

# Understanding the detail of company liquidations

## Frequently asked questions from directors of ailing companies

Many clients whose business revenues have been decimated by COVID-19 restrictions are appraising their options for when they can emerge to a new normal and get back to being fully open. However, in the interim, a number of companies may become insolvent, and as a result more and more directors are asking about options for liquidation and perhaps re-establishing a new business that is leaner and more resilient.

In this factsheet, Crowe's insolvency team answer some of the frequently asked questions from directors of ailing companies.

### How do I decide when it is no longer reasonable to continue to trade?

The first question to consider is whether your company is insolvent or not. An insolvent company is one where its debts outweigh its assets, or where the company cannot pay its debts when due. There are two simple tests to assess whether a company is insolvent – the balance sheet test and the cash flow test.

Of these two insolvency tests, the cash flow test is probably the most important, as you can have a strong asset position but if you cannot pay your bills on time you may find the company is forced into liquidation.

#### 1. The balance sheet test

If the value of your assets is lower than your liabilities, you are insolvent. This test aims to determine whether the company's cash at bank combined with the total value of assets gives a value that is more or less than the total quantum of its liabilities.

#### 2. The cash flow test

If the company cannot pay its bills as they fall due, you are facing insolvency. This test should map the amount of working capital you have available at any given time, comparing forecasted sales with payments due.

However, there are many circumstances in which a company may not pass one or both of the above tests but it is still reasonable for the directors to continue to trade. For example, certain companies may have a

seasonal business where the company may temporarily fall into insolvency during the quiet period and subsequently regain solvency once trade improves. This fact has been recognised by the courts, and in the case of *Re Hefferon Kearns Ltd* the judge remarked that:

“it would not be in the interests of the community that whenever there might appear to be any significant danger that a company was going to become insolvent, the directors should immediately cease trading and close down the business. Many businesses which might well have survived by continuing to trade coupled with remedial measures could be lost to the community.”

Therefore, the decision to cease trading and liquidate should be made when the company is insolvent and the directors are satisfied that there is no reasonable chance of the company being able to trade out of its insolvent position. Company directors should seek appropriate professional advice at this point as there may be alternatives available to winding up the company, such as informal restructuring, examinership, a scheme of arrangement, etc.

### Can I be a director of another company after a liquidation?

In most liquidations, no sanctions are placed on the directors of the company, and as a result there is no impact on their continuing to act in companies where they are already a director or on becoming a director of another company.

To avoid any sanctions, directors must demonstrate to the satisfaction of the liquidator that they have acted in an honest and responsible manner during their stewardship of the company. Recent guidance allows liquidators to discount the impact where a company traded at a loss during the COVID-19 challenges due to the unforeseeable and unknown extent of the pandemic on businesses.

Over the three-year period from 2017 to 2019, only around 13% of all insolvent liquidation cases resulted in a restriction or disqualification.

## What sanctions might I face if my company goes into liquidation?

There is a small proportion of cases where directors have acted dishonestly in their stewardship of a company prior to the liquidation. In these circumstances, there are different levels of sanctions that may be imposed upon the directors, depending on the severity of their misconduct. These sanctions are:

### ■ Restriction order

This sanction is placed on directors who are found to have acted irresponsibly or dishonestly in their actions as a company director. While an individual who is subject to a restriction order can still act as a company director, the company must have a minimum share capital of €100,000 to act as a capital base to protect creditors of the entity should losses arise.

### ■ Disqualification order

When a disqualification order is placed upon a company director, they are barred from acting as a company director for the duration of the disqualification order. The disqualification order is generally for five years.

## Can company assets be used to pay the costs of the liquidation?

The assets of a liquidated company, other than those secured by a fixed charge, are in the first instance used to pay for the costs of the liquidation. These costs include:

- The costs and expenses incurred in connection with the calling of a creditors' meeting
- The costs and expenses incurred in the preparation of a statement of the company's affairs
- Any necessary disbursements by the liquidator
- The costs payable to the solicitor for the liquidator
- The remuneration of the liquidator
- Any out-of-pocket expenses necessarily incurred by a committee of inspection

In short, priority is given to the liquidation costs, so if a company has fixed assets or stock that can be sold or debts that can be collected, the liquidator can use these assets to pay the costs of the liquidation and there is no legal requirement for the directors to cover these costs from their own resources or put cash into the company at the start of the liquidation.

## How can liquidation costs be kept to a minimum?

The costs of a liquidation can be greatly reduced by the directors co-operating and assisting the liquidator. This may involve the directors bringing the assets of the company to one location and helping to identify any potential buyers for those assets, or assisting in the collection of debts either by way of dealing with customer queries or ensuring all supporting documentation for

outstanding invoices is made available. The quicker the liquidator can realise value from any assets, the lower the administrative costs associated with that aspect of the liquidation will be.

Providing accurate books and records, having tax filings up to date and replying to the liquidator's queries in a timely manner can cut what is normally up to an 18-month appointment in half, thus saving time and costs.

## Who will pay for redundancy costs in a liquidation?

In circumstances where an employer is unable to pay statutory redundancies to their employees because of an insolvent liquidation, the Department of Employment Affairs and Social Protection have established a Redundancy Payment Scheme that can cover the cost of the statutory redundancy due to the employee. The rate of statutory redundancy is two weeks' pay for every year of service (over the age of 16) plus one additional week's pay. Payment is subject to a limit of €600 per week.

As a result of the scheme, the state will guarantee that all qualifying employees will be paid their statutory entitlements regardless of the asset position of the company, and the liquidator will administer this process.

## Are directors allowed to buy the assets of their company if it is being liquidated?

A liquidator is permitted to sell the assets of a company being liquidated to a former director. Prior to selling the assets to the director, the liquidator must give 14 days' notice to the creditors of the company of his intention to sell the assets to the director, pursuant to section 629 of the Companies Act 2014.

## Can creditors pursue me personally for the debts of the company?

When a limited company is liquidated, under company law the limited liability status of the company generally protects the directors from any liability to company creditors. The main exceptions that can arise are:

### 1. Personal guarantees

The directors should review the potential recourse from suppliers, landlords and funders if personal guarantees have been given. Crowe has seen instances where personal guarantees for overdrafts have not materialised, as the bank have instead exercised their right to set off other bank balances against the overdraft. Also, amounts due to suppliers who have retention of title clauses and hold personal guarantees are often dealt with by way of return of their goods, which reduces their claim. Landlords, if assisted with the return of the property in a lettable condition, can be sympathetic as regards personal guarantees and are often open to negotiation on the level of claim if engaged with early in the process.

## 2. Unpaid PAYE on directors' remuneration

The protection of limited liability that a company offers does not extend to directors in cases where there is an element of unpaid PAYE attributable to their own remuneration. In these cases, the director may be personally liable for the element of PAYE the company has failed to pay.

## 3. Personal liability for the debts of the company

In extenuating circumstances where directors have acted recklessly and this is proven to the satisfaction of the High Court, they may be made personally liable for some or all of the debts of the company.

## What is required of a director once a liquidator is appointed?

When a liquidator has been appointed to a company, its directors are under a duty to co-operate with the liquidator. The liquidator takes full responsibility for selling the assets, collecting debts and dealing with creditor and employee claims. In fact, there is a limited time requirement from directors once the liquidator has been appointed. Very often once a liquidator is appointed it can be a relief for directors, as the pressure from creditors seeking payment is focused on the liquidator and not the director.

## How long does the liquidation take?

The length of time taken to complete a liquidation is very much dependent on the individual circumstances arising in each case. Some liquidations can continue for a number of years. However, in a straightforward liquidation where the directors have acted honestly and responsibly and the assets of the company can be easily disposed of, it could be assumed that a liquidation can be completed within 12 months.

## Supporting directors through the process

Each company's circumstances will be different. Many directors of companies facing insolvency will seek to trade out of the current difficulties, while others will see liquidation of the insolvent company as the appropriate strategy. These are significant and difficult decisions for directors to make, and Crowe can provide the advice and support they need so they can appraise their options and identify what is best in their circumstances.

We offer a free initial consultation to company directors who wish to avail of an independent perspective and attain clarity as to their options and available strategies.

With 80 years' experience and expertise, we are the trusted partner providing a range of specialist services for many professional services firms. We would be delighted to meet with any client referrals you might have who could benefit from this service line.

## Special offer

*The Companies Act 2014: Annotated and Consolidated* is the successor to the *Combined Companies Acts* and its publication marks 30 years of Crowe overseeing this essential annotated reference to the legislation. The first edition was published by Crowe in 1989 under the firm's former name, Bastow Charleton.



We would be delighted to offer a complimentary copy of the latest edition on the referral of any assignment and work with you on projects going forward.

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We work with a variety of clients across commercial and public sectors. Our services include Audit & Assurance, Tax, Corporate Insolvency & Recovery, Corporate Finance, Consultancy, and Outsourcing.

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At Crowe we pride ourselves on delivering hard-working, practical solutions to all our clients' business challenges. We help clients make smarter decisions today that create lasting value for tomorrow.

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