COVID-19 and Insolvency Law: Key Implications of the Corporate Insolvency and Governance Bill, Part II

The COVID-19 pandemic has caused unprecedented disruption to the economy and to businesses, many of whom are now facing significant financial difficulty. The Government presented the Corporate Insolvency and Governance Bill to Parliament on 20 May 2020 ("the Bill"). The Bill includes several provisions designed to guard against a deluge of insolvencies during this period and, if enacted, will operate retrospectively.

This article is a brief guide to the new provisions introduced by the Bill.

Company Moratoriums

Companies that are likely to become insolvent will be given 20 business days to restructure or seek investment without the threat of creditor action, extendable to 40 business days by filing a notice and certain documents at court. Further extensions will be possible with the agreement of creditors and by an order of the court.

Which companies are eligible?

Any company is eligible to obtain a moratorium, unless it is an excluded company. Excluded companies include:

- Any company with a moratorium already in force on the filing date, or where a moratorium was in force at any time during the 12-month period ending with the filing date;
- Any company subject to an insolvency procedure on the filing date for the moratorium, or a company subject to a voluntary arrangement or in administration at any time during the 12-month period ending with the filing date;
- Insurance companies;
- Banks;
- Electronic money institutions;
- Investment banks and firms;
- Companies that are party to market contracts or subject to market charges;
- Companies that are participants in designated systems;
- Authorised payment institutions, small payment institutions and registered account information service providers;
- Operators of payment systems and infrastructure companies;
- A recognised investment exchange, a recognised clearing house or a recognised central securities depository (CSD);
- Securitisation companies;
- Parties to capital market arrangements;
- Public-private partnership project companies;
- Certain overseas companies.

How does a company obtain a moratorium?

For all eligible companies (except those subject to an outstanding winding-up petition and overseas companies), the directors of the company must file the following with the court:

- A notice that the directors wish to obtain a moratorium;
- A statement from a qualified person (the proposed monitor) that the person is a qualified person (i.e. a person qualified to act as an insolvency practitioner) and consents to act as the monitor;
- A statement from the proposed monitor that the company is an eligible company;
- A statement from the directors that in their view the company is or is likely to become unable to pay its debts; and
- A statement from the proposed monitor that, in the proposed monitor's view, it is likely that a moratorium for the company would result in the rescue of the company as a going concern.

In the case of a company subject to an outstanding winding-up petition, the directors must file the same documents listed above. However, the court will only grant the moratorium if it is satisfied that a moratorium would achieve a better result for the company's creditors as a whole than would be likely if the company were wound up without first being subject to a moratorium. The moratorium must therefore be granted by the court in such a case, unlike in the case of an eligible company that is not subject to an outstanding winding-up petition.

What protections will the moratorium provide?

During the moratorium, the potential for insolvency proceedings to be brought against the company is restricted. Of particular significance, no petition can be presented for the winding up of the company (except by the directors) and no order may be made for the winding up of the company (except on a petition by the directors). There are also restrictions relating to voluntary winding up and the appointment of administrators and administrative receivers.

The moratorium also restricts enforcement and legal proceedings that can be taken against the company. The Bill contains several provisions, including that no steps may be taken to enforce any security over the company's property (save in certain exceptions relating to collateral security charges and securities created under a financial collateral arrangement). Further, no proceedings may be instigated against the company or its property other than in the employment tribunal and any instigated with the permission of the court.

Companies or directors making use of the moratorium procedure must note a few things:

- During the moratorium, the company must publicise on its premises, its websites and every business document it issues that a moratorium is in force in relation to the company, and the name of the monitor.
- Although the company will remain under the control of its directors during the moratorium, the process will be overseen by a monitor who must be a licensed insolvency practitioner.
- The moratorium will come to an end at any time in which the company enters into an insolvency procedure or enters into a compromise or arrangement (i.e. if the court sanctions a compromise or arrangement).

Restructuring plans

The Bill introduces a new restructuring plan. It is based on the existing scheme of arrangement procedure, and is similar to Chapter 11 bankruptcies in the USA with the potential to "cram down" across classes of creditors. It can bind both secured creditors and unsecured creditors.

The plan will not be limited to insolvent companies. Creditors will vote on the plan in separate classes, and it will require the approval of a minimum of 75% in value in each class.

The court must grant final approval of the plan if it feels the plan is just and equitable, and the plan can be approved even where one or more classes vote against it.

Supplier termination clauses

Suppliers will often stop supply to an insolvent company, or one undergoing restructuring. Further to the existing measures, the Bill seeks to prohibit suppliers from stopping supply by reason of the company's insolvency, provided that the suppliers continued to be paid for. It also prevents suppliers from amending the terms of the relevant contract to force increased payments.

Indeed, supply contracts often permit the supplier to do this, but such supplies may be important to allow the company to continue trading. Suppliers can be relieved of the obligation to continue supplying if it causes hardship to their business. There is also a temporary exception for small company suppliers.

Wrongful Trading

The Bill temporarily suspends the effect of wrongful trading provisions for four months, with retrospective effect, from 1 March to 30 June 2020 (or one month after the coming into force of the Act, whichever is later). Liquidators and administrators will be unable to bring claims against directors personally, and the effect would appear to be to excuse liability for an increase in net deficiency during the relevant period. However, it should be noted that the suspension of wrongful trading liability does not give directors complete free rein – they are still under the various other directors' and fiduciary duties, and a director who was wrongfully trading prior to the relevant period will still potentially face liability.

The wrongful trading suspension does not apply to companies that are excluded from being eligible for a moratorium, except for companies that are ineligible for a moratorium on the ground of a current moratorium being in force or because they are subject to insolvency procedures.

Winding-up Petitions

The Bill also introduces temporary provisions to protect companies in difficulty as a result of coronavirus from being wound-up.

A creditor cannot present a winding-up petition from 27 April 2020 to 30 June 2020 (or one month after the coming into force of the Act, whichever is later) unless the creditor has reasonable grounds to believe that: (a) coronavirus has not had a financial effect on the company; or (b) the ground on which the creditor relies to wind-up the company would have arisen even if coronavirus had not had a financial effect on the company. The Bill also introduces a prohibition on winding-up petitions based on statutory demands if the statutory demand was served between 1 March 2020 and 30 June 2020.

Coronavirus will have had a "financial effect on the company" if and only if the company's financial position worsens in consequence of, or for reasons relating to, coronavirus. We have already seen how the court may approach this issue, albeit prior to the publication of the Bill. After the Business Secretary set out similar proposals on 23 April 2020, Snowden J in *Re Saint Benedict's Land Trust Ltd* [2020] EWHC 1001 (Ch) dealt with a late-in-the-day submission that the respondents were suffering from cash flow issues as a result of coronavirus. At [84], Snowden J noted that "*it seems… the restrictions… will only apply where the reason that the company is unable to pay its debts is due to the coronavirus*". Our Chambers colleague, Olivia Wybraniec, has analysed the judgment further here.

Directors should note that this measure has been carefully worded to ensure that companies which are insolvent due to reasons other than coronavirus can still be wound-up during this period.

Filing requirements

Extensions of time for filing documents at Companies House have already been made. The Bill allows the Secretary of State to, temporarily, extend further the deadlines. The extended period for such filing must not exceed 42 days in a case where the existing period is 21 days or fewer, or 12 months in a case where the existing period is 3, 6 or 9 months.

To read Part I of Chambers' series on the insolvency reforms, please click here.

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2 June 2020