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Newman & Partners

Licensed Insolvency Practitioners

FOCUS ON INSOLVENCY BULLETIN

Welcome to the latest issue of our Focus on Insolvency bulletin, designed to keep you up-to-date on insolvency matters that may be of interest to you. If you have any feedback on this bulletin, or would like to know more about our services or how we can help you, please contact us on **020 8357 2727** or at **insolvency@newmanandpartners.co.uk**

Insolvency and wrongful trading

In an ideal world, it is the professional adviser who gets to hear early on about the financial problems a client is facing. It can often be the conversation with the adviser and subsequent advice that changes the future for the client entirely.

Quite often, directors do not know what to do when their company is experiencing financial difficulties. The first step is to identify whether the client company is insolvent and this is usually the easiest step. There are two tests: the cash flow test (is the company unable to pay its debts as and when they fall due?) and the balance sheet test (are the company's liabilities greater than its assets?). The company has only to 'pass' one of those tests to be insolvent.

If the company is insolvent, the directors have an increased responsibility to guide the organisation through its troubles, either by turning it around or appointing an insolvency practitioner to assist. Getting this stage wrong can be devastating for the creditors, the company and the other stakeholders, such as employees.

Wrongful trading is an offence that a director can commit if they knew or ought to have known the company was insolvent and then proceeded to worsen the position for creditors before the company enters into a formal insolvency procedure. The director can be personally liable for the increase in the loss to creditors, and they will find it difficult to say that they did not know the company was insolvent after they have sought advice from their professional advisers.

Disqualification as a director could follow.

That is not to say that trading on may not be the right option. If trading remains profitable and the losses continue to be reduced by doing so, it may be worth considering. The directors must understand the risk and their responsibilities in continuing to trade. If a decision to keep trading is made, the director must note in writing their decision to increase any liabilities and justify why creditors will not lose out in the longer term. If the contract is particularly profitable and liability to creditors is reduced from the proceeds, then a wrongful trading accusation is unlikely.

The right advice from the professional adviser at times like this can make all the difference. At Newman & Partners Insolvency, we combine a wealth of specialist knowledge and experience with being able to offer a broad range of solutions, so we can provide expert guidance on the best way forward.

Please contact us for more information and guidance.

The core team at Newman & Partners: Laurence Factor (left), Rona Bharania (centre) and Ben Salem (right)

It is preferable to pay

When a company is insolvent, one of the issues that can often catch directors out is preferring one creditor above another, causing problems for themselves and the creditor concerned should the company go into some sort of insolvency procedure.

A preference occurs when something is done to someone which, in the event of the company going into insolvent liquidation, will put them in a better position than the position that they would have been in had that thing not been done.

That, in itself, could mean any payment made in the lead up to a liquidation.

However, in addition to the above, there has to be a desire to prefer.

So, a director may be looking to trade the business out of trouble. However, a winding up petition arrives and the director decides to pay that creditor before anyone else. There appears no desire as such, just a commercial imperative. If the company is going to survive and trade out of a poor position, it cannot be wound up. In this instance, it may not be deemed to be a preference payment.

Proving desire can sometimes be difficult. However, if the person receiving the benefit is a connected party (or even the director himself or herself), desire is presumed, albeit rebuttable, meaning that it is a "guilty until proven innocent" issue.

Note that the law does not refer to a payment either, just "something done". So, if a creditor is not connected, but the director has given a personal guarantee and that creditor receives payment in full before any other creditor, something has been done to put the director in a better position than they were previously.

The big issue for directors at a time of financial crisis is sometimes the amounts owed to them personally. These sums can often be significantly more than those outstanding to the general body of creditors. However, if these sums are repaid, it may well be deemed a preference.

In such circumstances, it is best to go and seek advice from the professionals. At Newman & Partners Insolvency, we can provide timely advice right from the first signs of financial distress to ensure directors take the correct and necessary actions.

For more information and guidance, please contact us.

Insolvency rules must be obeyed

With news that two more company directors have been struck off and banned for six and 12 years respectively from acting as directors, individuals should be aware of their responsibilities in the case of insolvency.

The Insolvency Service investigated the case of one company director, who was banned from running a company for 12 years after being found guilty of laundering cheques for rogue builders, as well as taking a cheque (to be cashed) from a member of the public, with the payment not being honoured, after the company had become insolvent.

Meanwhile, a second director was disqualified from acting as a director for six years after an investigation found that she had made payments to herself and a company consultant, who was a friend, despite knowing that the company was insolvent.

David Brooks, Chief Examiner at the Insolvency Service, said that there is no place in the business community for individuals who act in this manner and that disqualification will remove their ability to trade through a limited liability company.

Under company law, wrongful trading occurs when the directors of a company have continued to trade a company past the point when they knew, or ought to have concluded, that there was no reasonable prospect of avoiding insolvent liquidation and they did not take every step with a view to minimising the potential loss to the company's creditors.

In the case of the second director, she was specifically warned at least twice not to pay herself ahead of other creditors, and when her firm finally collapsed, it owed unsecured creditors almost £400,000.

These examples show that directors who act improperly can face serious repercussions. Directors who allow their companies to trade whilst insolvent risk becoming personally liable for company debts, as well as being disqualified from running a company.

Newman & Partners Insolvency can provide specialist advice on directors' responsibilities as well as on all aspects of insolvency, including winding up the business to achieve maximum value and return for creditors.

For more information, please contact us.

Newman & Partners Insolvency
Lynwood House
373/375 Station Road
Harrow
Middlesex HA1 2AW

T: 020 8357 2727
F: 020 8357 2027

E: insolvency@newmanandpartners.co.uk
W: www.newmanandpartners.co.uk

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