Creditors Voluntary Liquidation:
A Step by Step Guide

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A Guide to Creditors Voluntary Liquidation (“CVL”) for Insolvent Companies

What is a Creditors Voluntary Liquidation?

A CVL is the process by which an insolvent company is formally closed (wound up and dissolved). A licensed insolvency Practitioner (“IP”) must administer the CVL and his/her primary objective is to sell the Company’s assets and maximise the realisations so that these proceeds, after costs, can be distributed to the Company’s creditors. If there are enough realisations to enable a dividend to be paid, each creditor within the class/rank that is receiving a dividend, will get the same percentage of their debt repaid based on their agreed proof of debt claim. For example, if there is £10,000 to distribute to creditors who total £100,000, each creditor receives 10% of their debt back, via the dividend paid to their class.

Each type of creditor is ranked in a specific class banding. This is because there is a set order which the liquidator must repay creditors as typically there is rarely enough funds or realisations to be had which will enable a full repayment to creditors meaning some, and sometime none, get paid. The order or priority of payment which is set out in the Insolvency Act is summarised:-

1. Secured (fixed charge) creditors, such as banks or factoring companies with registered charges – from fixed charge assets
2. The repayment of expenses
3. The Liquidator’s fees and costs
4. Preferential Creditors – Such as the Redundancy Payments Office for any wages or holiday pay sums that they have paid to former employees.
5. Secondary Preferential Creditors – Such as HMRC for VAT and PAYE/NIC debts
6. Floating Charge Creditors – The balance of funds due to secured creditors if the secured asset realisations didn’t repay their debts in full
7. Prescribed part – payment of a prescribed amount of funds kept aside to pay unsecured creditors
8. Unsecured Creditors – Such as suppliers, HMRC for CT debts, banks with no security and directors etc.
9. Shareholders.

The above is a simplified version of the full order of priorities. Specific advice should be sought from a licensed insolvency practitioner for full clarity of your Company’s position.

If there are insufficient funds/realisations to pay a dividend to creditors then the Company’s debt to the creditors are not repaid unless the creditor has obtained a personal guarantee, in which case the Guarantor is obligated to repay the Company’s debts. This is because a limited company is a separate legal entity form the directors or shareholders of the Company. Therefore they have no legal obligation to pay the Company’s debts unless they have signed a personal guarantee.

When is a Creditors Voluntary Liquidation appropriate?

Firstly, it should be stated that there are a number of options for insolvent companies, and determining the most appropriate course of action at the outset is paramount. With this in mind, we would recommend that you seek advice immediately from qualified insolvency practitioners such as Bridge Newland Limited if you believe that your company is insolvent.

However, in general, a CVL is appropriate where the Company is insolvent and has no prospect of a viable future in its current form. The Company is usually not in a position to raise further funding or trade out of its financial difficulties and there is often a risk of further losses being made if trading continued.

Common scenarios include

1. Creditors (such as HMRC) have made demand on the company or threats of legal action, for repayment of their unpaid sums, which cannot be paid.
2. Where the business has lost a major customer/contract or suffered a bad debt for a significant sum;
3. Where the business has failed to meet the required sales levels or has experienced increased costs that has either educed the profit margins or resulted in a loss; or
4. Where the Company's lenders have refused further credit or withdrawn facilities;

If the Company's business or assets have value, either to a third party or to the directors/shareholders these assets can be sold. Most sales are completed to the same directors or shareholders as typically there is an appetite from them to save the good parts of the business and to try and trade on through another company going forward therefore the sums they pay result in the best deal for creditors than a forced sale. If this sounds like you then advice can be given on the do's and don'ts when completing connected sales but the takeaway from this is that a CVL most certainly allows directors with a viable route and a fresh start whilst also securing the best outcome for creditors.

How does the Creditors Voluntary Liquidation process work?

Once it is established that a CVL is appropriate, the directors instruct a licensed insolvency practitioner who acts as the proposed liquidator and he/she then gives notice to the Company's creditors that the Company is to be placed into Liquidation.

The proposed liquidator will then ensure that the Company is placed into liquidation by undertaking the deemed consent process (where automatic agreement is received if not opposed) or the virtual meetings process (remote meetings virtually by videophone or telephone).

From the date of instruction, the Company will typically give 2 weeks' notice of the decision date/virtual meeting date, and all creditors receive a full pack of information on the Company's financial circumstances and liquidation proposals.

Should the liquidation decisions be approved by the creditors, and the necessary shareholder consents have also been received then the Company is considered in liquidation on either the decision date (if deemed consent) or following the virtual meeting.

The Liquidator will then take steps to deal with any outstanding matters, including realisation of the Company's assets and resolution of the company's tax affairs. There is also a statutory requirement for the Liquidator to conduct an investigation into the Company's affairs and the conduct of the directors.

If realisations are enough to enable a dividend to be paid to creditors, the Liquidator will advertise his intention to declare a dividend and give creditors a final opportunity to prove their claims. Once creditor claims are quantified and admitted, the Liquidator will pay the dividend and, if appropriate, take steps to conclude the liquidation.

When the Liquidation is being brought to a close, the IP provides creditors with a draft final account which summarises their dealings throughout the case, having brought the liquidation estate account to NIL. Then once an 8 week prescribed period has passed (for creditors to raise any objections), a final version of the draft final account can then be filed at Companies House, where the Company is then dissolved from the register 3 months from the date the final account was filed.

What are the advantages of a Creditors Voluntary Liquidation?

The advantages of a CVL include: -

1. The process is straightforward and inexpensive.
2. The directors instruct an insolvency practitioner to deal with the Company's affairs, rather than a government appointed Liquidator being appointed following a winding up petition from one of the creditors.
3. The good parts of the business can be bought back from the Company without inheriting the liabilities.
4. The public perception of a creditors voluntary liquidation is better as the directors are considered to have taken proactive steps to deal with the Company's financial situation, which can ensure the directors fair better when the investigations are done on their conduct given that Compulsory Liquidators have greater powers than Voluntary Liquidators when it comes to investigative matters.
5. The Liquidator can commence, or continue with, legal proceedings, on behalf of the Company, which often results in further realisations for creditors (e.g. against non-paying debtors or legal claims)
6. Although all liquidations must be advertised in the relevant Gazette, there is no longer a requirement to advertise in the local press
7. The directors are seen to comply with their fiduciary duties under the Companies Act 2006

Are there any disadvantages to a Creditors Voluntary Liquidation?

1. A CVL process is often considered to be a closure process, which can bring an end to contracts, as opposed to Administration which fully allows for complete control over the transfer of these. However, in practice most stakeholders such as employees and customers etc. allow for transfers of contracts within an CVL, just as much as in Administration, if handled correctly.
2. Other processes, such as Administrations, are a court driven process which once paperwork is filed at court, offer full protection from creditor legal actions due to the moratorium this puts in place. Whereas a CVL doesn't offer a moratorium. In practice however, the commencement of a CVL brings an end to 99% of any threats of legal action and most creditors will not commence or continue with any legal actions. However, on some rare occasions some creditors still issue a winding up petition which if done, would require their payment and permission to dismiss the petition, to continue with the CVL unless the IP is confident in attending at the petition court hearing to seek that the court judge dismisses the petition due to the CVL being commenced earlier.
3. The CVL process can sometimes require a break in trading rather than a seamless transfer from one Company to another and therefore IP's cannot fully guarantee that all stakeholders will agree to a seamless transfer.
4. Directors should note that although there is no prohibition on company officers forming a new company from the remains of a liquidated entity, there are nevertheless restrictions on the re-use of company names where the new name is either the same or so similar as to imply association with the old company. The rule is in place to help ensure that the interests of creditors and investors are not prejudiced by a lack of transparency relating to a director's involvement with an insolvent company. Directors wishing to trade again under a similar name must advertise notice of their intention to do so in the relevant Gazette prior to carrying on business.

What are the alternatives to a Creditors Voluntary Liquidation?

There are a number of options available to the directors of insolvent companies, and a brief description of these are shown below:-

- Company Voluntary Arrangement (CVA): A set arrangement with creditors whereby a company, under the supervision of an insolvency practitioner, reaches a binding agreement with creditors to repay all or a proportion of its debts over a period of time, usually five years, whilst the business is turned around. It is appropriate where the core business is viable and the company is in a position to continue trading and meet its ongoing obligations as well as to make additional contributions to the CVA.

- Administration: A powerful rescue procedure, which is appropriate where a company requires protection from creditor enforcement action whilst the business is restructured, sold or turned around under the control of an insolvency practitioner. The company may continue to trade under the control of the Administrator until the

business can be sold as a going concern, preserving jobs and minimising claims against the company by redundant employees.

- Prepack Administration: As above but where negotiations for the sale of the business are conducted prior to the date of the Administrator's appointment, and the sale is effected by the Administrator immediately after his appointment. The procedure is mainly appropriate where the risk of enforcement action against the company would severely impact the outcome for creditors as a whole, and where there is a risk of significant damage to the goodwill of the business due to adverse publicity.

- Compulsory Liquidation: A process by which the company is wound up by the court and dissolved, generally on the petition of a creditor.

However, a Creditors Voluntary Liquidation is by far, the most common insolvency process actioned by directors due to its low cost and speed leaving a CVL as the no.1 choice for 99% of our clients.

Should I liquidate my company?

If you believe a CVL is appropriate for your Company, or if you are unsure and need further help, please call Bridge Newland Limited for detailed advice, tailored to your situation. A licensed insolvency practitioner will then advise you on all aspects of voluntary liquidation, including practical tips on how to manage your creditors in the period leading up to the Liquidator's appointment.

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BRIEF SUMMARY

Creditors Voluntary Liquidation ("CVL") is a process used to close down an insolvent company, and is the most common form of liquidation in England and Wales.

For directors who have become aware that their company is no longer in a position to continue trading and cannot repay all of its creditors, the CVL process allows them to voluntarily take positive steps to deal with the situation and move forward both cheaply.

If you believe a Creditors Voluntary Liquidation is appropriate for your company, and would like to obtain advice from a licensed Insolvency Practitioner in this regard, please do not hesitate to contact Bridge Newland on (free phone) 0800 612 6197. All initial advice is free of charge, and rates for CVLs start from as little as £4,000 plus VAT, inclusive of all disbursements.