

JOINT INSOLVENCY EXAMINATION BOARD

*Joint
Insolvency
Examination
Board*

Joint Insolvency Examination (Scotland)

Tuesday 5 November 2013

ADMINISTRATIONS, COMPANY VOLUNTARY ARRANGEMENTS and RECEIVERSHIPS (3.5 hours)

ANSWER ALL FOUR QUESTIONS

EACH QUESTION CARRIES TWENTY-FIVE MARKS

SUBMIT ALL WORKINGS

The Examiner will take account of the way material is presented. Candidates should answer the questions set - and marks will not be awarded for extraneous material.

Note: References to legislation are to that which was in force on 30 April 2013. References to 'the Act' are to the Insolvency Act 1986 as amended.

References to Sections, Schedules and Rules are to Sections and Schedules of the Act and to Rules of the Insolvency (Scotland) Rules 1986 as amended.

References to Sections and Rules of other Acts, Regulations and Orders will mention the Act, Regulation or Order.

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1. Last week you were appointed Administrator of Wiley Automotive Importers Limited (“the Company”) by Proprius Bank plc (“Proprius”), the holder of a Qualifying Floating Charge.

The Company operates as a car dealer selling high value second hand vehicles sourced from the UK and overseas. The Company has banked with Proprius for over 7 years and during this period reported annual turnover of circa £20 million and net profits of £5 million. Until recently Proprius has viewed the Company as an excellent customer with its current account showing a high positive balance and high levels of cash turnover.

Following a recent bank merger Proprius undertook a review of its client files and established that it had not retained documentation or details as to the owners of the Company and had no record of ever meeting the customer face to face. As a result Proprius wrote to the Company seeking a meeting and requesting identification documentation from its owners.

Shortly after sending the letter the Company’s bank branch manager, alerted by an unauthorised overdraft position resulting from a large number of overseas payments, attempted to contact the Company by telephone. She was informed by staff that the directors and management team had disappeared without explanation and that the remaining employees were at a loss as to what to do.

You were asked by Proprius to visit the site in order to formulate a strategy to deal with the situation. It was clear from this visit that there was no one remaining capable of running the business. Following many unsuccessful attempts to establish the whereabouts of the directors it was concluded that it would be appropriate for Proprius to appoint administrators to take immediate control of the Company.

Following your appointment as Administrator you established the following:

- The yard supervisor explained that during a normal month the Company would buy and sell around 30 vehicles; maintaining a constant level of stock of around 75 vehicles. He believed that each vehicle was worth roughly £20,000.
- One of the Company’s customers; Shifty Executive Cars (“Shifty”) regularly purchased vehicles at a price significantly higher than what the members of staff thought they were worth. The sales manager at the Company has a verbal order from Shifty for 10 of the current vehicles. Payment for this order amounting to £350,000 is due to be paid in cash on collection in the next 5 days.
- The Company is not registered as an employer and has not accounted to HMRC for PAYE/NI or VAT. In addition the Company has been filing dormant accounts at Companies House.
- There is a bookkeeper working in the business. His responsibilities are limited to placing original invoices and payroll summaries onto a file; no manual or electronic accounts system was used. Since the directors’ departure the bookkeeper has been unable to locate the recent accounts files.
- The last annual return, dated 30 June 2011, lists 15 different businesses, including Shifty as shareholders of the Company. The Company bank statements show many recent substantial payments to these parties as well as the 2 directors.

Despite the difficulties, you decided that it would be in the interests of creditors to continue the trade of the business in order to best realise the stock.

Requirements

- (a) **For the purpose of trading the Company in Administration detail your obligations in relation to the Money Laundering Regulations 2007 and explain the procedures that you would put in place in this respect. (15 marks)**
- (b) **Set out the matters relating to the conduct of the Company’s directors that you would report to the Disqualification Unit and the initial information you would obtain to support your report. (10 marks)**

2. In October 2013 you joined Bombus & Co accountants as an insolvency manager. Your predecessor left Bombus & Co prior to your arrival but had prepared handover notes for each of the cases you are now dealing with. One of these cases is the administration of Barbut Limited (“the Company”).

Barbut Limited (Administration) - Handover Note

Background

The Company had been struggling for a number of years as a result of the poor economic climate, achieving a break-even position on trading. In an effort to reverse this trend, during the 6 months prior to its insolvency the Company had made efforts to improve the cash flow of the business by:

- Deferring preference share dividends saving £150,000 per year;
- Paying the 3 directors the equivalent of their net salaries (a total of £120,000 pa net) through director loans so as to save PAYE/Ni; and
- Making 5 employees redundant saving £150,000 pa

Despite these changes, due to further adverse changes in trading, the Company failed to return to profitability. As the Company was unable to service its bank debt repayments the directors concluded that there was no alternative but to appoint Administrators.

Administrators were appointed on 31 January 2013.

Statement of affairs

An extract of the statement of affairs completed and signed by the directors is shown below:

	Note	Book value £	Expected to realise £
Assets specifically secured			
Heritable property	i	750,000	600,000
Amount due to Horfield Bank	ii	<u>(600,000)</u>	<u>(600,000)</u>
		<u>150,000</u>	<u>–</u>
Assets not specifically secured			
Book debts	iii	300,000	150,000
Stock	iv	150,000	50,000
Plant and machinery	iv	50,000	25,000
Surplus from assets specifically secured		<u>150,000</u>	<u>–</u>
		<u>650,000</u>	<u>225,000</u>

Notes to the Statement of Affairs:

- The heritable property was originally purchased in 2004 for £400,000 and following a formal valuation during 2009 its carrying value in the statutory accounts was increased to £750,000. The property was subsequently valued two months prior to the administration at £600,000 and was sold to an unrelated third party on 30 April 2013 for £625,000.
- The amount due to Horfield Bank was based on a statement dated 31 March 2012. Company records showed that no payments were made since that date and interest on the loan continues to accrue at 5% pa. Horfield Bank has a standard security over the property and a first ranking bond and floating charge dated 22 September 2004.

- iii. Debts with a book value of £120,000 have been collected during the Administration, realising a total of £100,000. £25,000 of this was paid by the customer into the Company's overdrawn bank account, where it remains rather than the Administrators' account. There are 2 remaining debts:
 - a. Jone Limited has disputed their debt of £50,000 as they claim that they never received the goods concerned.
 - b. Heath Cove Limited has not responded to correspondence chasing for payment of its debt.
- iv. Shortly following appointment, as there was no potential purchaser for the business, the premises were closed and the Company's stock sold off for 30p in the £. Certain plant and machinery was also sold for £10,000. Both transactions were negotiated and completed by the Administrators' agents who withheld 10% commission and remitted the net proceeds to the Administrators. The remaining plant and machinery was placed in safe storage by the Administrators' agents.

Creditors

Other creditors of the Company include:

- Treetops Bank – Treetops provided the Company with an overdraft facility amounting to £130,000 at the date of appointment supported by a bond and floating charge dated 21 August 2008.
- Unsecured creditors – the total level of unsecured creditors is £500,000.
- Employees – the workforce was employed by a related company and provided on a contract basis. As such there were no employee liabilities within the Company.

Statutory matters

- All statutory reporting is up to date.
- A meeting of creditors was held at which the basis of the Administrators' remuneration was approved on a time cost basis. Shortly following the meeting remuneration amounting to £32,500 was paid.
- The meeting of creditors also resolved that the Company would exit Administration into Creditors Voluntary Liquidation pursuant to Paragraph 83 of Schedule B1 to the Act.

Requirements

- (a) Outline the steps that you would take to realise the remaining assets of the Company. (10 marks)**

As a result of your realising the remaining assets, the following transactions were completed:

- The remaining plant and machinery was sold for £25,000.
- You settle Jone Limited's and Heath Cove Limited's claims, at 75% and 50% of the debt respectively.
- Interest receivable during the course of the Administration amounted to £150.
- All other claims realise 20% of their gross value.
- Total legal costs for the entire case amount to £45,000 and Administrators' costs total £80,000.

- (b) Assuming that all assets are dealt with and making other reasonable assumptions prepare a final Receipts and Payments account for the Administration. (15 marks)**

NOTES:

**Corporation tax rate 30%, ignore indexation allowances
Ignore VAT**

3. Your office has been contacted by Orinoco Pension Limited, a firm of independent trustees in relation to the Alderney Products Limited Defined Benefit Pension Scheme (“the Scheme”).

The Scheme has been underfunded for some time and the employer, Alderney Products Limited (“the Company”) has entered into a recovery plan providing for the deficit to be paid off over 15 years. Whilst profitable the Company had been struggling to meet its obligations into the Scheme.

Mr Roberts of Roberts & Co, a firm of insolvency practitioners, has written to the Scheme’s trustees (“Trustees”) on behalf of the Company setting out the situation and proposals for dealing with it. The letter’s contents can be summarised as follows:

- The Company cannot afford the level of contributions set under the recovery plan and will be unable to do so for the foreseeable future.
- The Company’s assets and liabilities are:

	Assets		Liabilities
	£’000		£’000
Book debts	500 (book value)	HMRC	75 (all current)
Stock	150 (book value)	Trade creditors	350
Heritable property	750 (valuation)	Employees	300 (if made redundant)
Plant and machinery	120 (valuation)	Pension Scheme	3,700 (buy out deficit)
		Overdraft	150
		Other creditors	100
Total assets	<u>1,520</u>	Total liabilities	<u>4,675</u>

- The overdraft is provided by Bungo Bank and is secured by a standard security and bond and floating charge dated 1 May 2007.
- There are 2 alternative proposals:

(i) Proposal A (directors’ preferred option)

- The Company will enter into an invoice finance agreement and pay the initial proceeds to the Scheme. The Company has an agreement (subject to agreement of this proposal) with a reputable invoice finance company to provide funding at 75% of the book value of the debts.
- The liability of the Company to the Scheme following the above finance payment will be limited in any and all events to £1 million.
- The Scheme will be granted a first ranking standard security over the Company’s heritable property and a bond and floating charge ranking after both Bungo Bank and the Invoice Finance provider.
- The Company will relocate and sell its heritable property in 5 years’ at which time it will pay off the £1million due to the Pension Scheme.
- These terms have been agreed by the relevant stakeholders including Bungo Bank.

(ii) Proposal B (if Proposal A is not agreed within 48 hours)

- The directors of the Company will appoint Administrators to the Company. Due to the nature of the Company’s trade Administration is considered to be appropriate insolvency procedure.
- The directors will buy, through a new company, the trade and assets of the Company from the Administrators. A price of £25,000 for the goodwill and £100,000 for the plant and machinery of the business has been agreed between the directors and the proposed administrators. In addition they will pay the market value of 50p in the £ for the stock.
- The employees of the Company will be transferred to the newly formed company and it will agree to take on all associated liabilities. All other liabilities will remain in the Company.
- The acquiring company will help collect the book debts for 10% commission and they think they will be able to collect 80% of the ledger.
- The acquiring company will vacate the existing premises.

The Trustees of the Scheme are unhappy that they are being given 48 hours to provide a response and the undue pressure being exerted upon them. They are also highly sceptical as to whether the Company will survive for the 5 years under Proposal A.

The Trustees have asked for your advice as to how the outcome for the Scheme compares between proposal A and proposal B. In the latter case they wish to understand the outcome in both a situation where proposal B is successfully implemented and, assuming no material change in its financial position, where the Company fails prior to the expiry of the 5 year period.

The Trustees have requested that you meet with them to discuss the situation in advance of them having a meeting with Roberts & Co.

Requirements

- (a) Using the information provided and where appropriate stating your reasonable assumptions, set out a comparison of the outcomes from the Scheme's perspective. (15 marks)**
- (b) Set out a list of commercial points relating to the proposals that you would cover with the Trustees in the meeting. (5 marks)**
- (c) Set out the occasions when and the reasons why interaction may be required between the Scheme and the Administrators. Detailed procedural steps are not required. (5 marks)**

NOTES:

Ignore tax

Ignore office holder, legal and agent costs

PLEASE TURN OVER

4. You were appointed Administrator of Fortress Homes UK Limited (“the Company”) by its directors several weeks ago and, after a period of trading, you successfully sold its trade and assets. The secured creditors have been paid in full and there are sufficient residual funds to enable a large distribution to non-preferential creditors of the Company.

Whilst your actions have resulted in the best return to creditors there is a significant disgruntled creditor; Mott (Sunderland) Limited (“Mott”) that represents approximately 55% of the total unsecured debt. Mott had wished to acquire the trade and assets but had been unsuccessful. Mott has stated that it would be their intention to attend all creditors’ meetings and vote against all resolutions proposed by the Administrators.

You have decided to convene an initial meeting of creditors and have instructed your case manager to draft the relevant documentation.

Requirements

- (a) Outline the steps you would take to handle the situation with Mott in the lead up to the meeting of creditors. (5 marks)**
- (b) Set out in a note to your case manager the process that you would follow in the event that every resolution proposed at the initial meeting of creditors is rejected. (20 marks)**