Moratorium orders – court issues new guidance on when they will be approved

Standalone moratoriums were introduced under the Corporate Insolvency and Governance Act 2020 ("CIGA") as a new measure for helping companies in financial difficulties. Standalone moratoriums exist outside of an insolvency process and grant a period of breathing space, giving companies protection from creditors, whilst directors try to rescue the company. A moratorium for up to 40 business days can be obtained without court or creditors' consent. Alternatively, creditor consent can last up to a year and court orders can be even longer.

On 26 June 2023, the Insolvency Service published its official three-year review of the permanent measures introduced by CIGA which included the moratorium procedure. Overall, the review found that although the CIGA measures have been broadly welcomed and seen as enabling more companies to be rescued without first being required to enter insolvency proceedings, it has been under-utilised. As of 30 June 2023, only 45 moratoria have been obtained.

This could be because moratoriums are still a new measure and there is a lack of judicial guidance. Alternatively, it could be because companies are concentrating on the rescue of the company, rather than a short term solution for a longer term problem.

Case background

The recent case of *Grove Independent School Ltd, Re, 2023 WL 06795092 (2023)* highlighted the challenges of applying for a moratorium where a company has already been presented with a winding up petition.

The directors of the company, which traded as an independent school for around 200 pupils and 50 staff, sought a moratorium to allow it to continue to trade whilst it worked out refinancing after it was presented with a winding up petition from a creditor, HMRC, due to outstanding tax arrears.

In situations where a company is subject to a winding up petition, a court application is required in order to obtain a moratorium. This case provides helpful guidance on the test that the court will use when determining whether to grant a moratorium.

Judgment

The court compared the following two scenarios:

1. What is the result that would likely be achieved for the creditors as a whole by the imposition of a moratorium?
2. What is the result that would likely be achieved for the creditors as a whole without a prior moratorium?

The court had to be satisfied on the balance of probabilities that the former would be a better option. The standard of proof is therefore that there must be more than a 50% chance that a moratorium will achieve a better result for the creditors as a whole.

The test is different than applications for administration orders; where the court must be satisfied that the order would 'reasonably likely' achieve the purpose of the administration.

The court decided that granting a moratorium would likely lead to the rescue of the company and that liquidation on petition by HMRC would be worse for creditors. The judge also considered the social function of the school; closure would affect numerous parents, children and staff and it would cause disruption to studies.

Conclusion

Moratoriums are a useful mechanism for companies in financial difficulties to enter into a short breathing space to allow them to work out their finances, although they have been underutilised to date. The recent judicial guidance provided in *Grove* highlights that the court has a discretion to impose a moratorium when a company has already been presented with a winding up petition where, on the balance of probabilities, it would achieve a better result for creditors as a whole.

If you would like insolvency advice, please contact our commercial disputes team who will be happy to help.

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