
# Administration in Guernsey

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As Guernsey companies, like their international counterparts, fight to manage the COVID-19 crisis with differing levels of state support, much has been reported about potential changes to the insolvency framework available to bolster survival measures.

While Guernsey continues to consider what changes might benefit local companies, it is worth bearing in mind that the island already offers a restructuring regime that, if used correctly, can support the rescue and survival of businesses via a moratorium and light-touch intervention. That is a rarity in the offshore world, and is explored in further detail below.

## What is light touch administration?

The measures taken by governments around the world to slow the spread of COVID-19 have seriously impacted the cash flow of many companies. With an income stream reduced or disappearing overnight but costs remaining constant, the boards of companies can quickly find the company fails the solvency test.

Looking for forbearance from creditors and cutting costs is a priority. Furloughing employees (if possible) and, for example, agreeing a rent-free period may be of great assistance. However, forbearance may not be forthcoming from all creditors and/or these measures alone may not be enough to stave off the threat of collapse for a business that otherwise has long term viability.

Long term viability is, of course, a key factor. Making a prediction as to future viability is very difficult for boards at present. The level of uncertainty around the length of time measures will last is an important factor. Equally, the damage to consumer confidence and possible behavioural change driven by the measures may affect future revenue.

However, some businesses will remain viable as matters improve. It is those businesses that must be identified and may take advantage of the formal insolvency tools available to work towards that long term viability.

Whilst legal advisors and insolvency practitioners have a role to play, in a successful trading business, the incumbent management are best placed to understand its needs. If there is faith in management, the business can be wrapped in the protection of an administration order with management being allowed to continue their role (including some trading) with the light touch oversight of a Court appointed administrator.

The process requires faith between the administrator and the directors and will require formalisation. Readers are encouraged to review the suggested protocol for that relationship that can be found here.

This approach allows companies to minimise the costs of administration by working with current management. That is not to say that powers are or should be delegated from administrator to directors, but that the administrator rather consents to directors retaining some of their powers to permit them to participate in the continued running of the business.

This is a model that can easily be instigated for a Guernsey registered company and which not only can be deployed in aid of trading businesses. With thought, and the right level of engagement with the office holder, this approach could easily be adapted to assist financial services businesses and funds.

## How does Guernsey's administration regime work?

Guernsey introduced its administration regime within the Companies (Guernsey) Law 2008, as amended (the **2008 Law**). Substantive detail on the procedure can be found here.

However, it is the following features of Guernsey's regime which are particularly well suited to the now much-touted light touch approach:

- Speed and ease of commencement

Whilst there is no out-of-Court route to appoint an administrator in Guernsey, the Court driven process can deliver a time effective result when urgency requires it. Notably, the moratorium afforded by Guernsey administration is effective from the date an application is filed with the Court. Typically, that filing will occur on a Thursday of the week preceding a Tuesday sitting of the dedicated Commercial Court. Subject to the requisite notices having been given and the level of any opposition it is quite possible for the administration order to be granted at that hearing, *i.e.* with a delay of only 3 working days between application and order. During that time, the moratorium is already in place.

- Focus on rescue

The starting point of the administration process is corporate rescue. An order may only be granted for the purposes of the survival of the company as a going concern or the better realisation of assets than would be effected on a winding up.

The powers afforded to the administrator are extremely broad and flexible including a power to undertake any action that furthers the purpose of the administration. Entering into the light touch protocol to allow a business to continue with its existing management but under the wrapper of the moratorium falls within those powers.

- Flexibility of regime

Guernsey's statutory provisions on administration are few but that is no disadvantage in the current circumstances. There is less formal reporting required than in other jurisdictions and a reduced burden in terms of meetings. That suits the light touch intervention approach.

However, the lack of formal provisions has not limited the effectiveness of the regime.  The island's role as an international finance centre means that its Courts have experience in dealing with complex issues, and its lean legislative framework affords the opportunity for creative, nimble solutions. On multiple occasions, experienced advisors coupled with a commercially sensible Royal Court have been able to find solutions not written in statute by means of creativity and flexibility.

Recent examples include use of the process to deal with a multi-national construction business, the investment arm of a major philatelic trader, a significant care home group and others.

The system has also been flexed to allow a pre-packaged sale (under which the sale of all or part of an insolvent company's business or assets is negotiated by the directors with a purchaser prior to the appointment of an administrator or liquidator). Despite some negative connotations, this type of sale used in the right circumstances, with correct checks and balances, can be a vital tool for rescuing businesses.

- Availability of schemes of arrangement

Guernsey companies can, in broadly the same ways as English companies, use schemes of arrangement to compromise creditors. This may be a valuable option at the end of an administration process to compromise the claims of creditors or a class of them.

## What areas require caution or improvement?

Whilst Guernsey is extremely well placed in the offshore market for dealing with restructuring, there are points for practitioners and directors to be aware of.

- Limits on moratorium

The significant difference between an English administration and one in Guernsey is the extent of the moratorium. Guernsey remains an important jurisdiction for financing transactions and has always strived to be creditor friendly in that regard. Guernsey's regime does not offer a moratorium against the claims of secured creditors.

However, our experience suggests that this carve out does not undermine the regime. Often the secured creditor is a key stakeholder who ought to be engaged early in any distressed situation. If that creditor understands what is proposed and has faith in the management and office holder. Early engagement is the key here.

- No out of court appointment

There is no option to commence an administration without Court involvement in Guernsey. Again, the rationale is partly driven by protection of secured creditors. However, the speed with which a Court application can be deployed (as set out above) compensates for the lack of out-of-Court appointments.

- Risks to boards

The position of boards of companies in distressed situations is complex and beyond the scope of this note. Further thoughts can be found both here and here.

However, in the context of corporate rescue in the current climate, focus is thrown on future viability. Directors face an unenviable task of making decisions on an uncertain future without the benefit of clarity as to how long the current measures will last.

A fear for directors is to trade on with false hope of a business recovering. Whilst taking advice and involving professionals in the decision making will reduce risk, directors may feel under pressure to fund short term liquidity through borrowing. That borrowing may require the provision of personal guarantees by business owners. Lenders, advisors and directors must be mindful of not creating a wave of personal insolvency issues down the line in false hope of business recovery.

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- Availibility of state support

The support available to local businesses is discussed here. At present, no support is offered to financial services businesses despite the vital role they play in the Guernsey economy. More importantly, it is not clear whether any future support decided upon would be available to a business in administration, i.e. whether the administrator could, for example, use the furlough scheme. This firm continues to support the States of Guernsey in its decision making and has raised these issues.

## Are further changes to the regime needed or likely?

Many jurisdictions around the world have made temporary changes to their insolvency and other legislation in response to the distress arising. To date, the States of Guernsey has chosen not to do so albeit it has received a number of suggestions in that regard. A number of the higher profile suggestions from elsewhere are considered below in the Guernsey context:

- Relaxation of rules on wrongful trading

The potential for personal liability for wrongful trading is often a key concern of directors of companies facing financial difficulties.

Under Guernsey law, a director can incur personal liability for wrongful trading if he "*knew or ought to have concluded that there was no reasonable prospect of the company avoiding going into insolvent liquidation*", unless he took every step with a view to minimising the potential loss to a company's creditors.

It could be said that, with robust advice, boards should not be worried about this risk if their difficulties spring from the COVID-19 crisis and they hold a genuine belief that when matters improve, the company will survive. But, as set out above, decision-making will be difficult with the crisis unfolding in ways that no one can fully predict.

One view is that, if the law on wrongful trading were relaxed temporarily, it would help to remove uncertainty and the need for boards to seek expensive advice on their position before accepting support, in turn removing a perceived barrier to accessing emergency financing for many companies that could prove vital to their survival.

However, wrongful trading alone is not the only issue. Directors will still owe duties to the company including primarily to act in its best interests. When insolvency becomes a possibility, predominant regard must be given to the interests of creditors. Equally, directors may be asked to give personal guarantees for lending or take credit on themselves to lend money to their businesses. Any decision to trade on and take new financing must encompass all considerations and not just wrongful trading.

- Increase of statutory demand threshold

Currently in Guernsey, where a statutory demand of more than £750 has been formally served on a company by HM Sergeant and it remains outstanding for 21 days, the company will be deemed to be insolvent and liable to compulsory winding-up.

But as has been discussed, collective forbearance seems key if businesses are to successfully negotiate the current crisis. In recognition of this, Australia has amended its statutory demand procedure. In that jurisdiction, the monetary threshold has been increased to 20,000 dollars and the time limit for payment extended to 6 months.

A similar change in Guernsey would be relatively easy, yet very effective in encouraging forbearance for smaller businesses and removing some of the threat of imminent insolvency. An increase in threshold would not, however, denude significant creditors of seeking recourse in appropriate situations subject always to the Court's final discretion.

- A debtor in possession moratorium

It is sometimes said that the American insolvency and restructuring framework of Chapter 11 is culturally and legislatively more geared towards business continuity than its counterparts across the Atlantic.

England & Wales is moving to introduce a procedure whereby a moratorium is granted to a business that leaves management in control without intervention from the Court or an office holder.

The advantages for significant trading businesses of the system are clear especially in the current circumstances. However, the nature of Guernsey's economy and its position as a financial centre mean that the introduction of such a procedure here is extremely unlikely.

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