STRACHAN PARTNERS

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REVIEW OF THE COMPANIES AND ALLIED MATTERS ACT 2020: COMPANY RESCUE MECHANISMS

Introduction

An ideal insolvency regime is one that sets out strategic options for maximizing a business' viability as well as ensuring a smooth exit of non-viable businesses for the sake of freeing capital, which is a finite resource in the market space.
The recently enacted Companies and Allied Matters Act 2020 ("CAMA"), in line with global best practices and improving on the framework for insolvency contained in its predecessor, has introduced an improved regime for insolvency.
This CAMA not only provides exit options for ailing businesses but introduces three (3) company rescue mechanisms which offer an insolvent company a chance to continue as a going concern. These mechanisms are:

a. Company Voluntary Arrangements (CVAs);
b. Administration; and
c. Netting.

A. COMPANY VOLUNTARY ARRANGEMENTS:

Company Voluntary Arrangement (CVA) is a procedure that allows a company and its creditors reach a binding agreement regarding the payment of the entirety or a part of its debt over a definite period.

This procedure essentially allows the company the opportunity to restructure its operations for improved profitability and align its debt obligations with its estimated earnings under the restructured operational method.
Simply put, it allows a potentially-profitable but failing company an opportunity for rescue by relieving it of any creditor pressure and foreclosing the right of the creditors under the arrangement to initiate a compulsory winding up.
When is a Company Voluntary Arrangement Suitable?
It is important that a Company Voluntary Arrangement (CVA) is only used where the company is viable and is potentially-profitable. Alternatively, it may also be used where the company has disposable assets that can be readily transformed into money. The key underlying factor is the viability or potential-profitability of the business as a whole.

Procedure

1. To ensure the viability of the company's business, the process is initiated with a feasibility study and a subsequent proposal stipulating the objectives of the process and how the company intends to achieve it.

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2. Depending on whether the company is dealing in its ordinary course of business, in liquidation or administration, the relevant insolvency practitioner is nominated under the proposal to oversee the implementation of the arrangement.

3. The Board approves the arrangement by a resolution and transmits the proposal to the relevant insolvency practitioner.

4. Ultimately, the members of the company and its creditors consider the proposal and approve it thus giving the insolvency practitioner the go-ahead to implement.

Advantages:

i. The directors and company management remain in control;
ii. It is a cheaper option than a receivership or liquidation;
iii. It guarantees some degree of confidentiality as it comes with no publishing obligations;
iv. It precludes legal action and multiple repayment demands by creditors.

Disadvantages:

i. The agreement reached under a CVA does not bind secured creditors;
ii. The company's credit rating is affected by the arrangement;
iii. The agreement may span a long period of time.

B. ADMINISTRATION

Administration is a company rescue mechanism which allows an insolvent company, under the control of an administrator, an opportunity to rescue the whole or any part of its undertakings.
Simply put, it is a procedure which affords an insolvent company the opportunity to continue as a going concern for the primary purpose of managing its debt profile to ensure the company can resume the pursuit of its business, in whole or part.
An administrator, who must be a licensed insolvency practitioner,[1] is appointed to oversee this process as company's board cedes control to the said administrator. The administrator's appointment indicates the commencement of this process.

Appointment of an Administrator

An administrator may be appointed by:
a. the company or its directors (voluntary administration)
b. an administration order of the Court
c. the holder of a floating charge.[2]

The administrator is expected to conduct his business efficiently and expeditiously[3] and the company will remain in administration for an initial period of one year, after which it may only be extended by an order of Court or with the consent of the company's creditors.[4] Prior to this time, an administrator may be removed by the Court,[5] replaced by the party who appointed him[6] or may resign voluntarily.[7]

1 Section 447(1), CAMA
2 Section 443, CAMA
3 Section 445, CAMA
4 Section 513, CAMA
5 Section 526 & 528, CAMA
6 Sections 529, 530, 531, 532 & 533, CAMA
7 Section 536(1)(a), CAMA

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Purpose of Administration

The purpose(s) of administration are, in the order listed below, as follows:

a. rescuing the company in whole or part to enable it continue as a going business concern;

b. achieving a better result for company's creditors than would be likely if the company was immediately wound up without first being in administration; and

c. realizing property to make a distribution to secured/preferred creditors.[8]

Conduct of the Administration

Upon appointment, the administrator shall make a formal statement setting out proposals specifying how he intends to achieve the purpose of the administration including through company voluntary arrangements and arrangements and compromise.[9] This proposal shall be shared with creditors of the company, its members and the Commission.[10] The proposal shall be formally presented to a creditors' meeting which it will be considered and approved.[11] The administrator thereafter conducts the administration of the company in accordance with the approved proposals.

Effect of Administration

The Act provides for the effect of the commencement of an administration. The provisions of the Act, in this regard, ensure that the administrator can pursue his statutory mandate without legal interruptions. Some of these are:

1. The Board cedes control of the Company to the Administrator who shall become responsible for its management to ensure the objectives of administration are met.
2. The company shall conduct business, issue documents and correspondence with a clear indication that it is "in Administration" with the name of the administrator clearly stated.
3. All petitions for the winding up of the company shall be dismissed/suspended, save for those presented under special banking provisions of existing banking legislations and those presented on the grounds of public interest.[12]
4. No resolution may be passed for the company's winding up neither shall any order be made for its winding up.[13]
5. No steps shall be taken to enforce security over the company's property or repossess goods in the company's possession under a hire purchase arrangement without the consent of the administrator or permission of the Court.[14]
6. No legal process, including legal proceedings, execution, distress and diligence shall be commenced or continued against the company without the consent of the administrator or permission of the Court.[15]

The above-listed effects, although not exhaustive, ensure the administrator can perform his duties without legal interruptions, particularly, without creditors commencing winding up proceedings or other legal proceedings. The administration is essentially a moratorium period within which an administrator can pursue his mandate of company rescue in relation to the insolvent company without the hovering risk of liquidation or less adverse but compounding circumstances.

8 Section 444, CAMA
9 Section 486, CAMA
10 ibid
11 Section 490, CAMA
12 Section 477, CAMA
13 Section 479, CAMA
14 Section 480, CAMA
15 ibid

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C. NETTING

Netting is a contractual concept which, essentially, entails the consolidation of multiple payments, transactions or financial positions between two or more parties; with the aim of creating a single amount and determine which party is owed remuneration. This concept is commonly deployed in transactions relating to Other the Counter (OTC) derivatives to evaluate and settle risks between parties to a contract.

The recently enacted CAMA expressly introduces the concept of “netting” in relation to Qualified Financial Contracts (QFCs) and transactions such as foreign exchange transactions, currency/commodity swaps, collateral arrangements and derivatives generally etc.

The Act defines a QFC as any agreement that provides for the satisfaction of payment/delivery obligations within a specified period whether subject to any condition or not. The Act also gives the relevant financial regulatory authority the power to designate additional QFCs.[16] QFCs are guaranteed enforcement despite any provisions of the Gaming Machines (Prohibition) Act or other related laws which purport to invalidate any such agreements.[17]

In defining “Netting”, the CAMA broadly states it to be any arrangement which involves the four-step procedure set out below:

(a) termination, liquidation or acceleration of any payment or delivery obligation or entitlement under one or more qualified financial contracts entered into under a netting agreement;

(b) calculation or estimation of a close-out value, market value, liquidation value or replacement value in respect of each obligation or entitlement or group of obligations or entitlements terminated, liquidated or accelerated under item (a) above;

(c) conversion of any values calculated or estimated under item (b) above into a single currency; and

(d) determination of the net balance of the values calculated under item (b), as converted under item (c), whether by operation of set-off or otherwise.[18]

Simply put, Netting under the CAMA involves the arithmetic quantification/valuation of parties’ obligation arising from qualified financial contracts (QFCs) and setting off of same to arrive at a net obligation/entitlement of either party. For example, Chucks Motors owes Ahmad Enterprise the sum of N250,000 for the supply of engine oils to its fleet of cars. Similarly, Ahmad Enterprise owes Chuks Motors a total sum of N350,000 for its concierge services for the month of. By netting how much each party owes the other, a single invoice can be created for Ahmad Enterprise to pay Chuks Motors the outstanding N100,000. An agreement which provides for this arrangement inter parties is called a “*Netting Agreement*”, a term which is further broadly defined by the Act.[19]

In relation to its business rescue function, a netting arrangement allows an insolvent company balance its credits against the debts of its creditors for the purpose of immediately evaluating its gains and losses thus, in the best cases, offsetting its losses with gains (if any). Accordingly, the enforcement of netting agreements will see insolvent companies immediately call on prospective income to satisfy prospective liability and immediately place the company in a better position than it would have been prior to the enforcement.

16 These regulatory bodies include the Central Bank of Nigeria (CBN), the Security Exchange Commission (SEC), the National Insurance Commission and any other financial regulatory authority that may be established by an Act of the National Assembly. Section 718 CAMA.
17 Section 720 CAMA
18 Section 718 CAMA
19 Section 718 CAMA

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In many cases, under netting arrangements, insolvent companies will be able to call on obligations due to them that would otherwise have been written off. This call on future contractual obligations allows insolvent companies the opportunity to analyze its business posture holistically. With this in place, a winding up is reduced to a last resort option for a company intending to continue as a going concern.

Consistent with the above, the Act mandates the recognition and enforcement of netting agreements including against an insolvent party in accordance with its terms and without hindrance by any acts of a liquidator, any provisions of law relating to bankruptcy or any other provision applicable to an insolvent party/insolvency proceedings.[20] As such, netting arrangements take priority regardless of any laws precluding or regulating company insolvency and ensure company rescue is prioritized above all.

CONCLUSION

The introduction of the company rescue mechanisms, as detailed above, significantly improves the legal framework for insolvency in Nigeria and provides options to failing companies to avoid being liquidated in the face of a fighting chance at profitability. With these mechanisms being novel to our jurisdiction, their actual effect on business prosperity cannot be properly adjudged at this time. If their application in advanced jurisdictions is anything to go by, there are a lot of positives to look forward to. In any case, they are a welcome addition to our company regulation framework.

Disclaimer: This article is intended to provide a general guide.
For expert advice/opinion in any of the above areas,
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