**Section 233B of the Insolvency Act 1986: Implications for suppliers and debtor companies**

**Introduction**

For over twenty years, section 233 of the Insolvency Act 1986 (“IA 1986”) has restricted the contractual freedom of parties, but only in the context of a narrow range of contracts for the supply of utilities such as gas, water and electricity when a company enters into a specified insolvency process. In 2015, further restrictions to the enforcement of insolvency related contract terms were introduced, though again only with regard to this narrow range of contracts. The new section 233B IA 1986, by contrast, is far broader in scope and puts a significant dent in the ability of parties to enforce and vary contractual terms. This article considers the implications of the new provision, which entered into force on 26 June 2020.

**The key restrictions**

The most significant elements of section 233B IA 1986, introduced as part of the Corporate Insolvency and Governance Act 2020 (“CIGA 2020”), apply where a company becomes subject to a ‘relevant insolvency procedure’ (defined broadly in section 233B(2)), and are as follows:

*‘(3) A provision of a contract for the supply of goods or services to the company ceases to have effect when the company becomes subject to the relevant insolvency procedure if and to the extent that, under the provision-*

*(a) the contract or the supply would terminate, or any other thing would take place, because the company becomes subject to the relevant insolvency procedure, or*

*(b) the supplier would be entitled to terminate the contract or the supply, or to do any other thing, because the company becomes subject to the relevant insolvency procedure.*

*(4) Where-*

*(a) under a provision of a contract for the supply of goods or services to the company the supplier is entitled to terminate the contract or the supply because of an event occurring before the start of the insolvency period, and*

*(b) the entitlement arises before the start of that period,*

*The entitlement may not be exercised during that period.’*

*‘(7) The supplier shall not make it a condition of any supply of goods and services after the time when the company becomes subject to the relevant insolvency procedure, or do anything which has the effect of making it a condition of such a supply, that any outstanding charges in respect of a supply made to the company before that time are paid.’*

It is clear that the restrictions imposed on suppliers are far-reaching, in particular:

1. Section 233B(3) precludes reliance on standard insolvency termination provisions, whether or not they apply automatically.
2. The wording of section 233B(3), specifically ‘*any other thing would take place* and ‘*do any other thing’*  is deliberately broad and could apply to a range of contractually agreed contingent provisions, for example changing payment terms.
3. Section 233B(4) extends the restrictions to contractual rights triggered before the company enters the relevant insolvency procedure (the explanatory notes make it clear that the restriction will not apply where the event in question, e.g. non-payment, occurs after the company enters the relevant insolvency procedure).
4. The wording of ‘*an event’* in section 233B(4) is potentially broad in scope and not specifically defined. An obvious application would be to a contractual provision providing a right to terminate the contract or supply in the event of non-payment: if for example payment was due on 1 April and the right to terminate accrued on 2 April after payment was not made, a supplier would not be entitled to exercise the right on 5 April if the company entered a relevant insolvency procedure on 4 April. However, it could potentially extend further, for example to a contractual provision allowing for termination of the contract or supply on 30 days’ notice in writing. It seems that such a provision could conceivably (though perhaps improbably) also be caught if the giving of the notice constituted ‘*an event*’ and the company entered a relevant insolvency procedure before the 30-day period expired.
5. Section 233B(7) prevents a supplier from demanding outstanding sums that were owing before the company entered the relevant insolvency procedure.

Aside from these implications arising from the text of the statute, it is also worth noting that the Explanatory Notes state that ‘*Where an event has occurred that would have allowed a supplier to terminate a supply contract before the company entered a relevant insolvency procedure but that right has not been exercised, it is suspended once the company enters the relevant insolvency procedure’*. This suggests the intention is that section 233B(4) acts to prevent a supplier taking advantage of a common law right to terminate resulting from a company’s repudiatory breach as well as rights arising pursuant to provisions agreed between the parties.

This would seem to be a point of divergence between the statute and Explanatory Notes, as the former is specifically confined to an entitlement resulting ‘*under* *a provision of a contract’*. It seems unlikely that a court would consider that, as a matter of statutory interpretation, the wording of section 233B(4) extended that far.

**Avoiding the effect of the restrictions**

Unless an exclusion applies (as to which see schedule 4ZZA), if either of the restrictions in section 223B(3) or (4) is triggered, a supplier’s freedom of contract will be restricted as specified for the duration of the insolvency procedure, unless it can avail itself of section 233B(5):

‘*(5) Where a provision of a contract ceases to have effect under subsection (3) or an entitlement under a provision of a contract is not exercisable under subsection (4), the supplier may terminate the contract if-*

*(a) in a case where the company has become subject to a relevant insolvency procedure as specified in subsection (2)(b), (c), (e) or (f), the office-holder consents to the termination of the contract,*

*(b) in any other case, the company consents to the termination of the contract, or*

*(c) the court is satisfied that the continuation of the contract would cause the supplier hardship and grants permission for the termination of the contract*.’

As yet, there do not appear to be any reported cases addressing section 233B. In many cases the consent of the company or the relevant office holder might not be forthcoming, so suppliers will need to make applications under section 233B(5). The key issue in any application is likely to be the need to satisfy the court as to the likelihood of hardship. In reality, the best way of doing this will be to provide evidence of the detrimental financial impact that would likely result from continuation. For larger suppliers, this might well be difficult given the use of the word ‘hardship’, which is indicative of something more significant than simply demonstrating a weaker financial position than would have been the case had the company performed its side of the contract.

Note that until 30 September 2020, suppliers which are ‘small entities’ are temporarily excluded from the effect of section 233B. This exclusion is set out in section 15 of the 2020 Act and suppliers must meet conditions in order for it apply.

**Conclusion**

For companies dealing with suppliers in the context of the supply of goods and services, these provisions offer additional respite when they enter financial difficulty, and as part of the range of measures brought into effect via CIGA 2020, they are likely to have a positive impact on the economy.

However, there is no doubt that a large number of suppliers are likely to be caught by these provisions, and while large organisations might not suffer a significant impact, for small organisations or those who place significant reliance on relatively large contracts with companies who enter a relevant insolvency procedure (which includes the new moratorium process and an order in relation to the new restructuring process, both introduced via CIGA 2020), the provisions could cause significant financial hardship. At lot is likely to turn on the approach taken by the courts to applications under section 233B(5)(c): clearly a balanced approach will be required.

For those suppliers with existing contracts, if they wish to invoke contractual provisions they will need to be proactive in ensuring steps are taken before the restrictions in section 233B are triggered. For those who are entering into contracts, the best approach might well be to try to avoid reliance on a small number of large contracts with suppliers and to ensure that contracts are drafted with the provisions in mind, for example by operating for only a limited duration or being limited to one good or service.

**Nathan Webb**

Forum Chambers

nwebb@forumchambers.com

THIS ARTICLE IS NOT INTENDED AS AND SHOULD NOT BE TAKEN AS CONSTITUTING LEGAL ADVICE. Members of Forum Chambers advise regularly in relation to insolvency matters and if we can be of any assistance, please to get in touch with us on 0203 735 8070 or clerks@forumchambers.com