



# The CPD Fest 2020

## Corporate Insolvency What the Advisor Needs to Know

### Presenter:

Jim Stafford - Friel Stafford

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**Corporate Insolvency: What the Advisor needs to know**

18<sup>th</sup> November 2020 and 18<sup>th</sup> December 2020

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**Important Notice**

The information contained in this document is for general guidance only and should not be taken as a definitive statement of the law in this area in relation to the subject matter of this document. This document should not be regarded as a substitute for professional advice, which should always be sought in relation to specific cases.

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**About Friel Stafford**

Established over 25 years ago, Friel Stafford is a niche accountancy firm specialising in four distinct areas –

Corporate Recovery & Insolvency	Personal Insolvency & Bankruptcy
Forensic Accounting & Expert Witness	Business Valuations & Corporate Finance

Our firm was founded in 1994 as a Specialist Corporate Recovery and Insolvency practice and is one of Ireland's leading firms in this area. We have been appointed as Liquidator, Receiver or liquidator to over 1,000 companies.

We provide prompt commercial advice to directors of a Company who are encountering financial difficulty. Crucially - we do not assume that insolvency proceedings are always inevitable, and we will examine all options available to a Company.

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**Contents**

1. Under what conditions can a company continue to trade whilst insolvent?
2. Should clients put more of their personal money into their insolvent company in order to save it?
3. Advice on how a director can buy back his business from a liquidator in the unfortunate scenario that the company needs to be placed into liquidation.
4. Issues to consider in Landlord/Tenant cases
5. Turnaround strategies
6. Overview of formal insolvency processes
7. Review of Companies (Miscellaneous Provisions) (Covid-19) Act 2020
8. Case law update/Forthcoming legislation



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**Issues for Accountants and Advisors in advising companies in difficulty**

- Acting as shadow directors: Always present “options” and let the directors decide.
- Negligence

Inappropriate Advice *e.g.*

- As to whether continue trading
- Advice re implications of insolvency procedures
- Advising to borrow on strength of personal assets

- Going Concern
- Fraud
- Bad Debts



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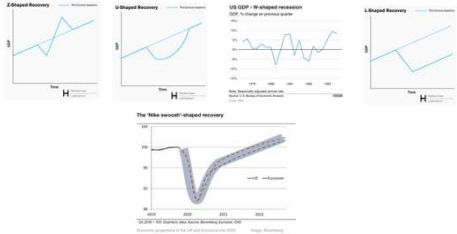
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**Realistic assumptions are vital for business plans. What type of recovery are we looking at?**

- Will it be a Z, V, W, L or even K? Perhaps a Nike Swoosh?





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**Continue trading whilst insolvent?**

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For background info on reckless trading click on [Claims for Reckless Trading](#)


The reality is that many companies will be unable to pay their debts as they due.

The Irish courts acknowledge that companies should be provided with a reasonable opportunity to trade out of their difficulties. In such cases the directors are under an obligation to keep the overall position under review and, in particular, "to keep creditors' interests to the fore".

The directors may be deemed to have engaged in reckless trading if, having regard to all of the information available to them, and to the general knowledge, skill and experience that may reasonably be expected of persons in their position, they ought to have known that their actions or those of the company would cause loss to its creditors.

Directors in such situations require expert advice as to whether they should continue trading. The decision will depend on the information provided by detailed cash flow and profit and loss projections.

Continuing to lose money could expose directors to greater calls on personal guarantees, **Section 997 assessments**, Restriction and Disqualification.

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**Trading insolvent: ODCE guidance on its approach to directors of companies made insolvent by the COVID**

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- In the UK – the government has suspended wrongful trading during Covid-19. This is not the case here.
- Proposals were advanced by certain organisations for relief for directors from the risk of restriction or imposition of personal liability for reckless trading during the pandemic
- ODCE issued guidance 5<sup>th</sup> June 2020
  - Restriction / Disqualification
  - Proceedings regarding personal liability

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**ODCE guidance on its approach to directors of companies made insolvent by the COVID-19 pandemic**

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ODCE Guidance

- If a company has become insolvent because of events outside the directors' control, the ODCE would not generally consider that they have behaved improperly.
- It is the actions taken, or not taken, by the directors in response to financial difficulties being faced by the company that will inform the assessment as to whether directors should face a restriction application
- The ODCE notes that the courts allow some latitude to continue to trade while insolvent where:
  - there is a reasonable prospect of survival; and
  - the directors have acted honestly and responsibly in other respects.

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**ODCE guidance on its approach to directors of companies, made insolvent by the COVID-19 pandemic**

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ODCE will consider

- the adequacy of the directors' processes and procedures for monitoring the company's financial position;
- whether the directors sought appropriate professional advice;
- the basis on which the directors formed the view that the company would be able to trade out of its difficulties, including grants, loans and other supports;
- how long trading continued after it should have been apparent that the company was insolvent;
- how much the position deteriorated and what kind of additional liabilities accrued after it should have been apparent that the company was insolvent;
- if there are significant tax liabilities, whether the company availed of, and complied with, the Revenue Commissioners' requirements for deferred payment and warehousing of liabilities; and
- the steps taken to reduce costs and/or to restructure the business.

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**ODCE guidance on its approach to directors of companies, made insolvent by the COVID-19 pandemic**

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*However, provided that directors' decisions and judgements were:*

- a) made on the basis of objectively verifiable evidence;*
- b) based on assessments and assumptions that were reasonable in the context of the circumstances pertaining at the relevant times;*
- c) made in good faith and the directors otherwise acted honestly and responsibly,*

*it is unlikely that the ODCE will consider that the company directors concerned should be restricted.*

**In effect ODCE are saying that Directors who apply common sense in evaluating, documenting and monitoring their company's financial position should have no concerns regarding trading insolvently.**

**Conclusion: Nothing has changed. ODCE attitude is now in line with the High Court**

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**Zombie Companies?**

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- The number of companies going into liquidation has actually fallen significantly in recent months due to loan repayment deferrals by banks and revenue and various Government supports.
- Many companies will find that COVID-19 is not just a liquidity problem. It is eventually a solvency problem. **ISSUE FOR DIRECTORS**
- Many businesses have taken advantage of huge levels of government support in recent months, but once that support is withdrawn, they may struggle to get back to where they were before the pandemic.
- **Covid-19 cannot be used as an excuse to keep unviable businesses running, load up on unsustainable debt or dodge paying worker entitlements.**
- Directors must continue to think carefully about their ongoing duty to act in the best interests of the company, including
  1. the interests of creditors when approaching insolvency, and
  2. whether incurring additional liabilities would be a prudent course of action.
- Directors should also remember that there is a serious risk if you are trading while insolvent and that they could incur personal liabilities if they do not take reasonable steps to deal with the problem

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**Monitoring**

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- Regularly update cashflow and balance sheet forecasts, together with sales, pipelines and other operational matters (employees, suppliers, etc.).
- If applicable, check insurance policies and maintain contact with the company's insurance broker, together with addressing any potential claims (e.g. business interruption).
- Address sources of financing whether that is bridging finance, loan facilities (taking one or extending current facilities) and/or taking advantage of government schemes.
- Evaluate arrangements with key suppliers (including landlords and Revenue Commissioners) and customers (together with cash collection), with a view to understanding whether there is any flexibility in the underlying terms and discussing time to pay arrangements.
- Fully investigate any available reliefs and funding offered by the government.
- Regular contact with the stakeholders of the business and keeping them properly informed, including shareholders, creditors (particular key creditors), key suppliers and customers.

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**Monitoring**

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- Convene regular board meetings at which cash flow details, and operational matters and other above mentioned matters are reviewed in detail. Depending on the circumstances, these meetings can be weekly or more frequently as circumstances dictate.

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**Lessons from 2008-2011: Quit when you are ahead**

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- If there is one lesson that could be heeded from the financial crash of 2007/2008 it is that it might be wise to 'Quit when you're ahead'. In the years after crash, we saw too many Directors of businesses lose their personal assets, be it pension funds, investment properties, homes etc. as a result of trying to support and prop up a failing business.
- The issue is more acute this time, as there are many second generation/third generation under massive financial pressure = more egos/family names under pressure
- I have seen too many directors lose their family homes/pension schemes as a result of either:
  - Ignoring good professional advice
  - Following negligent advice (and you do not want to fall into that camp)
- Accurate projections are essential in order to advise. However, projections are only as good as the underlying assumptions. Do not be overoptimistic on the "bounce back". Given the current Covid crisis, it is difficult to validate assumptions. Brexit? Domino effect of bad debts? Loss of major customer(s)?

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### Should a client cut its losses and liquidate now? Case study of company that went into a Members Voluntary Liquidation

- As a result of the pandemic, there is no doubt that some companies would be well advised to cease trading now and protect their retained earnings to date by placing the company into a Members Voluntary Liquidation, as opposed to incurring losses by continuing to trade in a hostile trading environment.
- Some directors might be able to avail of either the 10% Entrepreneurs' Tax Relief Scheme or Early Retirement Relief.
- In late 2007 a plastering company asked us for advice, given that they had formed the view that the housing bubble was about to crash. The company had net assets of €1.5 million, but the assets were comprised of WIP and debtors.
- If they told the main contractors that they were exiting the market, they may have not received payment. We devised a simple strategy. The company priced new tenders at 40% above what they would have normally charged = they won no new work.
- By September 2008 they had finished all of their WIP and collected all of their debtors, and went into a MVL. If they had not taken the above strategy they would have lost everything.

(For further info on MVL's click on <https://www.frielstafford.ie/members-voluntary-liquidation/>)



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### Securing investment in Companies

- One of the most challenging questions that clients will ask accountancy firms will be **"Should I put my own money into the Company to save it?"**
- Before putting new money in, Examinership should be considered, as new money can frequently guarantee the success of an Examinership.
- Options such as Examinership and Schemes of Arrangements can be valuable tools as part of any restructuring and should not be dismissed or seen as an admission of 'failure'. They can help prevent corporate insolvency and ensure that the business continues in the short-term.
- In fact, by utilising Examinership or Schemes of Arrangements, the business may be given breathing space to restructure, and in doing so, it could enable the company to develop a sustainable competitive advantage and provide opportunities for raising further finance.
- In any event, if Directors are putting money into the business, they should consider securing the payments advanced by taking a charge over Company assets. Legal fees to do so are about €2,000 to €3,000 and could be money well spent.



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### Starting Again: Phoenix Companies

1. Irish law recognises that the directors have a right to earn a living and so are not prevented from setting up a new company and starting again.
2. A Phoenix Company is a new company set up from the ashes of one that has become insolvent. It is usually set up by the same directors, and with the same assets, including intellectual property. The new company is set up to trade in the same or similar trading activities as the former.
3. The main point with setting up phoenix companies is that any assets purchased should be done so at fair value. This means they must be independently valued and a transparent record keeping maintained. Creditors can challenge phoenix companies for assets sold at undervalue.



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**"Prepack" Liquidation**

- A pre-pack liquidation is the process where the assets and business of a company are sold at market value to a new company sometimes, but not always, managed by the same directors.
- "NewCo" is formed to take over assets of a failing company ("OldCo") at a pre-agreed price for assets. NewCo trades on and OldCo is liquidated
- Resources of OldCo are used then by NewCo
- Not common in Ireland **AS THEY SHOULD BE**, common in UK.
- Has many advantages – but process can be obviously controversial.



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**How a Prepack liquidation works**

*A swift secure planned transition of a business to a new company.*

- The sale is negotiated, agreed and documented before the onset of formal insolvency procedure and are effected on or shortly after the appointment of the Liquidator.
- Independent valuation of business and assets **REQUIRED**
- Has to show what the market value is
- Transaction agreed between NewCo and OldCo
- Proper board meetings and shareholders meetings approving the sale should be held.
- Proceeds ringfenced for Liquidator to apply to creditors in priority
- Liquidator has to be satisfied not transferred at undervalue.



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**Advantages of Prepacks**

- It can offer a higher possibility of preserving goodwill offering a better return for creditors than a straightforward liquidation.
- NewCo will be "debt free" and offers possibility of saving jobs. It may also have a better chance of future success.
- Cheaper than examinership
- Investment used for growth not debt repayment.
- Debt is written off
- Can be very pragmatic for smaller companies.



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**Disadvantages of Prepacks**

- Overdrawn directors accounts and PG's still liable
- Employees must transfer to new business (TUPE)
- Conduct of directors of OldCo (particularly in relation to sale) will be investigated by Liquidator
- NewCo requires separate financing. It may be difficult to attract investors
- Lose tax deductibility of trading losses
- GDPR can be a big "blocker" to transferring "on-line" or "consumer" type business if contracts with customers did not provide for transfer of their contracts to a third party.

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**Prepacks: Issues for Insolvency Practitioner**

- Statutory duty to get the best price reasonably obtainable
- Not exposed to market testing – important to get at least one independent, professional valuation of the business or assets.
- Needs to "represent the best price reasonably obtainable at the time"
- Perception
- Must comply with Statement of Insolvency Practice.

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**Prepack: Sales to a connected party**

- Irish company law prevents a Liquidator from selling an asset of the company to an officer of the company unless the Liquidator has given at least 14 days' notice of his or her intention to do so to all known creditors of the company.
- Can by-pass 14 day notice period if sanction provided by Committee of Inspection or by majority of creditors.
- For the purpose of the relevant provision, 'officer' includes a director or shadow director as well as a 'connected person'. The definition of a person connected with a director of a company is extensive and extends to natural persons and legal persons. A body corporate will be deemed to be connected with a director of a company if it is controlled by that director.

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**Issues to consider in Landlord/Tenant cases**

- The well advised landlord will seek full financial information about the tenant, to include accounts/projections and possibly copies of recent bank statements. The landlord will then assess if the tenant has the capacity to pay.
- The landlord will also review personal guarantees.
- As some guarantees are subject to time limits, the landlord needs to assess his options quickly.

If the tenant is unable to make full payments then the landlord can negotiate around the following options:

- Agree a rent free period.
- Defer the rent.
- Charge rent on a % of turnover.
- Have tenant abandon any break clauses.
- Extend the lease.
- Vary the other terms of the lease, such as re-locating tenant to a less favourable "pitch" within, say, a shopping centre.
- Charge interest.



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**Issues to consider in Landlord/Tenant cases**

- If charging rent on a % of turnover basis, then the landlord needs to consider also obtaining a % of on-line sales. This particular aspect of negotiations can be tough as the tenant may have a separate company for on-line sales or may claim that the on-line sales derive from other stores.
- Some retailers have considerably bumped up their on-line sales and deciding to close less profitable outlets.
- In practice, we are now seeing many landlords moving away from their initial aggressive position at the beginning of the Covid crisis to a more pragmatic position of "sharing the pain." We have seen all types of deals from one tenant only paying rates and service charges for the next 12 months, to personal guarantees being called upon.
- Some tenants are attempting to rely on *Force Majeure* defences. Such a defence has more chance of success in respect of a newly signed lease.
- A detailed review of the lease might identify other possible defences for a tenant such as Landlord breaching terms etc



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**Decision Tree for advising clients**

Is the Company Insolvent			
Yes		No	
Is the Company a viable business?			Steps to consider in Difficult times
Yes		No	
Consider if Suitable for Informal Scheme of Arrangement		Consider if Suitable for Examinership	
Advising Client on Liquidation Process		Advising Client on Liquidation Process	
Yes	No	Yes	No
Advising Client on Liquidation Process		Advising Client on Liquidation Process	



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### Turnaround Strategies

- Identifying the problems
- Assessment of business viability
- Devising a Recovery Strategy
- Monitoring of Recovery Strategy
- Implementation



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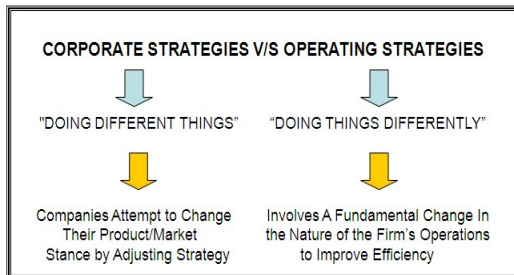
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### Corporate Strategies v/s Operating Strategies



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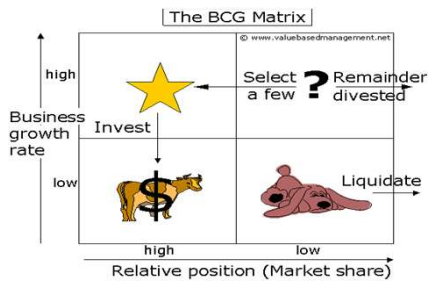
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### The BCG Portfolio Matrix



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### INDICATORS OF A VIABLE BUSINESS:

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- Profitable Order Book
  - Adequate Production facilities
  - Supplier Co-Operation
  - Bank/Shareholder support
  - Customer Support
  - Good Product/Brand name
  - Identifiable market position.



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### INDICATORS OF A NON VIABLE BUSINESS:

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- Industry Over Capacity
- Competitor Price cutting
- Market Collapse
- High Fixed Cost base
- Long term loss making contracts
- Old Obsolete plant

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### PROFITABILITY ANALYSIS

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PROFITABILITY ANALYSIS: PRODUCTS OR SERVICES	
ANNUALISED GROSS MARGIN FROM THIS PRODUCT OR SERVICE	€
LESS TRADE DISCOUNTS, REBATES, BROKERS FEES, AND SO ON	€
LESS DIRECT PROMOTION COSTS: COUPONS, ADVERTISING, PUBLIC RELATIONS, AND SO ON	€
DIRECT PROFIT	€
OTHER SELLING COSTS	
RETURNS AND ALLOWANCES	
STOCK/DEBTOR FINANCING	
RESEARCH AND DEVELOPMENT	
COMPLEXITY OF ORDER ENTRY	
SHIPPING COMPLEXITY	
BILLING COMPLEXITY	
SENIOR MANAGEMENT TIME REQUIRE	
OTHER COSTS OR CONSIDERATIONS	
BASED ON THE ABOVE, IS THE PRODUCT/SERVICE PROFITABLE	

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### PROFITABILITY ANALYSIS

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PROFITABILITY ANALYSIS : CUSTOMERS	
ANNUAL PROFIT FROM CUSTOMERS OR CUSTOMERS GROUP – NET REVENUES	€
LESS DIRECT COSTS (BE EXHAUSTIVE: INCLUDE COMMISSIONS, BROKERAGE FEES AND SO ON)	€
LESS COST OF GOODS SOLD	€
PROFIT FROM CUSTOMER	€
ARE THERE UNUSUAL COSTS ASSOCIATED WITH THIS CUSTOMER?	
UNUSUAL FIXED-CAPITAL COSTS	
DEBTOR FINANCING	
COMPLEXITY OF ORDER ENTRY	
RETURNS AND ALLOWANCES	
BILLING COMPLEXITY	
COMPLEXITY OF ORDER ENTRY	
DISTRIBUTION COMPLEXITY	
CUSTOMER SERVICE COMPLEXITY	
SENIOR MANAGEMENT TIME REQUIRED	
OTHER COSTS OR CONSIDERATIONS	
BASED ON THE ABOVE, IS THIS A PROFITABLE CUSTOMER?	

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### PRODUCT/MARKET RE-ORIENTATION

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- Entry into a new market
- Withdrawal from a market
- Adding or deleting particular products
- Adding or deleting particular customers
- Changing the mix of products made
- Changing the mix of customers

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### MARKETING STRATEGY

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- Product Range
- Pricing
- Customers
- Advertising
- Selling
- Distribution Channels
- Warranty
- Service
- Sale or Return

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### Blending the Strategies for Covid/Brexit

Everything needs to be combined:

- **Cost reduction:** Lay offs/Redundancies/Deals with landlords/ pay cuts etc
- Accelerate move to on-line sales/takeaway sales
- Avail of every Government/State Agency and County Council package/grant
- Close outlets etc



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### Formal Insolvency Procedures

Please click on the links below for detailed information on each procedure

- [Members' Voluntary Liquidation](#) Requires Special Resolution 75%
- [Schemes of Arrangement](#)
- [Receivership](#)
- [Examinership](#)
- [Creditors Voluntary Liquidation](#) Requires Ordinary Resolution 51%



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### Practical Aspects of holding virtual creditors meetings

- The legislation provides that there must be 3 creditors present in person, or by proxy, at the venue advertised for the creditors meeting in order to have a valid quorum. Other creditors may attend virtually, if they decide to do so.
- Ask all those physically attending the meeting to use sanitiser upon entering the building.
- Consider establishing a dedicated Gmail account, in the name of the company going into liquidation, to accept Proxies and to collate a list of email addresses that Zoom invites can be emailed to. The advantage of a Gmail account is that it may be accessed from anywhere.
- In the statutory advertisement for the meeting consider advertising the Gmail account that creditors can send proxies to. Sometimes the directors do not have the addresses of all creditors, such as holders of Gift vouchers, so such creditors can only be notified by advertising.



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**Practical Aspects of holding virtual meetings**

- Have a "stand by" lap top available with the Zoom app already down loaded so that if the Chairman's lap top does not work that you have a back up. (We had one case where the Chairman's lap top would not accept our WiFi password.) In some cases the chairman may not have a laptop etc.
- Ensure that the person hosting the Zoom call has a Zoom account in order to avoid the meeting cutting off after 40 minutes.
- Have extension leads available.
- The liquidator should be in a separate room if he/she is using his/her own laptop to participate in the Zoom call, otherwise you will get an echo effect.
- If a significant number of creditors are expected to attend, the Chairman should have a colleague who can host the Zoom meeting on his/her behalf, so that the Chairman can focus on the meeting and not be concerned about admitting late entrants to the call.

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**Practical Aspects of holding virtual meetings**

- Have a Conference call facility available, and know the number and PINs required. (We had one Zoom meeting where the Virgin Media WiFi became unstable, and we had to ask the creditors to dial into a conference call instead. We were able to enter the number and the relevant pin into the chat box feature on Zoom.)
- Zoom meetings are better than conference call meetings, as creditors can be identified etc. The chairman can also remove individuals during a Zoom call if they are being deliberately obstructive etc. It is also easier to hold a confidential Committee of Inspection meeting immediately after the creditors meeting.

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**Recent Case Law**

- **New Look** Examinership case. Key takeaway: The company should have consulted with creditors prior to entering Examinership. (This was an exceptional case, as the Company had €15 million in cash available.) The Examinership did not proceed.
- **Monsoon** Creditors Voluntary Arrangement case. Key takeaway: No automatic cross-border recognition of a UK CVA. The Court was held that the Irish landlords were not bound by the UK as the procedures followed in that particular CVA were essentially unfair to them.

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**Companies (Miscellaneous Provisions) (Covid-19) Act 2020**

**Creditors Meetings:**

- Companies will be explicitly enabled to convene and hold creditors' meetings to commence a winding up and during a winding up partly or wholly by virtual means.
- There are no specific technology requirements – However:

**Key requirements for such meetings are:**

- the technology must enable real time transmission and real time two-way audio-visual or audio communication enabling relevant attendees as a whole with a reasonable opportunity to participate in the meeting
- the person holding the meeting must ensure so far as practicable that certain data security and integrity measures are put in place
- notices of the meeting will have to include certain information about the technology to be used and any processes to verify identity of attendees
- participants must be enabled to hear what is said and speak and submit comments during the meeting

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**Companies (Miscellaneous Provisions) (Covid-19) Act 2020**

The Act addresses areas of concern in respect of operational matters in relation to compliance under the Companies Act and Industrial and Provident Societies Acts, such as the requirement to hold an Annual General Meeting, and protective measures designed to pre-empt certain impacts the crisis may have on a company's solvency with a view to protecting viable businesses, retaining employment and supporting economic recovery post-crisis.

Three of its provisions are particularly relevant to insolvency processes during the COVID-19 crisis.

1. Creditors Meetings
2. Creditors Winding Up Petitions
3. Potential extension of Examinership period

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**Companies (Miscellaneous Provisions) (Covid-19) Act 2020**

**Creditors Winding Up Petitions:**

The amount claimed by a creditor to ground a winding up petition is to be increased to €50,000 (from the current levels of €10,000 for a single creditor and €20,000 for creditors acting together).

**Potential extension of examinership**

The High Court is to be given power to extend an examinership by up to 50 days beyond the current 100-day limit.

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**Companies (Miscellaneous Provisions) (Covid-19) Act 2020**

**Duration**

- The Act provides that the temporary measures envisaged will apply until 31 December 2020 with a possibility of extension (but no later than 30 June 2021).
- This mirrors the possibility of an extension of the other emergency Covid-19-related legislation passed earlier in the year.

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**Companies (Miscellaneous Provisions) (Covid-19) Act 2020**

**What is missing in the Act:**

Disappointing that the proposed legislation is not enacting more immediate measures to introduce a low cost Rescue mechanism for SME's.

- The Examinership legislation is not fit for purpose for many SME's due to its costs.
- The reality is that most corporate rescues in today's environment require a *write off of debt*. The UK have a low cost Rescue mechanism, the Creditors Voluntary Arrangement, that provides write off of debt and does not require Court involvement. Unfortunately, any corporate debt write off in Ireland may require Court involvement as a result of the "Private Property" provisions in the Irish Constitution.
- Perhaps the long term solution to introducing a low cost Rescue mechanism is to hold a National Referendum to amend the Constitution to allow CVA's in Ireland

**UPDATE:** Following a recent report from the Company Law Review Group to the Minister, we can expect a "low cost" Scheme of Arrangement" type legislation next year: *Summary Rescue Procedure "SRP"*

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**THANK YOU**

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