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I

INTRODUCTION – TURNAROUND TO SUCCESS

BANK OF SCOTLAND

Gareth Oakley, *Managing Director, Business Banking*

Businesses are emerging from one of the most challenging periods in history. The combination of a rapidly evolving technological landscape, changing customer demands and, of course, Brexit and the COVID-19 pandemic is sure to have long-lasting effects on many businesses. There are also a number of factors which could lead to a business needing a turnaround regardless of the economic backdrop, including an unexpected shock to the company or overtrading.

However, while a turnaround is no doubt a challenging experience, the process can also bring significant opportunities for businesses to pivot, adapt and find their place in the new economy. Whether that's by embracing digitisation and Industry 4.0, focusing on going green or introducing more agile working practices to suit the modern workforce.

Over the course of this book, we'll guide you through the process of undergoing a business turnaround. We'll cover everything from how to stabilise your business, build stakeholder support and determine the right restructuring options, right through to rebuilding your team and positioning yourself for growth and building resilience. It combines expertise from Bank of Scotland, with key insights from supporting contributors and practical steps to help you manage the turnaround process and beyond.

We hope it will be a valuable tool as you navigate the coming months and further into the future. We know it's been a challenging time, and we want to play our part in helping Britain recover by supporting as many businesses as possible to find their place and thrive in the new economy. We believe in business, and we believe in the UK.

Gareth Oakley

1

TURNAROUND TO SUCCESS

POTTINGER

Nigel Lake, *Founder and Executive Chair*

Almost every business – and almost every business leader – will eventually face a crisis. Sometimes turbulence appears rapidly, due to uncontrollable external events such as the global pandemic or internal failures. More often, social and technological change drive creeping shifts in the commercial and competitive landscape that place companies under progressively greater pressure. Either way, both trigger the need for an urgent response and may even imply a risk of impending insolvency.

Disruption and opportunity are, however, frequent travelling companions. For the well-prepared, well-resourced or just plain nimble organisation, external turmoil and internal disruption can set the stage for dramatic shifts in market position. To achieve long-term success, every business and every leader must navigate uncertainty, whether in the form of short-term challenges or longer-term market shifts. The stronger your business and the better your leadership, the more you will be able to make headway in stormy weather.

Whatever the cause, preparation and informed decision-making can help transform crisis into commercial opportunity. This book provides perspectives and tools to help you thrive in an uncertain world, looking across the full spectrum of issues that you will face. The insights we have gathered from business leaders and professional advisors provide both practical guidance as to what to do and inspiration to act early and decisively.

My own first experience of an overnight crisis came near the start of my career, working in the corporate finance team at Barings in London. At the time, we were in the thick of advising on one of the largest public take-over bids ever announced in the UK – very much business as usual for what was then the leading mergers and acquisitions house in Europe. From learning that there may be some issues in Barings' international equities division to administrators being appointed to the entire business took barely 48 hours. Yet, through effective leadership and remaining firmly focused on our clients, we ended that year with the corporate finance business entirely intact under new ownership and top of the league tables for a second consecutive year.

Since then, I've advised companies, financial institutions, governments, entrepreneurs and social enterprises of all shapes and sizes through times of crisis, in dozens of countries around the world. Though the circumstances, commercial dynamics, people and cultures have varied dramatically, the same underlying themes come up time and time again, and they are embodied in the chapters in this book. We've divided the material into two parts, reflecting the natural priority to stabilise the business first and then to seek opportunity for growth.

STABILISATION

Before all else, you must act to give the business the best possible chance of surviving the storm. In doing so, whether the crisis emerges rapidly or is the result of a long period of incremental change, it's essential to be grittily realistic about the problems that you are facing, whilst keeping in mind the potential for new opportunities to be lurking just around the corner.

- First, you must grasp the situation quickly. This means confronting the challenge you face in the most complete and holistic way possible in the available time. You will need to make tough decisions quickly, so you'll also need clarity about the order in which to deal with problems and the implications that this will have for stabilising operations, conserving cash and maximising your ability to make the most of opportunities that may follow. Beware of simply slashing costs to the bone as you may be left with nothing on which to rebuild. In 'Change Becomes the Norm', we reflect briefly on the turbulent environment that small and medium businesses have had to navigate over the last decade, explore what turnaround means and the types of support that are available to support you.
- Very early on, you must devote serious thought and energy to 'Crisis Communications and Building Stakeholder Support'. No matter how good your understanding of the challenges that you face and your plan to address them, to deliver an effective response you will need a strong, motivated and aligned team alongside you. More broadly, although the environment will likely be stressful for you, and perhaps for your stakeholders, there is also a significant opportunity to deepen your relationships through this period. Honesty and transparency will help to build trust, but you must take care not to trigger a crisis of confidence in the future of the business. And though we mention this topic early in the book, remember that effective communication will be critical throughout the stabilisation phase and beyond.

Before all else, you must act to give the business the best possible chance of surviving the storm.

In tackling the crisis, you will need to live and breathe the financial performance of your business week by week or even day by day. Frequently, this means that you will need new types of reports and forecasts that give you the ability to manage financial resources much more tightly than in normal times. A strong CFO who provides you with reliable information efficiently and objectively is invaluable as this helps to create a calm space in which to think and act. Once again, there are various steps that are common to almost every situation.

- First, urgent 'Financial Stabilisation and Risk Reduction' measures are likely to be required. This means evaluating the financial implications of the current situation, understanding the underlying issues and engaging with lenders and creditors at an early stage so that they know you are in control of the situation. This will maximise the chances of avoiding administration or insolvency.
- Building on this, you will need to identify and prioritise the 'Financial Restructuring Options' that are available to you, including debt restructuring, raising new equity, government support packages and even selling the business (as occurred with Barings). We provide a simple overview of some of the issues and options that you may wish to consider.
- Often, a turnaround will involve working with external advisors. We provide 'A Turnaround Practitioner's View' so that you can get a feeling for how they approach the challenge. Whether you're a director, manager in the business or external consultant, you should think about the longer-term implications of every decision so that you lay the right foundations for growth.
- No matter how hard you work to address your short-term challenges, longer-term

success will always be driven by people. This means that you need to think from the outset about what steps you will take to '(Re)Build a Winning Team'. If the crisis is purely financial, then you may well already have exactly who you need, and your primary goal will be to figure out how best to support and retain them in the near term. Alternatively, if your business needs significant reshaping, you will need to assemble the best possible mix of skills, hustle and vision so that you can make decisions quickly and effectively and restore confidence in the business. Either way, remember that the best thing a captain can do when facing a storm is to make sure that the crew are safe below deck, well-fed and focused on addressing critical tasks.

- In parallel, legal elements and processes can become critical, so you must understand your 'Directors' Duties in a Financial Crisis' and ensure not only that you are making the best commercial decisions possible but also that you are doing this in a manner that is responsible from a legal perspective in order to avoid creating new risks for both your board and the wider business.
- You should also consider the various issues related to 'Navigating Corporate Insolvency', including restructuring, administration and liquidation. This is a complex area where specialist advice will be essential. Importantly, as every company director should be well aware, in the face of crisis, your risk comes not from the unattractive cards that you may have been dealt but rather from how you respond to the situation.
- Lastly, entering administration may provide the best pathway to protect the interests of all stakeholders and preserve the maximum possible value from the business. Thus 'Understanding Insolvency Laws and Procedures' in advance of getting caught up in such a situation is valuable.

GROWTH

Though stability may make for business security, change frequently creates significant commercial opportunity. So whatever the root cause of the challenges you currently face, it's also important to look beyond the immediate crisis and seek out opportunities to build and strengthen your business. Humans naturally become more inventive and adaptive during times of crisis, so the very environment that may be threatening your company can also be the crucible from which significant new business opportunities can be forged.

As many companies have experienced, the global pandemic has led to profound changes in both consumer behaviour and working practices in many countries and industries. Perhaps the most significant of all is the wholesale adoption of video communication and the wave of international collaboration and flexible working that has emerged as people and companies have discovered that they can work effectively together across time zones and locations. This shift is creating spectacular new opportunities to hire great new employees or to win new customers in locations that might have been unthinkable a couple of years ago.

Humans naturally become more inventive and adaptive during times of crisis, so the very environment that may be threatening your company can also be the crucible from which significant new business opportunities can be forged.

Though these trends were already under way, they have been accelerated by perhaps as much as a decade, changing the game for many people and businesses. Take a moment to reflect on the ways the world in which we live and work are evolving profoundly.

- The entire energy value chain, from where and how we generate power to the cars that we drive and the trucks that deliver goods, is transitioning from fossil fuels to renewable solutions. This is reshaping energy markets, power grids and even the role of the domestic automobile. Over US$500 billion per year is now being invested in this shift as business

and society unite to tackle the rapidly growing effects of climate change.

- Technology is displacing millions of management, administrative and clerical jobs as we see machines extend their capabilities from the automation of manufacturing to the automation of decision-making. Over a few decades, a significant proportion of employment will shift from the tertiary sector of the economy to a new quaternary sector. This comprises all activities with an intrinsic need for human interaction, including caring, creativity, collaboration, communication and culture. These shifts will have a profound impact on the workforce and society more broadly, and both governments and companies will face growing pressures to focus on the importance of creating well-paid jobs.
- Consumers are demanding action on ecological sustainability. Humans – and the animals we are breeding for food – now account for 96 per cent of the bodyweight of all mammals on the planet. Pets and wild mammals account for just 4 per cent. Meanwhile, demand for meat is growing rapidly as wealth increases, especially across Asia, placing ever greater strain on our agricultural supply chains. Unsurprisingly, we are seeing an explosion of interest in plant-based diets and animal-free meats, fish and cheese. Looking ahead, by 2025, our oceans will contain one tonne of plastic for every three tonnes of fish. Widespread calls to reduce both waste and limit environmental pollution are welcome and important.

> Conversely, if you focus solely on efficiency and eliminate all human interaction, you may find yourself in a race to the bottom on costs and little else to differentiate yourself from your competitors.

These industrial and philosophical shifts are affecting almost every industry and every business, contributing significantly to the accelerating pace of change. As a result, it is important for every business leader to cut through the hype and understand where and how these forces are operating and how to make the most of the opportunities that they will create.

- New technologies are enabling new business models and new approaches to supply chains that can transform the profitability of businesses and the prosperity of entire communities. In 'Thriving in the New Economy', we provide a down-to-earth explanation of what is really meant by buzzwords such as industry 4.0, the internet of things and the circular economy, and how these can create significant new opportunities.
- As always in business and in life, 'Building Financial Resilience' is of paramount importance. This means thinking about every aspect of your business and how you manage it so that you understand where upside and downside risks lie and how you plan ahead so that you are best placed to make the most of the opportunities and to act quickly to neutralise the threats.
- ESG has become a hot button issue for many companies and investors, so 'Making Sustainability Work for Your Business' is more important than ever. This includes action on climate change and environmental degradation, as well as issues related to diversity, equity and economic inclusion. With the right approach, you will find that action on ESG can be synonymous with improving business efficiency, stakeholder relationships and growth (ESG by another name) and can both reduce risk and make your business more resilient.
- Meanwhile, new technologies enable increased efficiency in many areas of business, which means exploring opportunities for 'Transforming Your Business through Digitalisation'. In doing so, consider how you can use automation to humanise your business, both through greater personalisation as well as through more extensive human interaction. This will

build customer appreciation and loyalty – and create valuable new jobs to boot. Conversely, if you focus solely on efficiency and eliminate all human interaction, you may find yourself in a race to the bottom on costs and little else to differentiate yourself from your competitors.

- With all of the above unfolding, you may also find opportunities in new business models and, in particular, 'Partnering for Growth'. Many of the most successful startups over the last decade have entailed a collaborative approach, either in the nature of the product itself or in how that product is delivered to customers. The fundamental point is that with greater flexibility and connectivity than ever before, significant value can be unlocked through the right type of collaboration with the right partners.

On a personal note, I can vouch for the effectiveness of these recommendations. As the COVID-19 outbreak began to expand beyond China, we were able to shift our entire business to working from home overnight, thanks in part to a disaster plan that contemplated the total loss of access to entire city centres. Within a couple of weeks, we had engaged with all our key stakeholders and shifted some relationships to reflect the new environment whilst retaining all our employees and providing certainty of ongoing income to our suppliers. Our teams were thus able to focus on delivering for our clients and taking care of their own communities, too.

In saying this, I know we were also lucky in that professional services have been much more adaptable than businesses that depend on physical premises, so we went out of our way to provide pro bono support to others wherever we could, building some wonderful new relationships along the way. We also looked for ways to address the effects of isolation, helping to launch ESGX.org, a non-profit online sustainability community that has since featured contributions by the likes of environmentalist Dr Jane Goodall, New York Times best-selling author Dr Stephanie Kelton and many others.

As the last year has unfolded, we have seen many of the themes described in the various chapters first hand, both in our own business and through the eyes of our clients around the world. Most powerful of all have been the new collaborations that have emerged across borders and across industries, helping to create new products and services, launch new businesses and support entire communities. We've also seen new multinational startups form and grow rapidly despite the constraints of local lockdowns and travel bans. And on 31 December 2020, Pottinger closed its first '100 per cent remote' M&A transaction, where the vendor, the target business, the various bidders, the eventual purchaser and their respective advisors never met face to face at any point. What might have been unthinkable in 2019 is today's business as usual.

THE PATH TO ACTION

Any strategy and any plan is only as good as its execution, so remember that the ideas and perspectives set out in this book aren't just theory. They are distilled from the real-life experience of both business leaders and professionals across a host of different businesses, and these chapters are packed with pragmatic advice. 'The path to action' may at times feel daunting, but many have undertaken similar journeys before, and there is a wealth of advice and resources available to support you.

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2

CHANGE BECOMES THE NORM

THE INSTITUTE FOR TURNAROUND

Milly Camley, *CEO*

Over the past decade, small and medium businesses have faced intense changes through accelerated market forces such as technological challenges and opportunities, increased costs of doing business and most recently the COVID-19 pandemic.

As we emerge from an extended period of constrained commercial activity, even the most able leadership teams are stressed by unprecedented challenges. Successful businesses have built up debt, depleted working capital and deferred obligations to stakeholders such as landlords, lenders, and government. As the myriad of important government schemes, deferrals and moratoria are withdrawn, there is a crucial window of opportunity for businesses to restructure debt, build up working capital, transform their operational models and cost base, and deliver on a plan for recovery and growth that benefits all stakeholders. For some businesses, turnaround experts can help provide immediate viability and confidence, giving them the space to recover and build for the future.

WHAT DOES TURNAROUND MEAN AND WHEN CAN TURNAROUND EXPERTISE BEST HELP YOUR BUSINESS?

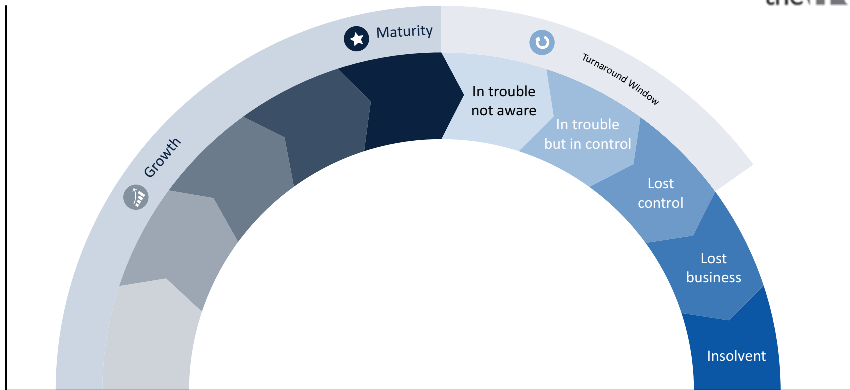
While some business failure is inevitable in a healthy economy, a troubled business can survive and thrive with the right management, financing, strategy and governance. A turnaround process using expert external help can provide the necessary catalyst for change, taking a business from the brink of insolvency through radical change to renewal.

While a cash crisis catapults many firms into turnaround situations that without rapid intervention would result in insolvency, not every business making a turnaround is facing a cash crisis.

Three features define a turnaround business:

1. *Stressed not fatal*: These firms lie on the spectrum from underperformance through to distress.
2. *At risk*: Failure to reverse business decline will lead to failure.
3. *A viable future*: If it can overcome its immediate troubles, the existing offering or potential offering means that the business has a good chance of succeeding in the medium to long term.

FIGURE 1. Corporate health



STRESSED NOT FATAL

The decline curve for a business usually starts with underperformance, progresses to a state of stress, then distress and crisis. Underperforming firms can address their problems through a transformation programme. A company in crisis is usually on the point of insolvency and a workout to reduce losses. Looking at the curve of company health in Figure 1, turnarounds can be effective if they take place between a company first becoming stressed, i.e. while they are having troubles but ultimately remain in control, and distressed, i.e. when they have completely lost control and are at real risk of losing the business. In order to ensure a turnaround has the best chance of success it's important to be aware of the early warning signs that a business is in distress. These can include:

- cash flow problems;
- rising stock levels;
- customers requesting longer payment terms or not paying on time;
- major contracts ending; and
- needing external funding for reasons other than growth or expansion.

AT RISK: CAUSES

EXTERNAL PRESSURES

A crisis can come in many shapes and sizes. Changes in the economic cycle can affect consumer and business sentiment and spending. Black Swan events, such as terrorist attacks, or outbreaks of disease, like COVID-19 that spread worldwide in 2020/2021, can dramatically reduce demand, as can a product recall, factory fire or litigation.

Competitor innovations can disrupt whole industries seemingly in short order, as demonstrated by recent technological changes such as online selling and streamed entertainment. Regulatory or government policy can also fundamentally shape the operating environment.

INTERNAL FACTORS

Many internal factors leading to decline are within the firm's control. People, governance, financial or strategic challenges can constrain and even severely disrupt a business.

- *People challenges* can include: shortages of skills and management failures, leaving the business poorly placed to respond to a changing market environment.
- *Governance challenges* like inadequate, undocumented, misunderstood or even overly bureaucratic control procedures can hamper success.
- *Strategic challenges,* including a lack of clear strategy, over-diversification, growing too fast and poorly judged acquisitions, can place undue pressure on a business.

- *Financial challenges,* from a lack of cash, inadequate capital, high debt and expensive financing to insufficient management information and poor budgetary controls are common problems.

A VIABLE BUSINESS

A business must be capable of being resuscitated to be turned around – that means ultimately there must be a profitable market for its goods or services. If the finances are stable or have been fixed through a turnaround process, *operational turnaround* provides a means of adapting the operating model to make a viable product or service profitable in the marketplace.

WHAT TYPICALLY HAPPENS DURING A BUSINESS TURNAROUND?

The typical turnaround stages are outlined in Figure 2. The first three stages hinge upon intensive fact-gathering and the art of creating breathing space, whilst the latter stages provide a platform for sustainable success.

STEP ONE: DIAGNOSE THE PROBLEM

The first step in a turnaround is identifying and prioritising the key issues to be tackled and formulating a short-term plan to address them. Typically, this is a very rapid process using

FIGURE 2. Typical turnaround stages

financial information and the knowledge of the business and its stakeholders.

Once there is a full understanding of what challenges the business is facing, it will be clearer whether a turnaround is viable. Turnaround experts can help identify the underlying value in a business and take steps to ensure conditions are right for that value to emerge.

STEP TWO: MAKING AN ACTION PLAN

Once it has been determined a business is viable and what the underlying issues are, it's time to formulate an action plan for the turnaround, i.e. what needs to change, what should continue and what new activities need to be started. At this stage a SWOT analysis can be helpful. Identifying Strengths, Weaknesses, Opportunities, and Threats can help determine areas of focus.

It's recommended to set a clear timeline for the turnround. Speed is critical and if everyone knows what needs to be done by when, it can give a business the best chance of success and avoid wasting time on unimportant details.

It's also important to allocate clear roles and responsibilities within the turnaround and have someone ensuring people are completing the tasks assigned to them. It can be all too easy for people to drift to more enjoyable jobs and neglect some of the difficult duties required during a turnaround.

STEP THREE: BUILD STAKEHOLDER CONFIDENCE

After a crisis, when trust levels between a company and its stakeholders are at an all-time low,[1] identifying key stakeholders and managing their expectations is a key aspect of a turnaround director's role. This has become a greater challenge in recent years as the sources of company funding include not only traditional commercial banks, but also newer commercial lenders, private equity, venture capital, and debt funds: the stakeholders are much more diverse.

Customers, suppliers and employees are key stakeholders, and it is important to balance their needs and manage conflicts, but it can be difficult. Engaging with people on the 'shop floor' is as important as working with the top manager because it provides a different and valuable point of view – and their buy-in and commitment will be crucial to turnaround success.

All of this requires financial, situational and soft skills that enable effective collaboration.

> Engaging with people on the 'shop floor' is as important as working with the top manager because it provides a different and valuable point of view – and their buy-in and commitment will be crucial to turnaround success.

STEP FOUR: STABILISE THE FINANCES: CASH FLOW, DEBT AND CAPITAL

Running out of cash is often a trigger point with additional debt, obligations and capital requirements. As we emerge from the pandemic, businesses may be experiencing this challenge for the first time. While fixing the capital structure will not turn the business around by itself, it will provide time and liquidity to effect operational changes.

Measures may include:

- accelerating the collection of cash – often, not collecting cash has been an ongoing issue for the business;
- restructuring debt;
- reducing costs; and
- rationalisation of business acquisitions – putting cash in the bank or reducing losses.

Equipped with the experience of managing lenders and equity providers in stressed situations, turnaround experts can quickly manage stakeholders, source finance and reduce financial pressures.

STEP FIVE: ORGANISATIONAL RENEWAL

Change at the top is not always required. Some of the most satisfying turnaround assignments

are those that enable an existing management team to carry out the necessary business renewal themselves.

Another pressing challenge is being able to motivate the people of the organisation from top to bottom. The turnaround process can deliver long-term benefits by identifying the 'hidden heroes' in a business, providing new situational skills and helping leaders and staff to create positive change.

Redundancies are sadly inevitable in some turnarounds but are by no means the norm. Nearly two thirds of IFT respondents had not made any redundancies in their last assignment. When they are necessary, they must be handled with sensitivity and humanity – redundancy is always personal.

STEP SIX: ARTICULATE A STRATEGY FOR GROWTH

For a turnaround to take place, a strategy for growth needs to be put in place before the turnaround director exits.[2] That means finding a way to do things better, cheaper, or differently than competitors and having a vision that can be turned into a long-term recovery plan.

It may also require reshaping a business to remove elements that are not sustainable. Most importantly, turnaround provides a platform for sustainable business, so it is the best time to get a sustainable strategy, structure and plan in place.

STEP SEVEN: EXIT FROM TURNAROUND

Turnaround is a time-limited process, not an ongoing state. Once the immediate stresses have been handled and a viable plan is in place, any independent specialists engaged by the business will move on, and it's the responsibility of the directors and senior leadership team to ensure that the agreed new strategy is enacted and be on the lookout for any further potential issues.

We analysed submissions from our annual awards spanning a decade to understand the most common interventions in successful turnarounds, defined as at least two years' successful trading since a company or organisation's low point. We found distinct and sometimes counterintuitive patterns: for example, a lower prevalence of redundancy measures than might be expected. The top three interventions were:

1. cutting costs featured in 66 per cent of successful turnarounds;
2. improvement of governance and controls appeared in 64 per cent; and
3. 63 per cent involved a change in the organisational structure.

Source: IFT analysis of shortlisted award submissions 2010–2019

TURNAROUNDS IN SMEs

SMEs are vulnerable to the same challenges as bigger businesses – too much debt, internal stresses or a difficult external environment. Working with SMEs brings some specific challenges too, whether it's a longer turnaround period, the need to embody different types of support, or the complex and varying challenges of family businesses. An important part of the service that turnaround professionals provide is a sensitivity to the human dimensions around troubled businesses: a particularly useful skill in an SME context. It helps to be a good listener, and turnaround advisers are effective negotiators who approach each new project with equal measures of honesty and empathy. They work for the firms and alongside the management teams to help to weather tough times, address specific forms of stress and help make businesses better.

Turnaround in SMEs can often be complicated by the fact that many are family businesses. When the personal and professional are entangled, both in terms of management and finances, the stakes can be very high for all concerned.

> SMEs are vulnerable to the same challenges as bigger businesses – too much debt, internal stresses or a difficult external environment.

The dynamics of managing a family turnaround are complex, with the complexity increasing in relation to the number of generations the firm has been in the family. First generation turnarounds tend to be quite straightforward, and third generation or beyond are much more problematic.

Sometimes blood is thicker than water, and the family bonds work in the business's favour. "A family lingerie business lost 60 per cent of its turnover virtually overnight, and faced significant operational, financial and legal problems," recalls John Playfair, IFT Member and a specialist in SME turnaround. "We needed to win every battle… and we did because everyone brought their A game to play, and it was a real team effort. They were lovely people and we saved them from personal bankruptcy."

AN OWNER'S PERSPECTIVE

"My bank introduced me to a turnaround expert who forensically examined our accounts and produced a report detailing where we were haemorrhaging money – and more importantly, why. Working together, we outlined a plan which both gave the bank comfort that we were serious about survival and a set of actions that we would need to work through to try and save the company.

"The whole difficult process took possibly 18-24 months to work through and, being a family-owned business, it was a difficult time as I always felt I was letting my family down. The entire turnaround process was one from which I learnt a lot, both about the financial side of running a company and about me.

"The sense of relief when you get through the other side, everyone gets paid and suppliers want to again trade with you is palpable, but one thing I do know, is that our successful business would not be trading had it not been for the skills, expertise and support of our turnaround partner". Small business owner and MD, Building Company, Playfair Client.

FINDING AN EXPERT

'We wish we had brought you in sooner.' This is a familiar refrain from businesses that have benefitted from a successful turnaround. The earlier that a business starts on a turnaround journey, the greater the likelihood and scale of success. By any measure, the shock of the C-19 pandemic and related business and trading constraints have taken a heavy toll on UK companies. It is a climate that has significantly increased the burden of daily challenges that SMEs face. Some firms may find it beneficial to seek advice from turnaround professionals even if they are not in full-blown distress.

Turnaround specialists are independent, with situational skills adapted to the demands of stressed and distressed businesses, including:

1. an in-depth knowledge of operating in a stressful or distressing situation;
2. the capacity or capability to carry out detailed due diligence on the customer's business, in terms of analysing its commercial relationships and financial structure; and
3. the experience to provide advice on some of the key turnaround options that may be available to the customer, with an understanding of the different stakeholders, processes and options available in a turnaround context.

IFT members are highly experienced business leaders who have a proven track record in resuscitating troubled but viable businesses. To become an IFT member, individuals have been through a rigorous accreditation process to demonstrate their skills and track record.

Members are bound by a code of conduct and therefore work to high professional standards. Their skills deliver outcomes and provide certainty for all stakeholders – owners, investors, lenders, employees and the economy. However, IFT members are not just focused on immediate rescue measures, they are skilled at finding the underlying value in a business and ensuring its sustainability beyond their departure.

Most of our members work alongside management teams in small and mid-market businesses, providing a fixed-term specialist resource to advise, assure and deliver. Engaging accredited expertise is an investment for your business. They need not be a full-time appointment – many operate on a part-time basis as and when needed. A good turnaround professional will more than cover their cost over a relatively short period.

We can connect businesses to the right specialist in terms of specific business needs and the resources required from intensive help to flexible advisory options. Find out more by emailing us at info@the-ift.com, calling us on 0207 947 9515 or visiting our website at www.the-ift.com.

KEY TAKEAWAYS

- Be aware of early warning signs your business is struggling, there's a clear window when businesses can gain the maximum benefit from turnaround support.
- An independent turnaround specialist can help find the underlying value in a business and ensure its sustainability beyond their departure.
- The earlier a business starts on a turnaround journey, the greater the likelihood and scale of success.

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3

CRISIS COMMUNICATIONS AND BUILDING STAKEHOLDER SUPPORT

STICKY

Jamie Wood, *Head of Communications and PR Services*

At some point, every business will run into difficulties that might be made public. The way those difficulties are communicated to stakeholders, customers, suppliers, investors and the general public can have a huge impact, not just when the crisis is happening, but once the business has stabilised and is trying to move forward.

WHEN TO COMMUNICATE

Business crises that have the potential to cause financial loss can take many forms, from product recalls to accidents to loss of investment. Businesses are also vulnerable to reputational threats, perhaps sparked by something said on social media, and this in turn can escalate to a financial threat.

While a business won't need to let the outside world know about every blip, crisis communications need to be brought into play in the case of any significant threat that can have negative consequences if it is not tackled properly and efficiently. In these cases, it is vital that your staff, key stakeholders, investors, partners and wider supply chain understand what your response is to the situation. So, crisis communications are not only to be deployed during a turnaround, but they are also something your business needs to be prepared to use on an ongoing basis during and after its return to health and growth.

PLANNING YOUR CRISIS RESPONSE

When a business is experiencing difficulties, crisis communications must not be done without preparation; this is how mistakes can be made, exacerbating the situation and making it more difficult to encourage support, turn things around and restore confidence in the longer-term.

Every business understands that a crisis can escalate very quickly in a world of social media where even 24-hour news is no longer the fastest source of information. So, the key is making sure the business has a strategy so it can respond and communicate well in a crisis. Businesses will have robust financial plans for Brexit and any challenges that it might create for their supply chain. They will have a growth plan over the next three to five years. In the same way, businesses, whatever their size, need to have a crisis communications plan.

Messages will be aimed at different audiences, but the core message should always be consistent.

IDENTIFY RISKS AND RESPONSIBILITIES

Whoever is responsible for communications in a business – whether that is a dedicated department, a single individual or an outsourced partner – must ensure that the crisis communications plan is in place.

The first step in creating the plan is to carry out an audit to identify business vulnerabilities and risks in the way a business portrays itself externally.

Once these risks have been identified, those responsible for communications need to establish:

- Who needs to be contacted internally and externally in the event of a crisis?
- Who are the key people dealing with areas of vulnerability in the business? Which of them has the experience and ability to respond quickly in a crisis involving these areas?
- Who will talk directly to the media in a crisis? Are they trained to do this?
- Who will create written crisis comms – emails to stakeholders and customers, press releases, social media posts?
- Who will prepare a report for the board if necessary?

PUT A TEAM TOGETHER

Having people operate in silos must be avoided in a crisis. It is essential to make sure that everyone across the business who needs to be involved in communications understands the crisis plan, understands the response and has access to all the messaging that the business is going to put out, whether to traditional media, on social media and to clients and stakeholders. This way, they can act as a team who are brought together especially for this purpose.

It may be that your crisis team involves people across functions who do not work together day-to-day. In a typical business this might be people from communications, legal, and operations functions, for example, to ensure that there is a coordinated response from across the business.

PLAN YOUR MESSAGING

Crucially, the big risk is when crisis messaging is neither consistent nor coherent. What must be avoided, for example, is one response going out on your social media channels and a different response going to mainstream media, clients or investors. Again, to get this right, it is vital to plan ahead.

- *Create holding statements*: Although it is essential to take control of the narrative during a crisis and respond to any questions quickly, you may not initially be in a position to give much detail about what is happening. For this reason, it is important to have holding statements prepared. These will not be sufficient for long, but they will avoid a vacuum and reduce the risk of the situation escalating while you prepare more detailed messaging. Also prepare templates for press releases and social media posts to avoid wasting time thinking about how your messages will be presented.
- *Consider how to speak to different audiences*: Messages will be aimed at different audiences, but the core message should always be consistent. However, you may want to change the emphasis when talking to different audiences – investors may need particular reassurance that a situation is being dealt with, for example.
- *Use language carefully*: Businesses can be tempted to use jargon and technical terms in their communications, but it is vital to remember that the people you are talking to may not be experts in your industry. They also need to be able to understand your messages quickly and feel their questions have been answered; filling communications with

acronyms and jargon can simply raise more questions. Use plain language and make sure the people designated to talk to the media are able to communicate messages in a clear and straightforward way.

- *Be clear and concise*: While a one-paragraph statement will be insufficient in most crisis situations, avoid giving people too much information so that your key messages do not get bogged down by details.
- *Build on messaging*: As a crisis develops, facts change, so it is vital that a first response is not the only response and that you continue to keep people in the loop as the situation progresses. The more information you have, the more you will need to update. This will not only help build trust and support, but it will also avoid information leaking from elsewhere and enabling someone other than your business to lead the narrative.

> If a business fails to put out its own messages in a crisis or doesn't respond to requests for comments from the media, others will fill the silence for them.

CONSIDER MEDIA TRAINING

There are two types of communication likely to be deployed in a crisis: (1) written communication (e.g. press releases, emails to stakeholders and customers, and social media posts) and (2) verbal and visual communication (e.g. appearances on TV and radio).

The people designated to communicate on behalf of your business may be experts in their field but may not have any experience in these types of communication – so, to make sure your messages land, media training is worth considering.

Appearing on camera, as we've all discovered from Zoom and Teams meetings, is not easy and is a skill. To win trust, spokespeople need to make sure they come across as confident, reliable and relatable – and also that they convince viewers they are being transparent.

Unfortunately, while a spokesperson may be an extremely credible interviewee and give entirely the right messages, people may judge them on the way they say things rather than what is being said.

Media training can address this by covering:

- *How to dress*: Certain colours and styles don't render well on television and can give the wrong impression.
- *How to use your voice*: Many of us have verbal tics – for example, saying 'you know' to punctuate sentences. This doesn't matter in ordinary conversation, but a media interview is not an ordinary conversation and tics can distract from the message you are trying to get across.
- *How to stand*: Fidgeting or waving your arms can be distracting.
- *How to look at the camera*: And how to feel as relaxed as you can while you're doing it so you can get your message across confidently.

Traditional media training focuses on media interviews, but copywriting is another skill that comes into play in crisis communications. It is important that communicators can write clearly and have an idea of what the business should sound like in written comms; therefore, training in this area is also something to be considered.

CRISIS COMMS TIPS FOR THE EARLY DAYS

When a crisis comes to a head, or if an incident happens suddenly, do not wait to communicate regardless of whether it's a weekend or outside working hours. Your first communications are crucial, so your team should gather as much information as possible, check that the facts are accurate and get your message out to the people on your list within the first hour of the crisis emerging in the media. This is vital to prevent the narrative spiralling out of your control.

Once that initial response is decided, make sure your spokesperson and those posting on social media understand the key messages and the form of words you're using and that you are using all your business's communications channels to put your messages out.

THE PITFALLS OF NOT HAVING A PLAN

If a business fails to put out its own messages in a crisis or doesn't respond to requests for comments from the media, others will fill the silence for them. Lack of proactive communication and response invites speculation, alienates stakeholders and customers, and may look as if you don't care about your reputation or are simply unable to manage the situation.

> A crisis does not have to be caused by a dramatic incident to attract media attention.

Without word from you, the media will find people who are experts within your field and get their take on what has happened. They will comment on your crisis while your voice is not heard.

Not only does this mean you are not containing the situation, it may also cause a crisis to escalate from something quite low-level that could have been managed if there had been a response plan in place.

UNDERSTANDING THE MEDIA LANDSCAPE

The sheer speed in which information can be conveyed has accelerated significantly, as has the multiplicity of channels and sources through which it is communicated. For businesses in crisis, this means they have no option but to engage. While once it was only journalists who would uncover business stories, this has changed in the age of social media, making silence no longer possible. A customer or supplier may interact with your business, realise there are problems and put it on their social media account where it will be noticed, and the story will grow.

A crisis does not have to be caused by a dramatic incident to attract media attention. A business's financial difficulties may come to the attention of not only traditional media but of financial experts who now no longer work for large mainstream organisations but operate as commentators and bloggers, with the multiplicity of channels making it easier for information to emerge.

CONTROLLING YOUR OWN NARRATIVE

While there is serious risk in failing to manage your crisis communications, the benefit of getting it right is that you are the one leading the narrative. You are telling the story. You are not allowing others to tell it on your behalf.

This matters in a turnaround because the way you handle the situation can influence the outcome of a crisis. You cannot undo the fact that your business has experienced difficulties, but you can absolutely minimise any long-term reputational harm as much as possible by being seen to deal with problems quickly and correctly.

POST-CRISIS ACTIONS

A crisis should be a learning experience for a business on the effectiveness of its communications:

1. Use your experience to evolve

It is important for the crisis communications team to meet in the immediate post-crisis phase to identify what did and didn't work and then update your crisis communications plan.

2. Acknowledge the crisis

Be aware that no matter how effective your crisis communications have been, there will be a record of what has happened, whether it is on social media or even just in emails to stakeholders.

The existence of search engines means your story cannot be forgotten. And depending on the seriousness of your difficulties, they may be associated with your business every time it is mentioned in the media, whether in a positive

or negative way, for a few years after the event. Although it may seem counterintuitive, it is very important to acknowledge your difficulties. If you do not acknowledge what has happened, you will be creating a vacuum for others to step into.

3. Provide regular updates

Your successful crisis communications will have built trust and support. We advise that, during the first six months or so of your recovery, you provide regular updates to those you communicated with during the crisis on how the business is doing now and how you are moving forward.

The key to maintaining a positive reputation and potentially gaining business is to continue to handle your communications well. Talk about your recovery to show how well you are progressing and how your business is growing. Using the crisis as a reference point one year later creates a positive opportunity with the media, stakeholders and investors to show how you have managed to turn the business around.

KEY TAKEAWAYS: CRISIS COMMS CHECKLIST

Use our checklist to build your crisis communications plan.

- Carry out a crisis comms audit: understand your vulnerabilities and where crises could occur within your business.
- Make a list of who will need to be contacted in a crisis: staff, stakeholders, customers, media, suppliers, investors and any other interested parties.
- Identify key experts: who are the people working in areas of vulnerability who will be called upon in a crisis?
- Identify all your communications channels.
- Make sure mailing lists are up to date.
- Put together your crisis communications team with members from different areas of your business.
- Arrange crisis notifications: set up an instant messaging channel for the crisis communications team (e.g. WhatsApp), and make sure it is only used for this purpose.
- Identify individuals who will be communicating externally.
- Organise media training for people who will be communicating externally.
- Create holding statements and crisis comms templates.
- Get your messages out as soon as possible when a crisis emerges.
- Ensure the team is aware of core messaging and form of words.
- Ensure all channels are being used and that core messaging is consistent across channels.
- Tailor messaging emphasis for different audiences.
- Continue to message and respond to media requests for comment as the situation develops.
- Hold a post-crisis discussion to evaluate your communications.
- Update your communications plan based on your findings.
- Continue to message with news of your turnaround.
- One year later, use your crisis as a reference point in messaging to show how far your business has come.

4

FINANCIAL STABILISATION AND RISK REDUCTION

BANK OF SCOTLAND

David Bates, *Senior Credit Officer, Business Support*

'Cash is king' is a phrase many business owners will be familiar with, and it's particularly true when it comes to implementing a turnaround strategy.

Being in a financially stable position, where you have sufficient cash to meet your obligations, is key. Your business's financial stability not only determines the timescale of a turnaround – it also affects what options are open to you in terms of restructuring and exploring new revenue opportunities. Ultimately, you can have a brilliant business idea and a structure in place to make it work, but without solid finances you're likely to experience difficulties at some point in your business lifecycle.

THE SIGNS OF A FINANCIALLY STABLE BUSINESS

All businesses work in different ways, but financially stable companies usually have several things in common, including:

- Reliable and robust financial controls.
- Regular monitoring and analysis of financial accounts, with decisions based on the findings.
- Clear financial forecasting and the ability to mitigate risk and take preventative action early.
- Good communication with key stakeholders.
- An understanding of what their key financial metrics are – not just key performance indicators (KPIs) for the sake of it.

If you're in a position where your business requires a turnaround strategy, the idea of achieving this level of financial stability may seem unrealistic. However, there are a number of avenues you can explore.

But first, it's important to fully understand what caused your financial difficulties in the first place.

EVALUATE YOUR FINANCIAL SITUATION

Businesses experience financial difficulties for many reasons, some of which are out of their control. Their market may have been negatively affected by external economic factors, such as the COVID-19 pandemic. Over-borrowing, insufficient liquidity, failure to invest or introduce changes in line with market changes or a lack of control around working capital cycles may also be factors. In some cases, businesses are too focused on turnover, rather than making decisions based on how much profit a deal or contract will bring in.

Regardless of what caused your business to become distressed, it's important to get to the root of the problem to ensure the same mistakes aren't repeated. Taking a step back to understand your current situation will likely pay off in the long run.

ASSEMBLE YOUR SUPPORT TEAM

For this process to run smoothly, you need the right team around you. This could include your accountant, an external advisor, senior stakeholders or your relationship manager at your bank – people who can really help you develop a comprehensive perspective on the challenges you face.

ASK YOURSELF THE RIGHT QUESTIONS

Once your team is in place, it's time to ask some difficult questions. These questions may include:

- Was the situation caused by a drop in sales due to a worsening economic backdrop?
- How realistic was your business plan?
- Was your business plan realistic but you weren't able to execute it as hoped?
- Are you holding too much debt?
- Did you overestimate growth or the speed of growth?
- Do you have high fixed costs?
- Do you prioritise turnover and market share over profit?
- Have you changed strategy multiple times?
- Are you over reliant on a small number of customers?
- How well defined were your KPIs?
- Does your management team consist of people with the right skillsets?

These questions will help you get to the root of what caused the issues your business is facing and help identify areas to focus on as you develop your turnaround plan. Putting your business under the microscope, so to speak, will also highlight what's gone well and ensure that you can maintain that success moving forward.

Putting your business under the microscope, so to speak, will also highlight what's gone well and ensure that you can maintain that success moving forward.

TAKE IMMEDIATE ACTION

While you're examining the causes of your business issues, there are some steps you can take to stabilise things in the short-term. This allows you time to reflect and make the right decisions for the future of your business, rather than making choices based on gut reactions that may prove to be the wrong path.

We explore some of these short-term measures here.

SPEED UP DEBT COLLECTION

Ensure you're collecting debts as quickly as possible. Reminders should be issued on the first day payments become overdue and you should proactively chase late payments. You may be able to offer customers an incentive, such as a small discount for accepting shorter payment terms or for early payment. It's also worth looking at what payment methods you accept. Accepting a number of payment options (e.g. card payments, direct bank transfers via the Internet or electronic banking, and BACS payments) could help customers speed up the process on their end.

REDUCE EXPENDITURE

Freeze non-essential spending and tighten up your expenditure processes so that all purchases undergo a level of additional scrutiny. You may want to consider what cost reduction measures could be targeted; examples might include a change in working patterns or a review of marketing spend.

STRETCH YOUR CREDITORS

Consider reviewing the timing of when you pay creditors to preserve cash. If your usual suppliers can't offer flexibility, consider seeking alternative suppliers. However, be warned that stretching your creditors without negotiating with them first could ultimately have a negative effect on your supplier relationships and credit score.

DISPOSE OF ANY NON-CONTRIBUTING ASSETS

Do you have any assets which are inactive or not contributing to revenue? Selling them could give you a much-needed influx of cash. If you have property assets, consider looking at sale and lease-back opportunities or simply moving to cheaper rented premises.

LIQUIDATE STOCK

Having extra inventory hanging around can be a real drain on your cash reserves, so a focus on reducing stock holding and turning surplus stock into cash can be helpful. There are specialist companies which will buy excess stock in bulk, or you could hold a flash sale to speed up sales of certain products or lines.

LOOK TO YOUR PERSONAL RESERVES

As a business owner, shareholder or director, do you have sufficient personal reserves to support the business? This could be a temporary measure or a longer-term re-capitalisation of the business which improves the strength of the balance sheet.

IDENTIFY THE RIGHT LONGER-TERM STRATEGY FOR YOU

Once you've got some short-term cash management measures in place, it's important to shift your focus to the bigger picture and capitalise on the time you've bought yourself.

All too often we see that when a cash situation stabilises, the business starts to relax and lose some of that focus. This is the time to double down and start putting things in place to ensure your future security and growth. If you haven't already, this is usually a good time to bring in some outside guidance, to help keep the momentum up.

This is by no means an exhaustive list, but the following points give a good overview of some of the popular turnaround strategies which could work for your business in the long term.

Once you've got some short-term cash management measures in place, it's important to shift your focus to the bigger picture and capitalise on the time you've bought yourself.

SEEK INVESTMENT

Can your shareholders introduce more cash or seek external investment? If your directors have directors' loans in the business, can they turn those into equity to strengthen the balance sheet and to remove the future repayment liability that might be sitting against them?

MAKE MANAGERIAL CHANGES

You may wish to introduce new management to lead the company (e.g. a new MD or CEO) or appoint someone to lead a specific function to address a particularly weak area, such as a new financial director to strengthen the financial function.

SEEK REVENUE IMPROVEMENTS

This could include changing your pricing structure, introducing a price increase, running promotions or increasing your minimum order. You may also wish to benchmark your pricing against your competitors, but always keep your own costs to supply your goods and services in mind.

STRENGTHEN FINANCIAL CONTROLS

Consider producing cash flow forecasts which predict future demand and use of cash. You may want to hold regular 'cash' meetings to take stock of your situation. It's also important to ensure your procurement is aligned with production and sales plans, and to prioritise spending accordingly.

REORGANISE STRUCTURES

Could your trading divisions be restructured in a more effective way? This could be an

opportunity to remove unnecessary operational requirements and to empower middle management to enact change.

RESTRUCTURE DEBT

Can you change the type of debt you're holding? For example, shift from short-term debt to long-term debt or alter your repayment terms to more favourable ones. It's also a good idea to focus on any gearing issues (e.g. do you have too much debt versus too little equity?).

EXPLORE NEW FUNDING SOLUTIONS

If you have certain assets within the business, you could finance those to generate some cash. Depending on your turnover, Invoice Factoring or Invoice Discounting could be another option to give you faster access to cash by releasing a percentage of an invoice's value, within short time frames.[1]

MARKET RE-ORIENTATION

Can you look to expand into other markets or diversify your product set? Now's the time to stop selling poorly performing product lines and to refocus on more profitable markets.

When it comes to identifying the right long-term strategy for your business, your plan might follow a single vision, or be multi-dimensional in approach. Let's say you want to enter a new market or invest in the business in some way but do not have the cash to do so. You may need to first combine with another strategy which has the power to generate the funds you need.

GIVE YOURSELF THE BEST CHANCE OF SUCCESS

Whichever strategy you choose, there are a few things you can do to give your business the best chance of succeeding.

MAKE SURE YOU HAVE THE RIGHT SKILLS BEHIND YOU

Some management teams are very well-equipped to go on this journey themselves. Others aren't, so it's about recognising where you've skill gaps and making sure you have a team which can help you through every stage of planning. Ultimately, if you don't plan correctly, you'll just be enacting a strategy with risks to its implementation.

Ideally you need someone with very good operational skills and financial planning experience to help you translate your vision into a workable plan and to ensure you have the liquidity to see it through without further impact on cash reserves.

It may be that you have a strong financial function or super savvy financial director already, but if you're looking around your business and not finding anyone who can fulfil this role, don't panic. The key is recognising you have a gap. Options may include speaking with your accountant for help or seeking an interim restructuring specialist.

Bringing in external support can seem off-putting when you've lived and breathed your business for years, but having someone who is open-minded to change, can act as a sounding board and is willing to challenge you a bit can really help you get the momentum going.

> Ultimately, if you don't plan correctly, you'll just be enacting a strategy with risks to its implementation.

ENGAGE EFFECTIVELY

Whichever strategy you opt for, you'll need the support of creditors, investors, HMRC and other stakeholders – so effective engagement will give you the best chance of success. Maintaining an open and honest dialogue is key. No one likes surprises and keeping everyone in the loop helps maintain trust. This can be a challenge and sometimes even prove disruptive to the process but, typically, successful turnarounds are those with very open and transparent dialogue with all stakeholders.

Think about who is best suited to have conversations with stakeholders. If you're making a request, whether it's for extra investment or restructuring debt, you may

only get one chance, so you need to present a compelling story.

MINIMISE RISK

Even after you've successfully completed your turnaround, the work is far from over. You need to take steps to minimise risk and maintain your financial stability for the long term. We explore some of the steps you can take here.

IMPLEMENT ROBUST INTERNAL CONTROLS

Set budgets, hold monthly board meetings and regularly review financial accounts to see how you're trading against budget and what you can do to correct any variances. This helps keep you accountable and ensures you're aware of any early warning signs.

Bringing an external source into these conversations, like a non-executive director or chairperson, means they can act as a sounding board, share their experience of other companies and offer a healthy challenge to your assumptions to help keep the business moving in the right direction. For smaller companies, this role could be fulfilled by a member of a trade association or a business mentor.

SET CLEAR KPIs

Having a well-considered and clearly outlined set of KPIs acts as an early warning system. Information is key to ensuring you don't experience further financial instability and are able to take swift action at the first sign that something isn't right. Make sure your KPIs are tailored to your business and give real insight into performance, rather than being just a generic set of measures.

STAY ON TOP OF CASH MANAGEMENT

If you've had problems in the past and you've stabilised your cash position, it's important to check that it isn't slipping once more. If your debtor or stock days are drifting out and your creditor days are coming in, it could be a sign that your working capital cycle is out of balance.

LEARN FROM PAST LESSONS

Keep all the lessons you've learned from your period of difficulty at the front of your mind and build them into a contingency plan. Identifying and having a plan in place to manage potential risks will minimise the impact if you find yourself in that position again.

REGULARLY FORECAST AND MONITOR CASH FLOW

Cash-flow forecasting isn't just for the period when you're in distress. It needs to become a habit for the lifetime of your business. Looking at your cash flow forecast over a 13-week period can help you identify when to make key investments and help the business keep growing and evolving. If you do make capital investments, you need to have a clear idea of what your return should be in terms of incremental profitability and cash generation and to monitor it to ensure it delivers.

REVIEW YOUR BORROWING

When you first embarked on your turnaround, your appetite for consolidating or simplifying borrowing may well have been low. However, as you move through the stabilisation process, it's vital to regularly review borrowing and ensure it's set up in a way that supports your long-term objectives.

Some businesses do experience difficulties during their lifecycle. If you're in a financially stable position, you've got the ability to trade through those difficulties and deal with them effectively, rather than ending up in a situation of distress. As we've discussed in this chapter, achieving – and maintaining – that level of financial stability can be a long process, but one which helps secure the future of your business.

KEY TAKEAWAYS

- **Understand your working capital.** You need a clear understanding of all your working capital components. What money do you have coming in and out, and when? Is your inventory well managed? Regular forecasting and monitoring of cash flow are essential.
- **Pro-active communication is key.** Keep an open dialogue with everyone involved in your turnaround and raise any issues proactively.
- **Remember, all businesses are different.** While you may be using a tried-and-tested turnaround strategy, how it applies to your business will be completely unique. Develop a plan with a mix of actions that suit your specific needs, and a timeline that works for you.
- **Keep up the intensity and be accountable.** Once you have agreed to a plan, you need to take accountability and be prepared to drive it forward and stick to the actions and timelines you set out for yourself. Never get too comfortable.

FURTHER RESOURCES

- Bank of Scotland Business Recovery Hub: Contains support on financial worries, mental health and guidance on improving cash flow.

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5

EXPLORING RESTRUCTURING OPTIONS

POTTINGER

Nigel Lake, *Founder and Executive Chair*

Every turnaround situation has its own particular complexities and dynamics, making independent, objective guidance invaluable as you explore how best to navigate the challenges you face and/or unlock new opportunities.

Typically, when a business is facing financial difficulty, they'll be referred to their bank's support function. The bank will then work with them to develop consensual turnaround strategies. That may involve signposting to a choice of professionals including a restructuring accountancy firm or turnaround executive.

Below we've outlined a number of turnaround approaches which may be considered as part of this process. Which is right for your business will depend on a number of factors, including:

- the reasons why your business is in distress;
- market conditions i.e. is there still sufficient demand for your products and services; and
- your business's financial health.

You may choose one strategy, or a combination of several. Whatever path you follow, the goal must be for the business to emerge stronger, nimbler and more resilient to future stresses.

KEY TAKEAWAYS

- Your bank's support function can help you consider turnaround strategies and refer you to appropriate expert help.
- There are a variety of turnaround strategies – the right one for you will depend on how your business is structured and the challenges you've faced.
- The ultimate aim of a turnaround is for your business to emerge more resilient.

What are the underlying challenges you face?
The *amount* of capital you need
The *type* of capital you need
How you run the business
What the business *does*
What do you need to do to tackle them?
Raise new equity
Financial restructuring
Operational restructuring
Business repositioning
Current shareholders
Renegotiate debt terms
Improve efficiency
New products
New financial investors
Use different forms of finance
Improve sales processes
New customers
A strategic ('trade') investor
Secure new facilities
Manage working capital better
New markets
Convert some debt to equity
Shift to a new business model
Sell non-core assets to repay debt
Exit unprofitable activities
Lease or own? | In-house or out-source? | One-off payments or "as-a-service"

6

A TURNAROUND PRACTITIONER'S VIEW

WAYPOINT CHANGE

Nick Winks, *Founder and Director*

What follows is a distillation of the experiences of the WayPoint Change directors and associates, all of whom have many years of experience in operational turnaround with businesses of all sizes, in all sectors.

Usually, the need for a business turnaround becomes evident with the realisation that there is little or no cash headroom and that most likely scenarios show the business requiring further funding rather than generating cash.

Sadly, this prognosis often becomes apparent to the business stakeholders before the directors. The early signs of the cash shortage are thus often flagged by banks and other creditors, shareholders, auditors, trade insurers or even employees, especially those in finance roles.

The reason that some directors may be slower to respond could lie within human psychology. Directors may have a fear of admitting failure or a natural belief in their ability or the ability of the business to win that next contract, gain additional overdraft headroom or persuade a new investor to rescue the business.

When directors need encouragement to engage, some expert advisers overemphasise the directors' personal liabilities if they trade a business that is insolvent instead of helping the directors navigate next steps. Unfortunately, the statutory definitions of insolvency include arcane ideas (e.g. a negative balance sheet) that may be confusing to directors. Some expert advisers often have more to gain from a company going into administration than from it being successfully turned around.

Most directors of a distressed business are experiencing corporate distress for the first time. They may be, therefore, inexperienced and susceptible to sellers of deceptive marketing and quick-fix solutions. Consequently, the turnaround expert is unlikely to gain traction with the directors without positive sponsorship from the company's bank, auditor or major shareholder.

In the UK, the 21st century has seen the emergence of a rescue culture (encouraged by the Enterprise Act of 2002). This change has often been initiated by banks who now recognise that their ability to facilitate and positively influence the turnaround of a distressed corporate customer is better for them and the wider economy. Prior to this century, the main priority for many banks was to seek out and speedily recover their money from a distressed customer, a policy that usually involved the customers' receivership and insolvency.

Most banks these days have specialist units that handle distressed corporate customers. The aim is to use available expertise, both inside and outside the bank, to facilitate a return to viability. These specialist bank units still have an objective of recovering the funds owed by the distressed business, but the recovery is now done in a timescale that allows for a turnaround. In exceptional situations, these specialist bank units may extend borrowing if they believe the turnaround is credible.

If the turnaround expert is willing to share any risk by becoming a director, the other directors are likely to be encouraged.

There are two reasons why a turnaround expert should join the distressed company as a director, rather than as an adviser or any other designation. The first reason is that the turnaround person should be empowered, by being an executive, to make decisions, often with very short notice. Being a director bestows authority in the eyes of employees and external stakeholders. The second is to reassure the other directors that they are taking sensible risks in deciding to undertake a turnaround. If the turnaround expert is willing to share any risk by becoming a director, the other directors are likely to be encouraged.

IMMEDIATE PRIORITIES

There are two immediate priorities for the distressed business as it begins its journey back to viability.

The first relates to the cash resources and the level of 'cash burn'. By looking at headroom and the rate of burn, the turnaround director has an immediate picture of the likely life expectancy of the business under present conditions. The focus should first be to control the cash by ensuring that only essential payments are made. Similarly, debtors should be encouraged to pay promptly. Any overdue debtors should be urgently pursued.

This initial understanding of the available cash and the rate at which it is being depleted provides a maximum timescale for the first stage of the turnaround: get to cash break-even.

Many distressed businesses make the error of not talking to their creditors. This is a big mistake because without clear communication, creditors worry more and are more likely to take precipitative action to recover their money if they feel locked out of the conversation. Directors of the distressed business should be clear to creditors about what cannot be done ('we can't pay you for at least three months') without giving specific promises of when payments can be made unless there are clear milestones ('when our customer pays us'). Directors can be personally liable to creditors who are both knowingly misled and consequently disadvantaged by false information.

The second immediate priority involves determining the leadership of the business. The turnaround director is an obvious candidate for a central role, but as they may not understand the nuances of the industry and market in which the business operates, it is essential for them to be supported by a competent team. One of the important considerations is the extent to which the top executives are tainted by their performance in bringing the company to its state of distress. This assessment is not just about an objective determination of their culpability; creditors and staff may have lost faith in the executives' judgement and abilities.

When exiting directors that have lost the confidence of lenders, employees, or other stakeholders, it is worth realising that many such directors go on to have successful careers in other businesses. Their relative failure is often situational and not fundamental to their underlying abilities.

Managing a distressed business back to viability is a specialist skillset. Most managers and directors have never had to do this, so they have no experience guiding them on how to successfully turn around their company. In addition, the psychological damage caused by leading a business down a steep decline may have impaired these leaders' self-confidence. They are likely to recover but in a new setting with another business.

SECOND WEEK PRIORITIES

The turnaround director should now produce a rolling 13–week cash forecast, reflecting what is known about likely costs, debtor receipts and creditor payments. It is important for assumptions to be prudent but not unduly pessimistic. The forecast will show the timing and amount of any cash shortage. This knowledge should inform the process of cutting costs in the business. Often, this involves redundancies, office closures and curtailing capital expenditure.

LET THE TURNAROUND BEGIN

Only once all the internal savings have been implemented is it possible to look outside the business for support. This may be achieved by agreeing to deferred terms with creditors, for example, Her Majesty's Revenue & Customs or trade suppliers. There is often a reluctance to discuss cash pressures with suppliers because of a perceived reputational risk. This is nearly always unfounded; suppliers will usually have already recognised, by payments being delayed or missed, that there are problems. Most of them will be relieved to be involved in a constructive discussion to help their customer recover. They know that, in the event of a default, they will be unsecured creditors with little prospect of full payment.

Banks are usually much more helpful if they understand the extent of the problem and the turnaround plan, and if they have faith in the new leadership to deliver that plan. Often banks are, however, reluctant to provide further funding if that money is used (all or in part) to pay historic creditors. Of course, any business's bank is a creditor itself, and it will not want to put other, often unsecured, creditors in a better position at the cost of putting themselves in a worse position.

Shareholders, too, may be willing to invest to aid the recovery of the company. They will generally prefer to do this only if they are sure the bank will not give sufficient support. In many cases, the lending bank's support may be conditional on shareholders agreeing to partially fund the turnaround. The logic of the banks' position is that the value of shares in the business, once returned to viability, will be greatly enhanced; accordingly, shareholders should be funders, at least in part, of the turnaround.

If the current shareholders are unable or unwilling to fund further equity, the turnaround director should be able to introduce new shareholders if that is the way to avoid insolvency. High-net-worth individuals who have made money from previous turnarounds are ideally placed to invest again and can often do so with minimal due diligence.

With some, if not all, of the cash parameters settled, and new senior management installed, the turnaround process can begin.

This usually starts with an assessment of what the minimum level of sales is likely to be over the coming year. It is important that this assessment is cold-eyed and excludes speculative opportunities. Typically, the minimum level of sales over the coming year is about the same level as the past years' actual sales.

Having established a sales forecast, the next task is to ensure a cost base that is commensurate with the business not losing cash at that level of sales. Both cost of sales and overheads may need to be significantly reduced if the cash break-even objective is to be achieved. Management often limits their thinking in these scenarios by hesitating because of the cash needed to fund severance or redundancy of employees. In the UK, this cost rarely averages more than three months' pay. However, if delayed, these decisions will never cost less, and in the meantime, the business may have failed to right-size.

The components of cost of sales also need careful analysis.

The spike in cash due to severance costs should be reflected in the short-term cash forecast. However, this outlay will typically be recouped at least three times over in the coming year.

The components of cost of sales also need careful analysis. An increase in the gross margin

can be achieved by either a lower unit cost of sales or a unit sales price increase. One of the benefits of thinking only in terms of a minimum sales volume over the first year is that the temptation to 'buy' new business is gone. Some simple arithmetic can demonstrate the power of price increases.

By way of example, imagine the gross margin of sales is, say, 30 per cent. A 10 per cent price increase would increase the gross profit by 33 per cent, meaning the business could lose a quarter of its sales (after increasing prices) without reducing profitability. Very few products or services are so price elastic for such a large reduction in sales to occur in practice, at least in the short term.

An explanation of cash break-even is now appropriate. Accounting profit is always struck after some costs (and sometimes includes a portion of sales) that are non-cash. Examples of non-cash costs are depreciation, amortisation and rolled up interest (often on shareholder loans). Non-cash sales are less prevalent but may include retentions and long-term maintenance contracts.

The objective is to get the failing business to cash break-even as soon as possible; a thorough understanding of the cash components of both sales and costs is imperative.

By now, the turnaround director should be the leader of the management team tasked with rescuing the business. He or she will eschew long-term or strategic plans whilst the first focus, on cash break-even, is being pursued. During this phase, it is common to have the team working to a 100-day plan, often subdivided into 10-day milestones. Achieving these short-term milestones builds confidence in the management team as well as lenders and other creditors. Boosting the confidence of lenders will be invaluable later in the turnaround if the business plan is driven off-target by unforeseen events.

One important and often overlooked stakeholder is the credit insurer. They are key to suppliers being able to insure any trade debt extended to the company. Without insurance, many suppliers will insist on pro-forma terms which make cash break-even much more difficult to achieve. Trade insurers respond favourably to a management that shares their plans and regularly provides them with management information on the progress of the turnaround.

Communication to all stakeholders is always important but in the early stages of a turnaround, it is even more true. As a company falls further down the decline curve (pre-turnaround), management often adopts a 'bunker' mentality, and communication is both minimal and unrealistically optimistic. This bunker approach will have eroded trust and often made employees and creditors suspect things may be worse than they are.

The top team *must* brief employees on the 100-day plan and update them as the 10-day milestones are achieved or not achieved. This is best done face to face rather than by written communication. Anything written is likely to end up with the trade press, ex-employees or even with competitors. Face-to-face communication has the added benefit of enabling the turnaround leaders to answer questions and reassure doubters. Similarly, creditors' confidence can be rebuilt by careful explanation of the company's plans and giving realistic dates for payment of their invoices. There is never an excuse for not communicating with stakeholders. Silence is always taken as a sign that things are in a worse state than they are.

Some turnaround directors see the achievement of cash break-even as the end of the turnaround. This is a mistake.

BEYOND CASH BREAK-EVEN

Once cash break-even is achieved on a sustainable basis, it will be time for the management team to think about growth and profitability. Some turnaround directors see the achievement of cash break-even as the end of the turnaround. This is a mistake. Break-even is

only the first stage of the process. The objective of all turnarounds is the business' return to long-term viability and economic value. A business is not viable unless and until it can pay its long-term debts and afford the capital investment to grow profitability.

After the break-even phase, the turnaround director should consider the shape of the management team, particularly in choosing the leader of that team post-turnaround. One of the key tests of viability will be the strength and ability of the top team once the turnaround director has gone. So, one of the key tasks of the turnaround director in years two and three is to prepare incrementally for their departure by handing over more responsibility to others in the top team.

An authoritarian style of management may be justified in the first months of a turnaround, especially if the survival of the business is in doubt. This style is tactical and temporary: the turnaround director should manage a return to a collegiate and consensus management style once an authoritarian style is no longer necessary.

Part of this transition of leadership at the top of the business is to ensure that stakeholders, such as banks and shareholders, are weaned off their dependence on the turnaround director. The transition also demonstrates that the top team now has the strength and ability to maintain control of the business without repeating the mistakes of the past.

In conclusion, the main advice we at WayPoint Change give to any leader of a business in decline, or to any stakeholder in such a business, is to get help early on. Successful turnarounds need two ingredients: time and cash. Early intervention provides more time, resulting in less cash required to get the business to viability. Waiting until the last minute will vastly increase the difficulties of the turnaround, including the risk of insolvency, and it will need more cash to be successful.

KEY TAKEAWAYS

- Delay is fatal – Engage key stakeholders early (funders, suppliers, credit insurers, employees).
- Draw on specialist expertise – Most managers have never been through a turnaround.
- Understand cash burn rate – How long before headroom runs out?
- Deliver on promises – Creditors accept realistic payment plans but be clear and stick to them.
- Build a reality-based turnaround plan – Base on recent revenue run rate and drive cash costs (cost of sales and overheads) down to match.

7

(RE)BUILDING A WINNING TEAM

WHITE OAK EUROPE

Annabel Giles, *Director of HR*

When you are managing a crisis or attempting a business turnaround, people are incredibly important. From the mailroom to the boardroom, the culture you build, the people you hire and the way you support them impacts all areas of a company and influences your chance of future success.

In this chapter, I'll explore some of the key elements to consider when building and managing a team to successfully navigate a turnaround and beyond.

GETTING THE RIGHT MIX

Having the right people onboard is essential if a turnaround is to be successful. Do your existing staff have the skills necessary to enact your chosen turnaround strategy or will you need to embark on upskilling and/or a recruitment drive? Does the departmental structure need altering? Might you need to let people go? Are some employees particulary critical to the success of the turnaround, and if so what steps will you take to retain them?

And it's not just about having the right skills mix. To help a company navigate a turnaround you need people who support the future vision and aren't resistant to change. Ensuring that key employees are a part of the turnaround team and invested in the process can help messages cascade through the business.

Preparation is key and having job descriptions and organisation charts ready to communicate as soon as possible can help ease the transition.

It may be that you need to bring in external support in the form of a turnaround specialist for a limited time period. Again this needs to be managed sensitively. The HR function will be pivotal in helping advisers build rapport and trust with the leadership team and key staff, so they can gain the information and support they need to do their job effectively. When their job is done, their exit also needs to be managed. Is there someone in house who can confidently pick up the work they were doing and continue to champion the new strategy?

BALANCED LEADERSHIP

Strong and effective leadership is clearly critical to successfully managing a turnaround. At times of crisis, all too often, senior managers can become dictatorial, imposing decisions on the team which may not be properly thought through in either operational or human terms. Other senior teams tend to go

too far the other way, asking for input from every quarter, failing to provide direction and eroding confidence in the entire leadership team.

Thus, striking the right balance is critical. You will need clarity regarding the challenges to be addressed, the decisions which you need to make and the actions which need to be taken as a result. Nevertheless, you must also remain attuned to how your team sees the issues and the implications for navigating through the crisis as effectively as possible for all of your stakeholders.

This means listening with an open mind to what all workers are saying, the problems which are causing them particular stress and the way they perceive the issues. Remember that it is usually day-to-day workers who will likely face the most stress and who are usually the most important people in delivering your products and services to customers.

The pandemic has highlighted, once again, the huge differences in priorities between different generations, and indeed how they think, work and live.

For example, many of our Gen Z workers live in rented accomodations with flatmates. I remember one man who lived in a house with 10 friends. His daily challenge was where to locate himself in the house – his bedroom or the kitchen table – with his friends all facing the same dilemma. We worked with him and other employees in the same situation to ensure they were in regular check-ins with their managers and teams and had access to mental health facilities at all times. Friday afternoon Zoom drinks only went so far in the early days, and the novelty quickly wore off.

On the flip side, many of our older workers have houses with places like gardens, but they faced different challenges, such as homeschooling several children within a confined space. This was also, by far, the demoraphic which was most concerned about their own health being compromised by the virus.

By providing people with platforms for employees to share experiences and talk through their own situations, we were able to foster continual, open dialogue. This also enabled us to factor our employee thinking into subsequent decision making. The importance of transparency should never be underestimated. Not only does it pave the way for open and honest dialogue, but it also highlights the integrity of the firm.

COMMUNICATION CADENCE

Managing the flow of information to your teams is essential. No matter what size your business might be, it is not enough to just send out a solitary email from the CEO and expect everything else to fall into place. Some people may not read the message, and most will probably not take in all of the nuances and implications of what is being communicated.

> Managing the flow of information to your teams is essential.

So, it is very important that there be a cascade of messages to people throughout the business. Think carefully about what information is needed at different levels, where that information will come from, when this should be provided and how best it can be presented at different levels in the organisation. In addition, make sure you develop plans for how to support mid-level managers in the business. This is where the large bulk of communication will take place for mid-sized and larger businesses, so it is essential to ensure a consistent organisational response.

Unsurprisingly, senior executives respond to crises and feel pressure in different ways. So, it is important the HR team understand the stresses which they perceive to be the greatest and help the management team work together as effectively as possible to ameliorate them. Figure out where scarce leadership time is best invested, and think about what is best done as a team. Consider what key meetings take place on a daily, weekly and monthly basis, along

with the audience, and how you can utliise these effectively to cascade key messages at an appropriate cadence.

In developing and adapting your communication strategy, remember that navigating effectively through a crisis is an opportunity to *strengthen* teamworking and *build* morale. Effective leadership will instil trust and confidence and will play a profound role in motivating and mobilising people to rise to the challenges and adapt to the environment.

EVOLUTIONARY OPPORTUNITY

Disruption – whether it is operational, economic or social – frequently drives rapid change in both working practices and customer needs. As a result, it can present an opportunity to evolve the way you operate to increase efficiency, improve the services you offer to customers and accelerate the implementation of strategic initiatives.

Disruption – whether it is operational, economic or social – frequently drives rapid change in both working practices and customer needs.

In exploring these opportunities, it is important to keep hold of what really matters operationally and culturally, whilst being able to let other things go. All too often, companies implement new technologies whilst preserving dated operating models which were originally designed within constraints which no longer apply.

For example, well-organised call centre operators had included 100 per cent remote operations as part of their disaster recovery plans. Some had speculated that this might be the best way to operate on a day-to-day basis, but they never had the courage to attempt implementation. The pandemic forced changes in working practices which put these theories to the test, allowing companies to discover – at least for some roles and employees – that the new approach was better for both the employer and employee.

Meanwhile, just as companies have discovered entirely different ways to work, employees have discovered entirely different ways to live. In countries such as the UK and US, where employers have held the balance of power, this has driven significant change. Individuals have learned that they can create a better balance between the hours they work, the amount they earn and their quality of life by changing the nature and location of their role and cutting down on commuting time.

Rather than seeking to fight these shifts, explore whether you can harness them to your advantage by accessing new pools of talent in new locations – or adapting your service delivery models in a manner which provides greater accessibility to your customers and flexibility to your employees. This may also allow you to compete in new markets, or it may mean that new competitors enter your home markets too.

Lastly, remember that many of these shifts reflect the use of computers to automate decision making, displacing many clerical, administrative and management roles in the process. Significant cost pressure has encouraged companies to seek new areas in which technology can be applied to cut costs. For example, Amazon outsourced HR functions in relation to a fleet of drivers entirely to a machine which could track each driver's efficiency in making deliveries. When individuals underperformed, they were automatically terminated and new drivers were recruited.

This type of approach creates new risks which need careful management. In the Amazon example, systems glitches meant that some data was not properly recorded, leading to unfair decisions being made in relation to some employees. At a deeper level, if the decision making engine were to use non-parametric approaches common to big data analytics, it would be impossible for humans to understand why any particular decision has been made. The decision might thus be right, but it could be impossible to prove this in a court of law.

Meanwhile, remember that more and more employment will be concentrated in areas which have intrinsically human essential elements – these include creativity, collaboration, caring, communication and culture. This illustrates that people will become an evermore important part of business. A company which favours only efficiency will end up in a race to the bottom on costs. By contrast, if you can use technology to humanise your business, then you can follow a race to the top on personalisation and differentiated service.

FUTURE FOCUS

No matter how great the short-term pressure on your business, make sure you continue to think about the longer-term impacts, as this is where the greatest opportunities will lie. The more you can align the short-term actions you *must* take with positioning your business for the future, the better placed you will be as less stressful operating conditions emerge.

No matter how great the short-term pressure on your business, make sure you continue to think about the longer-term impacts.

The disruption we have seen in 2020 and 2021 is going to be a real game changer. In some ways, it is a great shame that it has taken a global pandemic to force large employers to think more deeply about the potential benefits of remote working and the flexibilty it can provide. On a more positive note, these forced shifts have given much more visibility to related societal issues and impacts, including the inequity which flows from lack of access to basic 21st century infrastructure such as broadband internet connections.

Amongst other things, a raft of new case laws will emerge, as employees who were fired for their inability to work remotely (or refusal to return to a daily commute) bring forward unfair dismissal cases. Performance management practices and key performance indicators will doubtless evolve, perhaps with a growing emphasis on quantity and quality of output and a decreasing emphasis on hours worked. Together, these changes will define who benefits from productivity gains. As one example, in the US, Google is seeking to reduce pay for 100 per cent remote workers by as much as 25 per cent, in order to capture the benefits for shareholders.

Over time, these changes will flow through into almost every part of your business, including where and how you interact with customers, where and how you recruit and how you measure performance and employee turnover. Some companies have already moved to a 100 per cent remote operating model – or perhaps even better, a 100 per cent connected operating model – and are thus beginning to redefine their entire industries.

GRIT AND DETERMINATION

Whether the disruption you are living and working through is positive or negative, the entire experience can be exhausting, particularly if it is drawn out over many months. Leadership teams and employees must deal with an unpredictable environment, where the implications for their jobs, the businesses they work in and even their communities may be uncertain. The longer this lasts, the more tiring and stressful it can become.

During the global pandemic, one of the biggest challenges has been the many changes in guidance on how both individuals and businesses should operate. In some countries, this has been further exacerbated by ignorant and irresponsible public statements by both politicians and media commentators, adding both conflict and confusion to an already challenging situation.

On a practical level, this can make it hard for both individuals and businesses to plan ahead. Employers have a significant responsibility here, particularly if they have the resources to assess the risks and provide certainty to their employees. For example, during the middle part of 2020, Google indicated that it would not require a return to the office for at least 12 months. This allowed many employees to choose to relocate away from major cities, thus reducing their living costs, providing access to

better space for remote working and improving their quality of life.

At a deeper level, long-running uncertainty can be particularly wearing for everyone in your business. Whilst each company's circumstances will be different, it will be helpful to implement measures which deliver a level of predictability and certainty in at least some areas. Connection – in person or otherwise – remains paramount.

Most of all, never forget to look after yourself. Invest a little time every day in your own physical and mental health. Ensure you have strong boundaries to protect the personal activities which matter most to you, and don't be afraid to ask for support when you need it.

KEY TAKEAWAYS

- People are key to the success of a turnaround.
- Business leaders need to provide clarity regarding the challenges to be addressed, the decisions to be made and the actions to be taken.
- Turnarounds can create opportunities to rethink ways of working and make changes that benefit everyone.
- Don't solely focus on efficiencies – look for opportunities to humanise your business.

8

DIRECTORS' DUTIES IN A FINANCIAL CRISIS

BURNESS PAULL

Michael Thomson, *Partner*

Allana Sweeney, *Director*

Directors of companies in a financial crisis face several issues, including if and how to continue trading and whether doing so risks committing an offence or incurring personal liability. This guide outlines the main duties and potential liabilities of directors of companies in financial difficulty, including wrongful trading, fraudulent trading and disqualification. It also gives practical steps that may be taken by directors. It does not provide an exhaustive list of all potential duties and liabilities and one of the central recommendations is that directors in this scenario should take independent advice.

DUTIES OF DIRECTORS TO ACT IN THE BEST INTERESTS OF CREDITORS

Once a company is at risk of insolvency, the scope and nature of the duties of its directors shift significantly. In particular, the directors' primary duty shifts to acting in the best interests of the company's creditors (rather than its members). The change of primary duty to acting in the best interests of a company's creditors is triggered when the directors know or should know that the company will probably become insolvent.

Insolvency law does not formally recognise any distinction between the duties and liabilities of executive and non-executive directors. However, a non-executive function may affect the evaluation of the general knowledge, skill and experience that might be reasonably expected of the director and of someone carrying out that role in relation to wrongful trading (see Wrongful Trading).

Problems can arise for a person who is a director of more than one company in the same group. The director will need to consider the position of each member of the group separately: this may give rise to irreconcilable differences in the actions and decisions required of the director to comply with their duties owed to each company.

WRONGFUL TRADING

WHAT IS WRONGFUL TRADING?

If, in the course of an insolvent winding up or insolvent administration of a company, it appears that a person who is, or was, a director of the company knew or ought to have concluded at some point before the commencement of the liquidation or

administration that there was no reasonable prospect that the company would avoid going into insolvent liquidation or insolvent administration, the liquidator or administrator of the company can seek a court declaration that the director make a contribution to the company's assets. The risk of liability for wrongful trading is one of the main catalysts for the instigation of restructuring and/or insolvency.

LIABILITY AND REMEDIES FOR WRONGFUL TRADING

Only directors can be liable for wrongful trading. *Directors* include any person occupying the position of director, by whatever name called and include a shadow director. This means that a de facto director or a shadow director may be liable for wrongful trading. The person must be a director of the company at the time they knew or concluded that there was no reasonable prospect of the company avoiding insolvent liquidation or insolvent administration. Liability only arises if, on a net basis, it is shown that the company is worse off as a result of the continuation of trading. The court will not make an order for wrongful trading if, knowing there was no reasonable prospect that the company would avoid going into insolvent liquidation or insolvent administration, the director took every step with a view to minimising the potential loss to the company's creditors as they ought to have taken. To bring a successful action, in practice, a liquidator or an administrator will need to undertake a significant amount of work and expense. Therefore, in practice, the theoretical risk of personal liability for wrongful trading is sometimes greater than the practical likelihood of an action being brought, or being brought successfully. The relevance of wrongful trading to directors is often more that it instigates a restructuring or insolvency, rather than in the risk of proceedings. Directors of a company should take professional advice aimed at managing the risk of wrongful trading. This advice often influences the timetable by which restructuring or insolvency proceeds.

> Only directors can be liable for wrongful trading but this includes de facto directors and shadow directors.

COMPANY DIRECTORS DISQUALIFICATION ACT 1986

A person held liable may also be the subject of a disqualification order (see Directors Disqualification).

PRACTICAL CONSIDERATIONS FOR DIRECTORS TO MANAGE THE RISK OF PERSONAL LIABILITY FOR WRONGFUL TRADING

FOLLOW BEST PRACTICE AT DIRECTORS' MEETINGS

It is crucial that regular full board meetings are called if the company is in financial difficulties and that the commercial decisions of the directors are reported in full in the company's minutes.

ALWAYS HAVE UP TO DATE FINANCIAL INFORMATION

Directors must ensure that they have up to date financial information at all times. Directors should not wait for an event like a creditor's claim, a winding up petition or a failure to meet sales or cash-flow forecasts to alert them to the fact the company is in financial difficulty. Directors should be careful to monitor compliance with financial covenants contained in any arrangements with lenders.

TAKE ADVICE

As soon as a director is aware that there is no reasonable prospect of avoiding insolvent liquidation or insolvent administration, or has concerns that this may be the case, they must raise the problem with the rest of the board with a view to taking immediate independent advice. Further credit should almost certainly not be incurred until they have taken advice.

CONTINUED TRADING

Identifying the exact point at which the financial position of the company means that

insolvent liquidation or insolvent administration is effectively inevitable is difficult in practice. The directors' fear of wrongful trading may sometimes cause them to consider instigating insolvency procedures before they are really necessary or when they are premature. Precipitative action can be as damaging to creditors in some circumstances as waiting until the situation becomes clearer. Liability for wrongful trading cannot arise unless there is, objectively, no reasonable prospect that the company can avoid going into insolvent liquidation or insolvent administration. Directors cannot simply avoid the issue by resigning. They must take every step to minimise potential loss to creditors. A company can simply cease to trade without resorting to a formal insolvency procedure, but unless the company is solvent and can pay off all its debts (actual, contingent and prospective), the directors should consider pre-empting any action by an unpaid creditor, and definitively concluding any period for which they might be found liable for wrongful trading, by themselves causing the company to implement a formal insolvency procedure, like administration.

RESIGNATION

Resignation is not generally looked on favourably by the insolvency profession or the courts, as it may be regarded as an abrogation of the director's responsibilities. A court may therefore regard a resignation as an insufficient step to enable a director to avail themselves of the loss minimisation defence. However, if a director comes to the conclusion that there is no reasonable prospect of the company avoiding an insolvent liquidation but fails to persuade the majority of the board of that despite their best efforts, it may be sufficient if they resign as a director.

COVID-19

The UK Government announced on 28 March 2020 that it was to suspend the operation of rules relating to wrongful trading for a period of initially three months from 1 March 2020. Legislative provisions were enacted and subsequently renewed and extended. These provisions require a court to assume, in determining the amount, if any, that a director should be ordered to contribute to the assets of the company on a finding of wrongful trading, that the director is not responsible for any worsening of the financial position of the company or its creditors that occurred from 1 March 2020 until 30 September 2020 or from 26 November 2020 to 30 June 2021.

FRAUDULENT TRADING

WHAT IS FRAUDULENT TRADING?

If, in the course of the winding up or administration of a company, it appears that any business of the company has been conducted with the intent to defraud creditors, or for any other fraudulent purpose, the liquidator or administrator can seek a court declaration that anyone who was knowingly party to the fraudulent business make a contribution to the company's assets. This is known as fraudulent trading.

LIABILITY FOR FRAUDULENT TRADING

Only persons who were knowingly party to the fraudulent trading are liable. It is not enough for fraudulent trading to show that the company continued to run up debts when the directors knew that it was insolvent; there has to be actual dishonesty. It is not only directors who may be liable for fraudulent trading. Anyone who is knowingly party to conducting business with intent to defraud may be liable for fraudulent trading.

> Only persons who were knowingly party to the fraudulent trading are liable.

REMEDIES

The court may order a person to make such contribution as the court thinks proper. Where more than one person is liable for fraudulent trading, the court should apportion liability between the defendants by reference to the degree of control that each party had over the

company's affairs and the benefit that each party obtained from the fraudulent trading.

COMPANIES ACT 2006

Fraudulent trading is also a criminal offence under the Companies Act 2006.

COMPANY DIRECTORS DISQUALIFICATION ACT 1986

A person held liable may also be the subject of a disqualification order (see Directors Disqualification).

DIRECTORS DISQUALIFICATION

Under the Company Directors Disqualification Act 1986, a court may make a disqualification order against a person that they shall not, without leave of the court, be a director of a company or in any way, directly or indirectly, be concerned or take part in the promotion, formation, or management of a company for a specified period beginning with the date of the order. *Director* is widely defined to include any person occupying the position of director, by whatever name called.

DISQUALIFICATION ORDERS AND INSOLVENCY

Upon initiation by the Secretary of State, a disqualification order may be made by the court against a director or shadow director of a company that becomes insolvent if their conduct as a director makes them unfit to be concerned in the management of a company. For these purposes, a UK company is insolvent if it has gone into an insolvent liquidation, administration or had an administrative receiver appointed. When assessing conduct, the court is entitled to judge a director unfit on the strength of their conduct regarding:

- The insolvent company alone or taken together with the director's conduct as director of any other company or companies (including overseas companies).
- Any matter connected with or arising out of the insolvency of any such company (including overseas companies).

The minimum period of a disqualification order is two years and the maximum is 15 years. It is open to a disqualified director to apply to the court for leave to act as a director or manager of a company.

DUTY TO REPORT ON DELINQUENT DIRECTORS

Liquidators, administrators and administrative receivers are required to submit reports about directors (including shadow directors) to the Secretary of State if they believe that the conditions for disqualification are satisfied in relation to a person who is or has been a director of the company for which they have been appointed. With effect for insolvencies starting on or after 6 April 2016, the obligation to report applies in respect of all directors and shadow directors (current and past within the previous three years), irrespective of their conduct. They must submit their reports within six months of their appointment or, in insolvencies started on or after 6 April 2016, three months.

DISQUALIFICATION UNDERTAKINGS

The Secretary of State, instead of initiating disqualification proceedings, may accept a voluntary disqualification undertaking from a director to speed up the disqualification process. The advantage to directors of giving a voluntary disqualification undertaking is that they will not need to pay the costs of going to court and may also be given a discount on the length of any disqualification period. If a director agrees to give a voluntary disqualification undertaking, the Secretary of State has a discretion whether to accept the undertaking or apply to court for a disqualification order. Disqualification undertakings will only be accepted where it appears to the Secretary of State that it is expedient in the public interest to accept an undertaking instead of applying for, or proceeding with, a court application for a disqualification order. A breach of the terms of the undertaking has the same criminal and civil consequences as a breach of a disqualification order.

DISQUALIFICATION FOR FRAUDULENT TRADING AND WRONGFUL TRADING

The court can make a disqualification order against a person if they have been found liable for fraudulent or wrongful trading.

COMPENSATION ORDERS AND UNDERTAKINGS

Legislative provisions introduced in 2015 provide for the payment of compensation by a disqualified person for the benefit of specified creditors or creditors generally.

DISSOLVED COMPANIES

Legislative proposals have been put forward to allow disqualification orders to be made, and disqualification undertakings given, in respect of directors of dissolved companies. This would enable disqualification in appropriate cases where a company has been dissolved without it first having been in insolvent liquidation, administration or administrative receivership.

> The court can make a disqualification order against a person if they have been found liable for fraudulent or wrongful trading.

PERSONAL GUARANTEES

The directors of a company are generally not personally liable for the debts of a company. However, if a director has given a guarantee for the liabilities of the company, the director may be personally liable under the guarantee.

MISFEASANCE OR BREACH OF FIDUCIARY DUTY

If, in the course of a winding up, it appears that a present or former director has misapplied or retained, or become accountable for any money or other property of the company, or been guilty of any misfeasance or breach of any fiduciary or other duty, the court may order the director to repay, restore, or account for the money or property with interest or contribute such sum to the company's assets by way of compensation as the court thinks just. This also applies to any present or former officer of the company and any person who is or has been concerned, or has taken part, in the promotion, formation, or management of the company. The definition of *director* includes any person occupying the position of director, by whatever name called (and thus includes de facto directors).

LIABILITY OF DIRECTORS FOR TAX DEBTS

Since 22 July 2020, directors and other persons involved in tax avoidance, evasion or phoenixism are jointly and severally liable for a company's tax liabilities where certain conditions are met.

PRACTICAL STEPS FOR DIRECTORS OF A COMPANY IN FINANCIAL CRISIS

DO

- Ensure you understand your responsibilities as a director. Being a director of a company during financial difficulties can expose you to personal liability, for example for wrongful trading.
- Obtain professional advice in relation to the crisis and document any major decision taken by the company.
- Hold regular board meetings. All directors should be present.
- Circulate minutes after meetings. The minutes will be evidence of whether the steps taken by the directors minimise potential loss for the company's creditors, for the purpose of avoiding liability for wrongful trading.
- Create a list of all possible funding sources for the company. The board's attitude to pursuing any source of funding should be documented. The list will be useful for the board in identifying the time at which the company no longer had any reasonable prospect of avoiding insolvent liquidation, for the purpose of avoiding liability for wrongful trading.
- Draw up a timetable by when financial milestones like new funding levels for the company must be met. The timetable should identify when the company's failure to meet a milestone will mean that there is no reasonable prospect of the company avoiding insolvent liquidation or insolvent administration. The timetable should be strictly adhered to.
- Keep a written record of all discussions and meetings, or instruct lawyers to do this.

DON'T

- Let the company incur any new substantial liabilities until it is clear how such liabilities will be paid. An exception may be if the company's board considers any such liabilities essential and in the best interests of the company and its creditors.
- Wait for a winding-up petition to alert you to financial problems. Directors must ensure that they have up-to-date financial information at all times and should closely monitor compliance with any financial covenants contained in arrangements with lenders.
- Ignore events like creditors putting pressure on the company, the company filing its accounts late or judgments being entered against the company. These could be evidence of insolvency, which a reasonable director should have known about.
- Delay raising a problem with the rest of the board. As soon as a director is aware there is no reasonable prospect of the company avoiding insolvent liquidation or insolvent administration, or fears that this is the case, they must raise the problem with the rest of the board so it can take immediate legal and financial advice.
- Just resign to avoid the problem. Directors must take every step to minimise potential loss to creditors. If they conclude that the company cannot continue to trade, they must implement one of the insolvency procedures, like liquidation or administration.
- Forget to check the terms of your directors' and officers' insurance policy. Make sure you understand the extent of the cover and, if in doubt, obtain professional advice.

9

NAVIGATING CORPORATE INSOLVENCY: RESTRUCTURING, ADMINISTRATION AND LIQUIDATION

BEGBIES TRAYNOR

Julie Palmer, *Regional Managing Partner*

Running a business is not always smooth sailing. Navigating challenging times is also part and parcel of being a company director. Sometimes these challenges are related to the company itself, such as changing consumer preferences, reduced customer demand or new entrants to the market, while others are related to unavoidable macro-environmental factors, such as political decisions, changing legislation and the wider economic landscape.

BAD TIMES, NOT A BAD COMPANY

Regardless of the reasons behind the problems you face, it is important to remember that a company experiencing financial challenges is not necessarily a bad company. Often, periods of financial or operational distress can strengthen a company through successful management and leave it more resilient in the face of future challenges.

While a period of financial distress does not signify the end of your company, it is important that steps are taken to mitigate losses and to ensure that a robust plan is put in place to ensure a successful turnaround of the business. The longer a situation like this is left alone, the harder the problem is to untangle.

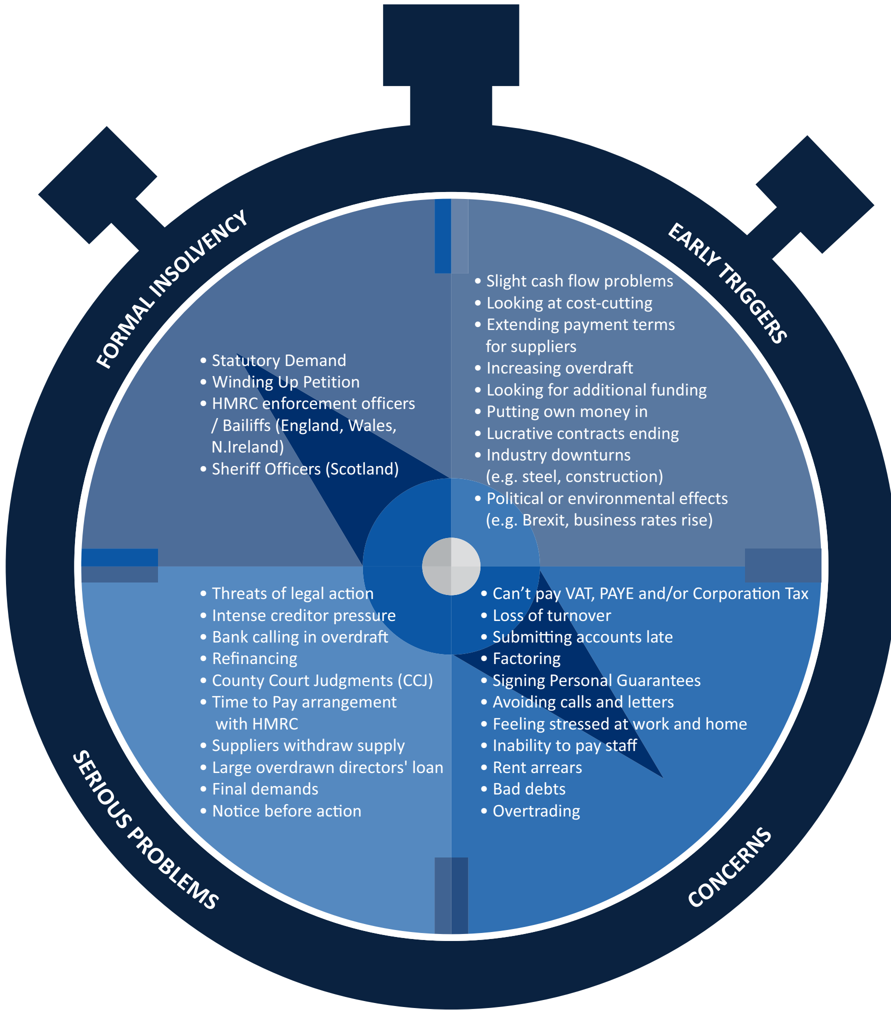
History has shown us that it is businesses that possess the agility to pivot their offerings to accommodate the changing climate which thrive the most when wider macro-environmental challenges present themselves. You need to ensure that a plan is put in place for your business which is robust enough to weather current problems and is also flexible enough to allow for unforeseen and unexpected changes to be confronted head on.

THE WARNING SIGNS OF INSOLVENCY

When it comes to company insolvency, there is not a one-size-fits-all solution. A number of factors must be considered before a plan can be put into place. These include the current financial position of the company, its ability to repay outstanding creditors, the viability of the company moving forward and the ongoing ambitions of the company's shareholders and their desire to continue operating the business.

However, what all instances of company insolvency have in common is the need to seek swift, professional advice as soon as practically possible. Left alone, financial problems

FIGURE 1. The warning signs of impending insolvency



have a tendency to escalate. A company can go from a state of cash flow concern into a fully-fledged insolvency process rather quickly. Being alert to the warning signs of impending insolvency (see Figure 1) puts you in the best possible position and allows you to seek advice at an early stage.

WHERE TO TURN FOR HELP

During times of financial distress, you need to know the right questions to ask, as well as the right people to ask. Whether you want to throw everything you have at saving the business, or if you are looking for a way to bring the company to an end in an orderly manner, the input of a licensed insolvency practitioner at this time is crucial. They will be able to take an objective and impartial view of your company and talk you through the options available for getting the company back on the road to recovery.

DIRECTOR DUTIES AND RESPONSIBILITIES

It is important to note that if you suspect your company may be edging closer to a position of insolvency – or if you believe the company to be already insolvent – seeking professional advice must not be delayed. As the director of an insolvent company, you have a number of legal responsibilities, particularly when it comes to how your creditors are treated at this time.

Once you know your company to be insolvent, you have a duty to place the interests of your creditors above those of yourself and your fellow shareholders. This means you should not engage in any activity which could cause your creditors to suffer further losses and you should take whatever steps necessary to maximise returns. By enlisting the advice of a licensed insolvency practitioner at the early signs of insolvency, you are prioritising creditor interests and complying with your legal duties.

SUCCESS THROUGH RESTRUCTURING

When a company is suffering from tight cash flow and increasing overheads and is in danger of falling behind to its creditors, a restructuring process can quickly identify non-performing areas of the business, suggest cost-saving measures and immediately improve efficiency. Simplifying an operating structure which has become overly complex ensures effort, resources and money are directed at the right place and at the right time to maximise profitability.

Often when a company experiences a period of sustained growth it expands in a way which conversely limits its potential for further expansion. Overly complex operating structures are rarely cost-efficient, as valuable resources are swallowed up in the unnecessary layers of the company's operating structure. Stripping this back and winding down the non-performing areas of a business can immediately boost cash flow and free up valuable resources.

When a company is suffering from tight cash flow and increasing overheads and is in danger of falling behind to its creditors, a restructuring process can quickly identify non-performing areas of the business, suggest cost-saving measures and immediately improve efficiency.

In some cases, a company's financial problems will be so severe that a formal insolvency process is the only way to save the company or its underlying business. Depending on the company's individual position and its likely future viability, this may involve either placing the company into administration or entering into a formal repayment plan with creditors.

UNDERSTANDING COMPANY ADMINISTRATION

For those companies facing threats of litigation or other debt recovery action from increasingly impatient creditors, placing the company into administration could offer breathing space while a plan is put in place to restructure the company.

Administration can help to save viable elements of a business even if the company as a whole cannot be rescued. In many cases, administration can protect jobs, maximise creditor returns and allow for meaningful trade to continue. Once a company enters administration it is protected by a moratorium which halts any ongoing – or threatened – legal action from creditors. While creditors still retain their rights and the claim over the money they are owed, this legal ring-fence provides valuable protection to the insolvent company in the interim.

THE PURPOSE OF ADMINISTRATION

Administration is a powerful tool; however, it can only be entered into if it serves one of the three statutory purposes as set out in the Insolvency Act 1986:

1. To rescue the company as a going concern.
2. To achieve a better return for creditors than would be possible if the company were liquidated without first being in administration.
3. To realise property in order for a distribution to be made to one or more secured or preferential creditors.

The administrator – who must be a licensed insolvency practitioner – will assess the situation and determine whether one of these objectives can be met. If not, administration will not be recommended, and alternative options will need to be explored. If it is decided that one of the statutory purposes can be achieved, the insolvency practitioner will be appointed as administrator and from that point on they will assume control of the company and work towards satisfying this aim.

EXIT FROM ADMINISTRATION

It is important to understand that administration is a temporary measure. A company cannot remain in administration indefinitely and at some stage it will need to exit the process. This exit may take the form of the company's business and assets being sold out of administration, continuing to trade following a process of financial and operational restructuring or by entering into an alternative insolvency process such as a Company Voluntary Arrangement (CVA) or voluntary liquidation.

PRE-PACK ADMINISTRATION

Pre-pack administration is a specific type of administration in which the business and assets are sold to a third party, with the terms of the sale being agreed to prior to the formal appointment of the administrator. This differs from a standard administration where the administrator would commence a marketing and sales strategy for the business after their appointment. With a pre-pack, the sale of the company's business and assets to the new company (newco), is completed immediately after the insolvency practitioner is appointed.

Pre-pack administration is a specific type of administration in which the business and assets are sold to a third party, with the terms of the sale being agreed to prior to the formal appointment of the administrator.

PRE-PACK ADMINISTRATION: STEP-BY-STEP

1. A financially distressed company contacts a licensed insolvency practitioner to discuss the situation and to help them better understand their options. A business assessment is performed, and a range of options is presented to the company.
2. If a pre-pack administration is deemed the most appropriate solution, the insolvency practitioner will obtain a valuation of the company's assets and prepare a Statement of Affairs. Note that there is a duty to carry out a widespread marketing campaign in respect of the business and assets for sale in the event of a third party wanting to enter the bidding process.
3. If business assets are to be sold to an existing company, checks will be made to ascertain that the buyer has the necessary funds to facilitate the purchase.
4. If the intention is to transfer the assets to a newco, then cash flow, profit and loss, and balance sheet forecasts should be provided to demonstrate the viability of the new company and its ability to purchase the assets.
5. The insolvency practitioner is appointed as administrator and the company enters administration. Any legal action against the company is suspended, and the assets are sold immediately.
6. The insolvency practitioner prepares their proposal for achieving the statutory purpose of administration, which provides an explanation for why the pre-pack route was taken. The creditors may accept, reject or modify those proposals.
7. Creditors are paid using the funds generated from the sale of assets, according to the hierarchy as determined by the Insolvency Act 1986.

WHAT PRE-PACK MEANS FOR EMPLOYEES

Pre-pack administration provides a number of benefits to employees, creditors and customers.

As the business is sold, there is no disruption to trade, ensuring continuity of employment for staff and no interruption of service for customers.

All employment contracts are transferred to the successor company through the Transfer of Undertakings (Protection of Employment) Regulations (TUPE). This ensures that employees retain all existing terms and conditions of employment, including length of service, which is extremely valuable in the event of any future insolvency proceedings particularly if the newco enters into liquidation at any point.

If administration is not deemed to be an appropriate solution, there are other options that can be explored.

CVA

A CVA functions as a legally binding payment plan between an indebted company and its creditors. Debts are repaid over the term of the CVA, which is typically 3–5 years, at a rate which is both affordable and sustainable to the company while also being agreeable to creditors. A CVA works on the premise of using future profits to repay existing debts, generally meaning only those companies which can demonstrate viability as an ongoing entity will be able to use this process.

Once the company's options have been assessed and the insolvency practitioner determines that a CVA is appropriate, they will draft a proposal detailing how much your company can afford to repay and present this to creditors on your behalf. Creditors may request revisions to the proposal if they consider the plan not satisfactory before a vote is held to determine whether creditors are to accept the proposed CVA.

> A CVA works on the premise of using future profits to repay existing debts, generally meaning only those companies which can demonstrate viability as an ongoing entity will be able to use this process.

COLLECTIVE SUPPORT IS KEY

At least 75 per cent (by value) of creditors (counting only those who actually take part in voting) need to give their consent for the CVA to be implemented and become legally binding. For this to happen, creditors need to be convinced that the company will be able to maintain the agreed repayments for the duration of the CVA. If there is any doubt over the viability of the company, it is highly likely that creditors will not vote in favour of the CVA.

If negotiated correctly, CVAs can be a positive solution for both creditors and the indebted company. The company is given the chance to continue trading and servicing its debts in an affordable manner while it returns to a position of profitability, while creditors – particularly unsecured creditors – often see a greater return on the amount owed to them through the CVA rather than if the company entered liquidation.

LIQUIDATION AND CLOSURE

The unfortunate fact is that sometimes, despite the best efforts of all involved, a company's problems take it beyond the point of rescue. When this is the case, placing the company into liquidation is often the best course of action for all concerned. This can be achieved through a formal director-initiated process known as a Creditors' Voluntary Liquidation (CVL).

UNDERSTANDING VOLUNTARY LIQUIDATION

A CVL facilitates the orderly shutdown of an insolvent company and is administered by a licensed insolvency practitioner who will adopt the role of the company's liquidator throughout the process. The appointed insolvency practitioner will be responsible for identifying and recovering company assets before realising the value of these for the benefit of outstanding creditors. There is a set order of payment priority for creditors during liquidation, with each class of creditors being paid in full (with the exception of 'prescribed part' creditors)

before funds can be allocated to the next class. Creditors are ranked as follows:

- secured creditors holding a fixed charge;
- preferential creditors – HMRC as secondary preferential creditor, ranking behind employee preferential claims;
- secured creditors with a floating charge;
- unsecured creditors; and
- shareholders.

Unsecured creditors typically make up a large proportion of a company's total creditors, with most trade creditors falling into this category. However, due to the low ranking they are given when it comes to distributions, they typically recover very little of the money they are owed when the insolvent company is placed into liquidation. The 'prescribed part' helps to increase the realisations to unsecured creditors by setting aside an amount from the sale of floating charge assets – such as stock, plant and machinery, vehicles, etc. – net of costs of the liquidation. 50 per cent of the first £10,000 realised from the sale of floating charge assets is set aside in this way, followed by 20 per cent of any further realisations up to £600,000.

COMPANY DEBTS AND LIQUIDATION

Once the insolvency practitioner has realised all available assets and distributed these to creditors, the liquidation will be complete and the company's name will be removed from the register held at Companies House at the point of dissolution. The company will then cease to exist as a legal entity, meaning any debt which remains outstanding at this point will be written off unless it has been personally guaranteed.

If a personal guarantee has been provided for any borrowing, this will crystalise at the point of liquidation, and the responsibility for repaying the outstanding balance will fall to the director (or the individual who signed the personal guarantee). If you are in this position, your insolvency practitioner will be able to talk you through the implications of this and what your options for repayment are.

FIVE THINGS YOU CAN DO RIGHT NOW

- Be aware of the impending signs of insolvency: the sooner you take action, the more options will be open to you to maximise your chances of saving the business.
- Seek professional advice early: having a trusted advisor you can turn to during times of financial distress is key.
- Maintain a dialogue with creditors during this time: they are more likely to be open to the idea of negotiating a payment plan if you are transparent about your situation and the problems you are facing.
- Conduct an insolvency test: if your outgoings exceed your income or your liabilities outweigh your assets, you are classed as cash flow or balance-sheet insolvent, respectively. Conducting this test on a regular basis can help determine your position.
- Understand your responsibilities: as the director of an insolvent company, you have certain legal duties to your creditors. If your company enters liquidation your conduct as director will become subject to investigation, so it is important you know your responsibilities and adhere to them.

10

UNDERSTANDING INSOLVENCY LAW AND PROCEDURES

BURNESS PAULL

Michael Thomson, *Partner*

Allana Sweeney, *Director*

In this chapter, we give a general overview of different types of insolvency procedures that are available in the UK. We also look at actions that an insolvency practitioner may use to challenge actions of the company in the run up to insolvency, pensions issues and the protection of supplies to companies in insolvency processes. Finally, we look at how creditors are paid in an insolvency and at restrictions that apply on restarting after insolvency.

UK INSOLVENCY PROCEDURES

ADMINISTRATION

Administration is a procedure whereby a company is given 'breathing space' under the protection of a statutory moratorium to allow it to be rescued, reorganised, or its assets realised. The administrator (a qualified insolvency practitioner) is appointed either by a court order, or by the filing of a set of forms at court where the appointment is made by the directors, the company itself or the holder of a floating charge (subject to the floating charge meeting a number of conditions such that it is recognised as a 'qualifying floating charge' for the purposes of insolvency legislation).

Administration can only be initiated for one of a number of statutory purposes. The first of these is the rescue of the company itself as a going concern. If that is not possible, the purpose must be to achieve a better result for creditors as a whole than would be likely in a winding up. If that is not possible, the purpose must be the return of monies to secured or preferential creditors. Unless the administrator is appointed by a qualifying floating charge holder, the company must be unable to pay its debts (on the basis of a cash flow or balance sheet test) as a prerequisite to the appointment of the administrator.

The executive powers of the directors of the company cease upon the appointment of the administrator. The administrator takes over the running of the company and its business and runs the administration in accordance with proposals that they put to creditors for their approval. Often, the administrator will sell the company's business and assets, and the company will be put into liquidation or dissolved afterwards, but occasionally, a company will be rescued through the process.

Typically, a company in financial difficulty will face considerable outside pressure from its creditors who will want to take steps to protect themselves should the company fail. However, this can prejudice the prospects of successfully rescuing the insolvent company or its business. Administration is designed to give a company breathing

space when it enters into the process, with the aim of rescuing the company or its business. Administration therefore provides the company with the benefit of a moratorium, preventing most creditors or other third parties from taking legal action against the company or its assets (unless the action is taken with the consent of the administrator or the permission of the court).

PRE-PACK ADMINISTRATIONS

A 'pre-pack' administration takes place when a company is put into administration and, immediately upon the appointment of the administrator, its business and/or assets are sold by the administrator in a sale that was arranged prior to the administrator's appointment. Often a pre-pack involves the sale of a company's business on a going concern basis.

For the following reasons, pre-packs can be useful tools for preserving value in a business, minimising the erosion of value in a business due to a seller's insolvency, reducing the costs of the administration process, and therefore promoting a better return for creditors in the insolvency:

- A pre-pack sale can bring about the swift and smooth transfer of a business to a new owner, compared to a sale negotiated for a period of time after the insolvent owner goes into administration.
- Pre-packs can save more jobs than an administration that attempts to continue to trade the business. A trading administration may result in redundancies having to be made by the administrator upon their appointment or while they trade.
- Pre-packs can mitigate the loss of confidence of a business' suppliers, customers and employees caused by insolvency proceedings.
- If funding is not available for an administrator to trade the business, in the absence of being able to execute a pre-pack sale, the alternative is liquidation and the immediate end to the company's business.

Pre-packs can be controversial, often owing to the perception that they allow directors to sell a company's assets to a connected party without proper marketing and with no warning to the company's unsecured creditors. Regulations and practice statements attempt to address this by regulating how insolvency practitioners conduct pre-pack sales. In cases where an administrator makes a substantial disposal of a company's business or assets to a connected party within the first eight weeks of administration, the administrator must first either (a) obtain approval of the transaction from creditors, or (b) have received and considered a report obtained by the connected person from an independent evaluator on the reasonableness of the proposed disposal.

COMPANY VOLUNTARY ARRANGEMENT (CVA)

A company voluntary arrangement (CVA) is a procedure that aims to help a company to address its financial difficulties by compromising its debts with creditors. The company proposes a CVA to its creditors, and it becomes binding if it is approved by an appropriate majority of creditors. Unless they consent, a CVA does not bind secured or preferential creditors (for more detail on these terms, see How are Creditors Paid in an Insolvency?). A CVA aims to avoid insolvency and promote the survival of the company.

During the CVA, the directors continue to be involved in running the company. CVAs are common in hospitality, retail and leisure: industries where distressed businesses use them to compromise amounts that they owe to (often large numbers of) landlord creditors.

> A CVA aims to avoid insolvency and promote the survival of the company.

PART A1 MORATORIUM

A Part A1 moratorium allows the directors of a financially distressed company to apply for breathing space from enforcement action by certain types of creditors in order to attempt to rescue the company and avoid insolvency. The moratorium is only available to companies where the proposed monitor will certify that the moratorium would likely result in the rescue of that entity. The directors must also certify that

the company is currently or likely to become unable to pay its debts as they fall due. The moratorium initially lasts for twenty business days but may be extended and can last up to forty business days without creditor or court consent. With creditor consent, the moratorium can carry on for up to a year, or longer with a court order. The company remains under the control of the directors, but their actions are reviewed by a monitor (who is a qualified insolvency practitioner). During the moratorium, creditors are precluded from taking action against the company. A moratorium does not involve the compromise of creditor claims or the realisation of assets for the benefit of creditors.

SCHEME OF ARRANGEMENT

A scheme of arrangement is a compromise or arrangement with creditors (or any class of creditors) or members (or any class of members) that is binding if the appropriate majorities of each class of creditors/members agree. Unlike a CVA, a scheme of arrangement must be sanctioned by the court. When sanctioned by the relevant majority in each class of creditors/ members and the court, the scheme will bind all members and creditors. A company does not need to be in financial difficulty to use a scheme of arrangement, but a scheme is often used as a restructuring tool for companies in distress.

It might also be used alongside administration wherein the moratorium in administration gives the company breathing space to agree to any proposals with creditors for the scheme of arrangement.

> A company does not need to be in financial difficulty to use a scheme of arrangement, but a scheme is often used as a restructuring tool for companies in distress.

PART 26A RESTRUCTURING PLAN

A Part 26A restructuring plan is similar to a scheme of arrangement but is intended only for companies in financial difficulties. Unlike schemes of arrangement, there is no requirement that the plan be approved by a majority of the creditors in each class. A Part 26A restructuring plan allows for 'cross-class cram down', meaning that a dissenting class of voters cannot block the plan if the court is satisfied that:

- none of the members of the dissenting class would be worse off than they would be if the plan were not sanctioned (for example, if the company were to enter into liquidation in the absence of the sanction of the restructuring plan), known as the 'relevant alternative'; and
- at least one class (whether creditors or members) who would receive a payment under the restructuring plan, or have a genuine economic interest in the company in the event of the relevant alternative, votes in favour of the plan.

WINDING UP OR LIQUIDATION

Liquidation or 'winding up' involves the appointment of a liquidator (who must be an insolvency practitioner) who collects in, sells the company's assets, distributes the resulting money, and, at the end of the process, dissolves the company. Liquidations can be:

- compulsory, by order of the court (following a court petition, often filed by a creditor on the grounds that the company is unable to pay its debts); or
- voluntary, by resolution of the company. The voluntary liquidation of an insolvent company, known as a creditors' voluntary liquidation, begins by the members passing a special resolution. Creditors are given more control over the process, including control over the choice of liquidator, than in a compulsory liquidation. It is also possible for solvent companies to enter into voluntary liquidation, known as a members' voluntary liquidation, where the directors give a statutory declaration of solvency to the effect that the company will be able to pay all its debts in full within 12 months. As the debts will be paid in full, shareholders have control over the process, including the choice of liquidator.

ADMINISTRATIVE RECEIVERSHIP

Administrative receivership is a remedy for a secured creditor who has a floating charge over the company's assets and, including that floating charge, fixed or floating security over all or substantially all of the company's assets. It allows the charge holder to appoint an administrative receiver (who must be a qualified insolvency practitioner) to manage and sell the company's business and assets. The powers of the administrative receiver are a mix of contractual powers (granted under the security, usually called a debenture, containing the charges) and powers conferred by law. If the floating charge was created on or after 15 September 2003, administrative receivership is no longer available (except in limited circumstances as a remedy to enforce that security). For this reason, administrative receiverships are decreasingly common.

POWERS TO CHALLENGE TRANSACTIONS IN THE RUN UP TO INSOLVENCY

When a company has entered administration or liquidation, transactions entered into by the company within certain timeframes in the run up to the insolvency may be challenged by the liquidator, administrator and, in some instances, creditors. These are often referred to as challengeable or reviewable transactions. The rationale of the power to challenge transactions is to help achieve the best possible return to the creditors of the insolvent company. It also promotes the principle that the available assets of a company in administration or liquidation should be shared equally among its unsecured creditors. In most cases, the challenge involves making an application to court. If the challenge succeeds, the court has a wide discretion to make an order undoing the effect of the transaction (for example, by ordering the return of assets to the insolvent company). It is also possible for an administrator/liquidator to assign certain types of these challenges to third parties. Examples of transactions that may give rise to challenges are:

- when a company enters into a transaction at an undervalue if the company was at the time of the transaction (or as a result of the transaction became) unable to pay its debts as they fell due;
- when a company does something that puts a creditor in a better position than it would otherwise have been in if the company went into administration or liquidation; and
- when a floating charge is granted to an unconnected party within 12 months of a company's insolvency and no money is paid or goods or services are supplied in exchange for the floating charge at the same time as or after its creation.

PENSIONS ISSUES IN PRE-PACKS OF BUSINESS AND ASSETS OF COMPANIES WITH DEFINED BENEFIT PENSION SCHEMES

A pre-pack transfers an insolvent company's business and assets to a purchaser but all liabilities, including any debts due to a pension scheme, remain with the insolvent company. If a company deliberately uses a pre-pack to avoid a pension scheme liability, the Pensions Regulator can investigate this and require anyone connected or associated with the insolvent company to contribute to the pension scheme in the company's place.

In the UK, the Pension Protection Fund (PPF) pays compensation to members of eligible defined benefit pension schemes when an employer goes into certain types of insolvency processes, including administration, and where there are insufficient assets in the pension scheme. When a pre-pack involves an underfunded defined benefit scheme eligible to enter the PPF, it is in the interests of the PPF to ensure the pre-pack is dealt with as effectively and transparently as possible. The PPF has issued guidance making clear that it expects insolvency practitioners considering a pre-pack to involve and correspond with the PPF as early as possible where there is an underfunded defined benefit pension scheme.

If insolvency practitioners fail to do so, and the pre-pack subsequently results in the scheme entering the PPF, the PPF may seek to nominate

an alternative insolvency practitioner following the administration (in order that they can independently review the background to the pre-pack and the actions of the directors and administrators).

THE PROTECTION OF SUPPLIES TO COMPANIES IN INSOLVENCY PROCESSES

In some insolvencies, the insolvency practitioner will attempt to continue to trade during the insolvency procedure. The company will therefore need continued access to supplies (such as electricity, raw materials or other goods or services). However, supply contracts will often try to give the supplier a right to terminate contractual supply arrangements by virtue of the customer's insolvency. Legislative provisions prevent certain contracts from being terminated by a supplier because a company goes into an insolvency process. They ensure that supplies are not cut off when a company becomes subject to an insolvency process due to a supplier refusing to supply, terminating the contract, or making other adverse changes to the terms on which they are prepared to continue supplying. The supplier will be paid for the supplies used by the company during the period of the insolvency practitioner's appointment.

HOW CREDITORS ARE PAID IN AN INSOLVENCY

The money generated from a sale by an insolvency practitioner of the assets of an insolvent company is used to meet the claims of creditors. Legislation ranks creditors in different classes. These classes of creditors are paid in a statutory order of ranking. When one class of creditor claim has been repaid in full, the remaining funds are applied to satisfy the claims of creditors in the next class until no further funds are available. Ordinarily, money is distributed in proportion to the debts due to each creditor within a class. The statutory order of ranking is as follows:

Order of payment in insolvency

1. Funds generated from the sale of assets subject to fixed charges are paid to the fixed charge holders (after deducting costs of realisation, which are agreed between the insolvency practitioner and the fixed charge holders).
2. Where there has been a Part A1 moratorium but the company then enters administration or liquidation within 12 weeks of the end of the moratorium, any remaining funds are used to pay certain debts incurred prior to and during the moratorium that are given priority ranking in insolvency.
3. Any remaining funds are used to pay the remuneration and expenses of the insolvency practitioner.
4. Any remaining funds are used to pay 'preferential creditors'. Preferential creditors' claims include some employee claims, certain contributions to pension schemes and some tax liabilities owing to HMRC.
5. Funds generated from the sale of assets subject to floating charges are used to pay the 'prescribed part'. The prescribed part is a part of the proceeds that comes from realising the assets covered by a floating charge, which must be set aside and made available to satisfy unsecured debts. It is calculated as a percentage of the value of the company's property, which is subject to a floating charge. The percentage value is 50 per cent of the first £10,000 of net floating charge realisations plus 20 per cent of anything after that, subject to a maximum prescribed part of £800,000 if the first ranking floating charge granted by the company was created on or after 6 April 2020, or £600,000 if created before then.
6. Funds generated from the sale of assets subject to floating charges are used to pay the holders of floating charges.
7. Any remaining funds are used to pay unsecured creditors.
8. Any remaining funds are used to pay shareholders.

RESTRICTIONS ON RESTARTING AFTER INSOLVENCY

A director of a company that has entered into an insolvency process can become a director of a new company unless they are subject to a disqualification order or are in bankruptcy. A disqualified or bankrupt person can obtain leave of the court to be a director.

The use of the name or trading name of a company that has gone into insolvent liquidation is subject to restrictions. Anyone who was a director or shadow director within the 12 months prior to liquidation is prohibited from being a director or otherwise being involved in the business of a company with the same or similar name as the liquidated company for five years from the liquidation (unless they satisfy one of a number of exceptions). Breaching this prohibition gives rise to imprisonment or a fine in addition to potential personal liability for the debts incurred by the company while using the prohibited name.

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11

THRIVING IN THE NEW ECONOMY

RODIN GENOFF & ASSOCIATES

Rodin Genoff, *Managing Director*

Narelle Hooper, *Editor in Chief, Company Director Magazine*

'I can mash-potato... I can do the twist... Now tell me baby...do you like it like this?' In December 2020, Boston Dynamics robots Atlas, Spot and Handle lifted spirits amidst a relentless global pandemic jiving to The Contours' 1960s hit 'Do You Love Me,' while simultaneously sending chills up the spine.[1] The result of a collaboration between engineers, dancers and choreographer, Monica Thomas, it wasn't just that the robots could cut the moves better than many of us humans could.[2] The deft combination of art, machine and algorithmic capability revealed how far technology had come in a short space of time. In the process, it led to rapid improvements in the strength, capability and endurance of the oddly endearing robots. Spot the Robodog is on the job from diagnosing COVID-19 patients to inspecting oil platforms and nuclear plants to monitoring progress on real ones in agriculture production.[3] A majority stake in the Massachusetts Institute of Technology offshoot was sold to South Korean carmaker Hyundai in mid-2021, valuing it at more than US $1 billion.

COVID-19 has driven SMEs to make transformative digital leaps too. Though often stressful, this has given them new capability and confidence to grapple with the ubiquitous digital connectivity that is known as Industry 4.0. Likewise, we will need to make similar leaps in responding to other existential business risks too – climate change and the impact of automation on society.

Clearly there is a lot at stake for everyone, from the community to businesses. In this chapter, we explore six themes that will help your company seize new opportunities and mitigate risks. We also show you how to ride the momentum of the new economy.

Notwithstanding the relentless march of digitalisation and a global pandemic, this is a good time to pause and reassess. It is a time of great, new opportunity.

INDUSTRY 4.0

We are entering an exciting new industrial era that sees the convergence of smart devices, robotics, material sciences, genomics and biotech. We have seen a glimpse of this through the breakthrough with Pfizer and Moderna vaccines in the fight against COVID-19, based on a technology not previously used in therapeutics. The messenger ribonucleic acid (MRNA) is manufactured through a chemical process rather than a biological one and can be quickly redesigned and mass produced unlike traditional vaccines which can take years to perfect.

Convergence is also accelerating digitalisation. The rollout of 5G mobile communication on our phones and other devices is the manifestation of this. The shrinking price tag on various technologies, which are becoming ever more powerful, has led to an era in which devices, data analytics and artificial intelligence are integrated seamlessly.

'By 2030, Stanford researchers estimate 500 billion connected devices (each housing sensors), which, according to research conducted by Accenture, translates into a $14.2 trillion dollar economy,' explain Peter Diamandis and Steven Kotler in *The Future is Faster than You Think* (2020).[4]

The world's biggest engineering and production companies, including Siemens and Bosch, are already using the twin Industry 4.0 pillars of automation and efficiency to corner new markets.

However, many companies have yet to seize these opportunities and are still operating with legacy automation processes and IT systems, making them slower and less cost-efficient than their competitors.

And yet, the prize in this brave new future of work is not all about breakthrough technology. It is about how we apply human capital. Michael Priddis, founder of the artificial intelligence analytics platform Faethm,[5] has been modelling the impacts of emerging technologies on workforces in Germany, the US and Australia.[6] While there is plenty of fear-mongering, the reality is that the situation is far more nuanced: 'Whilst technology will eliminate the need for people in certain roles, it will also create a number of new jobs that need to be filled by humans,' he and colleagues wrote in a recent blog.[6]

This work is helping organisations pave the way for Industry 5.0 – people working alongside robots and 'smart devices' that are capable of machine learning. It is ushering in a new era of personalisation defined by human-to-machine interface and real time sharing of information across the Internet of Things.

However, these transformative opportunities also come with a significant increase in terms of organisational and systemic risk. With global cyber opportunity comes a rising cyber arms race. Cyberattacks from bad actors are expanding the definition of critical infrastructure from the traditional power, water and sewerage to defence, transport and communications. Financial services, markets and governments are responding with tightening legislation. At the corporate level, US tech giants ranging from Apple, IBM, Google and Microsoft have committed billions to fight cybercrime in coming years.[7]

THE RENEWABLES REVOLUTION

With interest rates at historic lows, massive government stimulus, the transition to low carbon economic infrastructure and the scale and pace of changes needed to achieve a net-zero emissions by 2050, this is an exciting time for business owners to invest in the future.

> The signals are loud and clear, and momentum is building as governments and businesses around the world take action.

In November 2020, the UK Government announced a £12 billion 10 point plan, named the Green Industrial Revolution,[8] with the aim of creating 250,000 jobs by 2030. A month later, the European Union agreed to a €672 billion COVID-19 recovery fund, 37 per cent of which must be invested in projects that support its climate objectives.[9] In August 2021, this was followed by a rare bipartisan act by Democrats and Republicans to pass US President Joe Biden's $US 1 trillion infrastructure package[10] to renew the country's declining transport and utilities systems, install electric vehicle charging stations and other public works to embed sustainability. And along with the European Union, the US is looking at imposing carbon tariffs as a regulatory stick to drive the agenda.[11]

The signals are loud and clear, and momentum is building as governments and businesses around the world take action. In August 2021,

the sixth Intergovernmental Panel on Climate Change Report issued a code red warning that climate change represents an existential threat to humanity and of the imperative for urgent collective action.[12]

In short, the energy transition is a once-in-a-century industrial and economic paradigm shift. Grappling with the systemic issues forever disrupts how you do business.

Companies of every size that position themselves ahead of these changes will benefit – the rest will be left behind.

Research by the British Chamber of Commerce (BCC) in 2021 warns that only 1 in 10 businesses measure their carbon footprint. 'This research is a real eye-opener and shows just how big a challenge the UK's net zero target is,' says Shevaun Haviland, Director General of the BCC. Do not let your company be the one that gets caught short.[13]

OPPORTUNITY IN THE NEW ECONOMY

Yet, there is a way to go. What we are seeing is an existential tussle between 'business as usual' – which we now see as an 'old economy' way of doing things – and the 'new economy.'

Old economy companies, CEOs and investors continue to aspire to profit targets at any cost. Look no further than the destruction in 2020 by UK and Australian listed global miner Rio Tinto of Jukaan Gorge in Western Australia, containing the world's oldest artifacts painted by the world's oldest continuous culture, Australia's first nation peoples, in order to mine just $135 million in ore.[14]

What is clear is that most companies are not deliberately setting out to cause harm; they are just doing business as usual. But that is no longer going to cut it. It is also a long road to effect change.

> What we are seeing is an existential tussle between 'business as usual' – which we now see as an 'old economy' way of doing things – and the 'new economy.'

For example, Unilever CEO Paul Polman drew a line in the sand in 2009 when he abolished quarterly returns. The following year, the company introduced a long-term Sustainable Living Plan, declaring its intention of decoupling growth from its environmental footprint and increasing positive social impact. As Polman described it, it was 'creating value through values, versus pursuit of value at any cost.'[15]

In doing so, he demonstrated the 'new economy' mindset. It is one inspired by inclusion, shared values and creating long term social and natural capital as well as financial value.

Despite some investors actively opposing the approach and fearing the impact on performance, a decade on, Unilever has continued to thrive.[16] Among recent initiatives, it has also pledged $2.1 billion to fast-track sustainable practices amongst its suppliers and support local communities, accelerating gender equality through its value chain and moving to zero waste. Partnering with Google Cloud, it can now pinpoint satellite images of deforestation and monitor the data to verify supplier sustainability.

Polman departed in July 2019, but the company board and management have held the line and prospered.

STRENGTH IN DIVERSITY

One of the enablers of Unilever's transformation has been a policy embedding gender balance in its boardroom and management, which it achieved in 2020.[17] Polman's successor, Alan Jope, said: 'Women's equality is the single greatest unlock for social and economic development globally, and having a gender-balanced workforce should be a given, not something that we aspire to.'

Likewise, global miner BHP has set an aspiration of gender balance across its workforce of 80,000 by 2025.[18] Chair Ken MacKenzie told *Company Director Magazine* in August 2021, 'Our data shows inclusive and diverse workforces outperform on safety, productivity and wellbeing.'

Investors are recognising the superior performance benefits of companies with

gender balanced teams.[19] The key is psychological safety, which in turn allows for greater experimentation. As we showed in our 2015 book *New Women, New Men, New Economy*, organisations with gender balance are twice as innovative and deliver superior financial performance.[20] Large pension funds are also demanding it of companies they invest in.[21]

THE CIRCULAR ECONOMY

There is something else that new economy companies are doing. They are profoundly changing where they look for new value by adopting 'circular economy' or 'closed loop' practices. They are retooling to design out waste and transform it into a valuable input.

The defining feature of the circular economy is about finding ways to create value without maxing out our fragile and limited environmental resources. If it is not obvious why this is important, watch the new David Attenborough film *Breaking Boundaries* on Netflix.[22]

> Going circular means rethinking your product and services design and business models.

Currently, we operate a linear, extractive economy. We take, we make and we create waste. Valuable materials are extracted from the environment, used once, then thrown in the dustbin or, worse, left to pollute our food chains and waterways.

Going circular means rethinking your product and services design and business models. It applies three key principles: designing out waste and pollution, keeping products and materials in use and regenerating natural systems. From this, you can create new generation products and services that are more appealing to customers, cheaper to produce and deliver and less at risk from litigation and regulatory change.

Nordic countries such as Finland have been early adopters of this approach and over the past decade the UK based Ellen MacArthur Foundation has pioneered its global uptake by business and government.[23]

In July 2021, the UK based Aldersgate Group, chaired by former British prime minister Theresa May, released 'Closing the Loop: time to crack on with resource efficiency,' which estimated that adoption of circular practices would create 517,000 new jobs by 2030.[24] It would also contribute £9.1 billion to the UK's bottom line and deliver 80 per cent of the UK's next Carbon Budget.

It does not matter which industry you are in – chemistry, design, manufacturing, engineering, fabrication, IT, venture capitalism, marketing – what an exciting time to be in business. It opens up the capacity for the creation of new business models – product-as-a-service, sharing platforms – and will also put you on the front foot in meeting changing community expectations.

A powerful example is the UK's fashion icon and sustainability pioneer Stella McCartney, who revolutionised how clothes are sourced, worn, shared and re-used.[25] Uncharacteristically for a fashion label, Stella McCartney sinks significant resources into research and development to create new yarns from recycled materials, even turning mushroom waste into leather-look fashion accessories.

Equally inspiring is the UK's Presca Sportswear, a thriving circular economy start-up now six years old.[26] 'We're proud to be the world's first climate positive sportswear company,' explains Presca co-founder and CEO Rob Webbon. A scientist by training, Webbon's collaborations with fabric suppliers have turned 108,594 plastic bottles into high-tech sports fabric. 'We're aiming for all our new ranges to be fully recyclable by 2022,' he says.

From circular start-ups to global giants, the weight of investor money is driving demands for greater accountability and transparency and a change of the guard.

In 2020, Morningstar said investor demand to invest in funds which focused on environmental,

social and governance (ESG) issues jumped during COVID-19, driving assets under management up 29 per cent in the fourth quarter to nearly $1.7 trillion.[27]

Investors and regulators are demanding organisations provide greater transparency and accountability for their production practices and what happens in their supply chains, and alert for potential greenwashing.

Awareness of modern slavery risks and carbon footprints are powerful drivers of change. There is a saying in the human rights movement — 'Once you know, you can't un-know,' says Dr David Cooke, chair of the UN Global Compact Network Australia, a former CEO of Konica Minolta Australia.

ECOSYSTEMS THINKING

Organisation for Economic Co-operation and Development (OECD) research has long shown how business networks drive innovation. Twenty years of working with SMEs globally has shown us the importance of adopting ecosystem thinking to maximise the benefits for SMEs.

We have mapped industrial ecosystems such as advanced manufacturing, bio-economy and renewable energy, identifying connectivity between SMEs that can be harnessed to deliver new products and services that in turn allow companies to unlock new business opportunities. Put simply, companies that connect with other companies and organisations outside of their own industry can fast-track innovation and speed up commercialisation, benefiting the entire ecosystem.

> Twenty years of working with SMEs globally has shown us the importance of adopting ecosystem thinking to maximise the benefits for SMEs.

One example is a project in Sweden's industrial heartland to develop Region Dalarna's bio-economy ecosystem. Through a strategic partnership between two dynamic enterprises, Mondo Architects and Structor Engineering in the small city of Falun, the combined strengths in industrial design and engineering unlocked projects that were previously out of reach to both companies in both scale and complexity. Together, they could punch above their weight.

The partners then joined forces with Fiskarhedenvillan, Sweden's second largest home building company. Together, the three businesses have raised capital, shared know-how and realised their dream of designing and building the next generation of sustainable residential homes. 'Without this project and an ecosystem thinking mindset, this project would never have gone ahead,' says Gunnar Jönsson, Fiskarhedenvillan CEO.

In the meantime, there is another exciting chapter ahead. We have gone on to work with Mondo and Structor's business ecosystem to establish a network of some 30 companies led by female CEOs named Women Building Sweden. It's tasked with creating new local business and investment opportunities in their region. 'We've already secured a women's construction team to build our house with Fiskarhedenvillan. Our network of amazing women has only just got going,' says Gabriella Hagman, CEO of Mondo Architects.

CONCLUSION

It may be tempting to wait till things settle and there is less uncertainty. It is sobering to reflect that not acting is a choice in itself. Given what is at stake, the risks of not acting are greater.

Where to start? As the World Economic Forum noted in 2020, urging a Great Reset for capitalism to respond to the twin crises of the pandemic and climate change, 'humanity has no shortage of creativity, imagination and problem-solving ability.'[28]

'What we need more of is responsible leadership that inspires collaboration, sympathy and vision on local and global levels for humanity to land new and safe heights.'

We invite you to join us to become 'architects of difficult solutions' by beginning the conversation. There is no better time than now to get started.

KEY TAKEAWAYS

- **INDUSTRY 4.0**

  As you seek to digitise your business, focus on ways to put human connection and service in, not just using technology to take costs out. Ensure you have a comprehensive cyber security plan in place and that all employees are appropriately aware and trained. For further information on the future of work and automation go to **Faethm**[29] and for cyber security go to the **National Cyber Security Centre**.[30]

- **RENEWABLES REVOLUTION**

  Look for industry resources to help guide you. There is help out there from the British Chamber of Commerce and government. **Chapter Zero**[31] and the **SME Climate Hub** provide useful support to make the transition to zero carbon.[32]

- **NEW ECONOMY OPPORTUNITY**

  The Sustainable Development Goals make a good framework and guide to rethink business strategy for organisations of all sizes. Go to **SDGs.UN.org**.[33]

- **STRENGTH IN DIVERSITY**

  The **Champions of Change** coalition of business leaders has good resources to guide organisations.[34] And, when you're employing someone new, a good first step is to switch off your autopilot and check in on your unconscious bias (we all have them). Project Implicit's **IAT** (implicit assumptions test) is a good place to start.[35]

- **CIRCULAR ECONOMY**

  The **Ellen MacArthur Foundation**[36] and **UN Global Compact Network** have practical information, case studies and global resources on circular economy practices and responding to modern slavery issues.[37]

- **ECOSYSTEMS THINKING**

  By reaching out to market connections and tapping into the know-how and financial resources of trusted companies and other organisations in your business ecosystem, you have project enablers at your very fingertips. ***New Women, New Men, New Economy*** outlines examples.[38]

Whether it is finding a new way to deliver a traditional product or service, or taking the essence of what you do today and turning into something entirely new, opportunities abound.

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BUILDING FINANCIAL RESILIENCE

BANK OF SCOTLAND

Andy Fish, *Director, Invoice Finance and Asset Based Lending*

David Weatherhead, *Head of SME and Mid Corporate Trade and Working Capital Sales*

When businesses emerge from a challenging period, taking steps to avoid finding themselves in the same situation again should be top priority, so building financial resilience is key.

WHAT IS FINANCIAL RESILIENCE?

The COVID-19 pandemic put the idea of financial resilience firmly under the spotlight as the most resilient businesses were able to adapt quickly when the landscape changed seemingly overnight.

Put simply, businesses which are financially resilient don't just survive; they're positioned to grow and thrive. They're ready for all scenarios, good and bad. If conditions are favourable, they're able to capitalise and create new opportunities, or, if they're faced with challenging times, they're able to quickly consolidate and move on.

Some key indicators that a business is financially resilient include:

- Being able to plan ahead and articulate what your future looks like, not just in terms of financials, but also strategy and how the business operates.
- Being agile and able to adapt and evolve plans based on rapidly changing market conditions and diversify into new markets and revenue streams as needed.
- Having a strong understanding of your end-to-end working capital cycle and being able to utilise your balance sheet effectively to support growth.
- Being clear on your role within the supply chain, in relation to both customers and suppliers, and understanding how any issues that affect the chain will ultimately impact your business. This is even more pertinent when global supply chains are facing disruption.
- Having a quality management team with a strong understanding of the financials and the overall business strategy and who are also visionary thinkers.
- Having a culture of 'healthy challenge'. If everyone in your business is happy to maintain the status quo, you may struggle to adapt and grow in the long term. You need people willing to put brave ideas forward and question whether plans need to be adapted.

So, how can businesses reach this point? As well as understanding your marketplace and the position of your business within it, if you want to be truly financially resilient, it is essential that you:

- understand your end-to-end working capital cycle, from order placed to debtor receipts; and
- develop a strong supply chain.

UNDERSTANDING YOUR WORKING CAPITAL CYCLE

Your working capital cycle is the amount of time it takes to convert your net current assets and current liabilities into cash. A strong working capital cycle is essential if you're going to be able to meet the day-to-day needs of your business and have resources available to invest in growth (see Figure 1).

You can easily work out the length of your working capital cycle using the below formula:

stock days + receivable days – payable days = number of days in your working capital cycle

Stock days are the time it takes, on average, to sell your stock.

Receivable days refer to the number of days your debtors take to pay once you've invoiced.

Payable days are the number of days it takes you to pay your suppliers.

So, for example, if it takes you 90 days to shift your stock and 90 days to pay your suppliers, and your debtors pay you in 21 days, your working capital cycle is:

90 + 21 – 90 = 21 days

There are a variety of factors that can affect your working capital cycle including:

- *Delayed payments*: If you've paid your suppliers according to your usual terms *or earlier* but your debtors' payments are delayed, your working capital cycle is prolonged and your cash position will be affected.
- *Unfavourable payment terms*: To secure a deal, your sales team may agree to longer payment terms, increasing your working capital cycle.
- *Supply chain delays*: For example, if freight journeys are delayed, it could take 10–15 days longer to receive your stock, which adds to your stock days if you've already paid.
- *Fluctuations in demand*: If demand falls, for whatever reason, you may find your cash is tied up in stock.

It's important to be aware of all the things that can affect your working capital cycle so you can take the most appropriate action to improve it.

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IMPROVING YOUR WORKING CAPITAL CYCLE

- *Establish regular monitoring*: your working capital cycle can change significantly, so it's important to keep on top of it with regular monitoring. Regularly review your stock, debtor and creditor management reports, as well as your 13-week rolling cash-flow forecast so you can see your whole working-capital picture. You can use publicly available information to benchmark against your competitors. You might also find it useful to use accountancy software to help manage future cashflow. Bank of Scotland's Business Finance Assistant can help with accurate cash-flow forecasting by highlighting predicted shortfalls in advance.[1]
- *Renegotiate your payment terms*: if your working capital cycle is longer than you'd like, can you renegotiate payment terms with either your customers or suppliers? For example, suppliers may be willing to accept longer payment terms if you commit to a certain level of orders. Make sure all your sales team members are aware of the impact on working capital in sales negotiations.
- *Improve stock management*: slow-moving stock or a build-up of stock can have a huge impact on your working capital, so it's important to have someone within the

business monitoring how demand is shifting and managing your inventory accordingly. If you're holding onto stock for longer, you're also more vulnerable to fluctuating costs on the global market. You need to have measures in place to hedge against this (e.g. can you pass costs on to the end customer?). It's important to liquidate old stock regularly – marketing pushes or offering discounts can help reduce your inventory days, or if you usually sell business-to-business, why not try selling business-to-consumer at a higher margin via a pop-up shop or ecommerce?

- *Proactively chase debts*: make sure you always invoice on time and chase up outstanding debts. Protect against the risk of late payment by using credit software to check the strength of a new customer's business before offering credit terms. It's important to appreciate the pandemic has had long-term impacts for many businesses, including your customers.
- *Stay on top of market developments*: understanding what's going on in your market and the wider economy can help you predict how your working capital might be affected and take steps to mitigate it. For example, if there are labour shortages or supply issues around particular materials, your stock may be delayed.
- *Stress-test your cycle*: it's impossible to anticipate every event which could affect your working capital. Take the Suez Canal blockage for example. It's important to stress-test your cycle and see how it would be altered if a key customer declared insolvency or deliveries of a key component were significantly delayed. What tactical initiatives could you deploy to minimise risk in these scenarios? How might your longer-term strategy have to be adapted? If you've worked out your cycle based on the worst-case scenario, you'll naturally build a bit of flex into it.

Even taking all these steps, it can still be challenging to maintain an optimal level of working capital. However, being proactive and understanding your cycle can at least prevent overtrading – where you have insufficient working capital to support your business activities – or overcapitalisation – where you have too much available working capital, and your business isn't operating efficiently as a result.

FINANCIAL PRODUCTS AND TOOLS TO HELP YOU MANAGE YOUR WORKING CAPITAL

There are a number of financial products and tools available which can help you manage your working capital cycle and mitigate any potential risks, including:

- *Invoice Finance*: Invoice Discounting and Invoice Factoring can help you bridge the gap between invoice generation and payment by releasing funds from your unpaid invoices, giving you greater financial flexibility and boosting your working capital cycle.[2]
- *Commercial Cards*: Most commercial cards offer a period of interest-free credit, allowing you to meet creditors' payment terms while being able to maintain your cash position.[3]
- *Letters of Credit*: Letters of Credit give you reassurance that payment will be made to you as a seller, providing all the terms and conditions are met. This is especially useful if you are dealing with new customers and/or markets.
- *Trade finance*: The time between the start and completion of a transaction is often longer when you are trading internationally. Pre-shipment, Post-shipment or Import/ Export Finance can help you manage working capital effectively during the trade cycle and ensure you have sufficient financial assistance in place at each stage.[4]

These products can be used separately or together to create a seamless scenario of trade loans repaid by invoice discounting and invoice discounting repaid ultimately by trade receipts, all while maintaining the ability to maintain turnover and underpin growth.

> The key is to understand your working capital cycle and the points at which you may struggle.

Driving efficiencies within your working capital cycle

TRADE RECEIVABLES DAYS + INVENTORY DAYS – TRADE PAYABLES DAYS = CASH CONVERSION CYCLE

Understanding the trade cycle is key to understanding where working capital problems may occur. This is often illustrated by the Cash Conversion Cycle and is central to the overall health and efficiency of your business.

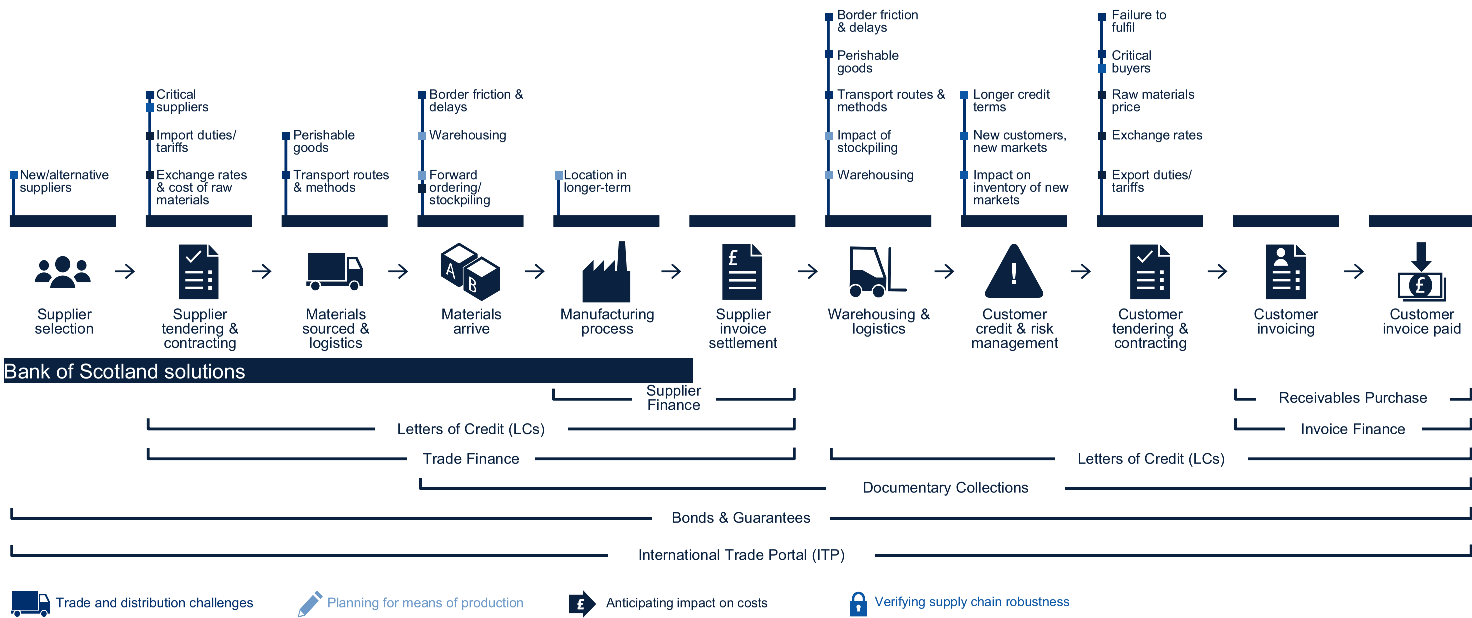

FIGURE 1. Driving efficiencies within your working capital cycle

The key is to understand your working capital cycle and the points at which you may struggle, then speak to your bank who can help you interrogate your supply chain and identify the right solution, or solutions, for your business.

BANK OF SCOTLAND'S WORKING CAPITAL MANAGEMENT TOOL

Bank of Scotland's Working Capital Management Tool can help businesses quickly calculate the capital tied up within their working capital cycle.

It can be used to benchmark competitor sales, margins, debtor days, creditor days, stock days, cash conversion cycles and funding requirements.

Our team can run various scenarios to help you quickly calculate the effects of growing or reducing sales or altering terms of trade, and we can discuss any additional financing which may be required.

Speak to your Business Manager for more information.

BANK OF SCOTLAND'S BUSINESS FINANCE ASSISTANT

Bank of Scotland's Business Finance Assistant accountancy software can help with working capital management, enabling you to track and chase unpaid invoices, as well as cash-flow forecasting.

See more about Business Finance Assistant

DEVELOPING A STRONG SUPPLY CHAIN

Between Brexit and the COVID-19 pandemic, supply chains have come under an immense amount of pressure, highlighting just how big a role a strong supply chain plays in being resilient and able to adapt and grow.

UNDERSTAND YOUR PLACE IN THE CHAIN

Where does your business fit in the overall supply chain? Knowing this can help you understand what challenges you face and steps you may need to take to prepare. For example, if you're quite high up in the supply chain, such as a seat manufacturer supplying a large car manufacturer, everyone else supplying the components that make your products has the potential to affect your business if they fail. It's also worth understanding your size in relation to the rest of the supply chain. How much leverage do you have with your suppliers? Are they dealing with larger companies who can dictate the terms of the supply and potentially leave you vulnerable?

MAINTAIN STRONG LINES OF COMMUNICATION

It's important to have a very open and honest dialogue with your supply chain because, ultimately, you need to know if they are experiencing any issues that are going to impact your business.

You need to build trust by proactively highlighting any issues with your suppliers so they can take steps to prepare.

And it goes both ways. You need to build trust by proactively highlighting any issues with your suppliers so they can take steps to prepare. Over time you'll build up a clear understanding of what your supply chain needs to function well and what factors typically affect it, enabling you to take steps to mitigate any risks to your business and support your supply chain.

CONSIDER DIVERSIFICATION

Are you over-reliant on one supplier? What happens if your supply chain fails? It's important to always have a plan B, and diversifying your sourcing bases and partners means you're less likely to suffer if a particular global market is facing issues or a key supplier goes bust. Diversifying your supply chain not only prepares you for disruption; it can also open opportunities in new markets and with new audiences you wouldn't have encountered otherwise.

PRIORITISE SUSTAINABILITY

Customers and investors are increasingly interested in businesses' sustainability credentials. Taking steps to make your supply chain greener and more sustainable can make it more resilient and ensure you're able to capitalise on the growing demand for eco-friendly and ethical products. You may also find that, as shareholders place a greater emphasis on green activity, if you're not taking steps to be more sustainable, your place in the supply chain could come under threat.

It goes back to having that market awareness – knowing what your consumers want, knowing how the world and trends are changing and being ready to adapt in response. And once you have a plan in place, consider the implications it will have for your working capital.

MAKE USE OF TRADE INSTRUMENTS

Trade instruments can help protect you from supply chain risk. Often, your supply chain will ask for deposit payments, meaning that if for some reason your order can't be fulfilled, you will lose your money. This can impact not only your own business profitability and working capital but also other parts of your supply chain.

It's important to communicate with your bank to make sure you're putting in the right solutions that protect you and your interests, look after your working capital and support your supply chain.

GETTING THE SUPPORT YOU NEED

Building financial resilience within your company can be challenging and isn't something that happens overnight. When you've been in survival mode there are a lot of pressures on your time – you're trying to manage your day-to-day cash flow and business needs. But it's important to take a step back and look at the bigger picture and the measures you need to put in place to secure your business's future beyond just the coming weeks and months.

At this stage, bringing in an external advisor, someone who can take a more holistic view such as an accountant or someone from your bank, can be invaluable. When you're navigating a challenging period, you always have a long list of things that need your immediate attention, but ultimately it could be that one thing you've deprioritised which will help your business grow and thrive. Sometimes it takes someone from outside the organisation to see that necessary prioritisation.

GETTING STARTED: YOUR FINANCIAL RESILIENCE CHECKLIST

This isn't an exhaustive list, but doing all of the following will help you start building financial resilience within your business.

1. Work out your optimum working capital cycle.
2. Start a 13-week cash flow forecasting process; plan for potential future events.
3. Set up regular review sessions for your stock, debtor and creditor management reports.
4. Review your debtors: do any payment terms need renegotiating? Are there any payments which need chasing?
5. Speak to your bank about any financial products which can help support your working capital cycle.
6. Review your supply chain: are you too heavily reliant on one source? Are there opportunities for diversification?
7. Make sure the lines of communication are open with both your supply chain and your bank.

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MAKING SUSTAINABILITY WORK FOR YOUR BUSINESS

BANK OF SCOTLAND

Glen Bemment, *Head of ESG, SME & Mid Corporate, Commercial Banking*

Gary Lapthorn, *Head of Sustainability and Responsible Business, Commercial Banking*

Making sustainability central to business repositioning can open up enormous opportunities – not just in terms of cost savings, but also in opening new avenues for growth. However, it's an area in which businesses can struggle to find their way, and it may not be front of mind when they are faced with challenges.

Sustainability is now firmly on the radar of most UK businesses – our Road to Net Zero research shows that 91 per cent of them see it as important. But that doesn't necessarily mean businesses understand how to grasp the opportunities greater sustainability can offer and – even more crucially – what steps they can take to get started on their sustainability journey.

It is crucial, however, that sustainability plays a role in plans for growth. The journey towards the legal requirement to reduce UK net greenhouse gas (GHG) emissions to Net Zero by 2050 has begun, and business will play a key role in this. Despite this, our research shows that 40 per cent of SMEs don't yet know how Net Zero will impact them. A quarter of SMEs are not aware of this requirement at all, while some of those who are see it as a worthy but distant goal.

So, how can businesses bring sustainability into sharper focus and leverage it for recovery and growth?

FACING THE CHALLENGES

We are in an era of multiple challenges for businesses, all of which will impact the journey towards greater sustainability.

- Some businesses are in survival or recovery mode as we emerge from the pandemic. That said, our research shows COVID-19 has actually increased the importance of all elements of sustainability – environmental, societal and economic ones – to businesses (see Figure 1).
- Brexit will affect different businesses in different ways. Some businesses will see this as an opportunity, while for others it will be seen as an additional constraint or challenge.
- As the climate emergency becomes more mainstream, end customers, whether business-to-business (B2B) or business-to-consumer (B2C), have an expectation

COVID-19 has further exacerbated the importance of sustainability. Indeed, only a minority report it has made them think about it less

Q. What impact, if any, has the COVID-19 pandemic had on how your business thinks about each of the elements of sustainability?

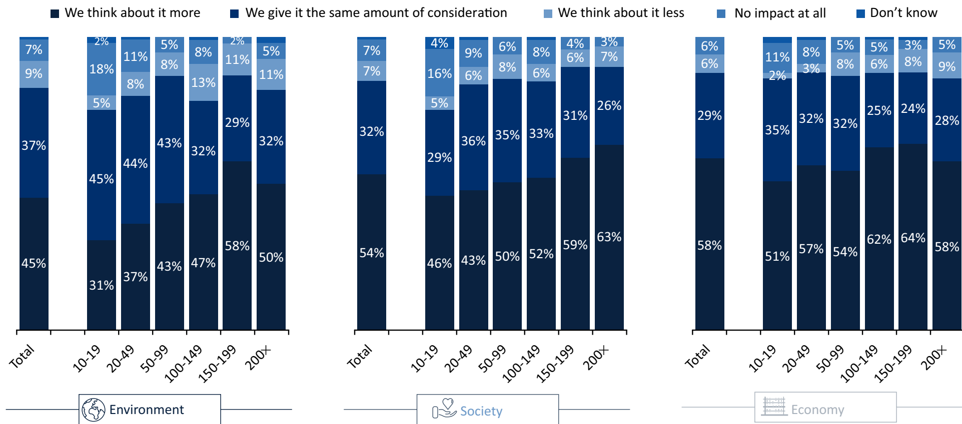


FIGURE 1. How COVID-19 has impacted the importance of sustainability

that businesses play their part in becoming more sustainable. They are voting with their feet, adding another layer of pressure for some business owners.

- Sectors are at different states of decarbonisation – compare transport and agriculture, for example – and the sets of challenges they face are very different.
- The landscape is very much reliant on the behaviour of consumers. What vehicles are people going to drive? How will diets change? What will consumers demand in terms of the localness or sustainability credentials of food?
- Size matters when it comes to making progress towards Net Zero. Our research shows that the larger the organisation, the more resources it has, naturally, for focus on Net Zero initiatives. This is why support for smaller organisations is vital, so that they can play their part in the transition.

This is the backdrop to the fact that businesses sit on a vast spectrum in terms of where they are on their sustainability journeys. There are those who have not taken any action at all at this point, all the way up to those who have thoroughly transformed their businesses and may already be able to claim that they are net carbon neutral or even carbon positive.

Sustainability is complex. But it's a challenge that businesses can rise to, and they are.

RISKS OF INACTION

While the journey towards greater sustainability presents challenges, the risks of not making sustainability central to a recovery and growth plan are greater.

LOSS OF RELEVANCE TO CUSTOMERS

Consumers are becoming very selective in terms of sustainability. Businesses which are seen as part of the problem rather than part of the solution risk losing ground to competitors as customers look for greener products and services.

BEING CUT OUT OF SUPPLY CHAINS

As the institutional shareholder sentiment of large corporates becomes greener, businesses not on a sustainability journey will not be able to

compete with those which are – notwithstanding the length of the relationships, products, supplies and services they provide. This is a real risk when corporates have a big choice of suppliers.

LACK OF INVESTMENT

Businesses which are not seen as being on the sustainability journey may miss out on attracting third-party capital and private equity.

TRANSITION RISK

Businesses which lag on sustainability risk being unable to deliver their products or services in the context of carbon reduction targets. For example, a business may not be able to continue trading from a premises that does not meet emissions regulations.

ENVIRONMENTAL RISK

Failure to reduce emissions affects businesses in general, with operations being disrupted by floods and other extreme weather events.

START THE SUSTAINABILITY JOURNEY

Our Road to Net Zero research shows that businesses tend to think tactically, rather than strategically, about sustainability. This is unsurprising, given the fact that the idea of formulating a sustainability strategy as a first step may seem overwhelming for many businesses.

However, the important thing is to make a start. The longer you leave it, the more likely competitors are to get ahead of you on the curve.

During this period, businesses need to take the actions which are right for them at their phase of recovery. To begin, look at the following areas:

- *Premises*: Premises and the built environment make up a large component of the UK's emissions and can provide significant steps towards emission reductions in terms of energy efficiency and energy purchase.
- *Transport and travel*: Transport – which contributes around a quarter of the UK's emissions, according to Government figures – will be another key area of focus.[1]
- *Operating costs*: Businesses can look for opportunities which will pay back in terms of finances, costs and emissions. These will be different for each business. For example, while some will be very reliant on transport, others will depend on raw materials or water.

Our Clean Growth Sustainability Audit checklist will help you think through the activities your business undertakes and what you consume and spend on, as well as the outcomes of those activities for your business and customers. It will also help you to start monitoring your initiatives by showing you where you've made progress and where there are opportunities for improvement.[2]

Using the checklist, you can identify your emissions hotspots and start thinking about quick wins which are relatively cost effective and which can pay back in the short term.

The checklist can also prompt you to start asking deeper questions about your business's carbon footprint. Can you reduce your energy use overall as well as change where you get your energy from? Is the size of your business premises appropriate for your needs?

LOOK AT THE LONGER TERM

When you have an idea of the CO_2 footprint of your business, you can start making incremental inroads into it. But while there are quick wins – changing all of your building's halogen lightbulbs to LEDs and putting basic recycling facilities in your office might be effective tactical moves, for example – your journey towards sustainability won't happen overnight.

What, then, do businesses need to do to create a strategic plan for sustainability as they return to growth?

Once quick wins have been actioned, businesses can ask themselves questions about, and define their longer-term goals:

- What are your strategic targets? Do you intend to halve emissions or get to Net Zero by a specific date?
- How will this strategy be communicated to key stakeholders – your board, regulator, employees and customers?
- Who will oversee and promote sustainability in your organisation?
- How will you monitor and measure the impact of your initiatives? This is crucial in becoming more strategic in your efforts.

Strategic areas of focus include:

- *Your supply chain*: This is not just around suppliers having sustainable practices, but in terms of the wider meaning of environmental, social and governance (ESG) criteria. What are working conditions like? Are workers paid the minimum wage? Is your supply chain free of modern slavery?
- *Your products*: Can you move towards a circular business model and, in turn, reduce your waste outputs?
- *Your premises*: Can you move towards renewable energy – fitting solar panels, for example? Do you need as many premises as you have? How would people working regularly from home affect your carbon footprint?
- *Fleet*: What is your medium- and long-term plan for your fleet?
- *Travel*: During the pandemic, online meetings replaced business travel. What will be your long-term approach to this? Will you pay higher costs for travel to reduce your CO_2 footprint?

CREATE A SUSTAINABILITY CULTURE

For some organisations, board-level accountability for sustainability is vital. But while you may choose to appoint an ESG director, or make sustainability part of the CEO's remit, in order to really succeed, sustainability has to be integrated with the rest of the organisation, creating a culture where *everyone* applies a lens of sustainability to their daily activities and tasks.

Encouraging your employees to demonstrate their passion in the area of sustainability is enormously powerful. Many people care deeply about sustainability and have huge amounts to contribute in terms of ideas for change. Furthermore, integrating ESG measures and tracking them means you will be aware of what happens on a day-to-day basis, enabling you to make sure any initiatives are genuinely effective.

Joining business sustainability–focused organisations, such as edie's Sustainability Leaders Club, can further immerse your business in sustainability culture, offering insights, support and opportunities to help you on your journey.

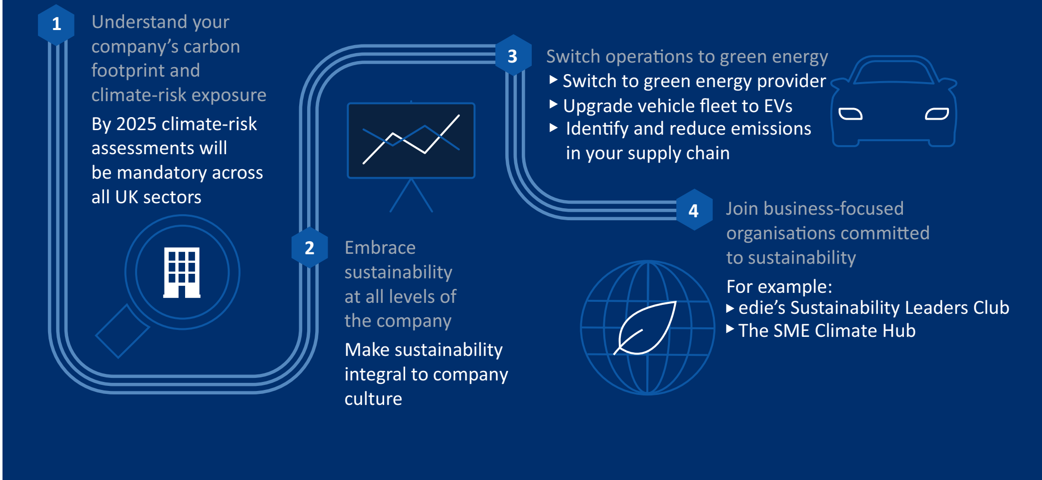
The best examples of sustainability are when an organisation's people have embodied and embraced it (see Figure 2). In Certified B Corporations – which win the certification by considering the impact of decisions on their workers, customers, suppliers, community and environment – any employee could be asked questions about sustainability and give almost the same response as an ESG director or CEO.

REAP THE BENEFITS OF SUSTAINABILITY

We've talked about the risks of lagging behind in the sustainability race. But there are enormous and wide-ranging benefits to be gained by making your business more sustainable.

IMPROVED CREDIT RISK

Businesses improving sustainability are likely to be the winners in their sectors. They'll be attracting new clients and doing more business, making it easier for them to access third-party or bank capital.



EV = electric vehicle

FIGURE 2. The path to Net Zero

COST REDUCTION

Carrying out a sustainability audit will help businesses focus on key areas of spending. They will be able to see how these link to areas where emissions and waste are generated and what they can save overall by becoming more efficient. The more people they involve in this process, the more ideas for cost reduction they will get.

WINNING CUSTOMERS

The public is looking at the interplay of green energy and sustainability in its consumer decisions. Smaller businesses which can communicate their sustainability credentials to new and existing customers can differentiate themselves in the market. As customers focus on quality and provenance, they may be more willing to accept that there is sometimes a higher cost attached to greener products.

OPENING UP NEW MARKETS

Being a greener supplier can help you do more business with existing and new clients. Large buyers and government contractors are insisting on smaller suppliers having sustainability credentials, so small businesses are becoming more sophisticated and more engaged, opening up more opportunities for entering supply chains and winning new contracts. If you can evidence your green strategy and your green supply chain, there's an opportunity to point out that this comes at a cost – one which customers may be willing to pay.

ATTRACTING TALENT

Your ability to attract and retain the staff you need can be influenced by the way you portray your organisation. People want to work for organisations which are doing the 'right thing' – being a responsible business and acting with purpose.

SUSTAINABILITY AND PRODUCTIVITY

Mark O'Mahoney, Senior Communications Manager at our productivity partner, Be the Business, looks at how sustainability and productivity work together.

There's an inherent link between sustainability, resource efficiency and productivity. The most obvious way in which this works is in reducing inputs and input costs – reducing packaging costs, for example. This applies regardless of business type or business model.

A second-order productivity benefit arises when business owners get into the good habit of keeping an eye on inputs, understanding exactly how and where they're using them and knowing what the costs are. This is something that a busy small business owner does not always take time to do, and once they begin it brings the overall efficiency of a company into a new focus.

Once you start to measure one element of your cost base or operations, you can then move on to measuring all sorts of other elements of the business process.

ENGAGEMENT AND PRODUCTIVITY

Research shows that increased staff engagement leads to increased productivity. If your team members want to come to work, are proud to work for the organisation, and feel they are stakeholders in the business, there is a productivity dividend to be gained.

Some of the businesses we work with say their teams are much more engaged when they can come up with mini-projects around how the company can be more sustainable and environmentally friendly. This gives people pride in their workplace; they're happier to work in the organisation and one of the benefits of this is increased productivity.

PRODUCTIVITY CHALLENGES

Going towards Net Zero, there is a rush for large businesses to ensure they are being as sustainable as possible. However, sometimes their expectations of what their smaller business suppliers can do in a short time frame are to the detriment of their productivity or their core business.

There's a strong case for large buyers working in tandem with their supply chain, so SMEs are not forced out unnecessarily or have unrealistic expectations placed on them in terms of what they can do to help make the supply chain greener.

Related to this is potential risk among small business, trying to make absolutely everything in their business green. The key is to focus on where you can make impactful changes which align with your core business and communicate this well, rather than trying to do a multitude of small initiatives which might take a huge amount of company resources but which do not necessarily deliver major impact in terms of sustainability or carbon reduction.

You can always bring more green initiatives on stream over time, but in the short term, focus on where you can make the most impact and what your stakeholders care about. You can ask your employees to come up with ideas, as well as asking suppliers or customers for their input. They often have very insightful perspectives from being outside the business.

You also need to make as much effort as possible to measure and communicate externally the positive impact of your sustainability activities.

LOOKING TO THE FUTURE

The road to sustainability can seem poorly signposted – our SME Road to Net Zero research shows that lack of access to information is one of the challenges which stands in the way of SMEs being more sustainable. However, there is support available.

- There is a range of online tools and action-based insights from experts to help businesses on their sustainability journey on our sustainability hub.[3]
- The SME Climate Hub is a global initiative offering tools and support for businesses to help them halve greenhouse gas emissions before 2030 and achieve Net Zero before 2050.[4]

Business has forever been the richest source of innovation and change. Some businesses are already making enormous sustainability strides, alongside others which are at the earlier stages of maturity. This decade is going to see change like we've never seen, and business will be the engine room of that.

KEY TAKEAWAYS: QUICK SUSTAINABILITY CHECKLIST

Get started by focusing on these initial questions. For more detail, see the full **Sustainability Audit Checklist**.[5]

	Yes	No	Don't know	N/A
Have you set clear emission reduction targets?				
If you have your own fleet or company cars, are they hybrids or EVs?				
Do you support staff walking and cycling to work (e.g. by providing showers and taking part in the Cycle to Work scheme)?				
Do you have a recycling policy for your premises?				
Can your packaging be recycled?				
Do you have a strategy in place for recycling any waste created as part of your production process?				
Can your products be reused, recycled or composted?				
Are suppliers all asked to adhere to a code of conduct ensuring that their production processes meet certain sustainability criteria?				
Are all your lightbulbs compact fluorescent lamp (CFL) or LED lights?				
Are you on a green energy tariff?				
Do you regularly monitor your water usage?				
Do you have any green spaces in your workplace?				

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TRANSFORMING YOUR BUSINESS THROUGH DIGITALISATION

BE THE BUSINESS

Carla King-Molina, *Digital Marketing & Communications Manager*

Mark O'Mahoney, *Senior Communications Manager*

Technology can hold untold opportunities for small and medium-sized businesses, and these opportunities are becoming more and more important with each passing year. In the past, technological gains were often only open to the big players in the industry, but now, it seems like each year, more tools are available to help smaller businesses to do what they do – just better. At its core, digitalisation can help business leaders improve their business productivity, enable growth and give them back the time they need to think strategically and enhance the way they work. Importantly, technology can help you to better understand your clients, provide enhanced services and build stronger relationships with your customers.

Digitalisation holds the key to unlocking productivity gains and can give you the tools to simplify complex and time-consuming processes, such as automating your invoicing, fast-tracking your HR processes, managing your bookkeeping, keeping track of your supply chain and so much more! Simply put, digitalisation helps you automate the processes which take up a great deal of organisational resources but do not necessarily contribute to growing your business.

Technology can do much more than automate processes. If you start collecting and analysing your data with simple digital tools, you will rapidly be able to forecast future demand and customer behaviours, or even unlock new products. Invoices and customer orders are full of information which is useful for your business but is difficult to interpret – technology can help you to harness its power. You might even get ideas for a new product or find new ways to communicate with your customers.

As more businesses across the UK ramp up their digital efforts, it's getting harder and harder to avoid doing the same. Being one of the first movers in an industry has always been a huge advantage, but adopting tech has gone from bringing a competitive advantage to being a competitive requirement. Gone are the days where you could depend on your loyal customers to stick by you regardless of your technological capacity. Businesses now constantly need to be innovating in this space – and tech can help. Small businesses do have one big advantage in terms of tech adoption – the process can be a lot more straightforward than it is for their bureaucratic, multi-layered and larger competitors. This makes them more agile, nimble and better able to adapt to digitalisation at the pace required for success.

The pandemic has fundamentally changed the way UK SMEs operate, and this change will be permanent.

In this chapter, you will learn about why you need to be using tech; how tech can help you re-imagine your products and help you create new revenue streams; how to develop your digital strategy; how to embrace ecommerce; and how to find the best, most effective technology for your business.

HOW THE PANDEMIC HAS MADE SMEs GO DIGITAL

Small and medium-sized businesses of every type have been forced to re-think and re-shape their business models over the last 18 months. The restrictions and challenges brought by the pandemic have meant that in order to continue to trade, rapid innovation would be required. For a great many, this necessitated the use of technology. The requirement to find ways to keep businesses trading and keep serving customers has led to a wave of technology adoption across the UK.

This tech transformation of the UK's small business community has been seen throughout every sector and region. Research Be the Business conducted in partnership with The Open University has shown that COVID-19 accelerated the adoption of collaboration and ecommerce software in more than half (54 per cent) of all small businesses.[1]

It also appears that this tech transformation will be permanent – our research tells us that of the business leaders who adopted new technology or accelerated its use due to COVID-19, at least 85 per cent plan to continue using it at the same level once restrictions are fully lifted. The pandemic has made business leaders more likely to invest in digital skills development, both for themselves and their employees.

The pandemic has fundamentally changed the way UK SMEs operate, and this change will be permanent. The reality now for many businesses is that if they haven't already started utilising technology and digitalising, they need to start. If they have begun their digitalisation journey, they need to make the most of their tech and use it to reshape their business model.

RE-IMAGINING YOUR PRODUCT/SERVICE AND BUSINESS MODEL

We've already explored how COVID-19 has accelerated the uptake of tech across businesses of all shapes and sizes. Not only did small business leaders have to transform ways of working, but in certain cases, they also had to completely re-imagine their products, services and business models. There are countless accounts of businesses making the shift to ecommerce during those early months of the pandemic. They may have already been planning these pivots, and they may have brought investment and changes forward. In many cases their hands were forced, and in the search for new revenue streams, they transformed their business.

A great example of this quick type of tech-enabled pivot is Dunsters Farm. Before the pandemic, they mostly supplied educational institutions, restaurants and cafes. Over the course of just a few days in 2020 they saw 95 per cent of their business disappear. They had to move quickly to find new revenue sources and moved into business-to-consumer (B2C) sales, building a new website for a home delivery service and working with other suppliers locally to build a new offering for local consumers. This temporary change enabled by rapid digitalisation proved so successful that it has now become a core element of their business model.

Food production company Flower and White, also innovated during the pandemic, spotted a gap in the market for at-home activities. This pushed the business to launch a new set of products online, including home-baking kits requiring less staff interaction to tap into new markets. Within weeks of establishing this ecommerce option, online orders increased by 800 per cent, with orders being made from multiple countries including the US.

Having the capacity to go digital and get new services online quickly can be transformational

for your business – and it makes putting in the necessary technological infrastructure well worth the investment. Developing new products or services is not necessarily optional any longer either. Up to 63 per cent of customers expect companies to provide new products or services – a higher percentage than ever before. If you are not bringing new products to market, you run the risk of losing customers. Technology can also help you in the new product innovation process by enabling you to get feedback from your customers from social media, email and surveys and allowing you to incorporate their views or expectations in your thoughts.

HOW TO DEVELOP YOUR OWN DIGITAL STRATEGY

From the research we have carried out on success rates in SME tech adoption, we know it to be a difficult process. However, the figures around failure rates are stark. More than 53 per cent of SME tech adoption projects end in failure. Interestingly, cost is not often identified as a reason for failure. The main challenges and barriers to successful adoption are a lack of engagement by employees and the tech solution failing to deliver the expected results.

Overcoming these two barriers unfortunately does not mean you will have a successful digitalisation journey. SMEs have identified other significant challenges at every stage of the tech adoption journey:

- At the acquisition stage, 44 per cent of SMEs said there was too much confusing information on tech solutions in the marketplace.
- At the implementation stage, one in three SMEs said they struggled to integrate the tech across other business processes.
- Finally, at the service stage, 41 per cent of SMEs said switching providers was disruptive to their business and the most challenging part of the adoption process.

> More than 53 per cent of SME tech adoption projects end in failure.

With all the push factors encouraging SMEs to go digital, but with very high failure rates for tech adoption projects, it became apparent that small business leaders wanting to embrace digital processes will need support to do so effectively. This led us to develop Be the Business Digital, an online platform to enable small business leaders to develop their own tech adoption strategies and digitalisation journeys. We have identified a six-stage process of questions a small business leader should ask themselves at the beginning of a tech adoption process to help them plan their journey to digitalisation:

- Have you set a clear objective: do you have a clear goal for what you want to achieve in your business? Have you identified any potential barriers to achieving your goal? Is technology the right solution for what you want to achieve?
- Selecting technology as a solution: can you assess the costs, benefits and risks? Have you correctly identified the role technology should play in your business?
- Selecting the right product: are you able to navigate the market and trust the information available to you?
- Purchasing successfully: are you happy you can deal with a potentially complex sales process? Do you trust the sales process and have enough information to make an informed purchase?
- Implementing successfully: are you happy that you can manage a tech transformation project within your business? Do you have access to examples of what 'good' looks like in tech adoption projects?
- Extracting the benefits: does your business have the ability to maintain the new system and adapt businesses processes? Can you identify further opportunities for tech adoption?

You can access free action plans, tools and templates to help you answer these questions and create your own digitalisation strategy on bethebusiness.com.

EMBRACING ECOMMERCE

The Lloyds Bank 2020 Transformation with Tech Report highlights the importance of implementing technology.[2] Almost half (2.7 million) of micro-businesses state they would have ceased trading without digital technology. More than a third have reduced costs, and 40 per cent have increased their online trading – one quarter now having an online presence for the first time. These are big shifts in business behaviours, but they're coming at an essential time.

Embracing ecommerce has never been a more essential part of doing business. Ecommerce now comprises almost a third of all retail sales, according to the Office for National Statistics (ONS). Even when sales are completed in person, a digital element is now a frequent step in the sales process. The amount of retail sales being made online jumped from 21 per cent in the first quarter of 2020 to 34 per cent in the same period in 2021.

It's hard to say exactly how much of this was caused by the COVID-19 pandemic, but it's clear it had a big impact on consumer spending, and it is likely these consumer behaviours will be maintained even once lockdown restrictions have eased. From normalising online grocery shopping to sending loved ones flowers from an online florist, it's likely the shift to ecommerce and the speed at which businesses filled in the gap which has completely changed how we purchase.

> Embracing ecommerce has never been a more essential part of doing business.

If you're a B2C firm, you're in luck. It has never been easier to start selling online. From opening up an Amazon marketplace to getting some ready-built ecommerce solutions, you're just a Google search away from finding an option which is right for your business. If you specialise in business-to-business (B2B) services, ecommerce might not feel like it is as pressing of an issue, but a good digital presence is not just a 'nice-to-have' any more – it's essential. Even if ecommerce or efulfilment doesn't fit your business model, a solid website can help you drive traffic to your business, build credibility and increase sales. The online presence of your business is a major vehicle for all of these efforts, so you need to prioritise it accordingly.

If you're thinking about getting started with ecommerce, here are three steps you can take to quickly make the most out of your efforts:

- Conduct competitor and customer research: what are the competitors you respect doing? Where are they pushing hard? What sorts of sales mechanisms do they have in place online? It doesn't have to be intensive – you can learn quite a lot from a visit to a website. Look internally, too. What are your customer demographics? There's a lot of demographic research available online covering how different types of customers behave and what platforms they use.
- Get expert insight: there's a bounty of ecommerce and digital sales expertise out there. Yes, it might cost you a little money to access – but it can be worth it, especially if you're targeting a new market. Incisive, expert guidance can help you quickly identify a few key adaptations or localisations you need to make to your product. A few sessions with an ecommerce or digital marketing expert or consultant can really pay dividends and save you money in the long run. While expert insight is not a complete replacement for your own legwork and experience, it can be a valuable addition to it.
- Get a customer relationship management (CRM) system: bring in a CRM system and optimise it to fit your sales process. The software doesn't need to be top-of-the-line or expensive. The market is well developed, and there are solutions now available catering specifically to SMEs and smaller businesses.

  A CRM system helps you collect and analyse the right customer data. You could update the information collected to make more

informed decisions about the digital sales channels you use – for example, capturing the source of deals and tracking what email campaign prospects interacted with.

Not having a CRM system for organising data means SMEs often use a great deal of resources trying to sell through multiple channels – and they don't put enough focus on the most successful ones. It is difficult to grow without access to data. You need to be able to monitor information regarding customers, products and sales channels – and a well-maintained CRM system makes this much easier.

COST EFFECTIVE TECH

The prospect of paying a significant amount of money upfront for a tech solution you're not 100 per cent sure is right for your business can be daunting. You may not be sure the tech will do the job you need it to do, or you may have questions about how it will integrate with your other systems. Concerns like these can often prevent small business leaders from even starting their digitalisation journey. The good news is there are low and no-cost options available for those business leaders who want to test how effectively a tech solution will work before making a long-term commitment and a more substantial investment.

Increasingly, tech companies are making their products available to small and medium-sized business owners for trial at no cost. There are free trial periods available for a very wide variety of productivity-improving software, from ecommerce to CRMs to team communications platforms. The trial periods can vary from product to product but can be from 30 days up to 90 days in some cases. Very often, you can try these products with access to tech support from the company sales team to help you get set up. This is an excellent way to get a feel for whether a tech solution will work well for your business.

Additionally, many large tech companies have developed free training programmes for small business leaders who wish to quickly get upskilled in a specific tech product – this is also an excellent way to quickly understand how a tech solution works and whether it could be a good fit for your business. Most major tech companies have short free training programmes available, and again, these can be a great way to learn about the solution and its benefits before committing to it.

CONCLUSION – EVERY BUSINESS IS NOW A TECH BUSINESS

In 2021, every business is now, to a greater or lesser extent, a tech business. From using technology in your day-to-day work, to creating a virtual storefront for your products and services, it is as much a competitive requirement as it is a competitive advantage. It's definitely not an easy process at first, but if you talk to your staff, you never know what hidden talents and knowledge they possess. There's also so much free support out there. If you're wondering what the best next steps to take are, you can always visit our website, bethebusiness.com, where there is a dedicated section on technology adoption. Bank of Scotland Academy also has terrific resources to help you get started. If you're a step ahead, you can find grants to invest in tech solutions, like the government's Help to Grow: Digital scheme or other local initiatives.

Simply put, when it comes to going digital, you just can't afford not to. Diving into the world of digitalisation is scary, and fear of the unknown is a common deterrent for SME leaders, but with the right preparation and the right support, you'll soon be reaping the rewards. From increasing your sales to improving your HR processes, there's a digital solution to any query you might have. Technology, somewhat counter-intuitively, can be the most effective way to humanize your business and build meaningful engagement and relationships with your customers. So, start researching, planning and weaving digital processes into your business strategy.

FIVE STEPS TO GETTING YOUR BUSINESS TECHNOLOGY READY

- **DO YOUR RESEARCH**

  What does your competitor's website look like? Are they on social media? Take note of any ideas you love and want to implement for your business.

- **GET SOCIAL**

  Make it easy for your customers to get in touch with you, and make sure you have relevant social channels and all your information is up-to-date. If you're a B2C organization: Facebook, Instagram and now even TikTok are non-negotiables. If you're B2B, make sure your business is on LinkedIn and Twitter.

- **GET SALES, GENERATE LEADS!**

  Do you sell products online, or are you hoping to generate leads? Make sure your website is helping you collect data so you can reach out to your customers and tell them why they should choose you.

- **BRING IN A CRM SYSTEM**

  Now that you're improving how you collect data, sales and leads, it's time to make sure you're keeping tabs on everything. Make sure you're marketing through the channels which work and keeping on top of your customer preferences.

- **SEE WHAT TECHNOLOGY IS AVAILABLE FOR FREE**

  When you're building up the rest of your technological armoury, it is always useful to see what tech companies are offering SMEs for free. If the free (for now) solution tackles something you want to work better in your business, then it's a great sign to add a new tool to your repertoire!

FURTHER READING

https://www.bethebusiness.com/

https://www.bankofscotlandacademy.co.uk

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PARTNERING FOR GROWTH: AN INTRODUCTION TO PRIVATE EQUITY

LDC

John Garner, *Managing Partner*

LDC is the private equity arm of Lloyds Banking Group and is the UK's leading mid-market private equity firm. We are committed to supporting management teams across the UK to fulfil their growth ambitions and build great businesses.

There comes a time in every business' growth journey where the business leaders driving the company forward may need an extra boost to help unlock new growth opportunities. This is where the support of an external investment partner can help.

Private equity can be an incredibly useful avenue to access investment and expertise to help to grow your business. And you'll be backed by experienced business partners who will support you in building your business no matter the economic climate. It can also mark the first step of a succession plan, enabling business owners looking to take a step back to hand over the reins to their management team without letting go entirely.

Before looking outside of the business, however, the key is to first understand what support is needed and what type of partnership may be the right fit – what style of investment, and what kind of backer suits your business and your ambitions best?

This chapter will serve as an introduction to private equity, guiding you through the process of raising investment and helping you to understand whether it's the right choice for you, your management team and your company.

WHY CHOOSE PRIVATE EQUITY?

Private equity is ultimately a means of opening up new growth opportunities to help scale a business without losing control.

The combination of investment and strategic support means partnering with a private equity investor can help you achieve your ambitious growth plans, whether that's expanding into new domestic or international markets, driving organic growth, targeting complementary acquisitions, or investing in new products and services.

The reasons for choosing to partner with a private equity investor are based on individual circumstances. Common themes include:

- *Pursue a new growth avenue.* The management team may wish to explore a new avenue to growth but lack the capital or specific expertise to deliver on

it. A private equity partner can offer the investment and experience to kick-on with this growth strategy, such as acquiring a competitor or expanding into a new international market.

- *Kickstarting a succession plan and supporting a change in ownership.* Private equity is not only a way of driving growth. For some business leaders, it can also provide an opportunity to open up succession plans. For example, this could involve enabling your existing management team to increase their shareholding, which in turn allows other shareholders to divest, either fully or partially.
- *Helping business owners to de-risk whilst retaining control.* For other business leaders, it can be an opportunity to de-risk and sell a minority shareholding of the business to realise some value, whilst still retaining control. This is often an option for those business leaders who have experienced a shift in their own personal circumstances, or where their plans have changed.

A private equity partner will support your ambition. You know your company better than anyone, and your investment partner should act as an extension of your team – on hand to work by your side to provide expertise, support and capital along the way.

CASE STUDY: PLIMSOLL PRODUCTIONS

You may not have heard of Plimsoll Productions, but you'll certainly know their shows. The team behind programmes including John Bishop's Great Whale Rescue and Tiny Earth, Bristol-headquartered Plimsoll Productions is the biggest independent production house in the UK, with a client base including Apple, Disney and Netflix.

Plimsoll's management team, led by CEO Grant Mansfield, first partnered with LDC in August 2019 in a transaction that valued the business at £80 million. Grant explains his journey so far:

"Three years ago, I decided to look at investment options for the business. I wanted capital to pursue acquisitions, to give existing stakeholders the opportunity to realise some of the value they had generated in the business and to ensure our talented team remained at the heart of driving growth."

"I spent two months in Los Angeles, talking to around 15 trade buyers – and we had some attractive offers from some of the largest media companies in the world. In our industry, trade sales are the norm, so before meeting LDC I hadn't considered the private equity route at all. But when we looked at the offers we had, they were all predicated on us handing over complete control of the business. I wasn't ready for that – with private equity, I could raise the investment I wanted while still retaining a majority stake."

"LDC took the time to get to know us. This personal chemistry is key to choosing the investor that suits your business best – you need to spend time with the people who want to back you, and you have to like them and trust them."

"Now, every month, we sit down with our management team and our partners at LDC, and talk through recent developments and where we want to take the business next."

"My advice to other founders? Don't discount private equity. This has been a genuinely positive both for me and for Plimsoll, and we are on track for great things!"

STRATEGIES FOR GROWTH

The support of an investment partner can help to open up new, or accelerate existing, growth opportunities in many different ways.

Whether you're interested in expanding internationally or funding business improvements, private equity can often be the catalyst for that change. Here, we take a closer look at some businesses who have been there and done it, and the routes they chose with the support of a committed investor.

ORGANIC GROWTH

Your business is already growing – but private equity can help you to grow even quicker, while maintaining your unique culture. It could be anything from finding new premises, developing new products or rolling out new services or recruiting additional staff.

Long-term support is key to any private equity partnership supporting organic growth, so growth is sustainable, even during the most challenging times.

CASE STUDY: TEXTHELP

What do you do if you're a college student struggling to keep on top of your workload because of dyslexia or because English is your second language? Where can you turn at work when you're being pulled up on spelling mistakes in documents and emails? Texthelp is helping millions of people across the globe grappling with these challenges with technologies that allow them to understand and to be understood.

Today, the company offers solutions to its 40 million worldwide users including literacy support software *Read&Write*, maths product *EquatIO*, web accessibility toolbar *Browsealoud* and writing achievement tool *WriQ*. Founder and CEO Martin McKay is working towards his ultimate goal to reach 1 billion people around the world with his products.

LDC backed Texthelp in May 2019 to help Martin and his team realise this ambition. "Our existing investors wanted to exit the business, but I didn't," said Martin. "LDC helped come up with a structure that would allow me to roll my investment forward, while also reinvigorating the business for the next stage of growth." Over the two years that followed, the business invested heavily in product development to drive growth.

He said: "Our partnership with LDC helped us to go further, faster. Initially I was a little concerned that a new investor might come in and try to take over, but LDC made it clear they weren't about to break something that was working well. The team believed in the potential of our business, and our ability to deliver on our plans. They provided the investment, support and expertise to help us accelerate a truly differentiating digital transformation in a relatively short space of time."

BUY AND BUILD

Acquiring complementary businesses can help to create a company that is greater than the sum of its parts, building scale and resilience, and subsequently boosting market share. It can unlock new markets and geographies and add valuable expertise to a growing business.

A private equity partner can work with you to identify businesses that are a good fit, as well support the purchase with funding and expertise, and help deliver a smooth integration.

CASE STUDY: STUART TURNER

Founded in 1906, with strong heritage in engineering and product innovation, Stuart Turner is an international market leader in water-boosting solutions. Drawing on over a century of engineering excellence, it has established a reputation for high-quality products in the commercial and domestic markets, including a patented solution for mains water pressure issues.

In 2017, LDC backed the management buyout of Stuart Turner with an investment that is enabling the team, led by CEO Richard Harden, to accelerate its buy and build strategy and target international expansion.

Richard explains he turned his ambitions into reality: "The aim at Stuart Turner has always been to take our market leading knowledge and experience in the residential sector into the commercial building services and industrial sector – and to continue to build our export markets."

"We found that acquisitions were a great way for our company to achieve rapid growth over a short period, and acquiring complementary businesses helped us expand our offering to customers not just in the UK, but overseas, giving us a real competitive edge."

"Over the past three years, we have made three acquisitions. All have boosted our access to industry experts and resources, and allowed us to successfully break into new markets and expand our customer base."

"LDC have provided us with follow-on funding to support our continuing buy and build trail, and the sector experience to help us identify and successfully integrate the businesses we acquire."

INTERNATIONAL EXPANSION

The combination of funding and expertise from an investor can help create new partnerships, increase exports, acquire an international business or establish a new offer overseas. With this support, it's possible to identify and deliver the best international growth strategy for your business.

CASE STUDY: EVEDEN

When Tracy Lewis joined lingerie maker Eveden back in 2003, the company sold its wares wholesale to just a few buyers across the UK. Tracy had spent her entire career in retail, working for high-street stalwarts including Mothercare, M&S and Next. Tracy could see an opportunity to turn the small business into a true global player.

LDC backed Eveden in 2006 to support CEO Tracy's international growth strategy. Over a six-year partnership, it helped the business to roll out its core brands of Freya and Fantasie across the US, Europe and Asia, employ more than 200 new staff members, and complete a strategic acquisition in France. In 2012, Eveden was acquired by Japanese conglomerate Wacoal for £148 million, turbocharging its continued international growth.

In Tracy's words: "Once I met the guys at LDC, I realised straight away that the team would be an invaluable sounding board. They had so much brand-building experience and had already helped some household names in the Midlands, where we were based."

"Partnerships always come down to chemistry – and I felt I could really work with these people. They got what we were about. They were enthusiastic and passionate about the business, but didn't want to run it – they didn't think they knew more than I did. It was all about the value they could add to us, and to me."

"We had considered expanding overseas through acquisitions – and it would have been one way of accelerating growth – but it would also have been a big distraction. The challenge from LDC was always 'why don't you accelerate what you're already doing instead?'. And sure enough, we grew with an unfaltering focus on our own brands and our own growth, which created real value throughout the business."

STEPPINGSTONE FOR IPO

If taking your business public is your ultimate end goal, private equity can be an important stepping stone – or an alternative path in uncertain times. Helping to build value and consolidate your offering, your backer will work alongside you and your team to make sure your business is fully prepared.

CASE STUDY: TEAM17

Indie games developer Team17 is best known for games including its iconic *Worms* franchise, as well as *Overcooked* and *The Escapists.* Over the past five years it has achieved extraordinary growth selling its titles worldwide through distributors including Sony, Microsoft, Apple and Google.

In September 2016, LDC partnered with CEO and founder Debbie Bestwick MBE, injecting £16.5 million to support Team17's ambitious overseas growth plans, investment in product development and to pave the way for a listing on AIM (Alternative Investment Market).

The business grew significantly, with international sales increasing 40 per cent and both revenues and EBITDA growing by more than 100 per cent ahead of an IPO in May 2018.

Debbie Bestwick shares her journey: "I'm not sure we could have got to where we did without private equity investment. We would have grown but not at the rate we did. We needed the support – and the push."

"LDC helped me to develop as a person, as well as developing the business. For example, the team encouraged me to enter the EY Entrepreneur of the Year awards. Because of that, I did loads of interviews and really learned how to position the business to outsiders. If I hadn't done that, I wouldn't have had the skill for the IPO meetings."

GETTING YOUR BUSINESS INVESTMENT READY

Every path to growth is different, but if you've made the decision to explore private equity investment there are some key steps every business owner should take to ensure they are ready for investment. Here, we take a look at the key things every business leader should consider.

1. Check the books

Always take time to make sure your books are in order. Potential investors will be looking to identify opportunities for growth – so it is key to be able to evidence your success to date, and outline a clear, achievable plan for the future.

Future opportunity is often more important than current scale. If the numbers are heading in the

right direction, that shows a potential partner there is opportunity for them to support.

2. What's your vision?

Every business leader is fuelled by their ambition and vision for the future success of their company. Funding partners will look out for a clear articulation of this ambition, and the strategy your team will follow to get there.

For LDC, if we can easily understand the management team's vision and strategy, we know it's one we want to back – it means we're best placed to support the team from day one.

3. Focus on people

A private equity partnership is all about building strong relationships and working closely with those running a business to help make their ambitions reality. Having a strong team gives a private equity firm the confidence to invest.

Investors will also value plans to retain and nurture existing talent in the business, and opportunities to bring in new skillsets – showing that you're focused on safeguarding the business' future prosperity.

4. Consider the risks

Don't fall into the trap of constructing your business plan wearing rose-tinted glasses. Factoring in any potential bumps along the road shows you have thought carefully about how your business will adapt to potential challenges over the next few years.

A private equity partner can help you to absorb some of the shocks along the way, as long as you have a plan for maintaining cashflow through any peaks and troughs – this means an investment partner can easily see where their support will be needed.

COLLABORATION AND PARTNERSHIP

A successful private equity investment is all about partnership. As well as giving you access to capital and strategic support, the best relationships are founded on collaboration with all parties working together to help the business thrive.

The key to success is to take the time to get to know and understand each other to establish the best possible working relationship that fosters success and allows for patience and flexibility as the particulars of the transaction are worked through.

Approach your new partnership with an open mind and take the time to get to know your investor to ensure you find a backer that believes in your ambition and is ready to help your business thrive. This is the key to any successful collaboration.

KEY TAKEAWAYS

Why choose private equity?

- Unlock new growth opportunities to realise your ambition.
- Access new investment and expertise.
- Kickstart a succession plan and support a change in ownership.
- Enable you to de-risk whilst retaining control.

Growth strategies that private equity partnership can support

- Organic growth – invest in people, product development, infrastructure or new sites.
- Buy and Build – support your business to identify, complete and integrate complementary acquisitions.
- International expansion – help to increase exports, acquire an international business or establish a new offer overseas.
- Future IPO – professionalise your business and prepare for a public listing.

How to get your business ready for investment

- Check that your accounts and latest trading figures are accurate.
- Be able to articulate your vision for the business.
- Have a strong and backable management team in place.
- Ensure you have considered the risks your business will face.

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CONCLUSION – WHAT NEXT?

Bank of Scotland

If you're embarking on a turnaround journey, or if you've realised that your business needs to change its focus significantly, remember: the critical first step is recognising the challenge that lies ahead.

As we've seen in the first section of this book, you must start by taking urgent action to stabilise the business. This means taking a cold, hard look at the way the business operates today – and external support will often be helpful to make sure that you are being both objective as to where you stand and realistic as to what is possible.

Take heart that, though some of the difficulties may turn out to be more significant than you might have hoped when you first began to investigate them, tackling them may open up new avenues for growth. In other words, no matter how tough the situation, keep in mind that positive opportunities can often be found, though it will take a clear head to identify them and courage to unlock them.

Having invested time and effort in to begin to grapple with the challenge, it is then essential to take a proactive approach to finding the right solution for your needs and circumstances, identifying your ultimate objectives or 'strategic destination'. Once you know clearly where you are going, it is much easier to identify how best to get there, and to adjust your course as necessary along the way should circumstances change.

You must then translate this into an action plan, with clear responsibilities and agreed implementation dates. Depending on the circumstances that you need to navigate and the particular challenges you face, different types of external support may be particularly important. This may come from business consultants, insolvency experts, legal advisors, communications specialists and your bank.

One common theme through all of this is the importance of ensuring that the business can achieve stability and establish a resilient platform for future growth and development. Limiting the downside and making the most of the upside will take both timely action and teamwork, both within the business and with your customers, suppliers and other stakeholders. Effective, open and honest communication is a critical ingredient to success and merits careful attention from the start of your turnaround journey.

Once you have addressed the most pressing near-term issues and stabilised the business, you can begin to turn your attention to making the most of the medium to long-term opportunities. In doing so, one of the most important steps is to consider whether and how you need to build, or indeed rebuild, your team so that you have the right skills, support and attitude to support your turnaround. Having the right people, with the right mindsets and the right balance between positivity and pragmatism is

almost always the single most important factor of whether your plans are likely to succeed or fail.

As we've explored in the second part of this book, once-in-a-century shifts are under way that will have a profound impact on the world of work – and indeed how we live – for the next hundred years. From the shift to renewable and adoption of zero-emission vehicles, to restructuring of the agricultural value chain and localisation of production, these trends are both permanent and profound.

Although the future can seem murky at times, with the right perspective you should be able to identify ways that you can position your business to ride the waves of change, rather than fighting a tiring and inevitably losing battle to hold onto old economy businesses and business models.

As many early adopters have shown, adopting sustainable practices can help make your business more resilient and more profitable, not to mention more popular with your employees, customers and other stakeholders. As a result, ESG is likely to remain part of the business lexicon for a long time to come.

Importantly, you don't have to navigate a turnaround on your own. There's plenty of help and support available, including from the team at Bank of Scotland.

In the meantime, other resources you might find useful include:

- Support for customers facing financial difficulty
- Mental health in the workplace
- Sustainability hub
- Bank of Scotland Academy digital courses

We're here to help you on your turnaround journey in any way we can.

REFERENCES

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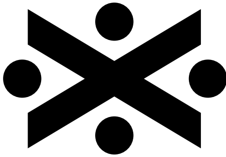

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Glenn is Head of ESG (Environment, Social and Governance) for Bank of Scotland SME and Mid Corporate Business, which looks after clients with turnover from £3–100 million, with

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Gary joined Lloyds Banking Group in 1986 as a management trainee and spent his early years in a variety of customer facing roles in Retail and Business Banking around South West England. He has worked in Commercial Banking for most of the last 21 years, with leadership roles covering proposition development, marketing, and credit risk strategy before setting up the Sustainability and Responsible Business team in 2016. Gary leads the Commercial Banking sustainability strategy, which is focused on the bank's ambitions to be a leader in supporting clients to transition to a low-carbon economy. He is passionate about inclusion and equality and leads a broader range of Responsible Business activities including the bank's programme to better support Black entrepreneurs.

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Gareth Oakley's current role is Managing Director Business Banking where he has responsibility for more than a million business customers. He is a trustee for the Lloyds Bank Foundation and Chairman of the UK Finance Corporate and Commercial Board. Gareth has over 30 years of experience in banking and has run a number of large businesses within many of the Bank's divisions including Retail Banking, Wealth Management and Commercial. He was also formerly Chairman of the Agricultural Mortgage Corporation (AMC) and Lloyds Banking Group Ambassador for the East.

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Carla King-Molina is a Digital Marketing & Communications Manager at Be the Business, a movement launched by UK business leaders to transform the nation's productivity. In this role, she looks after the company's social media, digital marketing, and data strategies. Prior to joining Be the Business, Carla was a part of Hill + Knowlton Strategies' Financial and Professional Services team, where she worked with a variety of clients across a number of sectors including Coca-Cola, P&G and HSBC. Carla also supported the implementation of Trinity College Dublin's internationalisation and recruitment programme as a Communications Executive. In this role she led several social media marketing campaigns across the US and Asia. Carla graduated from Trinity College Dublin, with a first in Economics and Political Science. She is currently learning to code in Python, so she believes in the future of tech and the importance of lifelong learning.

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Mark O'Mahoney is Senior Communications Manager with Be the Business, a business-led and government-supported independent charity created to close the UK's productivity gap. He has worked in economic development, international

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An Oxford University law graduate, Julie Palmer qualified at Price Waterhouse before moving to Smith & Williamson. This was followed by running her own successful corporate recovery practice. She joined Begbies Traynor as Managing Partner at the firm's Salisbury office in 2006, and was promoted to South West Regional Managing Partner in 2013.

Julie deals with all aspects of corporate recovery and turnaround work and takes on all forms of personal insolvency appointments. She has successfully managed many high-profile insolvency and restructuring cases, including the successful sales of Bournemouth Football Club, Bristol Rugby Club, Shakeaway and Mostyns.

Julie is a member of the Insolvency Practitioners Association and is a Fellow of The Association of Business Recovery Professionals, as well as working with a number of their policy groups.

Julie is the national media face of Begbies Traynor and is regularly called to comment on economic issues, high profile insolvencies and restructurings, as well as being seen as an expert on the retail sector.

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Michael Thomson is a specialist in insolvency law and heads Burness Paull's market leading restructuring and insolvency practice. He is ranked as a leading insolvency lawyer by the *Chambers* and *Legal 500* legal directories. He has significant experience and a breadth of expertise in this field and practises in a range of sectors on assignments involving:

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Michael was named in *The Lawyer* magazine's 2020 Hot 100, which recognises the most innovative and creative lawyers shaping the future of the UK legal profession from in-house, private practice and the Bar.

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Allana Sweeney is a director in Burness Paull's market leading restructuring and insolvency

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John Garner is a Managing Partner at LDC and is the driving force behind the firm's commitment to invest £1.2bn across the nation in the next three years to support the growth of UK mid-market businesses. He leads LDC's investment efforts across all 12 of its regional locations in the UK.

Since joining the firm in 2006, he has supported a broad range of fast-growing businesses across multiple regions, investing over £500 million in 30 mid-market businesses.

Investments of note in recent years include: the minority investment and subsequent IPO of Team17, the MBO of NBS from the Royal Institute of British Architects, the minority investment into iamproperty and the MBO of Commsworld. John has been a leading figure in the private equity community for more than two decades, working across a wide variety of sectors, including technology, consumer goods, business services, healthcare and manufacturing.

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Nigel Lake is an investment banker, strategic advisor, sustainability expert, entrepreneur and author. Founder and Executive Chair of Pottinger, he has lived and worked in most of the world's top fifty economies and across all major industry sectors. He has an insider's view of decision-making at dozens of the world's largest companies and has advised on hundreds of billions of dollars of M&A transactions and numerous strategic assignments.

He co-founded corporate advisory firm Pottinger in 2003, Runway 41 (a B2B virtual accelerator program) in 2017 and the global sustainability community and education network ESGX.org in 2020. He is also an advisor to Change Foods, an animal-free dairy business.

From an early age, he has had a fascination with how things work, and a passionate belief that with the right perspective there is (nearly) always a more insightful alternative to conventional wisdom. Nigel has a background in science, finance and systems thinking and is a graduate of Cambridge University.

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Rodin Genoff is the founder and Managing Director of Rodin Genoff & Associates (Sydney and Singapore). Rodin is an award-winning industry cluster expert and his company works globally mapping and activating industry clusters ranging from energy and advanced manufacturing to the bio-economy and creative industries. His work spans collaborating with the Organisation for Economic Co-operation and Development in Paris to undertaking innovative ecosystem projects in the US, Europe, Singapore and Australia. Author of several books, his latest sell-out book co-authored with Narelle Hooper, *New Women, New Men, New Economy* was launched at the Sydney Opera House at the Advance Global Innovation Awards. In 2013, Rodin was named by ABC Carbon (Singapore) as one of the world's top 100 sustainability leaders.

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Nick has been a prominent member of the Institute for Turnaround (IFT) for almost twenty years. He was a director for six years and has been an elected Fellow for ten. He has also Chaired several of their key committees. In 2014, he received the IFT's first "Above and Beyond" Award.

Nick believes in helping the voluntary sector and has worked for the Addiction Recovery Foundation, the Royal National Institute for Deaf People and has been a school governor. He is currently Chair of Action Homeless.

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