Dechert LLP

New Insolvency Act: Some breathing space

The COVID-19 pandemic has brought forward the government's plans for major reform of the UK's insolvency framework. The Corporate Insolvency and Governance Act 2020, which came into force this June, introduced some permanent landmark changes as well as temporary measures to help businesses cope with the crisis. Anthony Frost of Dechert LLP highlights those of particular relevance to company directors.

COVID-19 temporary measures

- **Suspension of winding-up petitions and statutory demands**

  From 27th April, statutory demands served on companies between 1st March 2020 and 30th September 2020 can't be used as the basis for presenting a winding-up petition. During the same period, creditors can't present a winding-up petition unless they have reasonable grounds to believe that COVID-19 hasn't had a financial effect on the company, or that the company would still be unable to pay its debts even if COVID-19 had not had a financial effect on the company. The courts will probably find this a difficult question to determine.

  These changes should help to reduce the use of statutory demands and winding-up petitions as an aggressive form of debt collection (a winding-up petition can be presented if no payment is made within 21 days of a statutory demand). In particular, these provisions seek to prevent landlords using statutory demands to get around the moratorium on forfeiture introduced in previous coronavirus related legislation.

- **Suspension of wrongful trading rules**

  Under the wrongful trading rules, directors can be personally liable if the company enters into liquidation or insolvency administration and the director knew (or should have concluded) that there was no reasonable prospect of avoiding such proceedings. The New Insolvency Act temporarily suspends directors' personal liability for any worsening of a company's financial position during the period. This should help directors of companies affected by the pandemic to make decisions without fear of personal liability arising from the application of the wrongful trading rules.

  However, directors will still be subject to their usual duties – such as promoting the success of the company and considering creditors' interests in certain circumstances – and may still incur liability for fraudulent trading. It remains important for directors to take legal advice. Furthermore, the temporary suspension doesn't apply to certain excluded companies, such as those financed by rated or listed bonds.

Permanent insolvency law reforms

- **New statutory moratorium mechanism**

  Companies in distress may be given more breathing space to negotiate with creditors if they take advantage of a new statutory moratorium mechanism. This stops creditors taking enforcement action, restricts insolvency filings and provides a payment holiday for certain types of pre-moratorium debts as well as post-moratorium debts. The moratorium must be proposed by the company's directors and lasts for a fixed period. As with wrongful trading, some companies are excluded from using the mechanism.

- **Restructuring plan**

  A company in financial difficulty will be able to propose a compromise or arrangement between its creditors or shareholders, subject to the approval of the court and 75% of each class of creditors. In certain circumstances, the court may sanction the plan even where one or more classes don't vote for the plan. The first plans presented to the English courts will be closely watched to see the scope of these provisions.

- **Other provisions**

  The Act prevents suppliers from relying on contractual clauses that allow termination because a counterparty enters an insolvency or restructuring process. It also includes COVID-19 related measures for company meetings and filings.

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