Newsletter June 2020

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INSOLVENCY LAW FIRM

Update

Welcome to the CRI Insolvency Law update, a summary of recent judgments and insolvency related reports and news items which we hope you find of interest.

Corporate Insolvency and Governance Act 2020

The Corporate Insolvency and Governance Act 2020 received Royal Assent on 25th June 2020 and came into force at midnight.

This Act creates the largest change to the corporate insolvency regime in more than 20 years. Reams of text have already been produced on the subject and we do not intend to replicate that.

One of the key provisions is the introduction of the new role of a "Monitor" to oversee the moratorium period it introduces. This is a role reserved for licenced insolvency practitioners, and so another tool for them to utilise when advising businesses. We look forward to seeing how the changes introduced by the Act work in practice.

Carrick Read Insolvency is a specialist insolvency law practice providing legal and technical advice to insolvency practitioners, debtors and creditors involved in the insolvency process.

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Issues surrounding the Government Furlough Scheme and insolvency framework

Carluccios

On 30th March 2020 Carluccios Ltd entered administration. The Italian restaurant chain employed approximately 2,000 staff nationwide. Due to the coronavirus pandemic the Government had implemented a Furlough Scheme ("the Scheme") for employees who were unable to work due to the outbreak and confirmed the scheme was intended to apply to companies in administration. However, the Government had only provided limited guidance on the Scheme and how it would interact with the current insolvency framework.

The Administrators in the case wanted employees to be Furloughed to allow the employees to form part of any future sale of the business as a going concern. The administrators did not however, want to furlough staff if it meant that it would increase their liability later on down the line pursuant to para 99 Schedule B1 Insolvency Act 1986. Para 99 provides that where Administrators adopt employment contracts 14 days after their appointment any liability due to employees under the employment contract will become a super-priority. The Administrators issued letters to staff explaining they wished to put staff onto the Scheme, but would only be able to pay employees once the company had received funds from the Government and made it clear to employees that their consent was required in order to be placed on the Scheme. The vast majority (around 95%) of employees consented to the change, a minority objected and around 4% failed to respond by the deadline.

The administrators applied to court for guidance as to how the Scheme should be implemented in line with current insolvency legislation.

Snowden J considered submissions from the Administrators and Unite Union who represented some of the employees.

He concluded that in terms of those employees who consented to the Administrators' letter this had the effect of amending the contract between Carluccios and the employees so that the company's liability to the employees was limited to the amount received from the Government under the Scheme. As for those employees who objected to the variation letter, their contracts would not be altered, and they would be made redundant. For the employees who did not respond by the stipulated deadline, Snowden J concluded that the employees consent could not be inferred as the variation letter specifically requested a positive response from employees failing which they would be at risk of being made redundant.

The Judge did not consider para 66 of Schedule B1 to have any assistance. He

further rejected submissions that para 99 (5) required employees to render their services and held para 99 would be applicable to employees under the Scheme. The Judge considered the decision of *Powdrill v Watson & Anor (Paramount Airways Ltd)* and considered that just because the administrators had failed to terminate the employment contracts, it did not necessarily mean that the employment contracts had been adopted, for the contracts to be adopted it required election by the Administrators. In normal circumstances election can be inferred from the company requiring the employee to continue working, which was not possible due to the Covid-19 pandemic. The Judge considered the position of the three types of employees:

Consenting Employees

Their employment contracts had been varied by the acceptance of the variation letter, agreed within the initial 14 days of the administration and that nothing up to that point attracted super-priority. For the purposes of para 99 (5) the contracts were adopted at the point of applying to the Scheme and/or making payment to the employees under the Scheme.

Objecting Employees

Their employment contracts would not be adopted.

Employees who failed to respond

Their contracts were not considered to be adopted simply because the Administrators had failed to terminate their contracts within the initial 14 day period. These individuals would not be required to work and although the contract would still continue it would not attract super-priority under para 99. Should the employees respond to the Administrators at a later date it would not impose super-priority on any liabilities incurred up to that point. The later acceptance would have the effect of classifying the employee as a consenting employee.

Re Carluccio's Ltd [2020] EWHC 886 (Ch)

Debenhams

Two days after the above Judgment regarding Carluccios, Trower J received a similar application from the administrators of Debenhams seeking directions on the Scheme. The two cases share similar facts however the main difference between the two cases is that when Debenhams entered administration on 9th April 2020 the company had already furloughed the majority of its 15,500 staff. The Administrators had calculated that should the employment contracts attract super-priority it may result in an additional

liability of approximately £3m per month. The Administrators sought a direction that they could implement the Scheme without formally adopting the employment contracts.

The Judge ultimately held that the fact employees had been placed on the Scheme prior to the Administration made no material difference. The Judge directed that the Administrators were at liberty to act on the basis that, if at any point after 14 days of their appointment they caused the company to make payments to employees in accordance with their employment contract, including amounts under the furlough scheme it would constitute adoption of the employment contract and trigger super-priority.

The above Judgments are a clear warning to administrators and Government of the conflicts between the Scheme and the rescue culture. Administrators should be live to the issues surrounding Furloughed workforces and the implications of those employment contracts having super-priority pursuant to para 99.

Re Debenhams Retail Limited [2020] EWHC 921 (Ch)

Statutory Demand Ban

In a recent case the High Court has given effect to the Governance and Corporate Insolvency Bill and the ban on statutory demands despite, at that time, the Bill not being passed. In *Re A Company 2020 EWHC 1406 (Ch)* the High Court granted an injunction to a retail tenant to prevent its Landlord relying on a statutory demand served in April 2020. The court considered that Covid-19 had had an impact on the tenants finances and that presenting a winding up petition would be damaging to the company even though it would not be possible for the petition to be successful due to the ban.

This case makes it clear that the courts are willing to take action against statutory demands prior to the ban becoming law.

Re A Company 2020 EWHC 1406 (Ch)

Administration Appointments

There have been a number of cases concerning potentially defective appointment of administrators. In a recent case HHJ Davies-White QC has attempted to provide some order to the various first instance decisions in this area and in doing so reviewed over 30 decisions on the subject.

In this case the Directions served a notice of its intention to appoint administrators on a qualifying floating charge holder, who subsequently consented. The Directors then filed a notice of appointment of administrators, but failed to file FCA consent, which had not been sought or filed. Searches to the FCA register showed that the company had been incorrectly registered without full stops after the

initial letters in its name, however, the company was in essence registered and required FCA consent to appoint administrators.

This was discovered one month into the appointment and the Directors applied to court for a retrospective appointment or in the alternative, relief.

HHJ Davies-White held that that for a regulated company FCA consent went to the genesis of the power to appoint administrators, rather than being a procedural requirement and therefore obtaining retrospective consent from the FCA would not on its own be sufficient. Adopting the approach in *Pettit v Bradford Bulls (Northern) Ltd* HHJ Davies-White granted an order to retrospectively appoint the administrators from the date of their initial but unsuccessful, out of court appointment. A number of questions were considered by the Judge, firstly the consequences of the breach, ultimately concluding that FCA consent was required to be lodged no later than with the notice of appointment. Secondly, the effect of the breach, in his decision the Judge emphasised the FCA's position as a regulator and its duty to protect the public interest and held that FCA approval was a trigger to appointing administrators, as opposed to a procedural requirement. Thirdly, if the appointment was invalid could it be cured by a retrospective order. HHJ Davies-White relied on the authority of *Bradford Bulls*, which had been relied upon for a number of years and commented that should there be a challenge to this jurisdiction it should be referred to the Court of Appeal.

A.R.G. (Mansfield) Ltd; Gregory & Ors v A.R.G. (Mansfield) Ltd [2020] EWHC 1133 (Ch)

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