



**KSA Group Turnaround Programmes™**

**KSA Group's Complete Expert Guide to**

**Turning Around or Restructuring Your Struggling or  
Insolvent Recruitment Company**

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**Welcome to KSA Group's Expert Guide to Turning Around, Rescuing or Restructuring Your Recruitment Company - written by Keith Steven, Managing Director.**

Keith has been turning companies around since 1994. He has been involved with hundreds of companies and SME businesses in that time, all facing insolvency, closure and bad debts.

Keith has been a non-executive director of several recruitment companies and has rescued many recruitment firms during the last 20 years of turnaround work.

Keith is an expert in innovative turnaround and insolvency techniques. With a national team of 25 turnaround specialists, KSA can quickly identify solutions and drive recovery for struggling recruitment companies.

Current problems for recruitment businesses:

1. Struggling to cut costs to match lower demand after the recession.
2. Cash flow crisis brought on by falling revenues and falling sales.
3. Slower payment by debtors.
4. Hiring bans by larger clients.
5. Highly leveraged debtor books through factoring companies.
6. HM Revenue & Customs debts and falling further behind with them. Legacy debts of a larger business being serviced by a now, smaller business.
7. Retention of quality recruitment consultants.
8. Finally, OVERDRAWN DIRECTORS CURRENT ACCOUNTS!

Are these familiar to you? If so read on for solutions that will fix or help you fix them and get you back in control of your recruitment company.

## **This is only a general guide so:**

We have set out this guide to be as user-friendly as possible, but please remember whenever you have questions you can email them to us for a quick answer. We will answer all questions during our office hours of 8.30 to 6pm, 5 days a week. This email support service is FREE.

[info@ksagroup.co.uk](mailto:info@ksagroup.co.uk)

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### Links Note:

This PDF is rich in hypertext links. By holding down CTRL and clicking with your mouse you will open a web browser and link to our main website (100% safe). Of course, if you read this in paper form the links are not live!

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## **Introduction to this Guide**

### **Are You A Recruitment Company Director?**

Well, as we all know, there are many thousands of things that can go wrong in a business but always remember this. YOUR recruitment business generates economic activity, employment and value added for the local and national economies.

If you started the business or are the sole director or directors, you will know that it is a lonely profession, being an entrepreneur or struggling MD! Well done you, great job, now let's fix your company's problems or even its insolvency.

If you are a director of a larger or more established concern, then you will know just how critical the business is to its employees, its suppliers and its employees. We deal with companies of all sizes and we know that all directors worry!

KSA has turned around recruitment companies from just under £300,000 sales to £120m so we know what the problems are. Make sure you read this guide and visit [www.companyrescue.co.uk](http://www.companyrescue.co.uk) BEFORE making any decisions on the options available.

### **Professional Advisor? Think of these Benefits.**

If you are a professional advisor to a struggling recruitment company, why not read this guide and learn how to SAVE YOUR CLIENTS. What is the point in passing the client to a firm of ordinary insolvency practitioners that will simply bury it? This programme could lead to improved cashflow, new billable time for your practice and the retention of long-standing clients.

### **KSA Group– Our aim is to Rescue Viable Businesses!**

We help many thousands of people every year, they run different and diverse businesses. Most are fantastically hard working, many are innovative and creative, others are great with numbers or processes, and still more are great leaders. BUT all of the people we work with and help share ONE COMMON TRAIT: The Emotional Roller Coaster of insolvency.

So it makes a lot of sense to protect your hard work, your monetary and time investment and your future by cutting costs, getting rid of surplus people.

**SO**, let's start with a well used turnaround phrase, "You are where you are". There is no time for blame or recrimination, it's all about one thing now.....

## **FOCUS ON SAVING YOUR RECRUITMENT BUSINESS**

***"Running a recruitment business that's approaching insolvency, or that's actually insolvent is an emotional roller coaster; there are good days and bad, great successes and depressing failures.***

***Placements fall down, candidates foul up, client's pull long term contracts.***

***Remember, although you have fought many battles before on your own, now you have the UK's leading Company Rescue firm on your side and we know what you're going through"!***

*Keith Steven KSA Group; September 2019.*

## **What are the Definitions of Insolvency?**

You may think that having a cashflow problem in your company is not the same thing as being insolvent, or the business is not at risk so why do I need to focus on saving it?

The UK insolvency law is built around the Insolvency Act 1986, Enterprise Act 2002, The Company Directors Disqualification Act 1986, and many examples of case law

and practical application, through case law. So, there is lots of law about! Plus all of this is regulated by the Government, regulatory bodies and committees.

It is vitally important to understand that, if the business is insolvent, this results in a shift in the director's duty of care from acting in the best interests of the shareholders, to ***acting in the best interests of the creditors' or ensuring that the creditors position is maximised.***

If your recruitment company IS INSOLVENT whatever you do from now on you must act to maximise creditors' interest, that's the law. That usually does not HAVE to mean stopping trading. Clearly, if stopping trading was a serious option or your preferred route, then you may not have downloaded this programme!

So, although maximising creditors' interests is paramount, it can have the added benefit of rescuing the company too.

Just to aid your understanding please now read the following definitions of insolvency:

### **There are three methods to determine insolvency:**

#### **The Cashflow Test**

Simply - can the company pay its debts when they fall due for payment?

For example, if you are not paying the tax deductions from employees for PAYE and NIC across to the HMRC on the 19th of the month following the month they were deducted, then the company could be insolvent.

If your trade creditors, for example bulletin boards and marketing consultants, sell to you on say 30 days terms and you regularly pay on 90-120 days, then the company could be insolvent.

[A director has a legal requirement](#) to understand this issue. If he or she believes that the company has insufficient cash to pay its liabilities on time then they must take advice/action.

## The Balance Sheet Test

Simply – does your company owe more than it owns as a company or are the company's assets exceeded by its liabilities? If yes, then the company could be insolvent.

It is important to point out that this test should include contingent or prospective liabilities. (If you need advice on these issues [email us](#)).

Many directors tell us that on a balance sheet test the company is not insolvent therefore they do not need to act. However, under the cashflow test above the company may still be insolvent. So, you must act if it is.

In our experience an apparently solvent balance sheet may include items that are overstated, such as doubtful debtors that are not really collectable. After deducting these items, many balance sheets become insolvent. So be prudent - you are legally required to present accounts to show a true and fair picture of the business.

## Legal Action Test

If a creditor such as HMRC has obtained a [County Court Judgment](#), this may demonstrate the company's insolvency and the creditor may petition to wind up the company. ([See compulsory liquidation](#)).

If a creditor has obtained a [statutory demand](#) for greater than £750 and it remains unpaid for more than 21 days, then the creditor may petition to wind up the company.

A creditor can also issue a winding up petition WITHOUT issuing a Statutory Demand, so they can go straight for the "jugular". If a winding up threat has been made contact us without delay, we can defeat petitions if a viable rescue is put together quickly.

## Summary

If you believe that any of the above tests are positive for your business, it is vital that you and the board of directors take action to address the insolvent position. However, don't panic, look carefully at all pertinent issues and consider the rest of this guide.



Remember, if the company is insolvent you must act to maximise creditors' interests. **If there is no reasonable prospect of the following options happening:**

- ▶ New or additional capital or finance being introduced to the business to return the balance sheet to a solvent position or to remove the cashflow pressures.
- ▶ A sale or acquisition of the company.
- ▶ A company voluntary arrangement or [administration](#).

Then the directors may be accused of [wrongful trading](#). If you are worried about this or your accountant has said he/she is concerned, then look carefully at [directors' disqualification](#).

So, if the company is insolvent you must act to MAXIMISE CREDITORS INTERESTS. Failure to do so could lead to personal liability!

## **How Do Recruitment Companies Get into Difficulty?**

First, a blunt truism. Setting up and running a recruitment company is relatively straight forward in comparison to setting up, say, a manufacturing or High-Tech company, fact.

So, in my fairly broad recruitment company experience, people start recruitment companies and don't worry too much about company accounts, tax compliance, business planning, monthly reports and regular board meetings. This is a common failing.

### **I would say think of the old adage - fail to plan is plan to fail!**

More importantly, HMRC sees lack of tax reporting and compliance as something that needs to be stopped. So, if you are relaxed about reporting and compliance with tax rules, don't be surprised if HMRC's attitude to you is blunt.

Many recruitment companies have grown quite well beyond the "kitchen table", but many still keep that "mom and pop" shop feeling to drive an informal, staff friendly working environment. First big mistake.

This is a business not a hobby, not a friendly gathering every day followed by drinks in the pub. I know, having been a director of a London based recruitment company that, needless to say I didn't recognise this culture till the first board meeting which concluded in the pub in Covent Garden, London. A couple of bottles of wine and the directors seemed to ignore my advice.

If you have started, or are running a company like that, then either change or fail! Not sour grapes, again fact.

As above KSA Group sees many of the problems below, repeated day after day.

### **Current problems for recruitment businesses:**

1. Struggling to control costs while trying to meet increased demand. How do you get rid of the overheads, how do you cut staff costs? Redundancy is expensive; landlords are often intractable, unless you are based in a flexible serviced office.

2. **Cashflow crisis brought on by falling revenues and falling sales. Having been a larger business with much higher costs, you can find yourself with "LEGACY DEBTS", from that period. How can 10 consultants service the legacy debts built up when the business had 25 consultants? Or any numeric equivalent.**
3. Slower payment by debtors. Look everyone is trying to preserve cash, so are you. When debtors take longer to pay this drives cash flow down. You should definitely be running a daily cash flow forecast to ensure that you are aware when cash flow holes are looming. Please email [info@ksagroup.co.uk](mailto:info@ksagroup.co.uk) for a free easy to use daily cash flow.
4. Hiring bans by larger clients. Fewer temps required. That dreaded phone call, "we don't need any more recruits or temps for a while give me a call in 3 or 6 months". This can hammer projections, KPI's and CASHFLOW. With your cash flow, do "what-if" planning and see what would happen if your larger clients failed to pay you in 30 days and unilaterally moved to 60 days?
5. Highly leveraged debtor books through factoring companies. When sales are flat or rising factoring or invoice discounting is a brilliant financial product. When sales are falling it's not so good. A wall of debt has to be serviced and draw downs and cash collections from factoring have fallen. Double whammy time. We often see companies paying premiums to get over advances against their debtor book. In really bad cases we see "fresh air invoicing". This is based on the notion that "John will definitely be starting at Clientco so let's invoice a week/fortnight/month early, and then we can draw down from the factoring company"!!
6. HM Revenue & Customs debts and falling further behind with. The "de facto bank of choice" for recruitment companies, is what I call the HMRC! As directors we are supposed to pay PAYE on the 19<sup>th</sup> of the month and VAT at the quarter ends. The day comes when the cash won't meet that payment profile and the company starts to borrow from the "Crown" creditors. Coupled with fresh air invoicing you have a toxic mix and one that can lead to meltdown very rapidly.

7. Retention of quality recruitment consultants. Or you may be hanging on to consultants in the hope that a turnaround is just around the corner and he /she has lots of possible placements. I like optimism, but it could be misplaced loyalty or optimism based on naivety – if sales are not happening costs MUST be cut.
8. Finally, [OVERDRAWN DIRECTORS CURRENT ACCOUNTS!](#) This is when you have taken money every month and it has not gone through the PAYE scheme. Its tax efficient says your accountant, and true, dividend tax is much lower than income tax for high earners. BUT, when something happens and profits fall or losses are made you end up unable to pay dividends to cover the drawings, result? An Overdrawn Directors Current Account.

**This means YOU and your other directors OWE the company money as DEBTORS. If the company enters insolvency you will be forced to pay some or all of that back to the liquidator or administrator.**

**KSA's Cost Cutting Guide for companies needing to survive a downturn in sales.**

**[Our TOP 20 Cost Saving Rules and Cashflow Tips for SME's](#)**

1. You should set up a daily cashflow to control all cash in and out. This may protect you from wrongful trading, as it helps manage cash and stops bounced cheques. If you don't have a daily cashflow forecast call KSA Group and we will email you it free of charge.
  - 1.1. PS don't bounce cheques its bad form! Oh and its possibly a fraud if you meant to!
2. All purchases are approved by you as MD/FD/Operations director/Owner. You should sign all cheques or approve all BACS/CHAPS payments in writing.
3. No purchases are approved unless signed by you, which will make "them" produce a purchase order. Then you can check if they are doing their job, is the price fair, are they and your supplier ripping you off, or are they just lazy and not getting the business best value?
4. No petty cash is drawn from the bank unless you personally go and get it... makes you question what every pound is spent on when people ask for cash won't it? By the way you get out of the grind and time to think.
  - 4.1. If not possible because your business is too big, why not make a trusted person do it. NOT a big issue if cash is king?
5. Review all expenses claims by the staff; reject all that are not really necessary. If you get complaints or murmurings (they may be too scared to act professionally and debate with you), then meet with them and explain the position. BLUNTLY, tell them survival is now the main aim.
6. Remember survival is KEY, if you lose people or profits that's not vital, CASH IS KING for now. Profits will soon flow from very tight cashflow management. If people sue for unfair dismissal, call us we can help, we may be able to kill off their claims with straight talking. Or perhaps a CVA can kill these claims too.
7. Ask every supplier for a review of their prices, can they cut you a better deal? Ask them to for a few extra weeks payment grace. They may object but they will welcome smart business people staying in business. That's better from a creditor's point of view than people putting heads in the sand!
8. Ask the landlord for a breather on rent. Can you please pay monthly not quarterly for a while? This helps cashflow. It actually puts you in arrears but that's maybe ok at this stage. AGAIN they want a paying tenant not an Ostrich who won't talk!
9. Ask your accountants to accept monthly payments. If your accountancy fee is £10,000pa then ask to pay over say 10 months that's £1,000 per month. The same applies for anyone else that issues a big annual fee note.

**10. MANAGE cash EVERY DAY! Did you do that yet!**

11. Get someone else's view; do you have a trusted friend? If so talk to them about your business, actions and get them to sanity check you. They may suggest cost savings, test your closeted vies and make you think.
12. Do you need that company car; can you use your own and give it back?
13. Can you sell any assets, will it raise cash? Make sure they're not owned by a leasing company first.
14. Ask your factors to cut their costs, only drawdown weekly. Using your daily Cashflow model will of course help in this. This can save hundreds of pounds a week.
15. Cut ALL overtime to the bone, why do you need it? Is your production planning so poor or weak? If you need more people hire them, at lower rates.
16. If you need to make redundancies and cannot afford them, use the DBIS (ex DTI) Hardship Scheme. Call us for help.
17. Did we say "**Manage cash EVERY DAY**".
18. Use the internet to buy or price everything; you can get fantastic value over the net.
19. Work all hours, to build the recovery plan and set out the Time To Pay Deals with TAX AND VAT.
20. KEEP MINUTES or notes OF ALL DECISIONS. If you're a partnership or sole trader KEEP NOTES. This will help protect YOU. We can help, talk to the experts now.
21. Finally (I know this is 21), be aware that people will be less organised than you, for goodness sake, if a customer is not paying find out why!

## Is My Company Viable for a Turnaround?

### GUIDE TO ESTABLISHING BUSINESS VIABILITY

#### 1. Work out cashflow

- 1.1. If you want a daily cashflow model to help you work out your business email us or visit [www.companyrescue.co.uk](http://www.companyrescue.co.uk)
- 1.2. This will help you lay out the next 90 days of cashflow and see what the real cash position is. We use this for all of our clients. You should use it too!
- 1.3. Using a spreadsheet like the free model available from [www.companyrescue.co.uk](http://www.companyrescue.co.uk) plus VAT; enter all known receipts from your factor and all known payments out.
- 1.4. Put them in where you think they will be received (cleared funds!!!) and when payments need to be paid.
- 1.5. Enter bank position.
- 1.6. Work out the cashflow for the next 90 days.
- 1.7. So what does this say? You run out of cash? Or can you live within facilities if payments are pushed out a week or two? What if you move the PAYE and VAT out by a few months paying say a 6<sup>th</sup> each month? Can that work?
  - 1.7.1. If so click here for a [Time to Pay Guide programme](#)
- 1.8. Does the cashflow say it just cannot work?
  - 1.8.1. Don't panic! Now you have established cashflow that's a good start to working out the solutions.
  - 1.8.2. You can stretch out the cashflow to 6 months if that would be useful to you.
  - 1.8.3. Move onto the next step.

#### 2. Work out your Sales

- 2.1. Now let's look at sales, are they falling rising or flat?
- 2.2. If they're falling we know we need to work out if the company's costs are falling too. If not rising costs and falling sales are a real problem.
  - 2.2.1. If you need to cut costs, read the section on costs above.

- 2.3. If sales are falling, is this a marketing problem? See our marketing section online. Or get external advice on marketing. Do you have a marketing plan?
- 2.4. Can you increase sales, if so how? Is there a new product or service that you can sell/ how long will it take to get it selling. Do you need to spend money to get it to market? How much? Put that in the cashflow.
- 2.5. What about sales people, are they performing? Do you have a web presence? If so is it working for you?
- 2.6. Work out the best sales you can expect for each month for 6 months, and then work out the lowest. This is called sensitivity analysis
3. **Look at your margins:**
  - 3.1. Work them out carefully. Can you put prices up and improve margins. Can you buy better and get cheaper supplies?
  - 3.2. If you cut the margin would you sell more? Remember 10% cut in price equals a much bigger cut in margins!
4. **What are the fixed costs of the business?**
  - 4.1. These include rent, rates, utility bills insurances and so forth. Add them up and see how much you spend on each and all fixed costs.
  - 4.2. You need to have a enough gross margin each month to cover those costs
  - 4.3. Can you cut fixed costs like rents?
    - 4.3.1. If not is the property too big and would the business do better in smaller premises.
    - 4.3.2. Think about using a CVA to exit the property and terminating the lease.
    - 4.3.3. If you cannot cut fixed costs then you may be able to save money on variable costs or overheads.
5. **What are your overhead (or variable costs)?**
  - 5.1. These include people, travel, accounting, cars, electricity, consumables, stationery etc.
  - 5.2. Are these too high? Save a pound or two on all of these and you could make a huge difference to the business' net margins.
6. People – good, bad, remove or recruit?



7. Customers, have you got enough are they satisfied with your service/product?
8. Marketing: have you got a plan, how do you get to market, what's about the brand/ product and market?
9. Business Plan – have you got one? Marketing plan? Why not?
10. Decide to ACT!
  - 10.1. I have a Viable Business???
  - 10.2. I have an Unviable Business???
  - 10.3. I have a Viable Business but it needs Restructured???
11. If it is not viable think about [creditors voluntary liquidation](#). Call 0800 9700539 now for honest advice and to quickly get the liquidation under way.
12. If it is viable and you cannot decide whether CVA or Pre-Pack Administration is appropriate, we can offer a free face to face meeting to help you decide.

**Or just call KSA Group and we will start doing this for you. 0800 9700539**

## **What if our Recruitment Business is NOT insolvent? A Guide to Trading Out.**

A common sense way to trade out of cashflow problems.

This is a very common approach. You hit a problem that is not life threatening but you have serious cashflow difficulties, possibly Tax and VAT arrears and creditors shouting loudly. Following this guide and applying common sense may help you get out of that position.

First bit of good free advice: Beware, note down ALL ACTIONS, DECISIONS and keep replies and correspondence with creditors.

If the company has suffered a downturn in circumstances because of a finite set of issues and the business is not fundamentally weakened or about to fail, then this is a great solution. Including the largest companies, every business faces a cyclic cash flow problem. Measurement of success cannot be short term, but events dictate that every company will suffer at times.

### **A key element of this policy is honesty.**

Be honest with yourself, the employees and your creditors and your bank if you have any debts. Without this there is real risk that you will only make the current problems worse.

It is important that you carefully and honestly consider the problems facing the business. Ask yourself the following questions and gauge the answers:

1. Is this business viable? If you could remove the problems or the pressure does it have a real long term future?
2. Is money all it needs to sort the problems? Can you safely introduce new money, perhaps from your own sources?
3. Can you achieve sufficient sales, activity or momentum to cover your costs? We call this critical mass.
4. Have you cut all costs to the minimum efficient level?

5. If your activity does rise can you:
  - a) Fund it - working capital problems are just as acute for too many sales as too few!
  - b) Justify any further credit you may have to take - is there a reasonable prospect of repaying that credit? If not you may be risking wrongful trading.
6. Can you maintain the key people you need?
7. Are you able to provide your service at a price that the market can sustain?
8. Would it be better to close the business and look at other opportunities?
9. Have you got the fight in you to keep battling on without support?
10. Have you taken advice from professionals? If not talk to KSA Group's turnaround experts for guidance.
11. Have you involved the key partners in your business?
12. Are you fearful of taking decisions to close, restructure or sell the business and are seeking to trade out to defer that decision-making process?

If you now believe that the company HAS a future and that the problems are not insurmountable then read on.

Trading out can be a very effective tool if handled correctly. There are a number of ways to do this. The key is to achieve a breathing space for the company. This lifts cashflow pressure, right now CASH IS KING!

### **"Informal" deal:**

Merely calling the key creditors, explaining the position: you want to pay them back in full as fast as possible but cashflow is tight and can you pay them over an affordable timeframe, can work wonders. BUT do not do this without a planned approach. You must

1. Work out your cashflow - be realistic. If a debtor is due to pay your company in 30 days check whether they are happy with the invoice and goods, check when they think they will pay. Then add on 10 days at least for a safe margin.
2. Build a daily cashflow, if you cannot write spreadsheets use a simple form on a sheet of paper, but update every figure as you go.

Why not contact us for a free cashflow model designed by experts for just this purpose? [info@ksagroupco.uk](mailto:info@ksagroupco.uk)

3. Not over promise. If it looks like you can pay all key creditors in 30-60 days ask for 60-90 days. Creditors will usually be happy to work with you if you are honest.
4. Not break deals. But if it is unavoidable, write and call the creditors and explain carefully where the plan has not worked. Honesty is the key. It does not guarantee support but you must be straight.

### **"Formal" deal:**

This is not a formal insolvency deal such as a CVA. But the use of a professional turnaround practitioner can ensure that the "honest broker" effect achieves a workable deal. Once again the deal broker will want to see evidence that the directors have planned their recovery and looked long and hard at the business and its cashflow. Some creditors may even accept write-downs of debt if they think the company will survive and prosper long term.

A professional firm can often extract deals with creditors that the directors cannot. This is the trust element, creditors often lose faith with directors but will trust a professional firm. Try using your accountants, lawyers to broker deals.

Alternatively, KSA can provide this service, in certain circumstances. We would require detailed financial forecasts to be built to support the proposed deal. These can be produced by our expert forecasting team, clearly fees will be required for this work and of course, the deal brokerage.

## Tips

Don't wait until legal actions have been taken against the company to ask for a deal. Try to plan the cashflow of the business well in advance - you have a legal obligation to do this! If the directors do not think the company has sufficient cash to trade they should consider the obligations and options like CVA and plan a way forward. Worried about [legal actions](#)? Go to that page for more details.

Keep a log of all calls and take copies of all letters to creditors - that way you can check back.

Have a review meeting each week - if you are falling behind take action. Inform the creditors.

**If the plan is clearly not working consider the other options in this guide such as company voluntary arrangement (CVA), administration, trade sale and refinancing.**

Don't wait too long to get professional turnaround help. Often a CVA, for example, can remove the stress and allow you to get back to running the company, not the deals with creditors.

## **Trading Out - Frequently Asked Questions**

### **Q: The company is struggling, but not that insolvent, can I safely trade out by cutting staff and overheads?**

A: It is important that you read and understand the Insolvency test section on page 10 before going further. Even if the company is insolvent that does not mean a formal insolvency action is the right way forward.

If you can produce a recovery plan that is achievable and that maximises creditors interests, then this can be a good way forward. Many thousands of businesses do this every year and recover well. Our advice is to produce your plan, discuss it with your senior people and then embrace it.

During the course of the recovery stage, constantly review the process, minute your meetings and compile information as to your actions. In the future if the plan does not work, this helps defend your actions.

In our experience making honest mistakes whilst trading out can be easily rationalised after the event if this information is to hand. But, merely verbally stating that it seemed a good idea at the time does not convey a sense of prudent and diligent actions having been taken. In other words cover yourself in case the plan fails.

### **Q: How can I go about cutting employees when we cannot afford the redundancy payments?**

A: Consider contacting the Department of Employment. Under the hardship scheme the company may be able to (provided conditions are met of course) borrow the redundancy payments if it can demonstrate an inability to meet the payments.

### **Q: What happens if the trading out plan does not work?**

A: Consider the facts regularly, if the plan is clearly not working then take advice from a turnaround practitioner or insolvency practitioner. KSA Group provides a free help line on 0800 9700539 to get you quick expert advice.

**Q: It has got to be better to struggle on with an informal deal than to go into a CVA?**

A: Actually, often it is the opposite! The CVA mechanism is also a very powerful corporate finance tool, it draws a line in the sand with all unsecured creditors and allows all creditors time to consider and vote upon a restructure if necessary. Allied to the ability to remove from leases and reduce employee numbers, it is a very far-reaching tool. Of course, it also mitigates wrongful trading issues and allows director to focus on running the business.

AND HMRC will support a well structured CVA. They support 97% of our CVA proposals!

**Q: Why not just wait and see?**

A: You have a duty of care to creditors if your company is insolvent. Failure to take action can be construed as badly as acting wrongfully. In any case procrastination and inaction are always in the list of causes of failure cited by liquidators.

## **Time to Pay – Informal Deals with HMRC**

Most recruitment companies only have a few creditors and usually they include VAT, PAYE/NIC and Corporation Tax! Along with some bank or factoring debt and a few online job boards the debt is concentrated with the “de facto” bank called HMRC.

Since December 2008 the government has operated a helpline for distressed but viable businesses to pay their tax debts over time.

Call HMRC: you can ring the Payment **Helpline** on 0845 366 1204 if you need a quick 2-3 month deal. You will find this very helpful and generally a fast response is received.

If you have already had a TTP (Time to Pay ) then you may still get more deals over time if you adhered to them. If you didn't then you may be passed upwards from the helpline to a tax collector. He or she will require much information, good evidence of viability, evidence that the bank cannot support and a plan. To help you we have prepared a UNIQUE Time to Pay Programme, Step by Step guides to the process.

This programme will help you get a time to pay deal (TTP) or we will give you your money back. Call 01289 309431

**We can show you a way to solve this horrible tax problem NOW! Easy to use STEP BY STEP guides that will**



- Give you a detailed professional system to set out the deal with all the letters, board resolutions and tools you need to protect you as directors or partners /sole traders.
- Help you dramatically improve your cashflow and stop the tax man making threats.
- Imagine if we could give you back up to **50% of your time.** The TIME THAT YOU ARE WASTING on fighting cashflow fires?
- Learn how to use the letters and confident language that our experts use when they talk to tax collectors, across the UK, EVERY DAY OF THE WEEK!
- Help target your proposal to the right TAX MAN; follow it up and get it approved!
- Protect you from personal risk and wrongful trading!

## Refinancing the Company

**What about raising money, (possibly) along with trading out guides (above) will this prevent the company falling into insolvency?**

Almost all businesses need to go through periodic refinancing exercises, whether replacing bank facilities, renewing overdrafts, obtaining bank term loans, enterprise

finance guarantee loans, factoring or capital expenditure requirements. This is normal business practice.

Where a company has encountered a significant downturn event or is under pressure, then the directors must consider whether raising further finance against assets is the solution to their problems. As the market changes and evolves almost daily, we cannot provide an exhaustive list of the financial products available but we give our own view of the various methods below.

### **Refinancing:**

Remember this section is not designed for ordinary business financing solutions, rather it is for companies under pressure to find adequate working capital.

Consider the products, weigh them up against the circumstances you find yourself in and decide. If you want help to decide and find the most appropriate suppliers of finance contact us. We know and have access to almost all providers of these products and can point out the pros and cons of each.

### **Bank Overdraft**

#### **Description**

It may be possible to obtain temporary increases in facilities from the bank. If the problem can be demonstrated to be short-lived the bank will want to try and help. If the problem looks more deep-seated they may want more investment from third parties (you). Prepare good information, your team's arguments and talk to the bank - early enough.

#### **Advantages**

Decision making process is usually short - if you have good information to give the bank. The existing relationship is very valuable - banks don't like losing customers. It may ask for more detailed work to be done on the figures, (despite the cost) this can be a valuable exercise. It may help pave the way to other financial products from the bank in future.

#### **Disadvantages**

If the bank cannot see how its money can be repaid (serviceability) or cannot see how it can get the money back in the event of liquidation (security) they will not

lend. Ill-prepared requests for funds will be looked upon less favourably. The bank may want a third view and ask for investigating accountants to examine the business.

It may be more costly than existing finance. They will probably want more security from the company and the directors - personal guarantees may be demanded or increased if in place.

## **Enterprise Finance Guarantee Scheme**

### **Description**

A government backed loan scheme to assist SME's with working capital requirements. Typically, the DBIS will underwrite up to 75% of the loan. Banks vary in their approach to the scheme but the DBIS is actively encouraging its use.

### **Advantages**

It can be good value and reasonably quick to raise this type of loan. The investment criteria are perhaps less stringent than non-guaranteed facilities. Capital and or interest holidays can usually be agreed. For distressed companies this can be a lifeline while they return to profitability.

### **Disadvantages**

Not all applications are approved of course. If the company is clearly distressed the bank and /or the DBIS may reject applications. Can you raise enough to provide a solution and adequate working capital whilst you return to profit? Can you service the loan. Merely creating more debt is not a solution where radical surgery is needed.

## **Factoring**

For recruitment companies this is the usual refinancing solution. Your company essentially sells the debtor book to a factoring company who then provide the company with working capital advances against that asset. They will provide from 50-95% advance against the debtor book and charge around 0.5% to 2% depending on the number of invoices, the quality of the book and how much work is

required. All your future invoices pass through the system and this sharply improves cashflow.

### **Advantages**

If you debtor control is poor this can help. It is an extremely flexible form of finance - the facility can rise and fall as your needs dictate. If the company is under pressure and your sales are growing it is a vital tool. Finding the right factor can lead to much more efficient use of your assets and the ability to plan production or activity - thereby creating improved efficiency.

### **Disadvantages**

Concentration in one or two customers can cause difficulties. It is perceived as expensive - but it is providing the commodity you need - money. Most banks have a factoring division - they may not be suitable for your business - shop around. Any bank overdraft is normally repaid from the advance from the factor (the bank's main security is sold to the factor). If you have very low margins or your debtors pay very slowly (more than 85 days) it is probably not suitable.

### **Asset Refinance**

#### **Description**

Most companies depreciate their assets faster than the value of those assets fall. Therefore, there are "unencumbered" assets to lend against. The assets of the business form collateral for the lender to secure themselves against. Assets include, property, office equipment. Used in conjunction with, say, factoring this method can provide a package of new finance to overcome distress.

### **Advantages**

It is usually a very quick method, access can be through commercial finance brokers or other contacts. Contact us by email for help if required. Where a short term crisis (say a large bad debt) has occurred this method can help the company round the problem very quickly by efficiently using its assets to raise cash. Better quality assets such as land and buildings can attract good rates of interest.

## **Disadvantages**

Raising finance this way is not cheap. Where the company has unencumbered assets it is tempting to raise cash against them but remember

NB: If the crisis is longer term can your company service the debt repayments? If not call us for a CVA now! 0800 9700539

Costs vary but rates of interest on refinancing assets (ie where previous debts are repaid and fresh advances made) can be as high as 35%. The value of assets is established by the lender - it is never as much as you expect.

## **Business Angel Investment**

### **Description**

The classic UK equity gap problem is getting worse. Too small for venture capital and too big a risk for the bank - where to turn? Angels can provide a mixture of loans and equity to distressed or struggling businesses. Most come from a business background and have lots of experience. They usually take a longer term view and can greatly assist the directors grow the company.

### **Advantages**

With bags of experience an angel can be just what the growing or struggling company needs. Chose carefully and the relationship can be very fruitful. The funds can be flexible and inexpensive. Further rounds of funding can be available. The fact that an investor is putting money in can also help persuade the bank to increase funds available.

### **Disadvantages**

Chemistry can be difficult - they are going to be involved long term therefore will take time choosing their investments. Equity: they will want a position in the company and the depth of the distress or pressure will determine how big a slice they require. Paucity: there are thousands of angels but finding an appropriate angel, convincing them to get involved and getting finance can be many months. Control: many angels will want control at board level.

## **Venture Capital**

### **Description**

Most small businesses in trouble are NOT suitable for Venture Capital. VC's invest in around 1 in 1,000 applications for finance and unless there is a huge growth potential and an almost unique nature to the business it will not get venture capital. If however the company is unusual in the above regard then contact us by email with a synopsis and we will look at the options with you.

### **Advantages**

Most directors are aware that equity is "cheaper" than debt. Having a quality non executive director to help guide the board (a pre-requisite of most VC's) is also a big plus. The company's reputation and PR are enhanced. Where growth is achieved and prospects remain good the ability to raise further finance is enhanced.

### **Disadvantages**

Classically, shareholder directors see the dilution of their equity as a no-go area. Would you rather have 70% of a company worth £10m or 100% of a company worth £100k? VC's only part with money after thorough due diligence, it is hard work and costly. In the end you may not get the money. Only the best management teams with the best ideas win through. It is very time consuming - in a distress situation do you have 3-9 months to wait?

## **Directors Loans**

### **Description**

It may be possible for the directors or senior people to raise funds privately. This can then be loaned to the firm. Tax efficient repayment may mitigate the PAYE due on directors pay. But if the company is insolvent, repaying your loans in advance of the creditors may contravene the law. In the event of liquidation the monies may have to be repaid to the company! Security may be taken for the loans - but this is a complex area.

**Beware you could create a potential preference (s239 Insolvency Act 1986) if you put money into an insolvent company and then pay yourself back!! Call for smart, expert advice 0800 9700539.**

### **Advantages**

It is cheap, you remain in control of the financial process. It is usually a quick method to raise finance. But be warned, taking out second mortgages will require showing the lender the company's accounts. You can repay the loan as convenient to cashflow. It can carry zero interest (you can however charge interest). Personal loans are now NOT that freely available

### **Disadvantages**

If you had lots of money it would probably already be invested in the business? Can you afford the repayments personally? If the company fails you still have to repay the loans. The bank may take some of their existing advance back after the funds are introduced. Finally, is the money you can raise really ENOUGH money to solve the company's problems?

### **What if Informal Trading Out and or Refinancing is not an option?**

The company directors should consider their personal objectives, those of the shareholders, but ABOVE ALL ELSE they must act in the best interests of the creditors.

**Assuming the company is insolvent then it may be necessary to use more formal turnaround / insolvency options. These broadly fall into Stop and Go options.**

#### **Stop**

**Creditors Voluntary Liquidation  
Administration  
Pre-Pack Administration (also a go option!)**

#### **Go**

**Company Voluntary Arrangement  
Pre-pack Administration  
Trade Sale (not covered in this version)**

**First we will consider the stop options. In the first - creditors voluntary liquidation – we assume that the directors have had enough and want to cease trading, the company isn't viable and there are few assets.**

## **Creditors Voluntary liquidation**

### **Company bankruptcy ?**

Many people call this company bankruptcy, but this is not the correct description, only people can go bankrupt!

Insolvent companies go into liquidation, [administration](#), [receivership](#), they [trade-out](#), [refinance](#) or they enter a [company voluntary arrangement](#).

Most accountants, lawyers and many other advisors are aware of a section of the Insolvency Act 1986 that is called "[wrongful trading](#)". When times are very difficult for the company and they don't know about the full range of options available to a distressed company , many such advisors tell the directors to talk to an insolvency practitioner (IP) and or consider liquidation to avoid being made personally liable for the company's debts.

It is interesting that most liquidators get their work this way! So we always recommend taking advice from third parties not just your accountants or their friendly insolvency practitioner. They may be giving "safe advice" but it's not always the RIGHT ADVICE!

We recommend that you consider [ALL options](#) before you decide! Do not let fear of "wrongful trading" get in the way of making the right decision for the company. As directors you must maximize creditors' interests first.

**Liquidation should only be used as the LAST OPTION, we believe it should not be a case of bury the company first, ask questions and worry about the results later! Using a simple medical analogy, would you go to the undertaker with a pain in the chest?!**



## **When is (Creditors Voluntary) Liquidation appropriate and what happens?**

It is appropriate when:

- The company is insolvent
- It does not appear to be viable - even if restructured
- The market has declined for the company's services or products
- The directors don't believe that they have the determination needed to rescue the company. Nor do the directors WANT to rescue it.
- It is used as part of the restructuring of a group

## **What happens in the liquidation process?**

**The easy answer is a good liquidator will deal with all of the following for and with you. But if you want to know in detail what happens read on.**

The directors of an insolvent company elect to call an extraordinary general meeting of the company. At this shareholders (members) meeting, the directors will report that the [company is insolvent](#), there is no reasonable prospect of paying existing creditors, they believe it would be wrong to take further credit and they advise the shareholders that the company should voluntarily enter liquidation.

At this general meeting the members (shareholders) pass a resolution to cease trading (normally) and to nominate a liquidator. This liquidator conducts a relatively quick investigation into the statement of affairs of the company and calls the creditors to a meeting.

He /she must place an advert in the [London Gazette](#) and in two local newspapers calling this meeting and then write to all known creditors inviting them to submit a claim for their debts. The liquidator is then appointed by the creditors at a creditors meeting (s98 Insolvency Act 1986). These are normally held virtually

If required, the creditors can elect to form a creditor's committee to monitor the activities of the liquidator during the course of the liquidation. This may be to monitor fees, sale of assets and investigation into the director's conduct. A creditors committee must have between 3 and 5 members.

The liquidator has four main tasks:

- To convert the assets of the business into cash (hence liquidation)
- To adjudicate the claims of the creditors (work out how much is owed by the company)
- To investigate and report upon the conduct of the officers of the company (directors and shadow directors)
- To make payments (where dividends are available) to creditors in order of priority

Of course, very often, the directors have tried many other avenues to save the company and the remaining unfettered assets are modest. (Unfettered means the assets have no outside owners like the bank or HP companies).

In many other cases the liquidator is asked to sell the assets of the business to another party. This can include the former directors or shareholders. This is commonly known as a "Phoenix".

### **How do we go about all of that!**

Don't worry the liquidator will handle almost all of the paperwork, the assets and the activity after liquidation. It is vital though that you have up to date information for the liquidator to use.

### **Is phoenixism legal and if so what happens?**

Yes, provided the rules are observed and the liquidator maximises the interests of creditors then the business assets can be sold to a "connected party". In this event the liquidator must satisfy himself that he/she has

- Obtained the best possible value for the assets
- Having typically advertised the assets for sale in the media and or on the internet.
- Ensured the creditors interests are not compromised by investigating the conduct of the directors prior to the liquidation.

- The trading name of the new company is not the same, or similar to the liquidated company, (s216 Insolvency Act 1986). This restriction on re-use of a trade name can be lifted if the court agrees.

Often a Phoenix will require new cash in the form of investment to get the company going. This can sometimes be a stumbling block too. As can the fact that the new company may have to take on the employees employment rights from the old company (TUPE). This is a very complex issue that must be considered before going down the liquidation path.

Typically, the company is very distressed and the board has decided to cease trading, the normal liquidation process starts but the directors or shareholders or both buy some of the assets from the liquidator. The new company starts to trade. Often a similar name is used to the old company - this can be a legal minefield so make sure you get good advice if you wish to set up a phoenix company.

### **Main Advantages of Liquidation**

From a director's point of view: the directors may avoid the risk of "wrongful trading", they draw a line in the sand - and crystallise the situation (often this is a very important benefit because it brings to an end the period of worry and terrible uncertainty) the creditors interests are hopefully maximised.

If wrongful trading can be proven then the director (s) can be made personally liable for the debts of the business. This is usually from the point where they should have known the company had no "reasonable prospect" of surviving.

From a creditor's perspective the benefits are that the directors conduct will be investigated by a liquidator (or ultimately even the DBIS), their position is crystallised and not worsened. Because it is the creditors who appoint the liquidator, alongside a creditors committee they can be sure that the company issues are dealt with correctly.

### **Main Disadvantages of Liquidation**

From a directors and shareholders point of view: any tax losses built up in the period prior to the liquidation are lost, goodwill is lost (even if there is a phoenix), the director's conduct will be investigated and it is a costly exercise. In virtually all cases there is no return for the shareholders and (because they are connected creditors) the directors.

Please see a [guide to creditors](#) for an explanation of "connected creditors".

From a creditors perspective a CVL can be a negative step because: assets tend to be sold for very much less than book value, creditors' claims can be much higher (for example claims from employees, landlords and secured creditors), there is often no prospect of continued trade. Coupled with the actual cost of doing the insolvency work, the return to creditors in liquidation is usually very low.

### **Directors Health Warning!**

If the [company is insolvent](#) and you are considering liquidation please follow this simple advice:

**From here on, make sure you take notes of any major decisions, write down important dates and the board's actions. Always write to creditors and banks, that way you will create a written record of the issues. Have regular meetings of the board, shareholders, management and if it's just you make sure you write everything down!**

In months to come, when you are asked questions, this will help you remember why certain decisions were made.

### **Summary**

There will be around 8-10,000 CVL's in the UK each year. Many of these are necessary and correct. However, if the company is viable the use of this mechanism to "restructure" the business is like using a sledgehammer to crack a nut.

We have heard some directors say they don't want to rescue the company if it means paying back the creditors, or "there is too much debt".

If tempted by this ethos remember you have a duty to maximise creditors' interests. After liquidation, if it can be proved that you set out to avoid this you may be personally liable for the debts of the company.

**Before deciding to liquidate, make sure that you go through the decision making process carefully.**

**If you have now decided to liquidate, we can get one of our in-house quality insolvency practitioners to talk to you. He will make sure a proper**

**and thorough job is done, cost effectively. Please, Sarah Massey or Iain Campbell to talk through the next steps on 0800 9700 539.**

**Just to remind you again - never decide to liquidate a distressed company unless you think it is not viable.**

We can assist with far reaching restructuring of the company including terminating leases, contracts of employment for unwanted employees, HP agreements and other onerous contracts. Would such a restructure help your company survive? If there is a viable business but you are tired and distressed we can still help.

Our advice is always consider all other options like CVA first before deciding to liquidate!

## **Pre-pack Administration**

### **For Larger Recruitment Companies that need RADICAL RESTRUCTURING**

Case Study for Pre-pack Administration - Learn how a recruitment company was restructured using pre pack admin.

**If your business is facing huge problems and legal threats, there is a powerful, legal way of selling the business on to a third party, a "newco" or to the existing directors.**

**This is called a pre-pack administration sale.**

**Examples of the steps for pre-pack are as follows.**

#### **Step 1:**

"Your Recruitment Company Ltd" takes expert advice from insolvency practitioners or turnaround practitioners on its very poor financial position. It is likely the company has threats from landlords, HMRC for PAYE and VAT, the bank and many trade creditors. The directors are worried about wrongful trading and their personal

risk. The business may have onerous contracts or too much property, too many employees and or lost market share/customers.

This advice should be thorough and a report prepared in writing for the board and possibly for the bank. All options such as company voluntary arrangement, trade sale, refinancing, administration, creditors voluntary liquidation and pre-pack administration, should be considered.

If good reasons for pre-pack, then this option should be very carefully considered by the board of directors. If a decision is taken to go down this path a board meeting should be held and a resolution passed stating the company's board will consider the option in greater detail.

It's likely the resolution will include the appointment of formal advisors either insolvency practitioners (IP), turnaround practitioners or accountants to act as advisors to the board.

## **Step 2:**

If the plan is to sell the business (not the company) to a "newco" then a business plan for the newco must be drawn up. We recommend that this includes detailed profit and loss forecasts, cashflow forecasts and balance sheet forecasts. This will give an indication of working capital requirements. The proposed administrator may require this as evidence that the new company can be viable.

If the plan is to sell to an existing trading company, the IP will require copies of management information and accounts from that buyer. Again this is necessary to ensure the acquiror is viable and can afford any payments for the assets being acquired.

A qualified accountant should be contracted to provide this forecast pack in my view. My trained accountants and specialist forecasters can provide such a service.

## **Step 3: - Compliance issues.**

Under insolvency practitioner's guidelines (known as Statements of Insolvency Practice or SIPS) the IP must market the business.

This often requires sending sales memos to a database of potential buyers, or the IP may place an advert on his website and/or a local or national newspaper. If he

gets no interest or no indication of interest he can then sell to the newco or third party. If there is a lot of interest and several offers, beware your business could fall into a competitors hands! You may still be able to buy the business back, but the outcome is not under your control

**For an example of this risk see this link to the Daily Telegraph [How the door almost closed on a pre-pack](#)** (click link)

The IP will also have to get formal valuations of the assets, intellectual property and or goodwill of the insolvent company, generally by RICS qualified surveyors. Generally any offer needs to be commensurate with such valuations.

At this stage, if you and your colleagues are planning to buy the business you must be careful with regards to your personal position. As directors of the dying company you have a fiduciary duty of care to the company's creditors.

Starting "newco" can put you at risk of conflict of interest. It's likely that you will need separate legal advice on both companies. Best to talk to lawyers with insolvency and pre-pack experience. Contact Keith Steven for a list of good lawyers.

The IP will take advice from his lawyers as to compliance and risk. He may require this advice to be paid for along with his disbursements. Strictly speaking he cannot charge time costs in advance for the pre-pack work but he will charge for consultancy and fees.

## **WARNINGS?**

Beware, will your client's contracts or BANK allow you to pre-pack? (The current standpoint of several clearing banks, is no, the bank will not pre-pack to the incumbent directors/shareholders).

Will your landlord(s) allow a new company to occupy their property? Are your suppliers prepared to supply a newco? Will your creditors be angry about this approach? Some readers may have seen negative media coverage of pre-packs is rising sharply, almost in line with the economy shrinking. In future we see many more people attacking pre-packs, especially creditors and the media.

## **Step 4: - Raising finance**

You will need finance to fund the acquisition of the assets and business. There are many specialist lenders who can provide: factoring, asset-based lending, loans and

bank facilities. Some venture capital companies or angels may help fund the pre-pack as part of a "buy and build" strategy. We have a number of contacts that can help with this.

Financing a pre-pack in 2019/20 is likely to be very difficult politically and will probably require personal guarantees from the directors for SME's. Larger companies may find that the private equity and venture capital buyer removes the directors as part of the pre-pack conditions.

Contact Keith Steven now on 07974 086779 or by email on [keiths@ksagroup.co.uk](mailto:keiths@ksagroup.co.uk) if you need finance.

Once again, the funders will require a detailed plan supported by forecasts, they will want to test the valuations, the possibility of making and funding a loss and how their security needs will be met. So, it's vital to get these built. Call us if you need that done.

## Step 5

Assuming that you have raised the finance, the proposed administrator has satisfied his compliance requirements and the board of "newco" believe they can fund the acquisition, then it's all systems go.

A contract is likely to be drawn up that appoints the proposed administrator formally. He will then initiate the pre-pack administration by contacting any floating charge holders like banks or lenders with security. If they have no objections (and often they are involved in funding newco) then he can proceed.

Beware some banks will NOT allow a pre-pack to a related party. RBS, HBOS and HSBC for example will not generally countenance a phoenix with/to directors /members of the failed company. So, it may be necessary to take out the bank first or use a nominee company, (ask us for details on this).

Assuming all is approved then the administrator makes an application to Court stating his proposals. Almost immediately after that, the business is sold to a newco or third party.

This can be done on a Friday night and by Monday the business is trading virtually uninterrupted. Having bought the company name, the "oldco" see its name changed to something else, like "Your Company (Realisations) Ltd".



## **Summary to the pre-pack administration guide.**

Clearly, this is a short guide and there are many pitfalls - with good advisors, quality practitioners and lots of determination this can be a very powerful and actually pretty quick solution. But remember the warnings above, if you are with RBS, HBOS and HSBC as a bank it is my experience that they will, generally, not support a pre-pack to the existing directors and may indeed appoint their own administrator or [receiver](#).

## **Statement of Insolvency Practice (SIP) 16**

The Insolvency Service has issued a statement saying it will use the new SIP requirements for administrators using this tool. This is called the Statement of Insolvency Practice 16. The SIP requires the administrator to report to creditors on their actions as follows.

Insolvency Practitioners should be clear about the nature and extent of their role and their relationship with the directors and officers of the insolvent company in the pre-appointment discovery period. Where they are instructed to advise the company, they should make it clear that their role is to advise the company and not to advise the directors on their personal position.

The directors should generally be advised to take independent legal advice, particularly if there is a possibility of the directors acquiring an interest in the assets in the pre-packaged new business or newco.

Practitioners must bear in mind the duties and obligations which are owed to the body of creditors in the pre-appointment period. They should be mindful of the potential liability which may attach to any person who is party to a decision that causes a company to incur credit and who knows that there is no good reason to believe it will be repaid, this could lead to wrongful trading issues.

When considering the restructuring or sale of the business or assets, the administrators should bear in mind the requirements of the Insolvency Act 1986. In administration these provide that:

- The administrator must perform his functions in the interests of the company's creditors as a whole, and

- Where the objective is to realise property in order to make a distribution to secured or preferential creditors, the administrator has a duty to avoid unnecessarily harming the interests of the creditors as a whole.

Administrators engaged in a pre-packaged sale should therefore be able to demonstrate that they have considered the above. If creditors believe that their interests have not been considered they may complain to the Insolvency Service or the IP's regulatory body.

Where a pre-pack is used the following information should be disclosed to creditors in all cases, as far as the administrator is aware after making his or her enquiries:

- The source of the administrator's initial introduction, in other words how did the case arrive on his desk.
- The extent of the administrator's involvement prior to appointment and any marketing activities conducted by the company and/or the administrator.
- Any valuations obtained of the business or the underlying assets. We would always advise obtaining independent valuations.
- The alternative courses of action that were considered by the administrator, with an explanation of possible financial outcomes in each scenario.
- Why it was not appropriate to trade the business, and offer it for sale as a going concern, during the administration.
- Details of requests made to potential funders to fund working capital requirements and whether efforts were made to consult with major creditors
- Details of the assets involved and the nature of the transaction to newco
- The consideration for the transaction, terms of payment, and any condition of the contract that could materially affect the consideration.
- If the sale is part of a wider transaction, a description of the other aspects of the transaction.
- The identity of the purchaser, directors and any connection between the purchaser and the directors, shareholders or secured creditors of the company.
- The names of any directors, or former directors, of the company who are involved

in the management or ownership of the purchaser, or of any other company into which any of the assets are transferred.

- Whether any directors had given guarantees for amounts due from the company to a prior financier, and whether that financier is financing the new business.
- Any options, buy-back arrangements or similar conditions attached to the contract of sale.

In my belief the pre-pack to a connected party will be a difficult "sell" now to creditors, unless all of these issues are carefully considered and noted. Where a business is pre-packed to a third party, independent of the directors and possibly even secured creditors, then it will still be a powerful tool.

The Enterprise Act 2002 and case law supports the use of the pre-pack sale, but I also believe that in some cases this will be open to challenge, unless ALL of the issues above are considered and answered as part of the scheme. Otherwise further pre packs could face challenge in court.

## **What About “Trading Administration? Is that Different”?**

### **Administration a Detailed Guide:**

This mechanism is designed to protect a company from its creditors while a restructuring plan is completed. This technique can be very powerful where the company has a very aggressive creditor or creditors and needs to protect itself from them whilst a rescue plan can be worked out. It is not the same as an [Administrative Receivership](#).

### **What are the key components?**

The company must be a reasonable size, have reasonably predictable cashflows and must be able to predict profitability. There must be an insolvent position or contingently insolvent position and the directors think that a hostile creditor will seriously affect the future trading possibilities. This is often a landlord or the Crown creditors.

The administration process requires a licensed insolvency practitioner (IP) to act as the Administrator appointed by the court. The court appointed Administrator takes over the management of the company and takes responsibility for restructuring the company or business.

If the company has little in the way of assets, poor cashflow and no future then [creditors voluntary liquidation](#) is probably more appropriate than administration.

There are two types of application to the High Court. There is the "without court order" appointment route for holders of qualifying floating charges and companies/directors – this is quick and does not need a court application or hearing. But sometimes it is better to still make the second type of detailed application which asks for a Court Hearing.

### **Who can appoint an Administrator?**

Companies and Directors can appoint an administrator quickly with the IP's guidance. This does not require a Court Order it requires a fax to be sent to the court with the appropriate forms. Clearly the IP must have done some work to establish if the company is insolvent, should it go into administration, what the process will involve and the planned outcome.

Where a company is in liquidation or in a CVA then the proposed administrator must obtain a Court Order.

No administration order will be granted unless the holders of all qualifying floating charges have been given 5 days clear notice of the company's or directors' intention to appoint an administrator.

The floating charge holder (usually a bank) will still retain the ability to step in and appoint their own choice of administrator should they so wish.

So it's possible that the board decides to appoint an Administrator and the bank refuses and appoints its own. Quality IP's will not experience much difficulty if they are recognised by the bank and there is a quality plan to protect the business.

### **How can the bank appoint an Administrator**

Banks can appoint an administrator if they hold a qualifying floating charge under new debentures granted after 15th September 2003. If the bank holds an older debenture it can appoint an [Administrative Receiver](#) the banks have the right to appoint an administrator.

Note as a dying approach, administrative receivership is not covered in this programme

But it should be pointed out that the administrator has a duty to act in the interests of all creditors not just on behalf of the bank/floating charge holders.

There must be one (or two) of three "Objectives" for the Administration:

In the application to the Court the proposed administrator must state which is his or her main objective of the following three:

1. Company Rescue, as a going concern, should be the primary objective. This usually means that the company proposes a [Company Voluntary Arrangement](#) or a scheme of arrangement.
  - 1.1. See [Admin followed by CVA](#) below
2. If that is not possible (or if the second objective would clearly be better for the creditors as a whole), then the administrator can achieve a **better result** for the creditors than would be obtained through an immediate winding-up of the company, possibly by trading on for a while and selling the business as a going concern.

2.1. In English this means trying to sell the business for more than a liquidation would raise.

3. Only if neither of the first two objectives is possible, can the administrator realise any property to make a distribution to secured and/or preferential creditors.

3.1. This means collecting and selling the assets for the best price to pay the bank.

In cases where speed is essential in making the appointment, the rules include a provision that will allow for filing a notice of appointment during times when the court is not open for business.

The filing of such a notice will bring into effect an interim moratorium on insolvency proceedings and other legal processes being taken against the company.

In a moratorium no one can “knock the company over” without the leave of the Court. When the Court has effectively ratified the administrator’s appointment this is unlikely! The Court will want to have as much information as possible to ensure that the application for Administration is correct and appropriate.

## **Administration sale**

### **The company can enter administration to be sold. A typical scenario would be**

1. Company is under severe pressure, creditors circling, possibility of legal action.
2. Directors decided to take advice from KSA or a similar firm. A decision is taken to protect the business and to stop legal actions. The company is insolvent but there is a viable business.
3. The company meets with KSA advisors; they draw up a report on the options available looking at CVA, Administrative Receivership, Administration, trade sale etc. The board believes that a sale could be achieved but the company needs to be protected.
4. An administrator is appointed and he / she will then run the business for a period of say 1-2 weeks.

5. In that time he markets the business under insolvency guidelines called Statement of Insolvency Practice 13, he must be seen to market the business for sale.
6. He will obtain valuations from a professional valuer for all of the assets, goodwill and so on.
7. In an agreed period the directors of "oldco" can buy the business provided the valuations are met and the administrator gets the best deal for the creditors.
8. "Newco" has no debt, no creditor pressure and it can take on leases for example.
9. General guideline is that TUPE applies and therefore all employees' rights move across to Newco.
10. The oldco is then liquidated or dissolved.

### **How long does the Administration process last?**

The process can generally only last for up to 1 year, although this can be extended by the consent of the creditors and/or by the court. The administrator is also required to do everything as soon as reasonably practicable. There is a time-limit of eight weeks for getting his proposals (in other words what he proposes to do with the company) out to creditors, and holding the initial creditors meeting. This can be extended by the creditors' consent and/or by the court.

These proposals will include full details relating to his appointment, and the circumstances leading up to it, as well as exactly how the administrator proposes to achieve the purpose of administration, including details of how he anticipates the administration will end.

### **Statement of Affairs:**

Upon appointment the Administrator will require one or more of the current or former directors or company officers to provide him with a statement of the company's affairs.

This is a prescribed form which details the company's assets and liabilities, including those assets that are subject to any fixed or floating charges. This can be difficult to produce.

A copy of the statement of the company's affairs, or a summary of it, must be attached to the administrator's proposals. See above for the 3 different types of proposals.

A copy of the proposals will also be filed with the registrar of companies for placing on the companies' public file. Interestingly though, where the information included in the statement of affairs is commercially sensitive, the administrator can apply to court to have the statement, or the relevant part of it, withheld.

Included with each creditor's copy of the administrator's proposals will be an invitation to the initial creditors' meeting, at which the creditors vote on those proposals and whether to accept them.

### **Creditor's Meetings**

The initial creditor's meeting must be held within 10 weeks of the date that the company entered administration, and the creditors must be given at least 2 week's notice of the meeting, although these time-limits can be extended by the creditors and/or the court.

- The business of this meeting could be carried out by correspondence, although if 10% or more of the creditors (in value of their claims) demand a meeting, then the administrator is still required to call one.
- The proposals can be accepted (by a majority vote, measure in value of claims), modified and then accepted, or rejected. If the latter, then the administrator is required to report that fact to the court and seek further directions from the court.
- Following the initial creditors' meeting, and any subsequent meeting of creditors, the Administrator is required to send a report of the outcome of the meeting to the court and to the registrar of companies for filing on the company's public file.
- A creditors committee can be formed if the creditors require it. This must be between 3 and 5 people.
- The Administrator then manages the company's affairs, business and property in accordance with the proposals that have been agreed by the creditors.



- He must send regular progress reports to the creditors, the court and the registrar of companies covering each six-month period from the date that the company entered administration until the administration ends, or until he ceases to act.
- These reports will provide full details of the progress of the administration to date, including a receipts and payments account (or what cash has been received and paid out) and any other relevant information for the creditors.

Just by reading this you will see that the law surrounding Administration is complex and very powerful for companies in distress.

BUT!! Do not appoint an Administrator before calling us to discuss any questions you have. Once appointed it's too late to change your mind! 0800 9700539

### **What are the disadvantages of Administration?**

- The directors are not in control of the business and an offer from a third party may lead to their removal as directors.
- Tax losses can be lost if no CVA is proposed.
- Another buyer may buy the assets.
- It is a public event, all creditors and all correspondence (invoices, advice notes, orders, emails, websites, letters) must say XYZ Co Ltd (In Administration). Most customers and suppliers therefore become very aware of the insolvency.
- All orders must be ratified by the Administrator or his staff.
- The directors have no powers to run the company.
- As soon as reasonably practicable after his appointment, the administrator must obtain details of the company's creditors and must notify the company and all of its creditors of his appointment. This is also an advantage as it stops legal actions.
- The appointment must also be advertised in the London Gazette and in a relevant local or national newspaper - one that the administrator thinks is appropriate for ensuring that the appointment comes to the notice of the company's creditors.

- Clearly the bank can be forced into appointing their own administrator if it decides its position is going to be compromised by the proposed Administration of the company.
- Costs are often very high for this procedure, therefore in our opinion it is only really suitable for larger companies where aggressive creditors threaten future viability.
- TUPE applies to Newco - in other words the new company cannot remove employees and must adopt their contracts. This can be a problem when planning how to cut costs in the new company.
- Financing trade and other supplies can be difficult unless adequate resources are available and or new funds can be introduced in the administration period.

## **What are the advantages of Administration?**

Administration can be a very useful and powerful tool for insolvency practitioners to control the company, banks, and creditors to ensure survival of the business.

- All legal actions are stayed by the process.
- It stops the financial position getting worse and putting directors at further risk.
- It can be very quick and cost effective if an "Administration pre-pack" is used properly. (See below).
- All unsecured debt is removed.
- From the creditor's perspective, because a licensed insolvency practitioner is appointed to administrate the company, it also ensures that the administrator considers all creditors positions correctly.
- Protection from creditors can allow the administrator a reasonable time frame (the 8 week period) to negotiate a deal to achieve the objectives which may include selling the company thus protecting jobs and economic activity.

- It is possible for the administrator to appoint directors or managers to run the company. With our vast turnaround experience this is often preferable to the administrator's staff. We are well versed in ensuring that the administrator works with turnaround advisors such as KSA. This can ensure that we are involved in the management of the company to ensure professional and pragmatic management at a time when the company is under severe distress.

**So if a winding up petition is live and a real threat to a viable business, the company can be protected by the administration process – possibly followed by a company voluntary arrangement after a period of assessment.**

### **Administration followed by CVA**

The company is protected by Court while the company and the administrator put together a plan for the Company Voluntary Arrangement.

If there is a risk of a creditor winding the company up or a landlord taking aggressive action, then this is a powerful (but expensive) way of controlling them.

KSA does not believe that Administration is necessary most of the time, going straight to a CVA cuts out costs (fees) and reduces market awareness of the troubles.

## **What does KSA think the Best Solution To Rescue A Recruitment Company is?**

### **Generally (if there's a viable business) it's a Company Voluntary Arrangement!**

A CVA is a deal between the company and its creditors; unsecured, trade and tax, to repay them from future profits or a deal may be written to sell assets and pay back creditors from the proceeds.

The deal is based on preserving the company, rebuilding sales and profits and paying something back over a period of time to be agreed. Directors remain in control, personal guarantees don't get called in (usually) and it gives your business a fighting chance to survive.

We start every CVA deal with a blank sheet of paper and a clear mind. Every case is different, but there are some crucial points to consider before embarking down this path.

### **Based on our experience, vital components of a successful CVA for a recruitment company are**

- A viable business that can return to profitability. It will have traded and been profitable in the past.
- A commercially structured deal - do not pay too much too soon.
- Introduction of appropriate levels of working capital in addition to the restructuring of debt if required (such as new factoring facilities).
- The management accepts that there has to be change in the management and company.

- Directors and management need to be determined and hard work is essential, plus a bit of luck helps.
- Directors need to use expert CVA advisors to build the deal. Always ask advisors claiming to do turnaround how many CVA's they've done!!
- Cautious forecasts - don't expect life in CVA to be easy!

So, if your recruitment company can be viable in future but pressure is mounting this could be a superb solution. Remember the directors should aim to maximise creditors' interests - by continuing to trade, you will do that in a CVA.

After the directors have considered the long-term viability of the company it is essential to take appropriate advice from experienced turnaround advisors. We believe that it is vital to have commercially pragmatic and creative specialists involved from as early a stage as possible.

If a company has a viable future, the directors and management accept the need for change, are prepared to fight for its survival and the appropriate funding can be found, then a CVA is a very powerful tool. BUT be prepared - it is a tough fight and it is harder than liquidating the business. By proposing a CVA you are demonstrating that you are trying to maximise creditors' interests so it can often be viewed positively.

If after that the CVA does work, then the company will be profitable and valuable for the shareholders. That's a good long-term objective too.

### **Who can propose a CVA?**

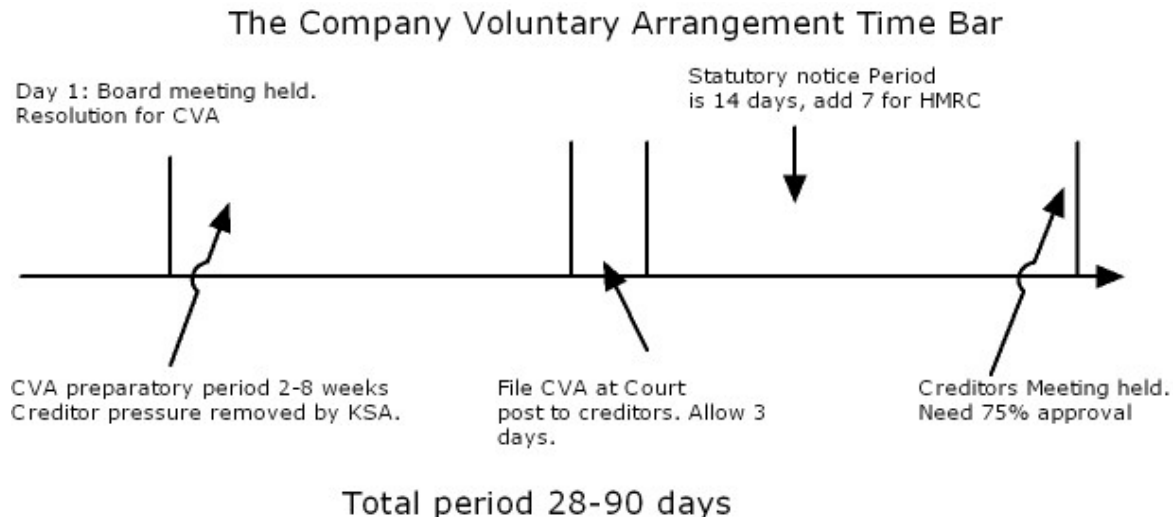
A CVA may be proposed by the directors of the company. When the company is either in liquidation or administration, the liquidator or administrator can propose a CVA.

Yes get this, the legislators have provided tools for liquidators and administrators to rescue a company from liquidation through CVA.

A CVA can only be proposed if a company is insolvent or contingently insolvent.

## How long does it take?

Here is a time-bar summary of the CVA process:



## Our STEP by STEP CVA Enquiry Assessment Process.

When we receive an enquiry for a CVA we always act in the same way. Our trained advisors listen to the problems, ask educated questions, obtain financial information from the caller and then consider the legal issues.

We normally have a chat through the issues facing people when they contact us. That way we can quickly ask questions that can help us form a view. If we feel we can help directly with a rescue approach, we often visit to have a face to face chat through the issues, followed by the issue of a detailed report. We do not charge for this process.

If we found a way forward then fees would be discussed in advance of any work being undertaken. Generally, our work is paid over a number of weeks from the savings we make in cashflow.

If we feel that the company needs to be closed or liquidated, we will introduce you to one of our insolvency practitioners. If you believe the business is viable, we can help rescue and restructure the business with our in-house expertise.

It helps us if you or your client can supply the following basic information to start the process.

1. Where is your business based?
2. What is the turnover?
3. What legal status – limited company, partnership or sole trader?
4. Assets - approximate value:
  - 4.1. Office equipment, motors, fixtures and fittings etc.
  - 4.2. Debtors, Work in progress and cash.
5. Liabilities:
  - 5.1. Bank – overdrafts, loans and etc.
  - 5.2. Inland Revenue and VAT Arrears and current.
  - 5.3. Trade creditors.
  - 5.4. Other such as hire /lease purchase, directors, EFG, SFLGS.
6. Viability:
  - 6.1. Marketplace - brief description
  - 6.2. Enquiries future prospects – brief description.
7. Management:
  - 7.1. Type of management.
  - 7.2. Any gaps in the team.
  - 7.3. Ability.

### **Summary:**

Please note we don't need lots and lots of paper to make a decision to help. Just provide the basic information above or as much as you can to start with!

We can provide free telephone, fax or email support even if only some of the above information is received. After receipt, if we believe that we can assist the company we will attend a meeting free to the client at a mutually convenient time and place (usually at their business address). This is then followed up by a detailed solutions report that guides the directors as to the rescue options.

## The CVA process a Detailed Guide

1. The directors appoint advisors, such as turnaround practitioners or an insolvency practitioner (IP) to assist in the construction of the proposal.
2. During this "hiatus" period the company should not materially increase or decrease debts to any creditor, suppliers should be paid for supplies made (not always easy!) and activity of the company continues. This does not apply to taxes. No payments should be made to VAT or PAYE while the CVA is being prepared.
3. A review of the company, its people, markets and systems should be undertaken. This is an important part of the process. Typically, the CVA will include detailed 1-5 year financial forecasts to assist the creditors to make their decision to support the deal or not.
  - 3.1. We ensure that a highly detailed bespoke (we wrote it) forecasting package is used. After our expert forecasters have produced this based upon the directors' guidance, the directors can then be shown various versions and what if planning can be used to build scenarios.
  - 3.2. What if we cut costs, what if we closed that office and removed 5 consultants? These and other questions should be carefully considered as part of the CVA process.
4. It is vital to remember that the company has the opportunity to sharply reduce costs of employment and overheads that would not be available to it ordinarily.
5. So, make sure that the lowest level of costs is targeted. Use the CVA to terminate employment contracts, leases of property and assets and any other onerous costs. If the company is struggling to drive placement sales up then try and "fit" the costs to lower levels of sales. Making sales in a recession or downturn phase is tough, so assume that in a CVA it will be even tougher!
6. KSA has a team of 95 financial forecasting experts across the country. Their role is to help the director build realistic and achievable forecasts



by questioning all of the financial information being produced. This process is never easy as sales have to be guessed at, but I would always advise people to aim much lower in their expectations! Being a pessimist is actually being more realistic for the company's future prospects

7. Once the draft proposal is ready the directors will typically review and refine it with the forecasting expert or accountant and agree that the proposal is appropriate, achievable and maximises creditors' interests. If the directors do not believe that it is sensibly structured, or that the process has highlighted weakness in the business then it is advisable to close the business.
8. When the CVA drafting has been completed the directors should then discuss the position with the company's' secured creditors. Experience tells us that the ability to deliver a quality draft proposal at this stage is preferable to verbal assurances that a CVA will be written and the bank told what the contents are when it's ready!
9. We find that the banks are very keen to get involved and assist where they see a viable company. Often they will want to see how the company will repay the bank's debts. This should be included in outline in the document - of course the bank may not agree with the suggested secured debt structure but will usually negotiate with the directors and their advisors.
  - 9.1. Now that many of the banks are in trouble, we find that the banks want to see credible plans for recovery of the debt that was loaned in perhaps more profligate times. A good plan will I find, always be received well.
10. During the CVA production or hiatus period, current assets such as WIP and debtors are collected, turned into cash and liquidity should improve. This should be used to fund the difficult period between appointment of CVA advisors and filing the document at court.
11. **In addition the company does not need to pay PAYE, NIC or VAT in the hiatus period. This too, can be used to improve cashflow.**
12. The CVA proposal is then filed at court only to ensure that the proposal is ratified and carries a legal originating number. Then it is printed and the proposal is distributed to all creditors. The court does not have an active part to play in this process but the CVA proposal, that is sent to creditors, must be a true signed copy of the document filed at court.

### **After the Proposal is completed:**

1. The proposal must then be sent to all creditors, who then consider it for the minimum notice period as above before the creditors meeting can be held. This is usually held at an independent venue (theoretically at the convenience of creditors).
2. We find that the HMRC team, called the Combined Voluntary Arrangement Service prefers to have up to 3 weeks to consider the proposals, so we always allow more than the statutory 14 day minimum period for consideration.
3. The meeting will be chaired by the advisor or an Insolvency practitioner (IP). Creditors are sometimes represented by technical professionals from other insolvency firms. The aim of the meeting is to allow the creditors to question the director's proposals; however it is not a place for settling disputes.
4. At the meeting the creditors vote on the proposal and the proposal will be approved if a majority vote of 75% by value of the total value of creditors at the meeting (whether in person or by proxy) vote in favour. A second vote excluding connected creditors is taken and provided that not more than 50% of creditors vote against the proposal it is approved.

**For a very simple example of votes at a creditors meeting see below**

### **Company Voluntary Arrangement - Example Voting**

Example of Voting at an CVA Creditors Meeting

£  
 Total PAYE Debt 22,000.00  
 Total VAT Debt 25,000.00  
 Total Unsecured Creditors 250,000.00  
 Employees Claims 33,000.00  
 Total Debt in CVA Proposal 330,000.00

Present at Creditors Meeting

PAYE 22,000.00  
 VAT 25,000.00  
 Unsecured Creditors 121,000.00  
 Total Votes Cast 168,000.00

In Favour 159,878.00  
 Reject 8,122.00

Total %age in Favour 95.17%  
 Total %age Rejecting 4.83%

Proposal Accepted

YES

REMEMBER IT IS 75% OF THE VALUE OF THE VOTES CAST AT THE MEETING THAT COUNTS. IF IN DOUBT ASK KEITH STEVEN FOR GUIDANCE ON 07974 086779.

5. **In our experience the voting at meetings is an area that concerns many directors.** Well, provided the work has been done thoroughly before the CVA is filed at court then the worry should be reduced. In our CVA's the Combined Voluntary Arrangement Service, (CVAS) which represents the HM Revenue and Customs, will always support viable proposals that are well built and show proper care and attention to detail.
6. Given that the CVAS often represents the largest votes, then we ensure that they are comfortable with the CVA process very early in the cycle of events.

7. Proper communication with creditors is a vital part of KSA's strategy for helping you build a CVA deal.
8. The Chairman controls the ability to vote and provided creditors have been asked to consider a sensibly structured deal, almost all proposals are accepted by creditors. Also the creditors may wish to modify the proposal - once again the modifications need to be approved by the majority votes above.
9. This is often done by the HM Revenue and Customs agencies to ensure future debts are paid on time and future filing of tax returns is done correctly. Occasionally other creditors may ask for a modification to the proposal.
10. At the same time as the creditors meeting, the members (shareholders) meeting is held. Members decide whether to accept the proposal as made or modified and a vote of 50% in favour is required.
11. If both meetings approve the proposal, then the meetings close. The chairman must then issue a chairman's report, within 4 days, to all creditors and the court, stating what happened, who voted and how they voted.
12. Once approved, all notified and included creditors are legally bound for the debt "frozen" in the proposal. No further legal action (except by leave of court) can be taken against the debtor company and the creditors will receive dividends from the supervisor as described in the proposal.
13. After the approval the company must make the agreed contributions to the trust account administered by the supervisor. Failure to keep up with contributions is deemed a default and the company voluntary arrangement can be "aborted". This usually leads to liquidation or receivership.
14. In our opinion the best way to avoid this is to structure the deal on the following basis. Prudent forecasts of directors should be further scaled back and modest forecast profits should be used as the basis for contributions BUT:
  - 14.1. No more than 50% of profits after tax and debt repayments over the deal period should generally be contributed.
  - 14.2. Contributions should be stepped to match profits achieved.

- 14.3. Any lump sum contributions during the currency of the CVA should be avoided where possible unless assets are being disposed of as part of the CVA programme.
- 14.4. The use of a profits ratchet allows higher repayments if modestly forecasts profits are exceeded. (This is a standard requirement of the HMRC).
- 15. **Even if the approach outlined here leads to small dividend repayment levels to unsecured creditors, the creditors usually prefer sensible contributions to hopelessly optimistic forecasts.**
- 16. **NB: there is no minimum %age payment required by law**

Provided the company conforms to the CVA proposal and makes its contributions, then the CVA continues for the agreed period. The supervisor is generally not involved in the business (in our CVA's). **THE DIRECTORS REMAIN IN CONTROL.**

### **What if things don't go well?**

If the company is not performing well and yet it would still appear to be viable, then it is theoretically possible to reconvene the creditors meeting at any time to ask the creditors to consider amendments. If the Supervisor has concerns, he can also ask the court for directions. In most cases the directors should inform the supervisor if there are any material changes to the company or its business.

### **What happens at the end of the CVA period?**

Once the agreed period is completed and the supervisor has issued a completion certificate, then the company leaves the CVA state. Any remaining unsecured debts (where partial repayment was approved) are written off and the directors continue to run the business for the shareholders.

It is also worth pointing out that the CVA is not a panacea for your company; but it is a very powerful framework for change and protection of a distressed but viable company. In reality although difficult to propose and get approved, getting the CVA approved is the easiest part of a rescue/turnaround– making a turnaround work is much more difficult and needs professional help.

**Remember:**

The CVA should aim to:

- Maximise creditors' interests.
- Preserve viable but distressed businesses.
- Preserve economic activity and save jobs.
- In time return value to the creditors.
- Provide a real prospect of a return for shareholders

## **Company Voluntary Arrangements - Worries and Mistruths!**

**We cannot use the CVA mechanism because:** Or the classic worries we have heard for the last 25 years doing CVA's!

So, you are considering a CVA, or your accountants or other advisors have carefully recommended using the CVA to rescue and restructure the company. But the directors have a lot of fears and worries about taking this path.

Clearly, this is a huge decision for the directors to make. Make it wisely by reading all of the relevant pages in this guide.

### **We will lose our clients and candidates (customers)!**

No, you will not. In over 500 cases people have said this to us and we understand why.

But, in practice, we have rarely seen a customer walk away from a business that is delivering its products and services; well and on time. Shouldn't that be your focus?

Stop firefighting and get back to doing your main roles. This way customers will stick with your company.

But keep at the old firefighting and sooner or later your performance will falter and their business may suffer. THEN you may lose them.

### **Should we tell our customers then?**

Many people say "we cannot tell our customers that we are doing a CVA or they will walk away". That is your decision and one that should be based upon knowledge of the business relationship, their requirements and any contracts. Sometimes the best answer is to tell them with professional CVA advisors in attendance. Often this is better than a competitor telling them that you have "gone bust"?

Think what you would feel if a major supplier did not tell you of their problems and their plans to deal with it, but instead they hear from a local rival that you have "gone into liquidation"?!

### **Our creditors will not supply us!**

Yes, they will. They need to maintain their sales to your company, as much they don't like losing the money owed. We spend a lot of time on "creditor liaison". By carefully explaining what the company is doing, how it will be in their best interests and asking them to work with the company and ourselves we ensure that creditors are kept informed and on side.

Don't expect any credit terms or any favours but being honest and open with them pays dividends in the long run. After all, it would actually be simpler to simply liquidate and walk away wouldn't it?

You are trying to maximise creditors' interests by doing the CVA, thus it's in their interests to work along with the plan.

### **Our staff will walk out!**

Generally, they will stay. If they walk out they will lose any employment rights and will not receive any redundancy, lieu of notice payments from the company or the DBIS. Further, they will not be eligible (generally) for unemployment/job seekers benefit.

So, I recommend being open and honest and working out a plan for and with the employees. Proper communication is vital.

Some employees may lose their jobs as part of the restructure; this is painful and at times inevitable. We can work with you to achieve this.

### **The bank will appoint a receiver/administrator!**

**Again this is simply not true** IF a cogently structured plan and a well, presented approach to the bank is used. In 15 years I have only see a bank do this once or twice and that was because they did not believe the directors were acting properly.

Most banks are much more supportive now of "out of court" restructurings like CVA, as it avoids the usual asset meltdown and costs of say administration. Although the CVA cannot affect the rights of the bank or lender they are stakeholders and should be closely involved in the process.



## HM Revenue & Customs will not support a CVA!

Yes, they will if it is a properly structured, well thought-through plan and the company has been compliant with tax rules in the past.

The HMRC agency that decides on these proposals is called the Combined Voluntary Arrangement Service. Currently it votes in favour of c. 73% of all proposals. However, we have a >80% approval record.

The VAS has a website that sets out their policies here>>> [https://](https://www.hmrc.gov.uk/manuals/insmanual/ins10105.htm)

[www.hmrc.gov.uk/manuals/insmanual/ins10105.htm](https://www.hmrc.gov.uk/manuals/insmanual/ins10105.htm)

## What if a Creditor Starts Legal Actions?

In 1995 case law was reported that provides a very powerful argument. **Re Dollar Land (Feltham) & Ors [1995] BCC 740** reported that the court decided that a winding-up order should be rescinded if there was a real prospect that CVA proposals would be approved by the company's creditors. In other words let the creditors' majority decide.

We use this argument to STOP petitions being issued in the first place, saving the creditor money for costs and fees and also removing the risk of the petition against the client.

If a petition is already issued before we're appointed to assist, and a hearing date is due before we can file the CVA meeting notice, we talk to the plaintiff to get them to stop their actions as above, or to prevent the advertisement of the petition. Usually the petitioner is the Crown (HMRC).

Most HMRC petitions are stopped or adjourned in this way, so we can get on with the CVA production. This is a powerful approach that is built on common sense and a case that said "look is it equitable for one creditor to knock a company down when all the other creditors may agree a CVA"? Obviously not and we've defeated petitions in courts across the UK this way.

## Aggressive Petitioners?

If the petitioner will not withdraw or threatens advertisement, the company could use an application to Court to request a hearing adjournment and seek a Validation

order from the Court saying that the hearing is adjourned and the company can progress the CVA proposal to filing and creditors meeting.

The bank account is usually frozen by the bank if the petition is advertised, although there is no legal requirement to do so. So by obtaining the validation order the bank can then reopen the bank facilities.

So, we believe that by careful discussions and complete honesty with creditors, using powerful case law and common sense we can effect a **de facto moratorium** that works in virtually every case.

### **Dealing with Secured lenders – Banks, Leases, Factoring and CID.**

Many of our clients are very worried that the secured lenders will not support the restructure of the company using a CVA or a pre-pack Admin.

All major clearing banks have a pretty healthy approach to restructure where the directors are acting responsibly and quickly. Banks fear control is taken away from directors by petitioning creditors like HMRC or suppliers.

So, when a company is at risk (and generally the bank will know there are difficulties even if the board has kept quiet) the bank will monitor events, filing of management information, County Court Judgments and other legal actions.

In our view, it is always best to get the bank involved as soon as appropriate. Usually we advise clients to go to the bank with the solution generally mapped out. This may require a plan in writing or PowerPoint Presentation and at least a semblance of a CVA proposal with a statement of affairs even if the finished article is some way off.

In general terms the bank will see the CVA as positive because it helps cashflow, reduces the risk of creditors' legal actions and it shows the board is acting professionally and properly in a timely fashion.

The bank manager or factoring manager will often pass the client to the bank's special risk teams for assessment and review.

Bank debentures and lending facility letters generally provide for the bank to appoint a receiver or administrator in the event of default. This is known as the

bank's remedy. But this is very rare in a CVA scenario. The bank will prefer to keep its powder dry and keep their remedy in abeyance.

The bank will generally not want to appoint an administrator or receiver, because this could lead to a reduction in the value of assets and in the business itself. In many cases the bank would see a lower recovery and therefore seek to rely upon personal guarantees.

A CVA does not normally impact upon the bank's security and may not crystallise losses unless agreement is reached with the bank as part of the CVA scheme.

A well structured CVA can greatly improve the bank's recovery, maintain its security and remedy and so the banks are, in our experience, very supportive of a well structured CVA recovery plan.

It is possible that a CVA alone cannot provide the working capital improvements needed. We have frequently asked for capital payments holidays for lease and HP agreements and bank loans. If a good case is made using quality financial forecasts and cashflow projections then often the secured lender(s) will agree to help the company through the dark periods ahead.

Banks want to support their customers, they don't want to knock the business down and see a possible loss. Even with personal guarantees in place, they will seek to find solutions with the company's board.

HOWEVER, don't "act", don't provide the bank with information and don't seem to "get" how bad things are and the bank can appoint investigating accountants or even worse administrators very rapidly.

### **What are investigating accountants (or reporting accountants)?**

When a business has financial or operating difficulties it can often breach its borrowing facilities from the bank or from factoring companies. This can lead to bounced cheques, problems with the payments of direct debits, missed loan repayments and generally builds pressure on the cashflow.

Banks have quite sophisticated systems for monitoring this risk, but often they are "in the dark" with regard to the up to date financial performance of the company

that owes it the money. One way of addressing this is to demand (as their borrowing conditions usually allow) detailed and up to date information from your company.

If such information is difficult or impossible to produce because of failings in the financial reporting systems within the business then they will worry that old and out of date information is being used to run the company and their lending could be at more risk.

You may have noticed by now that bank's do not like risk! So the next remedy is to insist upon the introduction of investigating accountants. This will normally be paid for by the company, thus the act of appointing investigating accountants could lead to further breach of the facilities!

Investigating accountants (IA) usually have a brief to investigate the following

- Cashflow, current daily and for say the next 12 months, month by month.
- The current profit and loss activity, previous results and forecasts for say the next 12 months month by month.
- Performance against your past forecasts (in other words can your forecasting be relied upon).
- They will investigate the current creditors and forecast that for say the next 12 months month by month. They will look for red letters from creditors leading to CCJ's Warrants, Statutory Demands and winding up threats.
- They will check to see if the company is up to date with the Crown creditors (PAYE and VAT), or if in arrears.
- They will check the quality of debtors in the business.
- The strength of financial reporting will be assessed, as will the people involved.
- They will look at the business and marketing plans and check whether they are fit and feasible for the business.

Taking all of the above into consideration they will then write a report for the lender to state the options the lender should consider and what their recommendations are.

The options they can outline for the bank are not covered in this guide (see [www.companyrescue.co.uk](http://www.companyrescue.co.uk) for more in-depth guides to receivership, administration, liquidation), advancing more money to help a short term requirement (yes that does happen!), withdrawing banking facilities, asking the shareholders to put more money in etc.

### **What will this cost?**

Well the answer is how long will it take and who is doing it. Usually it is an insolvency practitioner and some of his/her managers/admin staff as a team.

I have seen IA's charge anything from £7-10,000 to £200,000 depending upon the complexities and size of the company or group. BUT the bank almost always insists that the company pays for this as their terms of lending do allow this.

Even if you refuse to pay and refuse to issue a cheque, the bank has the ability to "dock" the money from the company's account!

### **But we cannot afford that?**

Yes, that's part of the problem. You can always refuse to pay and state that the board/finance managers will do much of the information provision, but generally there is a significant cost and it is seldom that the bank gets the work done for nothing or agrees to pay for it.

All the more reason to go to the bank and show your funder you are acting with a CVA and as a board, not sticking heads in the sand.

### **Will we see the report?**

Often no, however if you have a cooperative approach then the bank will share some or all of the report with you. Often the recommendation in the report remains confidential. So you may pay for it but you often cannot get access to it.

### **Will we have any input into the report?**

It's much better to take part and put your views across forcibly with good information to back it up. So if you have not got that level of information (particularly as described above allied to information on orders, sales, enquiries, marketing, restructuring plans, downsizing and cost cutting) then you must get it to get your views across.

### **Who can we get to help?**

You can often get assistance from your accountants/auditors. But if they're not up to speed with the problems, then that can be counter-productive as they will generally look on negative information as a weakness that the bank may exploit.

We can help your business prepare restructuring plans; we have worked with dozens of companies and advised them how to plan their actions when the bank starts putting pressure on the facilities and asking for investigating accountants. Then we will normally help present those plans to the bank, this may avoid investigating accountants or indeed reduce their negative reports to the bank.

**Our adage is "go to the bank with the solution not the problem"!**

In a pre-pack administration or trading administration the administrator MUST pay the PAYE and VAT during his appointment period. So, you can see in CVA the business can generate improved cashflow and working capital.

## Case Studies

### Case Study: Pre-Pack Administration for a Recruitment Company

As licensed insolvency practitioners we are never really shocked at the things we hear and see. However, the scale of the fall in sales in this London based recruitment company was stunning.

From sales of £3m pa and making £250,000 net profit in 2007-8 financial year, this business was hammered by the recession and saw sales fall to under £600,000 pa, making a loss. The legacy debts to HMRC were much too big for the now smaller company to repay and the directors were like rabbits in the headlights. How could the company repay hundreds of thousands of tax debts, get rid of a lease on a too-big office and keep the business functioning? They had let most of the 25 recruitment consultants go keeping the most productive sales people, so costs were now lower but the ball and chain of the debt remained.

KSA considered a CVA solution first for this business but the CVA would have been difficult enough when a winding up petition was threatened and delivered by a supplier. A third party also had approached the directors offering to assist and fund the business in future. The deal was the third party investor would look after the financial reporting, offer space in its own offices and provide guidance to the management. The plan was for a new smaller business with nil debt and the "oldco" directors would be shareholders in "newco". After being dragged down emotionally by the debt pressure, this was too good an offer to refuse.

The third party investor recognised the skills of the directors and the retained sales consultants, along with a good client base. It is a national consolidator of recruitment companies and as such wanted to buy the business without the risk of taking on the debt in a CVA.

Our IP's agreed to act as administrator and we set out the plan to pre-pack the business. Now many readers will be aware that there is a stigma attached to pre-packs, many commentators (including Newsnight's Jeremy Paxman!) have attacked pre-packs as scandalous. Yet the Government wants to see businesses survive especially in this recession, the Enterprise Act, actively encourages Company Rescues. So the key to pre-pack administrations is to DO IT PROPERLY from the outset.



Under Statement of Insolvency Practice 16 (SIP 16) the process is carefully controlled by the Insolvency Service and its vital to do it properly or the Insolvency Practitioner and directors of oldco can face attack by creditors. So our plan always sets out to comply with SIP 16 and best practice. Here are the suggested solution recommendations we set out for the client.

### **KSA Group - Proposed Pre-Pack Administration Solution for "Oldco Ltd"**

- Third party investor will support new company (newco) with
  - Non executive directors, centralised procurement,
  - High quality financial management
- Directors of (oldco) can move across to a professionally managed company
- Newco will acquire Goodwill, **trading name** and assets of oldco
  - Cost of assets to be determined by Royal Institute of Chartered Surveyors (RICS) Valuation
  - Deferred consideration for asset purchase as required
  - Newco will also acquire work in progress - for say 33-50p in £1
  - Debtors collected by invoice discounters any balance goes to creditors post administration
  - New factoring facility required
- Removes creditor pressure, oldco either liquidated in future or dissolved
- Short preparatory period, very swift execution period
- Clients and candidates largely unaffected or aware

- Refocus oldco directors on running the new business
  - Drive sales past break even, supported by professional team
- Initial new board remains in control until post creditors meeting (3 months)
  - Oldco directors join board of newco post creditors meeting
- Shareholders' have clean vehicle
- Possible small dividend to oldco creditors of 1-10%
- **Possible risks and downsides**
  - Directors conduct investigation for Oldco directors
  - Possible security deposit required by HMRC for Newco (unlikely)
  - New banking / factoring facilities required
  - No guarantee Asset Based Lenders will agree to novate asset finance to newco
  - NB: All insolvency processes carry risk for the oldco company directors
  - Cost of administration, valuers, lawyers.
  - Initial pre-administration advisory fee
  - Administration fee will be collected from realisations post administration
  - TUPE issues apply in Administration, all employees would be employed by newco
  - The directors may have a conflict of interest with regards to oldco and newco issues and may need to consider obtaining independent legal advice on this issue

The business was sold to the newco funded by the third party investor and is trading well. A small dividend of 7p in £1 was returned to creditors thus ensuring a better result for the creditors than a simple creditors voluntary liquidation.

We are experts in business rescue, corporate rescue and company rescue, we can help investors, shareholders, sole traders, partners and directors with pre pack administration solutions.

### Case Study: Pre-Pack Administration for a Suffolk Recruitment Company

Another tale of fast falling sales in the recession of 2009. This small recruitment company had had sales of £900,000. It had fallen sharply though in 2009. We were approached by a large group of recruitment companies to buy this distressed company. The Suffolk business had built up liabilities to HMRC of £70-90,000 and circa £10,000 to other creditors and the landlord. But it had a good name and strategic importance for the future plans of the group.

### KSA's Solutions (and their benefits) for \*\*\*\*\* Recruitment Ltd and ABC Newco Ltd

- **Pre-pack Administration, to newly formed Joint Venture company**
  - ABC Newco Ltd will support new company (newco) with
    - Non executive directors, centralised procurement,
    - High quality financial management
  - Directors of \*\*\*\*\* (oldco) can move across to a professionally managed company
  - Newco will acquire Goodwill, trading name and assets of \*\*\*\*\* Recruitment Ltd
    - Cost of assets to be determined by RICS Valuer (value say £5k)
    - Deferred consideration for asset purchase if required

- Newco will also acquire work in progress - placements made of £20,000 for say 50p in £1
  - Debtors collected by \*\*\*\*\* (Invoice Discounters) any balance goes to creditors post administration
- Removes creditor pressure, oldco either liquidated in future or dissolved
- Short preparatory period, very swift execution period
- Clients and candidates largely unaffected or aware
- Refocus oldco director on running the new business
  - Drive sales past break even, supported by professional team
- Initial new board remains in control until post creditors meeting (3 months)
  - Oldco directors join board of newco post creditors meeting
- Shareholders' have clean vehicle
  - 75% equity Mrs A
  - 25% equity ABC Newco Ltd
- Possible small dividend to oldco creditors of 1-10%
- **Possible risks and downsides**
  - Directors conduct investigation for Oldco directors
  - Possible security deposit required by HMRC for Newco (very unlikely in this case)
  - New banking / factoring facilities required
  - No guarantee Asset Based Lenders will agree to novate asset finance to newco
  - NB: All insolvency processes carry risk for the oldco company directors
  - Cost of administration, valuers, lawyers.
  - Initial pre-administration advisory fee £4,500
    - Administration fee will be collected from realisations post administration

- TUPE issues apply in Administration, all employees would be employed by newco
- The director may have a conflict of interest with regards to oldco and newco issues and may need to consider obtaining independent legal advice on this issue

### **Timetable**

Appointment of KSA to act as informal advisors to the company – w/c 1st June 2009

Pre administration “discovery phase” – 2 weeks

Petition High Court for Administration order say w/c 15th June 2009

From the above you can see we laid out a clear plan to close the old company down, sell the business to a newly formed company with strong management, access to central reporting and also investment from a large recruitment group. The plan was agreed by the company and the ABC Newco board.

Our IP's agreed to act as administrators and we set out the plan to pre-pack the business. Many readers will be aware that there is a stigma attached to pre-packs, many commentators (including Newsnight's Jeremy Paxman!) have attacked pre-packs as scandalous. Yet the Government wants to see businesses survive especially in this recession, the Enterprise Act, actively encourages Company Rescues. So the key to pre-pack administrations is to DO IT PROPERLY from the outset.

Under Statement of Insolvency Practice 16 (SIP 16) the process is carefully controlled by the Insolvency Service and its vital to do it properly or the Insolvency Practitioner and directors of oldco can face attack by creditors. So our plan always sets out to comply with SIP 16 and best practice.

All the remaining jobs were saved in this Suffolk business and the new company is trading reasonably well .

### **CVA for London Recruitment Company. Sales of £3m:**

This company had 3 offices in London offering recruitment services in accountancy and media. A fast expansion plan had backfired and costs ran ahead of budget and sales! Big losses were made quite rapidly and being a provider of temps its PAYE debts were very high as a result.

The owner was based in the southern hemisphere but a local MD was trying hard to get the train back on the tracks without any success.

HMRC had been asked for a time to pay deal and he was getting some positive noises, but then the collector decided to change tack and issued a winding up petition.

The MD had heard of our website from a friend who told him to get help fast.

We requested that HMRC did not advertise the petition and they agreed, 3 months later the company had a strong cash balance as it did not have to pay PAYE and VAT for that time using the CVA approach that we designed.

The CVA proposal was that it would pay 50% of its future profits after tax and a one off £150,000 was paid across the supervisor within 3 months. The overall dividend for creditors was over 55p in £1. Thus the creditors (mainly HMRC) got a good return in year 1 and were happy to accept the CVA proposals.

Despite the directors worrying about the creditors meeting no one showed up at all which is quite common for us.

### **KSA Group used a company voluntary arrangement (CVA) to rescue a recruitment business based in Scotland**

A Scottish based recruitment business approached KSA Group as it was struggling having seen its turnover fall from a peak of £6.75m to c. £3.5m.

Additionally, and crucially, the business had suffered from bad debts from customers linked to the construction industry. Debtor collection was slow and there were a number of invoiced debtors that the factoring company referred back to our client for collection due to the age of the debts. This ultimately caused the company to suffer worsening cash flow problems.

Our client was on a time to pay deal of some £43k a month with the HMRC and was not able to make the next payment. Trade creditors amounted to £80k and HMRC was owed some £237k for PAYE and £299k for VAT. Even if sales rose, the company's working capital could not sustain the monthly repayments under the time to pay deal and the ongoing monthly payments.

Our initial discussion highlighted another regular problem, the fact that the company director had a significant [overdrawn directors' current account](#). Mr M had been taking money out of the company using drawings with a view to future dividends. As the company had no profits to distribute, he was in fact now a company debtor to the tune of £75,000.

So, the business [failed the insolvency tests](#). KSA Group's standard approach for every client that we meet is to provide an independent report to the board on the options available. These included liquidation, administration, pre-pack administration, company voluntary arrangement and selling the company

However, the business still had some good orders going forward, and was a viable business if the legacy debts were restructured. Having considered all the options it was decided that a company voluntary arrangement was the best option. A "profit ratchet" was built in to the CVA to ensure that if the business made more money than originally predicted then further payments would be made into the CVA. The business was advised to terminate their lease on one of their offices and any future rent liability would be bound into the CVA, staff costs were reduced and creditors were paid in instalments.

Mr M agreed to repay the overdrawn directors current account by paying an initial £20,000 and then the balance over 60 months, the CVA being 5 years long. His salary was increased to allow for this.

If you listen to critics in Scotland they will tell you that no CVAs are supported by HMRC! On the contrary the HMRC team that deals with Scottish CVA's attended the meeting and took part in the process. The CVA vote was 100% in favour and the CVA was accepted by creditors in December 2009 paying 33p in £1.

The business continues to trade quite well even though the Scottish economy continues to suffer. Our client has been profitable in the first 9 months since the deal was approved. Mr M is so happy with KSA's work that he has referred a hotel and another recruitment company to KSA for advice and he will act as a referee for KSA

If your recruitment company has similar problems why not call Sarah Massey and ask for her advice. 01289 309431 or 0800 9700539.

**Free call national helpline on 0800 9700 539, London 020 7877 0050, Birmingham 0121 378 0671, Berwick 01289 309 431 or Newcastle 0191 482 3343.**

THINK OUR INNOVATIVE TURNAROUND APPROACH COULD BE A USEFUL TOOL TO HELP YOUR RECRUITMENT COMPANY? THEN YOU NEED TO TALK TO US NOW.

CALL 0800 9700 539 AND ASK FOR KEITH STEVEN.

Therefore, our strongly held view is IF THE BUSINESS IS VIABLE that the flexible CVA model is the most effective route forward. The bullet points of the suggested CVA strategy are:

- **Propose CVA in 2-4 weeks, use period to build outline plan, work out requirements**
- **Buy breathing space, remove freneticism, allows controlled restructure. Get you focused on your jobs.**



## CVA V Administration (plus or minus pre-pack) for ABC Recruitment Ltd – A comparison table

### CVA Approach

Control – directors remain in control. They are helped by KSA. Obviously some directors do not want such close involvement.

Breathing Space. Time to deal with the potential loss of confidence of any suppliers. Allow detailed analysis of the business requirements, production of marketing and business plan.

Creditors receive dividends over time, they will be happy to receive that and KEEP a customer.

The fees are not insubstantial for a CVA. They have to be paid out of cashflow. However, see below, cashflow is much improved by the CVA process. Effectively the tax man pays for the deal.

**Leverage tax debts into the CVA. By not paying VAT PAYE until the CVA is approved.**

Most overdrawn director's current accounts can be reversed back into PAYE. Increases tax debt but generally no action against the director.

Time defined process – fixed date of creditors meeting means crystallising of position. KSA talks to creditors, removes pressure from directors.

Flexible plan under the CVA, we would forecast minimal monthly contributions to the CVA as profits will be low in year 1. Profit related ratchet kicks in if the business exceeds profit forecast.

### Administration Approach

The Administrator is in control. He decides if company is sold, liquidated or put into CVA. Directors have no control or input.

Breathing Space to allow restructure, sale or closure. Company can propose a CVA if management and finance available.

In pre-pack creditors receive very little dividend but may keep customer if they supply newco. If Admin followed by CVA they receive dividend.

Administration fees would be higher than CVA. Administrator controls the cash and takes his fees as he needs them (subject to later ratification from creditors).

Lawyers generally must be involved and they cost!

Administrator MUST pay tax and VAT during Admin period. If pre-pack used then the "Newco" must also pay tax and VAT from the outset. NO tax leverage.

If not cleared before any Administration directors are required to **personally repay the loan**.

Equity value of the business written off. (Unless CVA proposed after Administration). Loans written off. You would have to "buy back" the business if pre-pack. Or third party can acquire it.

All invoices, purchase orders, faxes, emails and letters will have to state the company is in Administration. This would severely damage marketing and sales.

Does not apply in pre-pack.

Protects the company from aggressive action by creditors. Exclude critical creditors but likely that company will have to pay upfront (pro-forma) for new services/ supplies.

Unsecured creditors generally lose their money, no exceptions. Newco would have to pay upfront (pro-forma) for services/supplies.

The company can utilise current work in progress to turn into cash. Collect out WIP & debtors. Both over time and with no reduction in asset value.

If not a pre-pack the business will be advertised for sale as a matter of course under SIP 13. Under SIP 16, may have to market business surreptitiously Could be several interested parties who will need to be shown around and sales memorandum prepared. Debtors harder to collect.

KSA "quasi" Finance director involved going forward to help structure the financial reporting of the business, attract investment, adherence to CVA plan and building the final business plan.

If a trading Administration, the directors can be instantly removed without recompense under s13 Insolvency Act 1986. Administrator can appoint directors or managers.

**No investigation into directors' conduct.**

Investigation into the conduct of the officers in the 2-3 years up to the terminal insolvency of the company.

**No protection if the CVA fails quickly and liquidation follows.**

Could lift veil of incorporation and commence actions for recovery against officers.

## **Summary:**

Considering the advantages and disadvantages of the two options, our strongly held view is that the CVA model is the most effective route forward for most struggling but VIABLE recruitment Companies. The bullet points of the suggested CVA strategy would be:

- **Propose CVA in 4-8 weeks, use period to build outline plan, work out requirements. KSA controls the creditors for you.**
- **Buy breathing space, remove freneticism, allows controlled restructure. Get directors focused on your jobs not firefighting and fighting the Tax man.**
- **Recover control and refocus directors on the company.**
- **Get CVA approved, help to restructure and attract new profitable business.**
- **Save a viable business.**
- **Avoid the possibly huge meltdown of Administration or pre pack/liquidation**

- **You can still sell the business in future out of the CVA under board's control.**

## **Wrongful trading, Preferences and the other rules to be aware of.**

A man in the pub said to me if your company is insolvent, then this is Wrongful Trading"!

### **What is Wrongful Trading?**

We are often asked what this means because directors have talked to their accountants, advisors, insolvency practitioners or a man in the pub. They may have said "be careful if your company is insolvent then **you will be guilty of "wrongful trading"**!"

Often this is simply not true! The simple explanation is this:

Is the [company insolvent](#)? If yes then the directors must act properly and responsibly. If they do not act properly or the way any reasonable person would have acted, then this may possibly be seen as acting wrongfully.

If wrongful trading is proven, then the directors can be made personally liable for the company's debts from the time they knew the company was insolvent.

### **The tests for wrongful trading actions include:**

1. Not filing Annual Returns for the company at Companies House.
2. Not filing annual or audited accounts at Companies House.
3. Not operating the PAYE scheme correctly, failing to pay PAYE and NIC when due.
4. Not operating the VAT scheme correctly.
5. Taking excessive salaries when the company cannot afford them.
6. Taking credit from suppliers where there was no "reasonable prospect" of paying the creditor on time.
7. Willfully piling up debt.

## 8. When in a hole keeping digging!

Please note you don't have to tick all of the above tests to be at risk of wrongful trading!

Formal insolvency procedures

But this can only apply in terminal insolvency. Wrongful trading actions can only be commenced after a formal insolvency event. What is a formal insolvency event?

What if there is no insolvency event?

The actions may occur and the company may not enter any formal insolvency. If that happens then be very careful! Keep records of why returns were not filed on time. Write careful minutes of board meetings and shareholders meetings. Keep them safe. In future they **may help protect you as a director.**

The common sense answer to wrongful trading is – if your company is insolvent and you know it – DON'T KEEP DIGGING THE HOLE! Take advice from us immediately on 0800 9700539.

## What does not operating the PAYE/VAT scheme actually mean?

Not paid the deductions of PAYE and NIC across to HM Revenue & Customs? Well, as you will now know that is something that they do not like! Basically, its tax payer's money and the collectors are there to collect it.

HMRC (what was the Inland Revenue and HM Customs & Excise previously as separate government organisations) now has a central database and can spot slow payments or missed payments much more quickly now.

If your company is not paying PAYE & NIC on time then it is probably insolvent, so see our guide to "[Is our company Insolvent](#)".

Non payment of tax is a failure to comply with the tax legislation and also signifies publicly (loud and clear to HMRC) that the company is potentially insolvent. So, you need to act properly and deal with this serious threat to your company.

**If the company is still viable but just needs breathing space why not propose a time to pay deal? See our [guides to time to pay deals](#)**

## PERSONAL LIABILITY

Remember that if the company is insolvent you could be personally liable for the debts, if you continue to trade, whilst doing nothing about the problems that it faces. Wrongful trading can be a real problem where ongoing tax arrears are building up and the company later enters [insolvent liquidation](#).

So, act carefully, keep notes of any decisions and always write names of people you speak to at HMRC down. Take advice from experts, above all act promptly as delay may just lead to more problems for you as directors.

### What are the Available Options?

1. [Time to Pay Deal with Tax and VAT](#). Why not use our expert programme, written by our MD Keith Steven, we guarantee you'll get a time to pay deal with HMRC or your money back.
2. [Trading out](#), visit this guide to how to deal informally with the problem. This can avoid formal approaches like [Voluntary Liquidation](#), CVA, Compulsory Liquidation and Administration.
3. Some tips...on time to pay deals.
  - 3.1. Don't wait until legal actions have been taken against the company to ask for a "time to pay" deal with HMRC.
  - 3.2. Try to plan the cashflow of the business well in advance - you have a legal obligation to do this! If the directors do not think the company

has sufficient cash to trade they should consider the obligations and options and plan a way forward.

- 3.3. Don't be too ambitious in planning repayment; you will have bad months as well as good, so be careful with the cashflow forecasts.
- 3.4. Ask for 18 months to pay back PAYE, knowing that you will probably get 6-9 months at most.
- 3.5. Ask for 6 months for VAT.
- 3.6. If your cashflow forecast says you cannot afford that fast a repayment programme, then consider a company voluntary arrangement - CVA.
- 3.7. We think that, if the company is viable but insolvent, this is the most powerful way of dealing with a serious cashflow problem and tax arrears (which proves insolvency).

2.1. Important tips, HMRC supports well proposed CVA's!

2.2. Secondly, you do not have to pay back all of the debt.

2.3. Thirdly, you remain in control.

2.4. Fourthly, the creditors pay for the CVA!

4. Do Nothing! Are you serious? Actually this will lead to:

- 4.1. Bailiffs, Sheriffs, walking possession, distraint and more worry - see here for How to deal with [Legal Actions](#) .

**So, don't risk wrongful trading, it could lead to personal action against you, the loss of your home, your marriage and bankruptcy.**

**Directors Overdrawn Current Accounts? Why do they matter and what can we do with them?**

**Directors' overdrawn current accounts in Recruitment Companies.**

In more than 75% of our enquiries from directors of struggling companies, we find that this is a major problem, so what is an overdrawn director's current account?

Well, usually the company is making some profits and your accountants advise you to save tax by paying your directors a small salary and then you take dividends from the reserves of profits made in the past and current years. SO off you go taking money out of the business as instructed.

## **THEN something goes wrong!**

Although the advice is generally sound from a tax reduction perspective, when a company is performing well; it's when things go wrong that directors can end up with serious personal liability problems.

### **Technical Issues**

Having an overdrawn director's current account is actually a breach of the Companies Act 1985. All accounts filed at Companies House should refer to any overdrawn Current accounts as loans to the director concerned. You must try to get these paid back or reversed in subsequent periods as the Revenue will tax you on a fairly penal rate if you do not.

If the company has no distributable reserves, it cannot pay dividends. So if your company's balance sheet starts a year with nil or negative reserves, then if you make no profit you **MUST STOP** taking dividends as soon as you are aware of this.

It is much better to pay yourselves through PAYE and pay the tax/NIC. If the company cannot afford to pay you GROSS - then it is pretty much insolvent.

What can we do? Well options include:

- Repay the debt you personally owe to the company.
- Offset any loans the directors have made to the company (this is called set off).
- Take your full salary but reduce the cash you take out of the business to gradually offset the account. So pay yourself £4,000 per month but take £1,000. Remember to pay tax on the £4,000!
- Make a lot of profits in future periods to offset it!

## **What happens in liquidation if we have overdrawn current accounts?**

In liquidation the liquidator can demand that directors repay their overdrawn directors current account to the company for the benefit of the creditors. They can take legal action to make directors pay this or even make you bankrupt. **So you could lose your house if your director's current account is overdrawn and not recovered.**

### **Example Case Study**

So, here is an example case study / guide. If you need more detail call us now.

#### **See if this rings any bells and then call us for help.**

Mr Jones and Mr Smith set up a limited liability company based in London. It is a recruitment company and they formed it in 2007.

Sales built quite quickly based upon the contacts in the marketing sector and the company grew to £1.2m sales. Their accountants told them that the company had made £80,000 net profit in year 1 and that this would be taxed for corporation tax purposes at roughly 20%.

So, he advised them to leave their PAYE salaries at a lower level each month in year 2 and take dividends from the reserves and future profits.

This they did for a number of years and paid themselves quite well as the company was profitable each year.

Then that "something happened".

Their biggest debtor client went bust owing the company c. £158,000. Silly to let that debtor take as much credit in my view, but their view was "after all the company was a well known big name customer and we never thought it would fail". And it was good regular business for them so we understand why it got to be such a big debtor.

This led to a situation that was clearly not planned for. In 2008-9 the company had a bad trading year on top of the failed customer and so had to write the bad debt off. This made a huge loss for the year of £250,000.



As a result, the balance sheet then became negative and they saw the first flashes of a cashflow crisis looming.

So no further dividends could be taken AND the directors now had overdrawn directors' current accounts to the tune of £70,000. With cashflow pressure mounting they came to KSA and said they needed to restructure the company or close it.

This was our advice: consider the options, set out your objectives, look at the viability of the company and then make a decision to ACT. **Call KSA in and we will set out the options in writing and in expert detail - that will help you decide.**

### **Stop Options**

If the company entered a formal terminal insolvency like administration, receivership, voluntary liquidation or compulsory liquidation, then the insolvency practitioner/liquidator could have demanded that the directors repay the £70,000 back to the company for the benefit of creditors.

This could have caused them personal financial hardship and with personal guarantees to the bank of over £200,000, the last thing they wanted to do was liquidation or administration. Indeed, it was likely that personal Bankruptcy would follow.

### **Go Options**

So, we looked at the Go Options with them. (By the way we never charge for this detailed advice) and these included Trading Out, Trade Sale, CVA and or refinancing.

The key test is viability. We felt that one bad year and a huge bad debt did not equate to a bad business. Far from it, this was a good business with dedicated directors and staff. So we said look at Go options and try and select the best option with our help.

**We recommended that CVA would be the best solution and this was why.**

In a CVA the debt would be bound by the process. Along with reduction in people and managers (the lost contract meant that they had too many people) the company was forecasting a modest profit at best or just below break-even at worst.

- The benefits for creditors were that they got a deal paying 55% of their old debt back over 5 years and kept their customer.
- The benefits for the company were a downsized business, lower costs; long term survival, no lost contracts and we removed cashflow pressures whilst keeping the bank happy.
- The benefits for the directors were that they avoided personal liability, avoided the failure, avoided bank personal guarantees being called up and also avoided the £70,000 debt to the company.
- Plus, as owners of the company they have long term employment and a valuable future business.
- A great deal all round and guess what? HMRC supported the deal.

**So, if you or your directors have an overdrawn current account and a company that is under real pressure then call us on 0800 9700539. As the above case shows, we can save your business and help you as directors.**

**Employees and CVAs the process of redundancy in CVA and Pre-Pack**

Using CVA case law (Doorbar) the company can terminate the employment contract of ANY member of staff or members. This is often critical in deciding how to restructure direct costs and overheads.

1. Step 1: choose the roles /people to be made redundant.
2. Step 2: pay them to the date they are made redundant, and any holiday pay due.
3. Step 3: issue a P45 and ask them to leave immediately.

4. Step 4: hand them a letter explaining how they can claim redundancy and lieu of notice payments from the Government. They will need to file a RP1 form so they claim. NB they cannot claim until the company CVA is approved (Qualifying Insolvency Event).
5. Step 5: get on with the rescue!

So, the CVA can ride roughshod over employment legislation and normal contractual obligations. This is powerful stuff and KSA has internal experts who can guide CVA clients through this process. We are often asked to remove employees because most people do not know how powerful CVA is.

Now think how you can cut costs knowing that there is no requirement for 90 day or 30 day consultations, no skills matrix process and no risk of a tribunal award knocking cashflow.

Yes, that is right - even if a disgruntled employee is made an award by a tribunal the claim is bound by the CVA process and the Government will pay (to capped limits) their claims.

### **Pre-Pack Administrations and Unwanted Employees**

However powerful a PPA is for getting rid of debts, it has problems such as TUPE.

Generally speaking, under the Transfer of Undertaking rules the new company will have to meet the employment claims of the old company. This means it is practically difficult to remove unwanted employees.

The only way around this is to make unwanted employees redundant well in advance of the PPA process. This could of course lead to employment tribunals if not handled well and it is possible that this tribunal award could be awarded against the new company.

Specialist advice is required when planning pre-packs to ensure that this issue is carefully planned.

## **Summary: Turning Around or Rescuing Your Recruitment Company.**

We hope this guide is useful reading for you and your colleagues. Over many years we have built up this approach of giving good quality guidance to struggling company directors, accountants and investors. We figure that giving free general advice will save many businesses, whilst other people will need our hands-on advice and call us directly.

This programme is work in progress, as we have time, we add more and more content to our "Expert Guides" to assist more and more people. Version two will carry more case studies and worked example, we plan to publish that in mid 2010.

As you will know all recruitment companies are the same and yet all are different – so this general guide may not have answered all your questions. Please feel free to call our expert advisors on the numbers below, or email the author who has experience over 15 years of assisting recruitment companies.

Keith Steven 07974 086779 [keiths@ksagroup.co.uk](mailto:keiths@ksagroup.co.uk)

KSA Helpline 0800 9700539 Open 8.30 am to 5pm weekdays.

### **About The Author**

Keith Steven Turnaround Practitioner, Pre-Pack and CVA Expert!

**Keith Steven is a company doctor and Turnaround Expert.**

**His motto "We save viable businesses; we help you close those that are not"!**

Keith is the author of the content of this programme and all of KSA's web sites. He is managing director of Company Rescue Ltd and KSA - a specialist firm of



turnaround practitioners.

Keith started his career as a retailer and experienced the savage recession of the 1990's first hand. This was before the banks had any idea about dealing with SME's failure. Close struggling businesses first; ask questions later, was the response then. Of course this was driven by insolvency practitioners who wanted big fees.

So he learned a lot in a short time and thought **"how can we help struggling businesses"**?

He joined a specialist insolvency and turnaround firm in London in 1994 and has helped set up two venture capital companies since, specialising in the distressed / turnaround sector. What a great learning curve that was.

Keith is a former director of the UK Turnaround Management Association and an associate of the Turnaround Finance Group.

His website was launched in 2000 and was re-launched in 2011 and 2013. Since then we have added over 200 pages of content and are adding guides and information every week. So, now we have improved it but welcome any suggestions from you, the reader. So we hope our expert CVA guide and our website helps your business.

Over 5,000 people have contacted KSA since Keith launched [www.companyrescue.co.uk](http://www.companyrescue.co.uk) in 2000 and over 500 companies have now been directly assisted by the author over the last 13 years with assignments ranging from large multinational projects with £500m sales to small manufacturing companies with 3 people.

Contact Keith on **0800 9700 539** or **07974 086779** or by email at [keiths@companyrescue.co.uk](mailto:keiths@companyrescue.co.uk)

Keith will do everything in his power to help your business. As a team at KSA most of us have been there and know what you are going through.

**After thought from Keith: “If half of the recruitment people that use this guide chose the CVA path we would see a huge jump in Company Rescues in the UK. Right now most people don’t use CVA because of fear of the process. I think this is a waste of good businesses and huge emotional distress is the result.**

**Obviously, this guide is generalist, we have many years of hands on turnaround experience, and most of the tricks of our specialist trade ARE NOT included in this guide. If your recruitment business needs a rescue, call me.**

**Thank you for using our programme. We hope it has assisted you.**

**Please email any comments or specific questions to**

**[keiths@ksagroup.co.uk](mailto:keiths@ksagroup.co.uk)**

**KSA CompanyRescue's Expert Guide to**

**Turning Around or Restructuring Your Recruitment Company™**