Curtailing the use of multiple Notices of Intention to Appoint Administrators: The case for a moratorium?

Over the past decade there have been a number of proposals for reform of the corporate insolvency framework, with the expansion of pre-insolvency moratoria repeatedly on the agenda. Following Government consultations on the introduction of a separate moratorium process in 2009, 2010 and most recently 2016, the reception of variations on this common theme has been underwhelming. Many respondents have questioned the need and benefit of such reform, preferring instead revision of the existing structures or even maintaining the status quo.

The recent decision handed down by the Court of Appeal in *JCAM Commercial Real Estate Property XV Ltd v Davis Haulage Ltd* [2017] EWCA Civ 267 on the misuse of repeated Notices of Intention to Appoint Administrators may, however, change this perception and reopen the debate over the need for a new pre-insolvency moratorium as a gateway mechanism.

The Case

Davis Haulage Limited ("DHL") was a company that found itself in financial difficulty in early 2016. In the face of possession proceedings from its landlord (the appellant) and the threat of a winding up petition from HMRC, DHL's sole director filed a Notice of Intention to Appoint Administrators ("NoI") with the court on 22 January 2016, thereby creating an interim moratorium of up to ten business days pursuant to paragraphs 28 and 44 Schedule B1 Insolvency Act 1986 (all subsequent references to paragraphs shall be to Schedule B1 Insolvency Act 1986 unless stated). Three further NoIs were filed, immediately following the expiry of each prior NoI, in effect creating a pre-insolvency moratorium which ran from 22 January 2016 to 17 March 2016, a period of some 56 days.

The issue before the Court of Appeal was whether a director must have a settled intention to appoint an administrator when filing a NoI. It had been held at first instance that this was not necessary, but rather the appointment of an administrator could be considered a second best choice should other options under contemplation not work out.

Filing of the NoIs

DHL's sole director was entitled to appoint administrators in accordance with paragraph 22, subject to giving notice of the intention to the person entitled to appoint an administrator pursuant to paragraph 14. Accordingly, a NoI in the prescribed Form 2.8B was filed pursuant to paragraph 26 and Rule 2.20 Insolvency Rules 1986. Attached to the NoI was a record of the director's decision to appoint administrators, as required by the prescribed form. This decision recorded that the sole director had considered and discussed DHL's financial position and was of the opinion that DHL was insolvent and that he "should seek the immediate appointment of administrators to [DHL] as soon as reasonably practicable." The record went on to state that the director would complete and sign such

other documentation required "in order to effect the director's appointment of the administrator[s]."

Despite the contents of the first NoI, correspondence sent by the proposed administrators' firm suggested that the appointment of administrators was not imminent. An email to the appellant's agent dated 2 February 2016 stated that "a feasible solution to secure the business going forward" was being sought and that it was intended to "undertake a marketing exercise this week with a possibility of completing a sale of the business and assets of [DHL] as a going concern" – this just two business days before the interim moratorium was to expire. This was followed by an email enclosing the second NoI, stating that the proposed administrators' firm was working with the management team and secured lender of DHL to ensure the "business future survival", one element of the proposal being to settle the arrears to the appellant in full – suggesting that administration would not have been the intended outcome. The work to secure the "business future survival" was reiterated when the third NoI was sent to the appellant.

It became apparent that the NoIs were being filed to offer DHL the protection of the interim moratorium under paragraph 44 whilst the best means for securing its future were considered, rather than as a precursor to the imminent appointment of administrators as indicated in the director's original statement. On 23 February 2016, the appellants' solicitors were informed that a CVA proposal was being prepared, and subsequently on 29 February 2019 that it would be finalised the following day. The CVA proposal was then filed at court on 3 March 2016 and sent to creditors under cover of a letter dated 4 March 2016, with a meeting scheduled for 23 March 2016.

Having filed the CVA proposal on 3 March 2016, a fourth NoI was then issued on 4 March 2016. A different firm of insolvency practitioners now appeared to be advising the sole director of DHL. The sole director explained these actions in a witness statement, stating that following issue of the proposal significant creditors intimated they would not support the CVA. The sole director therefore considered it "appropriate and necessary for DHL to have the benefit of a moratorium" with the "intention to place DHL into administration should the CVA proposal not be approved." The disparity between the director's witness statement and the series of events appears to have been overlooked by the court. The fourth NoI, and the associated interim moratorium, subsequently expired and the CVA was approved with modifications on 6 April 2016.

The decision of the Court of Appeal

The appellant was seeking an order that the fourth NoI be vacated and removed from the court file on the grounds that it was an abuse of process. In turn, the appellant sought retrospective permission for commencement of possession proceedings, which it had originally attempted to initiate on 18 January 2016, before being informed of the interim moratorium following the first NoI.

It was held that the fourth NoI would be so removed, as notice had been invalidly given. Giving the lead judgment, David Richards LJ stated that the statute required a settled intention to appoint administrators, and in the absence of such intention, notice could not be validly given under paragraph 26 nor filed under paragraph 27. As a result, the interim moratorium under paragraph 44

was not validly invoked. David Richards LJ declined to declare the filing of repeated NoIs as an abuse of process.

In reaching this decision, the Court of Appeal considered three key characteristics of the interim moratorium pursuant to paragraph 44, which were deemed inconsistent with the use on the facts.

- Firstly, the purpose of the interim moratorium is both limited and specific, offering the company protection whilst the person with a prior right of appointment decides whether to exercise it. If there is no person with a prior right of appointment, then the interim moratorium cannot be invoked;

- Secondly, if the person to whom notice is given exercises its right of appointment, it would frustrate the proposed CVA being considered; and

- Thirdly, the presence of a specific pre-CVA moratorium under Schedule A1 and extensive consultations about extending this, suggest that the current legislative policy is to restrict a pre-CVA moratorium to companies eligible under Schedule A1, not to include all companies that have granted floating charges.

Impact on practice

Whilst David Richards LJ refused to frame the actions of the sole director and his advisers as an abuse of process, he did acknowledge that filing a NoI where there was not a settled intention to appoint administrators "is no doubt, in a technical sense, an abuse of the court's process."

In the earlier first instance case *Re Cornercare Limited* [2010] EWHC 893 (Ch), to which David Richards LJ does not appear to have been referred, Purle QC HHJ suggested (at para 11) that should "an unscrupulous individual or group of individuals" engineer a "continuing moratorium by filing repeated notices of intention to appoint … the court would have adequate power to treat that as an abuse and act accordingly." It was considered that these powers would include removing from the court file any abusive NoI.

The judgment handed down by David Richards LJ extends and clarifies this point. There is no requirement that a NoI be used unscrupulously for it to be removed from the court file. The judgment clearly states that "there is no reason to suppose that either [the sole director] or the experienced insolvency practitioners and solicitors advising him and the company did not believe that he was entitled to give and file the notices." Rather, a NoI would be invalid if not used for the proper purpose; that is there was not a settled intention to appoint administrators when filing the NoI.

It became apparent during both the first instance and appeal hearings that the filing of repeated NoIs to create a continuing moratorium was not uncommon in practice, despite the 2010 judgment of Purle QC HHJ. An email from a partner of the solicitors representing DHL in the first instance hearing, described as being of considerable experience in the area, stated that it was "not uncommon in situations like this where the success of a CVA is uncertain to run a parallel process and seek protection in that period." David Richards LJ appears to acknowledge that such actions

were accepted practice, however, his concluding remarks make it clear that this practice would not be possible in the future:

> "For the future, it will be clear, by reason of this court's decision, that a conditional proposal to appoint an administrator does not entitle or oblige a company or its directors to file a notice under paragraph 26 schedule B1."

The use of the interim moratorium arising pursuant to paragraph 44 to provide a company with breathing space to consider its options or continue trading will no longer be possible. Rather, the company or directors must have a settled intention to appoint administrators when giving and filing a NoI. Such notice will be invalid if not. How this will be evidenced, or challenged, remains to be seen. Perhaps guidance for insolvency practitioners could be included as part of the JIC's current consultation on revising the Insolvency Code of Ethics.

A need for a revised moratorium?

It is apparent that the sole director and advisers felt that DHL needed the protection of a moratorium on creditor actions in order to evaluate and pursue the best option to allow the business to continue, and in turn provide the best return for creditors. This is evident in the email correspondence from the proposed administrators' firm, which states that the first NoI was filed in view of imminent possession proceedings by the appellant and a possible winding up petition from HMRC.

According to the sole director's witness statement, trading in administration (and the protection of the moratorium under paragraphs 42 and 43) would not have been possible. Any administrator would not hold the necessary haulage licences. From records filed at Companies House, DHL was a medium-sized company so was not eligible for the protection of the Schedule A1 moratorium (though the uptake of this by eligible companies appears to be negligible, see for example Walters and Frisby *Preliminary Report to the UK Insolvency Service into Outcomes in Company Voluntary Arrangements* (2011)). On the facts, there was no suitable protection available to DHL to allow it to pursue the best possible return for creditors safe from adverse individual creditor action. It could be argued that this puts the onus on the company and its management to address issues at the earliest opportunity, however some events are difficult to plan for.

In this instance, following the improper moratorium period, a CVA was agreed with DHL's creditors on 6 April 2016. This was less than eleven weeks after the first NoI was filed and three weeks after the last NoI expired. Although the CVA subsequently failed, and a pre-packaged sale of the business and assets completed, it appears from the administrators' report filed at Companies House that significant payments were made into the CVA during 8 months of continued trading, before the loss of two key contracts appears to have undermined further trading. It is questionable whether a CVA could have been achieved, in light of the reported creditor pressure, without such respite in the preceding weeks.

Whilst more research is needed into what constitutes a successful CVA outcome (the University of Wolverhampton has recently been commissioned by R3, with the support of the ICAEW, to carry out such research), allowing a company the chance to instigate a CVA subject to approval by creditors

must be considered preferable to a rushed pre-packaged administration, or worse still a premature winding up of a company's business. The protection from creditor pressure during the evaluation period could be key.

Whether this be achieved by the extension of the small company CVA moratorium to all companies, with some major revisions to address concerns over some of the detailed provisions of Schedule A1, or the introduction of a separate flexible gateway mechanism is debateable. This author has previously argued in favour of utilising existing mechanisms rather than introducing more layers to an already complex system (see (2016) 385 Co.L.N. 1).

The risk of abuse

The introduction of an effective moratorium in some form for all companies appears a sensible development, especially in light of the restriction placed on the future use of NoIs by the judgment in *JCAM Commercial Real Estate Property XV Ltd v Davis Haulage Ltd* [2017] EWCA Civ 267. It will be important to set clearly the parameters of any moratorium process to avoid claims of improper use.

One of the overwhelming messages in the responses to the moratorium proposals in the 2016 consultation, *A Review of the Corporate Insolvency Framework: A consultation on options for reform* (available at www.gov.uk/government/consultations/a-review-of-the-corporate-insolvency-framework), was the risk of abuse of the process (see (2016) 388 Co.L.N. 1 for a summary of the responses). Such abuse under the present NoI system has been reported in a number of cases. In *X-Fab Semi-Conductor Foundries AG v Plessey* [2014] EWHC 3190 (QB), it appeared a NoI was filed to allow the company to complete orders, and maximise debtor payments, safe from enforcement of a possession order by the owners of rented factory equipment central to the ongoing production. Similarly, in *South Coast Construction Ltd v Iverson Road Ltd* [2017] EWHC 61 (TCC), three successive NoIs were filed seemingly to frustrate an application for summary judgment enforcing the decision of an adjudicator pursuant to a building contract, with the company entering liquidation immediately following expiry of the third NoI. In each case it was held that the moratorium would be (or would have been in the latter case) lifted to allow the claimant's case to be heard.

In light of the judgment of David Richards LJ, and the issues of improper use of NoIs raised in the abovementioned cases, if a new moratorium is to be introduced, it is crucial that careful thought is given to the framing of its purpose. Both users (companies and their management) and facilitators (insolvency practitioners) will need clear guidance on where the goalposts stand in order to avoid uncertainty and the risk of the moratorium being overturned. Alongside the statutory framing of such a process, again it may be something that a revised Insolvency Code of Ethics seeks to address.

Conclusion

The decision in *JCAM Commercial Real Estate Property XV Ltd v Davis Haulage Ltd* [2017] EWCA Civ 267 clarifies that, in order to file a NoI, the company or directors must have a settled intention to appoint an administrator, and nothing less. That is not of course to say that successive NoIs are forbidden. However, what appears to have been a common practice of filing successive NoIs to

create a prolonged pre-insolvency moratorium to allow a financially distressed company space to evaluate its options will no longer be possible.

Arguably an alternative form of protection is needed. This would protect both those companies that would otherwise have used successive NoIs as described above, but perhaps also those companies who would not have done so, having interpreted Schedule B1 in the same manner as David Richards LJ, but for whom a stay on creditor actions would be beneficial.

Questions remain as to what is the most appropriate mechanism for this. What is clear, though, is that the purpose and parameters for use of any pre-insolvency moratorium need to be clearly established. This will avoid uncertainty which could undermine the use of such a process and risk further misuse.