R3 – the trade body for Insolvency Professionals

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Compulsory liquidation: Q&A

What is liquidation?

Companies are liquidated when there is no prospect of rescue. In the Carillion case, the company has been placed into compulsory liquidation by the court. This can be on the petition of the company's creditors or directors. In a compulsory liquidation, the Official Receiver is automatically appointed liquidator and in this case is being supported by a team of insolvency practitioners at PwC (acting as special managers).

What does a liquidator do?

Once appointed, the liquidator works quickly to get as accurate a picture as possible about the company's affairs and financial position: its bank accounts, its operations, its assets. The liquidator will have to secure the company's assets and make decisions about what happens to the company's staff, pensions, and contracts etc.

Depending on the case, staff may be kept on and services may continue to be provided. In some cases, this will not happen and the liquidator will consult staff on redundancy and find a way to transfer the provision of services to another provider.

The company's pension fund may be transferred to the Pension Protection Fund with the approval of the Pensions Regulator.

It is the role of the liquidator to raise money to repay the company's creditors. This can be done by selling the company's business and assets. The business could be sold as a whole or individual assets could be sold off. Assets can include property, equipment, the company's brand, its ongoing contracts (if these can be sold or transferred) and any other asset (tangible or intangible) of value.

The liquidator must ensure that a fair distribution of the company's assets takes place among creditor groups. The overriding aspect as far as the liquidator is concerned is acting in the best interests of creditors to maximise their returns.

The liquidator will also pursue money owed to the insolvent company so that they can return this to creditors, too. This can include litigation.

The liquidator also has an important role to play in investigating the conduct of the company's directors prior to the insolvency. They will make a report to the Insolvency Service who may later begin disqualification proceedings against the directors.

Fees

In an insolvency procedure handled by an insolvency practitioner, fees are approved by the creditors. In a case handled by the Official Receiver, fees are charged at a statutory rate.

What are the different classes of creditor?

In an insolvency, usually there is not enough money left to repay everyone. Because of this, the government has created an 'order of priority' that determines the order in which creditors are paid.

This order prioritises major lenders with security, often banks. These types of lenders are further up the order of priority so that they feel confident continuing to lend to businesses.
In order, the classes of creditor in an insolvency are:

1. **Secured/fixed charge creditors -** usually banks whose lending is tied to a specific property or asset.

2. **The costs of the insolvency** - such as legal fees or rent on a commercial property, or any professional fees incurred.

3. **Preferential creditors** - usually the company's employees who are owed unpaid wages, holiday pay, and/or pension contributions.

4. **Floating charge creditors** – those whose lending is tied to a general type of asset, for example goods in a company's warehouse.

5. **Unsecured creditors** - such as trade suppliers, employees owed redundancy pay, customers with gift cards, and HMRC. Usually these are the largest group by number, if not by size of the debts owed.

6. **Shareholders and bond holders**.

Those lower down the priority list are less likely to see their money back.

If there is a floating charge holder, the liquidator may hold back a proportion of the funds owed to this group to ensure unsecured creditors do receive some money back. This is called the 'prescribed part' and is capped at £600,000.

ENDS

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Notes to editors:

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