TECHNICAL ALERT

CORPORATE INSOLVENCY AND GOVERNANCE BILL

The UK Government has published its '**Corporate Insolvency and Governance Bill' ('CIGB')** in order to help support businesses through the economic impact of COVID-19. The CIGB has been fast tracked "to give companies breathing space and keep trading while they explore options for rescue."

The CIGB sees a number of additions to the UK's corporate and insolvency framework, some temporary to provide for specific Covid-19 effects and others are long term tools:

Permanent measures[1]

- Moratorium – to provide a breathing space for eligible companies to seek the rescue of the company as a going concern (E&W , NI and Scot). (Sch. A1 of the Insolvency Act 1986 is repealed).
- Arrangements and reconstructions for companies in financial difficulty – the introduction of a new rescue tool as an additional rescue process, also available to companies in administration and liquidation.
- Termination clauses in supply contracts – the protection of most supplies and services etc. in all insolvency processes, expansion of S233 which protects "essential" supplies

Temporary measures

- Wrongful trading – the temporary suspension of personal liability for directors while they make their best efforts to continue to trade during the period associated the COVID-19 pandemic (with retrospective application from 1 March 2020) .
- Winding-up petitions – the temporary prohibition of petitions on the basis of statutory demands and the temporary restriction on winding-up petitions and orders being made as a result of Covid-19 financial difficulties.
- Power to amend corporate insolvency or governance legislation – temporary relaxing of filing requirements to facilitate the administration of company filings during the restrictions imposed due to Covid-19.
- Meetings and filings –the temporary extension of time periods and for providing information to registrar etc.

The CIGB can be accessed here.

R3 will be producing practical guidance to members on the changes being implemented once the technical committees have had sufficient time to digest the contents of the CIGB. In the meantime, R3's Technical Team and General Technical Committee have provided a high level overview of elements of the CIGB, which can be found below.

[1] *Temporary adaptations to the Permanent Measures – apply until the later of 30 June 2020 or one month from the Act coming into force*

The Moratorium
This is a new procedure under the Insolvency Act 1986 (new Part A1)

The moratorium is a 'debtor in possession' process and provides a limited payment holiday in respect of certain debts and restricts other insolvency proceedings, enforcement and legal proceedings from being initiated or continued against the company. The company cannot obtain credit over a certain threshold without disclosing the existence of the moratorium, and there are other restrictions, for example, on granting security and paying pre-moratorium debts during the period for which the moratorium is in force. However, debts incurred during the limited payment holiday must continue to be paid.

Directors can obtain a moratorium by filing relevant documents in court (there is no court hearing). However, if there is an outstanding winding up petition, or it is an overseas company, the directors will have to apply to court for the moratorium and the court will only make an order where it is satisfied that the 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 in a moratorium). (There are some temporary relaxations of the conditions for obtaining a moratorium until one month after the CIGB comes into force.

The moratorium will be for an initial period of 20 business days. This can be extended by the directors once for a further period of 20 business days by the filing of relevant papers in court; with creditor consent for a period of up to one year; or by the court to a date set at its' discretion. The moratorium may also be extended automatically where consideration of CVA proposals is pending and the court may also extend it where there is an application for a scheme of arrangement, or a new restructuring procedure to be introduced by the CIGB (see further below)

Certain companies in regulated markets are excluded from being able to access the moratorium, for example, banks and insurance companies. There are also certain exemptions to the impact of the moratorium in relation to a long list of financial services contracts, for example, bank loans will remain payable during the moratorium. Certain other debts are to be paid during the moratorium (including the monitor's fees (see further below)).

During the moratorium a monitor is appointed by the company or court (as applicable). The monitor must be a licensed insolvency practitioner and they will be an officer of the court. Joint monitors are permitted. The monitor must consent to their appointment, and state that the company is an eligible company and that, in their view, <u>it is likely that a moratorium for the company would result in the rescue of the company as a going concern</u>. This statement is adjusted for a temporary period until one month after the CIGB comes into force to take into account that rescue would be possible were it not for any worsening of the situation for reasons relating to coronavirus.

The monitor does not displace management but monitors the company's affairs during the moratorium for the purpose of ensuring that his/her view remains that it is likely that the moratorium will result in the rescue of the company as a going concern.

A company will not be eligible to obtain a moratorium by filing or lodging documents at court if it is:

(a) subject to an outstanding winding-up petition*, or
(b) an overseas company.

[this is relaxed until one month after the CIGB comes into force to allow director appointments even if a petition has been presented.]*

If the company is subject to a winding-up petition, the directors of the company may apply to the court for a moratorium for the company. The court may make an order under subsection only if it is satisfied that a moratorium for the company 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).

Further to note a company will not be eligible to obtain a moratorium if

- It is subject to an insolvency procedure,
- if, at any time in the period of 12 months ending with the filing date, a moratorium of the company was in force,*
- if, at any time in the period of 12 months ending with the filing date, the company was subject to an insolvency procedure.*

[this is relaxed until one month after the CIGB comes into force to allow director or court appointments even if the company was subject to a moratorium, administration or CVA in the prior 12 months]*

As part of the application process, the directors are required to state that they wish to apply for a moratorium and that the company is, or is likely to become, unable to pay their debts.

The monitor has to re-state his/her view as to the likely rescue of the Company in each proposed extension of the moratorium. The monitor also plays an important role bringing the moratorium to an end, either where it cannot pay the moratorium and other debts due, or it has either achieved its purpose or the purpose can no longer be achieved. Where there is a failure of the directors to co-operate with the monitor, then the moratorium can also be terminated by the monitor. There is a general ability for an application by creditors, directors, or members of the company to challenge the actions of the monitor, where the applicant can establish it has been unfairly harmed. The monitor's fees are to be agreed by the company and may also be the subject of scrutiny at a later date by a liquidator or administrator. In addition, there are provisions for the monitor to be replaced by the directors upon an application to the court.

Section A18(3) makes it clear that there is no payment holiday for monitor remuneration incurred in the course of the moratorium, and therefore is to be paid as it falls due. However, this does not apply to pre-entry moratorium work to determine that a rescue is likely and this will need to be paid up-front, or in weekly instalments or similar.

The accompanying explanatory notes to the CIGB emphasise that the moratorium tool is to be used as a gateway to a rescue of the company; thus, it is not intended to be used as a delaying tactic / gateway to administration or liquidation and there are criminal penalties to address any abuse of the process.

Monitor statements are amended to take into account the impact of Covid-19 i.e. it is likely that the company would result in the rescue of a going concern ***or would do so if it were not for any worsening of the financial position of the company for reasons relating to coronavirus.*** This applies to statements made in relation to entry, extension and termination of a moratorium by a monitor.

Arrangements and reconstructions for companies in financial difficulty
This is a new restructuring procedure under the Companies Act 2006 (new Part 26A)

Schedule 9 contains provision about arrangements and reconstructions for companies in financial difficulty. These provisions to facilitate a compromise or arrangement may be disapplied to exclude certain companies, such as regulated entities (i.e. banks, investment firms, insurers etc), but at present Part 26A of the Companies Act applies to all companies notwithstanding the fact that many regulated entities already have their own special resolution regimes. The new compromise or arrangement is also available to overseas companies which are liable to be wound up in England.

A compromise or arrangement under Part 26A is only available where the company has encountered, or is likely to encounter, financial difficulties that are affecting, or will or may affect, its ability to carry on business as a going concern. And that a compromise or arrangement is proposed between the company and—

(i) its creditors, or any class of them, or
(ii) its members, or any class of them, and

The purpose of the compromise or arrangement is to eliminate, reduce or prevent, or mitigate the effect of, any of the financial difficulties. The procedure for approving the compromise or arrangement is identical to that used for schemes of arrangement under Part 26 of the Companies Act 2006.

An application for the court to give directions for the summoning of meetings at which the proposal is considered and voted upon by the creditors and members (if applicable) may be made by the company, any creditor or member of the company, or, if the company is being wound up, the liquidator, or if the company is in administration, the administrator.

Subsequent to the meetings, and after the creditors have voted, the court may sanction the compromise or arrangement if 75% in value of the creditors or class of creditors or members or class of members has agreed. Where a dissenting class has not agreed the compromise, the court may still sanction the compromise if (A) none of the dissenting class would be any worse off than they would be in the 'relevant alternative'; and (B) the compromise has been agreed by at least one class who would have received a payment or had a genuine economic interest in the company in the 'relevant alternative' . This means that one class of creditors can impose the proposal on all other classes of creditors, even those classes which did not vote in favour as long as the conditions set out in A&B are satisfied (thus a "cram down").

<u>Special cases for a compromise or arrangement</u>
If an application for a compromise or arrangement is made before the end of the period of 12 weeks beginning with the day after the end of any moratorium for the company; a creditor in respect of a moratorium debt, or a creditor in respect of a pre-moratorium debt for which the company has not had a payment holiday during the moratorium cannot participate in a meeting to consider the compromise or arrangement. But a compromise or arrangement cannot be sanctioned by the court if it includes provision in respect of those same creditors and they have not agreed to it. This essentially provides such creditors with a veto on the compromise or arrangement where it follows within the 12 week period of a moratorium.

Creditors with "aircraft-related interests" cannot participate in a meeting to consider the compromise or arrangement as their rights cannot be compromised without their agreement. "Aircraft-related interest" means a registered interest within the meaning of the International Interests in Aircraft Equipment (Cape Town Convention) Regulations 2015 (S.I. 2015/ 912).

These special cases, and ability to veto, have also been made applicable in the existing scheme of arrangement under Part 26 of the Companies Act.

Termination clauses in supply contracts

The CIGB introduces a prohibition on the reliance by suppliers of termination clauses in contracts for the supply of goods or services that are triggered when a party has entered into a formal insolvency procedure, including the new moratorium, and the new compromise procedure (commonly referred to as *ipso facto* clauses). The prohibition applies in the context of formal insolvency procedures and the new measures introduced. The purpose of this measure is to allow a distressed company to continue to trade and benefit from supplies and also ensure that suppliers cannot insist upon the payment of outstanding charges as a condition of future supply. Certain relief is available from the effects of these provisions for those suffering hardship (small suppliers are also temporarily exempted from this during the coronavirus pandemic) and where the court officeholder/company consents. There are very wide exclusions for certain regulated entities and financial services contracts. These measures are in addition to the existing provisions for essential supplies (under section 233, 233A IA 1986).

The protection of supplies under s233B does not apply to 'small entities', which is defined as meeting two of three criteria:

(1) turnover not more than £10.2m
(2) balance sheet not more than £5.1m
(3) employees less than 50.

Wrongful trading – suspension of liability

On 28 March, the UK Government announced the suspension of the wrongful trading ('WT') provisions of the Insolvency Act 1986 retrospectively from 1 March 2020.

The CIGB will temporarily relax the threat of personal liability for wrongful trading from company directors. However, the provisions in the CIGB do not provide a blanket suspension of the wrongful trading provisions. When determining the liability of the director, i.e. the contribution (if any) the director must make to a company's assets, the court is to assume that the director is not responsible for any worsening of the financial position of the company or its creditors that occurs during the relevant period (1 March to one month after the Bill comes into force). Whilst directors may not be liable to contribute to the losses in this period, the periods before and after still remain a factor. Also, directors may still be subject to action for other breaches of duties during the COVID-19 period.

Section 10 of the CIGB states –

"*In determining for the purposes of section 214 or 246ZB of the Insolvency Act 1986 (liability of director for wrongful trading) the contribution (if any) to a company's assets that it is proper for a person to make, the court is to assume that the person is not responsible for any worsening of the financial position of the company or its creditors that occurs*"

There is a long list of companies (for instance insurance companies and banks) and entities (for instance building societies and credit unions) to which this 'relaxation' does not apply.

Temporary prohibition on the presentation of winding up petitions

Schedule 10 of the CIGB prevents the presentation of a winding up petition by a creditor on the basis of a statutory demand made during the period 1 March to 30 June 2020. It also prevents a petition being presented by a creditor for cash flow or balance sheet insolvency after 27 April 2020 until one month after the CIGB comes into force. The temporary prohibition will not apply where the creditor had reasonable grounds for believing that the coronavirus had not had a financial effect on the company, or that the company would still have been in financial difficulty even if the coronavirus had not had any effect.

The temporary prohibition also does not stop the presentation of a winding up petition by the directors, or by the Secretary of State on public interest grounds.

Where (1) a petition has been presented from 27 April 2020 until the date the Schedule comes into force, and (2) the court is satisfied the petitioner did not believe the coronavirus did not have an effect etc, then the court may make such order as it thinks appropriate to restore the position to what it would have been if the petition had not been presented. This may potentially include ordering the petitioner to pay damages.

If the winding up petition was presented in that relevant period and it appears to the court that coronavirus had a financial effect on the company before the presentation of the petition, the court may only make a winding up order if (in addition to the usual tests) the court is satisfied that the facts by reference to which the petition has been presented would have arisen even if coronavirus had not had a financial effect on the company.

This provision is deemed to have come into effect on 27 April 2020 and if the court has already made a winding up order on the basis the company is unable to pay its debts, it is to be treated as void. IF YOU ARE LIQUIDATOR OF A COMPANY PURSUANT TO AN ORDER MADE AFTER 27 APRIL 2020 YOU SHOULD SEEK ADVICE.

The commencement of winding up (for petitions presented in this relevant period) will be from the date of the winding-up order, rather than the date that the petition was filed. This means that the petition will not prevent disposals of the company's property (which are voided from the commencement of the winding up unless the court orders otherwise). As a result of the change, the company will not need to seek permission from the court to engage in its normal trading once a petition has been presented. The change also protects, for example, financial institutions who do business with the company who, due to the change in advertising of the petition, (paragraph 19(3)) may not be aware that a petition has been presented. Complicated consequential amendments are made to the look back period for many Insolvency Act provisions.

Meetings and filings

Meetings of companies and other bodies

Schedule 14 makes provision about meetings of companies and other bodies for the period 26 March 2020 to 30 September 2020.

A general meeting of a company need not be held at any particular place. The meeting may be held, and any votes may be permitted to be cast, by electronic means or any other means. The meeting may be held without any number of those participating in the meeting being together at the same place.

A member of the qualifying body does not have a right to attend the meeting in person, to participate in the meeting other than by voting, or to vote by particular means.

Other meetings include a meeting of any class of members of a company of a qualifying body, or a meeting of delegates appointed by members of a qualifying body.

Temporary power to extend periods for providing information to registrar

A number of time periods have been extended with regard to providing certain information to the Registrar. The periods (must not be exceeded) are as follows –

- 42 days, in a case where the existing period is 21 days or fewer, and

- 12 months, in a case where the existing period is 3, 6 or 9 months.

The extension of time periods ends on 5 April 2021.

The information to the Registrar to which the extension of time periods applies to can be found at section 38. Notable provisions in relation to insolvencies are as follows –

- section 87 (notice of change of address of registered office);
- section 167 (notice of change in directors etc);
- section 276 (notice of change in secretaries etc);
- section 790M (register of people with significant control);
- section 790N (notice of place where PSC register is kept);
- section 790VA (notice of change to the PSC register);
- section 853A(1) (confirmation statements);
- section 859A (registration of charge);
- section 859B (registration of charge contained in debentures).

~End~