

Compulsory Liquidation and Winding Up Petitions

by Lexlaw Solicitor Advocates

Professional Legal Solutions for Directors Facing a Winding-up Petition

If a winding-up petition is brought against your company, the consequences could be significant for your company and for you personally. Petitions can also be issued against partnerships. This guide will help directors or members to understand the consequences and what steps can be taken when facing a petition or the threat of one.

What happens when a Winding-up Petition is issued?

The presentation of a petition to the court will render any transfer of your company's property voidable unless validated by the court (per section 127 Insolvency Act 1986) and will almost certainly cause damage to your company's commercial reputation. If the petition is subsequently advertised in the London Gazette, your company's bank accounts could be frozen and the impact may therefore obviously be catastrophic to your business. Also, if the petition is advertised, other creditors may support the petition, and in some cases even take it over. This means that even if the petitioning creditor is paid, the winding-up hearing will still take place and the Court could make an order winding-up your company.

What to do if a Winding-up Petition is brought against your company

If presented with a petition you should employ one of the following solutions within 7 days (after 7 days the petitioner is allowed to advertise the petition):

Pay the creditor

This is the obvious way to prevent the petition from being advertised and halt the process of your company's liquidation. You may be required to pay the creditor's costs in bringing the petition.

Reach an agreement

Agree with your creditor(s) how you can pay your debt and request that they withdraw the petition. You may be required to pay the creditor's costs in bringing the petition.

Company Voluntary Arrangement (CVA)

A CVA is a legally binding agreement with the majority or all of your creditors allowing you to pay back the debt (or part of the debt) over a period of time. This is especially useful if your inability to pay is the result of a cashflow problem.

Administration

An insolvency practitioner is appointed administrator of your company. This will stay all legal action against your company, including a winding-up petition. The Administrator will be granted control of your company and he/she will work to pay creditors in the best way possible, for example by selling assets or by means of a CVA.

Dispute the existence or amount of debt

If you do not believe that you owe the debt or the amount of debt being demanded, you or your legal representatives need to write to the creditor giving reasons why the debt is disputed and requesting that they withdraw the petition. If the creditor is unwilling to withdraw, your company may be able to urgently obtain an injunction preventing advertisement of the petition.

Handling aggressive creditors and abusive tactics

Some creditors or debt collection agencies will threaten you with near immediate presentation or early advertisement of a winding-up petition in order to apply improper or undue pressure. Before a petition may be presented however, a 21 day Statutory Demand for payment must usually be delivered to you. Some debt collection agencies will demand costs from you, however they may not always be entitled to their costs – a specialist solicitor will be able to advise on this question.

Many debt collection agencies include words like 'law' or 'legal' in their company name, giving the impression that they are law firms when they are not. If in doubt, you should consult your own solicitor for advice.

If you are faced with a demanding creditor who is adopting questionable tactics, you should consider urgently obtaining an injunction restraining against the presentation of a petition.

How to avoid a petition being presented against your company

Communication is key. Negotiate with your creditor(s) and look to come to an agreement about how you can pay your debt. Often negotiations via legal representatives can avoid a stalemate in negotiations and help to broker time to pay agreements.

If your company is in dire financial trouble, and in order to avoid possible 'wrongful trading' you may wish to consider a Creditors' Voluntary Liquidation (a 'CVL') – this is where a company is voluntarily brought to an end by its directors and shareholders.

What happens if the Court orders a compulsory winding-up?

All of your company's employment contracts will be terminated by operation of law and the Court will appoint an official receiver to handle liquidation of your companies affairs. He/she will liquidate your company and use the proceeds to pay creditors.

What are your liabilities as a director of a wound-up company?

You may be held personally liable for some or all of the company's debts for example if there has been 'wrongful trading'. This takes place where at some point before the winding-up of your company began, you knew (or should have known) that there was no reasonable prospect of your company avoiding being wound up and you did not take all reasonable steps to limit the losses to the company's creditors. There is other misconduct which could result in your personal liability, examples of which include (but are not limited to):

- Using company money for non-business purposes;
- Making non-legitimate or illegal payments of dividends;
- Selling company assets below market value; and
- Falsifying accounts and misleading company creditors.

The penalties for wrongful trading can include fines, disqualification from being a company director for up to 15 years and potentially even imprisonment. Therefore, it is extremely important for directors concerned about potential wrongful trading to obtain specialist legal advice in order to minimise risk of personal liability.

Do I need specialist legal advice?

The insolvency regime and the winding-up rules and the procedure before the Companies Court are often complex and technical areas of law, therefore obtaining specialist professional advice is usually the most sensible course of action. Below are just some of the ways a specialist solicitor can assist:

A specialist legal adviser may be able to assist in restructuring and possibly writing off debt. Additionally, they will be able to assist by liaising and negotiating with creditors and advising on administration, CVAs and other voluntary arrangements.

Injunctions

A specialist adviser may be able to assist you by obtaining injunctive relief, restraining the creditor from a particular course of action, for example, restraining a creditor from presenting or advertising the petition.

Case study – Injunction

The directors of a care home business were served with a statutory demand for payment of a debt of over £50,000 debt relating to a contract for supply of goods. The directors instructed LEXLAW, who applied for an injunction to restrain the creditor from presenting a winding-up petition for the debt. We argued that the creditor had contracted to supply a specific quantity of goods and so was not entitled to recover anything until it had completed the entire contractual obligation. The Companies Court decided that there was evidence of a genuine and substantial dispute regarding the creditor's performance of the contract and therefore granted the injunction. The issues between the parties were then resolved on terms that were more favourable to our client. Validation Orders - This should go into a different box as it is a separate contribution

If the petition has been advertised then it may be that a Validation Order is needed. (Courtesy of Pitmans Law)

Once a bank finds out that its customer has a petition issued against it, accounts will be frozen. The reason for this is that any 'disposition of assets' (which includes use of cash at bank) by a company after the date a petition is issued is void. This means that suppliers and staff can't be paid and advisers (including a proposed CVA supervisor – see below) will not accept the payment of fees from the company. If they do the payment could be clawed back. This makes it difficult for directors to get the help they need. The company will therefore need to borrow money from other sources, usually its directors and these loans may be irrecoverable if the company cannot be saved.

The Court can order that the company may use its cash to make certain critical payments (e.g. to pay staff or pay for business critical supplies) if this will mean that the company will be in better (or at least no worse) shape, should it go into liquidation, than it would otherwise would be. This way the Court can ensure that the general body of creditors are not worse off as a result of certain other creditors receiving payment in priority. However, to obtain this 'validation order' from the Court the company needs to navigate the legal system, file evidence, put forward a compelling argument and deal with objections and is likely to need to engage the services of a lawyer. The company will need to find funds to pay these fees from elsewhere. This means that few companies can afford to make a court application.

Adjournments

In cases where HMRC (as a creditor) or other creditors are refusing to give your company more time to pay, with specialist help, your company may be able to obtain an adjournment – i.e. extra time to pay, enter into a voluntary arrangement, or otherwise resolve the problem.

Opposing the petition

Most companies will instruct a law firm to represent them at the hearing and to advise on the best way to deal with the petition and the claimed debt. Such work may include making a damages claim if for example a malicious petition has been issued or procedure adopted that is an abuse of the proper process of the Companies Court.

When a company ends up in compulsory liquidation, it is usually a sign that a creditor has given up trying to recover money from the company, or it indicates that a Crown or Government agency has wound up the company, using a winding up petition under the public interest.

Clearly, this is a very serious action for creditors to take (not least because of the cost) and if the company is subject to this process it can severely curtail the ability to conduct business.

It is possible to stop compulsory liquidation, but you have to act quickly if your company has been 'served a winding up petition'.

The costs of compulsory liquidation are not insubstantial and a creditor has to decide whether the debtor is likely to pay up. A debt of over £5000 (from 1st October 2015) must be undisputed and the creditor must have notified the debtor of its intent to collect the debt. This often involves issuing a statutory demand first. If the debtor fails to pay the statutory demand in 21 days and does not dispute the debt, then the creditor may issue a winding up petition.

The costs vary between solicitors but a typical cost of the action will be £250-£500 for a statutory demand, and £1,000-£2,000 for a winding up petition (includes Court costs). Despite this for larger debts it is a very effective way of collecting larger debts when the creditor believes that there is sufficient resource to pay it. Many larger companies use established debt collection law firms to collect their debts this way.

The application for a petition will be granted in cases where it can be proven to the Courts satisfaction that the debt is undisputed, attempts to recover have been undertaken and the debtor is not compliant. A petition will be issued and court hearing date granted. The date is usually well in the future because of court pressures. Once the petition is correctly served upon the company it has a period to pay the debt or to defend the action. This is expensive as the action is always in a High Court and requires a barrister to attend. The costs of such defence are high. If the case is found the company is wound up by the Court.

Note: even if the debt is paid (always with full costs) the fact that a petition is issued means that a winding up hearing (in the High Court) MUST be held. Between the date of the payment and hearing it is possible (and often happens) that another creditor learns of the petition and 'substitutes' their debt for the paid debt (thus 'piggy-backing' the action in order to get ahead of other creditors and get paid).

Case study – Malicious petition

Our corporate client carried on a vehicle supply and repair business and entered into a contract for the supply of vehicles. Our client considered that the vehicles supplied were of unsatisfactory quality; however the Petitioner presented a winding-up petition to apply undue pressure on the company. By way of witness statement evidence and exhibits prepared by us, the company was able to demonstrate to the Court that there was a substantial and bona fide dispute as to the quality of the vehicles and that the petition had been partially intended to dissuade our client from continuing legal action against an associate of the petitioner. The company was awarded significant costs against the petitioner in light of their conduct.

You can obtain specialist professional advice on any topic covered in this guide from LEXLAW Solicitors & Advocates. Call us on 02071830529 or email contact@lexlaw.co.uk. Visit our website: www.windinguppetitionsolicitors.co.uk for more information about our legal team and our successes.

Problems Caused by A Winding Up Petition

Once a company has been served a winding up petition there are some serious problems to consider. The best lesson we can give is this **DO NOT LET A CREDITOR TAKE THE ACTION IN THE FIRST PLACE.**

Once the petition has been issued and served it must be **HEARD**, this means the Court will have to consider the petition even if the debt is paid before the hearing. This means the company cannot

- Issue a notice of intention to appoint administrators
- Nominate a liquidator
- Pay suppliers as the bank account may well be frozen*
- Pay wages for the same reason*

*We can arrange for a validation order to allow the bank account to be used, but this can be an expensive process.

- Dispose of or sell assets
- Sell the business
- Secure new loans