

COVID-19: Changes to UK Insolvency Law to Support Affected Businesses

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Corporate

On 28 March, 2020, the UK Government announced that it intends to amend insolvency law to give companies breathing space and allow them to keep trading while they explore options for rescue. The changes include (a) a temporary suspension of wrongful trading by directors of UK companies for three months commencing on 1 March, 2020 and (b) the introduction of a moratorium for companies in financial difficulty preventing creditors enforcing debts for a period of time. Full details of the proposed changes are yet to be published.

Wrongful Trading

Trading uncertainty caused by the COVID-19 situation has made the wrongful trading offence a particular concern for directors. Current insolvency rules provide that directors of a company can be personally liable for the debts of the business if they allow the company to continue to trade once insolvent administration or liquidation becomes unavoidable. Once this point is reached, the directors must take all the steps which a reasonably diligent person would take to minimise any potential loss to the company's creditors. If it appears to the English courts that a director has failed to comply with this duty, the court can order the director to make such personal contribution to the company's assets as it thinks proper.

The UK Government's announcement stated that these wrongful trading rules were deemed to be temporarily suspended from 1 March 2020 for a period of three months. Suspension of the wrongful trading rules will give much-needed comfort to directors making critical decisions regarding the future viability of their businesses without being unduly influenced by the exceptional circumstances which are entirely beyond their control. In particular, it is hoped this suspension will assist directors in accessing new UK Government or bank funding without concerns regarding personal liability.

Existing laws for fraudulent trading—where the director knowingly carries on business with intent to defraud creditors or others for a fraudulent purpose—and the threat of director disqualification will continue as a deterrent against director misconduct during the crisis.

New Restructuring Plan and Moratorium Procedure

The UK Government previously announced plans to introduce new insolvency restructuring procedures in August 2018¹ which will create a much more debtor friendly environment than the current process which puts most of the negotiating power with creditors. The new emergency legislation will accelerate the introduction of the changes which will include:

- A new moratorium procedure to allow businesses to continue trading and keep purchasing needed supplies, while they seek a rescue or restructure. This will be similar to a US Chapter 11 process and will give businesses a period of time when creditors (including secured lenders) cannot take action. This allows the business to source funding or restructure without the constant threat of enforcement.
- Prohibition on suppliers terminating contracts as a result of a business entering an insolvency procedure, a moratorium or a new restructuring plan.
- A new restructuring plan, similar to existing court procedures but simpler to access and more efficient, which will be binding on creditors.

While it is clear that the changes to the wrongful trading regime apply from 1 March, 2020, the timetable for the other legislative changes is currently uncertain, not least as they will need to be approved by Parliament.

The changes are likely to be welcomed by directors of UK companies during these uncertain and turbulent times, but they will still need to ensure they follow existing laws and mitigate the risk of breaching their duties when exploring options for corporate rescue.

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¹ [Consultation on insolvency and corporate governance: government response](#)