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Client Alert Commentary

Latham & Watkins Litigation & Trial and Restructuring & Special Situations Practices

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Relief for UK Companies: Protection Against Winding-up of Companies Due to COVID-19

A number of decisions have preemptively given effect to the winding up suspension provisions now in force in the Corporate Insolvency and Governance Act 2020.

The COVID-19 pandemic has had a debilitating impact on companies and, particularly, commercial tenants in the UK, especially in the retail and hospitality industries. Many commercial tenants have sought rent and service charge deferrals, and have successfully worked with their landlords and suppliers to weather the pandemic.

Some landlords, however, have not been willing to accept the COVID-19 pandemic, and the measures taken by the government in response, as a valid reason for failing to pay rent. It was clear to the government that measures were required to support the retail and hospitality sectors. The Coronavirus Act quickly passed Parliament and came into force on 25 March 2020. Section 82 prohibited forfeiture and peaceable re-entry for non-payment of rent in respect of relevant business tenancies in the period from 25 March 2020 to 30 September 2020 (as now extended).

The Coronavirus Act did not, however, deal with alternative methods used by landlords to collect rent, such as via statutory demands and threatened winding-up petitions. This exposed a problem: whilst the majority of landlords have been supportive of commercial tenants, some landlords have pursued more challenging debt collection tactics. This behaviour has prompted a further legislative response to bar these tactics and allow companies more generally to restart their businesses (and, if required, to promote restructuring efforts to preserve going concern value for stakeholders and, most importantly, the jobs of employees). The government began to promote this proposed legislation in April 2020.

The Corporate Insolvency and Governance Act 2020

On 23 April 2020, the Business Secretary announced a suite of measures relating to commercial landlords and tenants, including measures to protect high street shops and other companies "from aggressive rent collection". The announcement noted that the "majority of landlords and tenants are working well together to reach agreements on debt obligations, but some landlords have been putting

tenants under undue pressure by using aggressive debt recovery tactics". The announcement described such practices as "unfair".

On 25 April 2020, the government stated that it would "temporarily ban the use of statutory demands (made between 1 March 2020 and 30 June 2020) and winding-up petitions presented from 27 April through to 30 June, where a company cannot pay its bills due to coronavirus".

On 20 May 2020, the government introduced the Corporate Insolvency and Governance Bill (the Bill) to Parliament. Following a highly expedited passage through Parliament, the Bill passed into law on 26 June 2020 as the Corporate Insolvency and Governance Act 2020 (CIGA). For a full briefing on the revisions to the insolvency and restructuring landscape, including permanent and other temporary changes, see Latham & Watkins' webcast UK Corporate Insolvency and Governance Bill: A Practical Guide.)

Re: A Company (Injunction to Restrain Presentation of Petition)[1]

The Court considered the Bill (as it was then) in a number of decisions relating to threatened winding-up petitions. It gave particularly clear guidance in this case, in which Latham represented the applicant.

This matter related to an application by a commercial tenant to restrain its landlord's presentation of a winding-up petition. The landlord had e-filed a winding-up petition in relation to the company on the basis of unpaid rent / service charges. However, the landlord had not yet paid the court fee, so the petition had not yet been presented to the company. Given that, in the absence of an injunction, the landlord could present the petition at any time, the company sought urgent relief. The Court noted that the rationale behind the non-payment was that the company was a high street retailer that had been forced to close the relevant premises in accordance with the instructions from the government in response to the COVID-19 pandemic.

As the Court explained in its decision, the grounds for the application were that: (a) a winding-up order in this case would be harmful to the interests of the creditors generally and would confer no benefit on the proposed petitioning creditor (that is, the landlord); and (b) that the petition was bound to fail, was brought for a collateral purpose, and was an abuse of the process of the court. However, the main focus of the application was the impact of the Bill.

Regarding the Bill, the judge decided that:

a) If the provisions of the Bill were enacted in their then present form, then their effect would be clear, and further, that the policy behind the relevant provisions of the Bill was self-evident.

b) If the Bill became law, a court would have to ask itself whether the COVID-19 pandemic had had a financial effect on the relevant company before the presentation of a winding-up petition, and if that were held to be the case, then the court could only wind up the company if the court were satisfied that the facts on which the petition was based would have arisen even if the COVID-19 pandemic had not had a financial effect on the company.

c) There was a strong case that the COVID-19 pandemic had had a financial effect on the company before the presentation of the petition and, further, that the facts on which the petition would be based would not have arisen if the COVID-19 pandemic had not had a financial effect on the company.

d) The presentation of a petition that would ultimately fail would nonetheless have a seriously damaging effect on the company.

e) Relying on *Hill v C A Parsons*,[2] *Sparks v Holland*,[3] and *Travelodge Ltd v Prime Aesthetics Ltd*[4] (the latter of which was a recent case in which the facts were essentially the same as this one), "when the court is deciding whether to grant relief and, in particular, relief which involves the court controlling or managing its own processes, that it can take into account its assessment of the likelihood of a change in the law which would be relevant to its decision".

f) The court is not powerless to prevent its procedures being used otherwise than for the purpose of obtaining a winding-up order but for the purpose of, or at any rate with the effect of, causing serious damage to the company.

g) "The grant of an injunction to restrain the presentation of the petition is powerfully supported by the clear policy objectives" of the Bill and that he would therefore grant the injunction sought.

Even though the hearing was ex parte, the judge decided that he ought to give the judgment in open court, as the points which were argued in this case might arise in other cases in the near future.

Re: A Company (ICCJ Barber)[5]

The company's application was issued on 13 May 2020 following the presentation by the petitioner of a winding-up petition on 1 May 2020. The petition relied upon a statutory demand dated 19 March 2020 and served on 27 March 2020. The company sought an injunction to restrain the petitioner from advertising the petition and from proceeding with it generally. The company further sought injunctions restraining two further respondents from presenting their own petitions based on statutory demands (each dated 19 March 2020 and served on 27 March 2020). As noted above, the draft Bill was published on 20 May 2020.

It was common ground that the Court should factor the provisions of the Bill into the exercise of its discretion in relation to the company's application, reflecting the decision of Mr Justice Morgan in *Re a Company (Injunction to Restrain Presentation of a Petition)* (as noted above).

To prevent suspension based on paragraph 1 of Schedule 10 of the Bill, the petitioner argued that it was implicit that at least one ground for winding up was s.123(1)(e) Insolvency Act 1986.

Paragraph 2 Schedule 10 then fell to be considered, again involving the "coronavirus test". It was accepted that few petitioners would be able to demonstrate that the coronavirus had not had a financial effect on the company, however on the facts it was found that the relevant ground for winding up (s.123(1)(e) (not caught by the paragraph 1 suspension and subject to the coronavirus test for application of the paragraph 2 suspension) would apply even if the coronavirus had not had a financial effect on the company.

The application of paragraph 5(1)(c) Schedule 10 was considered. The Court stated that the threshold was clearly intended to be a low threshold:

> "[T]he 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".

The application of paragraph 5(3) then fell to be considered:

> "The court may wind the company up under section 122(1)(f) of the 1986 Act on the ground specified in section 123(1)(e) or (2) of that Act only if the court is satisfied that the ground would apply even if coronavirus had not had a financial effect on the company".

The determination was made in favour of the company on the facts.

At present, these cases provide the best means of predicting how the provisions of Schedule 10 of the CIGA will be applied.

Additional protections

On 19 June 2020, the government published a voluntary code of practice between landlords and tenants for commercial property arising as a result of the COVID-19 pandemic.

The suspension of forfeiture of evictions has been extended to 30 September 2020[6] (previously set at 30 June 2020), and a landlord's ability to exercise commercial rent arrears recovery is temporarily prevented unless landlords are owed 189 days' unpaid rent (a number that was previously 90 days). This temporary measure applies until 23 August 2020[7].

Final remarks

The Coronavirus Act did not give commercial tenants enough protection to weather the effects of the lockdown and the evaporation of consumer confidence and spending, putting companies at risk of liquidation and widespread permanent job losses, despite the availability of employee, tax, and (for some businesses) bridging loan schemes. The CIGA includes measures to provide urgent incremental help, and the Court has now made clear that it will use the CIGA to protect businesses in relevant circumstances.

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Endnotes

[1] [2020] EWHC 1406 (Ch).

[2] [1972] Ch 305.

[3] [1997] 1 WLR 143.

[4] [2020] EWHC 1217 (Ch).

[5] [2020] EWHC 1551 (Ch).

[6] The Business Tenancies (Protection from Forfeiture: Relevant Period) (Coronavirus) (England) Regulations 2020 (SI 2020/602) and the Business Tenancies (Extension of Protection from Forfeiture etc) (Wales) (Coronavirus) Regulations 2020 (SI 2020/606).

[7] Taking Control of Goods and Certification of Enforcement Agents (Amendment) (No. 2) (Coronavirus) Regulations 2020 (SI 2020/614) in force (24 June 2020).