Directors' guide

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Updated September 2024

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business rescue and insolvency

Contents

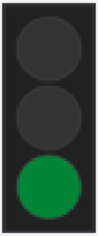
This easy-to-read guide is designed to help directors whose company is in financial distress. It will assist directors to navigate around insolvency issues and avoid potential pitfalls, split over ten sections this guide walks you through the matters in a logical order you are likely to need to consider including:

Running a company can be a lonely experience which becomes more so when it is underperforming and it cannot pay its bills. But it doesn't have to be. You don't have to face financial difficulties alone. Whatever the issue when it comes to businesses in distress we have helped directors many times before and would like the opportunity to help you too.

Early warning signs of trouble

This section covers warning signs that your company may be insolvent. Some warning signs are more obvious than others and the sooner you can identify them the better chance you'll have at resolving the issues and avoid any long-term damage to your business. Indications that something is wrong may be more obvious to others than they are to you.

Use the traffic light system below to self-diagnose your situation.



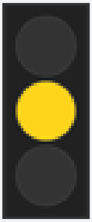
Green - go ahead but keep under review

- You are not losing money and do not need any credit.

- You can't pay creditors in accordance with normal terms but they continue to provide credit and services subject to interest charges and late payment penalties.

- You can pay current tax but you have tax arrears. You have agreed a schedule with the HM Revenue & Customs to pay off those arrears.

- You have to increase your overdraft facility or take out a new loan in order to pay your creditors near enough on time.



Amber - proceed with extreme caution

- You can't pay creditors within agreed terms. They have put you on stop but have agreed to give you longer to make proposals to pay.

- You can only get limited credit from new sources and you are using this to fend off your existing creditors.

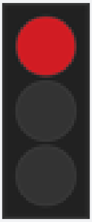
- You can't accept new orders because you can't purchase raw materials or pay for the overtime required to fulfil them.

- Your bank has decided to claw back your overdraft facility and you are missing payments to non-essential creditors.

- Your bank wants you to agree to an independent business review.

- Creditors are threatening legal action

Red - stop and seek professional advice immediately



▪ You are on stop with key suppliers, cannot raise working capital to fund your order book and turnover has dropped to below breakeven point.

▪ Your income will not meet your outgoings once interests and penalties are taken into account.

▪ County court claims, CCJs and statutory demands regularly land on your doormat.

▪ You are having sleepless nights and are on medication to steady your nerves.

▪ You have received notice of a winding up petition.

If action is taken early there is often a good chance of a successful business outcome. However, once decline sets in the chances of success become more remote and formal insolvency can end up being the only option.

When should I approach an Insolvency Practitioner?

We know from experience that most business people running an insolvent business are reluctant to talk to an Insolvency Practitioner (“IP”) for fear of immediately losing control – but that should not be the case and is certainly not how we operate.

The trigger for approaching an IP is nearly always running out of cash – typically when you can see you won’t be able to pay the wages at the end of the month but ideally sooner. You should also do so if you are thinking of injecting emergency funding or giving a personal guarantee to a supplier or funder as that money may be better deployed in a new company. Ideally if your forecasts show that your business will run out of cash you should consider making an early approach.

You might think talking to an IP is being defeatist but if you carry on trading whilst your Company is insolvent you could become personally liable for its debts and in extreme cases get disqualified from acting as a director – so it is best to be cautious.

If you do approach an IP what should happen next?

Make sure you remain in control – of course listen to what the IP has to say - but you are entitled to take your own time to make decisions – after all you know your business better than they do. IPs are good at making rapid assessments of a business's financial position. That should cover profitability, the reasons for trading losses, reviewing available forecasts, quantifying the cash shortfall and assessing solvency. The first question should be - can the Company be rescued without an insolvency process? For example, can it trade on successfully by managing working capital or negotiating with creditors? Only if the answer is a clear NO should insolvency options be considered.

Even if an insolvency process is necessary and the Company cannot survive it may be possible to save the business and jobs by selling the business and assets as a going concern. The main focus of the discussion will be on the company but the IP should also alert you to any obvious issues including director loan accounts, historic dividends that may have been unlawful and personal guarantee liabilities.

If you are not comfortable with what you are being told, then seek a second opinion.

Managing a cash crisis

Every year countless profitable businesses have to close because they run out of cash. It can happen in a number of ways. Perhaps you're working on a large project and being paid at the end. It's an incredibly lucrative piece of work but you have a lot of expenses to cover and in the meanwhile you can't cover them.

Be aware of the following:

Brexit has caused businesses to work in different ways. The Covid-19 pandemic brought large-scale restrictions, temporary business closures and swathes of office-based employees working remotely. In 2023 and beyond we are seeing rising energy costs, staff shortages and supply chain disruption adding to the increase of cost pressures on businesses while inflation continues to rise to levels not reached since the early 1990s. In some cases, businesses that had viable long term business plans at the start of 2020 have had to rethink and restructure in order to survive in this 'new normal' era. If you are a director who has been at the helm of profitable businesses and today find your Company with a reduction in cash resources, negative cashflow projections, increased creditor pressure or simply carrying unsustainable levels of debt then read on.

Directors should assess the risk of insolvency by considering two tests:

1. The 'cashflow test' – where a company is unable to pay its debts as they fall due.

2. The 'balance sheet' test – where the Company's assets are less than its liabilities.

If your company fails either test then your company is insolvent and directors should seek early professional advice.

Missing information

There is, of course, another simpler reason. Sometimes a company doesn't have quite as good a view of its cashflow as it should which could inform the way it manages its numbers. If your accounts aren't completely accurate and up to date it's easy to lose sight of how much money is in the bank, how much you are owed and when you're in danger of running out of cash. It's easy to assume that your bookkeeper or accountant is on top of your cashflow, but very often that simply isn't the case.

Confusing profit with cash

Then there's confusing profit with cash. Business managers see that the business is busy; they see the invoices going out and that the Company is projected to make a healthy profit by year-end, but they forget to look at how much cash is actually coming into the bank.

Get a daily cashflow forecast

The only real solution if cash is tight is for businesses to be absolutely draconian about managing their cash flow. In fact, this is the number one duty of any business owner because your business rises and falls on cash. Make sure that your bookkeeper or accountant gives you a daily – yes, daily – report about how much money is in your account, and what they expect to come in and out of it over the next few days and the coming month. That way, you can clearly foresee shortfalls ahead of time, and act early to prevent disaster. Similarly, make sure you're receiving monthly management accounts that are fully accurate.

Running a business is like captaining a ship

The more you can see, the safer you'll be. Cash is important - it's the lifeblood of your company and if that stops so does your business. Yet too many business owners don't pay enough attention to it. Every time a business forgets to look after its cash its directors are taking a risk with its financial health. Make sure that your business is safe.

Poor cashflow

If your creditors are regularly chasing for payment or have put you on hold consider talking to your suppliers/creditors. It is common sense to involve them otherwise they will feel that you are avoiding them. Arranging time to pay with creditors can be successful way to deal with cashflow problems.

However, as a director, you should be asking the bigger picture questions such as:

- Is the business viable?
- Can we make profits over the next period?
- Are we missing the fact that our cost base is much too high for our current income levels?
- Should we be taking professional advice from turnaround advisers?

If you are considering proposing time to pay with creditors, we recommend building a cashflow projection that is realistic. Apply common sense to it. What happens if a promised customer payment does not come in on time? Will you be able to meet promised creditors payments?

Always ensure that the payments promised to suppliers are based on a realistic cashflow. Do not forget things like PAYE, VAT, bank loans, direct debits etc. These are easily forecast-able as are salary payments and rent etc. All payments promised must be achieved otherwise creditors will lose faith.

Your company's relationship with HMRC

Do you recognise any of the following:

- Monthly PAYE & National Insurance Contributions (NIC) deductions are not being paid on time.

- You are not filing VAT returns or paying the VAT due on time.

- You have been issued VAT penalties or VAT surcharges.

- The local tax collector has passed your file to the enforcement office or the debt recovery unit.

- You have done deals with the taxman to pay back arrears over time (known as time to pay deals or TTP) but you have failed to keep to these arrangements.

- HMRC has taken legal action against your business. It has issued a CCJ or worse, a winding up petition.

- You have paid unsecured creditors instead of paying HMRC.

It should be remembered that HMRC are involuntary creditors. In other words, HMRC does not choose to give credit, your business just takes it. One ground upon which a director can be disqualified is trading to the detriment of the Crown. The Company having liabilities to HMRC over twelve months old should raise a big red flag. As they say, 'Cash is King'.

What a Personal Guarantee ('PG') means for you?

PGs are often given when a business is growing, after all, you believe in the future of the business and what could go wrong? Maybe nothing – but then again it might. So before giving a PG think carefully and if possible follow the advice below.

As a director of a limited company, it is standard practice for lenders (and indeed some trade suppliers) to request that you sign a PG to act as surety for company borrowing. By doing this the creditor will have recourse to you personally in the event the Company defaults or closes down. PGs are not used for sole traders or partnerships (except LLPs) as any debt is already a personal liability of the business owner(s). If you have been asked to sign a PG if possible you should always seek independent legal advice before signing anything as the terms can vary. It is also worth noting that most banks will keep a PG on file indefinitely even once the borrowing has been repaid. If you are in any doubt you should write to the bank and ask them to cancel the PG.

If a PG is called upon then get legal advice to ensure it is valid. It may not have been drawn up or executed correctly.

The second route is to talk to the creditor (if you haven't already). Legal action can be lengthy and costly and most creditors would prefer a negotiated settlement.

Some words of warning

- Don't give a PG if you can avoid it.

- If you can't avoid it seek to limit the value of the PG and put a time limit on it.

- Seek to limit the scope of the PG to a particular transaction or loan and ensure the documentation reflects that situation.

- Make sure you retain all the documentation associated with the granting of the PG – it may later provide a reason to question its validity.

▪ Try to avoid your spouse giving the same guarantee.

▪ Directors should be particularly wary of giving guarantees on finance agreements as the penalty for breaching those agreements can be extremely high and may involve the total outstanding payments under the agreement with no right to keep the asset that was the subject of the agreement.

If you are faced with a demand for payment under a PG:

▪ Do not panic - most creditors will give time to pay or refinance.

▪ Work with the funder and/or liquidator to maximise the value of the assets.

▪ If the Bank want to appoint administrators over the Company don't just accept the
Bank's choice of IP – they may be more expensive and eat into the assets available to repay the debt – choose your own IP to advise the Company.

▪ Speak to us – we can review the validity of the PG and help you negotiate a substantial settlement discount.

HMRC Powers - Joint Liability Notices

Effectively from 22 July 2020 directors can be made personally liable for repeated company insolvencies and non-payment of tax in a five-year period if they had...

▪ At least two old companies with a similar trade which became insolvent.

▪ The old companies had tax liabilities and at least one owed HMRC more than £10,000 and represents over 50% of that company's liabilities to unsecured creditors.

▪ A new company carrying on the same or a similar trade.

...HMRC can issue a Joint Liability Notice ("JLN") making the Director jointly liable with the old companies for tax liabilities at the date of the JLN and jointly liable with the new company for any tax it owes at the date of the JLN and any tax liability arising in the following five years. This vastly increases the personal risk to directors from multiple company insolvencies.

The only unknown is how often HMRC will use this power as it has other similar powers which we rarely see used.

Directors’ loan accounts and unlawful dividends

Until the Companies Act 2006 came into force on 1 October 2007 directors’ overdrawn loan accounts above £5,000 were unlawful. Since then directors’ overdrawn loan accounts are lawful below £10,000 and above this amount if fully disclosed to and approved by a resolution of shareholders. However, in many SME companies these formalities are often not followed. Unlawful overdrawn loan accounts are voidable (effectively making it repayable on demand). As long as there is no loss to the Company these days overdrawn loan accounts are considered normal and routine.

Often director/shareholder overdrawn loan accounts operate in conjunction with declaring dividends. Rather than paying wages/salary typically directors will draw sums in "lieu of wages/salary" over the year and at the year-end a dividend is declared and posted to the Directors' loan accounts bringing the balance down to nil. As long as the balance is extinguished within nine months of the financial year no S455 (formerly S419) tax arises and for annual drawings/dividends up to a limit per annum tax/national insurance is saved.

The problem comes if the "music stops", the Company ceases to have distributable reserves or become insolvent. Sure enough any directors' overdrawn loan accounts appear as bold as brass on the balance sheet but it is no longer lawful to declare a dividend and "put the loan account right". In effect the Directors have foregone wages/salary, worked for nothing and owe the Company a substantial debt exactly at the same time their principal source of income has or is in danger of drying up. An invidious position.

If a company faces insolvency or there are doubts about its ability to continue as a going concern the following simple steps taken in time should significantly improve the position:

- Obtain shareholder approval for any loans to directors above £10,000 to make them lawful.
- Do not continue to unwittingly build up loan accounts for example based on professional advice given when the Company was solvent.
- Paying directors by way of market wages/salary rather than through monthly drawings and dividends. Directors are entitled to reasonable remuneration just like any other employee. Even if the Company does not have spare cash to pay this the monthly net pay can be posted and set off against each directors’ loan account. Minute the reasons for doing this.

In the event of any insolvency if the Directors are employees then statutory pay in lieu of notice, redundancy, arrears of wages/holiday pay claims will usually be paid by the Redundancy Payments Service (“RPS”). For a director with over 10 years’ service this could be worth over £10,000 paid salary at a proper market rate for at least 12 weeks prior to an insolvency. (However, the Government department that pays such claims keeps adding conditions that must be met before director’s employment claims are paid so you will have to have all your paperwork in order.

For example if as an employee you have been earning minimum pay (which you will have been if all you have been drawing in salary is your personal allowance) you will likely be unsuccessful in any claim from the RPS. Your last three months’ payslips (as a minimum) will need to be above the minimum wage to stand any chance of a successful claim.

Directors’ duties and responsibilities

The Companies Act 2006

The Companies Act 2006 governs companies in the UK in just about every way a company is managed, run and financed. It was implemented in stages, the last starting in 2009 and provided public and privately run companies in the UK with common corporate laws.

As a director you are personally subject to the following statutory duties:

- To act within powers in accordance with the Company’s constitution and to use those powers only for the purposes for which they were conferred.
- To promote the success of the Company for the benefit of its members.
- To exercise independent judgement.
- To exercise reasonable care, skill and diligence.
- To avoid conflicts of interest (a conflict situation).
- The duty to not accept benefits from third parties.
- To declare an interest in a proposal or arrangement.
- To adhere to Section 172 reporting requirements.

Directors can become personally liable for any breach of these statutory duties particularly after a company becomes insolvent. You have a defence if you have taken every step to minimise loss to creditors and there are reasonable grounds to believe that you acted honestly and reasonably having regard to all the circumstances.

The duty to creditors

If a Company gets into financial difficulty and becomes insolvent the directors must act in the best interest of creditors, as the Company will have had use of creditors' money and creditors will suffer if the company goes bust, so this should include:

- Taking stock of your situation not incurring more credit.
- Don't prefer one creditor over another.
- Don't ignore threats of legal action from creditors.
- Be realistic.
- Seek professional advice from a Licensed Insolvency Practitioner.

Company Directors Disqualification Act 1986

When a company goes into an insolvency process like administration or liquidation the appointed Insolvency Practitioner has to file answers to a questionnaire with the Insolvency Service on the directors conduct. Based on this report The Insolvency Service will consider whether to apply to the Court for the director's disqualification which can be for a minimum of three years and a maximum of 15 years.

The list of disqualified directors is kept at Companies House. Anyone can call the general helpline giving the person's surname and initial and they can usually check over the telephone or the list can be found on the Companies House website.

The Rating (Coronavirus) and Director Disqualification (Dissolved Companies) Bill

This Bill received Royal Assent on 15 December 2021 and amends several sections of the Company Directors Disqualification Act 1986 ("CDDA") allowing the Secretary of State to investigate the conduct of former directors of dissolved companies. It assists in closing the loophole where directors either dissolve a company or take no action so Companies House does so rather liquidating it, thereby avoiding investigation under CDDA. It also brings to an end the current time consuming and costly process of applying to Court for a dissolved company to be restored to the register in order for the former directors to be investigated and subsequently disqualified.

Business rescue and insolvency options (in the order an Insolvency Practitioner would consider them)

Trade on and out

Prevention is better than cure. It is not unusual for businesses to have to juggle cashflow for short periods but it is not usually for them to have to do that all the time. As a company becomes distressed it usually happens slowly over a long period until towards the end when it can become rapid and directors have to fight on multiple fronts – for example when credit insurers can withdraw insurance from your suppliers.

To survive and trade on a company needs to be returned to profitability and cashflow kept under control. If cost cutting is necessary then do it as deep as you dare. There is often a time lag between cutting costs and seeing the positive effects on cashflow. If rescue funding needs to be introduced there are ways to introduce cash into the business which are lower risk for example by taking security and any directors/ shareholders considering doing this should take professional advice first.

If the business is struggling financially it is probably insolvent or near insolvent. If so the Directors duties change from acting in the interests of shareholders to acting in the interests of creditors and to protect themselves they should record decisions and take and follow professional advice. Case law has established that following professional advice gives directors a high level of protection.

Time to pay arrangements (“TTP”)

If creditors cannot be paid as they fall due by trading on whilst managing cash then your company is probably insolvent. If you can’t trade on and out without doing informal deals with creditors then you are going to have to enter into time to pay arrangements or TTPs. By doing a TTP a company becomes able to pay within the new agreed extended terms and so become solvent.

Historically agreeing a TTP with HMRC for over three months was a shoe in, it was usually possible to agree payments over six months but it was rare to see payments spread over more than 12 months. Post Covid 12 months+ TTPs with HMRC became common.

Informal TTPs with more than a few creditors are usually unworkable.

New moratorium/Restructuring Plan

If an informal TTP won't work then consider a formal moratorium using the new Moratorium procedure, this new procedure has been on the cards since 2016 but was finally introduced by the Corporate Insolvency & Governance Act 2022 in June 2020 (commonly known as CIGA).

Once you have filed documents at Companies House there can be no legal action against the Company for 20 days providing struggling companies with a short period of protection – effectively giving a company breathing space. This can be extended by creditors or the Court for up to 12 months. During this time a company can seek advice, negotiate with creditors and agree plans for their rescue as a going concern – so focusing on saving the Company rather than realising assets. Available to both companies and LLPs and directors remain in charge of the Company.

A monitor has to be appointed who is an IP who has to assess whether the moratorium will result in the rescue of the Company as a going concern and has to monitor the Company's ability to pay debts as they fall due in the moratorium period. If the monitor decides the Company cannot do either then they must terminate the moratorium.

Between its introduction on 26 June 2020 and 21 March 2023, 42 companies obtained a moratorium and 20 companies exited with a restructuring plan with creditors. In our view these procedures are not suitable for the vast majority of SMEs so we won't say more about them here.

Company Voluntary Arrangements ('CVA')

If a moratorium won't work then maybe a CVA could. CVAs were introduced in 1987 and got off to a slow start but with the decline in the high street and then since Covid-19 most national retailers/casual dinner businesses have either been in or thinking about doing one as they can be used to walk away from unprofitable outlets and reduce rents.

CVAs can be used if a company:

- Is profitable.
- Just needs time for something to happen (a contractual receipt/sell an asset/refinance/ win litigation) to enable creditors to be paid in full or part.
- More typically to allow a company to restructure and make voluntary contributions over five years.
- Used to wind down a business.

However, it has to be approved by 75% by value of creditors and it needs to offer something significantly better than administration/liquidation – typically 30p to 40p in the pound compared to a few pence in liquidation… and with the reintroduction of Crown preference this will be much harder to achieve.

A word of warning. A lot of CVAs fail - because most are based on voluntary contributions over five years when things change …

Administration

If a CVA won't work then maybe an Administration could. In 2003 Administrations became mainstream when banks could no longer appoint Administrative Receivers under new debentures. The major advantage over liquidation is that Administration creates a moratorium stopping creditors from taking enforcement which can assist to sell a business and assets as going concern. Most administration appointments are made by a company's Board of Directors but a lender with a floating charge has a five-day window to veto the Board's choice of IP and appoint their own choice. It can be a useful procedure to preserve all or part of the business or when the directors and shareholders cannot agree between themselves. However, it is expensive and will only be suitable for SMEs in specific circumstances.

Pre-pack administrations

An accelerated administration process that requires expert handling. In 2003 no one had heard of pre-pack administration but they quickly came to the fore and even today the majority of administrations are pre-packs. A pre-pack is where the sale of the business and assets is negotiated prior to the Administration and completed soon after.

Over the years pre-packs got a bad name seen as cosy deals behind closed doors and are increasingly regulated so that today there has to be open marketing and detailed disclosure to creditors soon after the deal is done.

Liquidation

If Administration won't work then that leaves Liquidation. Liquidations followed the introduction of limited liability companies in 1844 and are used when a company has reached the end of the road.

A solvent liquidation also known as Members' Voluntary Liquidation or MVL pays a surplus to shareholders taxed as capital gains rather than income.

An insolvent liquidation can be a Compulsory Liquidation (normally initiated by a creditor) or a Creditors' Voluntary Liquidation or CVL (initiated by the Directors and approved by the shareholders). Directors will always opt for CVL because it is quicker and they get to choose the IP. CVLs are the most common type of insolvency procedure for a company.

A run of case law in Europe and the UK has determined that TUPE applies to all Administrator sales which transfers all employee liabilities to a purchaser but does not apply to business and asset sales by a liquidator. For most smaller businesses whether employee liabilities transfer will make or break a sale as a going concern that can save jobs. Also in a CVL all the regulation around pre-packs does not apply and if you follow the right procedures it is also possible for a director's successor company to continue to use the same name.

Can I buy my business back from a Liquidator?

The majority of business and asset sales done by Insolvency Practitioners are back to a former directors' new company – particularly for smaller businesses. The directors' offer needs to be the best available to the liquidator, but it usually is because you know the business and assets best and they will be worth more to you than anyone else.

If you are going to buy the business and assets back from an IP you should want it to be in the best shape possible with its customers and supplier base intact. If you leave it too late customers and key employees will have gone to competitors. Also if the decline of the old company becomes drawn out you may have put all of your personal savings into it to keep it going and have nothing left to fund the new company.

Most business and asset sales by an IP have to be done quickly – because otherwise after a very short time there will simply be no business left to sell – think hours and days not months that it would be for a corporate finance sale.

The successful purchaser needs to know what it wants to buy, how it's going to pay for it, be able to put the money on the table at completion ... and working capital to fund the new business. This all takes time and the sooner you start to plan the quicker you will be able to move and the greater the likelihood of success.

When you are negotiating with an IP it is all about the art of the possible. You shouldn't make an offer you cannot deliver but ideally you should:

▪ Ensure some cash is paid on completion at least equivalent to the ex-situ auction value of tangible assets.

▪ Should be paying some premium over the ex-situ value of the assets and /or for goodwill. This varies a lot depending on the business but will typically be 50% above ex-situ values.

▪ Negotiate to pay for stock/WIP as it is used or pay upfront at a substantial discount.

▪ One thing which often gets missed is to offer to collect in book debts for say a 15% commission of realisations because you know the customers and will be wanting to deal with them anyway.

Suppliers will be very wary, don't expect credit for first few months and NewCo may have to provide sweeteners to secure future supplies often paying a slight premium over list prices for a period.

Most major banks won't provide bank accounts or facilities to phoenix companies - companies that have purchased the business and assets from an insolvent company with same directors – so do your research ahead or ask us.

When buying a business and assets the IP will give no warranties so caveat emptor applies 'let the buyer beware'.

Reusing a company name (S216 Insolvency Action 1986)

If you have been a director of a liquidated company and you decide to set up a new company, unless one of three statutory exceptions apply it is not allowed to have the same or a similar name to the old company as it would lead to possible confusion of creditors of the old company. This is called passing off and under section 216 Insolvency Act 1986 it can lead to criminal action against the Director. The Director can also be held liable for all of the debts of the new company should it too go into liquidation.

Speak to us if this is something you want to achieve as it is very important to follow the correct procedure in the correct order to avoid any breach of duty and future personal liability.

Top tips for directors of a struggling business

We start approximately 150 insolvency appointments a year and through those we see all sorts of director conduct, some very good and some very bad. Through that experience we have identified the top ten things that a director can do to avoid the worst pitfalls.

Know the financial position of your business and have a plan

▪ To be able to make informed decisions directors need to know the Company's current financial position.

▪ Exactly what information is required varies depending on the size and complexity of the business but at a minimum they should have up to date management accounts and be able to see that they have enough cashflow for the foreseeable future.

▪ If the cashflow looks tight we would always recommend that a 12-week rolling cashflow forecast is prepared.

▪ You should always have a plan and be realistic about it - you should always know where you want the business to go.

▪ Ideally you should have integrated profit and loss, cashflow and balance sheets at monthly rests covering the year ahead and if cashflow is tight a 12-week cashflow at weekly rests.

▪ Those forecasts should be flexed so that at a minimum you have a base forecast that you can be confident can be achieved and a more ambitious cashflow that can act as a target.

Treat creditors equally

▪ Once a business becomes insolvent the Directors need to switch from working in shareholders' interests to working in creditors' interests.

▪ That means making decisions to minimise the potential loss to creditors.

▪ ...and all unsecured creditors should be treated equally.

Seek professional advice early

▪ If the 12 week rolling forecasts or the long-term forecasts show that the business is running out of money then you should seek professional advice early and follow that advice.

▪ Re. World of Leather Case – found that as the Directors had taken and followed professional advice they had acted properly.

▪ McTear Williams & Wood provides free initial advice so you don't have to risk not taking advice early.

Don't let Crown debt get more than 12 months in arrears

▪ Whilst insolvency law requires that all creditors are treated equally the reality is that often HMRC get left behind.

▪ If your company is more than 12 months in arrears with its HMRC debts this is a red flag and could lead to directors' disqualification.

▪ Also, you should watch out for Joint Liability Notices for repeated offences where the Crown debt is >50% which we mentioned earlier.

Have a written service agreement or contract of employment

▪ ...and paid through the payroll/PAYE scheme.

▪ Helps to justify director claims for redundancy, pay in lieu of notice or PILN and arrears of wages which can easily be £15k+

Stop drawing against any directors' loan accounts or paying dividends if the Company doesn't have the distributable reserves to do so

▪ Taking into account losses since the last annual accounts instead change to PAYE and draw a salary instead.

▪ Remember that interim dividends approved by the board of directors have no standing unless paid or posted in the accounting records.

▪ If you keep drawing dividends a liquidator may have to ask you to repay them.

Pay yourself a fair market salary

▪ The case law is mixed but our view is that it is OK for directors to pay themselves a fair market salary in place of dividends.

▪ Even if there is no cash to pay it can be posted and used to reduce any director's loan account.

Be smart if injecting rescue funding

▪ Rescue funding is always very risky and director/shareholders should be wary of ending up as unsecured creditors.

Have a plan B

▪ As that will speed up how quickly you can act if continuing to trade ceases to be an option.

▪ It also helps directors to understand their options and aids current and future decision making.

Don't let it get you down

▪ The situation has gone too far if it does.

▪ This is a good test of whether the Director should take specialist advice.

▪ There almost certainly is a better way.

Summary

We hope you found this guide useful. If you have read through it all by now you will understand there are many factors that come into force when a company or LLP becomes insolvent or financially challenged.

Usually, directors have a duty under the Companies Act legislation to act in the best interests of the shareholders but when a company is or looks likely to become insolvent you must increasingly act in the best interests of the creditors. In the “twilight zone in between” there are lots of grey areas and our advice is always seek professional advice.

Please do speak to us to ask any questions that you may have. What have you got to lose; our initial meetings are always free.

The common theme that you will have seen running through this guide is - you should take advice as soon as possible, when a company looks like it may become insolvent.

We would be pleased to help you. You don’t have to disclose your name or the name of the business. You will get a sympathetic hearing; we will ask you questions about the business and what it does and what the issues are. We will ask what you want to do, then we will give you all the options.

Just like having an illness, the quicker you go to the doctor the better generally! You should therefore take advice from experts who spend all day looking after companies in distress.

Call us on freephone 0800 331 7417.

Disclaimer

This guide contains general advice only and specific advice should always be taken before reliance is placed upon it in any particular circumstances. Whilst all of the ideas put forward can work well they are mostly fact specific and in the wrong circumstances could carry high risk or be unlawful.

Contact Us

If you contact us we can advise you on the best course of action for your particular circumstances. We have years of experience and a track record of helping companies and getting results. We offer a free and confidential initial meeting with one of our senior team who can assess and understand the issues your business is facing and discuss all the options available.

Call us free on 0800 331 7417 or email info@mw-w.com.

MCTEAR WILLIAMS WOOD

business rescue and insolvency

McTear Williams & Wood was formed in 2000 and since then we have taken thousands of enquiries from directors of struggling companies and individuals who are worried about aspects of their business. We provide professional business rescue and insolvency services for SME businesses across East Anglia and London.

Today McTear Williams & Wood is one of the largest regional independent business rescue and insolvency practices in the UK providing SMEs with comprehensive and specialist corporate advisory and insolvency services. In the first instance we always recommend a free initial confidential consultation with one of our senior team where we can work to understand the issues facing your business and discuss all the options available.