



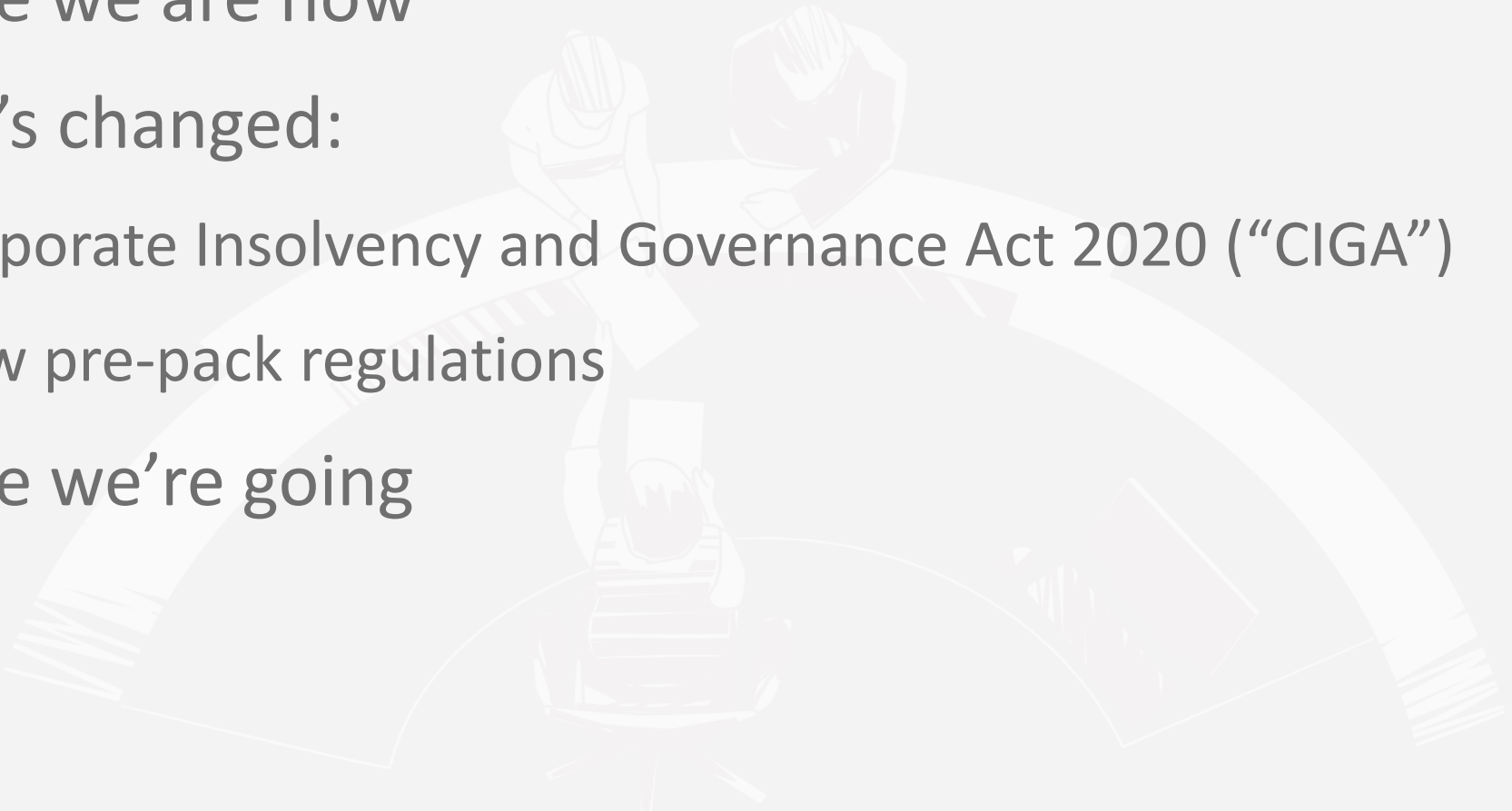
# Corporate Insolvency and Covid-19

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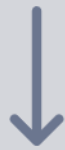
18<sup>th</sup> May 2021

# Corporate insolvency and Covid-19

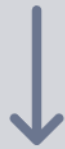
- Where we are now
- What's changed:
  - Corporate Insolvency and Governance Act 2020 (“CIGA”)
  - New pre-pack regulations
- Where we're going



# Trends in corporate insolvency over the last year



Total number of corporate insolvencies between April 2020 and March 2021 fell by more than a third compared with previous year



38.3% difference between Q1 2021 and Q1 2020

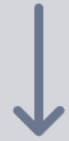
Compulsory liquidations: -85%

Administrations: -52%

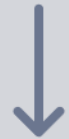
Voluntary liquidations: -24%

CVAs: -46%

# Q1 2021 picture



Lowest quarterly total of corporate insolvencies on record (2384)



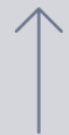
Still falling: 21.9% lower than Q4 2020

Compulsory liquidations: -26%

Administrations: -44%

Voluntary liquidations: -18%

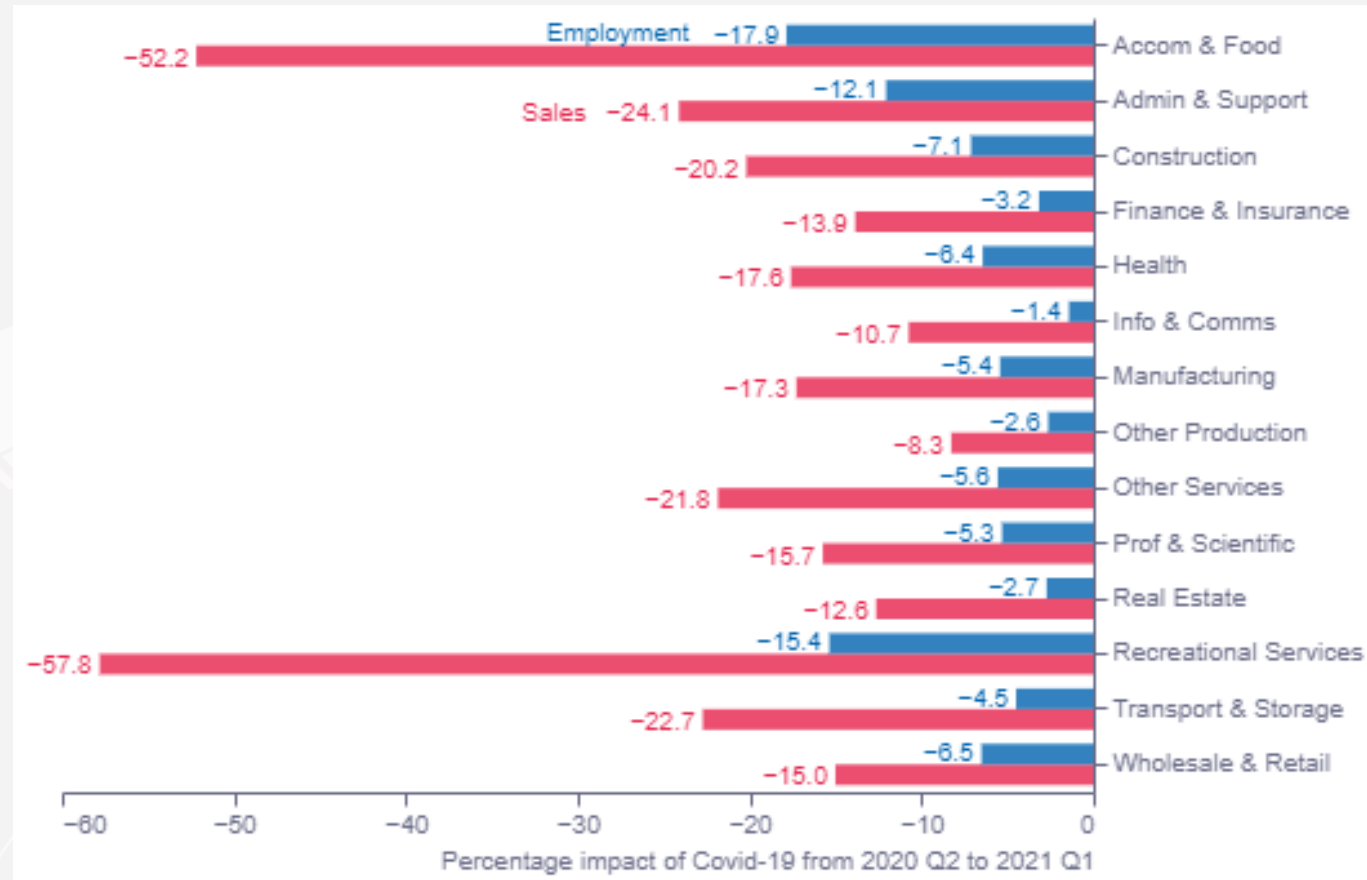
CVAs: -54%



Slight increase between February and March 2021

# Expected impact of Covid-19 on sales and employment from Q2 2020 – Q1 2021

- *Source:  
Decision  
Maker Panel*



# Corporate Insolvency and Governance Act 2020 ("CIGA")

Temporary provisions which are a direct response to COVID-19:

- Suspension of wrongful trading
- Restrictions on presentation of winding up petitions

Permanent provisions to assist with company rescue generally (in discussion for some time):

- Restrictions on provisions allowing suppliers to terminate by reason of insolvency
- New freestanding moratorium procedure
- New restructuring plan

# Temporary provisions

Apply during the “Relevant Period”:

- Initially 1 March 2020 to 30 June 2020 but since extended
- Current extension expires on 30 June 2021
- Described as “final” (but we have heard that before)

# Suspension of provisions relating to wrongful trading (s214 IA 1986)

- D can be ordered to contribute to the company's assets if they fail to take every step which they ought to minimise the loss to creditors once they conclude (or should have concluded) that there is no reasonable prospect of the company avoiding an insolvent liquidation or administration.
- Amount of contribution will usually reflect the amount by which the deficit to creditors increased as a result of the wrongful trading.



# Effect of CIGA

- Court now assumes that D is **not** responsible for any worsening of the company's financial position during the Relevant Period
- In theory would affect the amount of contribution D could be ordered to make to the company's assets
- Intent to reassure Ds that difficult decisions about future viability need not be unduly influenced by the exceptional circumstances of the pandemic

# Limitations

- Doesn't affect any of the other provisions in the Insolvency Act, or a director's statutory duties
- Large overlap with s172(3) Companies Act 2006 (duty to promote the success of the company): where a company is insolvent or close to insolvency, a director has a duty to give paramount consideration to the interests of creditors (BTI 2014 LLC v Sequana SA 2019)
- False sense of security?

# Gap in protection



CIGA 2020 originally provided for a suspension until 30 September 2020

Further regulations came into force on 26 November 2020 extending the suspension until 30 April 2021

CIGA Extension Regulations 2021 extend the suspension further until 30 June 2021

**But** no retrospective effect - no protection for 1 October – 25 November 2020!

# Restriction on statutory demands and winding up petitions



# Statutory demands

- Statutory demand: precursor to a winding up petition (application to court to put a company into liquidation)
- One of the ways of demonstrating that a company cannot pay its debts as and when they fall due (cash flow insolvency)
- Any statutory demand served between 27 April 2020 and 30 June 2021 is void.

# Winding up petitions

Creditor can present a petition without relying on a statutory demand, but cannot proceed unless:

- The creditor can show reasonable grounds for believing that COVID-19 has not had a financial effect on the company; or
- The company would be deemed to be insolvent even if any worsening of its financial position due to COVID-19 is ignored.

(the “Coronavirus Test”)

# The Coronavirus Test

Petitions presented during the Relevant Period:-

- Must set out grounds relied on for the purposes of the Coronavirus Test
- Will remain private (not be advertised or available for inspection) until the Court has considered whether the petition complies with the Coronavirus Test
- The company must file any witness evidence it wishes to rely on re the Coronavirus Test within 14 days of service of the petition
- New practice direction setting out procedure

# Non-attendance pre-trial review

Where petition not  
opposed and Coronavirus  
Test satisfied

Court will list the  
petition for hearing in  
the normal winding up  
list

Otherwise

Court will list the  
petition for a  
preliminary hearing to  
consider the  
Coronavirus Test and  
give directions.



# Preliminary Hearing



if the court is **not** satisfied that it is likely that it will be able to make a winding up order having regard to the Coronavirus Test, it will dismiss the petition.

if the court is satisfied on the evidence before it that it is likely that it will be able to make a winding up order then it will list the petition for hearing in the winding-up list.

# Permanent provisions

Nullifying of clauses in supply contracts providing for termination of the contract on insolvency

Wider access to moratorium protection, under the supervision of an insolvency practitioner

New insolvency procedure:  
“Restructuring Plan”



# Restricting termination provisions in supply contracts

Suppliers cannot:



Terminate or change terms on the basis that a company has entered an insolvency procedure or obtained a moratorium



Terminate the contract on other grounds until the insolvency procedure is at an end



Demand payment of outstanding sums as a condition of continuing supply

# Exceptions and safeguards

Supplier can continue to rely on such clauses where:-

- The company or office holder consents
- The court grants permission on the basis that continuation of the contract would cause the supplier hardship
- Temporary exclusion for small suppliers (until 30 June 2021)

# New moratorium procedure

- Allows companies in financial difficulties to get breathing space from creditors while a rescue plan is considered
- Supervised by an insolvency practitioner (the “Monitor”)
- Monitor must be satisfied that it is likely that the moratorium will result in a rescue of the company as a going concern
- Company remains under the control of its directors.

# Effects of moratorium

No legal action can be taken against the company or its assets without leave of the court

“Payment holiday” in respect of certain debts incurred pre-moratorium

Restricts company’s ability to pay pre-moratorium debts, to take on new credit, or to dispose of property

Company must be able to pay its ongoing liabilities

# Eligibility and procedure

## Two ways to obtain a moratorium:

- Simple filing of documents at court (similar to out-of-court administration appointment)
- Court application

## After 30 September 2021:

- a court application will be required if there is an outstanding winding up petition against the company
- Company **not** eligible if it has been in an insolvency process in the previous 12 months

# Benefits



Very debtor-friendly



Considerably widens access to moratorium protection



Flexible and potentially long in duration (initial period of 20 business days is extendable under various circumstances)



Benefits of the administration moratorium without needing to put the company into administration



# Barriers



## Company must continue to pay:-

- Monitor's remuneration and expenses
- Goods and services supplied during the moratorium
- Rent for the period of the moratorium
- Wages and salary
- Redundancy payments
- Financial services contracts, including bank loans.

Only four approved to 31 December 2020.

# Restructuring Plan

Any company which can be wound up under the Insolvency Act, including a foreign company, can propose a Restructuring Plan to its creditors / shareholders, provided:

- a) it has encountered, or is likely to encounter, financial difficulties which affect, or may affect, its ability to carry on business as a going concern; and
- b) the purpose of the compromise or arrangement is to eliminate, reduce, prevent or mitigate those difficulties.

Creditors and shareholders vote in “classes”, each of which are deemed to approve if 75% in value vote in favour.

# Restructuring Plan

## Designed to:

- enable restructuring of complex debt arrangements
- support the injection of rescue finance into the business
- Key benefit is “cross class cram down” - allows dissenting classes of creditors to be bound to the arrangement if the court is satisfied that none would be worse off under the arrangement than the “relevant alternative”.
- Requirement for court sanction that is not found e.g. in a CVA

## *Re Virgin Active Holdings Limited [2021] EWHC 1246*

Brand new: judgment 12 May 2021

Plan offered different compromises to different groups of creditors:-

- Some landlords offered reduced rent going forward

- Other creditors excluded entirely

Secured creditors and one class of landlord voted in favour

Several other classes of creditor voted overwhelmingly against



# The statutory test

- Court has to be satisfied that:-
  - Dissenting creditors would not be any worse off than in the “relevant alternative”; and
  - The plan is approved by 75% of those voting in any class that would receive a payment, or have a genuine economic interest in the company, in the relevant alternative.
- If these conditions are satisfied, Court has to decide whether to exercise its discretion to impose the cram down.

# Held:



Plan was sanctioned



Court cannot impose its own views of what is just and equitable



It doesn't matter if the “most likely” alternative is not likely to occur



On the facts, the only creditors who stood to receive a distribution in an insolvency process were secured creditors



The views of those other creditors “out of the money” were not relevant.

# Comment

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Paves the way for plans to be used to compromise the rights of landlords etc if those creditors would not receive anything under an alternative procedure

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There may be no need to ask those compromised creditors to vote.

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Emphasises broad scope of restructuring plans –makes them more attractive?  
(NB only two approved to December 2020)

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Importance of valuation evidence re “genuine economic interest”.

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# The new pre-pack regulations



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## *The Administration (Restrictions on Disposal etc. to Connected Persons) Regulations 2021*

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Require a mandatory independent opinion on all pre-pack sales in administration to a connected party

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Came into force for administrations commencing on or after 30 April 2021



# What is a pre-pack?

- A company agrees a sale of its business / assets prior to entering administration.
- The administrator completes the sale on or shortly after their appointment.
- Preserves jobs and goodwill
- Lack of transparency and trust for unsecured creditors, especially where the sale is to a connected person.

# The new pre-pack regulations

Prevent an administrator from executing a pre-pack sale if :

- the sale is of all or a substantial part of the insolvent company's business or assets;
- it is within the first eight weeks of an administration; and
- the disposal is to one or more persons connected with the company

Unless **either**:

- the administrator has obtained the approval of creditors for the disposal; or
- or the purchaser has obtained a “qualifying report” of an evaluator in respect of the sale.

## The evaluator

Independent	✓
Requisite knowledge and experience	✓
Professional indemnity insurance	✓
Professional qualifications	✗

## The report

- Opinion on whether the sale offers value for creditors
- Need not be in favour of the pre-pack but if it isn't, the administrator must provide reasons as to why they still wish to proceed.

# Comment



Replaces previous voluntary “pre-pack pool” – not well used



Will result in additional costs and delay when pre-pack are often time critical



Won't just affect pre-packs but any disposal within the first 8 weeks of the administration

# The future

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Recent monthly rise in corporate insolvencies comes after 11 months of very low levels

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Government support has probably postponed insolvencies rather than preventing them

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Likely will hit different sectors at different times

# The future

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Lack of usual “trigger events” may mean directors not prompted to take advice early enough

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Crunch point after 30 June 2021 in relation to winding up petitions, enforcement of rent arrears, VAT deferrals

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Risk of overtrading if cashflow can't support costs of reopening and restocking

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Will there be anything left to restructure?

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# The future

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Insolvency Service to be given stronger powers to investigate directors of companies that have been dissolved

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Intent is to prevent companies using dissolution to fraudulently avoid repayment of government backed loans

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Targeting directors who “inappropriately” wind up companies that have benefited from bounce back loans

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Will be retrospective in effect

# Any questions





# Contact details



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