

Common insolvency terms explained

Below you will find some explanations of a selection of insolvency terms which we come across most often in private practice and/or which are commonly misunderstood, including by journalists. The list is by no means exhaustive, so if you come across a term to do with an insolvency in which you are in some way involved, and which is not on the list and which is not explained on any other trusted source such as the Insolvency Service website or Citizens Advice, please feel free to contact us. We offer advice and guidance to all manner of people affected by insolvency, directly or indirectly, and even the occasional journalist, and if we cannot help with your particular issue, chances are we know someone who probably can.

Administration

Contrary to press articles about companies 'collapsing into administration', this is in fact a process designed to rescue a company. If rescue is not possible, it is possible to use an administration to achieve a better result for creditors than in a liquidation, or to realise property in order to pay preferential or secured creditors.

Administrator

A licensed insolvency practitioner, appointed by a company or the court, who takes overall control of the company in administration.

Antecedent transactions

Historic transactions or payments that can be challenged in court once a company or individual has entered into a formal insolvency procedure. The most common examples are transactions at an undervalue and unlawful preferences and void or voidable transactions (those which took place whilst there was a relevant petition in place).

Bankruptcy

Contrary to journalist reports, there is no such thing as corporate bankruptcy when talking about UK companies. Bankruptcy is a formal insolvency option for private individuals needing to deal with debts they cannot pay. The process seeks to convert an individual's assets into funds which can then be distributed among their creditors in a prescribed order of priority. Bankruptcy typically allows an individual to start again free from debt once they have been discharged. Not to be entered into lightly.

Bankruptcy order

A court order based on a creditor's bankruptcy petition whereby an individual becomes bankrupt. Sometimes also used to refer to an adjudication of bankruptcy after a debtor applies for their own bankruptcy.

Bankruptcy petition

Statutory court form by which a creditor can seek to have an individual debtor made bankrupt. Once a petition is in place there are restrictions on what the debtor can do with their assets, including money.

Charging order

A court order that secures a debt against property. Often gives charging order creditor a level of priority if the owner becomes insolvent.

Company voluntary arrangement (CVA)

A form of settlement or restructuring between a company and its creditors whereby the company's debts (often discounted) will be paid over time but the company's directors remain in control, subject to supervision from a licensed insolvency practitioner. Requires 75% by value of creditors to vote in favour.

Compulsory liquidation

Also known as compulsory winding up, this is the process by which a liquidation commenced by a court order is administered by a liquidator.

Creditor

A company or person owed money by another company or person. Creditors can be secured, preferential or unsecured. Creditors can also be future creditors (owed a sum of money at a future date) and contingent (will be owed a sum of money if something does or doesn't happen) – future and contingent creditors are relevant to insolvency procedures and their approval.

Creditors' voluntary liquidation (CVL)

A type of liquidation commenced by an insolvent company, usually as a result of pressure from creditors. Usually much more cost effective than a compulsory liquidation, and more flexible in terms of the company / its liquidator selling on assets including the company's main business. Requires a licensed insolvency practitioner to be willing to take appointment as liquidator, and creditors in principle can reject company's choice of liquidator and install their own.

Debt management plan (DMP)

A written but relatively informal agreement between an individual and their creditors to pay off 'non-priority debts' (so not including mortgages, utilities, tax, etc) in instalments of a single, set monthly amount over time. Not a formal insolvency procedure – managed by a DMP provider (some charge fees but by no means all) who deal with the relevant creditors. No insolvency practitioner involvement so no holistic advice available on full range of insolvency options. DMPs are not legally binding, so they do not ultimately stop creditors taking enforcement action, adding interest, charges, etc, and they often show on a credit record so they can sometimes just prolong difficulties rather than resolve them.

Debt relief order (DRO)

A streamlined formal insolvency procedure suited to individuals with lower incomes, lower value assets and a relatively modest amount of debt. A DRO is an alternative to bankruptcy but with strict eligibility requirements.

Directors disqualification

A court procedure whereby a registered director of a company or someone who acts as a director of a company can be banned for up to 15 years from being involved in the future management of a limited company. Directors can be disqualified by court order or voluntary undertaking. Usually the result of serious breaches of legal duties. Care should be taken never to go into business with disqualified directors.

Directors loan accounts

A record of money borrowed from and/or loaned to a company by its director, distinct from salary, dividends and expense repayments. Overdrawn DLAs need to be paid back following the insolvency of the company or compromised under arrangements made with the relevant insolvency practitioner.

Fixed charge

A form of registered security over some or all of a debtor's assets.

Floating charge

A form of security over one or more classes of the general assets of a company from time to time.

Individual voluntary arrangement (IVA)

A formal and legally binding agreement between an individual and their eligible creditors to pay back their debts over a period of time (often at a discount). An IVA is an alternative to bankruptcy and is supervised by a licensed insolvency practitioner. Some companies (not themselves insolvency practitioners) will advertise debt solutions claiming they are 'government legislation' to 'write off' large amounts of debt, whereas all they are really offering is to refer the debtor for an IVA.

Insolvency

The state of being unable to pay your debts as they fall due, or having total liabilities in excess of the total value of your assets.

Insolvency practitioner (IP)

An individual who is licensed and authorised to act in relation to or take formal appointment over the estate of an insolvent company, partnership or individual. Typically, IP's are qualified accountants who will offer free initial advice and are the only people truly qualified to advise on options involving one or more formal insolvency procedures.

Liquidation

Contrary to press reports that liquidation results in a company 'ceasing to exist', this is an insolvency procedure (also known as 'winding up') whereby an insolvency practitioner collects in, converts into funds and/or distributes the company's assets to those entitled to them under the statutory order of priorities. Companies in liquidation can enter into certain contracts and pursue litigation through their liquidators.

Members' voluntary liquidation (MVL)

Also known as members voluntary winding up, this type of liquidation isn't actually an insolvency procedure at all, despite the name. MVLs are commenced by a solvent company to distribute its assets among shareholders in the most tax efficient manner, under the supervision of a licensed insolvency practitioner.

Misfeasance

An incorrect or inappropriate action that is carried out by a company director in breach of their statutory or common law duties and which causes loss to the company and/or its creditors through the company.

Moratorium

In an insolvency context, this refers to a breathing space which restricts legal action being taken against a company. There are different types of legal moratoria with slightly different legal implications for creditors and companies, so it is worth clarifying which you are dealing with. If the company is in administration, legal action can be taken but only with the consent of the administrator or the permission of the court.

Notice of appointment

A document filed at court which formalises the appointment of an administrator when filed.

Notice of intention (to appoint)

A document filed at court which details a company's or a junior secured creditor's intention to file a notice of appointment to appoint an administrator and which creates a temporary moratorium. Multiple successive notices of intention can be filed but this is now largely frowned upon.

Office holder

A licensed insolvency practitioner appointed over the property or assets of an insolvent company or an individual's personal or deceased estate.

Official Receiver

A civil servant employed by The Insolvency Service who will be the default trustee in bankruptcy or compulsory liquidator of an individual or company, prior to the creditors having the option to seek the appointment of a private sector licensed insolvency practitioner in their place.

Partnership voluntary arrangement (PVA)

Similar to a CVA, but for a traditional partnership instead of a company, this is a statutory agreement between a partnership and its unsecured creditors to repay all or part of its debts over time, under the supervision of an insolvency practitioner.

Personal insolvency

A term used collectively to describe the situation in which an individual who has incurred debts which need to be repaid imminently is unable in a short timescale to reduce their assets to a cash value sufficient to meet those debts. Also used to describe a range of options available to an individual in this position, such as bankruptcy, IVAs and DROs.

Phoenix trading

The phenomenon whereby one or more directors of a limited company which goes into liquidation sets up a new company soon after liquidation, usually on the same premises and with the same staff and adopts the same (or a substantially similar) name to the liquidated company. This practice is unlawful unless the directors follow very carefully (preferably with the benefit of legal advice) one of the prescribed routes designed to protect creditors who might otherwise be unaware that they are dealing with a different company.

Preferential creditor

A class of creditor, including HMRC and similar creditors claiming crown preference, who can expect to be paid out of a formal insolvency in priority to floating charge and unsecured creditors, but behind fixed charge creditors.

Pre-pack administration

Contrary to press reports insisting that these are 'controversial', a pre-pack administration merely refers to the process whereby an administrator negotiates and lines up a sale of a company's business assets prior to their appointment being formalised. If the intended sale is to a connected party (such as the existing management of the company) the administrator must follow a number of careful precautions to ensure that full and sufficient value is being obtained and that creditors' rights are protected accordingly.

Receivership

This a process whereby typically, an insolvency practitioner or other authorised person such as a surveyor is appointed under contractual powers set out in a security instrument to sell or manage one or more assets (often real property assets) of a company or individual for the benefit of the appointing secured creditor. Not to be confused with 'Administrative Receivership', which is a general form of appointment over the whole of a company's assets which is technically still possible, but is very rarely seen today outside certain specialised sectors, a fixed charge (or sometimes LPA) receivership is not formally an insolvency procedure at all, although it does sometimes run alongside a liquidation of the debtor company.

Restructuring

A broad term referring to a range of options for dealing with problem debt from changing the structure of a group of companies or how their company holds its assets through to the negotiated release or deferral of liabilities and to a statutory restructuring under the Corporate Insolvency and Governance Act 2020. Formal restructuring, which in principle allows certain classes of creditor to receive enhanced returns over others are very rare and tend to be the preserve of very large and/or complex corporate groups.

Scheme of arrangement

A specific form of statutory restructuring between a company and its creditors and/or members, that allows a company to reschedule and/or reorganise its debts. Typically used with larger companies and those with significant cross-border interests.

Secured creditor

A creditor that holds security over a debtor's assets.

Statutory demand

A formal notice with formal service requirements which can be used as evidence of a debtor's inability to pay undisputed debts as they fall due, for example, as a prelude to bankruptcy or a winding up petition.

Supervisor

An insolvency practitioner appointed by creditors to supervise a voluntary arrangement entered into by a company, partnership or individual with its creditors.

Transactions defrauding creditors

A transaction entered into at an undervalue with the intention of putting assets beyond the reach of creditors.

Trustee in bankruptcy

A term referring to the Official Receiver by default and subsequently any private sector insolvency practitioner appointed as trustee of a bankrupt's estate, with powers to gather in assets and information and to pursue litigation on behalf of the bankruptcy creditors.

Undervalue

A gift or a transaction whereby the buyer pays significantly less than the true value of the asset being bought. Not unlawful in itself, an undervalue only becomes an issue for the recipient of the gift or the purchaser who has not paid full value if / when the donor / seller later enters a formal insolvency procedure, but an insolvency practitioner appointed at that time can and must then look back often over a number of years and pursue appropriate claims about these.

Unlawful dividends

A share dividend paid notwithstanding that there were insufficient retained or available profits in the company to justify the dividend and/or which is paid in breach of the company's constitution. Unlawful dividends are susceptible to being recalled and recouped by an insolvency practitioner later appointed over the company which paid the dividend.

Unsecured creditor

A creditor that does not hold any form of security over a debtor's assets. Typically, these creditors will be last in line in a formal insolvency, but in certain circumstances they may receive a guaranteed dividend, for example if the 'prescribed part' rules apply in an administration.

Voluntary liquidation

A form of liquidation initiated by directors and members of a company. Can take the form of creditors' voluntary liquidation (CVL) and members' voluntary liquidation (MVL).

Winding up order

A court order usually based on a creditors petition for a company to be placed into compulsory liquidation.

Winding up petition

Statutory court form by which a creditor can seek to have a corporate debtor subject to compulsory liquidation. Winding up petitions have an immediate impact on a company's ability to trade and/or access its bank accounts and are to be avoided wherever possible but acted on immediately if served. Companies who use serviced offices or professional service firms as their registered office should ensure arrangements are in place to open any post delivered to that address promptly and to notify the directors immediately.

Wrongful trading

Wrongful trading refers to the liability of a registered director or someone who acts as a director, trading a limited company beyond the point when they ought to have realised that the company would not be able to avoid entering into liquidation or administration. Liability for wrongful trading will normally be confined to the extent that the continued trading made the overall position of creditors worse. This is a particularly complex area of law and directors should be wary of answering formal questioning about historic trading without legal representation or advice.



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