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The compulsory winding up of companies - some practical considerations

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Introduction

Every year, hundreds of applications are made to the High Court for the compulsory winding up of companies. The vast majority of these are made by creditors in respect of companies which owe them significant sums of money. Prior to the commencement of the Companies Act 2014, the application could be made by creditors owed a minimum of €1,000 (or thereabouts) but that was raised by the 2014 Act to €10,000, or €20,000 where two or more creditors combine to make the application. The following are some of the practical considerations arising for the parties.

The petitioning creditor

There is little doubt that the winding up procedure is one of the most attractive and effective ways of getting paid a debt owed by a company. The application threatens the very existence of the company, meaning that its directors and shareholders need to sit up and take notice. Very often, this will result in the company paying off the petitioning creditor's debt, including his legal costs. In that sense, the winding up procedure can be regarded as the nuclear weapon of corporate debt recovery.

But as with most nuclear weapons, it ought not to be engaged lightly. It has to be remembered that the company probably has employees, meaning that livelihoods may be at stake. As well as that, it is possible that the reason the company is not paying the debt is because it simply cannot afford to. If all of the company's assets are mortgaged to banks and it has nothing by way of liquid assets then there is not much to be gained from the application. Even if the company does have some cash lying about, a successful application for winding up will result in those surplus assets being distributed rateably among the company's unsecured creditors, meaning that the petitioning creditor is likely to receive only a percentage of his debt. Finally, while an application for compulsory winding does not require the creditor to first obtain judgment against the company in respect of the debt, he should be certain that the debt is actually due and owing. In other words, the company should not have a defence to the claim. Because if the company does have a defence, for example the creditor's claim is in respect of goods which the company says were faulty, then the

application is not likely to succeed and the creditor may face adverse costs consequences.

The company's other creditors

Sometimes, the other creditors of the company (that is, the ones who are not petitioning for its winding up), will assume that the issuing of a winding up petition is good news because it equates to their work being done for them by another creditor. They assume that the company will be wound up, a liquidator appointed, the company's assets sold and the their debts being paid. In many cases, this could hardly be further from the truth. There is a good reason that a winding up petition is advertised in local newspapers prior to being heard by the court. It is meant to put other creditors of the company on notice, and they are entitled to attend the hearing and make representations.

Take the following situation. A company owes €100,000 to creditor A, €200,000 to creditor B and €300,000 to creditor C, all of the creditors being unsecured. The company has assets worth €320,000. If the company is wound up, and assuming the costs of the liquidation to be €20,000, each creditor would receive 50% of his debt because the company has sufficient assets to meet only 50% of its debt. But suppose creditor B applied for the compulsory winding up of the company and this negotiated in a negotiated settlement whereby the company agreed to pay him €180,000. This means that the company now has only €140,000 remaining to pay off the other two creditors. Thus, a liquidation at this point would result in creditors A and C receiving substantially as a result of creditor B being paid almost his entire debt. Therefore, the presentation of a winding up petition can often amount to a money-grab to the detriment of other unsecured creditors. They, in turn, need to be aware of their options in that situation. There aren't many options available to them, but the most obvious is to take over the winding up petition once it is abandoned by the petitioning creditor (who has been paid off) and to ensure that the company is wound up so that each creditor receives its fair share.

The directors and shareholders

Since the petition is an existential threat to their company, directors and shareholders need to be worried. Not only at the prospect of a court hearing, but the fact that the petition will be advertised in daily newspapers. That, in turn, will ensure the whole business community is aware of the company's financial problems resulting in the death of a company which may have been experiencing nothing more than temporary cash flow issues. The company can certainly defend the

proceedings, for example on the basis that it does not owe anything to the petitioner. But since such an argument can only be made at the hearing, much of the damage will have been done by the advertisements having been placed at this stage. To avoid this, the company may apply to the court for an injunction restraining the advertisement of the petition. It may instead apply for court protection, for an examiner to be appointed with a view to keeping the company afloat. Alternatively, many companies choose to initiate the procedure for their voluntary winding up in order to avoid the matter being dragged through the courts (and to appoint a liquidator if their choosing instead of the one proposed by the petitioner). The majority decide to attempt to settle the matter upon receiving a copy of the petition, but before it is advertised. The option cosen by the company will depend on its objectives and means. For example, a company with no further ambitions of funds, may simply do nothing and allow itself to be wound up.

Conclusion

The above is a brief overview of a highly specialised and complex area of law. As is evident, the presentation of a winding up petition under section 567(1)(d) of the Companies Act 2014 has the potential to affect a number of parties and each of them may be required to take urgent action in order to protect their interests. What precisely that action will be will depend on the circumstances of each case and ultimately on the financial position of the company itself.

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Important Note

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