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Restructuring moratoriums through an information-processing lens

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ABSTRACT
Using insights from complex systems theory, it is argued that financially distressed large corporates will seek the protection of a moratorium when the benefits it brings outweigh its signalling and information-processing problems – likely to be in the later stages of distress. Applying this insight, the article offers a somewhat gloomy assessment of the Part A1 moratorium introduced in the UK by the Corporate Insolvency and Governance Act 2020. It is suggested that the UK administration moratorium may be more fit for purpose, but that serious signalling and information processing concerns remain. After touching on possible adaptations of the tools, the article concedes that there may have been a deliberate decision to restrict the usefulness of both of them. The article ends by arguing that if this the case, the decision may not be sustainable in a rapidly changing economic environment, and that recent suggestions for reform should be supported.

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KEYWORDS Debt restructuring; moratorium; stay; Corporate Insolvency and Governance Act 2020; CIGA

1. Introduction

This article is about the moratorium (in United Kingdom (UK) terminology) or the automatic stay (in United States (US) terminology) in corporate insolvency proceedings.[1] A moratorium prevents creditors from enforcing their rights, without destroying those rights. In other words, an individual creditor's rights are suspended while the moratorium is in force unless the creditor can follow a process to have the moratorium lifted. As we will see, the

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[1]For ease of reference, the term moratorium will generally be used unless US Chapter 11 is being discussed specifically.

specific contours of the moratorium vary from jurisdiction to jurisdiction, but most corporate insolvency law regimes around the world provide the debtor with some moratorium protection.

The moratorium is generally conceived of as preventing a damaging grab race for the debtor's assets. In his path-finding work, Thomas Jackson argued:

> The grab rules of nonbankruptcy law and their allocation of assets on the basis of first-come, first-served create an incentive on the part of the individual creditors, when they sense that a debtor may have more liabilities than assets, to get in line today (by, for example, getting a sheriff to execute on the debtor's equipment), because if they do not, they run the risk of getting nothing. This decision by numerous individual creditors, however, may be the wrong decision for the creditors as a group. Even though the debtor is insolvent, they might be better off if they held the assets together.[2]

Thus, the moratorium prevents creditors from acting on their incentives to rush to grab what they can. Such a 'grab race' may result in the dissipation of the debtor's assets so that it becomes impossible to rescue the debtor or its business and assets as a going concern. At this point, a break-up of the business and a sale of the assets becomes inevitable, while a rescue of the company or a going concern sale will almost always produce a higher value for creditors. The central idea is that the moratorium plays a role in keeping such a value-maximising transaction on the table.

This classic theoretical framing of the moratorium is commonly cited in the literature – indeed, a great deal of corporate insolvency law scholarship starts with this proposition. Moreover, in much of the literature the moratorium is seen as part of a toolbox designed to encourage the debtor to file for corporate insolvency law protection when it is in the early stages of financial distress.[3] The idea is that a moratorium can create a breathing space for the debtor to work out a solution with its creditors and that the availability of the moratorium incentivises the debtor to seek protection and to address its difficulties. This conception of the moratorium is frequently reflected in international corporate insolvency law scholarship.[4] It is reflected in the European Union directive on restructuring plans, which includes provision for a stay on enforcement action and states that the purpose of the stay is 'to support the negotiations of a restructuring plan'.[5] And we will see that the UK Government also specifically referred to the role of moratorium protection

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[2]Thomas H Jackson, *The Logic and Limits of Bankruptcy Law* (1986) 12–13.
[3]Harvey R Miller, 'Chapter 11 in Transition – From Boom to Bust and into the Future' (2007) 81 American Bankruptcy Law J. 375, 386–87.
[4]Wai Yee Wan, Casey Watters, and Gerard McCormack, 'Schemes of Arrangement in Singapore: Empirical and Comparative Analyses' (2020) 94 American Bankruptcy Law J. 463, 471.
[5]Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks, on discharge of debt and disqualifications, and on measures to increase the efficiency of procedures concerning restructuring, insolvency and discharge of debt, and amending Directive (EU) 2017/1132 (Directive on restructuring and insolvency) OJ/26.6.2019/L, Article 6(1) (the European Restructuring Directive).

in encouraging directors to act early in consultations preceding reform efforts with which this article is centrally concerned.[6]

However, this article draws on both UK and recent US corporate restructuring practice informed by insights from complexity theory to challenge the idea that the moratorium is part of a toolbox to encourage early intervention. The core contention is that when the moratorium is viewed through a signalling and information-processing lens, it is best conceived of as a tool to create liquidity and stabilise the business of a debtor in the later stages of distress – at least for large corporates. Adopting the complex system scientist Melanie Mitchell's framework for assessing how complex systems process information,[7] the core contention is that the moratorium is of value when the benefits it brings outweigh the signalling disadvantages which are associated with it for large corporates in distress.

With this insight in hand, two moratoria available in UK corporate insolvency law are analysed and evaluated. The first moratorium which is considered is the new standalone moratorium introduced by the Corporate Insolvency and Governance Act 2020 (CIGA) into Part A1 of the Insolvency Act 1986. This can be used alone when a company is attempting a contractually negotiated restructuring or in combination with one of UK corporate insolvency law's restructuring tools (the Company Voluntary Arrangement (CVA); the Part 26 scheme of arrangement; or the Part 26A restructuring plan procedure). The argument is advanced that the Part A1 moratorium is well-designed from a signalling and information-processing viewpoint but that when it is analysed and evaluated as a late-stage large corporate restructuring tool it comes up short.

This leads to a comparison with the potential for the administration moratorium to be used as such a tool. The administration procedure was first introduced in the UK by the Insolvency Act 1986. A moratorium arises automatically when the debtor enters administration and remains in force for the duration of the proceeding.[8] The analysis in this article suggests that this administration moratorium does indeed offer more promise as a late-stage corporate restructuring tool. Yet, as we will see, the historical associations of the administration procedure create a very real challenge when it is viewed through a signalling and information-processing lens, while there are legal uncertainties associated with its use as a corporate restructuring tool. Thus, the conclusion is that the administration moratorium can only deliver on its promise as a tool to stabilise large corporates in late-stage distress and create much-needed liquidity if these signalling and information-processing challenges can be overcome, and if the courts embrace the use

[6]n 38, n 40 and accompanying text.
[7]Melanie Mitchell, *Complexity: A Guided Tour* (2009) 170. Thanks are due to Kenneth Ayotte and Adam Badawi for introducing me to this excellent work.
[8]Insolvency Act 1986, Sch B1, para 42–3.

of administration for this purpose. On the other hand, the Part A1 moratorium mitigates the signalling and information-processing challenges but does not do enough to stabilise a large business and create liquidity when it is in late-stage distress.

The information-processing lens is then turned away from the company's stakeholders and towards the company itself in considering whether the Part A1 moratorium may have a role to play as the company gathers information during the restructuring, learns from that information, and evaluates its options. A specific adaptation of the Part A1 moratorium is explored. Finally, with the information-processing lens still trained primarily on the company rather than its stakeholders, the question of whether small companies may find the Part A1 moratorium of greater utility is explored. A question is raised about transaction costs, but that largely falls outside the scope of this article and awaits further research.

The article is organised as follows. First, the role of the moratorium in large corporate reorganisation is explored and the argument is developed that for large corporates, viewed through a signalling and information-processing lens, the moratorium is most useful as a tool to stabilise the business and create liquidity when the company is in the late stages of distress. Second, the Part A1 moratorium is analysed and evaluated against this insight. Third, the administration moratorium is analysed as a late-stage restructuring tool in a comparative frame with the Part A1 moratorium and the information-processing lens is then trained on the company rather than its stakeholders in considering whether there may be strategic uses for the tool. The information-processing lens remains trained on the company in considering potential applications by small companies. The article then briefly concludes.

2. The role of moratoria in large corporate reorganisation

2.1. US

As foreshadowed in the introduction, in the US literature the automatic stay has traditionally been conceived of as a tool to grant the large corporate debtor 'a breathing space' in which to negotiate and implement a corporate reorganisation:

> The automatic stay is one of the fundamental debtor protections provided by the bankruptcy laws. It gives the debtor a breathing space from his creditors. It stops all collection efforts, all harassment, and all foreclosure actions. It permits the debtor to attempt a repayment or reorganization plan, or simply to be relieved of the financial pressures that drove him into bankruptcy.[9]

[9]S. Rep. (1978) No. 95–989, 54–55 cited in Vincent S J Buccola, 'Bankruptcy's Cathedral: Property Rules, Liability Rules, and Distress' (2019) 114 Northwestern University Law Rev. 705, 741–42.

The availability of such a 'breathing space' is conceived of as part of a toolbox designed to incentivise directors to file for bankruptcy protection early, before distress has deepened and the liquidity issues facing the group are so significant that corporate reorganisation becomes impossible.[10] Once the bankruptcy petition is filed, all the debtor's claims come within what Douglas Baird, Antony Casey and Randal Picker have called 'the bankruptcy partition'.[11] It is possible to designate a class of claims as unimpaired,[12] and to designate a class of 'administrative convenience claims' where the costs of bringing the claims within the compromise outweigh the benefits,[13] but all claims are placed within a class in the case. And the automatic stay comes into immediate effect, binding the debtor and the creditors so that the debtor is (subject to certain exceptions developed below) prohibited from paying prepetition debt.[14] Thus, broadly, all claims and payments are stayed, other than those arising during the case, to be dealt with at the end of the case in a plan of reorganisation or sale transaction.

Corporate reorganisation practice has, however, changed considerably in the US since Chapter 11 was introduced in 1978. Crucially for the purposes of this article, there has been a dramatic rise of prepackaged bankruptcies, typically targeting only financial liabilities, while all other creditors are paid in full.[15] In a prepackaged bankruptcy, the debtor negotiates, and seeks votes on, its proposed plan before it petitions the court. It then asks the court to move rapidly to confirm the plan, in weeks or sometimes even days.[16]

In her excellent book on complex systems, Melanie Mitchell proposes that when a complex system is processing information, three questions must be answered:

- What plays the role of "information" in this system?
- How is it communicated and processed?
- How does this information acquire *meaning*? And to whom?[17]

The changes in US restructuring practice are, in part, a result of increased focus on the ways in which information is communicated and interpreted in

[10] Miller (n 3) 386–87.
[11] Douglas G Baird, Anthony J Casey, and Randal C Picker, 'The Bankruptcy Partition' (2018) 166 University of Pennsylvania Law Rev. 1675.
[12] 11 USC § 1126 (f).
[13] 11 USC § 1122(b).
[14] 11 USC § 362(a).
[15] John McConnell and Henri Servaes, 'The Economics of Pre-packaged Bankruptcy' in Jagdeep S Bhandari and Lawrence A Weiss (eds), *Corporate Bankruptcy: Economic and Legal Perspectives* (1996) 322.
[16] For a useful table of recent expedited prepackaged bankruptcy cases see Angela Libby, 'U.S. Restructuring in the Last Decade; Key Developments and Emerging Themes' in Sebastian van den Berg, Lynetter Janssen and Ivén J Romo (eds), *Cross-Border Restructuring and Insolvency 2012–2022: Cases and Developments* (2023), 250.
[17] Mitchell (n 7) 170.

complex corporate reorganisations. For a company to restructure successfully, it needs its suppliers and customers to continue to support its business during and after negotiation of the plan. Suppliers and customers, faced with a good deal of uncertainty about the future of the business and about their own position, 'seek out signals – observable actions that provide information about unobservable attributes and likely outcomes … – that help close the gap between *what stakeholders know* about the firm and *what they want to know*.'[18] The problem with the automatic stay is that it signals to suppliers that at best payment of their pre-petition debts will be delayed and at worst they may not be paid in full. At the same time, it signals to customers that supplier relationships are likely to be under strain and that the future of the business is in doubt.

Thus, the prepackaged bankruptcy largely avoids engaging the automatic stay. The absence of stay protection may not damage attempts to reorganise the financial liabilities of a large firm before the Chapter 11 case is filed. As Vincent Buccola puts it:

> Senior lenders' acceleration rights and security interest imply that they will be first in right to a large fraction of the debtor's assets should junior investors precipitate a run by seeking to withdraw their investments … Because this dynamic is common knowledge, junior investors have correspondingly little reason to undermine the lenders' effective control.[19]

In other words, it may be perfectly possible to negotiate a prepackaged bankruptcy targeting only financial liabilities without the benefit of stay protection.

Once the company petitions for Chapter 11 protection, the company will communicate the information that a deal has been struck with financial creditors, and that trade suppliers, customers, and employees have nothing to fear. The debtor informs the trade creditors and employees that they will 'ride through' the case and will not be compromised. There is also often reassurance to customers that the company's operations will not be affected in any way. This information can be communicated explicitly, via the company's press release,[20] or implicitly via the fact that the debtor is not engaging with anyone other than financial creditors in the restructuring negotiations.

[18]Donald D Bergh, Brian L Connelly, David J Ketchen, Jr and Lu M Shannon, 'Signalling Theory and Equilibrium in Strategic Management Research: An Assessment and a Research Agenda' (2014) 51(8) Journal of Management Studies 1334, 1335.

[19]Buccola (n 9) 718–19 citing Randal C Picker, 'Security Interests, Misbehavior, and Common Pools' (1992) 59 University of Chicago Law Rev. 645, 657 and Lucian Ayre Bebchuk and Jesse M Fried, 'The Uneasy Case for the Priority of Secured Claims in Bankruptcy' (1996) 105 Yale Law J 857, 876 n 65.

[20]See, for example, Belk Inc. press release 24 February 2021, ' … plan of reorganization allows suppliers to be paid in full, has no impact to employees and all store locations to remain open' <https://www.prnewswire.com/news-releases/belk-successfully-completes-pre-packaged-one-day-financial-restructuring-with-backing-of-majority-owner-sycamore-partners-and-lenders-including-kkr-credit-and-blackstone-credit-301234984.html>.

Suppliers, employees, and customers take the 'meaning' from this information they will not be affected by the reorganisation and that they should be able to deal with the company in confidence after the reorganisation is completed. And, of course, if the prepackaged bankruptcy is confirmed extremely quickly, within days, the automatic stay is barely engaged at all.

As the company's distress deepens, however, the situation may become more difficult. Senior lenders may be losing confidence in the restructuring effort and may find it more challenging to sell out at a good price in the secondary markets. Distressed debt funds which have the benefit of credit default swap protection may trade in and may be motivated to prefer an insolvency over a restructuring transaction.[21] And relations with customers and suppliers may be considerably more strained. At this point, if the company is to be rescued, it may become critical to stabilise the situation and to create liquidity, so that signalling and information-processing concerns take a back seat.[22] As we will see, stays or moratoria can help with both objectives. Thus, the benefits of the stay in stabilising the business and creating liquidity may outweigh the information-processing and signalling disadvantages for businesses in the later stages of distress.

The strong mandatory automatic stay in Chapter 11 measures up well as a stabilising and liquidity-creating tool, given that it 'enjoins nearly all judicial and administrative proceedings, as well as most informal actions a creditor could take in an effort to collect a debt'.[23] Moreover, the so-called ipso facto ban is engaged. An ipso facto clause is a clause in a contract which allows the counterparty to terminate or amend the contract or take other action if the other party is in breach of certain matters specified in it.[24] US Chapter 11 bans a counterparty from relying on such an ipso facto clause that is conditioned on the insolvency or financial condition of the debtor; the commencement of the bankruptcy case; or the appointment of a bankruptcy trustee.[25] This can help to stabilise the business, by ensuring that the debtor does not lose vital contracts while it is trying to negotiate a restructuring plan. It can also help to create liquidity, by reducing the

[21] Frank Partnoy and David A Skeel Jr., 'The Promise and Perils of Credit Derivatives' (2007) 75 University of Cincinnati Law Rev. 1019, 1035; Henry TC Hu and Bernard Black, 'Equity and Debt Decoupling and Empty Voting II: Importance and Extensions' (2008) 156 University of Pennsylvania Law Rev. 625, 731; Daniel Hemel, 'Empty Creditors and Debt Exchanges' (2010) 27 Yale Journal on Regulation 159, 160; Douglas G Baird and Robert K Rasmussen, 'Antibankruptcy' (2010) 119 Yale Law J. 648, 681; David A. Skeel Jr and Thomas H Jackson, 'Transaction Consistency and the New Finance in Bankruptcy' (2012) 112 Columbia Law Rev. 152, 155.

[22] Kennet Ayotte and David A Skeel Jr, 'Bankruptcy Law as a Liquidity Provider' (2013) 80 University of Chicago Law Rev. 1557.

[23] Rodrigo Olivares-Caminal, Randall Guynn, Alan W. Kornberg, Eric McLaughlin, Sarah Paterson, and Dalvinder Singh, *Debt Restructuring* (2022) 163.

[24] Janis Sarra, Jennifer Payne and Stephan Madaus, 'The Promise and Perils of Regulating *Ipso Facto* Clauses' (2022) 31(1) International Insolvency Review 45.

[25] 11 USC § 365(e).

power of the counterparty to demand new terms as a condition of continuing the contract.

This leads us to the role of stay, or as it is known locally, moratorium protection in the UK.

2.2. UK

The history of moratorium protection in the UK is very different from the history of the US automatic stay. Until the 2000s, large corporate restructurings were guided by the principles of the so-called London Approach,[26] and implemented out of court. London Approach restructurings typically did not compromise claims other than financial claims.[27] Insofar as the financial claims themselves were concerned, the London Approach set down principles of cooperation to prevent financial creditors from seeking to enforce against the debtor.[28] These principles were widely observed, initially as a result of the regulatory power of the Bank of England which developed the London Approach; subsequently as a result of the informal power of the Bank of England; and finally because banks feared that if they did not observe the principles in restructurings they would not be invited to participate in loan syndications in the primary markets.[29] As a result, resort to formal moratorium protection by large corporates was largely confined to situations in which efforts to restructure the firm had failed and it had become necessary to turn to efforts to sell the business and assets or just the assets.

A detailed examination of why the London Approach ceased to be enforceable in the UK falls outside the scope of this article.[30] The crucial point is that the London Approach fell away, and the market increasingly turned to the scheme of arrangement to implement large corporate reorganisations.[31] Schemes of arrangement do not offer moratorium protection but in the last decade most restructuring schemes were limited to financial liabilities in complex capital structures.[32] It is usual for the relationship between financial creditors to be regulated by an intercreditor agreement in English law-governed deals. This intercreditor agreement ordinarily hands

[26]Pen Kent, 'The London Approach' (1993) Q1 Bank of England Quarterly Bull. 110; John Flood, Robert Abbey, Eleni Skordaki, and Paul Aber, 'The Professional Restructuring of Corporate Rescue: Company Voluntary Arrangements and the London Approach' (1995) ACCA Research Report 45; Alice Belcher, *Corporate Rescue: A Conceptual Approach to Insolvency Law* (1997) 116–22; John Armour and Simon Deakin, 'Norms in Private Insolvency: The "London Approach" to the Resolution of Financial Distress' (2001) 1 Journal of Corporate Law Studies 21.

[27]Flood et al (n 26) 7, 'in the London Approach the aim of the banks doing the reconstruction is to prevent the involvement of trade creditors'.

[28]Kent (n 26) 111.

[29]Armour and Deakin (n 26) 33–34, 46.

[30]For a discussion see Sarah Paterson, *Corporate Reorganization Law and Forces of Change* (2020) 100–03.

[31]Companies Act 2006, s 895–901.

[32]See, for example, *MyTravel Group PLC* [2004] EWHC 2741 (Ch); *McCarthy & Stone Plc* [2009] EWHC 712 (Ch); and *Bluebrook Ltd* [2009] EWHC 2114 (Ch).

enforcement control to the senior lenders, permitting the issue of a stop notice pursuant to which the debtor will cease making payments on the junior debt while the junior financial creditors are prevented from commencing enforcement action for a period (often 90 days). Acceleration of the senior loan is likely to require a vote from a qualified majority of senior lenders, ordinarily 66.66%. This means that if the borrower is confident at least 33.34% of senior lenders will not be willing to accelerate, it may be possible for it to be confident that no action will be taken. Meanwhile, a senior creditor which does not wish to support the restructuring can seek to sell out in the deep distressed debt markets which have existed for some time.[33] Overall, just as we saw in modern US corporate restructuring practice, there is often no pressing need for moratorium protection to address risks from financial creditors in the early stages of distress.

However, just as in the US, as the company's distress deepens the situation may become more difficult. The company may be reaching the end of the period pursuant to which it can stop payments to junior claim holders with relative impunity under the intercreditor agreement. And the standstill provisions in the intercreditor agreement are likely to be subject to an insolvency carve-out so that the worse the situation becomes the more concerned the debtor and the senior lenders may become that the junior creditors may seek to take some form of enforcement action. And customer and supplier pressure may be increasing dramatically. Thus, as the 2000s progressed concerns were raised about how large English firms would navigate late-stage distress without the benefit of a moratorium.[34]

In 2016, the Government launched a review of the corporate insolvency framework in the UK.[35] Among other things, it proposed the introduction of a new moratorium to help business rescue.[36] The review expressly recognised that, ' … the true benefits of a moratorium are most useful for large companies with complex financing and multiple creditors'.[37] It also expressly linked the introduction of a new moratorium with efforts to encourage directors to act early to address their companies' financial problems.[38] The review was followed, two years later, by a Government response.[39] The response confirmed that the Government was proposing to introduce a new moratorium and also stated that, 'Those who supported the [2016] proposal felt that a

[33]Sarah Paterson, 'Reflections on English Law Schemes of Arrangement in Distress and Suggestions for Reform' (2018) 15 European Company and Financial Law Review 472, 478–79.
[34]ibid; Sarah Paterson, 'The Rise of Covenant-lite Lending and Implications for the UK's Corporate Insolvency Law Toolbox' (2019) 39 Oxford Journal of Legal Studies 654.
[35]The Insolvency Service, 'A Review of the Corporate Insolvency Framework: A Consultation on Options for Reform' May 2016.
[36]ibid 10–19.
[37]ibid 11.
[38]ibid.
[39]Department for Business, Energy & Industrial Strategy, 'Insolvency and Corporate Governance: Government Response' 26th August 2018.

new moratorium could encourage directors to act earlier'.[40] Crucially, the proposal was to exclude companies that were already insolvent from eligibility.[41]

In a long and detailed joint response, the Insolvency Lawyers' Association Technical Committee and the City of London Law Society Insolvency Law Sub-Committee made the point that in the earlier stages of distress:

> a well advised director is unlikely to enter into the moratorium process, given the potential impact on customer, supplier and credit insurer sentiment of admitting that the company will become insolvent unless it can be rescued.[42]

Essentially the concern was that excluding companies that are already insolvent from eligibility for the moratorium would exclude the companies that need it – those in the later stages of distress.

Amid the Covid 19 pandemic and concerns for corporate solvency, CIGA finally introduced (among other things) a new, free-standing moratorium into Part A1 of the Insolvency Act 1986 (the Part A1 moratorium). The policy in introducing the moratorium was expressed in very general terms: 'allowing a company in financial distress a breathing space in which to explore its rescue and restructuring options free from creditor action.'[43] In the next section, the more finely focused framework of reducing information-processing challenges and stabilising, and creating liquidity for large companies in the later stages of financial distress is used to assess this new tool.

3. The Part A1 moratorium and large corporate restructuring

A quick recap of the moratorium through the information-processing lens may be useful at this point. The argument has been developed that proposing a moratorium may be interpreted as a negative signal by suppliers, employees, and customers, and that they may associate it with lower prospects of success for the restructuring and with lower confidence in their relationship with the debtor after the restructuring. As a result, when the debtor is in the early stages of financial distress it will avoid announcing that it is taking the benefit of moratorium protection. However, once the debtor's financial difficulties worsen, the need to stabilise the situation and create liquidity may outweigh the signalling and information-processing costs associated with the moratorium.[44] At this point, the company is

[40]ibid 42.
[41]ibid 47.
[42]The Insolvency Lawyers' Association Technical Committee and The City of London Law Society Insolvency Law Sub-Committee, 'Issues Paper Insolvency and Corporate Governance Proposals and Corporate Insolvency Regime Reforms 2018/19' 13 (the 'ILA/CLLS 2018 Issues Paper') <https://www.citysolicitors.org.uk/clls/committees/insolvency-law/>.
[43]Explanatory Notes to the Corporate Insolvency and Governance Act 2020, para 4.
[44]For a review of the tools in US Chapter 11 facilitating the raising of new debt to address liquidity problems see: Ayotte and Skeel (n 22).

experiencing widespread supplier pressure, as suppliers terminate contracts and other suppliers become nervous and terminate their contracts in turn or suppliers reduce debtor days or demand cash on delivery creating serious cash flow pressure. Customers also react to the deteriorating situation by taking their business elsewhere, and as customer orders are lost, the liquidity crisis deepens and prospects for the business deteriorate. The moratorium may offer the only hope of stabilising this situation and creating liquidity. Thus, for large corporates the moratorium is primarily useful as a late stage restructuring tool, when the firm is struggling to stabilise its operations and to stay afloat long enough to restructure successfully. While many, if not most, large corporates were able to restructure their financial liabilities successfully in the decade following the 2008 financial crisis, there were some notable examples of large companies where the financial situation deteriorated extremely rapidly so that they could not be saved.[45] Furthermore, it has been suggested that recent changes in lending terms in the finance market may result in debtors engaging with financial creditors later, when they are already in more serious financial distress.[46] The question is whether the new Part A1 moratorium can help to address the information-processing challenges and to stabilise large corporates which find themselves in such a rapidly deteriorating position.

3.1. The Part A1 moratorium through the information-processing lens

The design of the Part A1 moratorium does pay some attention to information-processing and signalling concerns. The procedure can only be used if, and for so long as, the monitor thinks that a company rescue is likely. If the monitor is unable to confirm that in their view a company rescue is likely, the moratorium protection is not available at all.[47] And if the monitor arrives at the view that a company rescue no longer remains likely, the monitor must bring the Part A1 moratorium to a close.[48] The information which is communicated to customers and suppliers is firmly that a rescue of the company is being pursued.

Moreover, while an insolvency practitioner, known as the monitor, is appointed, the monitor has a relatively limited role: primarily to confirm the likelihood of rescue of the company as a going concern; to confirm the company's ability to pay certain debts; and to approve certain transactions

[45]Carillion Group; Thomas Cook Group. It should be noted that no claim is being made that either the Carillion Group or the Thomas Cook Group could or should have been saved – merely that they were in late-stage distress and were not saved.
[46]Paterson, 'Covenant Lite Lending' (n 34).
[47]Insolvency Act 1986, s A6(e).
[48]ibid s A38.

(such as disposals of property and certain payments). Thus, the moratorium has a generally debtor-in-possession orientation. This is crucial if a moratorium is to promote a restructuring rather than a sale transaction once the company is experiencing more serious financial distress. At this point, suppliers, employees, and customers are faced with even greater uncertainty about the prospects of the company and, therefore, their own prospects. If the moratorium is a debtor-in-possession procedure, the company can signal to suppliers and customers that the aim is to stabilise the business and build confidence in anticipation of a successful reorganisation transaction. The directors know the business, and its stakeholders, best and can begin the work needed to build and maintain relationships for the company to trade successfully after the restructuring. Thus, the debtor-in-possession orientation of the moratorium is helpful for large corporates seeking to rely on it to stabilise the business and create liquidity in anticipation of a restructuring transaction when distress has become reasonably advanced.

Finally, CIGA introduces a new section 233B into the Insolvency Act 1986, creating a general ban on so-called ipso facto clauses in the UK for the first time. The ipso facto ban is engaged when a debtor files for the Part A1 moratorium. As with moratoria, the scope of an ipso facto ban may vary from jurisdiction to jurisdiction. The new UK ban applies to contracts for the supply of goods and services and provides, inter alia, that a provision that a contract or supply would terminate, or any other thing would take place, or the supplier would be entitled to terminate the contract or the supply or do any other thing, in each case because the company has the benefit of the Part A1 moratorium, would cease to have effect.[49] Moreover, the counterparty is prevented from exercising any right of termination which arose before the insolvency filing – not just insolvency-related termination rights (although the counterparty is free to terminate for something arising after the commencement of the Part A1 moratorium provided it does not relate to the filing).[50] Crucially, the counterparty is expressly prohibited from demanding outstanding payments as a condition of future supply.[51]

An ipso facto ban is, however, an imperfect tool. The counterparty may seek to rely on commercial excuses: the stock has not arrived; the van has broken down. The debtor scarcely wishes to launch litigation against all its critical suppliers. And perhaps even more significantly, signalling within restructuring has implications for how the supplier feels about the business after the restructuring. If the ipso facto ban is enforced against the supplier, the supplier may take the opportunity, after the restructuring, to reduce its reliance on the debtor and to seek out other sources of supply to guard

[49]ibid s 233B(3).
[50]ibid s 233(B)(4).
[51]ibid s 233(B)(7).

against future difficulties.[52] In the meantime, customers also pick up news of the stay against trade suppliers and suspect it means the debtor is in serious financial trouble, assessing the debtor's likelihood of survival accordingly.[53] And the ipso facto ban is only engaged if the debtor and the counterparty transact on the basis of a preexisting contract. If they simply transact from time to time on standalone terms and conditions, the ipso facto ban will have nothing to bite on. For all these reasons, in the US it has become common to seek to designate some vendors as 'critical' to the reorganisation and to pay their pre-petition debts in full,[54] notwithstanding the ipso facto ban. Against this background, the Part A1 moratorium provides an important provision which enables the company to pay debts incurred before the filing which it would not otherwise have to pay during the moratorium: up to the greater of £5,000 and 1 per cent of the value of the debts and other liabilities owed by the company to unsecured creditors when the moratorium began; with monitor consent (where the monitor, relying on company information, thinks the payment will support company rescue); or in pursuance of a court order.[55] Thus, where the company considers that it is crucial to pay a supplier, it is able to do so. All of this is extremely useful from an information-processing perspective.

Overall, the design of the Part A1 moratorium does pay attention to mitigating information-processing concerns. It could, however, be even better. Article 6(3) of the European Restructuring Directive provides that the optional stay which is available can be general (affecting all creditors) or limited towards individual creditors. Moreover, the article goes on to provide that were the stay is limited, only the creditors targeted by the stay need to be informed of it. Thus, while the Part A1 moratorium does go some way to addressing signalling concerns, the European Restructuring Directive trumps it by enabling the debtor to keep the moratorium confidential from creditors which it does not wish to destabilise and plans to pay in full. This leads us to consider Part A1's stabilisation and liquidity-creating tools.

3.2. The Part A1 moratorium as a late-stage stabilisation and liquidity-creating tool

There are certainly aspects of the new Part A1 moratorium which can help with the twin objectives of stabilisation and creating liquidity while a

[52]For a fascinating insight see: Peter Walton, Chris Umfreville and Lézelle Jacobs, *Company Voluntary Arrangements: Evaluating Success and Failure* May 2018 commissioned by R3, the insolvency and restructuring trade body, 50.

[53]For an equally fascinating insight on customer behaviour see: Samuel Antill and Megan Hunter, 'Consumer Choice and Corporate Bankruptcy' SSRN <https://ssrn.com/abstract=3879775>

[54]Mark J Roe and Frederick Tung, 'Breaking Bankruptcy Priority: How Rent-Seeking Upends the Creditors' Bargain' (2013) 99 Virginia Law Rev. 1235.

[55]Insolvency Act 1986, s A28.

restructuring is attempted where the company is at a reasonably advanced stage of distress. We have already seen that the ipso facto ban is engaged, helping to stabilise the business by preventing the termination of vital contracts and helping to create liquidity by reducing ransom-creditor hold-up power. Nonetheless, as we will see, there are also serious limitations in the design of the Part A1 moratorium to meet these aims.

3.2.1. Application and eligibility

It is possible to obtain the moratorium simply by filing documents with the court,[56] provided the company is not subject to an outstanding winding-up petition and is not an overseas company. Otherwise, the company can apply to the court for Part A1 moratorium protection.[57] In either case, the directors need to be able to confirm that the company is, or likely to become, unable to pay its debts.[58] Thus, the Part A1 moratorium expressly recognises that protection will be sought by companies in some degree of financial difficulty, and the 2018 proposal that companies which are already insolvent would be excluded has been abandoned. This contrasts with the approach taken in the European Restructuring Directive,[59] which sticks stubbornly to the idea of incentivising early debtor action, and which provides that debtors should have access to the preventive restructuring framework, including moratorium protection, if there is a 'likelihood' of insolvency falling short of insolvency as understood by national law.[60] Thus, if the debtor is 'actually' insolvent, the framework is not available – an obvious limitation if moratorium protection is most useful for debtors experiencing more severe financial distress which are seeking a last chance at a restructuring effort.

There are, however, some significant limitations in the eligibility criteria. First, the legislation exempts a relatively wide range of companies from eligibility to apply for the Part A1 moratorium.[61] Notably, a company is excluded from eligibility to file for the Part A1 moratorium if it is party to a capital market arrangement.[62] The effect of this is that many large corporates which have issued secured bonds in the debt capital markets will not be eligible to file for the Part A1 moratorium. When CIGA came into force, the Government committed to a review of its operation within three years of

[56]ibid s A3.
[57]ibid s A4 and A5.
[58]ibid ss A4 and A6.
[59]Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks, on discharge of debt and disqualification, and on measures to increase the efficiency of procedures concerning restructuring, insolvency and discharge of debts and amending Directive (EU) 2017/1132 (Directive on restructuring and insolvency) [2019] OJ 172.
[60]ibid Art 4.
[61]ibid Sch ZA1 (Moratorium in Great Britain: Eligible Companies).
[62]ibid para 13.

commencement. As part of that review, Professor Peter Walton and Dr Lézelle Jacobs from the University of Wolverhampton were commissioned to conduct an independent review. Their interim report was published on 21 June 2021 (the CIGA Interim Report),[63] and their final report was published on 19 December 2022 (the CIGA Final Evaluation Report).[64] The Government then published a post implementation review of CIGA (the CIGA Post-Implementation Review), based largely on the evidence of the CIGA Interim Report and the CIGA Final Evaluation Report.[65] The CIGA Post-Implementation Review expressly notes that eligibility criteria are preventing larger companies from using the moratorium.[66]

Moreover, while the single-minded focus on corporate rescue has signalling benefits, the lack of flexibility to consider other options may be problematic for a company in late-stage distress. First, the monitor may be reluctant to give the required confirmation. Secondly, the debtor may need a good deal of flexibility at this point, so that if a company rescue does not prove possible it can pivot relatively easily to another course of action. The CIGA Final Evaluation Report is based on semi-structured interviews with various stakeholders and an online survey of insolvency practitioners. The report notes that insolvency practitioners pointed to a further concern with the detail of the provisions. If a corporate rescue is not achieved during the Part A1 moratorium, and the debtor is subsequently placed into insolvency proceedings, certain pre and post moratorium debts are granted priority over other debts and the monitor's remuneration.[67] The report suggests that insolvency practitioners are not only concerned about the subordination of their own fees, but also the reputational consequences of subordinating other creditors' claims as a result of a failed moratorium. The CIGA Post-Implementation Review hints at the fact that this may be a particular concern for insolvency practitioners where secured creditors find themselves subordinated to other debts, given that secured creditors often have a say in whether insolvency practitioners are appointed in insolvency proceedings.[68] In other words, insolvency practitioners may be concerned about how secured creditors will receive information that they have been subordinated as a result of a failed Part A1 moratorium, and the meaning that they will attach to the information about the suitability of the insolvency practitioner for future appointments.

[63]Professor Peter Walton and Dr Lézelle Jacobs, 'Corporate Insolvency and Governance Act 2020 – Interim Evaluation Report March 2022' (Insolvency Service, 21 June 2022).
[64]Professor Peter Walton and Dr Lézelle Jacobs, 'Corporate Insolvency and Governance Act 2020 – Final Evaluation Report November 2022' (Insolvency Service, 19 December 2022).
[65]Insolvency Service, 'Post-Implementation Review: Corporate Insolvency and Governance Act' 21 February 2023 <https://www.legislation.gov.uk/ukia/2023/69/pdfs/ukia_20230069_en.pdf>.
[66]ibid para 5.69.
[67]Insolvency Act 1986, s 174A
[68]CIGA Post-Implementation Impact Review (n 65) para 6.4.

3.2.2. Length of Part A1 moratorium

Furthermore, the length of the moratorium may be a challenge. The initial period of the Part A1 moratorium is 20 business days, beginning on the business day on which the moratorium comes into force.[69] The moratorium can be extended once by the directors without creditor consent for a further 20 business days;[70] by the directors with creditor consent for up to one year (and multiple extensions within this period are possible);[71] by the court on the application of the directors (and multiple extensions are, once again, possible);[72] where a proposal for a company voluntary arrangement is pending;[73] and by the court in the course of an application for a scheme or restructuring plan.[74] The initial period seems rather short for a company in the late stages of distress attempting to create a runway towards a plan of reorganisation. Indeed, the CIGA Final Evaluation Report identifies that a majority of respondents felt the period of the moratorium was too short.[75] The report also suggests that those who had used the moratorium had found it to be 'easily extended'.[76] However, an application to court for an extension must be accompanied by: a statement from the directors that moratorium debts and pre-moratorium debts without a payment holiday that have fallen due have been paid or discharged; a statement from the directors that the company is or is likely to become unable to pay its debts; a statement from the directors about whether pre-moratorium creditors have been consulted and if not, why not; and a statement from the monitor that, in the monitor's view, it is likely that the moratorium will result in a rescue of the company as a going concern.[77] In other words, ease of extension may depend on creditor support and the particular facts of the case. This brings us to the crucial concepts of pre-moratorium debts; pre-moratorium debts without a payment holiday; and moratorium debts.

3.2.3. Creating liquidity

We have already established that a crucial role of a moratorium is to create liquidity. As we have seen, large corporates in the later stages of distress are likely to be suffering from supplier and customer action which is putting significant pressure on cash flow. And it is here that we encounter perhaps the most significant problem with the Part A1 moratorium as a tool for large, financially distressed corporates: its liquidity-creating potential

[69]For the day on which the moratorium comes into force, see Insolvency Act 1986, s A7(1).
[70]ibid s A10.
[71]ibid ss A11 and A12.
[72]ibid s A13.
[73]ibid s A14.
[74]ibid s A15.
[75]CIGA Final Evaluation Report (n 64) 35.
[76]ibid 36.
[77]Insolvency Act 1986, s A13.

is distinctly disappointing. The company is obliged to pay not only moratorium debts but also certain pre-moratorium debts which are not suspended by the Part A1 moratorium.[78] Unsurprisingly, the company must pay the monitor's remuneration and expenses and must pay for goods or services supplied during the moratorium.[79] The company must also pay rent in respect of a period during the moratorium.[80] The meaning of this is not entirely clear, but it seems that it would not be possible for the company to cease operating from premises which it no longer wishes to retain and to cease paying rent during the Part A1 moratorium. The company must also pay all wages or salary arising under a contract of employment and all redundancy payments, whether these fell due before or during the moratorium.[81] And, most significantly of all, the company must pay all debts or other liabilities arising under a contract or other instrument involving financial services.[82] This means that the company cannot suspend debt service or principal repayments falling due under loan agreements or bonds which are not excluded by the eligibility requirements. Moreover, the definition of financial services is relatively wide and other financial service contracts and instruments will be implicated.[83]

This is a serious constraint on the Part A1 moratorium as a tool for large corporates in late-stage distress. A large corporate debtor in the later stages of financial distress is likely to want to cease making capital payments to its financial creditors to create much-needed liquidity. At the same time, as we have already seen, it may be more difficult to hold the ring between financial creditors in the later stages of distress without the benefit of moratorium protection. The Part A1 moratorium is no help with this at all. It is therefore no surprise that the CIGA Final Evaluation Report records that interviewees held up the absence of a payment holiday for financial contracts as an example of why the moratorium is not of use for some distressed companies.[84] Interviewees also expressed concern for uncertainty as to which financial contracts are implicated in the exclusion.[85]

3.2.4. Financing the case

This disappointing liquidity-creating potential may be mitigated, to some extent, if the Part A1 moratorium smooths the path for raising new money while restructuring negotiations are in course. Unlike US Chapter 11, UK corporate insolvency law does not offer a specific regime for raising new debt in a corporate insolvency case. However, a question arises as to whether the Part

[78]ibid s A18.
[79]ibid s A18(3)(a) and (b).
[80]ibid s A18(3)(c).
[81]ibid s A18(3)(d) and (e).
[82]ibid s A18(3)(f).
[83]ibid Sch ZA2.
[84]CIGA Final Evaluation Report (n 64) 36.
[85]ibid 34.

A1 moratorium is able functionally to recreate two of the principal tools provided by Chapter 11's so-called debtor-in-possession financing regime which Ayotte and Skeel have identified. The first important set of tools are tools which enable the new lender to obtain priority for its debt, to reassure the lender of its prospect of repayment.[86] The second important set of tools are tools 'eliminating the effectiveness of negative covenants'.[87] The Part A1 moratorium certainly appears to help the priority position because any moratorium debt gets super priority in any insolvency happening within 12 weeks of the end of the moratorium.[88] The Part A1 moratorium would also prevent a creditor from raising a legal challenge based on breach of a negative covenant in another debt contract. The creditor would need to challenge the action of the directors in raising the new debt in breach of the covenant on the basis that it unfairly harmed their interests.[89] At this point, the court is likely to undertake a highly fact-sensitive inquiry,[90] and it is perfectly possible to conceive of circumstances in which the court concludes that the raising of new debt to make a restructuring possible does not 'unfairly' harm the interest of a creditor with negative covenant protection.

Crucially, however, the new ipso facto provisions do not prevent a lender from accelerating its debt during the Part A1 moratorium.[91] Thus, if the debtor grants new debt in breach of a negative covenant, the existing lender can accelerate its debt and, although the accelerated debt would not acquire a priority position,[92] the debt would be either a moratorium debt or a pre-moratorium debt for which the company does not have a payment holiday so that, unless the company was in a position to pay it, the monitor would be forced to bring the moratorium to an end.[93]

3.3. Summary

Overall, while the design of the Part A1 moratorium does pay some attention to signalling and information-processing concerns, there are serious doubts about how well-adapted it is as a tool to assist the large corporate which finds itself in a deteriorating situation. Of course, one of the crucial decisions for policy makers in moratorium design is balancing the benefits to the debtor against the costs to the creditor.[94] As Buccola puts it, 'each virtue of bankruptcy law has a correlative vice. The automatic stay, for example, can

[86]Ayotte and Skeel (n 22) 1576–78.
[87]ibid 1591.
[88]Insolvency Act 1986, s 174A.
[89]ibid s A4A(1).
[90]Jennifer Payne, 'An Assessment of the UK Restructuring Moratorium' SSRN <https://ssrm.com/abstracts=3759730> 16.
[91]See the exclusion for contracts relating to financial services: Insolvency Act 1986, Sch 4ZZA.
[92]ibid s 174A(3)-(4).
[93]ibid s A38(d).
[94]Payne (n 90) 13.

protect viable companies from inefficient, piecemeal liquidation, but it can also delay the breakup of doomed, money-losing businesses'.[95]

The later the debtor seeks moratorium protection, the greater the risk that the moratorium is being used to delay an inevitable insolvency, thus creating an unjustified interference with creditor rights. It is for this reason that the tools of the European Restructuring Directive cease to be available if the company is insolvent, and the consultations leading to CIGA point to a deliberate attempt in the working out of the English Part A1 moratorium to restrict its use to companies in the earlier stages of financial distress. Nonetheless, the question arises as to whether a Part A1 moratorium with this design motivation will be used by many large corporates. This question gains some further currency when we put the Part A1 moratorium in a comparative frame with administration. As we will see, however, signalling and information-processing theory will be important in this context too.

4. The Part A1 moratorium in a comparative frame with administration

The Part A1 moratorium is not the only option for stay protection for a large corporate. The administration procedure also offers a moratorium; the new section 233B ban on ipso facto clauses is also engaged in administration; and an administrator can propose a CVA, scheme of arrangement or a Part 26A restructuring plan to exit administration, rescue the company as a going concern, and return it to its directors. In many ways administration appears better adapted as a stabilisation and liquidity-creating tool for late-stage distressed corporates than the new Part A1 moratorium.

4.1. Administration as a late-stage stabilisation and liquidity-creating tool

4.1.1. Application; eligibility; and length

Administration is available to a company which is party to a capital markets arrangement. Moreover, while the Part A1 moratorium is only available if and for so long as the monitor is content that a corporate rescue is likely, administration offers a hierarchy of purposes with company rescue at the top,[96] but the ability to move down the hierarchy to a business or asset sale.[97] Thus, administration offers a moratorium during which options can be explored: if it transpires that a company rescue is not possible, the administrator can move down the hierarchy to a more realistic option. An administrator can

[95]Buccola (n 9) 713.
[96]Insolvency Act 1986, Sch B1, para 3(1)(a).
[97]ibid paras 3(1)(b) and (c).

be appointed out of court by the company or its directors,[98] and an administration lasts for twelve months, subject to extension with the agreement of the creditors for up to another year.[99] Administration therefore tackles many of the problems with eligibility and length which we uncovered in the Part A1 moratorium. Perhaps more significantly, administration also has much better liquidity-creating potential.

4.1.2. Creating liquidity: rent

While a company which files for administration must also pay rent on its premises until a restructuring of the leasehold liabilities is agreed, there may be more flexibility to cease operating from premises during administration and to stop paying rent at that point. In English law the term 'lease' refers to both the written document that creates the lease and to the tenant's interest in the land.[100] As Simon Garner and Alexandra Frith put it, 'The tenancy may be created by a contract, but once created it possesses qualities that run beyond the purely contractual'.[101]

Thus, leases are subject to their own, special common law and statutory regime which is fundamentally different from contract law. The parties are free to include a termination clause in the lease agreement, normally known as a break clause. However, break clauses are usually only exercisable at specific points in the term of the lease or on the occurrence of a specified event. If there is no break clause, or the specific point in time at which a break clause is exercisable has not occurred, a tenant with a fixed term lease has no right to terminate and the tenancy will come to an end only at the end of its term. The technical term for termination in this context is 'surrender' – the tenant who surrenders a lease gives up their estate in land and their interest is absorbed back into the landlord's larger interest.[102] However, unless there is a break clause or the lease has come to the end of its term, surrender can only occur by mutual agreement between the landlord and the tenant.

Zacaroli J has already concluded that this means that a tenant cannot unilaterally surrender a lease in a scheme of arrangement.[103] This analysis arises precisely because surrender is not a purely contractual matter, but rather involves the surrender of the tenant's interest in land and its absorption into the landlord's interest. As a result, surrender goes beyond the rights of

[98]Insolvency Act 1986, Sch B1, paras 22–34. An application can also be made out of court by the holder of a qualifying floating charge (Insolvency Act 1986, Sch B1, paras 14–21) or in court on the application of the company, its directors, one or more of the company's creditors or a combination of those persons (Insolvency Act 1986, Sch B1, paras 11–13).

[99]Insolvency Act 1986, Sch B1, para 76. It is worth noting that one free text comment at the end of the survey for the CIGA Final Evaluation Report specifically identified that 'an IP might prefer the longer period of administration to address issues which had arisen' CIGA Final Evaluation Report (n 64) 35.

[100]Simon Garner and Alexandra Frith, *A Practical Approach to Landlord and Tenant* (2017) 35.

[101]ibid 36.

[102]ibid 148.

[103]*Re Instant Cash Loans Limited* [2019] 10 WLUK 97.

the debtor company and its creditor as debtor and creditor and so does not fall within the scheme jurisdiction (nor, it is generally accepted in the market following Zacaroli's judgment, within the company voluntary arrangement jurisdiction or Part 26A restructuring plan procedure jurisdiction). While the author is not aware of any case law on the point, it is suggested that a company in administration is also prevented from unilaterally surrendering a lease.

However, it is also suggested that rent would not rank as an expense of the case if the administrator had offered up the premises with vacant possession and the landlord had declined to take them back. This arises because of the so-called Lundy Granite principle.[104] In *Lundy Granite,* Lord Justice James said:

> … if the company for its own purposes, and with a view to the realization of the property to better advantage, remains in possession of the estate, which the lessor is therefore not able to obtain possession of, common sense and ordinary justice require the Court to see that the landlord receives the full value of the property.

The modern application of the Lundy Granite principle was set out by Lord Justice Lewison in *Jervis v Pillar Denton Ltd*:

> The true extent of the principle, in my judgment, is that the office holder must make payments at the rate of the rent for the duration of any period during which he retains possession of the demised property for the benefit of the winding up or administration (as the case may be). The rent will be treated as accruing from day to day. Those payments are payable as expenses of the winding up or administration. The duration of the period is a question of fact and is not determined merely by reference to which rent days occur before, during or after that period.[105]

An administrator who offers up vacant possession is not retaining 'possession of the demised property for the benefit of the winding up or administration (as the case may be)'.[106] It is therefore suggested that although the company in administration may not be able unilaterally to surrender the lease, unpaid rent will not be required to be paid as the administration proceeds, if the landlord is able, but declines, to take the property back. If this is right, then administration does offer liquidity-creating benefits over the Part A1 moratorium for debtors with significant leasehold estates because, as we have seen, it does not appear that it is possible to cease paying rent on unwanted premises under Part A1. In administration, the rent can be left unpaid during the administration case and can be compromised in any restructuring transaction.

[104]*Lundy Granite* (1870 - 71) L R 6 Ch App 462 (CA).
[105][2014] EWCA Civ 180; [2014] 3 WLR 901.
[106]ibid.

During the administration of Debenhams, a major UK high street retailer, there were news reports which suggest this was the approach. Indeed, ITV News reported that when Westfield shopping centre refused significant rent reductions, Debenhams 'responded by emptying shelves and clothing racks and shifting goods to its other sites'.[107] The ability to cease paying rent during the period of the moratorium may be particularly important for retailers, casual dining operators, and hoteliers where a principal cause of the debtor's difficulties is an over-rented leasehold estate.

4.1.3. Creating liquidity: employees

Administration is also more promising where a business needs to reduce the size of its workforce to secure its survival. As we have already seen, the debtor must also pay all wages or salary arising under a contract of employment and all redundancy payments, whether these fell due before or during the Part A1 moratorium.[108] In contrast, once a debtor has filed for administration, the administrator has 14 days to decide which employment contracts to adopt.[109] At that point, the company in administration is only liable for wages or salary (including holiday or sick pay) or contributions to occupational pension schemes in respect of the adopted contracts of employment for the period after adoption. Redundancy payments, unfair dismissal payments, or protective awards for failure to consult are not included in 'wages or salary'.[110] In short, while a large corporate under the protection of the Part A1 moratorium must pay all wages and salary and redundancy payments, the company in administration can avoid paying employee claims other than wages or salary on adopted contracts for the period after adoption.

For sure, in a traditional administration in which the objective is to sell the business and assets as a going concern, complex questions arise around dismissal because of the Transfer of Undertakings (Protection of Employment) Regulations, 2006 (TUPE). In certain circumstances, TUPE can render a dismissal automatically unfair and pass liability for the unfair dismissal to the purchaser. This may require careful navigation for the purchaser to be willing to proceed,[111] and may still be a relevant consideration where a debtor seeks the late-stage protection of the administration moratorium, and a pivot to a business, rather than a corporate, rescue remains a possibility. Moreover, if a corporate rescue is to be achieved, any unpaid employee

[107] Joel Hills, 'Debenhams Empties Westfield Store as Landlord Fear Mass Store Closures' 8 April, 2020 <https://www.itv.com/news/2020-04-08/debenhams-empties-westfield-store-landlords-fear-mass-store-closures-administration>.

[108] Insolvency Act 1986, s A18(3)(d) and (e).

[109] Insolvency Act 1986, Sch B1, para 99(4) and para 99(5).

[110] *Allders Department Stores Ltd (in administration*) [2005] 2 All E R 122; *Huddersfield Fine Worsteds Ltd* [2005] 4 All E R 886.

[111] Craig Rajgopaul, 'TUPE and insolvency' 1 June 2008 Tolley's Employment Law Newsletter.

claims will need to be dealt with eventually in the reorganisation plan. Certain employee claims rank higher in priority than other unsecured creditors in English corporate insolvency law's distributional order of priority,[112] and are subject to a security scheme operated by the National Insurance Fund.[113] This may have implications for the payments that need to be made to employees either to achieve employee and State consents or for a court to be willing to impose the restructuring plan. Nonetheless, administration appears to offer more flexibility to create liquidity by reducing the wages bill than the Part A1 moratorium.

4.1.4. Creating liquidity: finance contracts

Crucially, from a liquidity-creating perspective, there is no requirement to pay debts or other liabilities arising under a contract or other instrument involving financial services in administration. As we have identified, even when a large corporate is in serious financial distress, it may still seek to keep its suppliers whole to the greatest extent possible. It may, however, be considerably less concerned about ceasing its capital payments to its financial creditors while a deal is sought. As with the Part A1 moratorium, the administrator can make payments to creditors where they consider it is 'likely to assist achievement of the purpose of administration'.[114] This means that it would not be unusual for payments to continue to be made to crucial suppliers, including payment of their pre-filing debts, while payments to financial creditors were suspended. In short, where the restructuring plan is focused on the claims of landlords, employees and/or financial creditors, administration offers a way to capture these debts within the moratorium protection while keeping a significant number of other claims outside it.

4.1.5. Financing the case

Finally, administration may also offer a better route to get finance into a late-stage distress situation. Recall the two features of a regime for raising new money in a moratorium identified by Ayotte and Skeel – the ability to provide a priority position for the new money and the ability to turn off negative covenants in existing finance contracts which may restrict the debtor's freedom to raise it – and the question mark about the ability to turn off negative covenants in the Part A1 moratorium.[115] There is a good argument that new debt raised in an administration would have priority over floating charge

[112]Insolvency Act 1986, Sch 6.
[113]Employment Rights Act 1996, s 166–69.
[114]Insolvency Act 1986, Sch B1, para 66. For Court of Appeal authority on the breadth of para 66 see *Re Debenhams Retail Limited (in administration)* [2020] 3 All E R 319.
[115]n 91 and accompanying text.

holders and unsecured creditors as an expense of the case.[116] There are also good arguments that negative covenants in other finance contracts do not prevent an administrator from raising new debt.[117] Thus, administration appears more promising in its potential to turn off negative covenants.

4.2. Administration through the information-processing lens

Nonetheless, when we view administration through a signalling and information-processing lens, matters become rather more complex. First, administration is primarily a management-displacing procedure. Paragraph 64 of Schedule B1 to the Insolvency Act 1986 provides that ' … an officer of a company in administration may not exercise a management power without the consent of the administrator'.[118] We have already touched on the signalling benefits of a debtor-in-possession procedure for the company's stakeholders. And there is, of course, the entirely practical consideration that directors may be reluctant to file for a procedure in which they lose control while there is any hope of a restructuring at all.

Paragraph 64 does offer a clue as to how administration may be adapted to a more debtor-in-possession orientation, as it provides that management power may not be exercised 'without the consent of the administrator'. In the administrations of T&N Ltd, Railtrack Plc, and Metronet Rail, the administrators entered a protocol in which management were left with management powers. The administrators then sought and obtained a First Day Order from the court memorialising the arrangements. In an article early in the Covid pandemic, the Insolvency Lawyers' Association suggested that this adaptation could be used more widely.[119] Mark Phillips QC, William Wilson, and Stephen Robins at South Square produced a consent protocol which was intended to act as a starting point for insolvency practitioners and their advisers in developing boundaries for the respective roles of management and the insolvency practitioners in the case.[120] Other trade associations and the press began to pick up the idea, and it began to be referred to by the slightly unfortunate name of 'light touch administration'.[121] Perhaps even

[116]Vanessa Finch and David Milman, *Corporate Insolvency Law: Perspectives and Principles* (3rd ed, CUP 2017) at 336–38; Gerard McCormack, 'Super-priority New Financing and Corporate Rescue' (2007) Journal of Business Law 701.

[117]Sarah Paterson, 'Finding Our Way: Secured Transactions and Corporate Bankruptcy Law and Policy in America and England' (2018) 18 Journal of Corporate Law Studies 247, 254.

[118]ibid Sch B1, para 64.

[119]Insolvency Lawyers' Association, 'Changing the Narrative Around Administration' 2 April 2020 <https://www.ilauk.com/news-events/news-view/changing-the-narrative-around-administration>.

[120]Mark Phillips QC, William Willson, and Stephen Robins, 'Joint Administrators' Consent under Paragraph 64 of Schedule B1 to the Insolvency Act 1986' ILA <https://www.ilauk.com/docs/ILA.consent_.protocol_.17.April_.2020.V2_.pdf>.

[121]Jonathan Eley and Tabby Kinder, 'Companies Explore 'Light Touch' Administration in Wake of Debenhams' *Financial Times* (16 April 2020) <https://www.ft.com/content/76c7c985-ff8c-4707-b4e4-28eb7a8f7b62>.

more significantly, it began to attract the attention of the judiciary, with ICC Judge Jones setting out one of the first judicial considerations of the technique:

> Administrators may decide at any stage to involve a director(s) and permit that director to exercise management powers. There is also a myriad of possible circumstances when administrators may do so. At one end of the spectrum are cases where to best achieve the purpose of the administration, directors will be empowered to manage the day to day running of the business subject to the administrators' supervision. This may be because of their expertise and reliability and/or because it reduces the cost and expenses of the administration which may be unnecessary and/or may be detrimental to the purpose. … The extent of the supervision will depend upon the circumstances and the administrators' assessment of the need for supervision.[122]

Two issues arise here. First, many insolvency practitioners have expressed concern about how the supervisory burden can be effectively discharged. Secondly, management can never be sure that the administrators will continue to leave management power with them; it is the administrator who is in ultimate control. Nonetheless, it is suggested that the first issue can be navigated through careful planning and a carefully drafted First Day Order and that the second is much less of a concern for management when the company's financial position is rapidly deterioriating and radical steps must be taken if there is to be any hope of rescue. It is suggested that the much more significant issue is the broader signalling and information processing associated with administration.

Let us recall Melanie Mitchell's three questions which need to be answered whenever information is processed in a complex system:

- What plays the role of "information" in this system?
- How is it communicated and processed?
- How does this information acquire *meaning*? And to whom?[123]

The relevant information is the information that the company has filed for administration. The company is required to make various legal filings and may also issue a press release; the administrators may write to affected stakeholders and, increasingly, in a large corporate situation launch a website with information about the case; and the news of the administration may well be reported by the broadcast and press media. The company's stakeholders receive this information and use it as a signal of the company's prospects and of their own likely fate. Crucially, administration has a specific meaning in the market because it has historically signalled that efforts to restructure

[122] *Ian Barry Dearing v Mark Skelton, Richard Fleming (Joint Administrators of ASA Resource Group plc* [2020] 5 WLUK 422.
[123] Mitchell (n 7) 170.

the company have failed. If this signalling effect cannot be changed, then there is a risk that administration becomes a self-fulfilling prophecy of collapse. If the company's stakeholders process the news that the company has been placed in administration and attach to that news the meaning that the company is beyond saving, they may become extremely reluctant to deal with the company during the administration and, perhaps even more crucially, may lose faith in the company for the future. One of the benefits of the Part A1 moratorium is that, because it is new and because it has clearly been explicitly designed only to support company rescue, it does not give rise to signalling problems of the same magnitude as administration.

The question which was posed by the ILA article is whether it is possible to persuade directors, insolvency practitioners, trade suppliers, customers, employees, and the media that administration does not necessarily signal the demise of the company? Some brave navigators have attempted to chart such a path. Although it was not ultimately successful, Debenhams plc did pursue an administration of this type which was widely reported in the press.[124] And a small number of other companies have used administration as a space within which to propose restructuring plans.[125] At the same time, if administration starts to be more frequently used to engage the moratorium while large corporate debtors in the later stages of distress seek a restructuring, creditors may raise challenges to some of the more novel liquidity-creating tools explored in this article. It is notable that the ILA/CLLS 2018 Issues Paper proposed two alternative routes for reform.[126] One route was to introduce a new schedule to the Insolvency Act 1986 which would only apply where an administrator was pursuing the corporate rescue purpose in administration.[127] The purpose of this would be to harness the benefits of the administration moratorium while attempting to address the significant problem, from an information-processing viewpoint, that administration has come to be associated with a sale transaction. The alternative route was to create a new, stand-alone procedure and the article expressly recognised the information-processing advantages of explicitly equating a new procedure with corporate rescue. As we have seen, the Government opted for the second route. Given this, it is not clear how much appetite there will be to attempt to change the narrative around administration, and how the courts will react to such efforts if cases become more frequent.

[124]Eley and Kinder (n 121).
[125]Amicus Finance plc [2021] EWHC 3036 (Ch).
[126]ILA/CLLS 2018 Issues Paper (n 42) 9–10.
[127]Insolvency Act 1986, Sch B1, para 3(1)(a).

4.3. Summary

In this section, the argument has been made that administration offers more promise as a stabilisation and liquidity-creating tool for large corporates seeking a restructuring in the later stages of distress than the Part A1 moratorium. On the other hand, administration also raises more significant signalling and information-processing concerns than the Part A1 moratorium. It is likely to be useful as a late-stage restructuring tool only if these signalling and information-processing concerns can be overcome and if the courts embrace the new adaptation of the tool. This also raises the question of whether there are any other circumstances in which the Part A1 moratorium may have a role to play as a large corporate restructuring tool.

5. The Part A1 moratorium as a strategic tool for large corporates

To explore other roles for the Part A1 moratorium for large corporates, we need to turn our information-processing lens away from the company's stakeholders and towards the company itself. At the beginning of the case, the company is also faced with uncertainty about the best way to resolve its difficulties. It must also seek out information to decide on a way forward. Uncertainty, here, has the meaning assigned to it by Jay Galbraith, ' … the difference between the amount of information required to perform the task and the amount of information already possessed by the organization'.[128] In his work, Buccola agrees that the concept of the moratorium as a 'breathing space' for the debtor has less salience for large corporates in modern markets. He puts this claim squarely in information-processing terms:

> A "breathing space" does not obviously offer much in the modern era. There is no magic to the bankruptcy petition. It generates no new information. If a deal to preserve a company's business is available – whether through a debt restructuring or a going concern sale – its managers can learn about it equally well whether or not a Chapter 11 case has begun.[129]

Thus, outside the moratorium, the company and its advisers are learning information about potential deals to save the company's business. The company and its advisers are likely to explore multiple solutions in parallel,[130] although not all possibilities are explored at the same speeds or to the same depth.[131] As Mitchell puts it, 'As information is obtained and acted on,

[128]Jay R Galbraith, *Designing Complex Organizations* (1973) 5.
[129]Buccola (n 9) 745.
[130]Mitchell (n 7) 182.
[131]ibid.

exploration gradually becomes more deterministic and focused in response to what has been perceived by the system'.[132]

Eventually, if the debtor is to restructure successfully, it is likely to develop a preferred plan and to take steps (borrowing from Mitchell again) to 'lock in this emerging view'.[133] This may not have been the only possible plan with a prospect of success: the company and its advisers will have considered rival plans in the information-processing phase and may have discarded other, potential plans because it was considered, sometimes on fine judgments, that the alternative plan out-competed those rivals. Ultimately, however, the company must develop a coherent plan which will be 'frozen in'.[134]

At this point, the company may find that its preferred way forward faces competition from alternative plans put forward by other stakeholders. As a recent case shows, the Part A1 moratorium may represent one means to achieve the debtor's ends (implementation of its preferred restructuring plan). The relevant case was *Minor Hotel Group* and arose as part of a bitterly contested fight between investors in the Corbin & King restaurant business and its founders.[135] The facts are relatively complex and do not bear repeating here. Suffice it to say that the founder-directors placed the operating companies into a Part A1 moratorium apparently to stymie attempts by the investors to take control of the group through an administration of the finance holding company. Litigation ensued as to whether the moratorium should be terminated. Yet, the important point for our purposes is that the Part A1 moratorium appears to have been employed as a tool to gain a strategic advantage in a strategic battle. Thus, the Part A1 moratorium may be mobilised by the directors of the debtor as a strategic tool to achieve their objectives. In the *Minor Hotel* case, the founder-directors used information about the objectives of the investors gained when the finance holding company was placed into administration to develop a strategy engaging the Part A1 moratorium.

Using Mitchell's analytical frame again, as the company gains information during the case, a strategic role may emerge for the Part A1 moratorium in pursuing the emerging restructuring plan. When we keep the information-processing lens trained on the company, we also find a different calculus once we consider the Part A1 moratorium and a small company.

6. The Part A1 moratorium as a restructuring tool for small companies

Many small companies are dependent on a single provider of bank finance for their working capital needs, frequently supported by directorial

[132]ibid 183.
[133]ibid 204.
[134]ibid 208.
[135]*Minor Hotel Group* [2022] 2 WLUK 221.

guarantees.[136] The CIGA Final Evaluation Report notes a 'general perception that the Moratorium is more likely to be used by SME companies than large companies',[137] but goes on to suggest that as many SMEs have a single main financial creditor, often their bank, and as the moratorium will not prevent the bank from enforcing its rights, it is 'not seen as an effective rescue tool in such cases'.[138] However, SMEs are unlikely to find it straightforward to replace this working capital provider if they are experiencing, or have experienced, financial distress. In practice, this often means that the bank will need to be content with the company's proposals and to remain supportive through the process.[139] As a result, it is unlikely that the company would wish to use moratorium protection to suspend payments to the bank without the bank's consent. This would communicate a hostile stance to the bank, which the bank is likely to interpret negatively, reducing the chances that it would support any restructuring effort. As a result, the fact that principal and interest due to the bank must be paid during the Part A1 moratorium may not be of concern to many SMEs. At the same time, it is highly likely that the company will need to compromise some or all of its operating liabilities for the bank to be prepared to support the restructuring effort. Thus, there may be benefits for the company in suspending payments to general unsecured creditors while it gathers information about the most promising restructuring plan, given that these liabilities will ultimately be included in any reorganisation plan. The Part A1 moratorium may, therefore, have more utility as a small company tool than a large corporate restructuring tool.

Nonetheless, the difficulty for small companies may be the transaction costs associated with moratorium protection.[140] Although the monitor has a relatively limited role, they must still be paid; there is a relatively high compliance burden for the company associated with the Part A1 moratorium; and legal advice will be needed both to put the moratorium in place and to maintain it. The question of the affordability of transaction costs associated with the moratorium for small companies falls outside the scope of this article, but it is undoubtedly relevant in determining the utility of Part A1 for such small firms.

[136] Ronald Davis, Stephan Madaus, Alberto Mazzoni, Irit Mevorach, Rizwaan Jameel Mokal, Barbara Romaine, Janis Sarra and Ignacio Tirado, *Micro, Small, and Medium Enterprise Insolvency: A Modular Approach* (2018) 10.

[137] CIGA Final Evaluation Report (n 64) 35–36.

[138] ibid.

[139] For a discussion of the relationship between a small business and its senior lender see Edward R Morrison, 'Bargaining around Bankruptcy: Small Business Workouts and State Law' (2009) 38 The Journal of Legal Studies 255.

[140] For a discussion of the real problem of transaction costs for a small business attempting a restructuring see Robin Greenwood, Benjamin Iverson, and David Thesmar, 'Sizing Up Corporate Restructuring in the COVID Crisis' National Bureau of Economic Research Working Paper 28104, November 2020 3, 19.

7. Conclusion

The argument has been advanced in this article that a large corporate is only likely to seek moratorium protection when the benefits which it brings, in terms of creating stability and liquidity, outweigh the signalling and information-processing disadvantages which are associated with it. As a result, a large corporate is likely to view moratorium protection as most useful when it can stabilise the business and create liquidity in the later stages of financial distress while mitigating signalling and information-processing costs as much as possible. The Part A1 moratorium does a relatively good job of containing the signalling and information-processing problems which arise but does not measure up well as a stabilisation and liquidity-creating tool. When the Part A1 moratorium is placed in a comparative frame with administration, the administration moratorium appears to hold out more promise as a stability and liquidity creating tool in late-stage distress. However, there are significant signalling and information-processing disadvantages associated with administration and it is only if these can be reduced or overcome that it is likely to find a place in the toolbox for large corporates seeking to restructure. Moreover, the administration moratorium is not designed solely to support corporate rescue and new challenges may need to be navigated if it is frequently mobilised for this purpose.

When the information-processing lens is trained on the company, rather than its stakeholders, we do find potential strategic applications of the Part A1 moratorium by large corporates. And keeping the information-processing lens trained on the company suggests that the Part A1 moratorium may be useful for smaller firms. One concern with the utility of the Part A1 moratorium for small companies may be the transaction costs associated with it, although that is outside the scope of this article and awaits further research.

Overall, the analysis in this article suggests that the Part A1 moratorium may not achieve widespread popularity without reform and that, although administration may hold out more promise as a late-stage restructuring tool, there are significant signalling and information-processing costs and legal uncertainties associated with it if it starts to be used seriously for this purpose. Of course, moratorium protection raises difficult questions about the balance of debtor and creditor interests, and it may be a deliberate policy to restrict the application of both the Part A1 and the administration moratorium. If this is the case, then the legislative regime may have achieved its aim. Yet, there are reasons to suspect that late-stage distress may be a more frequent phenomenon over the next decade than it has been over the last.[141] If this is right, then we may need either (i) to revisit the design of the Part A1 moratorium; or (ii) to consider the role which we expect the

[141]Paterson, Covenant-lite Lending (n 34).

administration moratorium to play and to consider whether it requires any further support.

Given that the UK Government chose to introduce the new Part A1 moratorium, rather than reforming administration, it is perhaps more likely that improvements could be made to Part A1 to address its current weaknesses. The CIGA Post-Implementation Impact Review suggests four areas of potential improvement: amending eligibility criteria; amending creditor priority in a subsequent insolvency procedure; clarifying the definition of 'financial services'; and including financial contracts within the payment holiday.[142] The review also suggests providing guidance on the role of the monitor and on extending the length of the moratorium. By focusing on the Part A1 moratorium through an information-processing lens as a late-stage corporate restructuring tool, and in a comparative frame with administration, this article aims to contribute to debate on these and other potential reforms, and on wider issues about the role of moratoria in modern corporate restructuring practice.

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[142]CIGA Post-Implementation Impact Review (n 64) para 6.3.