moorfields

A guide to the Administration Process

Appointment by an Unsecured Creditor

What is administration?

Administration is a court process whereby one or more qualified insolvency practitioners are appointed to manage the affairs of a company (or partnership). The benefit of this process is that it provides protection from the company's creditors whilst a restructuring plan or controlled disposal strategy is implemented.

The Administration process has been utilised by distressed companies since its introduction in 1986 and this legislation underwent an overhaul in 2003. The purpose of the 2003 legislation was to encourage the use of business rescue mechanisms in order to preserve viable businesses.

The Administration process is governed by a number of Statutory Instruments. These are:

- The Insolvency Act 1986 ("IA86")
- Insolvency Rules 2016
- The Enterprise Act 2002
- EC Regulation on Insolvency Proceedings 2000
- The Small Business, Enterprise and Employment Act 2015

Prior to seeking an appointment of an Administrator creditors should seek professional advice on the most appropriate recovery mechanism. In certain circumstances enforcing a debt through other means may prove to be a more effective and cost effective strategy than appointing Administrators.

What is the purpose of administration?

The Administrators appointed have a duty to act in the best interests of the creditors of the company. Legislation sets out the purpose of the Administration and since the introduction of the Enterprise Act 2002 (effective 15 September 2003) this has been split into 3 objectives. These are as follows:

Rescuing the Company as a going concern

The Administrators must perform their role to achieve this objective unless they consider that it is not practicable to rescue the company as a going concern or that the second objective (see next objective) would achieve a better result for creditors.

This objective would typically be achievable in situations where there are third party funds available to return the company to solvency, usually from an investor in the company or through the proposal and acceptance of a Company Voluntary Arrangement ("CVA").

Achieving a better result for creditors as a whole than would be likely if the company were wound up

If the first objective is not achievable then the second objective is to achieve a better outcome than a winding up of the company. This is often facilitated by the protection of the moratorium provided by an Administration Order allowing a sale of the business and assets as a going concern or through an orderly wind-down.

Realising property in order to make a distribution to one or more secured or preferential creditors

Should the previous 2 objectives not be achievable then the Administrators' objectives would be to realise the assets of the business and distribute them, in accordance with the priorities defined by the IA86.

If none of the 3 above objectives are achievable then Administration would not be the appropriate process. If Administrators are already appointed and it was established that one of the objectives could not be achieved, the Administrators would seek an end of the Administration.

Who can appoint administrators?

A number of parties are capable of appointing Administrators. These are:

- Qualifying Floating chargeholders
- The Company
- The Directors
- Justices chief executive for a Magistrates court
- One or more creditors of the company
- The supervisor of a CVA
- A liquidator
- A qualifying floating charge holder where the company is in compulsory winding up

The process for the appointment of Administrators differs depending upon the applicant. Outlined in section 6 below is the process for the appointment of Administrators by as unsecured creditor.

When can administrators be appointed?

The court may make an Administration Order in relation to a company provided it is satisfied that:

- The company is, or is likely to become, unable to pays its debts (as defined by Section 123 of the IA86 (see below); and
- The Administration Order is reasonably likely to achieve the purpose of Administration.

A company is deemed unable to pay its debts if;

- A creditor who is owed an amount over £750 has served a statutory demand on the company that the company has not paid (or agreed with the creditor a proposal for repayment) the amount within 3 weeks; or
- In England and Wales, execution or other process issued on a judgement or order of the court in favour of a creditor is returned unsatisfied; or
- In Scotland, the induciae of a charge for payment on an extract decree, extract registered bond, or extract registered protest, have expired without payment being made; or
- In Northern Ireland a certificate of unenforceability has been granted in respect of a judgement against the company; or
- It is proved to the satisfaction of the court that the company is unable to pay its debts as they fall due; or
- It is proved to the satisfaction of the court that the value of the company's assets is less than its liabilities (including contingent and prospective liabilities).

Who can be appointed administrators?

Only persons who are licensed Insolvency Practitioners can act as Administrators. The Administrators must be independent of the company and ensure that there are no actual or perceived conflicts of interest.

The Process for obtaining an administration order - By an unsecured creditor

Documents filed in court

Similar to other court processes, it is necessary to file relevant documents and evidence in support of the application in court prior to the hearing so that any interested parties can make appropriate representations. The following documents are filed and endorsed by the court with a date and location for the hearing:

1. Administration application in a statutory form
2. Statement of proposed Administrators in a statutory form; and
3. Witness statement in support – this document contains a statement that it is the applicant's belief that the company is or is likely to become unable to pay its debts. It must also contain information relating to the financial position of the company including:

- A statement of the company's assets and liabilities (to the best of the applicant's knowledge and belief);
- Details of security held by creditors of the company and whether these chargeholders have the power to appoint Administrators or Administrative Receivers;
- Details of any insolvency proceedings in relation to the company including winding up petitions;
- If it is intended to appoint a number of Administrators details regarding the exercise of their powers; and
- Any other matters that the applicant considers may be relevant to the application.

Copies of the endorsed documents are then served on a number of parties including any secured creditors who have the power to appoint Administrators or Administrative Receivers, any person petitioning for a winding up, the proposed Administrators, the company, any person who has distrained or levied execution and any insolvency practitioner currently in office. A certificate of service must be completed and filed in court to prove that these parties have received the documents.

Interim Moratorium

Upon filing the above documents an interim moratorium takes effect, protecting the company from action from its creditors (excluding certain secured creditors – see section below), without the express leave of court. This remains in place until the court hearing.

Secured creditors

Should there be any creditors of the company that are secured by a floating charge then it is likely that they will have the power to appoint Administrators and/or Administrative Receivers. These are known as Qualifying Floating Chargeholders ("QFCH").

Should such a creditor wish to make an appointment, they may do so prior to the court hearing and without an actual court hearing (known as an 'out of court' appointment. In this event the court hearing would not proceed.

Court hearing

A number of parties may attend the hearing but it is usual for the applicant and the company, to be represented by barristers experienced in dealing with such applications.

At this hearing the court may make an Administration Order, adjourn the hearing, dismiss the application or may make any such order as it considers appropriate.

Upon the granting of the Administration Order Administrators are appointed.

Following appointment

Moratorium

Upon the granting of an Administration Order no legal process or proceedings may continue against the company unless permission is obtained from court or the consent from the Administrators is obtained.

This moratorium protects the company against action from creditors who may wish to wind the company up or repossess

repossess goods (such as leased assets, stock subject to retention of title or landlords wishing to issue distress).

Management of the business

Following the appointment the Administrators or their staff will normally attend the company's sites to take control of the business. The Administrators, by statute, act as at all times as agents of the company and contract without personal liability.

The employees would be addressed and the impact of the Administration explained. Typically the existing management lines would be retained but any commitments would need to be authorised by the Administrators' staff.

Reporting lines and processes for ordering goods, etc. would be set up should it be considered beneficial to continue the business during the Administration and funding is available.

Trading

The Administrators often utilise the first few days to establish whether it is feasible and beneficial to cause the company to continue to trade although in certain circumstances it may have been possible for the proposed Administrators to undertake this review and planning prior to the appointment.

The decision to continue to trade is dependent upon a number of factors;

- The benefit to creditors of doing so;
- The working capital requirements and the funding (if any) available;
- Health and safety, insurance, and environmental or industry specific legislation;
- Support from employees, customers and suppliers; and
- The detriment to creditors of not continuing to trade.

The decision as to whether to continue the business is a balancing act and if it the decision is taken to do so it may be for a limited period. It is also possible that a number of cost cutting measures may be necessary such as employee redundancies.

Strategy

There are a number of strategies that the Administrators would consider in order to achieve the objectives of the Administration. The primary options are listed below:

Company Voluntary Arrangement ("CVA")

Should it be considered that creditors may accept a proposal for a voluntary arrangement and that the Administrators consider that it would be in the creditors' interest to do so then it is likely that in the early stages the Administrators will review the possibility in more detail. This would involve speaking to key creditors to determine whether they would support a proposal and drafting the detailed documentation.

Sale of the business

The Administrators may undertake a period of marketing of the business as a going concern. The business is typically continued during this period under the control of the administrators but this is subject to funding constraints and the benefit to creditors of doing so.

Customers, competitors, management and other interested parties would be approached and adverts may be placed in relevant publications. Some of these parties may attend the site in order to undertake due diligence work. The Administrators will normally set a deadline for offers. The timing of this is dependent upon the trading position in the Administration and the effect of a delay on the goodwill of the business.

Any such sale would typically involve a purchase of the goodwill, business and assets of the company and the purchaser would not acquire the majority of creditors (some TUPER liabilities and certain others may transfer).

Controlled wind down

This strategy may be implemented should a sale of the business as a going concern be unachievable or it may be the objective of the Administration in order to realise assets for the benefit of the secured or preferential creditors.

This would involve the Administrators instructing agents to dispose of the company's assets in the most appropriate manner and these would be sold off to one or more parties.

Statutory matters

There are a number of matters that, under Insolvency legislation, the Administrators must undertake following their appointment.

Notification to creditors

It is a legal requirement under the Insolvency Act that notice be given in the London Gazette. The costs of placing this advertisement are met as an expense of the Administration.

Notice needs to be dispatched to the members and creditors of the company within 28 days of the granting of the Administration Order.

Statement of affairs

The directors are required to provide the Administrators with a Statement of Affairs within 11 days of receipt of the notice requiring it. In practice, such notice is usually issued with one week of the Administration Order being granted.

The Statement of Affairs summarises the company's assets, their anticipated realisable value and the company's liabilities. It also contains a list of creditors and shareholders of the company. This, or a summary, is usually circulated to creditors at the initial meeting (see administrators' proposal below).

Report on directors' conduct

The Administrators are required to submit a report on the conduct of the directors of the company to the Department for Business Innovation and Skills ("BIS"). This report covers both the period leading up to and following the insolvency and is based upon the Administrators findings during the course of the Administration process.

In order to assist the Administrators in this task creditors are requested to provide details in writing of any matters they consider

should be taken into account.

The report is confidential between the Administrators and BIS and is used BIS to determine whether any action is required under the Company Directors Disqualification Act 1986 or if there are any civil or criminal matters to consider.

Administrators' proposals

Within eight weeks of their appointment, the Administrators must set out and circulate proposals for achieving the purpose of Administration, which must include an explanation, where applicable, of why objectives cannot be achieved and the proposed basis for their remuneration.

Committee

The creditors must be asked with every notification whether they wish to appoint a Creditors' Committee.

The committee must have at least three and not more than five members. Any creditor of the Company is eligible to be a member of the committee, so long as his or her claim has not been rejected for the purposes of being entitled to vote. The function of the committee is to generally assist the Administrators in discharging his duties. The committee often acts as a sounding board for ideas, and in addition it will monitor the further progress towards a conclusion of the Administration.

Costs and remuneration

The creditors decide the basis for the remuneration of the Administrators and this can be on either a time cost basis, as a percentage of realisations, as a set amount or a combination of these bases.

The costs and remuneration incurred by the Administrators in the performance of their duties is payable out of the assets realised. Similarly the costs incurred in obtaining an Administration Order are payable out of the assets of the company.

The Administrators would normally circulate a creditors' guide to Administrators fees prior to seeking approval of their remuneration.

Distributions to creditors

Administrators have the power to distribute funds to creditors. Typically, should there be funds to pay a distribution to unsecured creditors, the Administrators would seek to do this through placing the company into Liquidation (see 11.3 below). The Insolvency Act 1986 defines the priority of payments.

Ending administration

There are a number of routes to ending an Administration. If the appointment was 'in court' as for an appointment application by an unsecured creditor it is usually necessary for there to be a final court hearing.

The primary routes for both in and out of court appointments are:

Automatic end

The Administration automatically ceases after one year, or sooner if the purpose of Administration has been achieved, or cannot be achieved or a creditors meeting so requires. The creditors of the company or court may agree to an extension of this period (although the former of these parties can only extend the period for a maximum of twelve months).

Dissolution

The Administrators may file papers to say that the Administration has come to an end and that dissolution of the company is most appropriate. The company will be dissolved 3 months following the filing of the documents.

This exit route is used should there be no funds available for a distribution to unsecured creditors and there are no outstanding matters that a liquidator may need to consider.

Creditors Voluntary Liquidation ("CVL")

Where the Administrators think that they have paid or set aside sufficient to pay all secured creditors in full and there will be a surplus distributable to unsecured creditors, they file a notice to that effect. On registration of this notice, the Administration will end and the company will automatically go into CVL (some of the normal statutory provisions being disapplied and thereby avoiding the need to pass shareholders resolutions at a general meeting of shareholders). Whilst the creditors may nominate a different liquidator, in practice the Administrators usually become the liquidators thereby ensuring continuity and reducing costs.

Compulsory Liquidation

In certain circumstances the Administrator may apply to court for the company to be placed into Compulsory Liquidation. The Administrators may seek appointment as Liquidators or the Official Receiver or other insolvency practitioner may undertake this task.

This is typically used as an exit route where there are no funds to distribute but there are matters for a liquidator to consider.

About Moorfields

At Moorfields, we understand that any business – no matter what its size – can experience a reversal in fortune. We also know that when things are taking a turn for the worse, innovative thinking is as important to your survival as capital. And that's exactly what we offer.

We're business owners ourselves, so we know all about the pressures of trying to keep your stakeholders happy. We've also got years of experience in the world of finance, so we know a thing or two about keeping companies afloat.

But our innovative thinking isn't just about expert business advice. It's about breaking the mould of insolvency and rescue practitioners: helping you through your problems, treating you like a human being, and actually understanding exactly what you're facing.

We'll never surprise you with last-minute charges, because our fees are totally transparent (and actually quite affordable). We'll also never try to force you into a one-size-fits-all solution. Because we get it: your business is unique.

Finally, we'll never back out when the going gets really tough. We do what we say we'll do. And whatever happens with your business, we'll be here to help you every step of the way.

If you would like to discuss how Moorfields can assist you with an Administration or any other issues please contact

Simon Thomas:
T: 020 7186 1144
E: sthomas@moorfieldscr.com