

Solvency Test Checklist for Directors

The solvency test has two parts to it being Liquidity and then the Balance Sheet.

The Liquidity test requires the company to be able to pay its accounts as they fall due in the normal course of business; and the Balance Sheet test requires the value of the company's assets to exceed the value of its liabilities, including contingent liabilities.

This checklist provides areas for considering solvency requirements.

Profit projections

- Examine up to date profit and loss projections.
- Confirm the current trading position.
- Ensure that properly qualified personnel are taking personal responsibility for their accuracy.
- Discuss with other directors and key management any items requiring further clarification.

Cashflow budgets

- Confirm the company's current cash position and the current break even point.
- Identify the company's current equity position and burn rate to confirm when the reserves (if any) will be exhausted.
- Examine for any unusual items and ask for further clarification.
- Identify all major borrowings to be repaid including the likelihood of repayments being required where no repayment date has been fixed.

Ability to realise current assets, particularly inventories and receivables

- Enquire as to the age and collectability of ALL debtors and other receivables.
- Confirm the ability to convert inventories to cash and the timing of this.
- Make enquiries around WIP and when it is likely to be invoiced to clients in the normal course of business or as extras.
- Consider representations made and ensure they are sound and logical.

Ability to comply with normal terms of credit

- Confirm the company's current bank position and banking covenants.
- Enquire as to present payment terms.
- Enquire as to any legal action taken by creditors to recover money.
- Form a reasonable view as to whether the company can meet all debts as they fall due, eg by reference to cash at bank, amount owing to trade creditors and expected realisations from debtors and other cash receipts (including government support).

Value of assets

- Confirm the company's assets are the actual present value.
- Revalue large assets to current market value in the current environment.

Contingent liabilities

- Enquire as to whether any contingent liabilities (eg liabilities under guarantees) exist.
- If contingent liabilities exist, determine projected cost and probable outcomes.