flexible concept offering wide scope to establish jurisdiction in the English court.

The same procedure applies to overseas companies, except that the order sanctioning the Restructuring Plan must be published in the Gazette,[13] and the provisions for reconstruction or amalgamation (discussed below) do not apply.[14]

Moratorium debts

CIGA includes specific provision for companies seeking a Restructuring Plan in relation to moratorium debts or priority pre-moratorium debts (see the separate section relating to the Moratorium process under the new Part A1 to the Insolvency Act 1986).[15] If an application to court to convene a meeting is made before the end of the period of 12 weeks commencing on the day after the end of a moratorium and the proposed plan includes provision for creditors with moratorium or priority pre-moratorium debts, the court may not sanction the plan if the relevant creditor has not agreed to that provision. An equivalent provision has also been introduced in respect of schemes of arrangement under the existing Part 26 of the Companies Act 2006.[16]

8 Section 901F Companies Act 2006.
9 Section 901F(4) Companies Act 2006.
10 Section 901F(5)-(6) Companies Act 2006.
11 Section 901G Companies Act 2006.
12 Section 901A(4)(b) Companies Act 2006.
13 Unless the company is subject to s1046 Companies Act 2006; section 901F(6)(a) Companies Act 2006.
14 Section 901A(4)(a) Companies Act 2006.
15 Section 901H Companies Act 2006.
16 Section 899A Companies Act 2006.

Reconstructions and amalgamations

For cases where the court sanctions a Restructuring Plan involving the reconstruction of one or more companies or the amalgamation of two or more companies, the court has powers to facilitate the reconstruction or amalgamation including powers to: (i) transfer the whole or part of the undertaking, property or liabilities of one company to another; (ii) direct the allotment or appropriation of shares, debentures, policies or other interests; (iii) permit the continuation by or against the transferee company of any proceedings by or against the transferor company; and (iv) the dissolution of a transferor company.[17]

Articles of association

Where the court sanctions a Restructuring Plan and in doing so amends the company's articles of association or any constitutional resolution or agreement, the company must send a copy of the amended articles or resolution/agreement to Companies House together with a copy of the court order.[18] If the company fails to comply with this requirement then the company and every officer in default commits an offence.

Regulatory oversight

The provisions include amendments to legislation to allow banking and pensions regulators to have oversight of Restructuring Plans for companies that they regulate:

- A new s355A in the Financial Services and Markets Act 2000 allows the FCA or PRA to receive notice of applications under Part 26A and to participate in the resulting hearings and meetings, where those concern an authorised person under that Act, a recognised investment exchange, or certain other financial institutions (this provision is similar to some existing provisions, such as s371 in respect of winding-up proceedings); and the PRA's consent is required to make applications under s901C in respect of PRA-regulated companies. Under new s355B, the relevant regulator has the power to impose public censure or financial penalties for any breach of the notification and consent requirements of s355A.
- A new s124A in the Financial Services (Banking Reform) Act 2013 allows the Bank of England to receive notice of applications under Part 26A and to participate in the resulting hearings and meetings, where those concern an infrastructure company (such companies, which include some payment-systems operators, are subject to a special insolvency regime under that Act); and the Bank of England's consent is required to make applications under s901C in respect of infrastructure companies. The Bank's existing powers of enforcement, including public censure, financial penalties and injunctive relief, apply to any breach of the notification and consent requirements.
- Section 901I Companies Act 2006 provides that documents that must be sent to creditors must also be sent to the Pensions Regulator and to Board of the Pension Protection Fund, where the company operates a specified kind of pension scheme. The Board may also be able to intervene by exercising the powers as creditors of the trustees or managers of the pension scheme, for example by exercising a right to vote on the Restructuring Plan; but this will have to be provided for by regulations made by the Secretary of State.

Conclusion

The Restructuring Plan represents a marked change in law relating to reconstructions. It is tailored more to the requirements of financially distressed companies offering greater flexibility than schemes of arrangement. The most significant innovation is the introduction of the cross-class cram down provisions which focus on the competing financial outcomes available and offer to junior creditors the opportunity of greater influence than they enjoy in respect of schemes of arrangement. At the same time, the sanctioning of a Restructuring Plan on the approval of a single class in the face of opposition from a larger body of dissenting creditors or members is bound to lead to litigation. In particular, there will be highly contentious disputes over whether a creditor or member has a "genuine economic interest" and whether members of the dissenting class will be worse off under the restructuring Plan or the "relevant alternative". These issues will be all the more difficult in light of the financial impact of the COVID-19 pandemic.

17 Section 901J Companies Act 2006.
18 Section 901K Companies Act 2006.

3 VERULAM BUILDINGS
BARRISTERS

Winding-up Petitions and Statutory Demands

Jamie Riley QC and James McWilliams

Introduction

CIGA introduces a temporary ban which significantly curtails the ability of creditors to make use of the statutory demand procedure and/or the presentation of a winding-up petition in respect of debts which are rightfully owed but unpaid in the wake of the economic shock caused by COVID-19. The key provisions of the temporary ban are set out in Section 10 and Schedule 10 of CIGA; with effect from 27 April 2020 they restrict the use of statutory demands and winding-up petitions in four significant respects, discussed in turn below.

The restrictions

(i) Paragraph 1 of Schedule 10 provides that no winding-up petition may be presented on or after 27 April 2020 pursuant to section 123(1)(a) of Insolvency Act 1986 ("**IA 1986**") in reliance on a statutory demand where that statutory demand was served between 1 March 2020 and 30 September 2020 ("**the relevant period**"). A creditor who wishes to establish that the company is unable to pay its debts for the purposes of section 122(1)(f) of IA 1986 will therefore have to rely on one of the other and less straightforward grounds in section 123 of the 1986 Act.

(ii) Even if a creditor would otherwise be able to establish one of the other grounds contained in section 123 of IA 1986 Act to show that the debtor company is unable to pay its debts, paragraph 2 of Schedule 10 nonetheless prohibits a creditor from presenting in the relevant period a winding-up petition in reliance on such grounds unless that creditor is able to satisfy a new twofold test. Both in the case of section 123(1)(a) to (d) of IA 1986 (unpaid statutory demand or unsatisfied execution), and in the case of section 123(1)(e) or (2) or IA 1986 Act (the court is satisfied of inability to pay debts on a cashflow or balance sheet basis), the creditor's right to present a petition is contingent on the creditor having reasonable grounds for believing that (a) coronavirus has not had a financial effect on the company, or (b) the relevant ground would apply even if coronavirus has not had a financial effect on the company. Paragraph 3 of Schedule 10 imposes equivalent restrictions on winding-up petitions presented against unregistered companies.

(iii) Schedule 10 introduces a number of measures which mean that these restrictions have a limited retrospective effect. In particular:

a. Paragraph 4 provides that, where a creditor presents a petition on or after 27 April 2020 but before the day on which the Schedule comes into force, the court has a broad discretion to make whatever order it thinks appropriate to restore the position to what it would have been had the petition not been presented if satisfied that the creditor presented the petition without meeting the twofold test.

b. Paragraph 7 provides that, where a creditor has managed to obtain a winding-up order on the basis that a company is unable to pay its debts on or after 27 April 2020 but before the day on which the Schedule comes into force, the court is to be regarded as having had no power to make the order it in fact made if the court would not have made the order had the restrictions then been in effect.

(iv) Even where a creditor is able to present a winding-up petition in the relevant period under the Schedule, paragraph 5 limits the court's jurisdiction to make a winding-up order. In broad terms, the court is only permitted to do so where it is itself satisfied that the facts by reference to which the relevant ground applies would have arisen even if coronavirus has not had a financial effect on the company.

Following the Government's announcement on 23 April 2020 of its plans to restrict the use of statutory demands and winding-up petitions in respect of debts unpaid due to the impact of COVID-19 and in light of the Bill's introduction to Parliament, these provisions have already, on a prospective basis, been the subject of the court's scrutiny. In *Re Saint Benedict's Land Trust Limited* [2020] EWHC 1001, the applicant companies sought to rely upon the restrictions in seeking an injunction to restrain the presentation of a petitions by local authorities in respect of national non-domestic rates and unpaid costs orders. In refusing the applications Snowden J found that the reason why the debts had not been paid was nothing to the do with the economic effect of the coronavirus.[1]

More recently, there have been cases involving applications for injunctions to restrain winding-up petitions where the court decided that the impending legislation was likely to bring about a change in the law which would prevent the presentation of petitions in circumstances covering the particular facts of those cases.[2] In granting injunctions in each of those cases, the court held that, on the facts, there was a sufficiently strong case that coronavirus had the necessary impact on the company's finances as envisaged by the proposed legislation.

1 Snowden J, it appears with the benefit of hindsight, incorrectly anticipated that the legislation would be limited to companies in specific sectors such as retail and hospitality and would relate to debts claimed by commercial landlords in respect of unpaid rent arrears. In fairness to the Judge this was a justifiable prediction in light of the Government's announcement and subsequent press release.

2 See *Travelodge Ltd v Prime Aesthetics Ltd* [2020] EWHC 1217 (Ch); and *Re a Company* [2020] EWHC 1406 (Ch).

In *Re a Company (Application to restrain advertisement of winding up petition) (2020)* [2020] EWHC 1551 (Ch), Judge Barber similarly granted injunctive relief by reference to the provisions of the impending legislation which was aimed at protecting companies affected by the pandemic as in the facts of that case. In particular, the Judge held that:

- The requirement in paragraph 5(1)(c) of Schedule 10, viz. that it "appears" to the court that coronavirus had "a financial effect" on the company before the presentation of the petition, was clearly intended to create a low threshold. The requirement, she held, is simply that a "financial effect" had to be shown and it was not necessary to demonstrate that the pandemic was "the" or even "a" cause of the company's inability to pay its debts.
- The language of paragraph 5(1)(c), which only requires that it should "appear" to the court that coronavirus had a financial effect, stood in contrast to the wording of paragraph 5(3) which stipulates that the court must be "satisfied" of certain matters and so was to be regarded as imposing a higher evidential threshold. The use of the phrase "it appears" indicated that the applicant company had to establish a prima facie case rather than prove the existence of a financial effect on the balance of probabilities.
- In relation to paragraph 5(3), at the hearing of the petition, the petitioning creditor bears the burden of proving that, even putting aside a financial effect resulting from coronavirus, the company would still be insolvent. Accordingly, in the context of an application for an injunction to restrain a petition, the court had to consider whether there was a real chance of a winding-up order being made on the basis that the respondent creditor would be able to "satisfy" the court that the grounds for winding-up would apply even if coronavirus had not had a financial effect.

Modifications to the IA 1986

Paragraphs 8 to 18 of Schedule 10 contain some important modifications to the IA 1986. At the forefront of these changes is the change in the date of the commencement of the winding-up based on petitions presented in the relevant period. Paragraph 9 provides that instead of the winding-up being deemed to commence on the date of presentation of the petition pursuant to section 129(2) of the IA 1986, the wind-up shall be deemed to start on the date of the winding-up order. Consequently, where a petition has been presented in the relevant period, the important protection provided by section 127 of the IA 1986 will not be available and so dispositions of the company's property between the date of presentation of the petition and the date of the winding up order will not be rendered void.

Other changes to the IA 1986 which are worthy of note are to the periods applicable to the avoidance of antecedent transactions in respect of liquidations based on petitions in the relevant period as follows:

(i) Paragraph 15 introduces an amendment to the calculation of the "relevant time" in section 240 of the IA 1986, being the period before the onset of insolvency in which transactions at an undervalue ("**TUVs**") and preferences are actionable. In the case of TUVs, the period begins with the later of: (a) 2 years before the day on which the petition was presented; or (b) 2 years and 6 months before the day on which the winding-up order was made. In relation to preferences, the period begins on the later of: (a) 6 months before the date of presentation of the petition; and (b) 12 months before the date of the winding-up order.

(ii) Paragraph 18 brings modifies the definition of the "relevant time" at which a floating charge is created for the purposes of avoiding it pursuant to section 245 of the IA 1986. In relation to floating charges granted to connected persons, the relevant time is one which falls within the period beginning on the later of: (a) 2 years before the presentation of the petition; or (b) 2 years and 6 months before the date when the winding-up order was made. In relation to other, unconnected persons, the period in which the relevant times falls begins on the later of: (a) 12 months on the day on which the petition was presented; or (b) 18 months before the date of the winding-up order.

Modifications to the Insolvency Rules 2016

Paragraphs 19 and 20 of Schedule 10 contain some modifications to certain provisions of the Insolvency Rules 2016 in respect of petitions which presented on or after the day on which the Schedule comes into force but before the end of the relevant period. In particular:

(i) Paragraph 19(2) provides that any provision in the Insolvency Rules which requires or permits notice, publication or advertisement of the petition does not apply until the court has determined that it is likely to make a wind-up order under section 122(1)(f) or section 221(5)(b) of the IA 1986 on grounds that the company is unable to pay its debts.

(ii) Paragraph 19(3) inserts into rule 7.5(1) of the Insolvency Rules (contents of winding-up petition) an additional requirement that the petition must contain a statement that the petitioner considers that the conditions of paragraphs 2(2) or (4) or 3(2) or (4) of Schedule 10 (financial impact of coronavirus – see above) have been met.

(iii) Paragraph 19(4) restricts the right to inspect the court file under rule 12.39(3) to (5) of the Insolvency Rules in respect of a petition which has been presented in the relevant period. In short, the persons who ordinarily may inspect the file shall not be permitted to do so until the court has determined in relation to the petition that it is likely to make a winding up order on the ground that the company is unable to pay its debts.

Comment

Taken together, these changes to the statutory demand and winding-up procedure render winding-up proceedings significantly less attractive for creditors and offer a corresponding measure of protection for debtor companies for the following reasons:

(i) The inability of creditors to rely on statutory demands means that it is likely to be more difficult for creditors to establish that a company is unable to pay its debts because they cannot point to the mere non-compliance with a statutory demand. Given that, in many cases, creditors will know very little if anything of the state of the company's finances, they therefore face a more difficult choice in deciding whether to present a petition on the basis that the company is truly insolvent or to issue proceedings under the CPR to recover the debt.

(ii) As a consequence of (i) above, creditors are likely to be deterred from a high-risk strategy of presenting a winding-up petition and instead will have to consider pursuing other insolvency procedures or avoiding formal litigation and insolvency procedures altogether and compromising the dispute by negotiation.

(iii) Under the temporary restrictions, obtaining a winding-up order requires a creditor to show much more than that there is a debt due and owing to it in excess of the threshold. The requirement to show reasonable grounds for believing that coronavirus has either not had a financial effect on the debtor company or that, if it has, it would not have made a difference to the company's inability to pay the debt due is easily prone to give rise to disputes which can be used by debtor companies to oppose the making of a winding-up order.

(iv) Even if a creditor can establish reasonable grounds for belief so as to entitle it to present a petition, the limit on the court's jurisdiction to make an order unless it is itself satisfied of the matters of which the creditor must only have had reasonable belief means that there is yet further scope for debtors to effectively oppose the making of a winding-up order. An obvious example is where prior to the COVID-19 outbreak the company was suffering from financial difficulties which its board regarded as only temporary. The court will have to grapple with the difficult question of whether the board's optimism was justified notwithstanding the company's pre-coronavirus position.

Finally, the amendments to the date on which the winding-up is deemed to commence will no doubt be welcomed by debtor companies striving to maintain ongoing trade in the teeth of a winding-up petition as they will no longer need to apply to court to validate payments in the period prior to the hearing of the petition. However, the change introduces greater risk that some trade creditors will be paid ahead of others and without prioritising the interests of the creditors as a whole. Arguably this change as a step too far: as highlighted above, the reforms restrict the scope for a creditor to present and winding-up petition and for the court to make a winding-up order. If those conditions can be satisfied, as they are likely to be in the case of truly insolvent companies, then there is good reason to preserve the protection provided by section 127 and the *pari passu* treatment of creditors.

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BARRISTERS

Temporary Suspension of Wrongful Trading Liability

Jamie Riley QC, Angharad Start and Emmanuel Sheppard

CIGA will temporarily suspend directors' liability for wrongful trading from 1 March 2020 to 30 September 2020 or as later extended ("**the Relevant Period**").[1] Wrongful trading is the liability imposed by Insolvency Act 1986 ss s214 (in liquidation) and s46ZB (in administration) for continuing to trade when present or past directors knew or ought to have concluded there was no reasonable prospect of avoiding insolvent liquidation. Where liability under ss 214 or 246ZB is triggered, the Court may require that person to make a contribution to assets unless satisfied that he took every step with a view to minimising the potential loss to the company's creditors he ought to have taken.

Section 12 of CIGA purports to give legislative effect to the announcement made by HM Government on 28 March 2020 in response to the unfolding economic crisis caused by the outbreak of COVID-19. In that announcement the Government proposed a temporary suspension of the wrongful trading provisions with a view to providing company directors with certainty and instilling confidence by allowing them to continue to trade during the pandemic crisis without the threat of liability for wrongful trading hanging over them.

Modifications to the application of the Insolvency Act 1986

On close scrutiny the temporary reforms introduced by CIGA do not suspend but rather modify and limit the wrongful trading provisions. In particular, the knowledge test to be applied remains unaltered. What is changed is the application of ss214 and 246ZB of the 1986 Act during the Relevant Period: Section 12(1) of CIGA directs the Court *"to assume that the person is not responsible for any worsening of the financial position of the company or its creditors that occurs during the relevant period"*. Therefore, there is no obligation for the director to demonstrate that the company's worsening financial position was due to the COVID-19 Pandemic. However, this does not mean that directors avoid liability in respect of any wrongful trading which may occur either side of the Relevant Period. In addition, where the company is financially distressed, during the Relevant Period, directors will still have to give active consideration to the prospect of ceasing trade and placing the company into an insolvency process. Section 12(4) excludes a range of companies from the suspension including: insurance companies, banks, electronic money institutions, investment banks, payment institutions, and securitisation companies, namely those listed in Schedule ZA1 of the 1986 Act. Building societies, friendly societies and credit unions are also exempt along with companies carrying on regulated activities under s4A FSMA.

Commentary

The underlying aim of this temporary restriction of the wrongful trading liability is that viable companies suddenly plunged into uncertainty by COVID-19 will be more likely to survive given the perception of the wrongful trading regime as the driver for directors to tip their companies into liquidation. In allowing courts to assume the directors have no responsibility for their company's worsening position during the Relevant Period, it is hoped that directors will continue to run their businesses. With the suspension announced by the Government, the hope was and continues to be that directors would feel less inhibited to take steps needed to keep the business afloat during the crisis by, for instance, drawing down on a facility when in other circumstances the unlawful trading regime would have required them to be more cautious and consider more closely the impact on the creditors. The practical reality, however, is that because the liability for wrongful trading either side of the Relevant Period is not removed, the temporary reforms are unlikely to have such an unshackling effect. As a largely retrospective measure it is unlikely to have influenced behaviour and liberated directors to make important decisions about the future operation of their companies during the period of the pandemic. Instead, the temporary "suspension" is more plausibly going to influence directors prospectively once CIGA has come into force. Even then, such an impact is necessarily narrow given the confines of the Relevant Period.

The Explanatory Notes to CIGA accept that the proposal shifts risk on to creditors. However, it considers that the risks are slight because wrongful trading cases are rarely taken forward principally due to the difficulties already confronting applicants in establishing liability and obtaining relief. Moreover, it is assumed that there will be sufficient deterrence in the remaining protections of the insolvency and enforcing regimes, for example the liability for fraudulent trading[2] and the disqualification regime under the Company Directors Disqualification Act 1986.[3] Ignoring for a moment whether the "assumption" in the Explanatory Notes is correct, the difficulty from the directors' perspective is that there is no correlative suspension of their duties under Companies Act 2006 or other fiduciary and common law duties. Where the company is insolvent or teetering on the precipice, those duties effectively shift from protecting the interests of members to those of the creditors as a whole and so directors still need to be wary of incurring personal liability for breach of duty and misfeasance under s212 of the 1986 Act. Payments are still potential preferences[4] and transactions at an undervalue or those engaged by s423 of the 1986 Act remain open to challenge. Payments of dividends or increasing directors' loans to get through the crisis still present risks. Whilst it is anticipated that claims for misfeasance or fraud will be met with arguments that any liability is purged because the acts complained of amount to wrongful trading in the Relevant Period, those directors who would have been discouraged from continuing by potential s214/246ZB liability are likely to remain equally concerned about personal exposure. Those less concerned are, it is said in some quarters, being given a licence to trade whilst insolvent without risk given the absence of any need to demonstrate COVID-19 connection to the company's deteriorating position.

1 CIGA section 12.
2 Pursuant to s.213 of the Insolvency Act 1986.
3 See Annex B 2.3 of the Explanatory Notes to the Corporate Insolvency and Governance Bill.
4 The periods for calculating the relevant time for the purposes of preferences and transactions at an undervalue are amended pursuant to Schedule 10 of CIGA in relation to liquidations based on winding-up petitions presented between 1 March 2020 and 30 June 2020.

The suspension seeks to secure a practical benefit with the noble aim of eliminating all the complicating aspects of COVID-19. Certainly, some complications that might otherwise have arisen will be avoided. Those defending wrongful trading proceedings often complain that the s214/246ZB assessment is an artificial process. The court and officeholders come to the circumstances which directors faced in the heat of the moment, with the luxuries of time, hindsight and less stressful conditions. Without the suspension, the uncertainty caused by COVID-19 would have otherwise further strained that tension between the carefully balanced prospective assessment made by the director at the time and the retrospective assessment which the court is required to make under s214/246ZB of the 1986 Act. For instance, directors are entitled to trade at a loss in anticipation of a future profit, with a distinction being made between a rational expectation of future profit to benefit creditors and trading in the hope that something would turn up.[5] This distinction would have become finer when factoring in the uncertainty surrounding the future period of depressed demand and social-distancing/lockdown measures. COVID-19 is also prone to complicate the assessment of what constitutes *"taking every step"* to avoid potential loss which would be required without the suspension. That assessment ordinarily involves preparing a business plan and ensuring accounting records are kept up to date with budget and cash flow forecasts.[6] The precipitous drop in demand which some businesses have faced has required severe revision to their projections and models. In addition, there would be a blurring of the important distinction which the court uses when assessing liability between the losses that resulted from the wrongful trading and those caused by pandemic related uncertainty.

However, while the suspension eliminates some complications, it has either maintained or even added others:

- In formulating their plans for the company, directors need to have regard for the flexibility of the Relevant Period which potentially may be extended.
- As observed above, the temporary modification merely absolves the director for the worsening position of the company during the Relevant Period. Therefore, it does not remove the obligation for the directors to consider whether to place the company into administration or liquidation if prior to or during the Relevant Period they knew or ought to have known that there was no reasonable prospect of avoiding liquidation.
- Although directors are encouraged to continue trading during the Relevant Period, they must simultaneously be prepared, as soon as the Period ends, to revert to the ordinary statutory requirement to take every step with a view to minimising the potential loss to the company's creditors.
- Directors face the difficult dilemma of balancing the prospect of continued trade during the Relevant Period with reduced liability for wrongful trading against their continuing duties to creditors which may sensibly lead in the direction of ceasing trade.
- Liquidators already grapple with the question of what is only ever an estimate of loss between dates, often on a number of different bases. This forensic task is now further complicated by the need to identify and exclude those losses attributable to the Relevant Period in wrongful trading claims at least. Inevitably, directors will embark on a similar exercise in seeking to reduce liability for misfeasance claims.
- There are bound to be other complications. For example, directors may be aware before the Relevant Period that the company could not avoid insolvent liquidation but wanted to avail themselves of the Relevant Period as a final throw of the dice. It remains to be seen whether, without more, the court will regard such use of the Relevant Period as wrongful trading. Another issue which may arise is where the directors knew prior to the Relevant Period that liquidation was inevitable, but the company's finances only started to worsen during the Relevant Period.

Conclusion

The temporary suspension of the wrongful trading regime is a misnomer; instead of a wholesale suspension of the regime, it merely serves to narrow the scope of relief to exclude the Relevant Period. In so doing, it is anticipated that it will not achieve of the aim of reducing the uncertainty thrown up by the COVID-19 financial storm. Instead, the measure has been received as something of a mixed blessing, complicating an already difficult area of law. From the directors' perspective, it is unlikely to instil in them the confidence to make important decisions about the ongoing trading of their companies during the pandemic. As for creditors, there is the concern that the temporary "suspension" amounts to a licence to trade while insolvent free of risk. In that regard, during the House of Commons Debate on 3 June 2020, Jonathan Djanogly MP noted the potentially chilling effect on bank lending. It remains to be seen if, indeed, the "licence" has just that consequence.

5 See *SoS v Gash* [1997] BCC 172.
6 See *Brooks v Armstrong; Re Robin Hood Centre Plc* [2015] EWHC 2289 (Ch).

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Insolvency Termination Clauses

Jamie Riley QC and James McWilliams

Introduction

One of the most significant changes effected by CIGA are the restrictions it imposes on the operation of termination clauses (known as 'ipso facto' clauses) in contracts for the supply of goods or services where the company to which those goods or services are supplied enters a relevant insolvency procedure. These restrictions are not temporary – indeed, insolvency termination clauses had been a focus of government attention as part of a consultation process in 2018 long before the current pandemic – and will therefore become a permanent fixture of our corporate restructuring law.

The new restrictions

The new restrictions, echoing equivalent provisions in Chapter 11 of the US Bankruptcy Code, are contained in section 14 of CIGA which creates section 233B of the Insolvency Act 1986 ("**the IA 1986**"). They add to the existing rules relating to essential suppliers as set out in section 233 and 233A of the IA 1986 Act. The new restrictions have three principal effects so far as contracts for the supply of goods or services to companies are concerned:

(i) Section 233B(3) provides that any provision in a contract for the supply of goods or services which provides for the contract or supply to be terminated or for "any other thing" to happen consequent upon the company becoming subject to a "relevant insolvency procedure" will cease to have effect. In other words, a supplier will not be entitled to withhold supply, to terminate the contract or exercise any other contractual right in the event that its counterparty enters a relevant insolvency procedure.

(ii) Section 233B(4) provides that any provision in a contract for the supply of goods or services to a company which gives the supplier a right to terminate the contract or the supply because of an event occurring before the start of the "insolvency period" may not be exercised during that period. In other words, a supplier will not be entitled to terminate a contract or supply for a breach of contract which occurred prior to the relevant "insolvency period". However, the supplier's contractual right to terminate is not prohibited where the trigger event occurs at any point after the relevant insolvency event has commenced.

(iii) Section 233B(7) prohibits a supplier from making it a condition of any supply of goods and services after the time when the company becomes subject to the relevant insolvency procedure, or to do anything which has the effect of making it a condition of such supply, that any outstanding charges in respect of a supply made to the company before that time are paid. In other words, a supplier will not be able to make a condition of future supplied that pre-insolvency arrears are paid.

Materially, the restrictions contained in section 233B apply not simply to contracts entered into after the coming into force of CIGA but also to existing contracts.

What is a "relevant insolvency procedure"?

The relevant insolvency procedures caught by section 233B are listed at section 233B(2). They are as follows:

(i) A moratorium under the new Part A1 coming into force;

(ii) The company enters administration;

(iii) An administrative receiver of the company is appointed;

(iv) A voluntary arrangement under Part 1 of the Insolvency Act 1986 takes effect in relation to the company;

(v) The company goes into liquidation;

(vi) A provisional liquidator of the company is appointed; or

(vii) A court order is made under section 901C(1) of the Companies Act 2006 in relation to the company.

What is the "insolvency period"?

The insolvency period for the purposes of section 233B is defined by section 233B(8) as the period beginning when the company becomes subject to the relevant insolvency procedure and ending:

(i) In the case of a moratorium under Part A1, when the moratorium comes to an end;

(ii) In the case of a company entering administration, when the appointment of the administrator ceases to have effect under paragraphs 76 to 84 of Schedule B1 or pursuant to an order under section 901F of the Companies Act 2006;

(iii) In the case of the appointment of an administrative receiver of the company, when the receiver or any successor to the receiver ceases to hold office without a successor being appointed;

(iv) In the case of a voluntary arrangement approved under Part 1 taking effect in relation to the company, when the arrangement ceases to have effect;

(v) In the case of the company going into liquidation, when the liquidator complies with sections 94(2), 106(2) or 146(3) of the Insolvency Act 1986 or when the appointment of the liquidator ceases to have effect pursuant to an order under section 901F of the Companies Act 2006;

(vi) In the case of the appointment of a provisional liquidator, when the provisional liquidator or any successor to the provisional liquidator ceases to hold office without a successor being appointed; and

(vii) In the case of the making of a court order under section 901C(1) of the Companies Act 2006 in relation to the company, when the order takes effect or the court decides not to make such an order.

What is "any other thing"?

Neither section 233B nor CIGA generally seeks to define "any other thing" for the purposes of section 233B(3). The breadth of that wording is, however, obvious and it would appear to extend to the exercise of any contractual right triggered upon an event of insolvency. An obvious example, and indeed the only one provided by the government in its Explanatory Notes to the Bill that became CIGA, is a clause which changes payment terms.

What about the existing essential supplier restrictions?

The Insolvency Act 1986 already contains at section 233A similar, albeit narrower, restrictions as to the right of a supplier to terminate where what is being supplied falls into the definition of "essential supplies". The operation and scope of those restrictions falls outside the scope of this commentary but the material point is that the restrictions contained at section 233B(3) and (4) do not apply in relation to a contractual provision if that provision has already ceased to have effect under section 233A(1).

Are there exceptions?

There are numerous types of companies and contracts excluded from the scope of the restrictions set out in the new schedule 4ZZA of the Insolvency Act 1986 introduced pursuant to a new section 233B(10) under section 14 of CIGA.

So far as excluded companies are concerned, subject to the particular requirements of schedule 4ZZA, these include entities operating in the sphere of financial services such as insurers, banks, electronic money institutions, investment banks and firms, payment institutions, operators of payment systems, recognised investment exchanges, securitisation companies and companies whose activities are overseas.

As for excluded contracts, these include (again subject to the particular requirements of schedule 4ZZA) a wide variety of financial services contracts, securities financing transactions, derivative, spot contracts, capital market investment agreements, and public-private partnership agreements.

Finally, section 15 of CIGA provides for a temporary exclusion for suppliers which are small entities as at the time when the company in question becomes subject to a relevant insolvency procedure between the coming into force of section and 30 September 2020. The test for determining whether a supplier is a "small entity" for the purposes of the temporary exclusion is primarily set out in section 13(4) of CIGA.[1] According to the test, where the supplier is beyond its first financial year at the time when the company becomes subject to a relevant insolvency procedure, it must satisfy at least two of three conditions, namely: (1) the supplier's turnover is not more than £10.2 million; (2) the aggregate total for the supplier's assets recorded in its balance sheet is no higher than £5.1 million; and (3) the supplier has 50 or fewer employees.

1 Further, specific parameters of the definition are contained in subsections 13(5) to 13(10).

If the restrictions do apply, when can a supplier terminate the contract?

Where the restrictions apply and the provision of a contract ceases to have effect under section 233B(3) or an entitlement under a provision of a contract is not exercisable under section 233B(4), the supplier may still terminate the contract in certain circumstances. They are set out at section 233B(5) and include:

(i) Where the office-holder appointed over the company as part of a relevance insolvency procedure consents to termination;

(ii) In any other case, where the company consents to termination; or

(iii) The court is satisfied that the continuation of the contract would cause the supplier hardship and grants permission for the supplier to terminate the contract.

Conclusion

Of all the changes in CIGA, the prohibition on insolvency termination clauses is likely to one of the most significant. In terms of the policy, the introduction of a ban on ipso facto clauses aligns UK insolvency law more closely with other jurisdictions. On a practical level, these restrictions provide valuable further protection in enabling struggling companies to maintain the commercial lifeblood of key supplies. In particular, the changes will provide valuable assistance to those companies which are subject to insolvency procedures whose purpose is to rescue the company as a going concern. However, for suppliers of goods and services (encompassing both commercial and various financial agreements), they represent a very significant curtailment of their freedom of contract. As noted above, suppliers may nonetheless seek permission to terminate if they can satisfy the court that the enforced continuation of the contract would lead to “hardship”. However, the new provisions do not contain any definition of “hardship” nor do they offer any guidance as to what the term means in this context. Therefore, good or bad, the restrictions seem likely to generate disputes in due course while it is left to the courts to shape the meaning and effect of such important but undefined concepts that are readily open to interpretation.

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Barristers

Reserved Power

Angharad Start and Emmanuel Sheppard

Design

The design of sections 20-27 CIGA is to create a time limited provision to permit the Secretary of State (SoS) to temporarily amend corporate insolvency and related legislation (primary and secondary) through regulations made by statutory instrument (SI). These provisions will enable the government to react quickly to the COVID-19 pandemic's impact on business so as to protect otherwise viable businesses from being forced into insolvency proceedings, to create flexibility in insolvency and restructuring processes, to modify the liability and duties of those with corporate responsibility if necessary and temporarily modify the insolvency related enforcement regime so as to mitigate the impact of the pandemic on business.

The breadth and limits of the power

The legislation which the SoS may temporarily amend is the Insolvency Act 1986 (except provisions relating to individual insolvency or bankruptcy), Part 26A of the Companies Act 2006 (arrangements and reconstructions for companies in financial difficulty), the Company Directors Disqualification Act 1986, CIGA itself, related subordinate legislation, the Cross-Border Insolvency Regulations 2006 (S.I. 2006/1030), and Regulation (EU) 2015/848 on insolvency proceedings (per section 27).

Section 23 imposes a duty on the SoS to keep changes made under review and revoke them when no longer necessary or revise when appropriate due to changed circumstances.

Changes made become effective immediately subject to a "made affirmative" process requiring parliamentary approval within 40 days in default of which the change ceases though the SI may be remade (section 26). They last for a maximum of 6 months but can be extended (section 23). The power itself expires on 30 April 2021 unless that date is extended by SI. The date may not be extended beyond 30 April 2022 but such an extension can be made more than once (section 24). Temporary changes may be revoked through an SI subject to a negative resolution of either House of Parliament (section 26).

Section 21 prescribes the limited purposes for which the power may be used, namely:

(1) To reduce or assist in reducing the number of companies entering insolvency processes or restructuring procedures,

(2) To mitigate the impact of an increased number entering those procedures, or

(3) To mitigate the effect of the insolvency regime on directors and others with corporate responsibilities where businesses are facing difficulties due to the impact of the COVID-19 pandemic.

Section 22 imposes restrictions on the use of the power:

(1) The impact of proposed amendments on any likely affected person (such as a creditor or employee) must first be considered,

(2) The amendments made must be proportionate to the difficulties faced,

(3) The desired consequence must require legislative change, and

(4) The power may not be used where the proposed amendment could be made using existing legislation sufficiently quickly.

The power cannot be used to create any new criminal offences or civil penalties or to create or increase fees. The power may be used to modify the circumstances under which a person is guilty of an existing offence or civil penalty.

Commentary

It is said there is no present intention to use this power but there is concern to have a legislative structure ready to move rapidly to mitigate the impact of COVID-19 on a struggling economy. It is self-evidently desirable. The strength of the government's majority is likely to curb any risk of temporary amendments evaporating for want of approval. It is also difficult to see how the section 22 restrictions could be monitored effectively by the Courts save in extreme circumstances. All in all, this is thought a prudent and supportive step but its reception will obviously depend upon its implementation and whether creditors, debtors and those with corporate responsibility feel the protection is proportionate and sufficient.

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Meetings and Filings

Angharad Start and Emmanuel Sheppard

CIGA includes various provisions facilitating company meetings in circumstances of lockdown and social distancing even where these may override legal requirements and a company's articles. These provisions are set out in sections 37-40 and Schedule 14 to CIGA. It is designed to apply retrospectively and prospectively so that all proceedings at meetings held between 26 March and 30 September 2020 ('the Relevant Period') may be validated. The provisions may be amended subsequently whether to shorten the Relevant Period or extend it by periods of up to 3 months until 5 April 2021. The Secretary of State is further permitted to make Regulations regarding the form of all notices and other documents relating to meetings together with the method and timing of sending the same even where these may amend existing law and override provisions of a company's articles.

Changes to meetings

Meetings Generally

CIGA in Schedule 14 specifically provides that in relation to all meetings of shareholders and classes of shareholders of UK companies:

(1) Meetings do not need to be held in a particular place and may be virtual;

(2) The requisite quorum does not need to be present in the same place;

(3) Votes can be cast by electronic or other methods; and

(4) Those attending the meeting have no right to attend in person or to participate other than by voting or using a particular method of voting.

Annual General Meetings (AGMs)

Where companies were required either by law or their constitution to hold their AGM during the Relevant Period, that meeting can now be held at any time before the end of the Relevant Period. Accordingly, unless the date is altered by subsequent regulations, companies have until 30 September 2020 to hold AGMs and present public companies' accounts to members. Listed companies need to exercise caution before postponing AGMs given the potential for share allotment and pre-emption waiver authorities and approvals to expire.

Changes to Filing

Company Filings Generally

Sections 39-40 of CIGA enables the Secretary of State to make Regulations extending various filing dates for documents including accounts, the registration of charges, director and secretary appointments and resignations and confirmation statements. Those extensions are limited to up to 42 days and 12 months respectively, where the original requirements were 21 days and 3, 6 or 9 months.

Public Companies Filing Accounts and Financial reports

By section 38 of CIGA, public companies due to file accounts in the Relevant Period now have until 30 September 2020 or, if earlier, 12 months after their accounting period. Those with shares trading on public markets must have regard for the market rules.

Commentary

Meetings

Whilst the Companies Act 2006 already permits shareholders to attend, vote and speak at company meetings by electronic means, there were concerns that a virtual meeting may not be valid nor the business therein conducted. Various provisions of the Act pointed to the need for a physical meeting, for example the need to specify a place in the notice of meeting. There were also concerns there would be no sufficient quorum physically present in one place. Despite this, entirely virtual AGMs had been held. These pragmatic proposals from the Government provide some reassurance that actions companies may already have taken from 26 March 2020 may be retrospectively ratified in law. The question of whether a company can hold a "hybrid" meeting if its articles have not been amended specifically to provide for this has been clarified for the Relevant Period. Shareholders rights are thus preserved without exposing directors to liabilities for steps requiring shareholder endorsement.

There will be necessary practical considerations for virtual and hybrid meetings. Rules should be set in advance for how virtual and hybrid meetings will proceed including how the right to speak and vote should be exercised. For the meeting, and its business to be valid, those organising the same must ensure that all participants can see/hear and be seen/heard whether as a list of participants or on camera. The technology will need to be sufficient to that end for the participation of all those entitled and for the duration of the meeting. The chair of the meeting must enable a method to ensure people do not speak over each other and all those who wish to speak are equally able to do so.

Filings

The measures are designed to prevent the unfair imposition of financial and criminal penalties against directors or the company being struck off unfairly due to the impact of COVID-19 on business. The Companies Act 2006 generally requires the accounts of a public company to be filed within six months of the end of the accounting period so these are welcome extensions.

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