

# Newman & Partners

Licensed Insolvency Practitioners

## RECOVERY & REVIVAL BULLETIN

Welcome to the latest issue of our Recovery and Revival 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](mailto:insolvency@newmanandpartners.co.uk)

### Where do professional service firms come in the hierarchy of payments?

When your client is facing insolvency, it's important that they understand the hierarchy of payments, which dictates the order in which debts should be settled. This hierarchy ensures that the available funds are allocated fairly and legally, but we often get questions from accountants as to where they sit on the list.

Similarly, other professional service firms – like solicitors and financial advisers – have their own place. Here's a quick breakdown of the hierarchy:

- 1. Secured creditors:** These creditors have the first claim on the company's assets. Secured creditors typically hold a charge over the company's assets, such as property or equipment.
- 2. The insolvency practitioner:** Including payment of his/her disbursements, e.g. legal fees.
- 3. Preferential creditors:** These include employees who are owed wages, holiday pay, and pension contributions.
- 4. Unsecured creditors:** These creditors do not have any secured claim on the company's assets. Professional service fees, unless specifically secured, fall into this category.
- 5. Shareholders:** Shareholders are typically the last to be paid.

It is crucial to advise your clients that payments to solicitors or accountants should not precede the obligations to preferential and secured creditors.

It's equally important that your client does not pay off shareholders before settling their obligations to creditors.

#### Ensuring compliance

When advising your clients on paying professional services during insolvency, remember that the IP will help you ensure compliance with legal and regulatory requirements. They'll have a thorough understanding of the relevant laws and regulations governing insolvency and creditor payments.

The *Insolvency Act 1986* provides a comprehensive legal framework for to work from and consult. They'll ensure that your clients adhere

to the provisions outlined in this Act, particularly regarding the payment hierarchy of various types of creditors.

Similarly, the *Insolvency Rules 2016* supplement the Insolvency Act 1986 and provide detailed procedural guidance so it might be worth familiarising yourself with both pieces of legislation in case your clients ask about them.

The IP will closely follow the anti-preferential treatment regulations when making payments on your client's behalf. This is important as the law prohibits preferential treatment of creditors, and paying professional services before secured or preferential creditors can be construed as preferential treatment. This could potentially lead to legal consequences for both the directors and the company.



You and your client should consult with an IP who will then make any necessary payments to ensure they comply with the legal and procedural requirements. Your IP can explain to your client how they are managing creditor payments and avoiding preferential treatment issues. Essentially, it is the responsibility of the IP to comply with the rules that determine the order of payments.

Best practices for navigating professional service payments  
Your IP will do the following for you:

- Pay creditors according to the hierarchy of payments.
- Ensure your client maintains compliance during the process.
- Communicate with your client regarding payments.


However, we also recommend you implement the following best practices to ensure that the IP can successfully fulfil their role:

- **Maintain detailed documentation:** Encourage your clients to maintain meticulous records of all transactions. This should include invoices, payment receipts, and correspondence with solicitors and accountants. As you know, proper documentation supports transparency and accountability.

- **Consult the IP:** Create a clear line of communication between the two firms so that any records can be shared quickly and efficiently. Encourage your client to do the same.
- **Communicate with creditors:** Encourage open communication with all creditors, service providers. Transparently explaining the insolvency situation and the payment plan (with the help of the IP) can foster cooperation and understanding, potentially easing the process for all parties involved.

By following these guidelines, you can provide your clients and the appointed IP with the necessary support to manage payments to professional services during insolvency effectively and compliantly.

The advice you'll receive from an IP will be invaluable throughout the insolvency process. It can not be overstated how important communicating with an IP can be for maintaining compliance and ensuring that professional services are properly reimbursed for work provided to your client.

 We are happy to advise on the subject, so please get in touch with our team on **020 8357 2727** or email: [insolvency@newmanandpartners.co.uk](mailto:insolvency@newmanandpartners.co.uk)

## How to use CVAs to avoid liquidation

**A Company Voluntary Arrangement (CVA) is a powerful tool that can help businesses avoid liquidation by allowing them to negotiate with their creditors. They are a legally binding agreement between a company and its creditors to pay back debts over a set period, usually between three and five years. This arrangement provides a lifeline to companies struggling with cash flow, enabling them to continue trading while repaying their debts.**

To initiate a CVA, the company – with the help of an Insolvency Practitioner (IP) – must propose the arrangement to its creditors. This proposal outlines the repayment plan and any changes to the company's operations. It requires approval from 75 per cent (by value) of the creditors who vote on the proposal.

If approved, the CVA binds all creditors who were entitled to vote, even if they did not vote or voted against the proposal. This ensures a unified approach to debt repayment, giving the company enough breathing space to reorganise and recover.

The IP will manage this on the company's behalf, if approved. However, it is not a one-size-fits-all solution, and in some cases, liquidation might be the best option for your client. An IP will be able to help you determine if this is the best choice.

### Key benefits of CVAs

When advising your clients, we recommend you highlight the key benefits of CVAs in comparison to liquidation. First and foremost, a CVA allows the company to continue trading, preserving jobs and maintaining customer relationships. This continuity is often crucial for the long-term success of the business. By avoiding liquidation, the company retains control of its assets and operations, which can be a significant advantage over other insolvency procedures such as administration or receivership.

Secondly, a CVA can improve cash flow as the repayment plan typically reduces the immediate financial burden on the company, allowing it to allocate resources more effectively and invest in growth opportunities. CVA can also halt legal actions from creditors, providing the company with the stability needed to implement its recovery plan without the constant threat of winding-up petitions or enforcement actions.

Finally, a CVA can protect the company's reputation as liquidation often carries a stigma that can damage the company's brand and customer and supplier confidence. By successfully negotiating a CVA, the company demonstrates its commitment to repaying its debts and securing its future, which can enhance its market standing.

### CVAs: Not a one-size-fits-all solution

While CVAs do indeed have many benefits, it should be noted that they are not a solution that fits every business. This should be determined with the guidance and evaluation of a qualified and experienced IP.

Sometimes, liquidation is the best move for your client and entering a CVA can have a net negative impact on the business and only prolong the inevitable. Liquidation can provide a clear and definitive resolution, allowing stakeholders to move forward without the ongoing uncertainty that a struggling business might create. It can also ensure that the remaining assets are distributed in an orderly manner, in accordance with the legal hierarchy of payments, potentially maximising the returns for creditors.

### Advising clients on implementing CVAs

When a client approaches you with concerns regarding a potential liquidation, your role is to guide them through the CVA process and help them understand its implications. The first step is to assess the company's financial situation thoroughly. This involves analysing cash flow, debt levels, and operational performance to determine whether a CVA is a viable option. If so, you should work with an IP to develop a robust proposal that addresses the concerns of creditors while being realistic about the company's ability to repay its debts.

A licensed IP will oversee the CVA process and advise your client on the best course of action. The IP will help prepare the proposal, communicate with creditors, and manage the voting process – administering the whole procedure for you and your client.

It is crucial to choose an IP with experience in CVAs and a good track record of successful arrangements – like us. Throughout the CVA process, you should maintain transparent communication with creditors and encourage your client to engage proactively, explaining the company's situation and the benefits of the proposed arrangement through their IP.

 Call our team on **020 8357 2727** or email: [insolvency@newmanandpartners.co.uk](mailto:insolvency@newmanandpartners.co.uk)

# Trading misfeasance explained and strategies to mitigate it

Trading misfeasance is where directors or company officers breach their fiduciary duties, resulting in financial harm to creditors during the period leading up to insolvency. It involves actions such as wrongful trading, where directors continue to trade despite knowing the company is insolvent, or fraudulent trading, where there is an intent to defraud creditors.

Specifically, under the *Insolvency Act 1986*, misfeasance includes:

- **Wrongful trading (Section 214):** Directors knowingly continue trading when they should be aware that there is no reasonable prospect of avoiding insolvent liquidation.
- **Fraudulent trading (Section 213):** Directors engage in business with the intention of defrauding creditors.
- **Breach of fiduciary duties:** Directors fail to act in the best interests of the company and its creditors.

As you might imagine, the consequences of such trading can be severe both for the individual and the business itself. For example, in the case of the collapsed department store BHS, two directors were recently ordered to pay at least £18 million after they were found liable for wrongful trading.

## Key strategies to mitigate trading misfeasance


To mitigate the risk of trading misfeasance, there are several strategies that we often advise accountants to implement and advise their clients on:

- **Conduct regular financial reviews:** Encourage your clients to perform regular financial reviews to assess the company's solvency status. These reviews should include detailed cash flow forecasts, profit and loss statements, and balance sheets. Early identification of financial distress can help take corrective actions before it escalates to insolvency.
- **Maintain accurate and up-to-date records:** Accurate record-keeping is essential for demonstrating that directors have acted responsibly. Ensure that your clients maintain comprehensive records of all financial transactions, board meeting minutes, and key decisions. This documentation can serve as evidence that directors have taken appropriate steps to mitigate financial risks.
- **Seek professional advice early:** Advise your clients to seek professional advice at the first sign of financial trouble. Engaging with insolvency practitioners, accountants and legal advisors can provide crucial guidance on navigating financial distress. Early intervention can prevent actions that may later be deemed wrongful or fraudulent trading.

- **Implement a robust risk management framework:** Encourage your clients to develop and implement a risk management framework tailored to their business. This framework should include regular risk assessments, internal controls, and procedures for identifying and addressing potential financial risks. A proactive approach to risk management can help mitigate the chances of trading misfeasance.
- **Ensure compliance with fiduciary duties:** Directors must understand their fiduciary duties and the legal obligations they have towards the company and its creditors. Provide training and resources to help directors stay informed about their responsibilities. Emphasise the importance of acting in the best interests of the company and its creditors, especially during times of financial distress.
- **Monitor and control trading activities:** Encourage your clients to closely monitor trading activities, especially when the company is facing financial difficulties. Implementing strict controls on spending, credit management, and debt collection can help manage cash flow and prevent exacerbating the financial situation.
- **Develop a contingency plan:** Advise your clients to develop a contingency plan for potential insolvency scenarios. This plan should outline steps to be taken in the event of financial distress, including communication with creditors, potential restructuring options, and procedures for entering formal insolvency processes. A well-prepared contingency plan can facilitate a smoother transition and minimise the risk of misfeasance.

We also encourage your clients to engage with an IP when developing their contingency plan. An experienced practitioner can provide valuable insights and advice tailored to their specific situation, ensuring that all potential risks are adequately addressed.

This proactive step can significantly enhance their preparedness and ability to handle financial distress effectively. On top of this, it also gives you a great lifeline of advice and guidance on how to advise your clients.

 For more information or assistance with your clients' compliance, call our team on **020 8357 2727** or email: [insolvency@newmanandpartners.co.uk](mailto:insolvency@newmanandpartners.co.uk)

CAREFUL CONSIDERATION IS NEEDED BEFORE TAKING OUT ANY FORM OF FINANCE AND SPECIALIST ADVICE SHOULD BE SOUGHT. IF YOU HAVE ANY QUESTIONS, PLEASE CONTACT US.

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