3
HARE COURT

COVID-19 and Corporate Insolvency –

Initial Indications on the Ban on Statutory Demands and Winding Up Petitions

The economic consequences of the COVID-19 pandemic are putting incredible pressures on companies of all kinds and sizes. The UK Government has been at pains to signal its support for business during the COVID-19 pandemic, most notably the furloughing scheme and company loans announced by the Chancellor, and further announcements by the Business Secretary seeking to reduce the burden on businesses and keep companies running.

On 23 and 25 April 2020 the government confirmed that it would take steps to protect high street shops and other companies from aggressive rent collection by implementing a temporary ban on the use of statutory demands and presentation of winding up petitions "where a company cannot pay its bills due to coronavirus". This article will look at what we know so far about the temporary ban, and consider the comments of Snowden J in respect of submissions based on financial hardship caused by COVID-19.

The Proposed Temporary Ban on Statutory Demands and Winding Up Petitions

The Business Secretary announced on 23 April that high street shops and other companies under strain would be protected from aggressive rent collection during the coronavirus pandemic.

In response to this need, it was announced that the government would be temporarily banning the use of statutory demands made between 1 March and 30 June 2020, and winding-up petitions presented between 27 April and 30 June 2020, where a company cannot pay its bills due to coronavirus.

Although the stated objective implied the government's measures would provide protection from unfair practices in respect of commercial rents only, the proposed measures are worded in wider terms. The 'note to editors' accompanying the announcement states that in relation to any winding-up petition claiming that a company is unable to pay its debts, the court must first review why that is, and that the new law will not permit petitions to be presented or winding-up orders to be made where the company's inability to pay is the result of COVID-19.

These measures will be included in the Corporate Insolvency and Governance Bill, which is yet to be released in draft or presented to Parliament.

Comments from the Chancery Division

Although the ban on statutory demands and winding up petitions has not yet passed into law, it has already been the subject of judicial comment by Snowden J in Shorts Gardens LLP v London Borough of Camden Council [2020] EWHC 1001 (Ch), handed down on 27 April 2020, which provides valuable indications to both creditors and debtors on the court's likely approach to the measures.

On 7 April 2020 the court heard oral argument on behalf of two related companies who had applied to restrain the presentation of winding up petitions against them. The applicants sought injunctive relief on the basis that the debts were genuinely disputed on substantial grounds or subject to cross-claims; and further that it was inappropriate for winding up petitions to be proceeded with until the coronavirus pandemic had been brought under control and the UK released from lockdown. After the draft judgment

was circulated but shortly before being formally handed down, the applicants filed further evidence relying on the ministerial statement of 23 April 2020 that statutory demands and winding up petitions would temporarily be banned, and sought to rely on new witness statements from the companies' directors, which asserted that the companies were in financial difficulty as a result of COVID-19. The late evidence led Snowden J to hear further submissions before giving final judgment.

Counsel for the applicants emphasised the contemplation of a wider ban on winding up-petitions, derived from the references in the announcement to 'other companies under strain' and to 'any winding up petition', which would require court to review why a company is unable to pay its debts. The applicants' counsel accepted that the judge had to make a decision on the law as it stands, but submitted that in light of the government announcement on temporary bans and the new evidence before the court, the judge could and should exercise his discretion and find that it was just and equitable to grant an injunction against presentation of the winding-up petitions.

Snowden J commented that "it seems overwhelmingly likely that the proposed legislation will be limited to companies in certain identified sectors of economic activity, and to relate to statutory demands and petitions based upon claims by landlords for arrears of rent" (emphasis added). The judge accepted that the announcement might suggest a wider prohibition that that, but that the prohibitions would not apply in cases such as the applicants', who were not retail or hospitality tenants, and in whose case the petitions were not based on rent arrears but court orders and longstanding national non-domestic rates arrears under liability orders to local authorities.

Additionally, Snowden J asserted that the government announcement suggests the application of some threshold test, whereby the temporary ban would only apply where the reason that the company is unable to pay its debts is due to coronavirus – although it was accepted that the application for that test is unclear. However, in the case in hand, it was noted that the additional witness statements did not actually contend the applicants were unable to pay the petition debts as a result of the effects of the coronavirus nor any credible details to support such a conclusion, but merely contained sweeping statements about the economic effects of the coronavirus. In this matter, the majority of the unpaid debts pre-dated any impact of coronavirus, and had previously been contested for completely different reasons. Snowden J further commented that the new evidence of financial hardship as a result of the pandemic was a "complete volte face" from the position put forward at the first application hearing (which took in the course of the national lockdown) which was that the companies were not facing liquidity or operational challenges as a result of the global pandemic.

Dismissing the applications to restrain presentation of the petitions, Snowden J concluded that the new submissions based on coronavirus-related financial difficulties were "entirely opportunistic and not credible. The reason [the applicants] have not paid the debts that they owe has nothing to do with the coronavirus, and they are not the sorts of entity owing the types of liabilities which the proposed legislation seems to be intended to protect. I therefore see no reason to exercise any discretion in favour of the applicants based on upon the prospect that legislative measures are to be introduced to assist more deserving companies experiencing genuine financial hardship caused by the effects of the COVID-19 pandemic."
Snowden J also dismissed a related submission by the applicants premised on the impact of coronavirus: since the court system is under strain due to the pandemic, any challenges to the liability orders on which the petitions were based would only proceed through the courts very slowly, and that it would be unjust for the applicant companies to face winding up proceedings before they had the chance to exhaust their challenges to the liability orders. This point too was given short shrift by the judge, identifying that no such challenges has so far been made, there was no suggestion there was any legitimate basis for challenging the liability orders in the future, and any meritorious arguments on that basis could be advanced at the hearing of the petition.

What guidance can we take from Snowden J's comments

The judgment of Snowden J suggests that the courts are not going to allow companies to rely on the COVID-19 epidemic as a get-out-of-jail-free-card to avoid winding-up petitions. Although the judge's comments are non-binding, and crucially made before the precise terms of the measures are known or implemented, Snowden J suggests some guidelines as to how the court will determine whether the temporary ban applies. These are that the ban is intended to protect only those companies whose inability to pay their debts arises due to the effects of coronavirus; the effect of the coronavirus on the

company should be clearly explained; the effect of the pandemic on the company should meet a certain threshold; and the timing that the debt arose is relevant to whether the ban applies.

Prospective petitioning creditors will certainly welcome the indication that companies shouldn't be able to avail themselves of the protection for debts that pre-date the COVID-19 crisis, and that the company will have to explain how it is specifically affected by the pandemic.

However, Snowden J's comment that the protection will apply only to landlords' demands against retail and hospitality tenants raises concern that the intended measures could be too narrowly focussed to meet the pressing needs of companies trying to survive this period. Given the uncertain but pessimistic economic forecast, it is easy to see how industries other than retail and hospitality, and business liabilities other than payment of rent, will be directly and negatively affected by the pandemic. If the strict focus on commercial tenancies is borne out in the legislation, many of the businesses the government has pledged to support might find themselves denied the protection and breathing space they need through the temporary ban.

Until the precise terms of the legislation are known, judicial discretion is capable of examining the facts of each case and determining whether a statutory demand should be made or a winding-up petition presented in the current circumstances. Those contemplating making statutory demands or presenting winding up petitions should consider whether there is a legitimate COVID-19 issue affecting the debtor company's ability to pay; and those companies seeking to rely on the pandemic to avoid winding-up must clearly set out how the current situation is affecting them.

As with so many of the proposed measures announced to support businesses though the coronavirus pandemic, Parliament and the courts are going to have to tread a careful line between protecting business interests in these challenging times, and deterring opportunism by companies seeking to avoid their liabilities.

Written by Olivia Wybraniec, Barrister of 3 Hare Court Chambers
11 May 2020