AZETS

Small Company Administrative Rescue Process (SCARP)

What is SCARP?

SCARP is a formal corporate rescue mechanism which was signed into law in Ireland on 7 December 2021 under the Companies (Rescue Process for Small and Micro Companies) Act 2021.

The primary objective of SCARP is to save small and micro companies and preserve employment in the underlying enterprise, similar to examinership. The introduction of SCARP has provided businesses with a viable, cost-effective restructuring option to deal with the many issues that persist: the legacy impact of the COVID-19 pandemic, inflationary cost pressures, supply chain issues, and increased borrowing costs, to name just a few.

SCARP is a more accessible and cost-effective alternative to examinership and allows businesses to restructure their balance sheets within a shorter timeframe in a predominantly out-of-court environment.

Azets Ireland has advised over 280 clients on examinership. We can use our experience to assist your company with the SCARP process.

Azets is a multi-disciplinary firm best known for specialising in formal corporate recovery matters, specifically examinership and more recently in SCARP. Our firm has acted in over 280 examinerships over the past 20 years and has acted in more SCARP cases than any other firm. Our focus is unashamedly on working to help owner-managed, entrepreneurial and family-owned businesses. That experience provides us with a unique insight into both the legislation around restructuring, with which we are very familiar, and, importantly, the practical application of same.

Our team of restructuring experts have unrivalled experience in saving enterprises, many of whom would have successfully completed a SCARP process. No other firm has 4 process advisers undertaking SCARP appointments within our ranks and each of those process advisers having presided over successful SCARP cases. Over 98% of corporate bodies in Ireland meet the criteria for the appointment of a process adviser; we believe it has significantly altered the landscape in making restructuring more accessible for small and micro-sized businesses.

SCARP Process timeline:

Statement of Affairs (Pre-planning stage): Directors prepare the Company's SOA.

PA's Report (Pre-Planning stage: Process Advisor (PA) reviews the SOA and forms a view whether the company has a reasonable chance of survival.

Day 1 Commencement of the SME Rescue Process: Company directors convene a meeting and resolve to appoint a PA.

Day 2-16 - Excludable debts: Certain State creditors (incl. Revenue Commissioners and Dept of Social Protection for certain amounts payable under Redundancy and Social Welfare Acts) have 14 days to inform the PA if they are opting in or out of the process.

Day 2-46 - Preparation of the Rescue Plan: PA engages with creditors and formulates a rescue plan.

Day 42 - Meeting of Members and Creditors: PA shall convene a meeting of members and creditors to review, approve or reject the rescue plan.

Day 49 - Approval of Rescue Plan: Approved if 60% in number, representing a majority (over 50%) in value of an impaired class of creditors represented at the meeting vote in favour of the rescue plan.

Day 70 - Completion: If no creditor objects within 21 days (i.e. between Day 49 and Day 70) cooling-off period, the Rescue Plan becomes binding on all creditors.

Comparing SCARP vs Examinership

SCARP	Examinership
• Initiated by Director Resolution	• Court petition to appoint an Examiner
• SME or Micro Company only	• No restrictions apply
• Meetings must be held by day 49	• Must have returned to Court with the outcome of meetings by day 100
• State Creditors can choose to 'Opt Out'	• All Creditors are bound by the process
• Rescue plan must be approved by 60% in number and majority in value of those creditors represented at the meeting	• Simple majority in one class of impaired in-the-money creditor and majority in number
• Less likely for Directors to lose control	• Some risk of losing control – potential enforced regime change
• If creditors accept the scheme, no court approval is required, as long as no creditor objects	• Court approval is still required even if creditors approve the Scheme proposed by the Examiner
• Lower costs due to less professional advisors involved and quicker timeframe	• Likely to be more costly

Key considerations

Eligibility Criteria

SCARP is suited to companies which are about to be insolvent or are insolvent, but have a reasonable prospect of survival. In order to qualify to avail of SCARP, an applicant company must satisfy two of the following three criteria:

- Annual turnover of less than €12m;
- A balance sheet total of less than €6m;
- Average number of employees less than 50.

98% of all corporate bodies in Ireland will qualify under the above criteria, making this a very accessible restructuring tool for companies in difficulty.

Further restrictions are that SCARP is only available to companies where no resolution exists or no court order has been made for the winding up or liquidation of the eligible company.

In addition, applicant companies must not have availed of SCARP or examinership within the previous five years. There can be no petition for examinership currently before a court and no examiner appointed to the company concerned.

Appointing a Process Adviser

SCARP legislation was brought in to make restructuring options more accessible and less expensive for small and micro enterprises. In this regard, the appointment of the person tasked with overseeing SCARP (a 'process adviser') takes place in the boardroom; there is no requirement to make an application to court like in an examinership.

The appointment of the process adviser takes place via a board resolution i.e., the board of directors of the company resolve to appoint a process adviser. Prior to the appointment taking place, there are certain pieces of information which are required to be provided by the directors of the company to the nominee process adviser.

The primary document being the statutory statement of affairs for the company and financial information which is required for the process adviser to prepare their report. Based on all of this, the process adviser prepares their report on the affairs of the company and critically, whether in their view, it has a reasonable prospect of survival.

Within 7 days of the process adviser issuing their report to the company, accompanied by their determination on the prospects of survival for the company, the directors must hold the aforementioned meeting for the appointment of a process adviser.

Key Duties of Process Adviser

SCARP imposes a number of strict deadlines on the process adviser, which include notifying creditors and employees of the company within 5 days of their appointment. However, the primary duty of the process adviser is to formulate a rescue plan that enables the survival of the company which may include a write-down of the debts of the company.

The process adviser is required to formulate this plan and issue notices for meetings of members and creditors within 42 days of their appointment. The meetings of members and creditors are required to take place no later than day 49 of the process adviser's appointment.The process adviser will work to secure funding to enable the formulation of a rescue plan. This funding may come from a combination of any number of sources including: (i) fresh equity investment (ii) surplus cash flow (iii) new bank lending and / or (iv) sale of any non-core assets.

Having undertaken more SCARP appointments than any other firm, and having acted as examiner in over 280 examinerships, Azets Ireland has a bank of potential investors and refinancing solutions available to companies in any restructuring process.

Key considerations continued

Approval of Rescue Plan

The process adviser is required under the legislation by day 49 of the process to have convened meetings of members and creditors for the purposes of considering the rescue plan formulated. The process adviser is required to provide 7-days' notice to all members and creditors of the relevant meetings; therefore, the process adviser must issue the notices convening the meetings by day 42 of the process.

The rescue plan is a two-step process:

1. Firstly, the rescue plan must be approved by at least one class of impaired creditor (a class of creditor receiving less than the full value of their debt) where 60% in number of creditors voting, representing a majority (over 50%) of the debt vote in favour of the rescue plan; and
2. Secondly, there is a 21-day objection period after the process adviser has filed their notice of approval with the relevant court where any creditor can object to the rescue plan as formulated.

On expiry of the 21-day objection period, and where no objection has been lodged, the rescue plan is approved and becomes binding on all members and creditors of the relevant company, regardless of whether members or creditors voted to accept the rescue plan.

Onerous Contracts

SCARP provides for the repudiation of certain onerous contracts where the process adviser has determined that such contracts are particularly burdensome on the company and their continuation is negatively impacting on the company's prospects of survival.

The mechanism to repudiate any onerous contract is a vitally important tool in any restructuring and it has been regularly used to great effect in multi-unit retail restructurings where loss-making units were required to be surrendered to landlords and the only mechanism to do so in a going concern trading scenario was by way of a repudiation application in an examinership.

It is possible to disclaim onerous contracts in a liquidation but the distinction there is that to do so is not in a going concern scenario.

Examples of onerous contracts which typically arise in restructurings would include above-market lease terms or a loss-making customer contract.

Court Engagement

In the majority of SCARPs, there will be little to no involvement from the Court in the process. For example, there is no requirement to seek formal court approval of any rescue plan provided no creditors object within the 21-day cooling-off period that follows the creditors meetings.

In limited circumstances there may be a requirement to engage with the Court, for example:

- To seek Court direction on any matter that may arise during the tenure of the process e.g., serving notice of SCARP on creditors in foreign jurisdictions;
- Seeking a stay on creditor enforcement actions including receivership appointments;
- To repudiate onerous contracts, if agreement cannot be reached with counterparties to the contract.

In the event there is an objection to a rescue plan lodged by a creditor within the 21-day cooling off period, there will be a requirement for a Court hearing. During this time, the 70-day SCARP timeframe is paused i.e., 'the clock is stopped ' until the hearing of the objection has taken place.

Points for Business Owners

Business owners and managers will face many challenges in the coming years. Some of the key considerations for business owners when contemplating a restructuring process such as SCARP include:

Is there a good underlying business? – in order for any restructuring to succeed the underlying trade and business of the company must be sound. The company must have a reasonable prospect of survival and be capable of generating future profits if a restructuring takes place.

What are my immediate pressures? – business owners must consider whether there are any immediate financial pressures. For example, is the bank seeking the appointment of a receiver to enforce their security? Is a leasing creditor threatening to take back one of its leased assets which are critical to the operation of the business? Has a supplier threatened to issue a winding-up petition in respect of sums unpaid?

Have payment terms been breached with Revenue for current or historical taxes? Has the business suffered bad debts to the extent that current cash flow is at perilously low levels?

Any of these immediate pressures may necessitate the appointment of a process adviser.

Will I be able to break even during the rescue process? – as part of any restructuring it is key that the business will be in a position to discharge all ongoing liabilities as they fall due during the process so as not to worsen the position of creditors.

The preparation of detailed cash flows demonstrating the funding available to the company during the rescue process will be key to this. In the absence of being able to be cash-positive or neutral, a commitment will be required to shore up any deficit that arises.

How will I be able to exit the process and fund a rescue plan? – given the short timeframe of the process, it is imperative, but not essential, that business owners have a clear line of sight in terms of how they intend to fund a rescue plan and ultimately successfully exit the rescue process.

A pool of funds will be required in order to fund any rescue plan, pay the costs of the process and discharge dividends to creditors.

In conclusion, SCARP is a viable restructuring tool for small and micro companies in Ireland. Our experience at Azets shows that the process works. It allows for companies to restructure their affairs within a very short period of time and is a powerful tool in the armoury of business owners which can transform the balance sheet of a company in distress.

More importantly, the process will save viable enterprises and their underlying employment from liquidation and closure which would result in further losses to creditors and the State.

In short, SCARP is a restructuring option which should be fully explored prior to any decision being made to cease to trade or go into liquidation.

How we can assist with SCARPs

Our restructuring team has extensive turnaround experience in examinership and SCARPs across a wide range of industries

How Azets can assist SCARPs:

- Offering objective business advice including a range of solutions to turnaround a business in distress outside of a formal insolvency process;
- Reviewing business viability and determining whether the company has a reasonable prospect of survival;
- Acting as Process Adviser and assisting the company with creditor negotiations, engagement with potential financiers and the development of a rescue plan;
- Acting as adviser to any creditor whose debt is being included in a SCARP process.

Please contact us for a free, no-obligation and confidential consultation to see how we can help your company survive a period of uncertainty.

It’s in our DNA to save viable businesses.

Dessie Morrow

Partner

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As an experienced insolvency practitioner and appointment holder, Dessie's key focus includes the following; advisory support to accountants and solicitors seeking insolvency advice for their clients, Process Adviser acting in SCARP cases, Circuit Court or High Court appointed examiner to companies (which are insolvent but have a reasonable prospect of survival), fund-raising assignments, sale of business mandates, due diligence, preparation of expert witness reports, cross-border insolvency work with particular focus on the UK and Cyprus and debt settlements with secured creditors.

Diarmaid Guthrie

Director

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Diarmaid has over 10 years' experience in our Advisory & Restructuring department with extensive expertise in formal and informal restructurings together with independent business reviews. Diarmaid provides tailored business advise for businesses across a broad spectrum of industries. He is a licensed insolvency practitioner having been appointed by the Courts as examiner and liquidator together with acting as process adviser to a number of companies availing of the SCARP process. Diarmaid leads our Forensic and Litigation Support service line.

Conor Noone

Director

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Conor has over 13 years' experience in the Advisory & Restructuring department of Azets Ireland, and has fourteen months experience working in the audit department of a Big 4 accountancy practice at the start of his career. Conor has extensive creditors voluntary liquidation, court liquidation, receivership, deal advisory, SCARP and examinership experience, having acted as Examiner, Official Liquidator and Process Adviser to numerous companies to date. Conor also has extensive debt settlement, sale of business and fundraising experience having worked with clients across a broad range of sectors including retail, hospitality, construction and healthcare.

Case Study 1: Digital Advertising Group

A group of three companies in the digital advertising sector across a number of platforms which had suffered as a result of a reduction in advertising spend.

The issues faced by the Company were:

1. Covid-19 and the reduction in advertising spend;
2. Lack of support from the Group;
3. Cash flow pressures as a result.

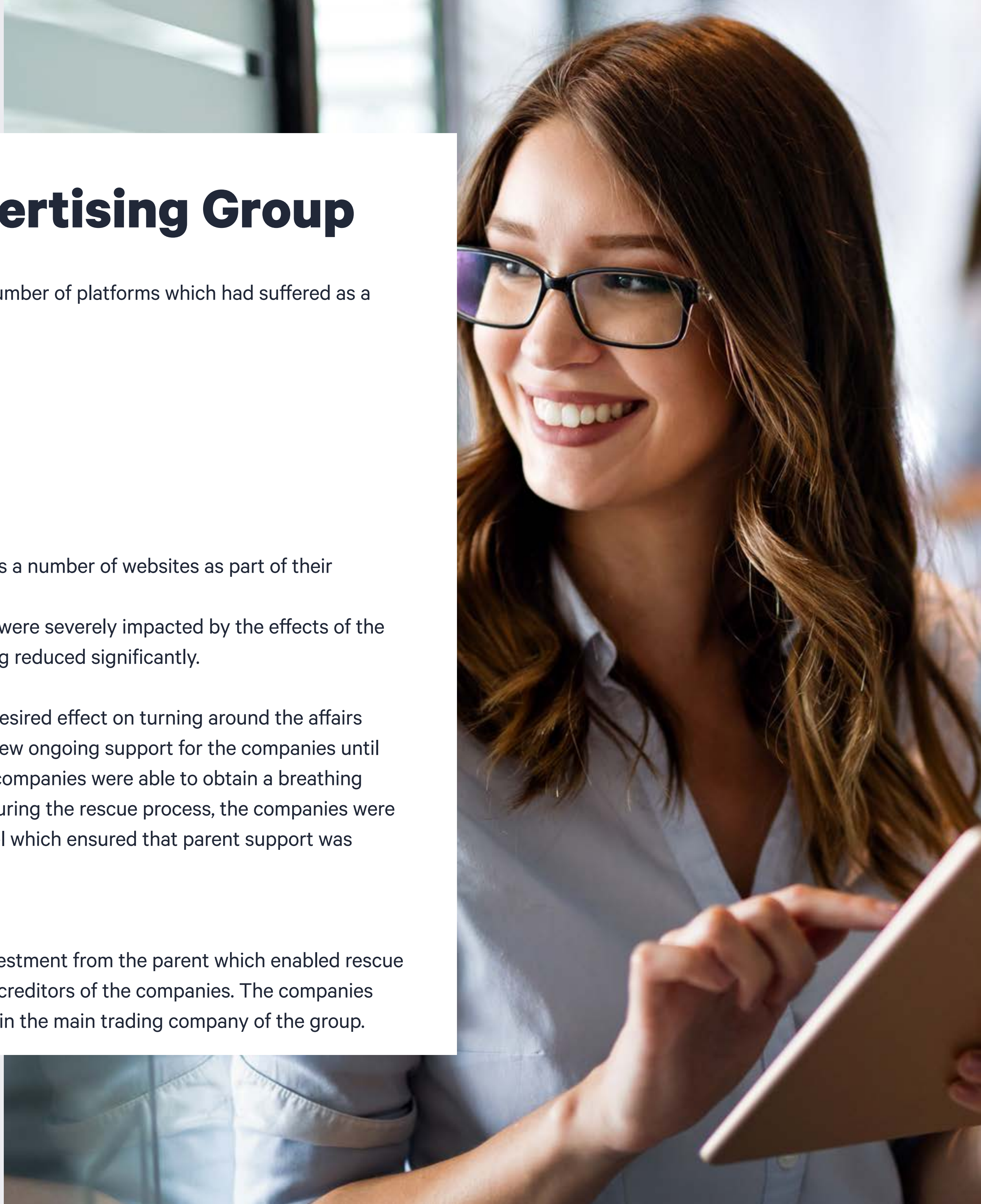
Background

The companies own and operate a number of online publications across a number of websites as part of their operation.
Similar to operators right across the advertising sector, the companies were severely impacted by the effects of the pandemic whereby discretionary spending by businesses on advertising reduced significantly.

Overhead reductions and scaling back of operations did not have the desired effect on turning around the affairs of the companies. In addition, at this time, the companies parent withdrew ongoing support for the companies until changes were implemented in terms of its future business model. The companies were able to obtain a breathing space fromcreditors as part of the appointment of a process adviser. During the rescue process, the companies were also in a position to implement changes in terms oftheir business model which ensured that parent support was forthcoming to fund a rescue plan.

Result

Diarmaid Guthrie of Azets Ireland was successful in obtaining fresh investment from the parent which enabled rescue plans be formulated. The rescue plans enjoyed strong support from all creditors of the companies. The companies successfully exited SCARP in January 2023 with 11 jobs being retained in the main trading company of the group.



Case Study 2: Public Relations Services – Digital Advertising

The business of the company is the creation and provision of digital marketing platforms to SMEs with a primary focus on multi-venue retailers.

The issues faced by the Company were:

1. The ongoing impact of the Covid-19 pandemic and reduction in turnover;
2. Failure to secure adequate funding;
3. Loss making revenue streams;
4. Cash flow pressures being faced as a result of the above issues.

Background

The company was founded as a social media services company offering support to SMEs. Its initial customer base was primarily in the hospitality sector. As a result of Covid 19, the company's customer base was significantly impacted, and the company took the decision to focus on offering its social media services to the grocery sector. The company identified that investment was required in order to fund current operations and develop the business further. Initial tranches of funding were raised; however, the overall sum raised was insufficient to meet current and future needs. As the business was coming under increasing cash flow pressures as a result of Covid 19 and the inability to raise new funding, the directors sought the appointment of a process adviser to restructure the affairs of the company.

Result

Conor Noone of Azets Ireland was appointed as process adviser in November 2022. The process adviser was successful in securing fresh investment in the company to allow for a rescue plan to be prepared. Loss-making revenue streams were identified and these lines of businesses were discontinued during the period of SCARP. The company was successful in pivoting to focussing on more profitable business streams.

The successful implementation of the rescue plan secured the future of 6 employees. The company successfully exited SCARP in January 2023.

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