



A creditor's guide to the moratorium

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A licensed insolvency practitioner ('IP') has given you this because you, or your business, may be owed money by a company that is in a moratorium.

This guide aims to help you understand your rights as a creditor and to describe how best these rights can be exercised. It is intended to relate only to England and Wales. It is not an exhaustive statement of the relevant law or a substitute for specific professional or legal advice.

We have made every effort to ensure the guide is accurate, but R3 cannot accept responsibility for the consequences of any action you take in reliance on its contents. If, having read the guide, you remain in any doubt about your rights, you should consult a licensed IP or solicitor.

We hope that you will read this guide carefully and consider whether taking an active role as a creditor in this case could benefit you or your business.

In what circumstances does a company find itself in a moratorium?

The moratorium is a statutory standalone procedure for eligible companies. It is a tool available to distressed companies (insolvent or likely to become insolvent), intended to provide them with a short breathing space to explore rescue and restructuring options, free from creditor action. The moratorium process will be overseen by a licensed IP acting as a 'monitor' although the directors will remain in charge of the day-to-day running of the company (sometimes referred to as 'debtor-in-possession' where the debtor is the company).

How can a company be placed into a moratorium?

A company may be placed into a moratorium by the directors filing the relevant documents in court (there is no court hearing). These documents include:

- a statement to the effect that they wish to apply for a moratorium and that the company is, or is likely to become, unable to pay their debts; and
- a statement from the proposed monitor that in their view, it is likely that a moratorium would result in the rescue of the company as a going concern.

However, if:

- there is an outstanding winding up petition, or
- it is an overseas company

the directors will have to apply to court for an order placing the company into a moratorium. The court will only make an order where it is satisfied that the moratorium would achieve a better result for the company's creditors, as a whole, than would be likely if the company were wound up (without first being in a moratorium).

Further to note, a company will not be eligible to obtain a moratorium if:

- it is already subject to a moratorium or an insolvency procedure,
- at any time in the previous 12 months, the company was subject to a moratorium or any insolvency procedure.

In addition, certain companies in regulated markets are excluded from being able to access the moratorium, for example, banks and insurance companies.

How long does a moratorium last?

The purpose of a moratorium is to provide companies in distress with a temporary period of protection from creditor action to allow them to fully explore the possible rescue of the company as a going concern. During this 'breathing space' the company has a 'payment holiday' in respect of most debts and liabilities to which the company either became subject to before the moratorium or becomes subject to during the moratorium period but relating to an obligation incurred before the moratorium (pre-moratorium debts).

A moratorium is a standalone process which is not linked to a particular insolvency procedure. It may be that a company is able to use the protection of a moratorium to formulate a rescue plan without the need to enter into a formal insolvency procedure.

What is a monitor?

During the moratorium a monitor is appointed by the company or court (as applicable). The monitor must be a licensed IP and in relation to the moratorium is an officer of the court. Joint monitors are permitted. The monitor must consent to their appointment, and state that the company is an eligible company and 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.

The monitor does not displace management but monitors the company's affairs during the moratorium for the purpose of ensuring that nothing happens which alters their view as to the appropriateness of the moratorium being in place. At no time is a monitor(s) in charge of the day to day running of the company.

Other than when occurs automatically, the monitor has to re-state their view as to the likely rescue of the Company for each proposed extension of the moratorium.

What are the powers and duties of a monitor?

The monitor has limited powers but can require the directors of the company to provide information which will help the monitor arrive at a decision about the company's future viability. The monitor has a key role to play in overseeing the actions of the company's directors and ensuring that these do not cause harm to creditors. The monitor may also bring the moratorium to an end.

How does a moratorium come to an end?

The moratorium is terminated either because:

(1) the monitor must do so where he/she considers:

- the moratorium is no longer likely to result in the rescue of the company as a going concern, or
- the objective of rescuing the company as a going concern has been achieved, or
- the directors failed to provide information requested by the monitor resulting in the monitor being unable to carry out his/her functions, or
- the company is unable to pay moratorium debts or pre-moratorium debts which are not subject to a payment holiday during the moratorium, for example a lender.

or

(2) the company enters into a scheme of arrangement, a restructuring plan, a company voluntary arrangement, an administration procedure, a liquidation.

What is the impact of a moratorium on creditors?

- **Does the monitor pay creditors the amount owed to them?**

No. A moratorium provides a limited payment holiday in respect of the pre-moratorium debts and restricts creditors and shareholders from commencing or continuing with any insolvency proceedings (administration, liquidation, administrative receivership), enforcement and/or legal proceedings against the company.

- **Does the company pay the amount owed to creditors?**

As mentioned above, generally, the pre-moratorium debts are subject to a payment holiday. However, there are several exemptions which includes a substantial list of financial services contracts. For example, repayments which would normally fall due during the moratorium under the terms of bank loans, a mortgage on a property or a regular payment for leased equipment must continue to be paid. Certain other debts also need to be paid during the moratorium (relevant debts listed below).

- **Is the monitor bound by contracts entered into by the company before or during the moratorium?**

No, the contract is with the company. The monitor is not involved in the day-to-day running of the company either before or during the moratorium.

- **Can I terminate my contract with the company?**

Many suppliers of goods and services will have a clause in their contract of supply which provides that an event of default which is triggered by the purchaser entering into insolvency will result in the contract being automatically terminated or entitle the supplier to terminate the contract (i.e. an ipso facto clause). Essentially, when a company is in a moratorium, this contractual provision is overruled by the law, thereby restricting the supplier's ability to terminate the supply contract. It also overrules any contractual right a supplier may have in the supply contract to change the terms of supply, such as amending the payment terms of supply. In addition, the supplier cannot make it a condition of the continued supply during the moratorium, that any outstanding invoices must be paid.

There are limited circumstances when suppliers may terminate the contract during the moratorium:

1. With the consent of the company.
2. With the approval of the court where the continuation of the contract would cause the supplier hardship.
3. If the moratorium supplies are not paid for when payment is due, the supplier is able to terminate the contract. As payment of on-going supplies is also a condition of the moratorium, the monitor will bring the moratorium to an end.

- **What happens to the amount owed to creditors if the moratorium process does not result in the rescue of the company and the company goes into a subsequent procedure?**

In this situation, the law divides the company's debts into three categories:

1. Pre-moratorium debts with a payment holiday: debts that existed before the moratorium or, if the debt did not itself exist, the obligation under which the company becomes liable to pay that debt existed before the moratorium.

2. Pre-moratorium debts without a payment holiday:

(a) Relevant debts

- the monitor's remuneration and expenses,
- payments for goods and services supplied during the moratorium,
- rent in respect of the period during the moratorium,
- wages or salaries arising under a contract of employment,
- redundancy payments,
- debts or other liabilities arising under a contract or other instrument involving financial services (for example bank loans, mortgages).

(b) Priority pre-moratorium debt: broadly reflect the relevant debts (above) but excludes liabilities under financial contracts that fall due during the moratorium because the moratorium has accelerated the repayment obligation.

3. Moratorium debt: this is broadly any new debt that arises because of an obligation incurred during the moratorium that falls due either during or after the moratorium period.

If the moratorium process is unsuccessful and the company goes into a subsequent procedure (i.e. a company voluntary arrangement, a scheme of arrangement, a restructuring plan, an administration or liquidation), which begins within 12 weeks of the moratorium ending, 'super priority' will apply to the moratorium debts and priority pre-moratorium debts. This means that where there are floating charge realisations, the office holder will have to make distributions in respect of these debts in priority to all other claims (except for the prescribed fees and expenses of the Official Receiver where applicable).

A CREDITOR'S GUIDE TO THE MORATORIUM

This 'super-priority' is reflected here:

Floating charge realisations



Moratorium debts and priority
pre-moratorium debts



The law provides that where there are insufficient assets to meet these in full, these debts are payable in the following order of priority:

- 1.Amounts payable for goods or services supplied during the moratorium where, but for the rules protecting the supply, the supplier would not have had to make that supply.
- 2.Wages or salary arising under a contract of employment.
- 3.Other debts or liabilities except the monitor's remuneration and expenses.
- 4.The monitor's remuneration and expenses.

Insolvency practitioner's fees and
expenses



Preferential creditors



Prescribed part



Floating charge holder



Unsecured creditors



Shareholders



Creditors with a claim that ranks in priority to other unsecured creditors and to floating charge holders and the prescribed part. Such claims include some employee claims, contributions to pension schemes and some tax liabilities.

This is a pot of money set aside from what would have been paid to floating charge creditors so that a repayment can be made to unsecured creditors instead.

Creditor(s) whose lending is secured against a class of non-constant asset (e.g. stock in a warehouse, but not specific items of stock).

This category covers almost all other creditors, including customers and trade creditors.

A person or institution which has invested money in a company in exchange for a share of the ownership

What restrictions apply to the company during the moratorium?

Certain restrictions on the company apply, including:

- the company may not obtain credit of more than £500 without telling the other party that it is subject to a moratorium,
- the company cannot enter into certain financial instruments (market contracts or financial collateral arrangements, transfer orders, markets charges or a system charges, or collateral security).
- security may only be granted over company assets if the monitor consents, on the basis that granting the security will support the rescue of the company as a going concern,
- the circumstances and amount that can be paid in respect of pre-moratorium debts for which the company has a payment holiday,
- restrictions on the disposal of company property unless the disposal is made in the ordinary course of business or the monitor or court consents,
- Restrictions on the disposal of hire-purchase property and/or other property subject to a security interest.

As a creditor what information am I entitled to?

Creditors will be notified:

- of the start of the moratorium,
- of any changes to the length of the moratorium (i.e. where it is to be extended without creditor consent or is extended with creditor consent or terminated),
- if the monitor is replaced.

Details of the moratorium must be published on the company's website and a notice must be prominently displayed at company premises. In addition, every business document issued by the company or on behalf of the company must provide these details.

What is the process for creditors to consent to an extension?

Where director(s) intend to seek a decision of pre-moratorium creditors for the purpose of extending the moratorium then notice of the intention to do so must be given to creditors not less than 5 days before the date on which the decision is to be made.

In order to vote a creditor must have provided proof of a debt to the directors in writing before the decision is made.

How is the monitor's fee determined?

The monitor's fees will be subject to an agreement between the monitor and the appointing company. These fees may also be the subject of scrutiny at a later date by a liquidator or administrator of the company.

What should I do if I am dissatisfied with the monitor's handling of the case?

You should first contact the monitor to try to resolve the problem. If you are still not satisfied, there is a general ability for creditors, directors, members of the company or any person affected by the moratorium to apply to court during or after the moratorium, in order to challenge the actions of the monitor, where the applicant can establish it has been unfairly harmed.

If you think the monitor is guilty of misconduct, you should contact the IP's regulatory body (see the box below).

R3 is the UK's leading trade association for licensed insolvency practitioners and business recovery professionals. R3 does not license or discipline its members; this is the responsibility of the practitioner's regulatory body. The regulatory bodies are:

The Institute of Chartered Accountants in England and Wales

Tel: 01908 248100 www.icaew.co.uk

The Insolvency Practitioners Association

Tel: 0330 122 5237 www.ipa.uk.com

The Institute of Chartered Accountants of Scotland

Tel: 0131 347 0100 www.icas.org.uk

Chartered Accountants Regulatory Board

Tel: 028 9043 5858 www.carb.ie/en/CARB/

Disclaimer

Information in this guide is intended to provide an overview only and relates to standalone moratoriums under Part A1 of the Insolvency Act 1986 in England and Wales. It is not a replacement for seeking advice specific to your circumstances.