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Guide to the Creditors' Voluntary Liquidation Process

Moorfields
Corporate Restructuring & Insolvency

What is a Creditors Voluntary Liquidation ("CVL") ?

Creditors' Voluntary Liquidation ("CVL") is a legal process defined in the Insolvency Act 1986 ("IA86") and associated legislation.

It is a process instigated by the shareholders of the Company (and hence 'voluntary') when the Company has insufficient assets to meet its liabilities or it is unable to pay its debts when they fall due. In a CVL, one or more liquidators are appointed to 'wind up' the affairs of a Company in an appropriate manner. Once completed, the Company will cease to exist.

It should be distinguished from a Members' Voluntary Liquidation ("MVL"); where the Company has sufficient assets to meet its liabilities and from a Compulsory Liquidation where the Court appoints a liquidator to wind up the Company, usually at the request of one of the Company's creditors.

The alternative procedures to a CVL include; informal arrangements with the creditors, Company Voluntary Arrangements ("CVAs") where creditors are asked to approve a legally binding proposal for repayment, Administration or Compulsory Liquidation. Professional advice should be sought as to which process is most appropriate.

Appointment process

Directors' Meeting

A meeting of the Company's directors is held. At this meeting, they consider the financial position of the Company and resolve to convene a meeting.

This meeting would also resolve which of the directors were to sign the Statement of Affairs (see below) and which director would act as chairman of the meeting of members.

Notice of meetings

Members

A meeting of the members (shareholders) of the Company would be called in order to resolve to wind up the Company and appoint a liquidator.

14 days' notice of this meeting must be provided to the members although the members can agree to waive this notice period.

Secured Creditors

Creditors who may be entitled to appoint Administrative Receivers or Administrators should be informed of the proposed liquidation. The latter of these must receive a minimum of 5 days' notice.

The secured creditor would then have the option to appoint an Administrator or Receiver prior to the shareholders meeting. The former of these would prevent the appointment of a liquidator. A liquidator could still be appointed if a receiver is appointed but advice should be sought as to whether this is necessary or appropriate.

Period leading up to the shareholder meeting

Directors remain responsible for the Company up until the appointment of a liquidator. They must, at all times, act in the interests of the Company' creditors to ensure that their position does not deteriorate. Failure to take all steps to minimise losses to the creditors could result in the directors becoming personally liable for the Company debts.

Directors should seek advice from qualified Insolvency Practitioners as to what action should be taken during this period.

Statement of Affairs’

Prior to the meeting the directors must prepare a Statement of Affairs. This lists all of the assets, liabilities, creditors and members of the Company and details of security granted.

The purpose of this document is to illustrate the insolvency of the Company and provide information to the creditors on the likely return to creditors.

A director must sign a statement of truth to confirm the contents of the Statement of Affairs.

Report

In advance of the meeting directors would be responsible for the preparation of a report detailing the statutory information of the Company, its history, reasons for its financial difficulties and details of the financial position. The directors often seek the assistance of a professional in the preparation of this report but it would remain the directors’ ultimate responsibility.

Seeking Creditors views on appointment of Liquidators

Once the history, stationary information and statement of affaires have been completed they must be sent to the creditors of the company for them to take part in the decision-making process for the appointment of the liquidators.

The documents can be sent by post or by email if that process of communication was previously the normal method between the creditors and company.

The creditors can initially be asked to decide only by either:

- A deemed consent process
- A virtual meeting

At the same time as asking them about the appointment of Liquidator Creditor must be invited to nominate themselves to sit in as a liquidator committee of Creditors. If there are sufficient nominators (a minimum of 3 and no more than 5) a liquidator committee will be formed to assist the liquidators and to determine the basis of the remuneration To be paid to the liquidator.

The minimum notice period for the creditors are as follows:

- For determine whether a liquidator committee should be formed- 5 days from date of delivery
- For appointment of liquidators- 3 business days from date of delivery

Delivery is deemed to have occurred 2 days after 1st Class posting or next morning if sent by email.

Once Creditors have received documents they can then object to the appointment of the Liquidators and can request a physical meeting of Creditors.

If the objections total more than 10% in value of unsecured Creditors, then deemed consent or virtual meeting procedure is stopped and a physical meeting of Creditors must be covered on days’ notice.

If objections are received it causes problems regarding the timing of the shareholders meeting which passes the resolution placing the company into Liquidation. The resolution should be passed no more than 14 days before the conclusion of the Creditors decision making, process or physical Creditors meeting.

As discussed below before the Creditors have decided upon the appointment of a Liquidator the powers of the member nominated liquidators are limited. It is therefore usual to hold the shareholders meeting as close as possible to the date that the appointment of the Liquidator.

Meeting of members

The director nominated to chair the meeting, reports to the shareholders on the financial position of the Company and presents the Statement of Affairs.

At the meeting of members, resolutions are passed for the Company to be wound up and the Company is placed into liquidation. A liquidator is appointed but has limited powers pending the ratification of the creditors. This member nominated liquidator has the power to:

- Take control of the Company’s property
- Dispose of goods of wasting nature
- Do all necessary to protect the Company’s assets

Following appointment

Effect of appointment

Once a liquidator is appointed they take responsibility for the Company and its assets.

If the Company has continued to trade in the lead up to the liquidation, the liquidator would consider whether the trade should be continued for a period of time and would, as necessary, close the business down.

The powers of the directors of the Company would be suspended and the provisions relating to ‘phoenix companies’ would take effect. These provisions restrict the re-use of the Company’s name (or names similar to it) and impose severe consequences on those who breach this.

Notification

Notices are sent to the Registrar of Companies informing it of the appointment and the details advertised in the London Gazette.

Creditors would also be circulated with the outcome of the decision making process.

Powers of the liquidator

The Liquidator has certain statutory powers to obtain and take control of the Company’s records from parties holding such documents. The directors and employees (including former) of the Company also have a statutory obligation to assist the liquidator in their inquiries.

Realisation of assets

The liquidator would make an inventory of the assets of the Company and arrange for them to be realised. The funds from such a process would be held by the liquidator and distributed in accordance with the priority defined by the IA86.

Ongoing statutory matters

The liquidator has a duty to send a progress report to creditors following the anniversary of the appointment. There is also a statutory obligation to send with that progress report an account of the receipts and payments made by the liquidator.

The liquidator also has other statutory duties including a duty to prepare a confidential report to the Insolvency Service on the conduct of the directors (both current and former) in the lead up to, and subsequent to the liquidation.

Distributions

Funds realised from the disposal of assets are utilised to discharge the costs of the liquidation process and, if sufficient, are used to pay off elements of the Company's indebtedness. The priority of the relative debts is complex in light of recent court cases but can be summarised as follows:

Fixed charge creditors

Where the liquidator disposes of assets subject to fixed charges, the process (less costs) are available to the fixed chargeholder (providing the security documentation is valid)

Preferential creditors

The primary preferential claims relate to employee entitlements to unpaid wages and accrued holiday pay and certain pension liabilities. From December 2020 HMRC now rank as a secondary preferential creditor in relation to certain outstanding taxes held by a business on HMRC's behalf, such as; VAT, PAYE, employee NICs, student loan repayments and Construction Industry Scheme (CIS) deductions.

Assets that are not subject to a fixed charge are available to the preferential creditors in priority to the floating charge-holder (and after certain costs).

Prescribed Part

The funds available (if any) after paying the preferential creditors are subject to what is known as the Prescribed Part. These funds are defined as net property. The purpose of this fund is to ring fence a percentage of a Company's assets, after costs, for the benefit of the unsecured creditors in cases where the Company gave a floating charge over its assets to a chargeholder.

This fund is only applicable to chargeholders who have charges dated after 15 September 2003. Those with charges prior to this date do not suffer from the allocation of the funds to the Prescribed Part.

The prescribed part is calculated based upon the net property available to the floating charge- holder as follows:

- 50% of the first £10,000 of net property; plus
- 20% of the remainder;
- Subject to a cap of £600,000.

From 6 April 2020, the cap has been increased to £800,000 ("the New Cap").

The cap can only remain at £600,000 if the lender has a 'relevant floating charge', which is a charge:

- created prior to 6 April 2020; and
- in respect of which no floating charge over any of the company's assets created on or after 6 April 2020 ranks equally or in priority to.

This means:

- if the company has no floating charges created on or after 6 April 2020, the New Cap will not apply and the prescribed part cap will remain at £600,000; or
- if the company only has charges created on or after 6 April 2020, the New Cap will apply and the prescribed part will increase to £800,000; or
- where the company has floating charges created both before and after 6 April 2020, the situation is a little more nuanced and will depend on the ranking of the later charge.

It may be necessary to dispense with the Prescribed Part should it be considered cost ineffective to distribute the funds and the Court agrees. Otherwise the amount set aside is to the unsecured creditors.

Floating charge creditors

Any funds available after the payment of preferential creditor and after deducting the Prescribed Part (if applicable) are available for floating charge creditors.

Unsecured Creditors

The unsecured creditors would participate in any funds from the Prescribed Part and any funds remaining after the payment of the floating chargeholders. The level of dividend varies from case to case.

Case closure

Once the liquidator has realised all of the assets and fulfilled their statutory obligations then they may seek an end to the liquidation. This would result in the Company being dissolved and taken off the Registrar of Companies.

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.

If you would like to discuss how Moorfields can assist you with a CVL or any other issues please contact:

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