

## Insights

# SUPPLIER BEWARE: THE CIGA 2020

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## SUMMARY

The Corporate Insolvency and Governance Act 2020 (CIGA 2020) came into force on 26 June 2020. While intended to provide a lifeline to struggling businesses during the COVID-19 pandemic and beyond, it fits uneasily with the legislation, measures and standard terms in place to combat the construction industry's cash flow challenges. This article explains how the new rules operate and provides practical tips for suppliers and customers.

The **Corporate Insolvency and Governance Act 2020** (CIGA 2020) came into force on 26 June 2020 after a fast-tracked consultation process. Intended to provide a lifeline to struggling businesses during the COVID-19 pandemic and beyond, it consists of temporary measures, meant to alleviate the short-term disruption caused by the pandemic and permanent measures, which are more broadly designed to assist companies in times of difficulty.

But while it may sit more comfortably with “traditional” contracts for the supply of goods and services, it pushes against the legislation, measures and standard terms that have evolved to combat the inherent cash flow challenges present in the construction industry and protect supply chains.

The CIGA 2020 not only has a significant impact on the **Construction Act 1996** but also requires updates to construction standard forms such as the JCT and NEC (explored further in this post and in **Practical Law's practice note on the CIGA 2020**). These changes demand that parties upskill on what the new rules entail at a time when (arguably) they may have more pressing concerns.

This blog post focuses on the CIGA 2020's permanent provisions intended to protect the supplies of goods and services. It starts with a quick recap of the key provisions and then provides some practical tips to help affected parties navigate the new rules.

## The CIGA 2020 – what does it do? A quick recap

Section 14 of the CIGA 2020 introduces a new *section 233B* to the Insolvency Act 1986, which provides that in a contract for the supply of goods or services (so a typical construction contract):

- Any provision that would otherwise terminate or give the supplier (contractors, consultants and sub-contractors and so on) the right to terminate, as a result of the customer (the party immediately above them in the supply chain) being subject to relevant insolvency procedures, ceases to have effect.
- Any provision that provides for “any other thing” to take place, or gives the supplier the right to do “any other thing” as a result of the customer being subject to relevant insolvency procedures, ceases to have effect.
- Upon the commencement of a relevant insolvency procedure, a supplier is prevented from terminating for any reason if the right to terminate arose, but was not utilised, before the customer entered into the relevant insolvency procedure.
- Upon the commencement of a relevant insolvency procedure, a supplier is prohibited from making the continued supply of goods and services conditional upon the payment of outstanding charges relating to a supply made before the commencement of such insolvency procedure.

If the circumstances above apply, and depending on the insolvency procedure in question, termination may only occur if one of the following occurs:

- The insolvency practitioner consents.
- The customer consents.
- A court is satisfied that non-termination would cause the supplier “hardship” and grants permission to terminate.

### **When do these restrictions apply?**

A “relevant insolvency procedure” is defined in s233B(2) of the Insolvency Act 1986. It includes the **new moratorium established by the CIGA 2020**, administration, the appointment of an administrative receiver, the approval of a CVA, liquidation, the appointment of a liquidator and a court order made under section 901C(1) of the Companies Act 2005 in relation to the company.

It is important to note that the CIGA 2020 does not:

- Prevent a party higher up in the supply chain from exercising its contractual right to terminate. Therefore a contractual provision entitling an employer to terminate for contractor insolvency would still be valid.

- Prevent the supplier from terminating for other reasons, such as, non-payment **provided that such right to terminate has arisen following the commencement of insolvency procedures**. This would include a termination at will clause, although construction contracts for works rarely allow contractors to terminate the contract at will.

A question mark remains over the extent to which the CIGA 2020 overrides section 112 of the Construction Act 1996, which provides the supplier with the statutory right to suspend for non-payment (further explored in **Practical Law's material**).

## Some practical tips

Suppliers and customers:

- Depending on the wording of the contract, definitions of “insolvency” may require updating to take account of the new moratorium and the new restructuring plan (for example, see **Practical Law's amendments to clause 8.1 of the JCT Design and Build Contract, 2016 Edition**).
- Keep “termination on insolvency” type clauses. A customer's right to terminate for supplier insolvency is unaffected by the CIGA 2020 and retaining such a clause for suppliers gives suppliers the option of applying to court for permission to terminate due to “hardship”.

Customers:

- Upon entering an insolvency procedure, be careful to ensure you do not give the supplier a fresh right to terminate by, for example, failing to pay any invoices that are payable after the commencement of a relevant insolvency procedure.
- Suppliers are likely to be monitoring customers for signs of financial distress and may exercise any right to terminate sooner than they otherwise would have. Be conscious of the increased risk of termination and take steps to mitigate the risk.

Suppliers:

- If you are aware that your customer is in **financial difficulty**, consider exercising pre-existing rights to terminate (if any have been triggered) before they are suspended by the customer entering into a relevant insolvency procedure. Alternatively, consider renegotiating the contract to provide for alternative protections such as further guarantees, advance payments or shorter invoicing periods.
- Ensure that rights to terminate for non-payment are in place. Consider these clauses carefully to ensure that you are able to cease supply quickly if payments are not forthcoming.
- Before terminating, ensure that you are within your rights to do so. If you terminate for customer insolvency in ignorance of the prohibition in the CIGA 2020, this may result in claims

being made against you for wrongful termination and repudiation of the contract leading to unintended (and very costly) consequences.

- Ensure your customer has provided any security that the contract requires it to procure. Your ability to terminate the contract for failure to provide such security (if the contract provides that right) may be lost upon commencement of a relevant insolvency procedure unless you are able to successfully argue that the continuing failure to provide security gives rise to a fresh right to terminate.
- It is likely that the right to terminate is suspended in relation to outstanding amounts that became payable after the relevant insolvency procedure commenced, but which relate to the provision of goods or services **before** the commencement of such procedure. This is because section 233B(7) prevents a supplier from doing anything which makes it a condition of supply that any outstanding charges “**in respect of a supply** made to the company before that time are paid”. It is risky to terminate in these circumstances given the risk of being met with a claim for wrongful termination.

## Final thoughts

While the CIGA 2020 is aimed at maximising a customer’s chance of survival, the provisions discussed above are likely to cause concern among construction industry suppliers given the cash flow issues that already plague the industry.

Aside from the protective measures suggested in this post, it may be of some comfort to suppliers that, in relation to the supply of goods or services made during an administration or liquidation, they will rank ahead of most other creditors, making it more likely that they will be paid for such supplies eventually. The impact of these provisions may also be further limited by the courts’ interpretation of supplier “hardship” and how willing they are to grant suppliers permission to terminate.

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This [article](#) first appeared on the Practical Law Construction blog dated 12 August 2020.

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