

Administration – Scotland

a guide for unsecured creditors



Administration When a company is facing financial difficulties it can be placed into administration. This means that the affairs, business and property of the company will be managed by a person appointed for that purpose.

A licensed insolvency practitioner has given you this because you, or your business, may be owed money by a company that is in administration.

This guide aims to help you understand your rights as a creditor and to describe how best these rights can be exercised. It is intended to relate only to Scotland. It is not an exhaustive statement of the relevant law or a substitute for specific professional or legal advice.

We have made every effort to ensure the guide is accurate, but R3 cannot accept responsibility for the consequences of any action you take in reliance on its contents. If, having read the guide, you remain in any doubt about your rights, you should consult a licensed insolvency practitioner or solicitor.

Depending on the circumstances of the case, creditors who play an active role in an insolvency can make a significant difference to how much the insolvency practitioner will be able to recover for them. We hope that you will read this guide carefully and consider whether taking an active role as a creditor in this case could benefit you or your business.

In what circumstances does a company find itself in administration?

When a company is facing financial difficulties it can be placed into administration. This means that, during the period for which it is in administration, the affairs, business and property of the company will be managed by a person ('the administrator') appointed for that purpose. The administrator must be a licensed insolvency practitioner.

How can a company be placed into administration?

A company may be placed into administration:

- by an order of the court, on application by, amongst others, the company, its directors, one or more creditors, or, if it is in liquidation, its liquidator;
- without a court order, by the direct appointment of an administrator by the company, its directors or a creditor who holds comprehensive security of a type which qualifies him to make such an appointment.

What is the purpose of administration?

The administrator must perform his functions with the objective of:

- rescuing the company as a going concern, or
- achieving a better result for the company's creditors as a whole than would be likely if the company were wound up (without first being in administration), or
- realising property in order to make a distribution to one or more secured or preferential creditors.

The administrator must perform his functions with the first of these objectives unless he thinks either:

- that it is not reasonably practicable to achieve that objective, or
- that the second objective would achieve a better result for the company's creditors as a whole.

The administrator may perform his functions with the third objective only if:

- he thinks that it is not reasonably practicable to achieve either of the first two objectives, and
- he does not unnecessarily harm the interests of the creditors of the company as a whole.

What are the powers of an administrator?

An administrator's powers are very broad. They include powers to carry on the company's business and realise its assets. The administrator displaces the company's board of directors from its management function and has the power to remove or appoint directors.

The administrator must prepare proposals for approval by the creditors setting out how he intends to achieve the purpose of administration.

Does the administrator pay unsecured creditors the money owed to them?

Debts due to unsecured creditors are frozen at the date of the administrator's appointment.

If the outcome of the administration is survival of the company, the management of the business and assets can be returned to the directors on the conclusion of the administration. The directors and staff of the company will then deal with unsecured creditors' pre-appointment claims.

If survival of the company is not possible, but sufficient sums are realised from the sale of the company's business and assets to enable funds to be distributed to unsecured creditors, the administrator may be able to deal with their claims and pay them a dividend, but he may only do so with the permission of the court. Otherwise, after payment of the costs and expenses of the administration, any surplus funds will normally be passed to a liquidator, who will deal with creditors' claims. The administrator may himself become the liquidator.

Sometimes the outcome of the administration will be a company voluntary arrangement, within which creditors' claims will be dealt with.

Six months after writing off a debt in your accounts, you can claim VAT Bad Debt Relief from HM Customs and Excise for the VAT you have paid.

If you believe that you own something in the company's possession, you should contact the administrator as soon as possible with full proof of ownership and be prepared to identify what you are claiming. The administrator will examine your claim carefully before deciding whether to release the goods in question, pay you for them or otherwise.

How does administration come to an end?

An administration may come to an end:

- automatically after one year – but this period may be extended with the agreement of the creditors or the permission of the court if more time is needed to achieve the purpose of administration;
- by court order, if the administrator thinks the purpose of administration cannot be achieved, or, where he was appointed by the court, if he thinks the purpose has been achieved;
- where the administrator was appointed out of court, if he thinks the purpose has been achieved.

On conclusion of an administration:

- the company may be returned to the control of its directors and management;
- the company may go into liquidation;
- the company may be dissolved (if there are no funds for distribution to unsecured creditors);
- if a voluntary arrangement has been agreed during the administration, the arrangement may continue according to its terms (it is possible for a voluntary arrangement to run concurrently with an administration).

Is the administrator bound by contracts entered into by the company prior to his appointment?

An administrator has a general duty to the company to attempt to achieve the purpose of administration. In doing so, the administrator may find it impractical to have the company perform certain contracts entered into prior to his appointment, although he will have regard to the financial implications of breaches of the company's contracts. Special provisions apply to employment contracts.

Is the administrator liable for sums due under contracts entered into by the company subsequent to his appointment?

An administrator is not personally liable for contracts entered into as administrator, but normally the administrator will pay for goods or services provided subsequent to his appointment, as an expense of the administration.

As an unsecured creditor, what information am I entitled to?

The administrator must notify all known creditors of his appointment as soon as reasonably practicable, and must send a copy of his proposals for achieving the purpose of administration to all creditors within eight weeks of his appointment. A meeting of all creditors must then normally be held within ten weeks of the date the company went into administration in order to consider the administrator's proposals. However, there is no need for the administrator to hold a meeting if he has stated in his proposals that:

- the company has sufficient property to enable all creditors to be paid in full;
- the company has insufficient property to enable a distribution to be made to unsecured creditors except out of the reserved fund which may have to be set aside out of floating charge assets; or

■ neither of the first two purposes of administration can be achieved. However, he must hold a meeting if requested by creditors whose debts amount to at least 10% of the total debts of the company.

After approval of the administrator's proposals, a report on the progress of the administration is sent to all creditors every six months and at the end of the administration.

Can the unsecured creditors form a creditors' committee?

Yes. A creditors' committee may be appointed at a meeting of creditors and must consist of at least three and not more than five creditors. The creditors' committee receives reports from the administrator and may meet periodically.

Creditors' committee members are not paid, but will receive their reasonable travelling expenses as a cost of the administration.

Can a creditor initiate or continue legal actions against a company in administration?

No. Any petition for the winding up of the company must be dismissed or suspended. In addition, except with the consent of the administrator or the permission of the court:

- no steps may be taken to enforce security over the company's property or to repossess goods in the company's possession under any sale or hire agreement;
- no other proceedings, execution, or legal process may be commenced or continued, and no diligence may be levied, against the company or its property; and
- a landlord may not exercise a right of irritancy in relation to premises let to the company.

How is the administrator's fee determined?

The creditors' committee (if there is one) agrees the administrator's fee. Otherwise, it can be fixed by the creditors or the court. Although the fee can be fixed as a percentage of the value of the property dealt with, it is normally based on the following factors:

- the work which, having regard to the value of the company's property, was reasonably undertaken by the administrator; and
- the extent of his responsibilities in administering the company's assets.

R3 has produced a separate guide explaining insolvency office holders' remuneration, which is available from the person who gave you this guide.

What should I do if I am dissatisfied with the administrator's handling of the case?

You should first contact the administrator to try to resolve the problem. If you are still not satisfied, you may be able to make an application to court.

If you think that the administrator is guilty of professional misconduct, you should contact his regulatory body.

R3 is the UK's leading trade association for licensed insolvency practitioners and business recovery professionals. R3 does not license or discipline its members; this is the responsibility of the practitioner's regulatory body. The regulatory bodies are:

The Association of Chartered Certified Accountants

Tel: 020 7396 7000 www.accaglobal.com

The Institute of Chartered Accountants in England and Wales

Tel: 020 7920 8100 www.icaew.co.uk

The Institute of Chartered Accountants in Ireland

Tel: 00 353 1 637 7200 www.icaei.ie

The Institute of Chartered Accountants of Scotland

Tel: 0131 347 0100 www.icas.org.uk

The Insolvency Practitioners Association

Tel: 020 7623 5108 www.ipa.uk.com

The Law Society of England and Wales

Tel: 020 7242 1222 www.lawsoc.org.uk

The Law Society of Northern Ireland

Tel: 028 9023 1614 www.lawsoc-ni.org

The Law Society of Scotland

Tel: 0131 226 7411 www.lawscot.org.uk

The Insolvency Service

Tel: 020 7291 6895 www.insolvency.gov.uk

Further advice and information for creditors of failing businesses is contained in R3's *Ostrich's Guide to Business Survival*, which can be downloaded from the R3 website www.r3.org.uk free of charge.

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