SLAUGHTER AND MAY

THE CORPORATE INSOLVENCY AND GOVERNANCE ACT: KEY MEASURES

June 2020 (updated September 2020)

The Corporate Insolvency and Governance Act (the "Act") entered into force on 26 June 2020.

The Act makes three significant permanent reforms to our restructuring and insolvency regime, and also contains temporary measures designed to mitigate some of the economic and practical challenges of COVID-19. On 24 September 2020 the Government announced the extension of certain of the temporary provisions which had been due to expire on 30 September 2020.

In this update we provide a brief overview of the key restructuring and insolvency measures introduced by the Act.

Temporary COVID-19 Measures

Winding up Petitions

The Act introduces temporary restrictions on the presentation of winding up petitions and the making of winding up orders which have subsequently been extended so that they apply beyond the 30 September 2020 to 31 December 2020:

- Creditors will not be able to present a winding up petition based on a statutory demand served between 1 March and 31 December 2020.
- Until 31 December 2020 creditors will only be able to present winding up petitions on other grounds if they have reasonable grounds for believing that coronavirus has not had a financial effect on the company, or that the relevant ground would have arisen anyway.
- This is not a blanket ban but, while these restrictions remain in place, it is likely to prove challenging for creditors to obtain a winding up order in many circumstances (as has been demonstrated in a number of recent cases).
- These restrictions will not stop a debt becoming due and directors will need to be mindful of the other consequences of defaulting on payment, including the possibility that a creditor might seek to place the company into administration.

Wrongful Trading

In March, the Government announced that the wrongful trading provisions would be suspended temporarily. The Act implements that pledge, but modifies rather than suspends the provisions:

- The Act focuses on the financial consequences of a wrongful trading finding: the court must assume that a director is not responsible for any worsening of the financial position of the company or its creditors between 1 March and 30 September 2020. This significantly reduces the risk that a director will be held personally liable for wrongful trading during this period.
- Some companies do not benefit from the modified regime and the list of excluded companies is widely drafted.
- The risk of disqualification following a wrongful trading finding in relation to this period has also been significantly reduced, but all other aspects of the directors' duties and disqualification frameworks remain in place.
- The Government has announced that this temporary modification will not be extended beyond 30 September 2020.

Permanent Reforms

Restructuring Plan

The Act introduces a restructuring plan procedure to offer companies facing financial difficulty a new, flexible means of implementing a restructuring. The procedure is closely based on the scheme of arrangement but with some important distinctions. Most notable is the inclusion of a cross-class cram down mechanism. This will allow the court to sanction a plan even if the support of a class has not been obtained, as long as certain conditions are met. The restructuring plan has the potential to be a very useful addition to the toolkit although there are a number of complex issues that will need to be worked through and tested in court. Although the first restructuring plan was sanctioned on 2 September 2020, for Virgin Atlantic Airways Limited, it was not necessary for the court to explore many of these issues given the high levels of support from creditors.

Moratorium

A standalone moratorium procedure is available under the Act, with the aim of allowing distressed companies breathing space while they explore restructuring options. When in force, the moratorium will protect a company from winding up petitions and most types of legal proceedings, give the company a payment holiday in respect of some liabilities incurred before it came into force, and prevent creditors from taking certain enforcement action. However, the utility of the moratorium is likely to be limited by a number of factors, including a number of widely drafted exceptions which limit the companies that will be eligible to apply for a moratorium and the liabilities that will be caught. There will be almost no protection against financial creditors.

Termination Clauses

The Act provides that certain provisions in supply contracts will cease to have effect if the counterparty becomes subject to an insolvency procedure (including liquidation, administration, a CVA, the new moratorium or the new restructuring plan but not a scheme of arrangement). This includes provisions for automatic termination and provisions that allow the supplier to terminate or

do 'any other thing' by reason of the company entering the procedure. Also in scope are provisions that would have allowed the supplier to terminate before the company entered into a process, if the termination right arose but was not exercised. Suppliers will also be prevented from making payment of outstanding debts a condition of continued supply. This measure offers some protection for distressed companies but it will not apply to a wide range of financial contracts or where one or both of the contracting parties is in the financial services sector. Nor will it cover all types of commercial arrangements. There is also a temporary exemption for "small entity" suppliers if the counterparty enters a relevant insolvency procedure before 30 March 2021 (extended from 30 September 2020). For those that are in scope, it is likely to lead to greater focus on including and exercising early warning triggers.

Are the tools ready to use?

Our earlier briefing *The Corporate Insolvency and Governance Bill: A Toolkit for the Covid Era and Beyond?* discusses the reforms in more detail, and considers whether they are likely to promote company rescue in the way the Government intends. That question was also debated, to an extent, as the legislation was fast-tracked through Parliament. Questions were asked about the operation of the new measures and whether the right balance has been struck between key stakeholders.

A number of amendments were proposed but only a handful of changes were made, including to extend the temporary measures (some of which have since been extended again), to extend the scope of the rights of the Pension Protection Fund in certain circumstances and to address some potentially significant unintended consequences of the provisions which alter the statutory order of priority for certain moratorium debts in a subsequent procedure. However, very few of the questions raised thus far have been resolved, in part because of the speed at which this legislation has been implemented.

Although the Government has narrowed some of the short-term powers to amend insolvency legislation that are contained in the Act, it remains possible for changes to be made, and further guidance issued, to address difficulties encountered in practice. It will be crucial for the Government to assess the efficacy of the new reforms after they have been in force for a short time. There is still scope for a wider review of the UK's restructuring and insolvency framework (including whether to introduce measures to facilitate rescue or DIP financing).

Despite the uncertainties, there has been significant interest in the new tools and some have already been used in practice. It is hoped that stakeholders, practitioners and the judiciary will be able to find innovative approaches in order to harness their potential to assist with company rescues and restructurings, alongside more familiar tools such as administration and the scheme of arrangement.

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