

Corporate insolvency

This article offers a brief survey of causes of insolvency, some of the practical problems that arise in administering the affairs of insolvent companies and of the ways in which these may be tackled by a liquidator or receiver, or otherwise.⁽¹⁾ It is intended to inform the interested but non-specialist reader and does not address in any substantive way the issues that are currently being considered in the Insolvency Law Review Committee. In the preparation of the article, advice was sought from a number of banks, firms of chartered accountants and others who have had close experience of insolvency cases. Their help has been greatly appreciated and was the basis for the material that is incorporated in parts of the article. A brief appraisal concludes the article.

A company is usually considered to be insolvent if it cannot pay its debts as they fall due. If the insolvent company has granted a lender a floating security over its assets, that company will normally be placed in receivership, which need not result in the cessation of the business of the company, because the receiver may be able to continue to manage the business as a going concern with a view to finding a purchaser. Indeed, it is usually to the benefit of all creditors to ensure that, if possible, at least part of the business of an insolvent company is sold as a going concern to try to preserve the goodwill, the value of the plant, machinery and stocks, and employment. The alternative is liquidation—the formal winding up of a company with a view to its dissolution—or, occasionally, a financial reconstruction.

Causes of insolvency

Although the immediate cause of insolvency is almost invariably a lack of cash resources rather than of profitability, this financial situation is in most cases reached only after a phase of erosion in the underlying business, often the result of poor management. In cases encountered during the Bank's enquiries, the more common underlying causes of insolvency in recent years have been, in no particular order of importance:

- Low and declining real profitability, often masked in the last few years by historic cost accounts which may show a steady, but in reality inadequate, return on capital—a particular problem in capital-intensive industries.
- Large commitments or acquisitions, and diversification into unfamiliar products and markets, possibly to replace a decline in an existing product range. Equally, however, inadequate anticipation of a decline in a traditional market or over-commitment to the introduction of new product ranges can cause insolvency.
- Increased import penetration in home markets. Loss of competitiveness may be due to a number of factors, such as lower labour costs in the exporting country, appreciation of sterling, poor and declining

productivity, and the reputation of the company for quality and delivery.

- Deterioration in the financial structure of the business, manifested in increasing dependence on borrowing, especially short-term debt. Businesses may fail to foresee a period of heavy cash outflow and so fail to take remedial action, such as cutting expenditure, especially excessive or extravagant overheads, and obtaining appropriate and secure types of finance.
- Underestimation of problems in starting up in new locations and of maintaining control of operations at a distance.
- Excessive scale of operations in relation to the capital base of the company, commonly characterised as over-trading.
- Inadequate financial control over contracts, especially fixed-price long-term contracts. This can lead to large losses through underestimation of costs, which will threaten solvency if the capital base of the company is inadequate.
- Inadequate control over working capital, resulting in an excessive scale of stocks and debtors in relation to turnover, and to unbalanced inventories which cannot be reduced quickly when required to generate cash.
- Failure to identify and eliminate loss-making activities or to foresee future losses. A company may retain an inadequately profitable division, possibly to avoid redundancy pay, until its financial position has so deteriorated that not only can the cash drain no longer be sustained but it cannot afford the costs of reorganisation and closure.
- Adverse changes in terms of contracts entered into, such as large increases in rent.

Symptoms of weaknesses such as these can often be observed before the financial affairs of a company deteriorate to a critical state. Recent developments in techniques of discriminant analysis—that is, systematic examination of a number of key ratios drawn from the annual accounts of a company—provide an analyst with a

(1) The practices described in this article are based on the position under English law.

useful screening device to help identify possible problems ahead for a company. Where such disquieting features in a company are identified by investors or bankers sufficiently early, there will be the possibility and time for an independent review, perhaps followed by remedial action and continued monitoring of the company. But in other cases matters deteriorate to a point at which the loss of confidence by investors or bankers in the company board or management is such that receivership or liquidation appears the only satisfactory (or least unsatisfactory) means of effective action.

Among the features of such a financial crisis may be one or more of the following:

- Large and unexpected losses and provisions; in part, these may represent losses unrecorded in previous years because of inadequate accounting controls, especially relating to stocks or contracts in progress.
- Delays in the preparation of accounts and in the submission of figures by the company to its bankers, sometimes accompanied by more frequent enquiries as to the standing of the customer or by a request from the auditor for confirmation of continued bank support.
- An unforeseen requirement for cash, manifesting itself in a rapid exhaustion of, or inability to stay within, bank credit lines, and repeated requests for increases in facilities.
- Breaches of conditions in debenture and loan stock trust deeds or borrowing agreements, commonly concerning maximum debt/equity ratios, interest cover, and maintenance of working capital cover.
- Requests from directors for a release of personal guarantees.

The extent of cash outflow is frequently not fully reflected in movements in overdraft balances with any individual bank. This can arise if a company uses, over a quite protracted period, short-term credit lines supplied by alternative lenders, or delays settlement of trade debts despite demands or threats of legal action for payment, or makes use of off-balance sheet finance or the accelerated collection or factoring of outstanding trade debts. A bank may not know about all of these, particularly the extent of facilities granted to their customer by other banks.

The immediate reason for action as drastic as receivership is normally either an immediate shortage of cash as a result of losses, or pressure from creditors, or the need to defer a scheduled repayment of existing borrowings beyond a point which a prudent lender could normally contemplate, having regard to the solvency of the company and the value of the available security. If the directors consider the company to be insolvent, they will sometimes request the appointment of a receiver in order to avoid the risk of personal liability. Before a company reaches this stage, one or more of its bankers may have been expressing disquiet to the board and management for some time and may have been losing confidence in the ability of those in charge to put matters right. The banks consulted by the Bank emphasised

that they regard receivership or liquidation as a last resort, and that they have in recent years sought to identify and deal with potentially difficult cases well before they come to crisis point. The appointment in a potential rescue case of a firm of chartered accountants to carry out an investigation is often used, especially for larger companies; occasionally the in-house specialist services of a bank are appropriate for smaller companies.

There has been a substantial increase in the rate of insolvencies this year, though the figures have to be treated with caution because this in part reflects the growth in the formation of new small businesses, whose mortality rate is higher than that of established companies. In the first half of the 1970s, liquidations (as recorded by the Department of Industry) averaged 3,200 a year; over 1975-79 the average rose to 5,400; and there were 5,600 liquidations in the first ten months of this year alone. These figures may overstate the number of businesses becoming insolvent, because a business may be operated through a number of separate companies, each of which would be recorded as an individual liquidation. In the quinquennium 1970-74, the London clearing banks on average appointed receivers in some 150 cases a year; the average rose slightly in the period 1975-79, but there has been a sharp increase recently, with approximately 400 receivers appointed by the London clearing banks in the first ten months of this year, against a total of about 250 over the whole of 1979.

In deciding whether to appoint a receiver or—where there is no charge giving the power to appoint one—to take action which might result in winding up, a bank will assess the following major factors:

- The underlying soundness of a business, if the financial structure can be rectified.
- The strength of the management and the reliability of the financial data.
- The solvency of the company and the prospect of improving its financial structure, often by sale of part or all of the business.
- The security of the debt to the bank, and the margin available to cover additional lending to enable the company to ride out its difficulties, provided that the underlying business is viable. In particular, the bank will have to consider the risk of erosion of security if the company continues to trade.
- The value of the assets, which, if insufficient to pay the preferential creditors and the costs of receivership, may not make it worthwhile to appoint a receiver.
- The social background, for a bank may be especially reluctant to appoint a receiver where there are a large number of jobs at risk in an area of high unemployment or where there have been a number of other insolvencies in the sector and where a further receivership could seriously damage confidence. However, protracted delay can be harmful if it erodes the business, and may be prejudicial to the interests of trade creditors.

Alternatives to insolvency

An alternative to liquidation or receivership may be a reconstruction of the debts of a company, for example by rescheduling or conversion into share capital. But, while more or less formal arrangements are frequently established between companies in difficulty and certain of their creditors (notably banks), schemes of reconstruction under the Companies Act 1948 are rare, in particular because of the difficulty of establishing the necessary agreement of a majority of creditors and of the delay in preparing and obtaining agreement to the scheme (which requires Court sanction to be binding on all members and creditors).

Other methods short of receivership or liquidation are frequently employed. These include:

- An extension of banking facilities for a limited period, subject to tight conditions and supervision on behalf of major lenders, while the company disposes of assets, raises further longer-term capital, or takes other appropriate action to reduce gearing or eliminate loss-making activities.
- Supervision, often by a firm of independent accountants with experience in reorganisation and insolvency work, which reports directly to the principal creditors.

Types of insolvency procedure

The business of a company which has become insolvent does not necessarily cease, but there are often differences between the approach of a receiver and a liquidator to continuing the business. It is usually to the advantage of creditors to seek a purchaser for the underlying business, or part of it, as a going concern, and in the meantime to continue operations in order to preserve the goodwill and the value of the plant, machinery and stocks; this may be beneficial even if there is no prospect of selling the business. A receiver will usually try initially to keep the business of a company going, whereas it is rare for a liquidator to do so.

Receivership

A receiver may be appointed with or without the power to manage the business, his appointment being made by a debenture holder—often a bank—either at the request of the directors or as a result of default on a covenant or borrowing condition. A receiver may be appointed under either a fixed or floating charge, or both,⁽¹⁾ although an appointment under a fixed charge, relating only to the assets which are the subject of the charge, confers no right of management. Such an appointment is, however, rare. The discussion that follows relates principally to a receiver appointed under a floating charge, who would usually have the power to manage the business.

The primary duty of the receiver is to realise the assets in order to repay the liabilities which are the subject of the charge or which rank in preference to that charge. The

receiver is an agent of the company, effectively taking over the executive powers of the directors, as well as having other powers, such as the ability not to continue contracts. Once his liabilities are satisfied, the duties of the receiver cease.

The extent to which a floating charge can enable a debenture holder to obtain priority and control over the realisation of the assets of an insolvent company is often the subject of criticism. However, receivership is a long-established feature of the commercial system in the United Kingdom and has been widely seen as a significant help in enabling a grip to be taken on the business of companies in trouble, with a view to maintaining the business. Without receivership, a decline might have gone further, worsening the position of the creditors generally and the prospect of saving some or all of the business; indeed, the ability to take a floating charge, giving the debenture holder the right to appoint a receiver in certain circumstances, is almost unique to the United Kingdom, and those consulted by the Bank considered it to be a constructive and effective device for dealing with corporate insolvency. There is, however, some concern that an increase in preferential creditors, a greater use by suppliers of reservation of title clauses, and a greater prevalence of fixed charges, including the fixed charge over book debts (under which a receiver can have no general power of management), have tended to reduce the scope for the receiver and hence the prospects of continuing insolvent businesses.

Liquidation

A company may be placed in compulsory liquidation by the Court, or in voluntary liquidation with the agreement of a meeting of creditors, who have the right to appoint the liquidator in both cases. Occasionally a solvent company may be placed in voluntary liquidation by its members. A liquidator has a general responsibility to the creditors and may continue the business of the company. The liquidator is subject to the direction of the creditors as represented by the Committee of Inspection (or to that of the Court where relevant) in respect of certain proposed courses of action.

Differences between receivership and liquidation

Although a receiver and a liquidator have to observe a similar order of priority when repaying indebtedness, there are practical differences in their operations:

- The appointment of a receiver and manager, when available, provides the most straightforward method for a debenture holder to ensure that proper control is taken of the business and assets of a company with a view to obtaining repayment. The debenture holder executes a simple document and creates an immediate and effective moratorium on the demands of the creditors for payment.
- The debenture holder who appoints a receiver has the power to replace him, and may be kept more in touch with developments than an unsecured

(1) A fixed charge exists where a lender enjoys the security of a claim on specific assets: a floating charge provides security relating to that general category of assets of the company specified in the mortgage deed, which may change with the company's business.

creditor, who is not in such a position because a liquidator is primarily responsible to the general body of creditors, whom the liquidator is required to call together annually.

- Receivership is reversible in the sense that, once sums due to the preferential creditor and the debenture holder have been paid, powers of control and management can revert to a liquidator (if one has been appointed) or, occasionally, to the directors, if liquidation can be avoided. Once a company has been placed in liquidation, it is exceptional for the liquidator to be withdrawn.
- It is generally thought that a liquidator may carry on a business only where he believes that this will result in higher realisations than if the assets are sold immediately. As the liquidator may be personally liable for any losses incurred if he continues to trade, it is rare for him to do so beyond completing the work in progress or with a view to a very quick sale.
- Companies going directly into liquidation, which are often relatively small, are normally at a more advanced stage of decline than companies to which a receiver is appointed. This is frequently as a result of the delays which can occur, and the reluctance of creditors to incur the associated costs if a liquidator is to be appointed.

Some practical aspects

Appointment of a receiver and liquidator

Receivers and liquidators are normally practising accountants, and generally have some specialist knowledge of the industry of the insolvent company. A single debenture, and receiver, may be used where there are several debenture holders, with the priorities of repayment settled by separate agreement between them. Where several lenders have floating charges with different priorities, and have the power to appoint separate receivers, they have in recent experience normally agreed to make a joint appointment.

Relative position of creditors

Upon the appointment of a receiver, the right of unsecured creditors to obtain repayment of their debts ceases. Obligations are paid from the proceeds of asset realisations by the receiver or liquidator in the following order:

- Creditors having a fixed charge over a particular asset, to the extent of the proceeds of sale of that asset after payment of the realisation expenses of the receiver or liquidator. This includes the fixed charge over book debts, which has become more common in recent years.
- Costs of receivership in relation to a floating charge, and costs of liquidation where a receiver has not been appointed.
- Preferential creditors including, subject to various limitations, claims for local rates, income and

corporation taxes, VAT, wages and salaries, social security contributions and superannuation contributions.⁽¹⁾ The wages preference is for a maximum of four months wages with an overall limit of £800 per employee.

- Liabilities for tax arising from the activities of the receiver.
- Debenture holders, to the extent that their claims are covered by a floating charge over the company.
- Costs of the liquidator, where the company has first been placed in receivership.
- Unsecured creditors.
- Shareholders.

In addition to the claims which have a right of preference expressed in the Companies Act 1948 as amended, certain other creditors may be able to obtain a measure of repayment, including hire purchase companies (with a right to repossession) and utilities such as electricity, gas and water (if supplies are to continue as before).

The position of a receiver

A receiver is agent of the company and normally makes this clear in any contracts adopted and, for example, in any orders that are given, in order to avoid the personal liability which the Companies Act otherwise imposes on him. The appointment of a liquidator during the course of a receivership precludes the receiver from continuing to act as agent of the company; if the receiver wishes to continue the business thereafter, contracts with suppliers, customers and employees must be in his own name and he will be unable to exclude personal liability.

Immediately upon appointment, having previously informed the directors, he takes control of all the assets of the company, and stops the movement of goods in or out of the business, unless with his permission. He also informs the employees, the unions and all third parties connected with the company of his appointment.

Having taken effective possession, the receiver will assess the extent to which it is commercially sensible to continue part or all of the business with a view to its sale as a going concern. Often, particularly with larger companies, the receiver may have already been employed as investigating accountant at the initiative of the bank holding the debenture.

In order to preserve options, a receiver will usually try to continue the business while an assessment of its viability is made, and the debenture holder making the appointment will normally be prepared to advance money for this purpose, if required. On appointment, a receiver occasionally has to arrange for funds to pay the wages for the first week and for essential supplies. Thereafter, he will usually obtain sufficient payment from debtors for pre-receivership sales (unless these debts have been

(1) A bank may make advances specifically to meet wage and salary expenses; the amounts so advanced are subject to the preference accorded to wages and are often debited to a special wages account to protect the interest of the bank. Such advances may keep a company operating while solutions to its difficulties are sought. The opening of the wages account by a bank may also serve to bring home to the directors and management the gravity of the position.

factored), or from other realisations, to meet any subsequent outgoings. The accountants consulted by the Bank indicated that, where it was considered that the business should be continued, they rarely had any problem in arranging appropriate finance, especially as funds advanced for this purpose enjoy first priority of repayment.

Continuation of the business

After the initial assessment, the receiver may decide to continue the whole or a part of the business:

- Because the business as a going concern is likely to realise more than if the assets are sold piecemeal.
- Because the completion of work in progress, or of existing contracts, is likely to increase the realisable value of the stocks.

If a receiver decides to continue the business as a going concern, he will usually try to contact those interested in buying it, including those overseas, preparing for them a documentary summary of the main features and assets of the business. It is clearly of benefit to trade on at a profit (which the receiver may consider it best to do for some time while looking for a buyer), but a receiver may also trade at a modest loss if he has reason to believe that he can sell the business as a going concern, with the prospect of making good the trading loss by the additional value obtained. This is a difficult decision; the debenture holder will invariably be consulted about it, and also about other important matters concerning the strategy of the receivership.

Most of the accountants with whom the Bank had discussions in the context of this article thought that a receiver would normally be able to form a view whether a business should continue to be run as a going concern by the end of the first week; and that by the end of the first month he would have completed most of the work in progress and utilised such raw materials as could be converted into finished goods without making substantial additional purchases. In order to justify continuing the business further, a receiver would—unless he is trading at a profit—expect to have some evidence of prospective buyers; it would be unusual to run a business under receivership for much more than a year.

If a liquidator wishes to continue to trade, he faces much greater difficulty than a receiver, because the business will usually have been seriously run down, the assets substantially dissipated or eroded, and key employees may have left. Moreover, because he does not have the backing of a debenture holder, he may find it difficult to raise finance to continue the business.

Hive-down companies

All the accountants consulted by the Bank considered that it could be useful to transfer the assets of a company in receivership to a separate 'hive-down' company—which is a 100% subsidiary. Usually stock, plant and machinery are transferred, together with the trade of the insolvent company. Employees tend to be retained in the original company to avoid the hive-down company becoming liable

for redundancy pay. The accountants felt that hive-down companies were not usually appropriate to small receiverships.

The proponents of hive-down companies considered the major advantages to include the ability to continue to trade with limited liability, thereby avoiding the danger of personal liability for a large claim which could not be met out of the assets of the receivership or from the receiver's professional indemnity insurance; the preservation of trading losses or the isolation of capital losses for tax purposes; and the simplicity of selling a company rather than a selection of assets. Some of the disadvantages were seen as doubts by suppliers and customers as to the creditworthiness of the new company; the cost and complexity of setting up and running a hive-down company; and the need to liquidate the hive-down company if its business is not sold.

Other problems in the early stages

Among the concerns that commonly confront a receiver in the preliminary stages of his work are:

- Financial information; the decision whether to continue to trade requires accurate details of the financial position, product costs, and overheads, but a lack of such data has often been one of the causes of the company's downfall.
- The attitude of creditors and others who may be in a position to force repayment or otherwise hinder continued trading.
- Lack of cash, particularly where the company has already factored its debts or discounted its invoices, leaving few assets which the receiver can realise quickly to provide cash to fund the receivership; he may then have either to obtain finance or continue with the factoring or discounting arrangements in respect of post-receivership sales.
- An increasing number of companies now try to supply goods which they express to be subject to reservation of title; if the clause is valid, the goods belong to the suppliers until they have been paid for. Substantial stocks in the possession of the receiver or liquidator may thus not be the property of the company and must be bought if required for the purpose of continuing the business and completing orders. However, the debtor company must be seen to have agreed to reservation of title clauses on both orders and invoices. A receiver who sells or converts stocks subject to reservation of title must retain sufficient proceeds to pay the suppliers, as he can be sued for the tort of conversion.
- Maintenance of rights to occupy premises subject to a charge and to use plant subject to hire purchase or leasing arrangements. As to premises subject to a fixed charge, interest on the loan may have to be paid by the receiver as a cost of receivership, while leased plant may be bought at a negotiated price.
- Maintenance of confidence of customers and suppliers.

Relations between a receiver and a liquidator

When a receiver is appointed under a floating charge, a liquidator may also be appointed by the unsecured creditors, but he has no effective powers in respect of the assets until the receiver has finished dealing with them.

In the initial stages of a receivership, there is little to be gained from commencing winding up, but the appointment of a liquidator may be desirable at a later stage, especially if there is some chance that there will be assets available for the unsecured creditors. The receiver is accountable to a liquidator, and consultations about major decisions may minimise the chances of a subsequent challenge to the transactions of a receiver; moreover, the liquidator can proceed with the task of administration and agreeing the claims of unsecured creditors.

The appointment of a liquidator during a receivership may, however, make the task of the receiver more difficult in several respects. He is no longer able to contract as agent of the company or to 'hive-down', and has to choose between stopping work on contracts or taking on personal liability, unless he has previously arranged their transfer to a hive-down company. If the liquidator is appointed by the Court, employment contracts are terminated, giving rise to an unsecured liability for redundancy pay; if he then wishes to retain staff, the receiver will need to employ them personally. Long-term and other contracts which the receiver has previously continued may be terminated by the appointment of a liquidator. There are also tax problems as the appointment of a liquidator starts a new tax year. The receiver will normally try to persuade an unsecured creditor that it is against his interests to petition for winding up, because it may reduce the eventual dividend for unsecured creditors.

Directors and employees under insolvency

The executive powers of the directors cease upon the appointment of a liquidator, although they still have certain legal responsibilities such as the preparation of a statement of affairs. The contracts of employment of employees are automatically terminated where a liquidator is appointed by the Court. Receivership effectively suspends the powers of the directors to manage the company but, as with a voluntary winding up, does not itself terminate contracts of employment; and the receiver, if he is the agent of the company, may continue to pay wages and salaries under existing contracts without incurring personal liability for redundancy pay. Indeed, a receiver or liquidator (other than a liquidator appointed by the Court) who wishes to retain the services of employees generally arranges for them to be paid by the company under their existing contracts.

A receiver or liquidator will seek to maintain regular contact with employees and recognised trade unions. In the experience of the accountants consulted by the Bank there is generally a positive spirit of co-operation on the part of employees and unions, who are naturally concerned to assist in the continued running of at least part of the business so that some employment can be maintained.

Subject to certain limits, if an employee is dismissed and his employer is insolvent, he is entitled to claim from the Redundancy Fund in respect of arrears of pay, holiday pay, pay in lieu of notice, unpaid contributions to pension schemes, redundancy pay, and various other compensations; unpaid contributions may also be claimed by a pension scheme. The Redundancy Fund will then rank as a preferential or unsecured creditor according to the appropriate ranking of the claims it has paid on behalf of the company. In practice, the greater value of such claims are non-preferential and do not reduce the proceeds to the debenture holder. Unless a receiver or liquidator is confident of being able to provide continuity of employment to the work force, he will, as required by law, give notice of impending redundancy to the Department of Employment and consult the relevant trade unions.

The ability of a receiver to deal with overmanning or the closure of parts of a business by making redundancies which the company might itself have been unwilling or unable to tackle is a major factor in saving at least part of the operations of companies placed in receivership. Where redundancies are necessary, it is normal for the receiver to deal with these before a sale, the buyer of the business taking on only those employees he requires for the continuing operations.

Long-term contracts

An early and important task of a receiver is to examine outstanding contracts. Although the receiver cannot disclaim any onerous contracts he does not have to adopt them. He will normally take the course which appears to yield the more favourable cash flow, bearing in mind that claims for breach of contract will rank as unsecured creditors. But in some cases the receiver may have difficulty in persuading the customer to let him continue the contract as he is most unlikely to be able to offer any long-term warranty. Relevant considerations include:

- The expected net proceeds from completing the contract.
- How long it will take to complete, the accuracy of projecting the cost, and the risk of technical non-completion.
- The chances of renegotiating the contract on to more favourable terms, although this can be almost impossible for overseas contracts. If a contract is renegotiated, the customer will benefit from continuity of supply and avoid the expense of negotiating with others for its completion.
- The consequences of non-completion in terms of claims for damages, payments under bank guarantees (which may be covered by a charge), and the effect on the business and specialist personnel.

Realisations

In broad terms, the realisation of assets takes the form either of the sale of the majority of the business as a going concern, or of the piecemeal disposal of assets, or of some

combination of the two. An analysis of some of the recent larger receiverships under floating charges in which the London clearing banks have been involved suggests that these three methods occur with approximately equal frequency.

The consensus of those interviewed by the Bank was that, where part or all of a business is to be sold as a going concern, first responses tend to be from bargain hunters and seldom result in a firm offer; the actual sale is usually arranged by private treaty, although the tender method has been used occasionally where there are several prospective purchasers. Usually, as much of a company as possible is sold as a single package. Where buyers are allowed to select parts of a business, a receiver will generally be left with the less attractive portions and so may have to break them up and sell the assets for what they will fetch in a forced sale.

The specialists consulted by the Bank noted that the difficulties of finding a purchaser for a business as a going concern were inevitably greater in the present economic climate, which also made it harder to continue to run at least part of the business at a profit. These problems, coupled with the lower values being obtained for secondhand plant and machinery, the difficulty of selling industrial properties, and the growth in preferential claims, have resulted in a decline in realisations as a proportion of the book value of a company's assets to the point where debentures secured by a floating charge are, in general, less likely to be paid in full.

Possible purchasers of a business include the company's executive management. Such management 'buy outs' now seem to occur more frequently.

Length of receivership and liquidations

Those visited had experienced considerable variation in the length of receiverships and liquidations. Cases were mentioned where the sale of a business was agreed within a few days. At the other extreme, some protracted legal and other matters were still outstanding after more than fifteen years. In general, a substantial proportion of the work of a receiver or liquidator would normally be completed within the first twelve months, depending on the size and complexity of the company, but the resolution of all

outstanding matters might not be possible for up to five years, often because of legal actions. The timescale has recently tended to increase, particularly through the increased use of reservation of title clauses, which are usually challenged by a receiver, thereby involving him in substantial additional costs and delays.

If the receiver has managed to obtain substantial sums from realisations before the preferential claims and claims for retention of title are agreed, he often makes a payment on account to the holders of floating charges. This is usually on the understanding that the debenture holder will repay these sums to the receiver if the claims are much larger than expected. A bank appointing a receiver would normally expect any proceeds of the realisation to be placed on deposit with it.

Appraisal

With the deepening recession and rising financial deficits for many companies, the pace of receiverships has increased quite markedly in the past year. But, on the basis of experience both recently and over a longer period, a receiver is likely in the majority of cases to be able to preserve at least part of the business as a going concern. This will tend to yield higher realisations, improving both the position of the secured lender and, perhaps, unsecured creditors, as well as maintaining employment in at least part of the business.

Despite the increased frequency of potential and actual problem cases, the evidence suggests that banks and other creditors are ready to maintain their credit lines (and sometimes to increase them) where confidence in the board and management of a company remains; and they have been restrained in their readiness to use such security as they may have to appoint receivers. The experience that is being accumulated by the banks in coping with the present exceptional phase of financial pressure underlines the importance of continuous and well-informed contact between banks and their corporate customers. A major object of such contact is the anticipation of difficulties, most of which, if tackled in a timely way, can be put right well before unsustainable financial strains build up and doubts about solvency emerge.