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A guide to the Administration Process

Appointment by the holder of a Qualifying Floating Charge ("QFCH")

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 advantage 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 new legislation was to encourage the use of business rescue mechanisms in order to preserve viable businesses.

As a result of the 2003 legislation the Administration procedure has been made more accessible and streamlined, allowing a floating charge holder, the Company or its directors, to appoint Administrators, in certain circumstances, without a court hearing.

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
- Small Business, Enterprise and Employment Act 2015

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 the process of obtaining an administration order is the process for the appointment of Administrators by a Qualifying Floating Chargeholder ("QFCH").

Creditors who are holders of fixed rather than floating charges are creditors of the Company and as such can utilise the 'in court' procedure should they wish to do so.

What is a Qualifying Floating Charge?

A QFC is defined as an instrument which:

- States that paragraph 14 of Schedule B1 of the IA86 applies (Power to appoint an Administrator); or
- Purports to empower the holder of the floating charge to appoint administrators of the Company; or
- Purports to empower the holder of the floating charge to make an appointment which would be the appointment of an Administrative Receiver and on its own or together with other charges, the floating charge relates to the whole or substantially the whole of the Company's property and the charge is enforceable.

Those creditors who hold floating charges dated prior to 15 September 2003 may be in a position to appoint an Administrative Receiver as an alternative to an Administrator. There are respective advantages and disadvantages of the two differing processes and if in doubt professional advice should be sought as to which process is most appropriate for the circumstances.

When can administrators be appointed?

Under most circumstances Administrators can be appointed by a QFCH using the out of court procedure. There is no requirement for the Company to be insolvent but, as above, the charge must be enforceable. There must therefore have been some triggering event under the terms of the security such as the receipt of a notice of intention to appoint an Administrator by the Director/ Company, failure to repay a demand, etc.

However, if any of the following apply then appointment of Administrators may not be possible or an application to court would be required:

- If a Provisional Liquidator is in office; or
- If the Company is in liquidation; or
- If an Administrative Receiver is already in office.

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 QFCH

Type of application

In the majority of circumstances a QFHC can utilise the streamlined out of court procedure. A full court application and hearing is required if a winding up order has already been made but the mere presentation of such a petition does not prevent an out of order court application.

As the 'in-court' process is relatively rare, this document only deals with the 'out of court' procedure. The summary of the process for an in-court application can be provided upon request.

Enforceability of charge

The charge must be enforceable for an Administration Order to be obtained. This is typically achieved through the issue of a demand for the repayment of the outstanding balance. Provided time is given to the Company to repay the amount concerned and that the payment is not received this normally enables the charge to be enforced. It may be necessary for legal advice to be obtained for non-standard floating charges to ensure that the document is enforceable.

Notice of intention to appoint

A Notice of Intention to appoint is completed where the Company has prior ranking Qualifying Floating Chargeholders. These include both QFCHs who hold floating charges dated prior to that of the creditor seeking the appointment and where there is a priority agreement in place providing priority to another QFCH.

At least two business days notice must be given to the prior raking chargeholders. The prior chargeholders may consent to the appointment, remain silent or seek the appointment of their own Administrator or Administrative Receiver (if their charge pre dates 15 September 2003).

Should the Company require the protection of the moratorium during this interim period the notice of intention to appoint an Administrator is filed at court.

Interim moratorium

In the period between completion of the Notice of Intention to appoint an Administrator and the appointment, an Interim Moratorium may be obtained through the filing of the Notice of Intention to Appoint in Court.

Upon the filing of this document the Company is protected from action from its creditors (excluding prior ranking QFCHs), without the express leave of court. The Moratorium exists for a maximum of 5 days.

Appointment of administrator

Following receipt of the consent, or in the absence of an objection from the prior ranking chargeholder (and at the expiry of the two clear days notice period), the Administration Order may be made.

Where no prior raking chargeholders exist the notice of intention to appoint and the interim Moratorium can be dispensed with and a notice of appointment together with statements from the proposed Administrators filed in court.

It is possible where timing is critical, for an appointment to be made out of hours through the filing o an appointment document in court by fax.

Upon filing the relevant form the Administration becomes effective.

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

The moratorium also protects the Company against other secured creditors and prevents the appointment of Administrative Receivers and fixed charge receivers. The latter of these can be appointed with the consent of the Administrators or leave of court.

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.

The funding for the trading may come from a number of sources:

- Proceeds from disposal of floating charge assets;
- Customers, e.g. paying on a proforma basis
- Suppliers e.g. through credit terms; and
- Banks or secured creditors e.g. through repayable or non-repayable loans, provision of overdraft or invoice discounting facilities.

The existing lenders would normally be contacted at an early stage of the process to explain the benefits of continued trading and to determine whether they would be prepared to fund it.

Employees

As indicated in the trading section it is often necessary to make the difficult decision to make a number of employees redundant in order to reduce costs. The cost reduction exercise is often necessary to ensure the business' survival through the Administration process.

Employees who are made redundant will normally qualify for a payment of redundancy, arrears of wages, holiday pay and pay in lieu of notice from the government's National Insurance Fund. The Administrators will issue the affected employees with the forms to make such a claim. These payments are subject to weekly wage cap with any balance ranking alongside other creditors of the Company.

Insurance of the assets

Upon appointment the Administrators will consider the insurance position and either seek to maintain the existing policy or obtain a new policy. Insolvency Practitioners have access to open cover policies for most types of industry ensuring that, should a new policy be required, cover can be obtained immediately to protect the assets of the Company.

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 the constraints in trading the business.

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 employee 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. 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 document is filed at Companies House and is provided to the creditors of the Company at the initial meeting (see creditors' meeting below).

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 Meeting

The creditors must be asked with each 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 a time cost basis, as a percentage of realisations, as a set amount or a combination of theses 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 costs of the Administration also include certain unavoidable costs such as taxation on chargeable gains, legal and agents costs etc. These, together with the remuneration of the Administrators, form an expense of th Administration and are taken off prior to the distribution to creditors.

Distribution to creditors

Administrators have the power to make certain distributions to creditors and the IA86 defines the priority of payments.

Fixed Charge Creditors

Where the Administrators dispose of assets subject to fixed charges, the proceeds (less costs) are available to the fixed chargeholders. Provided the security documentation is valid, these funds can be paid over to the secured creditors without approval of creditors or court.

Preferential creditors

Since the introduction of the Enterprise Act 2002, the Inland Revenue and Customs and Excise (now known as HM Revenue & Customs) no longer have preferential status. Therefore the primary preferential creditors relate to employee and certain pension liabilities.

Assets that are not subject to fixed charges are made available to the preferential creditors in priority to the floating chargeholders (and after costs).

Prescribed Part

The funds available (if any) after paying the preferential creditors are subject to what is known as the Prescribed Part. The purpose of this fund is to make the amounts lost to preferential creditors as a result of the abolition of Crown Preference available to the unsecured creditors (thus by-passing the floating chargeholders).

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

The Prescribed Part is an amount set aside for the unsecured creditors and is calculated based upon the amounts available for the floating chargeholders as follows:

- First £10,000 – 50%
- Next £2,975,000 – 20%

This results in a maximum Prescribed Part of £600,000. It may be possible to dispense with the Prescribed Part should the Administrators consider it to be cost ineffective to distribute the funds, otherwise the amount set aside is payable to the unsecured creditors.

Floating charge creditors

Any funds available after the payment of the preferential creditors and after deducting the Prescribed Part (if applicable) are available for the floating charge creditors. Under the IA86, the Administrators are empowered to make a distribution to floating charge creditors without reference to the creditors or court.

Unsecured Creditors

Typically, should there be funds to pay a distribution to unsecured creditors other than by way of a Prescribed Part, the Administrators would seek to do this by placing the Company into liquidation (see 11.3 below).

Ending administration

There are a number of routes to ending an Administration. The routes are as follows:

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 such as antecedent transactions.

The Administrators obtain their release from liability from unsecured creditors, the court or in certain circumstances from the secured creditors.

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

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