INSOLVENCY UPDATE

MESTON REID & Co
CHARTERED ACCOUNTANTS

Introduction

As 2018 gathers momentum, some local commentators suggest that there are signs of the green shoots of recovery in the oil & gas industry, and that positive direction should continue if the oil price remains above $65 per barrel. Good news for employment prospects and the general economic wellbeing of the North East, but the property markets, both domestic and commercial remain challenging with supply comfortably outstripping demand.

On the personal financial front, last month's Bank of England figures report an increase in consumer credit of 9.5% : now standing at an eye-watering total of £207.1 billion. The charity Money Advice Trust noted that this level of debt suggests many households are relying upon borrowing to manage their finances. Such position is exacerbated by research reported last month by charity Step Change Debt that showed over 2 million people are stuck in persistent overdraft debt. Further, the same research report estimates that over 1 million people are using high cost credit to pay for everyday essentials. Clearly, the picture will vary across the UK but one conclusion is that many will be struggling with debt for some time to come.

Statutory interest : another cost to consider in a members voluntary liquidation

In late 2017, on the back of one of many legal cases arising from the collapse of Lehman Brothers, a court agreed that HMRC are entitled to receive statutory interest : the current rate is 15% : on any tax liabilities due by a company subject to solvent liquidation proceedings. It was somewhat curious that HMRC sought to ask a court to opine on their right to claim interest because The Insolvency (Scotland) Rules 1986 have provided this right since December 1986. That said, it is fair to say that HMRC have not exercised this right, which may explain the outpouring of complaints from the insolvency profession and, of course, shareholders who now receive a slightly lesser capital distribution from the liquidation process.

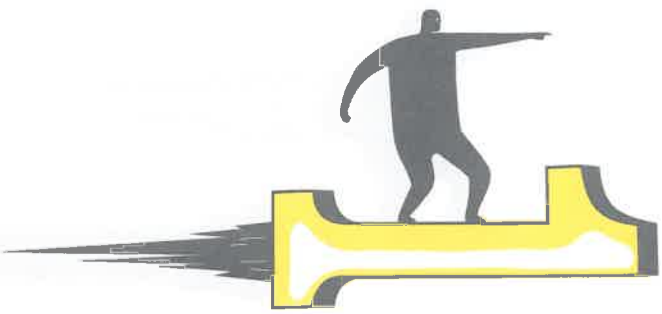
A technical discussion remains to be resolved with HMRC about whether the Scottish regulations are slightly different from the English ones that allow a period of grace for payment after date of liquidation. For example, it is well known that a company pays corporation tax 9 months after the end of an accounting reference period (enshrined in section 59 of the Taxes Management Act 1970) and thus, if the period end is, say, 31 March and solvent liquidation occurs on 30 June, would statutory interest start from 30 June or 31 December ? It seems unfair to suggest 30 June because the company still has 6 months to finalise accounts and submit a corporation tax return. Further, the insolvency legislation includes a section that says statutory interest is not payable on a claim until the date that it would otherwise have been payable. In the example above, such wording points to 31 December as the operative date for statutory interest to start running and thus, should provide a company with the opportunity to pay corporation tax without the imposition of interest. This issue has not been settled with HMRC and thus, many companies who enter solvent liquidation now include a plan to pay the estimated corporation tax arising in the final period as soon as possible after date of liquidation : not always possible in terms of gathering the cash to do so.

Further updates will be provided once the position is clearer.

Restructuring : a black art or common sense

Meston Reid & co participated in a recent Press & Journal Supplement about corporate restructuring and turnaround activity. The article is repeated below lest readers of Insolvency Update did not read that particular edition of the Press & Journal.

When one starts to use expressions such as turnaround strategy, corporate consolidation and business planning, many business owners respond that their company is too small to require the services of someone who can help with these issues. In fact, nothing could be further from the truth because, looking at the Report by the Department for Business, Innovation and Skills "BIS" in December 2017, there were slightly less than 5.7 million separate businesses employing between 0 and 250 people, of which 5.4 million had less than 9 employees and about 200,000 between 10 and 49 employees. Accordingly, the vast majority of employers need to take seriously the subject of business review and considering whether financial difficulties can be addressed and hence, a successful turnaround strategy achieved.



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Put simply, if a publican has three members of staff and sees income declining rapidly for whatever reason, losses may well arise if he does not reduce headcount. Thus, one or perhaps two members of staff will have to be released. Turnaround strategy at its simplest and in such case the publican is unlikely to feel the need to engage a third party consultant to provide a detailed report with recommendations. Similarly, if a small business is finding it difficult to deal with a fluctuating overdraft, a discussion with one's bank manager may well result in part of the overdraft becoming a long term loan which is repaid in equal monthly instalments in line with a cash forecast. Again, restructuring but without significant third party involvement.

However, as a company begins to expand there are various facets which tend to interact with each other such as sales, production, finance, staffing and premises. A business owner can sometimes find it difficult to keep a clear view over all aspects of the business, particularly when income is falling and pressure is being brought to bear by staff (salary increases), suppliers (quicker payment) and HMRC (VAT and PAYE in arrears). Rather than pressing the panic button, third party involvement can be helpful in terms of conducting an objective review of the business and producing a plan that provides the opportunity for survival of all, or part, of the business. Whilst the BIS Report also indicated that Scotland has a business birth rate just slightly higher than its death rate, the reality tends to be that a new business has only one or two employees at commencement, whereas the closure of a business often results in the loss of far more jobs. Thus, it is important that the ongoing birth rate is well above the death rate in order to ensure economic growth and benefits for the country in general.

Napoleon once commented that Britain is a nation of shopkeepers and the BIS Report reflects that retail activity comprises nearly one fifth of all employment in the service industry and about one third of total turnover.

Looking at the retail sector, large company reporting in the last few weeks has been mixed with some household names announcing plans to restructure/consolidate business activities in order to improve profitability and/or simply stay alive. Indeed, according to recent research, the number of retailers toppling into administration in the UK rose in 2017 for the first time in five years. 2018 has already witnessed some high profile casualties.

When speaking to a retailer about a turnaround strategy, one cannot ignore the impact of online spending (Amazon accounts for nearly 50% of all online spending in the US) and some shops consider themselves a place where consumers test a product and then go home to purchase online. That may be acceptable for a large company with both a high street and online presence, but if you are a one-location business and sales are falling, any turnaround strategy will have to be tailored accordingly.

Our TV screens bombard us with a new sales promotion every week. Even the period shortly before Christmas seems to feature a plethora of sales, commencing with "Black Friday". A turnaround strategy may require a company to either spend more money or refocus existing resources in order to change the business focus. For example, how do you make visiting your shop a memorable experience e.g. do the sales assistants wear the product "as walking models"? Do you provide fashion shows or fashion presentations, do you band together with other local retailers in order to offer a free delivery/collection service, are you positioned close to other retailer outlets which create a critical mass of footfall? Do you have a customer care programme that contacts customers for feedback on a regular basis?

Embracing all sorts of technology as it arises may well allow a retailer to attract customers and offer a unique selling proposition. For example, there is talk of being able to produce a hologram of each customer whilst in the shop and showing how clothes look on the customer : it makes changing colours, sizes and styles very easy. Once the business owner is clear upon exactly what is sold, what customers like (rather than what the business owner would like to sell) and the financial/staffing implications have been studied, the resulting turnaround strategy will involve a plan of action with dates, targets and responsibilities.

In reality, most successful businesses restructure and consolidate on a regular basis rather than assuming that the existing model will produce a successful outcome for many years without change.

No single business operates in a vacuum and thus, a turnaround strategy will not always be successful e.g. competitors can be expected to react, and further explains why ongoing adjustment is necessary if a business is to grow and prosper.

A licensed insolvency practitioner deals with both turnaround strategies and business closures which means that he is often the first port of call in terms of seeking suitable advice.

Conclusion

This Update is provided for general interest purposes and does not purport to offer definitive advice. Please contact either Michael J M Reid (reidm@mestonreid.com) or Michelle Byrne (byrnem@mestonreid.com) if you wish to discuss anything raised herein.

Thank you for taking the time to read this Update and feel free to pass it to anyone who you think might be interested in reading it

Meston Reid & Co

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