Pandemic Petitions: Winding up under the Corporate Insolvency and Governance Act 2020 and the associated Practice Direction

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1. With the recent introduction of the Insolvency Practice Direction relating to the Corporate Insolvency and Governance Act 2020 ("the CIGA 2020"), we consider some key practical considerations for solicitors dealing with corporate insolvency, especially in the context winding up petitions. We also consider some other aspects of the CIGA 2020 and how they might impact on winding up of companies.

A recap of the circumstances in which a Company may ordinarily be wound up

2. Section 122 of the Insolvency Act 1986 ("the 1986 Act"), prescribes the circumstances in which a Company may be wound up by the court. Such circumstances include where the Company is unable to pay its debts under section 122(1)(f) of the 1986 Act.

3. Section 123 of the 1986 Act defines when a Company is *"unable to pays its debts"*, which includes:

   "(1)(a)if a creditor (by assignment or otherwise) to whom the company is indebted in a sum exceeding £750 then due has served on the company, by leaving it at the company's registered office, a written demand (in the prescribed form) requiring the company to pay the sum so due and the company has for 3 weeks thereafter neglected to pay the sum or to secure or compound for it to the reasonable satisfaction of the creditor, or

   (1)(b) if, in England and Wales, execution or other process issued on a judgment, decree or order of any court in favour of a creditor of the company is returned unsatisfied in whole or in part, or [….]

   (1)(e)if it is proved to the satisfaction of the court that the company is unable to pay its debts as they fall due.

(2) A company is also deemed unable to pay its debts if it is proved to the satisfaction of the court that the value of the company's assets is less than the amount of its liabilities, taking into account its contingent and prospective liabilities."

Petitions based on statutory demands dated 27 April 2020 to 30 September 2020

4. Part 1 of Schedule 10 of the CIGA 2020 prohibits any petition for the winding up of a registered or unregistered Company being presented after 27th April 2020 pursuant to section 123(1)(a) of the 1986 Act where a statutory demand was served between 1st March 2020 and 30th September 2020. This is a complete prohibition and any petition brought after 27th April 2020 will be caught, even if the petition was brought between 27th April 2020 and the Act receiving its coming into force on 26 June 2020.

Petitions based on other grounds

5. For petitions not falling with Part 1 of the CIGA 2020 (i.e. petitions based on other grounds or based on a statutory demand which falls outside the relevant period), it is necessary to consider on what grounds the petition is presented.

What does the petitioning creditor need to demonstrate to obtain a winding up order if the grounds set out in section 123(1)(a) to (d) of the 1986 Act are relied on?

6. If a petition is presented between 27th April 2020 and 30th September 2020 and the grounds set out in section 123(1)(a) to (d) of the 1986 Act are relied on, the court is likely to expect evidence dealing with paragraph 2(1) and (2), Schedule 10 CIGA 2020. That is to say evidence that the petitioning creditor has reasonable grounds for believing:

"(a) coronavirus has not had a financial effect on the company, or

(b) the facts by reference to which the relevant ground applies would have arisen even if coronavirus had not had a financial effect on the company."

7. In reality, it is unlikely that many petitioning creditors will be able to satisfy ground (a) so the focus should be on ground (b), in particular if the debt accrued prior to March 2020.

8. If the petitioning creditor is able to establish the grounds in paragraph 2, Schedule 10 CIGA, the court is then likely to consider paragraph 5(1)(c), i.e. whether: "*it appears to*

the court that the coronavirus had a financial effect on the Company before presentation of the petition".

9. The evidential burden of showing that the coronavirus had a financial effect will then rest on the Company (see *Re a Company (Application to Restrain Advertisement)* [2020] EWHC 1551(Ch), at [44]). This burden of satisfying the test at paragraph 5(1)(c) "*is clearly intended to be a low threshold; the requirement is simply that 'a' financial effect must be shown: it is not a requirement that the pandemic be shown to be the (or even a) cause of the company's insolvency. Moreover the language of this provision, which requires only that it should 'appear' to the court that coronavirus had 'a' financial effect on the company before presentation of the petition, is in marked contrast to that employed in paragraph 5(3), where the court is required to be 'satisfied' of given matters. The term 'appears' must be intended to denote a lower threshold than 'satisfied'. The evidential burden on the Company for these purposes must be to establish a prima facie case, rather than to prove the 'financial effect' relied upon on a balance of probabilities.* (see *Re a Company (Application to Restrain Advertisement)* [2020] EWHC 1551(Ch), at [44]).

10. If the Company can meet the threshold test, the court will likely go on to consider whether it would wind the Company up under section 122(1)(f) of the 1986 Act on the ground specified in 123(1)(a) to (d) of the 1986 Act "*only if the court is satisfied that the facts by reference to which that ground applies would have arisen even if coronavirus had not had a financial effect on the company".*

11. The court have not considered this point yet with regard to grounds specified in section 123(1)(a) to (d) of the 1986 Act. However, when dealing with petitions brought under section 123(1)(e) of the 1986 Act, the court held that the burden should shift back to the petitioning creditor (see *Re a Company (Application to Restrain Advertisement)* [2020] EWHC 1551(Ch), at [45]). It is the authors' view that the petitioning creditor is required to demonstrate that even if the coronavirus is ignored, the Company would still not have satisfied the statutory demand or judgment.

What does the petitioning creditor need to demonstrate to obtain a winding up order if the grounds set out in section 123(1)(e) or 123(2) of the 1986 Act are relied on?

12. A similar test is applied if the grounds set out in section 123(1)(e) or 123(2) of the 1986 Act is relied upon, the court is likely to expect evidence dealing with paragraph 2(3) and

(4), Schedule 10 CIGA 2020. That is to say evidence that the petitioning creditor has reasonable grounds for believing:

"(a) coronavirus has not had a financial effect on the company, or

(b) the relevant ground would apply even if coronavirus had not had a financial effect on the company."

13. As mentioned above, in reality, it is unlikely that many petitioning creditors will be able to satisfy ground (a) so the focus should be on ground (b), in particular if the debt accrued prior to March 2020.

14. If the petitioning creditor is able to establish the grounds in paragraph 2(3) and (4), Schedule 10 CIGA, the court is then likely to consider paragraph 5(1)(c), i.e. whether: "*it appears to the court that the coronavirus had a financial effect on the Company before presentation of the petition*".

15. As mentioned above, the evidential burden of showing that the coronavirus had a financial effect will then rest on the Company (see *Re a Company (Application to Restrain Advertisement)* [2020] EWHC 1551(Ch), at [44]).

16. If the Company can meet the threshold test, the court will likely go on to consider whether it would wind the Company up under section 122(1)(f) of the 1986 Act on the ground specified in 123(1)(e) or (2) of the 1986 Act "*only if the court is satisfied that the ground would apply even if coronavirus had not had a financial effect on the company*".

17. The burden shifts back to the Petitioner (see *Re a Company (Application to Restrain Advertisement)* [2020] EWHC 1551(Ch), at [45]). The Petitioner is required to demonstrate that even if the coronavirus is ignored, the Company would be insolvent within the meaning of section 123(1)(e) of the 1986 Act (see *Re a Company (Application to Restrain Advertisement)* [2020] EWHC 1551(Ch), at [45]).

18. As is evident from the above care needs to be taken in respect of the evidence prepared for the purposes of the hearing of the petition.

Other considerations when the petition is presented: 27th April to 26th June 2020

19. If a winding up petition was made after 27th April 2020 and the day before 26th June 2020 and the petition was presented without satisfying paragraph 2(2) or 2(4) or paragraph 3(2) or (4) of Schedule 10, CIGA 2020, under paragraph 7 of Schedule 10,

CIGA 2020, the court may make such order as it thinks appropriate to restore the position to what it would have been if the petition had not been presented.

Paragraph 19, Schedule 10 CIGA 2020 and the Practice Direction

20. Whilst generally paragraphs 2 and 5 of Schedule 10 CIGA 2020 are likely to be applicable for the purposes of petitions presented between 27th April 2020 and 30th September 2020, consideration of paragraph 19, Schedule 10 CIGA 2020 is also important.

21. For petitions presented under section 124 of the 1986 Act on or after 26th June 2020 but before 30th September 2020, any provision of the 2016 Insolvency Rules which requires or permits notice, publication or advertisement of the petition, does not apply until such time as the court has made a determination in relation to the question of whether it is likely that the court will be able to make an order under section 122(1)(f) or 221(5)(b) of the 1986 Act (see paragraph 19(2), Schedule 10 CIGA 2020).

22. The Insolvency Practice Direction relating to the CIGA 2020 ("the Practice Direction") deals with the steps the court will take managing a petition where notice has not been given and the court is required to make a determination which includes listing the petition for a non-attendance pre-trial review to determine directions for a preliminary hearing; subsequent directions and preliminary hearings.

23. The Practice Direction introduces the concept of the 'coronavirus test' which means:

    a. *In the case of a petition to wind up a registered company on a ground specified in section 123(1)(a) to (d) of the 1986 Act that the condition in paragraph 5(2) of Schedule 10 to the 2020 Act is met;*

    b. *In the case of a petition to wind up a registered company on a ground specified in section 123(1)(e) or (2) of the 1986 Act that the condition in paragraph 5(3) of Schedule 10 to the 2020 Act is met;*

    c. *In the case of a petition to wind up an unregistered company on a ground specified in section 222, 223, or 224(1)(a) to (c) of the 1986 Act that the condition in paragraph 6(2) of Schedule 10 to the 2020 Act is met; or*

    d. *In the case of a petition to wind up an unregistered company on a ground specified in section 224(1)(d) or (2) of the 1986 Act that the condition in paragraph 6(3) of Schedule 10 to the 2020 Act is met.*

Moratoriums: sections 1 to 6 of the CIGA 2020

24. Sections 1 to 6 of the CIGA 2020 make provision for the addition of a moratorium procedure to be added to the 1986 Act.

25. Eligible companies may file at court documents (or apply to the court if the Company is overseas or subject to a winding up petition) for a moratorium preventing various actions, such as their creditors from presenting winding up petitions or have their lease forfeited by their landlord. The purpose of the moratorium is to give the distressed company time to consider their options to (hopefully) rescue the company.

26. Under paragraph A4 of the 1986 Act (as now amended by section 1 of the CIGA 2020) if the Company is subject to an outstanding winding up petition, the directors may apply to the court for a moratorium *"if it is satisfied that a moratorium for the company would achieve a better result for the company's creditors as a whole than would be likely if the company were wound up (without first being subject to a moratorium)"*.

27. Therefore, when faced with a winding up petition, companies (and their advisers) should consider whether a moratorium will achieve a better result for creditors and if so, obtain advice to that effect.

28. It will be interesting to see how the courts, in due course, consider applications by companies for adjournments during winding up proceedings after the expiry of a moratorium.

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