Hogan Lovells

Corporate Insolvency and Governance Bill: Highlights and lowlights

Tom Astle, Joe Bannister and Don McGown

27 May 2020

Introduction

- Context of the Bill:
  - Scope of these proposed changes
  - Driving forces behind Bill
- Status of the Bill / timing
- Speakers today and practicalities
- Other materials on topic

Agenda for today

- Permanent changes:
  - Moratorium
  - Termination or *ipso facto* clauses
  - Restructuring plan
- Temporary changes
  - Wrongful trading
  - Winding up petitions


The moratorium

The moratorium

- New free standing moratorium, applying to companies that are or are likely to become unable to pay debts, but not to companies that have been in moratorium or other insolvency proceedings in previous 12 months. Directors remain in charge but subject to supervision by a "monitor"
- Routes in: filing "relevant documents" in court unless company is an overseas company or a company that is subject to a pending winding up petition. In latter case court must be satisfied that the moratorium would achieve a better result for creditors as a whole than would winding up without a prior moratorium
- Monitor must express view it is "likely" moratorium would achieve rescue of company as a going concern. Process intended to be temporary and is focused on the rescue of the *company* not the *business*
- Initial 20 business day period capable of extension by additional 20 business days by directors, by up to 1 year by creditor decision and indefinitely by the Court

The moratorium

- Effect: very similar to administration moratorium. Court consent needed for:
  - Initiation of legal proceedings and peaceable re entry
  - Enforcement of security other than financial collateral and the enforcement of rights under hire purchase agreements.
- Directors may start insolvency proceedings and winding up on public interest grounds is possible, in each case without prior court consent
- **BUT**
  - Moratorium will not prevent the enforcement of set off rights so contrast eg a US Chapter 11 process
- **AND**
  - Note the interrelationship between the moratorium and the restrictions on exercising contract termination rights

The moratorium

- Secured assets can be disposed of in accordance with security terms or court application to dispose of assets free of security
- For fixed charge assets, secured creditors will receive the net proceeds of sale plus "*any money required to be added to the net proceeds so as to produce the amount determined by the court as the net amount which would be realised on a sale of the property in the open market by a willing vendor*".
- For floating charge assets, lenders will gain the same priority in the "acquired" asset as they had in the sold asset.
- But where does this leave lenders where the asset is "cash"? Finance documents allow cash to be used in the ordinary course of business.....
- Moratorium is inapplicable to market charges as it is to certain FS companies such as banks and insurers

The moratorium

- On the face of it the procedure is “debtor in possession" as a monitor (a licenced insolvency practitioner) oversees the process and must end the process if he ceases to believe the company can be rescued or if the directors have not given him enough information to do his or her job.
- The monitor can take a subsequent insolvency appointment; he is subject to an "unfair harm" sanction in the discharge of his or her role
- Key distinction is between pre- and post-moratorium debts; the latter *should* be paid; the former should not be paid unless they are pre-moratorium debts excluded from a" payment holiday"
- The "payment holiday" applies to all pre-moratorium debts save for specified exceptions: goods supplied in moratorium, rent and debts or liabilities arising under a contract or other instrument involving financial services
- Pre-moratorium debts can be paid if they are less than the greater of £5,000 and 1% of the company's liabilities or the monitor agrees. Payment otherwise is a criminal offence
- A procedure written in haste and one of unintended consequences?

Termination clauses

Termination

- New s 233B IA 1986. Where a company becomes subject to a relevant insolvency procedure:
  - a provision in the contract which:
    - causes the contract or the supply to terminate or any other thing to take place; or
    - entitles the supplier to terminate or do any other thing,

    in each case because the company becomes subject to the relevant insolvency procedure is void; and
  - If the supplier had a right to terminate the supply or contract because of something which took place before the start of the relevant insolvency procedure, the right to terminate is suspended until the end of the insolvency proceeding.
- "Relevant insolvency procedure"; includes new moratorium, administration, administrative receivership, CVAs, liquidation, provisional liquidation and the new rescue plan proceedings (but not schemes of arrangement)

Termination

- Again, certain FS companies are excluded: banks, building societies, insurers securitisation companies and overseas entities carrying out similar functions.
- "Financial contracts" are excluded (which covers a number of contract types including lending contracts), derivatives, capital market arrangements and contracts forming part of a PPP project. So are set-off and netting arrangements.
- The prohibition is wide; "Any other thing" would extend to any contract variation and the imposition of default interest.
- Suspension of pre insolvency termination rights is also wide; it appears to prevent termination on grounds of fraud or grounds that are unrelated to any insolvency event
- What about contracts between the insolvent company where the supplier is one of multiple parties?
- And what about contract breaches arising AFTER the start of an insolvency process?

Termination

- Payment of pre insolvency debts cannot be a pre condition of continued supply, save where those supplies are supplies of utilities and the insolvency process is not a moratorium
- Usual advice applies in dealing with insolvent counterparties; get in contact ASAP and agree payment terms to ensure that you receive payment as an expense
- Otherwise a supplier may terminate a contract with consent of an administrator, liquidator provisional liquidator or receiver
- And the court may give a supplier permission to terminate a contract where it is satisfied that continuation of the contract would cause the supplier "hardship"
- Again, these new concepts; eg "any other thing", "hardship" and the position of other contractual parties will take time to "bed in" and will inevitably be the subject of judicial interpretation

Restructuring plan

Restructuring plan

- Introduced as part of the Companies Act, not the Insolvency Act 1986
- A new process based on the existing Companies Act scheme of arrangement (scheme) but permitting cross-class cram-down, so provides greater scope for making the plan binding on dissenting creditors than would be possible under the existing scheme process.
- Applies to a company liable to be wound up under the Insolvency Act that "*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*".
- Such a company will be able to propose a restructuring plan with its creditors and/or members which is intended to eliminate, reduce or prevent, or mitigate the effect of their financial difficulties.
- This may be combined with the moratorium discussed above which will prevent action against the company while the restructuring plan is being proposed.
- The Secretary of State can exclude certain companies from being able to use the restructuring plan process including those regulated by the Financial Services and Markets Act

Implementation

- In many respects, the process of binding creditors or members to the restructuring plan will follow the well-tested process for approval and sanction of the current scheme process (and scheme case law is likely to be relevant).
- Thus, an explanatory statement must be produced and a meeting of affected creditors or members convened. If 75% or more in value of each class of creditors or members agree to a restructuring plan, the court may sanction it.
- Where the restructuring plan relates to debts which were covered by a moratorium which ended less than 12 weeks previously, the court may not sanction the plan if creditors with a moratorium debt or a pre-moratorium debt in respect of which the company does not have a payment holiday are affected and have not agreed to it. A similar change will be introduced in respect of schemes of the traditional scheme of arrangement.

Cross-class cram-down

- The procedure will allow the court to sanction the restructuring plan despite it not having been approved by 75% in value of each class of creditors or members. This will only be possible if
  - none of the members of a dissenting class would be any worse off under the restructuring plan than they would be in the alternative scenario of the restructuring plan not being sanctioned (ie that they are not financially disadvantaged by the restructuring plan) and
  - at least one class who "would receive a payment or have a genuine economic interest in the company" in the event of that alternative has voted in favour of the plan by the 75% in value majority.
- There are some exceptions to this provision in particular companies with aircraft –related interests

Scheme of arrangement v plan: the differences

- The key differences with a scheme of arrangement are as follows:
  - The availability of the cross-class cram-down;
  - If the court is satisfied that no members of a certain class have "a genuine interest in the company" – so-called “out of the money” creditors – it may order that creditors or members in that class are excluded from any meeting convened to consider the restructuring plan.
  - a scheme requires approval by 75% in value and 50% in number of creditors or members in each class. A restructuring plan will not have a majority in number requirement, so a plan is less likely to be undermined by a number of creditors with low-value debts or a large number of minority shareholders.

Comments

- A number of changes to existing legislation are being made to facilitate the implementation of a Restructuring Plan so that shares issued as part of such a plan are not required to have corporate authority to allot and statutory pre-emption provisions are excluded
- Approach to be taken under:
  - Articles of Association
  - Listing Rules
  - Takeover Code and whitewash
- Anti-trust considerations
- Applicability to overseas companies

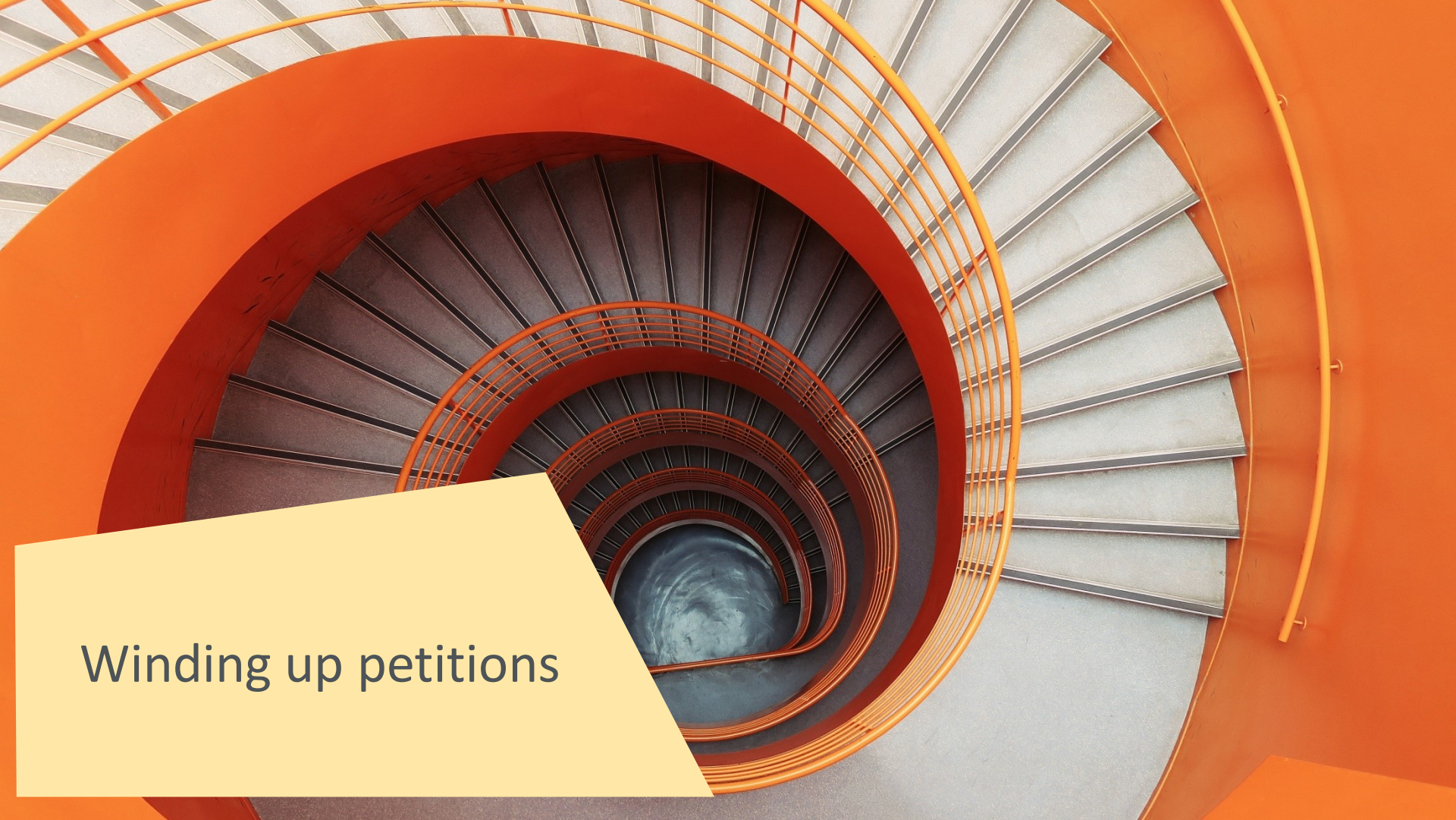

Wrongful trading

Wrongful trading – the current position

- A director will be found to have wrongfully traded:
  - where the Company has gone into insolvent liquidation or insolvent administration; and
  - at some earlier point, that director knew or ought to have concluded that there was no reasonable prospect that the Company would avoid going into insolvent liquidation or insolvent administration
- The court may require a contribution to the assets of the company from a director who has wrongfully traded if the director failed to take every step with a view to minimising the potential loss to the company's creditors as he ought to have taken
- Government announcement – suspension of wrongful trading from 1 March to 30 June 2020 so directors "*…can keep their businesses going without the threat of personal liability*"

Wrongful trading – the legislation

- The Bill:
  - does not suspend the wrongful trading regime
  - provides that when determining the contribution a director who has wrongfully traded should make to the 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 in the period from 1 March to 30 June 2020 (or one month after the Act comes into effect if later).
- Points to consider:
  - Directors who have continued trading during this period in reliance on the announcement may be surprised that the suspension is of the sanction, not the liability.
  - If the claim of wrongful trading is not limited to the suspension period, how can you calculate what losses are to be attributed to the period of suspension?
  - It is irrelevant if the worsening of the position was for reasons unrelated to the COVID-19 pandemic.
  - Directors of certain types of companies are excluded. Fair?



Winding up petitions

Winding up petitions (WUPs)

- Government announcement:
  - temporary new measures to safeguard the UK high street against aggressive debt recovery actions during the coronavirus pandemic;
  - statutory demands and winding up petitions issued to commercial tenants to be temporarily voided
- The Bill provides that:
  - No WUP based on a statutory demand made between 1 March and 30 June 2020 (or one month after the Act comes into force (the **Termination Date**)) can be presented on or after 27 April;
  - A WUP based on an inability to pay debts cannot be presented by a creditor in the period from 27 April to the Termination Date (the **relevant period**) unless the creditor believes the inability to pay has not been caused by the COVID-19 pandemic
    - Where presented after the date the Act comes into force, the WUP has to contain a statement to that effect;
  - Even if the creditor had that belief, the court will not be able to make a winding up order based on that WUP unless it is satisfied that the inability to pay would still have arisen even if the pandemic had not had a financial effect on the company;

Winding up petitions (WUPs)

- The Bill provides that (cont):
  - Where a WUP has been presented after 27 April but before the Act comes into force, if the creditor did not have the necessary belief the court can make orders restoring the company to its pre-petition position;
  - Where a winding up order is made after 27 April but before the Act comes into force, if the order is one that the court would not have made had the Act been in force, the order is void and again the court can make orders restoring the company to its pre-order position
  - Where the WUP is presented in the relevant period and a winding up order is made:
    - the winding up will be deemed to commence on the date the winding up order is made
      - relief from the effects of s.127 IA86;
    - transaction avoidance periods are extended by six months if the order was made more than 6 months after the WUP was presented
  - WUPs presented after the Act comes into force but before the Termination Date can't be advertised until the court has made a decision as to whether the court is likely to be able to make an order

Application and timing

- Provisions apply to:
  - companies registered under the Companies Act 2006 in England and Wales or Scotland and to companies liable to be wound up under Part 5 IA86
  - all in-scope debtors and all creditors, not just landlords and tenants of commercial premises
- Most of the provisions have retrospective effect and are back-dated to 27 April 2020
- Power given to the SoS to curtail or extend the Termination Date by six months

Points for consideration

- Statutory demands issued on 1 March likely to relate to pre-pandemic liabilities, so why should they be banned?
- Positive obligation for a creditor to prove a negative
  - May result in more contested petitions
  - As well as the statement in the WUP does the creditor have to provide other (financial) evidence?
- Is it a two stage process where the court first determines whether it is likely that the court will be able to make an order and then the winding up hearing?
  - Impact on court time;
  - Evidence?
  - Appeals?
- Why would a creditor not wait until the Termination Date?

Conclusion

Conclusion and other materials

- Impressive in the time
- Will the measures be brought in quickly enough to benefit companies currently struggling?
- Will we end up with a best-in-class toolkit or a ragbag mix of unusable tools?
- Other sources of information:
  - COVID-19 hub
  - Engage

Speaker CVs

Tom Astle

Partner, Head of Restructuring, London

Tom is head of our restructuring team in London, and works for credit funds and investment bank special situation desks involved in domestic and multi-jurisdictional special situation lending and restructurings. The majority are implemented with successful negotiation of a consensual solvent solution, although he has regularly used pre-packaged administration, and/or Schemes of Arrangement, to deliver his clients' preferred solution.

Representative experience includes:

- Fortenova: advising debt fund on refinancing of the Fortenova group's €1.2bn existing facilities via a secured private note issuance
- Thomas Cook plc: acting for providers of c€500m bonding, in connection with the ultimately abortive restructuring
- Agrokor: acting for ad hoc bond committee, subsequently €1bn DIP funding providers, negotiation of the settlement plan, and UK Scheme
- Autobar/Pelican Rouge: advising for an investment bank advancing €100m of super senior working capital into this restructuring
- Apcoa: acting for the Agent in structuring of the scheme of arrangement in this leading case
- Polestar Printing: acting for the lenders in restructuring of their uni tranche facility and subsequent pre-pack administration
- Infrastructure: acting for special situation desks on the restructuring and debt for equity swap of a European infrastructure project
- Sepura Plc: advising FTSE listed corporate on liquidity funding, debt restructuring and subsequent takeover by strategic Chinese buyer
- Acting for a fund in delivering the West Cornwall Pasty Company business through a pre-packaged process to take ownership
- OfficeTeam: Advising the senior lender syndicate on the restructuring , delivered through a debt for equity swap via a pre-packaged administration
- Advising listed UK/US group AEA Technology plc on accelerated M&A process and sale, including compromise arrangements with the PPF, pension trustees, and secured lender
- Advising the senior lender syndicate to Peacocks, and acting for the administrators on subsequent trading administration and sale of over 900 stores
- Advising the senior lender syndicate to Bon Marche, and acting for the administrators on subsequent trading administration and sale of over 900 stores
- Advising the lending syndicate in relation to their exposure to listed nightclub operator, Luminar Group, and acting for the subsequently appointed administrators
- Advising administrators on the £3.2bn pre-packaged administration of major music group, EMI

T: +44 20 7296 5603

E: tom.astle@hoganlovells.com

Rankings:

Ranked – Chambers UK 2020

Leading Individual – Legal 500 2020

Accolades

"a dynamic and diligent trusted adviser" - Legal 500 2020

The "detail-oriented, smart and responsive" Tom Astle has a growing profile for his skill in high-profile, often multi-jurisdictional restructurings. Clients report: "He's very robust in his legal analysis and very commercial with it." Others note: "He is commercially aware, gives valuable insight and has great deal experience." – Chambers UK 2019

Joe Bannister

Partner, business restructuring and insolvency London

Joe Bannister is a seasoned, international, restructuring and insolvency lawyer. For more than 30 years, Joe has helped the entire range of restructuring stakeholders to address and resolve the most difficult restructurings and insolvencies. He has experience across all industry sectors, and has dealt with cases in the UK, Europe, Asia and the US. Joe is a member of the City of London Law Society Insolvency Sub Committee. He deep interest in legislative reform most recently advising clients on and contributing through to the discussions and development to the 2020 Insolvency Bill.

Joe's international assignments have encompassed a number of offshore jurisdictions, including Bermuda, the BVI, Cayman Islands, Cyprus, Mauritius and the Isle of Man. He has particular expertise (and interest) in diversified industrial and automotive cases and in cross border and financial services cases, including insurers and banks.

Joe has worked at Hogan Lovells and its predecessor firms for his entire career. Joe is admitted as a solicitor in both London and Hong Kong, where he worked between 1998 and 2002 and again in 2014 and 2015 as the partner in charge of the firm's business restructuring and insolvency practice in Hong Kong and China. He is widely recognised as a leading practitioner in directories such as Chambers and Legal 500.

Representative experience includes:

- Advising a major international bank on the workout and recovery of a US$3.5 billion facility owed by an international energy and steel group in Hong Kong, Singapore, London and India
- Advising a major motor manufacturer as a creditor of various distressed suppliers; the Liberty and Amtek Groups, JVM Castings, Collins & Aikman, Visteon Group Schefenacker and others, including the negotiation of funding arrangements both outside and within formal insolvency proceedings and negotiating the pre-packaged sale of the business, assets and undertakings of distressed suppliers on terms acceptable to OEM clients.
- Acting as UK counsel to the Official Committee (the "Committee") of asbestos creditors in the formulation of company voluntary arrangements ("CVAs") for Turner & Newall Limited and its subsidiaries and co-ordinating that work with parallel Chapter 11 proceedings.
- Advising the Nortel group pension trustees.
- Advising Ataer holdings, one of the bdders for the British Steel group
- Advising a creditor on the protection of its rights in relation to the LDK Solar Group schemes of arrangement, both in Hong Kong and Cayman.
- Acting in the administrations of home improvements and fashions businesses and companies in the leisure and hospitality sectors, both In relation to trading issues and on the sale of the businesses, assets and undertaking of the companies concerned.
- Advising on a number of insurer insolvencies and insurer solvent schemes of arrangement including Orion and London & Overseas Insurance; including designing a cut-off scheme to accelerate the conclusion of this long running and complex insolvency.
- Advising the Icelandic Government in relation to the Icelandic financial crisis including the capital reorganisations of Iceland's three principal banks.
- Acting for the administrators of Lehman Brothers Holdings Plc in the evaluation and settlement of liabilities to subordinated creditors through a combination of negotiation and court proceedings.

T: +44 20 7296 2900

E: joe.bannister@hoganlovells.com

Rankings:

Ranked – Chambers UK 2020

Leading Individual – Legal 500 2020

Accolades

Sources say that Joe Bannister is a "great technical lawyer who is very knowledgeable." He has a wealth of experience advising on a wide array of restructuring and insolvency matters both domestically and internationally. Chambers UK 2019

Joe Bannister…has experience advising on matters involving offshore jurisdictions and is adept at handling schemes of arrangement. Clients say: "He is approachable, very experienced and infinitely professional."– Chambers UK 2020

Don McGown

Senior counsel, corporate London

Don McGown has over 35 years of experience in International M&A and Corporate Restructuring whilst working in London, New York, Hong Kong and Brussels.

During his career, he has assisted clients in acquiring and selling companies and businesses in over 70 countries, particularly in the TMT, Industrial and Financial Institutions sectors. He has acted on a number of major M&A deals over the past three decades for clients including 21st Century Fox, News Corporation, Vodafone, ITV, AECOM, DS Smith, Cable & Wireless, TUI, Nippon Sheet Glass, BAT and BNP. Major restructuring deals include Heron International, Marconi, Schefenacker, USP Hospitales, Mecom, and Quinn Group. Many bids and restructurings have involved schemes of arrangement.

Don has been considered a highly effective and skilled practitioner for many years by legal publications . Before joining Hogan Lovells as a partner 6 years ago, Don was at Allen & Overy for over 30 years, 25 as a partner.

Representative experience includes:

- Advising Tetra Tech Inc on its £43m acquisition of WYG plc by scheme of arrangement.
- Acting for Paysafe Group plc on its £2.9bn recommended acquisition by a consortium of funds managed by Blackstone and CVC Capital Partners by scheme of arrangement.
- Acting for Acon Equity Management on its £165m consortium bid for APR Energy plc by scheme of arrangement.
- Advising 21st Century Fox on the spin off of News Corporation, its abortive bid for Sky and the disposal of its Eastern European TV and outdoor advertising interests.
- Advising AECOM on many of its European, Middle East and Asian acquisitions.
- Advising DS Smith as a corporate client and on its transactions for 20 years, most recently on its acquisition of SCA Packaging .
- Advising Emap on its breakup, C+W on its sale of Hong Kong Telecom, United Newspapers on its merger with MAI and Nippon Sheet Glass on its acquisition of Pilkington by scheme of arrangement.
- Advising banks and financial institutions such as Barclays, ABN Amro, SE Banken, BNP, Chase, BT Investment Management and Bank of Montreal on acquisitions and disposals.
- Advising on high profile corporate restructurings including Heron International, the Maxwell private companies, Imry, Marconi, Schefenacker, Metronet, Mecom and Sepura.

T: +44 20 7296 5420

E: don.mcgown@hoganlovells.com

Rankings:

Recommended– Legal 500 2020

Accolades

Listed as legal expert in Corporate M&A in Legalease's Legal Expert Guide for past 10 years.

Highly regarded' Legal 500 2015

Hogan Lovells

www.hoganlovells.com