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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**

Financial difficulties faced by charitable companies

Some of you may act as accountants or auditors of incorporated or unincorporated charities, and this article may therefore be of interest.

There has been talk of economic recovery since the start of 2014. Unfortunately, this recovery has not reached everyone. Donations to charities remain low and with costs already cut as far as possible, some charities face the threat of insolvency.

In times of financial difficulty it can be hard for trustees to know exactly what action to take and when; although it is important to remember that in matters of insolvency, trustees - as directors of charitable companies - will be judged by the same standards as those that apply outside the charitable sector and they can be found personally liable in certain cases.

Insolvency can often be avoided by increasing revenue or cutting costs, but for many charities little more can be done that has not already been tried. One option is, if the charity's constitution permits, to apply for a loan. If loans are taken out and the charity is still unable to avoid insolvency then the trustees could be held personally liable for wrongful trading. Like any business, charities must have a very clear, rational and plausible plan for recovery before they borrow to implement it.

If financial recovery cannot be effected by borrowing, sometimes costs can be cut. The extent to which savings can be made will vary, but few charities can reduce their costs to zero, and with ongoing costs, trustees need to pay particular attention to their duties and the risks which come with insolvency.

In matters of insolvency, charitable companies are treated no differently from non-charitable companies. The Insolvency Act 1986 refers to a company being "unable to pay debts" which occur when:

- it is unable to pay its debts as they fall due (the cashflow test), or;
- the value of its assets is less than the amount of its liabilities, taking into account its contingent and prospective liabilities (the balance sheet test)

If the company cannot pay its debts as they fall due, then the test is failed.

If a charitable company might be insolvent, trustees should consider whether or not they have a plan which gives the company a reasonable prospect of being restored to financial health. Where a charitable company is in serious financial difficulty, the interests of the charity's creditors are paramount. The temptation to continue to operate through difficult times should be resisted unless there is a viable plan to avoid insolvency which has been reviewed and approved by independent advisers like Newman and Partners Insolvency. For more information, please contact us.

Director duties and responsibilities for individuals who are trading insolvent

If a company is unable to meet its financial obligations and/or its liabilities exceed its assets, then it is operating in a state of insolvency. A director of a company that is trading insolvently has specific duties and legal responsibilities.

Failure to uphold these responsibilities could mean that the director may be accused of wrongful trading or misfeasance and held personally liable to reimburse the company. After a company is deemed legally insolvent the director is required to act in the best interests of creditors, beginning a formal procedure that will result in the repayment of as many of its outstanding debts as possible.

If a creditor has served an official notice (statutory demand) requiring payment of a debt for more than £750 and payment is not made within 21 days, the creditor can take you to court and have your company wound up. However, taking action to show that you are making an attempt to satisfy creditors can often be enough to postpone or avoid the demise of the company. If you cannot demonstrate action in the best interests of creditors, a director could, under certain circumstances, be personally liable.

Where possible, directors should avoid paying some creditors, but not others.

Although it may be difficult to act within your responsibilities as the director of an insolvent company, with the right independent advice from an insolvency practitioner such as Newman and Partners, personal liability may be avoided and a positive outcome reached. For more information, please contact us.

Post-liquidation transfers

Following the making of a winding up order, the powers of the directors cease. In the case of Park Associated Developments Limited (Park) (in liquidation) and Another v Kinnear and Another, the question of what happens to land which the directors have supposedly transferred following the making of a winding up order, is explored.

In this case, after the winding up order had been made, transfers of four plots of land were made to two directors. Although transfer documents recorded that £190,000 was payable to Park for the plots, evidence suggested that only £114,000 was actually paid (to a third party which held a charge over the plots so the balance on £190,000 was still outstanding). Despite this, the directors had registered the plot transfers with HM Land Registry and become proprietors of the plots. One plot was sold and the other three retained by the directors.

The Liquidator bringing proceedings on behalf of Park claimed entitlement to the three retained plots (asking that they be transferred back to Park since transfer to the directors was void) and to the £200,000 proceeds from the single plot sale. Following a request for summary judgement, the judge ordered that Park be registered as proprietor at HM Land Registry (but refused to decide the issue of repayment for the remaining plots).

Directors should be aware that after a winding up order is made, they do not have the power to bind the company and therefore should not be making transfers or disposing of any assets. If assets have been disposed of in the lead up to liquidation, or, as in the case of Park, after the company has already gone into liquidation, it can prove difficult to work out transfer details and even more complex where land is involved due to the registration of the transferee as proprietor at HM Land Registry.

This case shows that, where the transfer is a nullity, the land register can be amended to reflect the legal position. For more information about liquidation and purported transfers by directors, please contact us.

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The matters discussed in this bulletin are by necessity brief and comprise summations and introductions to the subject referred to. The content of this bulletin should not be considered by any reader to comprise full proper legal advice and should not be relied upon.