

EXPLANATORY MEMORANDUM TO
THE CORPORATE INSOLVENCY AND GOVERNANCE ACT 2020
(CORONAVIRUS) (EXTENSION OF THE RELEVANT PERIOD) REGULATIONS
2021

2021 No. 375

1. Introduction

- 1.1 This explanatory memorandum has been prepared by the Department for Business, Energy and Industrial Strategy and is laid before Parliament by Command of Her Majesty.
- 1.2 This memorandum contains information for the Joint Committee on Statutory Instruments.

2. Purpose of the instrument

- 2.1 This instrument makes provision to further extend the duration of some of the temporary measures introduced by the Corporate Insolvency and Governance Act 2020 (c. 12) (CIG Act) beyond their current expiration dates, namely: restrictions on the use of statutory demands and winding up petitions from their current expiry date on 31 March 2021 to 30 June 2021; the modifications to moratorium provisions and temporary moratorium rules from their current expiry date of 30 March 2021 to 30 September 2021; and the small supplier exemption from termination clause provisions from its current expiry date of 30 March 2021 to 30 June 2021.
- 2.2 This instrument also extends provisions suspending liability for wrongful trading in the Corporate Insolvency and Governance Act 2020 (Coronavirus) (Suspension of Liability for Wrongful Trading and Extension of the Relevant Period) Regulations 2020 (S.I. 2020/1349), made under the CIG Act, from the current expiry date of 30 April 2021 to 30 June 2021.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

- 3.1 The instrument is made using the powers given by section 20 and section 41 of the CIG Act to make regulations which amend or modify corporate insolvency or governance legislation, and to extend temporary provision in the CIG Act respectively and is subject to the made affirmative procedure. The power to amend or modify corporate insolvency or governance legislation given by s.20(1)(c) includes a number of conditions which must be satisfied before that power may be exercised. In summary, it must be expedient to modify the duties or liabilities of persons with corporate responsibility due to the effect of coronavirus on businesses or the economy of the United Kingdom, and the Secretary of State must have considered the effect of the regulations on those likely to be affected by them. The Secretary of State must also be satisfied that the need for regulations is urgent, the regulations are proportionate, and that the same result cannot be achieved either without legislation or by using a different power. The Secretary of State must also keep the need for the regulations under review and revoke or amend them if appropriate. This power is being used to amend secondary legislation.

- 3.2 The power to extend the insolvency measures under section 41(1)(b) CIG Act includes a condition which must be met for the relevant measures to be extended. The condition requires the Secretary of State to consider it reasonable to prolong the relevant period of the temporary measures to mitigate an effect of coronavirus. This power is being used to amend primary legislation.

Matters relevant to Standing Orders Nos. 83P and 83T of the Standing Orders of the House of Commons relating to Public Business (English Votes for English Laws)

- 3.3 The territorial application of this instrument includes Scotland.
- 3.4 The powers under which this instrument is made cover England, Wales and Scotland (see section 48 CIG Act) and the territorial application of this instrument is not limited by the Act or the instrument.

4. Extent and Territorial Application

- 4.1 The territorial extent of this instrument is England, Wales and Scotland.
- 4.2 The territorial application of this instrument is England, Wales and Scotland.

5. European Convention on Human Rights

- 5.1 The Minister for Climate Change and Corporate Responsibility, Lord Callanan, has made the following statement regarding Human Rights:

“In my view the provisions of Corporate Insolvency and Governance Act 2020 (Coronavirus) (Extension of the Relevant Period) Regulations 2021 are compatible with the Convention rights.”

6. Legislative Context

- 6.1 The CIG Act contains both permanent provisions about corporate insolvency and temporary measures that have provided businesses with protection as they continue to be unable to trade at full capacity, or at all, as a result of national COVID-19 restrictions. The measures are designed to help UK companies and other similar entities by easing the burden on businesses and helping them avoid insolvency during the period falling after Spring 2020.
- 6.2 The CIG Act, as amended by the Corporate Insolvency and Governance Act 2020 (Coronavirus) (Extension of the Relevant Period) Regulation 2020 (S.I. 2020/1031) and the Corporate Insolvency and Governance Act 2020 (Coronavirus) (Extension of the Relevant Period) (No.2) Regulations 2020 (S.I. 2020/1483), provides that the temporary provisions in Schedule 10 relating to winding up petitions will automatically expire on 31 March 2021; the temporary provisions in Schedule 4 relating to the moratorium procedure and the moratorium rules will automatically expire on 30 March 2020; and the temporary provisions in section 15 relating to the small supplier exemption will automatically expire on 30 March 2020, unless regulations are made to prolong the period within those provisions have effect.
- 6.3 The suspension of liability for wrongful trading provisions, which are contained in the Corporate Insolvency and Governance Act 2020 (Coronavirus) (Suspension of Liability for Wrongful Trading and Extension of the Relevant Period) Regulations 2020 (S.I. 2020/1349), were made using the temporary power given in section 20 of the CIG Act. This was done to support directors to continue trading through the pandemic without the threat of personal liability when national restrictions were

reintroduced late in 2020. The current wrongful trading provisions will automatically expire on 30 April 2021 unless regulations are made to prolong the period within which they have effect.

Powers to extend temporary measures

- 6.4 The power to extend the temporary measures is provided by section 41(1) of the CIG Act, which states that the Secretary of State may use a statutory instrument to prolong a relevant provision for a period of up to six months if it is reasonable to do so to mitigate an effect of coronavirus. The measures eligible for extension are the provisions restricting the use of statutory demands and winding up petitions, modifications to the moratorium and the temporary moratorium rules, and the small supplier exemption from termination clauses.
- 6.5 Temporary changes made in this way may last for a maximum of 6 months but can be extended using a similar "made affirmative" process. The temporary changes may also be curtailed through an SI subject to a negative resolution process and they must be revoked or amended, if it is clear that the impact of the pandemic has eased sufficiently.

Powers to make regulations to amend corporate insolvency or governance legislation

- 6.6 The power in section 20(1) of the CIG Act enables the Secretary of State to make regulations of time-limited effect to amend or modify insolvency law to, amongst other things, change or disapply any duty of a person with corporate responsibility or the liability of such a person to any sanction.
- 6.7 Regulations made using this power may only have effect for a period not exceeding 6 months, but this does not prevent further regulations from being made to extend the period for which earlier regulations apply by up to a further 6 months.

Measures within the scope of this SI

Restrictions on the use of statutory demands and winding up petitions

- 6.8 Section 10 and Schedule 10 of the CIG Act temporarily prevents creditors from relying on statutory demands to bring winding-up petitions and are prohibited from filing winding-up petitions where the company's inability to pay is due to COVID 19.

Modifications to moratoriums

- 6.9 Section 3 and Schedule 4 of the CIG Act introduced temporary relaxations which enable companies to enter moratoriums. In normal trading conditions a company in financial distress that wishes to enter a moratorium (i) must not have been subject to another insolvency procedure in the previous 12 months and (ii) where the company is subject to a winding-up petition, it must first apply to court before a moratorium may be entered; under the CIG Act both of these were relaxed as described below in paragraphs 6.10 and 6.11.
- 6.10 Under the CIG Act temporary relaxation, a company subject to a winding up petition can access a moratorium by filing the relevant documents at court but need not make an application to court;
- 6.11 Under the CIG Act temporary relaxation, a company that has been subject to a CVA, been in administration or in a moratorium in the last 12 months can enter a moratorium;

- 6.12 Negotiating and arranging a company rescue (and/or seeking new investment) can be a protracted process and extending these measures to 30 September 2021 will support companies in their recovery from the economic effects of the pandemic.

Temporary moratorium rules

- 6.13 Prior to the CIG Act there was no free-standing moratorium available for UK companies. The requirements on prospect for rescue, bringing the moratorium to an end, and certain of the exclusions for entry have been temporarily amended to account for the COVID-19 pandemic and will be replaced by permanent provisions that will sit within the Insolvency (England and Wales) Rules 2016 SI 2016/1024 and Scottish equivalent.

Small supplier exemption from the termination clause provisions

- 6.14 Section 14 of the CIG Act prohibits the use of termination and other insolvency related clauses in contracts for the supply of goods and services unless exempted as a small entity.
- 6.15 Section 15 of the CIG Act provides relief for small companies temporarily from the requirement to continue supplying whilst the economy recovers, and trading conditions improve following the conclusion of fiscal measures.

Wrongful Trading

- 6.16 The suspension of liability for wrongful trading provisions, which are contained in the Corporate Insolvency and Governance Act 2020 (Coronavirus) (Suspension of Liability for Wrongful Trading and Extension of the Relevant Period) Regulations 2020 (S.I. 2020/1349), modify the effect of sections 214 and 246ZB of the Insolvency Act 1986. The suspension provisions require a court considering what contribution to the company's assets it is proper for a person to make under those sections, to assume that person is not responsible for any worsening of the company's position that occurs between 26 November 2020 and 30 April 2021. This instrument extends that period from 30 April 2021 until 30 June 2021.

7. Policy background

What is being done and why?

- 7.1 This instrument extends a number of temporary insolvency measures, specifically a restriction on the use of statutory demands and winding-up petitions, a small-supplier exemption from the scope of the prohibition on termination clauses in supply contracts, and temporary modifications to the operation of the company moratorium procedure as well as temporary administrative rules for the operation of that procedure, and also extends the suspension of personal liability for wrongful trading.
- 7.2 The reason for extending the duration of the temporary insolvency measures is to continue to support businesses, many of which would be viable were it not for the emergence of COVID-19 and the continued national restrictions which have prevented business from trading at full capacity, or at all. This extension ensures that the measures remain available to companies that may be in financial difficulties caused by the pandemic and the duration of the extension for each measure has been determined having regard to the nature of the measure in question.

- 7.3 The restrictions placed on the use of statutory demands and winding-up petitions are extended to 30 June 2021. These restrictions help to protect companies from aggressive creditor action during the period when companies are continuing to be financially impacted by coronavirus, such as restrictions on being able to trade. The extension of these measures means creditors cannot rely on statutory demands to bring winding-up petitions and are prohibited from filing winding-up petitions where the company's inability to pay is due to coronavirus. It is nevertheless recognised that this temporary measure is a significant intervention into the normal working of insolvency law.
- 7.4 The temporary rules, and modifications detailed in Schedule 4 that allow the operation of the company moratorium are extended to 30 September 2021 and provides companies in financial difficulty with protection from creditors whilst they consider a rescue solution. The temporary modifications to moratoriums being extended by this instrument relax the normal eligibility criteria to enter into a moratorium which recognises the extraordinary and temporary difficulties being caused by coronavirus, in order to make the moratorium as widely available as possible. The extension of six months is the maximum possible at any one point.
- 7.5 The temporary modifications to moratoriums also provide temporary procedural rules to enable the operation of the moratorium. It was necessary to provide temporary moratorium rules in the CIG Act to ensure the procedure was operational as soon as the legislation came into force. These temporary rules need to remain in place to allow time for permanent rules to be drafted (and in respect of those for Scotland for the agreement of Scottish Ministers to be obtained) so that the permanent rules come into force in both jurisdictions on the same date. It would also be undesirable to require business to adjust to new procedural rules at a time of great economic uncertainty such as having to adapt to Government fiscal support being withdrawn and other regulatory changes as a result of coronavirus.
- 7.6 The small-supplier exemption from the termination clause prohibition is extended to 30 June 2021. The termination clause provisions in the CIG Act prohibit contractual terms that allow contracts to be terminated if a customer enters an insolvency procedure. To help support small business suppliers who are more likely to experience a greater impact from the effects of coronavirus, the CIG Act included a temporary carve-out which excludes small suppliers from the scope of the termination clause measure. Extending this measure provides certainty to small suppliers that whilst they attempt to recover from any financial impact coronavirus has had on their business, they can continue to rely on contractual termination clauses where their customer has entered a formal insolvency procedure.
- 7.7 The suspension of personal liability for wrongful trading protects directors of companies rendered insolvent by the pandemic from being held personally liable for debts incurred by the company during the insolvent period if they continue to use their best efforts to trade.
- 8. European Union (Withdrawal) Act/Withdrawal of the United Kingdom from the European Union**
- 8.1 This instrument does not relate to withdrawal from the European Union / trigger the statement requirements under the European Union (Withdrawal) Act.

9. Consolidation

9.1 Not applicable.

10. Consultation outcome

10.1 There has been no public consultation in relation to this instrument, however Government has engaged informally with a range of stakeholders, including business representative organisations and investor groups on these matters.

11. Guidance

11.1 The Insolvency Service issues regular bulletins to interested parties; these will be used to raise awareness of the new provisions and procedural changes at the time of laying this instrument to ensure public awareness.

12. Impact

12.1 There will be a positive impact on all businesses, charities and voluntary bodies that may be subject to a winding up petition due to their inability to pay debts as a result of coronavirus by giving essential breathing space in order to negotiate with their creditors or seek a rescue plan, or both. There will also be an adverse impact on those creditor businesses that have outstanding debts owed by other businesses which they will temporarily be unable to enforce unless they are able to demonstrate that those debts are not coronavirus related. This temporary removal of their rights to enforce their debts may increase their risks when doing business. However, the Government assesses this temporary rebalancing of risks as an appropriate intervention, alongside the Government's wider fiscal support and other regulatory interventions. The small supplier exemption to the termination clause provisions will assist small businesses, which represents 99% of the business community, although 63% of turnover is through businesses that do not fall within the definition of a small business. The temporary moratorium measures will make the procedure more accessible to companies during this difficult period, which therefore provides breathing space for companies to consider rescue and restructuring options, which ultimately could lead to the rescue of more companies impacted by coronavirus.

12.2 In respect of the wrongful trading measure, if businesses, charities, or voluntary bodies are creditors in a company winding up or administration then they may be financially worse-off if the insolvency office-holder is unable to recover a contribution from directors, or former directors, under the wrongful trading provisions. This is because the insolvent company will have fewer assets available for distribution to creditors. The amount that any creditor would stand to recover in any given insolvency is, however, dependent upon a range of factors, such as the number of creditors, the company's assets and liabilities, and whether a debt is secured or unsecured. The suspension of the wrongful trading provisions will therefore have a potential impact but cannot be said to have a specific quantifiable adverse impact upon any given business, charity or voluntary body.

12.3 The impact on the public sector falls on public sector creditors such as HMRC and local authorities that use winding up petitions to enforce national and local taxation and other related debts. However, the Government has assessed that any impact is an appropriate temporary intervention alongside with the Government's wider interventions.

- 12.4 An impact assessment has not been prepared for this instrument as it falls under the Civil Contingencies Exclusion and the administrative requirement to account for the impact of the measures on the Business Impact Target required by the better regulation framework will be done at the appropriate time. A full impact assessment was carried out for the CIG Act which considered costs & benefits in a steady state economy: <https://publications.parliament.uk/pa/bills/cbill/58-01/0128/IA200519.pdf>.

13. Regulating small business

- 13.1 The legislation applies to activities that are undertaken by small businesses.
- 13.2 No specific action is proposed to minimise the regulatory burdens on small businesses though it is expected that smaller sized businesses are more likely to benefit from the restrictions this instrument temporarily imposes.
- 13.3 The basis for the final decision on what action to take to assist small businesses is that the instrument is itself a temporary relaxation, or removal, of requirements that would otherwise apply under legislation.

14. Monitoring & review

- 14.1 The instrument does not include a statutory review clause; however, the Government will continue to monitor the need for these measures. The legal effect of the various provisions in this instrument will automatically expire on various dates that are specified in the instrument itself. At the time that the various provisions are due to expire it will be necessary to review whether the provision made by this instrument continues to be necessary and whether to re-exercise the power so as to further prolong the duration of the temporary provision.

15. Contact

- 15.1 Louise Chester at the Insolvency Service (Telephone: 0300 304 8357 or email: louise.chester@insolvency.gov.uk) can answer questions about these Regulations.
- 15.2 Angela Crossley, Director of Strategy and Change at the Insolvency Service can confirm that this Explanatory Memorandum meets the required standard.
- 15.3 The Minister for Climate Change and Corporate Responsibility, Lord Callanan at the Department for Business, Energy and Industrial Strategy can confirm that this Explanatory Memorandum meets the required standard.