

Insolvency - being smart and staying ahead of the game

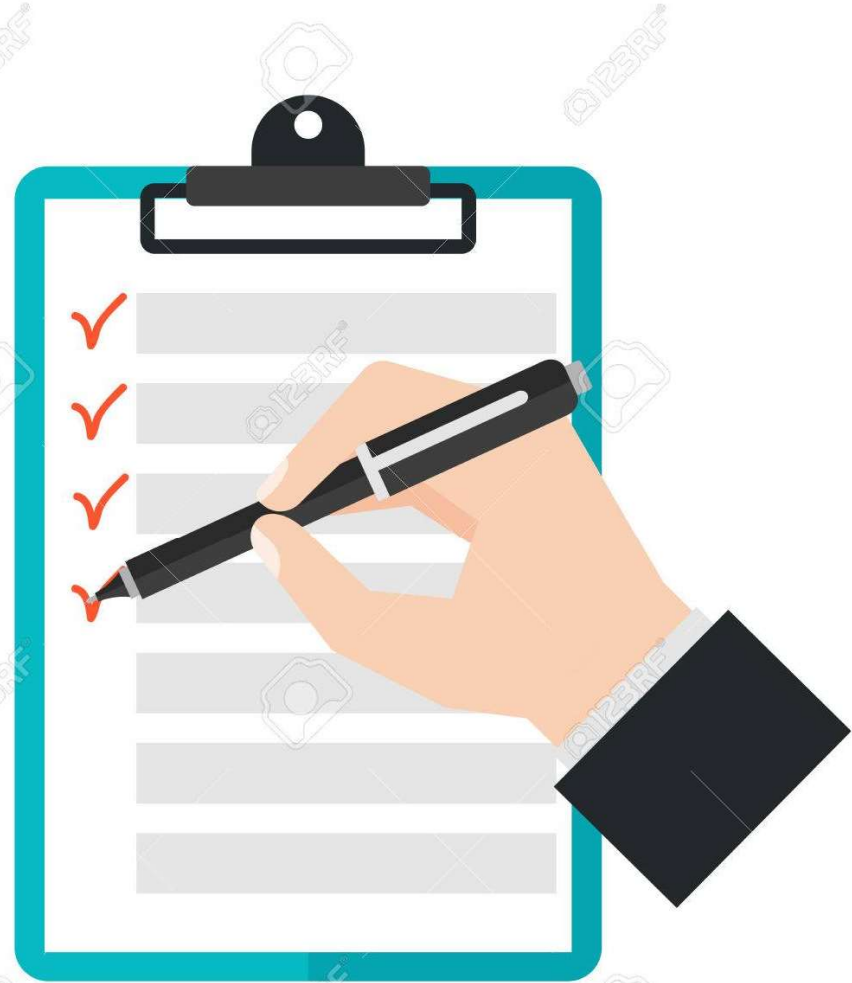
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Agenda

- Directors' duties and liabilities
- Company Voluntary Arrangements
- Administration
- Members Voluntary Liquidation
- Creditors Voluntary Liquidation / Compulsory Liquidation
- Personal insolvency
- Debt recovery



Directors' Duties

- Companies Act 2006 – codifies most duties imposed on directors
- Directors' duties generally apply to all directors, i.e. shadow and non-executive directors (as well as ordinary directors)
- One of the seven 'general duties' is:

“the duty to promote the success of the company for the benefit of its members as a whole”

- BUT: when a company becomes financially distressed, and it becomes likely a company will enter a formal insolvency procedure, the above is replaced with:

“the duty to act in the interests of creditors as a whole (i.e. to preserve the value in the company in order to maximise return to creditors)”

Warning Signs

- Turning point – when it is apparent that a company cannot avoid insolvent liquidation or administration
- Company unable to pay its debts as and when due (cash-flow test)
- Company's liabilities outweigh its assets
- Creditor taking steps to enforce its rights against the company
- Company unable to satisfy or secure a debt within 21 days of receipt of a Statutory Demand.



Directors' Liabilities

- Failure to act in the interests of creditors as a whole could lead to claims against directors for:
 - ❖ Misfeasance
 - ❖ Fraudulent trading
 - ❖ Wrongful trading
 - ❖ Voidable transactions (transactions at an undervalue, preferences, extortionate credit transactions, transactions defrauding creditors)
- Potential consequences:
 - ❖ Repaying monies
 - ❖ Returning property
 - ❖ Paying compensation
 - ❖ Imprisonment (up to 10 years for fraudulent trading)
 - ❖ Disqualification (2-15 years)
- Some claims can be brought against other members of a company and / or third parties

Steps to take when a company is in financial distress

- Instruct company's accountants to report on current position (to help determine if insolvency can be avoided)
- Raise concerns about insolvency at board meetings and ensure that concerns are recorded in minutes
- Take legal advice on responsibilities and proposed transactions
- Consult insolvency practitioner to review recovery options
- Enforce effective credit control
- Keep banks and major creditors informed
- (With advice) consider alternative methods of raising finance if bank unwilling to extend existing facilities
- Commencing insolvency proceedings in a timely fashion

Company Voluntary Arrangements (CVA)

- Contractual arrangement between a company and its creditors
- Recovery option!
- Advantages:
 - ❖ No need to prove insolvency – can be entered into at early signs of distress
 - ❖ Can be approved if 75% in value of creditors vote in favour (and not opposed by 50% of independent creditors)
 - ❖ Binds creditors unaware of proposals





CVAs continued...

- Moratorium:
 - Prevents new proceedings being brought against a company and existing proceedings continuing
 - Affords a company breathing space
 - Runs during the time a CVA is being negotiated
 - Only available to small companies
 - Not automatic – application required
- Considering a CVA? ...consult an Insolvency Practitioner
- NOTE: if you are a creditor being asked to consider signing up to a CVA, carefully consider terms

Administration

- Designed to give a company breathing space, to allow either rescue or restructure
- Must be likely to:
 - ❖ Rescue company as a going concern;
 - ❖ Achieve a better result for a company than if it were wound up, or;
 - ❖ Realise property in order to make a distribution to creditors
- Moratorium:
 - Prevents new proceedings being brought against a company and existing proceedings continuing
 - Affords a company breathing space
 - Automatic!
 - Applies throughout period of administration
 - Interim moratorium can apply prior to entering into administration

Members Voluntary Liquidation (MVL)

- Procedure by which members can wind up a company and move to dissolution
 - Company must be solvent
 - Typically used when a company has served its purposes and members no longer wish to retain it as a corporate entity
 - Also a way for members to recover their investments in a company in a tax efficient manner
- MVL vs strike off:
 - ❖ Further actions against a company post an MVL can only be brought within 6 years of dissolution (no limit in strike off)
 - ❖ MVL puts timing in the hands of shareholders (strike off can be at any time)
 - ❖ MVL provides greater protection for shareholders / directors
 - ❖ Strike off is not available within 3 months of change of name, trading or sale of company property
 - ❖ Strike off is cheaper and may be more appropriate if the company is dormant or has never traded

Other Corporate Insolvency Procedures

Creditors Voluntary Liquidation

- Procedure used to wind up a company when the company is insolvent
- Voluntary process instigated by meeting of a board of directors
- Directors can appoint their choice of Liquidator
- Alternative to being wound up by the Court on petition of a creditor

Compulsory Liquidation

- Procedure where a company is wound up following an order of the court
- Typically follows petition to the court made by a creditor
- Company has no control whatsoever

Personal Insolvency

Bankruptcy

- An individual can be declared bankrupt upon a personal application or petition of a creditor
- A bankrupt cannot act as the director of a company
- A bankrupt cannot obtain credit above £500.00
- Consider effect of becoming bankrupt if running business as a sole trader

Individual Voluntary Arrangement (IVA)

- Contractual arrangement between individual and creditors
- Alternative to bankruptcy
- Can include terms to compromise all unsecured creditors' claims and prevent unsecured creditors from enforcing claims
- No automatic moratorium, although terms can be included to this effect

Debt Recovery

- If your company is owed a debt, this could be recovered by:
 - ❖ Sending a letter before action to the relevant company or individual
 - ❖ Personally serving the relevant company or individual with a Statutory Demand
 - ❖ Bringing insolvency proceedings against the relevant company or individual
 - ❖ Recovering the debt within winding up proceedings (company) or bankruptcy proceedings (individual)
- Debtors are often encouraged to pay upon receipt of a letter before action or a Statutory Demand, negating further action
- It can take a number of years to realise monies within insolvency procedures
- Could only recover a percentage of the debt (or nothing at all)

When to seek advice

- If your company is in financial distress and you need advice about:
 - Directors' duties
 - Proposed transactions
 - Entering into an insolvency procedure
- If your company is in receipt of a statutory demand, winding up petition or winding up order
- If you (as an individual) are in receipt of a statutory demand, a bankruptcy petition or a bankruptcy order
- If you or your company want to recover debt
- As soon as possible!



Summary

- Directors duties - if you are a director and your company is insolvent or on the brink of insolvency, your duty is to act in the best interest of the creditors and failure to observe this duty could lead to claims against you.
- CVAs / Administration – potential rescue options.
- Members voluntary Liquidation – way for members to dissolve company and recover investments in a tax efficient manner.
- Creditors Voluntary Liquidation – way for directors to retain some control over liquidation (i.e. to avoid Compulsory Liquidation).
- Bankruptcy / IVAs – bankruptcy could be detrimental to running a business, IVA could be an alternative.
- Debt recovery – insolvency procedures can be used to recover debt owed to your company.



Any Questions?

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