

### 56.1 A drill on some consequences of insolvency

A firm is insolvent with net liabilities, as shown in the statement below.

		£	£
ASSETS			1 200
LIABILITIES			
Creditors:	A	900	
	B	700	
	C	400	
			<u>(2 000)</u>
NET LIABILITIES			<u>£(800)</u>

Determine how much will be received by each creditor under each of the following assumptions:

**1.**

If all creditors are unsecured and rank equally for payment.

#### Response

The £1 200 of assets will be shared between the creditors in proportion to their claims, and

$$\begin{aligned}
 \text{A will get } & \text{£1 200} \times \frac{900}{2\,000} = \text{£540} \\
 \text{B will get } & \text{£1 200} \times \frac{700}{2\,000} = \text{£420} \\
 \text{C will get } & \text{£1 200} \times \frac{400}{2\,000} = \text{£240} \\
 & \underline{\underline{\text{£1 200}}}
 \end{aligned}$$

**2.**

If the liability to A is secured on an asset which is disposed of for £900 or more, and all other creditors are unsecured and rank equally for payment.

**Response**

A will first recover £900 in full from sale of the asset on which the debt was secured. This will leave the firm with £300 of assets, and liabilities as shown below:

		£	£
ASSETS			300
LIABILITIES			
Creditors:	B	700	
	C	<u>400</u>	
			(1 100)
NET LIABILITIES			<u><u>£(800)</u></u>

The remaining £300 of assets will then be shared between B and C in proportion to their claims. In summary:

<b>A will get</b>		<b>£900</b>
<b>B will get</b>	$£ 300 \times \frac{700}{1\ 100} =$	<b>£191</b>
<b>C will get</b>	$£ 300 \times \frac{400}{1\ 100} =$	<b>£109</b>
		<u><u>£1 200</u></u>

**3.**

If the liability to A is secured on an asset which is disposed of for £500, and all other creditors are unsecured and rank equally for payment.

**Response**

A will first recover £500 from sale of the asset on which the debt was secured. This will leave A with a remaining claim of £400. The firm will have £700 of assets, and liabilities as shown below:

		£	£
ASSETS			700
LIABILITIES			
Creditors:	A	400	
	B	700	
	C	400	
		<u>1 500</u>	(1 500)
NET LIABILITIES			<u><u>£(800)</u></u>

The remaining £700 of assets will then be shared between A, B and C in proportion to their outstanding claims. In summary:

<b>A will first get</b>	<b>£500</b>
<i>subsequently</i>	
<b>A will get</b> £ 700 $\times \frac{400}{1\ 500}$	<b>£187</b>
<b>total for A</b>	<b>£687</b>
<b>B will get</b> £ 700 $\times \frac{700}{1\ 500} =$	<b>£327</b>
<b>C will get</b> £ 700 $\times \frac{400}{1\ 500} =$	<b>£187</b>
	<b><u><u>£1 200</u></u></b>

**4.**

If the liability to A is secured on an asset which is disposed of for £400, and the liability to B is secured on an asset which is sold for £600, while the liability to C is unsecured.

**Response**

A will first recover £400 from sale of the asset on which his debt was secured. This will leave A with a remaining claim of £500.

B will recover £600 from sale of the asset on which her debt was secured. This will leave B with a remaining claim of £100.

The firm will then have £200 of assets remaining, and liabilities as shown below:

		£	£
ASSETS			200
LIABILITIES			
Creditors:	A	500	
	B	100	
	C	400	
			(1 000)
NET LIABILITIES			<u>£(800)</u>

The remaining £200 of assets will then be shared between A, B and C in proportion to their outstanding claims. In summary:

			total for A	total for B	total for C
<i>First:</i>					
<b>A will get</b>		<b>£400</b>	<b>£400</b>		
<b>B will get</b>		<b>£600</b>		<b>£600</b>	
<i>subsequently</i>					
<b>A will get</b>	$£ 200 \times \frac{500}{1\,000}$	<b>£100</b>	<b>£100</b>		
<b>B will get</b>	$£ 200 \times \frac{100}{1\,000} =$	<b>£20</b>		<b>£20</b>	
<b>C will get</b>	$£ 200 \times \frac{400}{1\,000} =$	<b>£80</b>			<b>£80</b>
		<u><b>£1 200</b></u>	<u><b>£ 500</b></u>	<u><b>£ 620</b></u>	<u><b>£ 80</b></u>