

Frequently asked questions – and answers of course!

The last few years have been strange to those of us who got used to the boom and bust cycle and knew where we were in the cycle simply by working out when the next general election was due to be held!

Since 1999 there has been a widespread belief (or fear) that a recession is imminent. For years directors and their professional advisors have regaled me with tales of cost cutting, downsizing, overhead reduction, margin shaving and similar euphemisms for “we’re not making any money”.

But, if one ignores the formal insolvencies of start-ups and Bankruptcies, the statistics do not reflect this mood of despair and impending doom. There is no consensus on why this might be, although factors must include better management of *potential* failure (especially by the high street banks), the glut of finance available to any entity with even a hint of a track record and the willingness of creditors to do deals in order to avoid the insolvency of their customers.

Directors also appear more open to taking early advice from their friendly local business recovery professional (read insolvency practitioner if you are older than 25). In the not so distant past an avoidable appointment with an IP was as likely as confiding in your wife’s best friend about your girlfriend’s rubber fetish.

Not any more – rubber is so early 90’s – and the gradual acceptance of insolvency as one the unavoidable risks associated with a capitalist economy seems to have heralded a sea-change in peoples perceptions. As a result many of the directors I am asked to advise are pleasantly surprised when I tell them that their problems can be managed perfectly well without the need for a formal insolvency process, often by doing deals with one or a handful of key creditors.

I do, however, get asked the same questions time and time again and these, together with my answers, are summarised below. One word of warning, however, the questions are very general and specific circumstances may alter the advice provided, so if in doubt, it’s safer to ask.

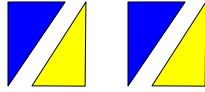
I’m not insolvent but because my debtors are having trouble paying me I am not paying my suppliers on time. Does this have any implications to me as a director?

Insolvency is defined in two ways. The balance sheet test – do liabilities exceed assets? – or as set out in Section 123 Insolvency Act 1986, basically the inability to pay debts *as they fall due*. A company is deemed to be insolvent if it fails on either basis and in such a scenario directors need to be aware of the implications of wrongful trading, by which they could lose the benefits of limited liability be made personally responsible for the company’s debts if they continue trading to the detriment of creditors.

If I stop trading how will my employees get paid?

Under the provisions of the Employment Rights Act 1996, the government protects an employee’s rights and discharges:

- Arrears of wages.
- Outstanding holiday pay.
- Pay in lieu of notice; and
- Redundancy pay



subject to maximum weekly amounts of £290.00 (from 1 February 2006). The balance of an employee's claim (if any) will rank either preferentially (arrears of wages to a maximum of £800 and outstanding holiday pay) or as an unsecured claim (pay in lieu of notice and redundancy pay).

I have heard that a CVA is a pain-free alternative to insolvency. What is it?

A Company Voluntary Arrangement is, despite its name, an insolvency process, the contents of which are detailed in the Insolvency Act and Insolvency Rules. A CVA is effectively a contract between a company and its creditors designed to maintain the survival of the company while providing a better return to creditors than they could expect to receive under any alternative process.

It does sound almost painless but the reality is often very different. The company will still be reliant on its suppliers for credit and terms may be withdrawn at the insistence of credit insurers on the implementation of an arrangement (so get any agreement in writing).

The creditors will obviously wish to maximise their return and may demand that the arrangement lasts much longer than the directors would like it to.

A significantly large creditor will also be able to effectively dictate the terms of the arrangement on a "take it or leave it" basis. In either of the last two scenarios the directors will need to carefully consider their options and whether there is any risk of the CVA failing. It would be galling to agree to an extended arrangement that fails after, say, 54 months.

Like any other procedure, in the right circumstances this is a very effective tool but it is not a "soft option" and should not be undertaken on the "we'll give it a go and see what happens" basis.

I would be profitable if I could afford to pay the redundancy of some employees and re-negotiate my lease. Is there anything I can do?

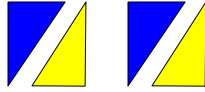
Yes there is, but only a restructuring involving an insolvency process, including a CVA. It will not be possible to isolate individual creditors or groups of creditors but if a company is losing money insolvency may be preferable sooner when the directors still have control rather than later when this control has passed to creditors. Getting initial advice will not cost anything and will determine what options are available.

Is there anything stopping me placing my company into Liquidation and starting again with a similar name?

Not a popular move with one's creditors, phoenixism (as it's known in the trade) is heavily frowned on but an unavoidable aspect of a business recovery professional's life. That pile of machinery is worth as little as they can get away paying for it to an unconnected third party but to a director, who remembers buying it, spending weekends repairing it and is feeling guilty about the loss to his creditors, it might be worth a damn sight more.

Section 214 of the Insolvency Act 1986 places a five-year restriction on the re-use of company names (or similar names) by a director following the Liquidation of a company unless certain hoops are jumped through. These include an application to court for leave to use the restricted name or notice to creditors following the purchase of goodwill from a Liquidator.

There is nothing preventing a sale of assets to a connected party as long as the provisions of Statement of Insolvency Practice 13 are followed, asset realisations are maximised (ie connected parties may need to pay a premium) and any such sale is disclosed to creditors.



I would like to buy the business of an insolvent competitor but am worried about being held liable for that company's employees. How should I proceed?

When a business or part of one is transferred to a new employer, under the provisions of the Transfer of Undertakings (Protection of Employment) Regulations 1981 the new employer maintains continuous employment of all the transferred employees' statutory employment rights.

Broadly speaking, a transfer is deemed to have been effected when a business (or part of a business) is sold or retains its identity following such a transaction. It is almost impossible to provide an example as every scenario will have its own nuances. Our usual starting point is that it is impossible to acquire part or all of a business without being responsible for the current employees and then looking at any possible mitigating circumstances.

It is worth pointing out that the Regulations are law and as such cannot be contracted out.

A purchase of assets only will not lead to the Regulations applying and such a transaction (in reality only such a transaction) can be entered into with confidence.

Stephen Goderski

Geoffrey Martin & Co was formed in 1983 by Geoffrey Martin, who was until then a partner with Arthur Andersen. It now operates from offices in Leeds and London which collectively employ 5 partners and 30 staff.

We are business recovery professionals (the new term for what used to be called insolvency practitioners). We have no audit or corporate finance arms or associations and are solely dedicated to assisting companies, partnerships or individuals with financial or cash flow difficulties.

We would welcome the opportunity of working alongside you to provide bespoke solutions to the needs of your clients. These would not necessarily be formal insolvency procedures.

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