Common Starting Points

- Failing UK business.
- Proposed withdrawal from UK market following unsuccessful operations of an international group.
- Proposed solvent restructure involving corporates incorporated in the UK.

Common Questions Raised by Corporations Facing These Difficulties

- What options are available?
- How much will it cost?
- How long will the process take?

The UK's insolvency regime provides a wide range of ways to undo business in either solvent, distressed or insolvent scenarios.

The scope of this note will focus on companies limited by shares incorporated in the UK and trading as a going concern and the various paths to dissolution. Broadly speaking, the same processes apply to other corporates (such as partnerships or companies limited by guarantee) or non-trading holding companies, however advice should be sought in relation to these.

In the UK, companies are incorporated under the Companies Act 2006 and registered at Companies House - a public register containing the details of every company incorporated in the jurisdiction. Companies House identifies each company's registered office address, director(s), beneficial owner(s) and registrable security granted, among other details. When companies are incorporated, they are added to the register of companies. When they are "closed" they are struck-off the register and dissolved. Any assets owned by the company at the time of dissolution pass to the Crown and the company is extinguished as a separate legal personality. However, this is not necessarily final as the Companies Act provides for companies to be restored to the register after dissolution; effectively reviving the company.

Overview

English insolvencies are not "debtor in possession" processes. In most formal insolvency processes, an Insolvency Practitioner - specialist accountants licensed and regulated by an insolvency regulatory body - is appointed over the insolvent company (the administrator or liquidator) and manages all aspects of the business and assets of the company, effectively replacing the directors. The shareholders' position is similar in that they lose control over the company to the Insolvency Practitioner and, as the entry into an insolvency process typically renders their stake worthless, therefore play a passive role in the process.

Insolvency Practitioners owe their duties not to the shareholders, but to the creditors as a whole. Therefore insolvency processes are driven solely by the aim of maximising returns to creditors.

In administration, and liquidation, the money realised from the assets of an insolvent company is applied to meet the claims of creditors in a specified order of priority. Generally, when one class of creditor claim has been repaid in full, the remaining realisations are applied to the next class. The order of priority is as follows:

(a) holders of fixed charges and creditors with a proprietary interest in assets are discharged as far as possible from the realisations of those assets;

(b) expenses of the insolvent estate (in a set order);

(c) preferential creditors;

(d) prescribed part to unsecured creditors;

(e) holders of floating charges (that is, charges which were created as floating charges, irrespective of intervening crystallisation);

(f) unsecured creditors; and

(g) shareholders.

(h) In administration and liquidation the office holder pays the expenses of the insolvent estate and remuneration before paying any other claims (though assets which are subject to security which was created as fixed charge security remain available first for the benefit of the secured creditor and not for payment of expenses or remuneration until such secured claims are paid in full). There is a statutory priority in which the office holder pays expenses in respect of administration and liquidation respectively. Key points of the priority of expenses include:

  – expenses incurred in the course of trading an insolvent company or preserving the assets rank ahead of the remuneration of the office holder;

  – in administration, if the administrator does not dismiss an employee within 14 days of the insolvency date, the company's liability to pay wages or salary to that employee rank ahead of the other expenses of the administration.

Contracts of employment will only automatically terminate in the event that there is a compulsory liquidation or court appointed receiver and, in very limited circumstances, an administrative receiver. Under the other procedures contracts of employment will remain unaffected although specific rules apply concerning the adoption of contracts by administrators and administrative receivers and the extent of their liability. Office holders do however have the right to dismiss employees but subject to UK statutory employment laws.

Solvent

Company Voluntary Arrangements

Company Voluntary Arrangements, known colloquially as CVAs, are a court-sanctioned mechanism by which companies can compromise their debts with creditors, allowing the debtor company a chance to recover financially whilst providing its creditors with a better outcome than if they forced the company into insolvency. CVAs have received much media attention recently, with several high profile struggling High Street brands using them to re-structure the liabilities they owed to landlords of stores.

A company does not need to demonstrate that it is, or is likely to become, insolvent though in practice it usually is: a CVA is a proposal to the company and its creditors whereby if approved, debts may be compromised or their terms changed promising a return to creditors which is usually shown to be much more favourable that if the company entered liquidation. CVAs can be proposed by the company's directors or by an administrator or liquidator where the company is already in administration or liquidation.

A CVA is commenced by convening meetings of shareholders and creditors (separate meetings). Papers must be prepared and sent convening the meetings. A CVA comes into force when the company's creditors approve a CVA proposal. The company's shareholders can approve the proposals by a simple majority in value, although if they do not approve the proposals and the creditors do, the CVA will still be implemented. The approval of a CVA (or any modification to the proposal) by a creditors' meeting requires a majority of 75% (by value) of the creditors attending the meeting (in person or by proxy) to vote in favour of it. There is also a condition that at least 50% (by value) of the creditors that vote in favour of the CVA are unconnected with the company. The CVA process is public and papers relating to it will be available through various channels.

Under a CVA, the CVA is monitored and supervised by a "supervisor" who must be a licensed insolvency practitioner. The terms of the CVA usually allow the directors to remain in control of the day to day running of the business.

If successful, the CVA is concluded in accordance with its terms and the company reverts to its former status. If unsuccessful, the CVA will terminate with the company entering an insolvent process.

Members' Voluntary Liquidation

Members' Voluntary liquidation (or MVL) is the only solvent formal insolvency process. It is initiated by the shareholders of a company passing a special resolution (75% for carriage). The company must be able to pay its debts in full, together with interest, within 12 months of the start date of the MVL and a majority of the directors must swear a statutory declaration to that effect.

An Insolvency Practitioner is appointed as liquidator and carries out investigations into the company's affairs and fulfils certain statutory requirements. In the event that the company does have the funds to settle all outstanding liabilities, the liquidator will use the company's funds to pay these and distribute all remaining assets to the shareholders. The liquidator will then proceed to dissolve the company. In the event that the directors' statutory declaration of solvency is incorrect and additional creditors are identified that cause the company to be insolvent on a balance-sheet basis, the liquidator will convert the MVL into a creditor's voluntary liquidation.

There is no prescribed time period for a MVL and the duration of the liquidation will depend on the complexity of the company's estate. The cost of the liquidation is invariably connected to the length of the investigation and the charge-out rates of the Insolvency Practitioner and their employees.

Voluntary Strike-off

Companies can apply to Companies House for strike-off from the register of companies and subsequent dissolution. For the application to be made, the company must not have carried on any business for the preceding three months. The definition of "any business" is very wide and essentially captures any act of the company that is not necessary for the purpose of making the strike-off application. It is an offence for the directors of a company to make the application if the company has performed any actions in the previous three months.

The advantages of the voluntary strike-off process is that it is quick (generally between 3-6 months from application to dissolution) and cheap (the application comprises a brief form sent to Companies House). However, any assets left in the dissolved company automatically vest in the Crown's estate and will require a court application, and the associated costs, to reclaim ownership. Additionally, this method of dissolution does not involve any investigations by an Insolvency Practitioner into the affairs of the company and potentially fails to address any outstanding issues the company may have.

Insolvent

Receivership

The appointment of an administrative or fixed charge receiver is subject to the enforcement provisions contained in the relevant security documents. Administrative and fixed charge receivers are appointed by the holders of a floating or fixed charge (as the case may be) after an event of default has occurred. "Fixed charge" or "LPA (Law of Property Act) receivership is a self-help remedy available to holders of fixed charges over specific assets and is not a collective insolvency process.

Administrative receivership (where available) is a collective process and is regulated within the Insolvency Act 1986. It is only available to holders to security which includes fixed and floating charges over all or substantially all of the assets of a company and is only available in respect of such charges where they were created before 15 September 2003 or in very limited other circumstances. Administrative receivership is now extremely rare in practice as most chargeholders, even those who have a charge old enough to qualify, would still usually appoint administrators.

An administrative receiver manages and controls the affairs of the company to the exclusion of the directors. LPA/fixed charge receivers neither manage nor control the company but are appointed over, usually, a real estate asset which they will have power to deal with.

There is no time limit, but an administrative receiver usually seeks to realise and distribute assets as quickly as possible.

Once a sale has occurred and the administrative receiver has accounted to the secured creditor for the proceeds of sale (net of costs), control of the company is returned to the directors for either continued trading or liquidation. An LPA or fixed charge receiver will have sold the asset that he or she was appointed over and there is nothing to hand back.

Administration

Administration is a (relatively) recent addition to the UK's insolvency regime. It was introduced as a "rescue mechanism" designed to give companies an opportunity to recover without creditors being able to enforce their security. This is achieved through the statutory moratorium, which prevents third parties from commencing or continuing any legal process against the company.

For an administrator to be appointed, the insolvency practitioner has to conclude that one of the three purposes of administration is achievable: (1) to rescue the company as a going concern, (2) to achieve a better result for creditors as a whole than would be likely if the company was wound up without first entering administration, or (3) the realisation of assets to make a distribution to secured creditor(s).

Administration can be commenced by way of:

- an out of court appointment by the company or its directors; or
- by the holder of a "qualifying floating charge" that meets the requirements of paragraph 14(2) of Schedule B1 (in essence an enforceable debenture containing fixed and floating charges); or
- by an application for a court order by one or more creditors of the company, the company itself or its directors.

The procedure is entered into either by applying to court for an administration order or by filing papers with the court documenting an out of court appointment.

The administrator takes over management of the affairs, business and property of the company upon appointment, to the exclusion of the company's directors.

The administration will automatically end after one year unless the administrator's term of office is extended by the court or with the consent of certain of the creditors. Creditor consent can extend the administration by up to 12 months, and can only be obtained once. Any further extensions must be requested by application to the court.

If secured creditors are likely to be paid and funds remain for a distribution to unsecured creditors the company may proceed into creditors' voluntary liquidation. Alternatively, the administrator may make a distribution with leave of the court and the administration will conclude by way of a CVA, a scheme of arrangement or a compulsory liquidation. The company may be dissolved if it has no property with which to make a distribution to creditors. In theory, if an administration is successful, the company could be handed back to its directors to continue to trade.

Liquidation

Liquidation is the terminal insolvency process in the UK. An insolvency practitioner is appointed as liquidator to realise assets and distribute to creditors in accordance with the statutory order of priority.

Voluntary liquidation is initiated by the company itself passing a special resolution (75% for carriage) at a meeting of members. There must also be a meeting of the creditors within 14 days of the special resolution at which the directors must present a full statement of the company's affairs. At the creditors' meeting, the creditors vote to appoint a liquidator. The votes are based on the value of creditors' claims. Should the creditors' choice of liquidator be different from that of the shareholders, the creditors' nomination takes precedence.

Compulsory liquidation is started by the presentation of a petition to the court by the company, its shareholders, directors or creditors. The most common ground on which creditors petition the court for a compulsory winding up order is that the company is unable to pay its debts.

The compulsory winding-up procedure is commenced by the issue of a winding-up petition (sometimes after the expiry of a statutory demand but it is not always necessary to issue a statutory demand and, if the debt is clear and undisputed, it would be unnecessary to use one). The petition must be served on the debtor company and also (within time limits) advertised in accordance with statutory requirements. The petition is heard in open court and a court order is made: at that point the company officially goes into liquidation. At that point a government official becomes liquidator. Subsequently, the official receiver may stand aside and permit a private liquidator to take over the conduct of the liquidation. Before the order is made there are two critical junctures with legal significance, namely: (a) the issue of the petition: if an order is subsequently made, any disposals after this point will be void unless ratified by a court order (section 127 IA); and (b) advertisement of the petition: after the petition is advertised it cannot be withdrawn and other creditors may claim conduct of the petition at any time up until (very shortly before) the court hearing.

Once a company enters liquidation, the liquidator controls the company.

There is no time limit in a liquidation.

The company is dissolved once the liquidator has realised all the company's assets and made distributions to creditors and shareholders as appropriate.