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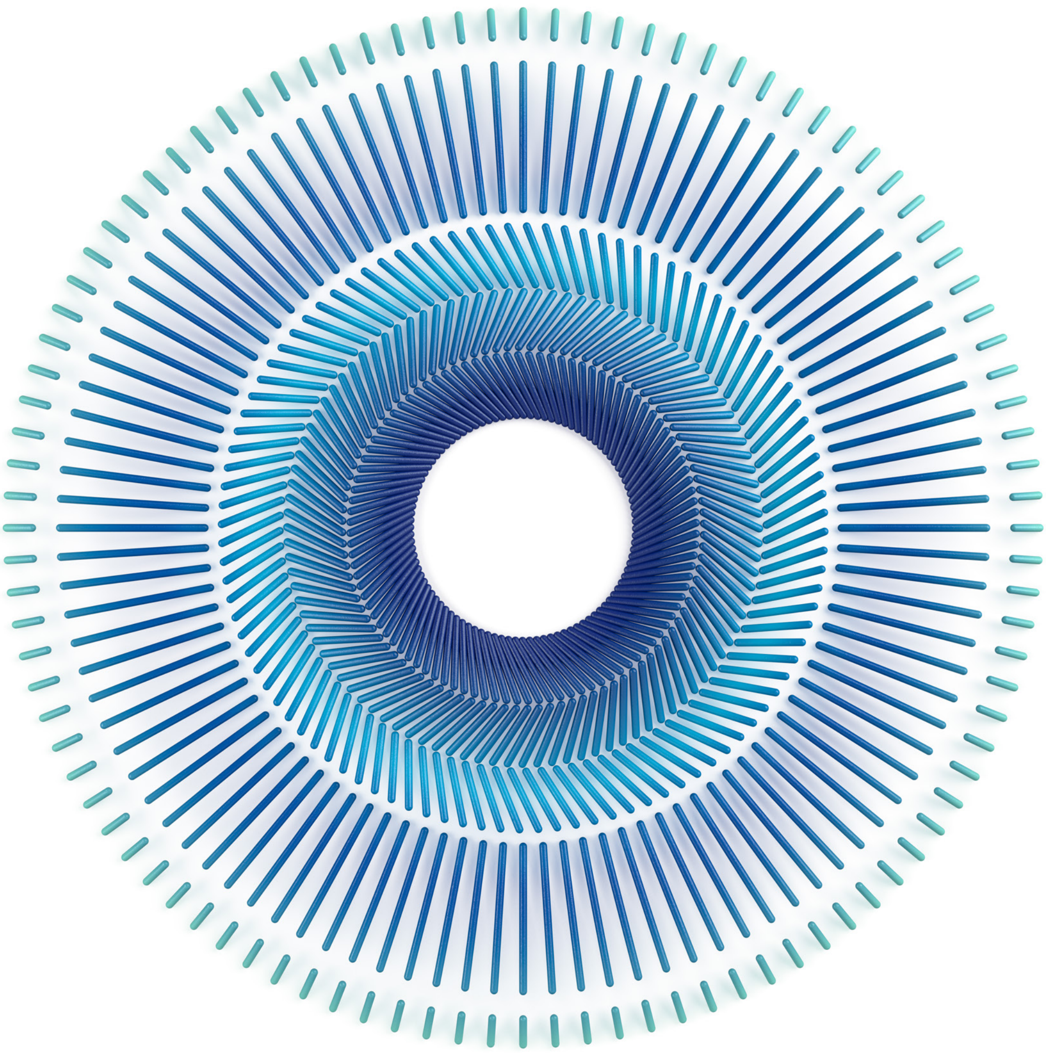

The Small Company Administrative Rescue Process (SCARP)

Accessible restructuring for small and micro companies

What is SCARP?

On 25th June 2021, the Companies (Rescue Process for Small and Micro Companies) Bill 2021 was published. The Bill follows the publication of the proposals for the Small Company Administrative Rescue Process (SCARP) on 25th May 2021, public submissions in March 2021 and a report by the Company Law Review Group in October 2020.

The proposed SCARP legislation aims to provide a more accessible and cost-effective restructuring process for smaller companies. SCARP is largely modelled on existing Examinership legislation with some elements of personal insolvency legislation. In June 2015, the Circuit court introduced Examinerships hoping that this would make the process more accessible and cost effective for smaller companies. But it has not had the desired effect. Whilst Examinership is a flexible and well-travelled restructuring process for larger companies, it has not been accessible for many smaller companies largely due to the costs involved in the process.

The impact of Covid on smaller companies (retail, hospitality, leisure and the services sectors in particular) has further exacerbated the need for a more cost-effective corporate restructuring process.

The SCARP Bill has now passed all stages of the legislative process and is expected to be enacted shortly.

What does this mean for the industry?

COVID-19 has disproportionately affected the hospitability, leisure, service and retail sectors. These sectors have been heavily reliant on government supports, creditor forbearance and debt warehousing. As of May 2021, the Revenue Commissioners estimate that almost 86,000 Irish businesses are availing of the tax warehousing scheme with an aggregate tax debt of €2.3 billon. It is estimated that almost 80% of companies in these sectors are small companies and as the economy reopens its vital that support is available. The recent announcements of further banks exiting the Irish market will also present funding challenges to SMEs. A cost-effective restructuring process is vital for the survival of viable smaller companies.

Although the current level of insolvencies are relatively low (our H1 corporate insolvency statistics show a 38% decrease in the number of insolvencies compared to the same period in 2020) it is worth noting that once the Global Financial Crisis began in December 2007, it took over 3 years for this to peak in Ireland in terms of formal corporate insolvency activity. The introduction of SCARP should assist viable companies in completing restructurings in a timely manner.

Whilst SCARP, mirroring the examinership process is a sensible approach, however, it is unclear how creditors with excludable debt will engage. The response from the Department of Enterprise, Trade and Employment to the public consultation in March 2021 alludes to the position of the Revenue Commissioners opting in to circa 90% of personal insolvency cases and is expecting a similar pragmatic approach for viable companies availing of the SCARP process.

In addition, the requirement to report on the historical conduct of Directors to the ODCE after completion of a SCARP process is another departure from examinership. It remains unclear how this will play out if issues of irresponsible and reckless behaviour by Directors arise. To ensure its success, it's important that this reporting requirement does not act as a deterrent to directors and companies engaging in the process.

Key Features of SCARP:

01. The SCARP process is **only available to Small and Micro companies** who meet two of the following criteria;
    A. Turnover less than €12M.
    B. Balance Sheet total less than €6M.
    C. Less than 50 employees.
02. The SCARP process will commence following the passing of a resolution of the directors of the company, as opposed to the presentation of a petition before the court, as is required in Examinership.
03. The process is led by a qualified insolvency practitioner who is appointed as the "Process Advisor" and who is tasked with formulating a rescue plan for agreement with creditors.
04. The process will have a **70-day timeline from commencement** - 49 days for creditors to receive & vote on rescue proposals and a 21-day cooling off period where creditors objections can be raised.
05. Unlike Examinership, there is **no immediate protection from creditor enforcement**, however, protection can be sought after the 'Process Advisor' has been appointed.
06. Cross **class cram down of debts is feasible** in the current draft of the legislation.
07. The majority of creditors required to approve a proposed rescue plan is 60% in number, with a **majority in value**.
08. The process allows for **excludable debt**, which encompasses taxes, duties, levies, and other similar charges payable to the state and debts arising under social welfare entitlements.
09. SCARP does allow for the **repudiation of onerous contracts**, but this will require a court application if it is not voluntarily agreed between the parties to the lease.
10. SCARP places a requirement on the 'Process Advisor' to **report to the 'Office of the Director of Corporate Enforcement' (ODCE)** on the historical conduct of the directors.

SCARP Vs Examinership

	SCARP	Examinership
Company size restriction	Small or Micro company only	None
Entry to Process	Passing of resolution by Directors to appoint Process Advisor	Petition presented to the court accompanied by Independent Experts Report
Day to day control of company during process	Directors of the company	Directors of the company
Immediate protection from creditors	No – Requires a court application	Immediate protection from creditors / enforcement
Timeframe to present rescue plan to creditors for approval	49 days	Up to 99 days pre Covid & presently up to 149 days under current temporary legislation
Approval threshold for rescue plan	60% in number with a majority in value of creditors represented of at least one class of impaired creditors	Majority in number & value of creditors represented of at least one class of impaired creditors
Repudiation of onerous contracts	Yes	Yes
Excludable creditors	Yes	No

SCARP Timeline

Day 0	**Prior to appointment of Process Advisor**	Company and Process Advisor engagement - directors prepare statement of affairs and Process Advisor completes report if the company is suitable and has a reasonable prospect of survival
Day 1-28	**Directors pass resolution appointing Process Advisor**	Process Advisor commences preparation of rescue plan for the company
Day 35	**Notification to creditors of excludable debt**	Process Advisor to notify any creditor of executable debt whether they are to be compromised under the rescue plan
Day 42	**Calling of meetings of members and creditors to approve rescue plan**	Process advisor calls meetings of members and creditors to approve the rescue plan – 7-day notice requirement
Day 49	**Meetings of members and creditors to approve rescue plan held**	Rescue plan approved is required to be voted for by one class of impaired creditor and cannot be unequitable or unfairly prejudicial on any class of creditor
Day 50-70	**Cooling off period / confirmation hearing**	Rescue plan will become binding if approved and there are no objections from creditors on the proposals. If there are objections, the court will consider the plan and approve unless its unequitable or unfairly prejudicial

Engaging with SCARP

Acting early in times of distress affords businesses more rescue options. Given the underlying liquidity challenges arising from the COVID-19 pandemic, carefully assessing the available options and engaging with stakeholders can allow a business to navigate through this unprecedented volatility.

For any companies potentially considering a SCARP process in the future, the following steps should be considered:

- Minimise the risk of the Revenue Commissioners not engaging in the SCARP process, by ensuring all tax returns are filed up to date, even where the liability is not currently being paid.
- Keep your creditors 'on board', including secured creditors, by keeping them informed, as you will need their support to achieve a successful SCARP.
- Maintain proper books of account and regularly review the financial performance of the company by preparing Management Accounts on a regular basis.
- Maintain accurate notes of meetings of Directors to demonstrate due care and attention for the financial position of the company.

Deloitte's restructuring advisory team in Ireland, supported by our wider Financial Advisory services (including tax, risk and accounting advisory teams), is best placed to advise clients in navigating the current environment. We have already advised a number of businesses in seeking available options and have provided support to clients in navigating the current volatility in the market. Reach out to us at the earliest opportunity to ensure you have sufficient time to plan and implement a robust recovery strategy.

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