Carter Clark
Financial Recovery

Briefing Sheet

Options for businesses in trouble

Recognising that a business is in trouble is a big step for many owners and directors. What to do when it becomes obvious that action is necessary will depend on specific circumstances but there are various alternative routes. Some may be determined by the company owners/ directors, assuming that action is taken in time: others may be forced on the company by the actions of third parties – usually creditors or shareholders.

These options are summarised below.

Business survival through trading

Trading out of a difficult situation might seem the most logical approach, especially if the company has suffered because of specific, short-term matters and the business is not fundamentally weakened. Every company will suffer at times but you must be honest with yourself in assessing the situation.

If you are certain that the business is viable – i.e. if by removing the current difficulty it has a long-term future – you need to determine what to do to address the specific problem. Improved cashflow or internal efficiency might be readily addressed: increasing sales might be more difficult and the same will be true of adjusting your business approach to make your business more competitive in the market.

Once you are happy that you have the capacity to improve matters fairly quickly, you can look at ways of getting the breathing space you need for the company to get back on its feet. Some form of deal with creditors may be the first approach: this is not as extensive as a Company Voluntary Arrangement but still needs to be based on hard fact and ability to deliver, not vague hopes and promises.

Call key creditors, explain that you want to pay them as quickly as possible but cashflow is tight: ask if you can pay them over an affordable time frame. Do not promise more than you can achieve – creditors who agree to work with you on this will not want to find you are not meeting your agreed schedule. If something further goes wrong, be sure to explain in detail to creditors what has happened.

Instead of this 'informal deal' you might opt for a formal arrangement using a turnaround practitioner as honest broker. This also stops short of a CVA but the professional you use will want to be certain that there is the capacity to make the proposed schedule work. With formal assistance of this sort, some creditors may even accept write-downs of debt if they think the company will survive and prosper long term.

Executive summary

Acting quickly and firmly is the key to making the best of a poor trading situation. Being honest about prospects – both within the company and with creditors and advisers – is essential. And sticking to any plan made is the only option once the plan has been communicated to interested parties. Professional help can ensure that the selected option is the best for the circumstances and can also gain credibility for the proposal. The sooner professional input is obtained, the quicker the stress is lessened and owners/ directors can get back to running the company, not dealing with creditors.

Have a question?

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Business survival through refinancing

Introducing additional funds to the company can help you gain the breathing space you need and is also a very strong sign to creditors that you are serious about the company's future. Finance options will range from a bank overdraft to directors' loans or injection of capital from third parties taking a share of the company. Factoring or asset finance might also provide the short-term boost needed.

Company Voluntary Arrangement

This is a more formal method of allowing the business to continue trading whilst seeking accommodation with creditors. It sets out an agreement to repay all creditors from future profits and is based on preserving the company, rebuilding sales and profits and paying something back over a period of time to be agreed. Current payments are frozen, improving cashflow. directors remain in control, personal guarantees are not normally called in and the business is given the opportunity to survive.

A CVA can be proposed by company directors prior to any other form of action being taken. However, it is dependent on the business having a viable future and the necessary future profitability being assured. It is dependent on assistance from appropriately experienced and qualified professionals and will also demand commitment from the company's directors and owners in making it work.

Administration

Administration is designed to protect companies from their creditors while a restructuring plan is completed. It can help where the directors think that a hostile creditor will seriously affect the future trading possibilities and the company needs to protect itself from them while a rescue plan is put in place. The company must be a reasonable size, have reasonably predictable cashflows and be able to predict profitability. The process is carried out by a licensed insolvency practitioner.

There are three main objectives for Administration, at least one of which should be achieved by the process:

- To rescue the company as a going concern.
- To achieve a better result for the creditors than would be obtained through an immediate winding-up of the company.
- If neither of the first two objectives is possible, to realise any property to make a distribution to secured and/or preferential creditors.

A 'pre-packaged' administration can be used where there is an agreement by a third party to buy the assets of the company at a fair price; this process reduces the associated costs.

Administrative Receivership

Different from administration, receivership is normally started at the request of a third party such as a bank, with floating charge security created prior to 15 September 2003. The directors are often 'requested' to appoint a receiver and, in the best cases, the bank and receiver will work together to save a company where the directors are not managing the business properly. In many cases, however, the net result is closure of the company and sale of assets to protect the position of secured creditors.

Creditors' Voluntary Liquidation

This is the most common form of director led liquidation in use in the UK. Usually the company has run out of cash, cannot pay its debts on time and the directors are concerned that the business is simply not viable. They choose to stop trading and close the business. Liquidators then deal with the remains of the business.

The liquidator has four main tasks:

- To convert the assets of the business into cash.
- To adjudicate the claims of the creditors (work out how much is owed by the company).
- To report on the conduct of the officers of the company (directors and shadow directors).
- To make payments, where possible, to creditors in order of priority.

Compulsory Liquidation

This course of action – to be avoided by directors – occurs where a creditor has pursued the debts due to it for a significant period and has exhausted all other avenues of recovery. The creditor then instructs a solicitor or debt collector to collect the debt and, if this should fail, follows up with an action through the courts to wind the company up.

This mechanism is used most by HM Revenue & Customs – because their exposure from continued trading increases the risk to the Crown. If the Crown winds up a company, the liquidator is court appointed and will investigate very carefully the actions of the officers of the company. If it can be proven that they have not traded in accordance with their specified duties, it is possible that action will be taken against them.

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