

Clients & Friends Memo

COVID-19 Update: Planned Changes to UK Insolvency Laws to Enable Companies to Continue Trading

31 March 2020

Introduction

On Saturday 28 March 2020, the Business Secretary, Alok Sharma, [announced](#) that the UK government would be introducing legislation to make changes to existing insolvency laws in response to COVID-19. The new measures seek to enable companies undergoing a rescue or restructuring process to continue trading and help them avoid insolvency, and include a temporary suspension of wrongful trading provisions retrospectively from 1 March 2020 for three months. This in particular will be welcome to directors who may be weighing the potential for personal liability when considering taking on Government or bank funding. Legislation to introduce these changes will be introduced in Parliament at the earliest opportunity, although the exact timing remains uncertain – Parliament is currently in recess until 21 April 2020.

Restructuring Plan / Moratorium

The government previously consulted on changes to the insolvency regime and [announced plans](#) in August 2018 to introduce new insolvency restructuring procedures. The legislation announced over the weekend will implement those proposed changes. New tools to be available to companies under the legislation are:

- a moratorium for companies giving them breathing space from creditors enforcing their debts for a period of time whilst they seek a rescue or restructure;
- protection of their supplies to enable them to continue trading during the moratorium; and;
- a new restructuring plan, binding creditors to that plan.

Some similar tools have of course been available to companies but only through a formal administration or other process. The legislation now announced should make the process easier to access and implement, and to become more widely available.

Wrongful Trading

The current wrongful trading rules have been of particular concern for directors of fundamentally healthy companies in recent weeks, as the impact of COVID-19 puts a strain on normally viable businesses everywhere, and the duration of the crisis remains uncertain.

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Under the current insolvency “wrongful trading” regime, a director of an insolvent company in liquidation or administration can become personally liable if he knew, or ought to have known there was no reasonable prospect of avoiding insolvent liquidation or administration. Directors are therefore understandably concerned about incurring new liabilities for the debt they need to see them through the crisis. For instance, under the COVID-19 related lending programs the UK government has created to ease the financial strain of this period (see our [memorandum](#) on this topic).

The suspension of the wrongful trading provisions at least during March, April and May (the legislation will provide for the changes to be extended if necessary) will give directors the time and confidence they need to assess the needs of and future viability of their business in a clear headed manner. As a deterrent to director misconduct, the rules against fraudulent trading (trading with the intent to defraud creditors (or any other fraudulent purpose)) and the director disqualification rules will remain unchanged.

Commentary

This announcement is timely and welcome on a broader scale. The wrongful trading suspension is a helpful step by the government to ease the strain on responsible directors dealing with an unprecedented blow to the business, and may help businesses that would otherwise opt for administration or liquidation to weather the storm. From that perspective, the sooner this legislation can be formally passed into law, the better.

The broader reforms to the Insolvency Framework have been in contemplation for years. While, as the 26 March 2020 [publication](#) by The Insolvency Lawyers Association points out, the English law insolvency regime has the first purpose of the rescue of the company, is flexible and has always been used innovatively in restructuring situations, these reforms will move the UK closer to the US style of debtor-in-possession restructuring. Once these framework changes take effect, stressed UK debtors in need of restructuring, particularly international businesses, will have a choice of a newly reformed (though untested) UK procedure or opting into a Chapter 11 case in US bankruptcy courts, which are traditionally welcoming to foreign debtors willing to submit to jurisdiction.

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