Examinership: Potential for Abuse

By Andri Antoniou*

A process putting companies *"on life support with no prospect of survival"* is how examinership was described by a Judge in Ireland in 2010, who went on to say he was *"more and more reluctant"* to afford protection to troubled companies. Yet, this is the regime which is about to be approved by our Parliament before the end of the year as a corporate restructuring tool for troubled companies.

During a recent seminar on examinership held at the Cyprus Chamber of Commerce and Industry, delivered by a member of the panel of experts that assisted the Government in formulating the Bill, it was explained that, in his opinion, examinership provides a more creditor friendly option than existing insolvency routes such as liquidation, further suggesting that the dividend to creditors will be much higher.

From practical experience of the lengths directors will go to to ensure their company remains in their control, despite its viability, the only people who stand to gain from this process will be the lawyers appointed to petition the court, the accountants instructed to prepare the Independent Accountant's Report and the Insolvency Practitioners acting as examiners, **definitely not** the creditors or the shareholders.

Not only will the cost of initiating examinership further burden an already ailing Company but, in my professional opinion, this process will serve as a tool to abuse the system.

Once the court is persuaded that there is a reasonable prospect of survival of a company (which means judges, who will need to rely heavily on the Accountant's Report, must possess the necessary skills to understand management accounts and feasibility studies), it will grant the Examinership Order, resulting in a moratorium period (initially) for four months, during which the company will enjoy protection from creditors, whilst directors continue to administer the affairs of the company, potentially further dissipating company assets.

Unfortunately, the safeguards put in place by the regulators, (the bodies or authority that will be licensing Insolvency Practitioners and monitoring their conduct) to protect creditors' interests in countries such as the UK, do not exist in Cyprus. We do not have Best Practice Directives and/or Statements of Insolvency

Practice ("SIP's), providing guidance on the standards to which Insolvency Practitioners must adhere, to avoid disciplinary action which may result in loss of authorisation, to deter those Insolvency Practitioners influenced by a desire to gain personally over their professional obligations, compelling them to think twice before they consent to act and put forward applications which knowingly misrepresent the financial position of a company.

Furthermore, it is likely that examiners will claim that the four month period they will have within which to prepare a Proposal and obtain Creditor Approval, will not be sufficient time and applications will be made to court requesting extensions (in Ireland this period has been reduced to 70 days extendable up to a maximum of 100 days).

Consequently, when examinership fails, assets will be depleted by soaring professional fees which will no doubt soak-up funds which may otherwise have been used to pay creditors, with detrimental implications for secured and preferential creditors. An alternative option, which the team of experts could have suggested, is a simple application to the Court for an interim order, thus affording protection from hostile creditors, whilst a Company Voluntary Arrangement (which is already provided for in existing legislation, s198 of CAP: 113), could be put in place.

In Ireland, only 2% of insolvent companies enter examinership (16 cases in both 2010 and 2011 and 27 in 2012) because this process places very stringent professional obligations on Insolvency Practitioners to vet each case carefully. If they do not, they will face the consequences.

There is no doubt in my mind, where a floating charge holder decides to enforce its right to appoint a Receiver Manager (RM), within a month of the appointment, the directors, guided by their advisors, will be applying to the court for an Examinership Order thus, frustrating the RM's right to take control of the assets.

Ultimately directors of heavily insolvent companies will use the examinership process as a way to "put their companies on life support" despite a lack of any prospect of survival; without safeguards in place to avert abuse of this process the risks of further loss to creditors are clear and unavoidable.

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