



What is liquidation?

Solvent and insolvent liquidations explained

Solvent liquidation (MVL)

If a company has fulfilled its purpose and the directors and shareholders wish to bring the company to a close, a Members' Voluntary Liquidation (MVL) may be a tax-efficient way to do this.

Funds returned to shareholders via an MVL are treated as a capital distribution rather than a dividend, meaning that they are subject to capital gains tax (CGT) as opposed to income tax.

In the majority of MVLs, this might mean the difference of paying tax at 20% rather than 33.75% or 39.35% (correct as at February 2023).

Furthermore, if the shareholders are eligible for Business Asset Disposal Relief, then the rate of CGT is reduced to just 10% (subject to a lifetime limit).

Additional savings can be made by utilising shareholders' annual exemptions for CGT (£12,300 tax free in 2022/23 and £6,000 tax free in 2023/24). A discount may also be possible for early settlement of certain debts, such as corporation tax.

An MVL also provides greater protection to the shareholders against future claims, so long as those claims were not known about at the start of the MVL.

If the assets are less than £25,000 then an MVL may not be necessary as the directors could apply to strike off the company with the same capital treatment as an MVL.

To find out more and get a competitive and personalised quote, please get in touch with our Insolvency & Recovery team.

Solvent vs insolvent

Liquidation is a legal process used to wind up the affairs of a company when it's no longer required or viable. Liquidations can be either solvent or insolvent, so what's the difference?

A solvent liquidation is when a company has sufficient assets to pay all liabilities in full and the shareholders are looking to extract the remaining cash/assets in a tax-efficient way.

An insolvent liquidation is when a company does not have sufficient assets to pay all creditors in full.

When a company is insolvent with no prospect of a recovery, the directors should seek advice from an insolvency practitioner as soon as possible to protect their personal position.

Insolvent liquidation (Creditors' Voluntary Liquidation or CVL)

When a company is in financial distress it's vital that the directors get advice from either their accountant or a qualified insolvency practitioner. The earlier advice is sought, the more options are available.

Section 123 of the Insolvency Act 1986 states a company is insolvent when it's unable to pay its debts as and when they fall due (cashflow test) or when the value of the company's assets are worth less than the amount of its liabilities (balance sheet test).

An insolvency practitioner can discuss the available options, such as an Administration, Company Voluntary Arrangement or a Creditors' Voluntary Liquidation. If it's not possible to preserve the business, or rescue even part of it, then it's likely that a CVL will be the most appropriate option to deal with the controlled wind-up of the company's affairs.

A CVL brings about the end of the company, which can only be initiated by the directors. The shareholders will pass a resolution to place the company into liquidation and appoint a liquidator. Unsecured creditors will not have any influence on whether the company is placed into liquidation or not, but they may try to appoint an alternative liquidator of their choice. Once an insolvency practitioner is appointed as liquidator, it's their role to realise the company's assets and, if possible, pay dividends to creditors.

Employees will be entitled to claim for any arrears of wages, holiday pay, notice pay and redundancy pay from the Redundancy Payments Service (see our brochure entitled 'Liquidation: What it means for employees' for further information, available on our website).

The liquidator will have a duty to realise the assets of the company for the best possible value, but often this may involve a sale to the former directors, shareholders or employees. The liquidator will also have a duty to review the conduct of the directors, to make sure that creditors haven't been intentionally left high and dry. If there have been any inappropriate actions, the liquidator can bring claims against the directors to recover the assets which were put out of the reach of creditors.

The liquidator's fee will generally be paid from the realisation of the assets and therefore the directors are not personally liable to these.

Insolvent liquidation (compulsory winding up by the court)

Both an MVL and a CVL are initiated by the company directors, however, if a company is unable to pay its debts but doesn't seek advice from an insolvency practitioner, a creditor may petition to wind up the company via the courts.

If a company is indebted to a creditor for more than £750 then the creditor may petition to wind up the company. If the court grants the winding-up order then the Official Receiver (OR) would be appointed as liquidator.

The OR is a government official who will deal with the statutory process of the liquidation. If there are significant or complex assets to be recovered, the OR may offer the appointment to an insolvency practitioner.

Alternatively, a creditor may also be able to request that an insolvency practitioner be appointed. The liquidator will have similar duties to the CVL appointed liquidator in respect of making asset recoveries where possible.



Need help?

Our Insolvency & Recovery team is able to help with all types of liquidations. We advise directors to speak to us as soon as possible so that all options can be considered.

We have two licensed insolvency practitioners with a combined sixty years' experience. For further advice, please get in touch.

0330 024 0888 | enquiry@larking-gowen.co.uk | larking-gowen.co.uk  [@LarkingGowen](https://twitter.com/LarkingGowen)