

Restructuring across borders
England and Wales

MORATORIUM | FEBRUARY 2024



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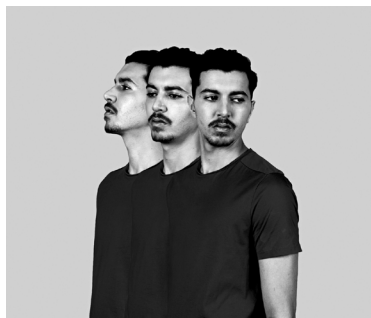
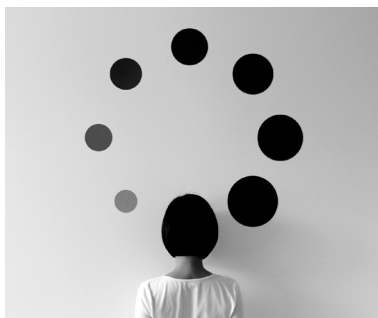
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Introduction

The moratorium is a relatively new procedure which provides companies with a statutory protection from creditors. It was introduced by the Corporate Insolvency and Governance Act 2020 by adding new provisions to the Insolvency Act 1986.

Whilst it is in force, the directors remain in control of the company but an independent monitor (usually an accountant) is appointed to oversee the moratorium process.

The moratorium will prevent creditors from taking certain actions such as initiating insolvency procedures, forfeiting a lease, enforcing security (apart from financial collateral) and commencing or continuing legal proceedings or other legal process against the company and its property. Another major benefit for a debtor who obtains a moratorium is that it will have a statutory payment holiday during which it will not be required to meet payment obligations in respect of certain pre-moratorium debts (with exclusions for payments due under certain financial contracts). The moratorium also triggers the ban on the operation of ipso facto clauses, preventing suppliers of goods and services from terminating or otherwise altering the terms of contracts solely by reason of the company having entered the moratorium. The moratorium may provide some breathing space to a distressed debtor while it negotiates a restructuring. However, given the exclusions from the payment holiday provisions, the debtor may need certain of its creditors (notably, the company's financial creditors) to be on board before commencing this process.

Since the introduction of the moratorium, the procedure has been subject to a number of temporary procedural rules and modifications. This bulletin considers the position for moratoria commenced on or after 1 October 2021, when a number of those temporary provisions expired and the temporary rules were replaced with permanent rules.



Entry into the moratorium

The moratorium is available to both English companies and foreign companies that have a “sufficient connection” to the United Kingdom (subject to certain conditions, described further below). Certain entity types are excluded from the scope of the moratorium – this largely applies to financial institutions such as banks, insurance companies, investment banks, investment firms and securitisation companies, among others. A foreign company wishing to demonstrate a “sufficient connection” to the United Kingdom could rely on the fact that it has contracts or debt governed by English law. In these circumstances, the court, in deciding whether to grant an order commencing a moratorium, will likely consider whether the moratorium would be recognised and have effect in key jurisdictions such as the jurisdiction of incorporation and where any significant assets are located.

For English companies, provided the relevant company is not subject to a winding-up petition, the moratorium can be commenced by the directors filing relevant documents with the court. For any foreign company, or any English company that is subject to a winding-up petition, an application must be made to court seeking an order commencing the moratorium. The court will consider whether the granting of the moratorium would achieve a better result for the company’s creditors than a winding-up without first being in the moratorium and will not order the commencement of the moratorium unless this is the case.

Before a company can enter a moratorium the following conditions must be met:

- (a) the company must not have been in a moratorium, administration, company voluntary arrangement or subject to a winding-up order in the previous 12 months;
- (b) the application must contain certain prescribed information, including a statement by the directors that in their view, the company is, or is likely to become, unable to pay its debts;
- (c) the application must contain a statement from the proposed monitor that the company is an “eligible company”, that the monitor is qualified and they consent to act as monitor in relation to the moratorium; and
- (d) the application must contain a statement from the proposed monitor that, in their view, it is likely that a moratorium for the company would result in the rescue of the company as a going concern.



Effects of the moratorium

For the duration of the moratorium, the following acts are prohibited:

- (a) the presentation of a winding-up petition and the making of a winding-up order by the court (except for petitions made by directors or certain public interest petitions);
- (b) the passing of a resolution for the voluntary winding-up of the company unless recommended by the directors;
- (c) the making of a winding-up order, except on petition by the directors;
- (d) the appointment of an administrator, the appointment of an administrative receiver, or the application for an administration order (except if made by the directors);
- (e) forfeiture of a lease by peaceable re-entry of business premises by a landlord;
- (f) the enforcement of security over the company's property except where security constitutes a collateral security charge or financial collateral or security has been granted during the moratorium with the monitor's consent;
- (g) the repossession of goods under a hire-purchase agreement;
- (h) the commencement or continuation of legal process against the company and its property (with limited exceptions); and
- (i) the crystallisation of a floating charge or any imposition of a restriction on disposal of a floating charge asset.

The court may give permission to creditors to take certain steps above, provided an application for permission may not be made for the purpose of enforcing a pre-moratorium debt for which the company has a payment holiday.

Entry into the moratorium also triggers the ban on the operation of termination or variation clauses in contracts for the supply of goods and services – sometimes referred to as the ban on ipso facto. Broadly speaking this means that where a company enters into the moratorium, suppliers are prohibited from terminating or varying their contracts, or exercising any other rights, solely as a consequence of the counterparty entering into the moratorium (although there are broad exceptions both for counterparty type and types of contract). Further information on this regime can be found in “England and Wales – Overview” factsheet available [here](#).



Duration of the moratorium

The moratorium will be for an initial period of 20 business days (beginning with the business day after it comes into force) with the possibility of extension by a further 20 business days by filing certain documents with the court (at any time after the 15th business day of the initial period). This one-time extension can be done by the directors without the consent of the creditors. We expect that most companies wishing to extend the initial moratorium will rely on this relatively straightforward option to begin with and, provided there is sufficient monies to pay the required debts, many moratoria will last for at least 40 business days.

In addition to the one-time extension route mentioned above, there are a number of other possibilities for extension:

- (a) the directors may extend the initial period (more than once) for a maximum period of up to 12 months from its commencement by obtaining creditor consent;
- (b) the directors may apply directly to court (more than once) for an order to extend the initial period. The court may make any order it deems appropriate taking into account the interests of the pre-moratorium creditors and whether the continuation of the moratorium will help rescue the company;
- (c) where the moratorium has been used prior to a proposal for a company voluntary arrangement, the moratorium is automatically extended until the proposal is implemented, accepted or rejected by creditors or withdrawn by the company; and
- (d) where the moratorium has been used prior to a scheme of arrangement or a restructuring plan, the moratorium may be extended over the duration of the scheme of arrangement or restructuring plan at the court's discretion.

Where creditor consent is required, consent is obtained:

- (i) if, of those voting, a majority (in value) of the pre-moratorium creditors for which the company has a payment holiday and whose claims have not been paid or otherwise discharged, vote in favour of the proposed decision; and
- (ii) provided that, of the total number of creditors voting in respect of the proposed decision that are unconnected with the company, a majority of those unconnected creditors have not voted against the proposed decision.

In other words, it is only those creditors who have not been paid during the moratorium who need to consent (with certain protections against connected creditors pushing through a vote). Lenders and other creditors with excluded contracts will not be given any consent rights.

The moratorium can only be extended if, at each extension, the directors confirm that the company has made all the payments it was supposed to make during the moratorium and the monitor confirms that the moratorium is likely to result in the rescue of the company as a going concern.

Payment obligations during the moratorium

During the moratorium, the company is given a “payment holiday” in respect of certain pre-moratorium debts, meaning that it does not have to pay those debts for the duration of the moratorium. Indeed, the company is not permitted to pay these debts where payments exceed, in aggregate, GBP5,000 or 1% of the total owed to unsecured creditors when the moratorium began unless the monitor consents to such payment. The company will be required to continue to pay all moratorium debts and any pre-moratorium debts that are not subject to a payment holiday.

A pre-moratorium debt is any debt or other liability of the company (other than an excluded debt) that has fallen due prior to the commencement of the moratorium or which becomes due during the moratorium but under an obligation incurred by the company prior to the commencement of the moratorium. This would include obligations under contracts entered into pre-moratorium but where payments fall due post moratorium.

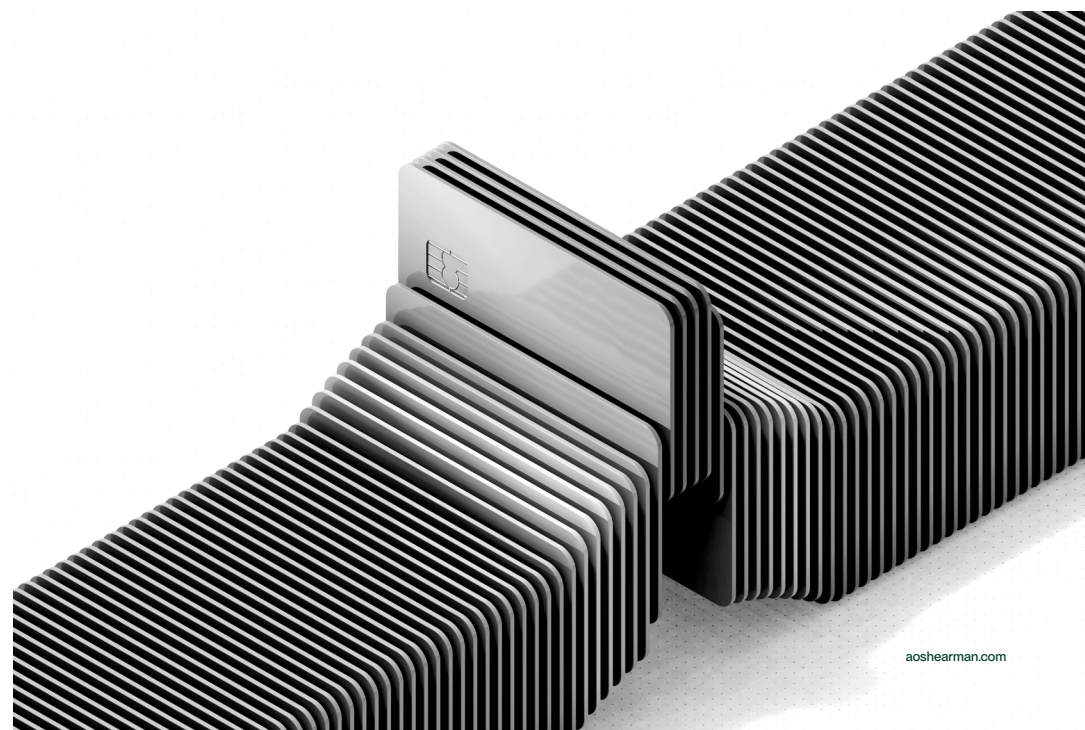
Conversely, a moratorium debt is any debt or other liability that the company becomes subject to during the moratorium (other than by reason of an obligation entered into prior to the moratorium) or to which the company may become subject after the end of the moratorium because of an obligation incurred during the moratorium. An example might be a debt arising under a new contract entered into by the company during the moratorium period.

Apart from excluded debts (referred to below), most pre-moratorium debts will be subject to a payment holiday. In other words, the company will not be obliged to pay those debts during the moratorium. The only exception to this is those pre-moratorium debts in so far as they consist of amounts payable in respect of:

- (a) the monitor’s remuneration or expenses;
- (b) goods or services supplied during the moratorium (and which would otherwise be pre-moratorium debts because the supply contract was entered into pre-moratorium);
- (c) rent in respect of a period during the moratorium (under leases entered into pre-moratorium);

- (d) wages or salary arising under a contract of employment, regardless of when those wages or salary fall due;
- (e) redundancy payments, regardless of when those payments fall due; or
- (f) debts or other liabilities arising under a contract or other instrument involving financial services. These include (amongst others) financial contracts (loans, financial leases, guarantees or commitments, commodities contracts, securities contracts), securitisation transactions, derivatives and spot contracts, capital market investments, market contracts etc.

The company is expected to keep making payment on the pre-moratorium debts listed in paragraphs (a) to (f) for the duration of the moratorium; this means all payments due under loan agreements and other financial services contracts should continue to be paid. If they are not paid, although the creditor is prohibited from presenting a winding up petition or applying for administration, the monitor is required to bring the moratorium to an end – at which time a winding up petition or administration application could be filed.



Effect on secured assets

During the moratorium, the company may continue to dispose of secured assets, either in accordance with the terms of the security or with permission of the court. This means that assets subject to a floating charge can continue to be disposed of in the ordinary course and holders of a floating charge are not permitted to crystallise the floating charge in order to inhibit such disposal. The right to crystallise the charge is not lost but is deferred and can be exercised by the charge holder as soon as practicable after the moratorium terminates.

Any provision in an instrument creating a floating charge that triggers crystallisation of the floating charge, imposes any restrictions on disposal of the company's property or provides for the appointment of a receiver on the commencement of a moratorium or anything done with a view to commencing the moratorium is void. Although this will happen

automatically by operation of law, the parties to a security agreement may want to carve the moratorium out from the crystallisation provisions to ensure that the rest of the clause is preserved.

These restrictions do not apply to a floating charge that is: a collateral security; a market charge; a security financial collateral arrangement; or a system charge (each as defined in the Insolvency Act 1986).

Where assets are sold with the permission of the court, the company must pay the secured creditors any net proceeds received and any additional money required to be added to the net proceeds to produce a total amount, which in the court's determination, would have been realised on a sale of the property in the open market by a willing vendor.



Termination of the moratorium

The moratorium is intended to be a gateway or an initial step to a company completing a recovery. There are therefore a number of ways that it might come to an end, as follows:

- (a) by agreement (for example upon the company entering into a consensual restructuring with its creditors);
- (b) when a court order sanctioning a scheme of arrangement or restructuring plan comes into effect;
- (c) automatically upon entry into a voluntary winding-up, administration or interim moratorium prior to administration and liquidation or initial steps to initiate such proceedings;
- (d) automatically upon the expiry of the moratorium time limit; and
- (e) by a court order.

The monitor will also be obliged to bring the moratorium to an end in certain circumstances including if the debtor ceases, or is likely to be unable, to pay amounts falling due during the moratorium, if the moratorium is no longer likely to result in a rescue of the company as a going concern or the directors are not

cooperating with the monitor to provide information. When deciding whether or not to bring a moratorium to an end on the basis that the monitor thinks that the company is likely to be unable to pay amounts falling due during the moratorium, the monitor may disregard any debts that:

- (i) the monitor has reasonable grounds for thinking are likely to be paid or compounded to the satisfaction of the creditor within 5 business days of the decision; and
- (ii) the creditor has agreed to defer payment until a time that is later than the decision.

Furthermore, the actions otherwise prohibited by the moratorium can be taken either with the consent of the monitor or the court. The monitor must consider, and the court is likely to consider, whether any such action will support the rescue of the company as a going concern.

The moratorium itself can also be challenged on the ground that the eligibility criteria and qualifying conditions are not met or that the continuation of the moratorium would result in unfair harm to the applicant's interests.

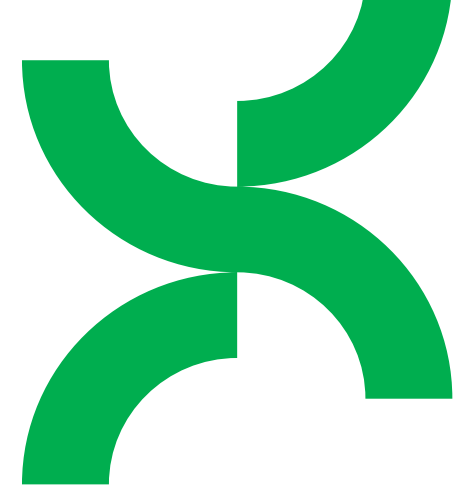
The hope will be that the company will emerge from the moratorium having achieved a rescue as a going concern and business will carry on as usual. However, if the company enters into a winding-up or administration process within 12 weeks following the end of the moratorium (or proposes a scheme of arrangement or restructuring plan in this period), there is an impact on the priority of creditors in such winding-up, administration, scheme or plan. Any debts that were not subject to the payment holiday in the moratorium but which were not paid will have priority over all other debts (except fixed charges), ie they will come ahead of preferential creditors, the prescribed part and floating charge holders. There is an exclusion, however, for debts arising under financial contracts where there has been an acceleration of that contract. This is important because otherwise the entire amount of an accelerated loan or bond would have priority under these provisions.

To date, we are only aware of the moratorium having been used in a a small number of cases.



Key contacts

If you require advice on any of the matters raised in this document, please contact any of our partners or your usual contact at A&O Shearman, or email rab@aoshearman.com.



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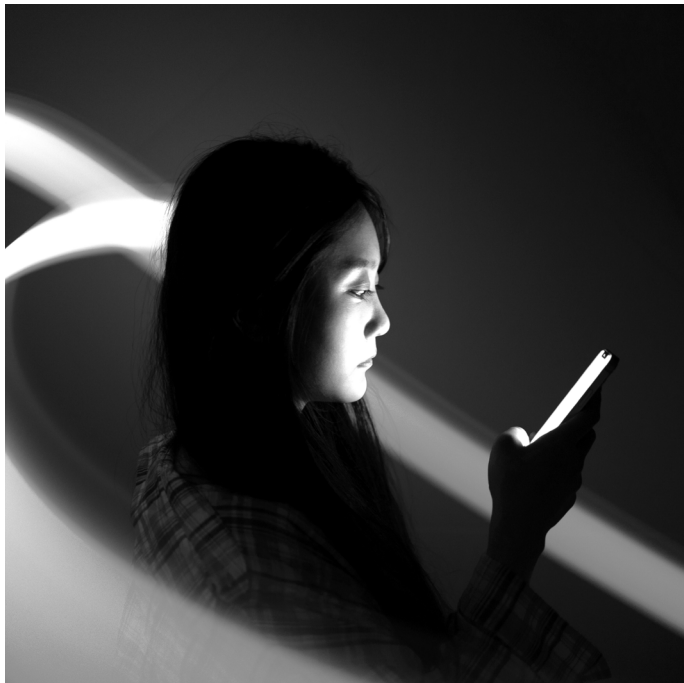
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Further information

Developed by A&O Shearman's market-leading Restructuring group, "**Restructuring Across Borders**" is an easy-to-use website that provides information and guidance on all key practical aspects of restructuring and insolvency in Europe, Asia, the Middle East and the U.S.

To access this resource, please [click here](#).



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