Creditor Compromises and Business Debt Hibernation

COVID-19 has created unprecedented challenges for New Zealand businesses, impacting on their ability to meet historic obligations while presenting the need to reshape operations to address the change in the economic climate.

Companies facing liquidity and working capital constraints or struggling to make payments to key creditors and suppliers will need to consider the options available to manage their liabilities.

Creditor compromise legislation and the new COVID-19 Business Debt Hibernation scheme provide businesses with two routes to engage with creditors and seek a binding agreement on debt deferral or reduction, giving the space and financial flexibility needed to trade towards recovery.

Selecting the appropriate option

Businesses should review the options available and carefully consider the relative pros, cons and likely outcomes of a compromise or debt hibernation procedure for themselves and their stakeholders. A high level summary of the two processes is included below.

Creditor Compromise

- Formal arrangement made between a company and its creditors under Part 14 of the Companies Act 1993.
- Arrangement to either pay creditors less than the full amount owing, or pay the balance over an extended period.
- Proposal voted on by creditors, with a 75% majority by value and 50% by number required for each creditor class.
- Decision of the majority becomes legally binding for all creditors.
- Typically lower costs and an improved return to creditors versus other forms of external arrangements.

COVID-19 Business Debt Hibernation

- Temporary regime to give businesses more time to pay creditors which have arisen as a result of COVID-19.
- Existing debts can be placed into hibernation for up to 7 months but there is no reduction in the quantum of debt.
- Businesses must have been viable prior to COVID-19 and meet other eligibility criteria in order to enact the debt hibernation process.
- The effect of hibernation is that creditors are prevented from taking steps to enforce payment of their debt during the hibernation period (subject to certain exclusions).
- A 50% majority vote by number and value is required to pass the proposal.

Potential challenges

Based on our experience of helping businesses of all sizes navigate financial distress, Directors and management teams are likely to face the following challenges:

- Building trust with creditors to secure the critical votes to pass a compromise or debt hibernation proposal;
- Securing the support of key lenders to underpin the process;
- Accurately assessing working capital requirements to support the business through a deferral period;
- Building a compelling recovery plan with avenues for future realisations;
- Balancing communication and reporting requirements with operational and financial pressures.

How we can support your business

We can help maximise the chance of success of your proposal by:

- Performing an assessment of the alternative outcomes to help determine the most appropriate course of action;
- Developing an action plan to guide you through the legal and practical requirements;
- Acting as compromise administrator to provide independent oversight and management of the formal compromise process;
- Managing creditor and other stakeholder communications, freeing up management time to focus on critical operational matters;
- Leveraging our significant restructuring experience and access to deep sector expertise to provide input into the recovery planning and implementation processes.

Contact us

PwC's Restructuring team has over 25 dedicated professional service staff located nationwide across our Auckland, Hamilton, Napier, Wellington and Christchurch offices. The team includes 10 partners and directors with extensive experience in helping businesses prepare for, respond to, and emerge stronger from crises.

Please get in touch if you would like a further discussion.

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