

Examinerships another view

by Neil Hughes, ACA



In our last issue, Tom Kavanagh FCA, set out his view of the failings of the examinership process and put forward the idea of Administrative Receivership as an alternative. In this article, Neil Hughes, ACA, explains why he takes an opposing view.

The 93% success rate of Examinership in Ireland in recent years surprises many. However, the fewer examinations that take place year on year, the less Irish business people and their advisors know about the process. In my view, more understanding of the benefits of examinership would reduce business failure in Ireland.

It is a simple fact of life in business that there will always be commercial failure for a wide variety of reasons. Insolvency of a business touches many parties: the directors and shareholders in relation to their investment and personal guarantees, the employees regarding their jobs and obviously the creditors who can stand to lose significant sums.

However, what all parties want from a crisis situation is for the result to be maximised and that the highest value is obtained for the company's goodwill, debtors ledger, leasehold interests, supplier certifications, agencies and other intangible assets. Normally, for suitable candidates that have a reasonable prospect of survival and are not 'terminally' insolvent, an examination will provide the framework that can allow this result to be achieved.

The importance of the size of the company can be overstated; a company with turnover as low as €600,000 and a company which was not trading both successfully came through the examination process last year. Recent figures from the US have shown that 22% of insolvent companies there enter the Chapter 11 process.

On average only 2% of insolvent companies in Ireland enter examinership. Although this under-use of the process is in my experience caused by a lack of understanding of how the process works in practice, there also appears to be a lack of appreciation of both how little it can cost to implement and the very high success rates of examinership in Ireland in recent years. Criticisms of the process (and there have been many) centre on the points outlined in the August issue of *Accountancy Ireland*.

Funding the protection period

The breathing space provided by Examinership will normally free up the company's cash flow for use during the process. No payments are made to pre-petition creditors unless specifically identified as necessary for the company's immediate survival. The process provides a company with a sound platform to resist claims from hostile creditors and attract investment on far better terms than are available to a liquidator or receiver, for the simple reason that the company continues to trade. In practice the company will put out as positive a message as it can to its customers: for example: yes, the company is in some difficulty but has chosen to restructure with the assistance of an examiner and essentially it is 'business as usual'. The goodwill which can be generated by this positive proactive approach to a company's difficulties with both customers and suppliers often surprises many professionals.

Cash from debtor collections that previously was immediately mopped up by creditors 'at the door' is now available to the company to allow it focus on the restructure. Accordingly, even a company that was experiencing serious cash flow difficulties prior to the appointment of an examiner will find this pressure eases and in many cases, disappears completely during the process. Normally (to their credit) the Revenue Commissioners will assist a Company in examination by issuing a Tax Clearance certificate for the protection period which will have a huge impact in particular on a company that deals with public sector contracts.

Many companies entering examination will be users of invoice discounting. The advantages to an invoice discounting house of the examinership process are very significant. Often the company in difficulty can have serious issues in its debtors ledger regarding collectibility which are only exacerbated by the appointment of a receiver or liquidator. The 100 day breathing space

provided by the process allows the invoice discounter to work with the examiner and the company to regularise the ledger, bringing into focus the problem debts while bringing the 'funds in use' percentages back into line. An examination will also allow an invoice discounter the opportunity to retain its customer into the future.

Securing an investor

On top of the maximum 100 day protection period the presiding judge will normally extend the protection period by 21 days to allow implementation of a scheme of arrangement. This effectively means that a company will have a 4 month breathing space in total before protection is lifted. It is my submission that any company that cannot attract investment and restructure its finances over a 4 month period with a team of professionals dedicated to the task was probably never a candidate for examinership in the first place.

Cost of Examinership

The actual costs of the petitioning process are also believed by many to be higher than is the case in reality. For example, the independent accountants report in a high profile examinership case last year was carried out for a fee of €5,000. The solicitor's fees incurred for the petition in another straightforward case I have recently been involved in were €3,000 plus counsel's fees of €5,000. Accordingly, the petition stage does not have to be a costly exercise but obviously the cost for this work can be higher if one of the larger professional firms are involved and the exercise is more complex or involves numerous subsidiaries, etc.

A common misconception amongst accountants and solicitors is that a company wishing to enter the process must have a war chest of cash in place in order to simply start the process. Many professionals believe that the full costs of the examination need to be available to be paid up front. This is simply untrue. The examiner and his solicitor are generally paid at the time of the investment, i.e. at the end of the process, or from the assets of the company should the company go into liquidation.

The Don Bluth Entertainment Limited examinership case of 1994 left the petitioning company solicitors in the unhappy position of being 'frozen' unsecured creditors in the examination when they sought their costs as certified examination creditors after the appointment of an examiner proceeded. However this precedent was reversed last year in the Branvard Limited / Shamrock Rovers case by simply including the costs of the petition as costs recommended by the independent accountant that be paid during the examination. This means that now a suitable company entering examination requires no money up front for professional fees. In fact the fees associated with the petition are now often paid along with the examination costs at the time of the ultimate investment.

In a situation where there will be no room in the restructured company for the former directors / shareholders, the costs of 'selling' an insolvent company's

Examinership in Ireland 2004 - 2006

Co. No.	Company Name	Effective Date	Result
2004			
38051	UPC Broadband Ireland Limited	11/02/2004	Successful
324246	Chorus Communications Limited	11/02/2004	Successful
10900	J. Langdon Limited	06/04/2004	Successful
124426	Kinbury Limited	06/04/2004	Successful
172441	Lyons Excavation Limited	24/06/2004	Successful
253343	Celtbury Limited	06/10/2004	Successful
2005			
169951	Gill's Bakery Limited	14/03/2005	Successful
245954	Branvard Limited / Shamrock Rovers	25/04/2005	Successful
347283	Skynet Airlines Limited	25/07/2005	Successful
354986	EU-Jetops Limited	04/08/2005	Liquidation
356302	The Farm Media Group Limited	28/06/2005	Successful
2006			
236908	Cookes Bakery Limited	14/02/2006	Successful
189278	Bromley Communications Limited	27/02/2006	Successful
274690	Shop to Shop Limited	24/03/2006	Successful

business to an investor through examinership are directly comparable to the cost of a liquidator or receiver selling the business. Generally, insolvency professionals will charge the same hourly rates for any type of appointment.

Success Rate

In reality therefore the key issue that arises when assessing examinership is the chance of success of the process for a suitable candidate. The table (above) shows that in the period 2004 - 2006 (to date), 93% of companies that entered examination emerged successfully. The examiner must demonstrate to the creditors that they are in a more advantageous position than they would be in a winding up scenario. This success rate would appear to suggest that for a company's unsecured creditors, examinership has to be worth the limited gamble that the process may fail and that the examiner's costs are taken from the assets of the company in addition to the costs of the liquidator/receiver.

For the company's promoters who often stand to personally lose out enormously in relation to personal guarantees should the company be liquidated, examination and restructure will often be the best option.

For the company's advisors who stand to retain a client if the process works, in my view it should be the first item on the agenda when a client consults with them regarding insolvency, before winding up is even discussed. In my experience the company's principals will thank any advisor who takes a positive, proactive self-help approach to the company's difficulties if the core business is sound. Advisors should keep in mind that often the business is something the promoters will have put huge personal effort into and they will not be thanked for advising promoters to take the winding up option if there is an alternative. Examinership is often the most natural option to take for directors when confronted with the bleak prospect of liquidation.

And finally for employees; I have no doubt that any employee who retains their job in a company that successfully emerges from a period of protection would concur that the under used process of examinership in Ireland is working.