

JOINT INSOLVENCY EXAMINATION BOARD

OVERALL COMMENTS ON THE NOVEMBER 2016 EXAMINATION (SCOTLAND)

To some extent these overall comments repeat, or in some cases amplify, comments that have been made by the Examiners on their individual papers. There are however comments of general application which have been made so that candidates are better informed about how best to present scripts in order to maximize their chances of passing the examination.

Poor handwriting continues to be an issue. Candidates must appreciate that no marks can be awarded for a word or phrase that is illegible. There is a limit to how long the Examination Team can be expected to spend trying to decipher handwriting that is difficult to read. This issue has meant that candidates have almost certainly lost marks this year.

In too many cases candidates do not refer to relevant case law, even when the requirements specifically ask them to do this. Candidates are not expected to have an encyclopedic knowledge of the names of decided legal cases, but should be able to augment their answers by referring to the principal legal case(s) that support what they are saying.

This year some candidates did not take sufficient care to ensure that they complied with the exact requirements of the question. This was particularly true of those requirements which were more specific in nature. If, for example, a requirement asks a candidate to make a recommendation as to a course of action or to opine on an issue, that is what should be done. Candidates who sit on the fence or who shy away from making a decision are losing marks by not answering the question and, in addition, are likely to present scripts which attract lower holistic marks.

The inability of too many candidates to apply their knowledge of the law and best practice to solving a practical problem is becoming a real issue. Candidates who can do this to good effect invariably present scripts that earn good marks, but they are in a minority. Too many candidates present scripts that show they know the applicable law but which fall short when applying this to the facts of the question. Candidates know that in the region of 40% of the total marks available in any paper will be awarded for the application of knowledge to practical situations. Not being able to do this means that they are putting themselves at a material disadvantage. It is also the case that, when considering the award of holistic marks for a question, the Examination Team will give greater weight to those points made which demonstrate that the candidate is taking a rounded approach to tackling the problem posed rather than those points made which simply lay down the basic rules without going on to apply them.

Candidates need to be reminded that compensating for the inability to deal with a practical situation by “brain dumping” all they can think of which is (or may be) related to the subject of the question is an approach which does not and will not work. This approach is likely to earn some marks, almost by default as mark-worthy targets are hit at random. However, the Examination Team’s experience is that this approach tends to result in candidates regurgitating checklists or similar which show all too clearly that the candidate is not focused on the question and its requirements. The flow of consciousness which is the product of the “brain dumping” approach means that, too often, candidates present pages of script which may not in themselves be wrong but which are either irrelevant to the question or are on point but too comprehensive for the marks on offer. Apart from anything else, this approach wastes valuable time. It is obvious to the Examination Team when a candidate is “brain dumping” and the result is invariably reflected in the award of low holistic marks.

Candidates who aspire to pass a paper should be aiming to present a script which earns twelve or more holistic marks. Ultimately the main determinant of whether a script passes or fails is not how many holistic marks it has been awarded but the Examination Team’s assessment as to whether or not it is good enough. However, holistic marks are becoming an increasingly potent indicator of the quality of a script. A script that has been awarded twelve holistic marks contains four answers that, on average, have been marked as being acceptable. Candidates should be aware that scripts attracting fewer than twelve holistic marks are increasingly unlikely to be considered pass-worthy.

JOINT INSOLVENCY EXAMINATION BOARD

LIQUIDATIONS (SCOTLAND)

EXAMINER'S REPORT AND MARK PLAN FOR THE NOVEMBER 2016 SITTING

General comments

All candidates appeared to have sufficient time to complete all the questions, but handwriting continues to be an issue.

As with previous years, an inability to apply knowledge to practical issues continues to be a challenge with candidates. Candidates need to apply the "so what" principle to take their answer that one stage further and gain the marks on offer. Equally, easy marks were lost by failing to answer the question asked, e.g. forgetting to state a recommendation. Candidates still failed to set out their answers as a file note or a letter to clients when the question directed it.

Candidates should also consider the mark allocation available, as this will indicate the level of detail required and therefore the time to allocate to answering that question.

Similar to last year there was very little if any mention of relevant case law even when specifically asked for.

As in previous years, candidates performed well in the numbers question, especially when preparing the Statement of Affairs.

The introduction of partial licensing necessitated the inclusion of other insolvency procedures, and this was tested in Q3 of this paper. Q3b required candidates to consider corporate insolvency and Q3c personal. This was the worst answered question overall.

Question 1

- a) Write a file note of the practical and legal steps you need to consider in the Liquidation to resolve the issues you have identified. You should make reference to relevant legislation and case law. (21 marks)**

Candidates were required to set out the practical and legal steps to address a variety of issues in relation to a company that had recently been placed into Creditors Voluntary Liquidation and ceased trading. The issues included the protection of essential supplies, ROT, environmental issues, potential third party funds, contractual licence issues, drawing remuneration and the retirement of one of the office holders.

This question was generally answered well. There were several issues so candidates who provided a few comments on each one tended to score highly.

The question asked for practical steps, and despite this some candidates failed to apply their knowledge to the facts of the question, stating generic advice or even copying out legislation. This was particularly evident when discussing ROT and disclaimers for which very few marks could be awarded (with some answer booklets including numerous pages on ROT alone). Candidates needed to apply their knowledge to the question to gain the marks on offer. Equally quite a few easy marks were missed if candidates failed to include obvious practical comments such as "obtain a copy of the lease" and "obtain an agents valuation".

The ROT issue was based on the Blue Monkey Gaming Ltd case law and candidates did not mention this although some mentioned that the onus was on the supplier to identify the goods.

- b) Set out the issues arising from the EC Regulation on Insolvency Proceedings that you may encounter when dealing with the French distribution centre (4 marks)**

This question was answered very poorly, with virtually no marks gained, particularly as the question specifically directed them to the EC regulations. Candidates failed to apply the facts of the case or state that

as the company was in CVL you need a court order to confirm the EC Regs apply and recognise the UK CVL as the main proceedings, or that you would have the ability to appoint a French Liquidator to safeguard the French property.

Question 2

Write a file note for the Liquidator setting out:

- a) **The duties and powers the Liquidator has to investigate the affairs of the Company (5 marks)**
- b) **The actions the Liquidator could take to recover assets for the creditors. (11 marks)**
- c) **Who should be included in your Director Conduct Report and on what basis (4 marks)**

Question 2 was based on a company in CVL where the Liquidator's investigations had uncovered various challengeable transactions.

Some candidates identified the duties and powers the Liquidator has to investigate the affairs of the company.

In Q2b there were a variety of actions candidates could identify enabling most candidates to achieve a reasonable score. Quite a few candidates avoided dealing with the loans secured by floating charges altogether.

Q2c asked candidates to identify who should be included in the Directors Conduct Report and on what basis, with the potential directors holding a variety of roles and responsibilities. This was well answered.

- d) **The steps the Liquidator should take to deal with the letter received from Mary (5 marks)**

To score well on this question, candidates were required to be aware of the *Insolvency guidance paper: - dealing with complaints*, however many of the points in that guidance paper are practical and therefore even if not familiar with this guidance paper candidates could have scored marks for stating practical comments such as "acknowledge the complaint". The lack of awareness of the Insolvency Gateway was also concerning.

Overall candidates performed poorly on this question, this was disappointing as one would expect them to be familiar with the procedures for dealing with complaints, even if this wasn't an obvious topic to revise for the exam.

Question 3

- a) **The consequences on the above matters of the winding up petition being presented and how these can be managed. Make reference to relevant legislation and case law. (12 marks)**
- b) **the other options which are available to the Company to enable it to continue trading, and how these would be achieved given the outstanding winding up petition. State which option you would recommend and why (9 marks)**
- c) **the options available to Pierre for dealing with the statutory demand served on him personally. Explain how each option could affect his directorship of the Company. State which option you would recommend and why (4 marks)**

This question was answered very poorly with a number of candidates scoring no marks for certain parts of the question.

Q3a required candidates to consider how various matters impacted a company where a winding up petition had been presented. The matters included the fact that the company wished to continue trading, an Irritancy Notice had been issued by one of the landlords, together with a threat of a calling up notice in respect of the owned store.

Those who did score marks, generally did so by identifying the consequences of the winding up petition on the company trading e.g. dispositions and validation. The property related matters in particular were not answered well and no candidates referred to relevant case law.

Q3b required candidates to consider other options available to the director to enable the company to continue trading and was also answered very poorly. The question was also testing candidates knowledge of other corporate insolvency and restructuring options.

Marks were available for identifying that the debt was disputed, alongside seeking a settlement with the petitioning creditor, identifying a CVA or Administration. Candidates who were looking to do well on this question would have had to mention administration and/or CVA as an option.

Candidates failed to state a recommendation despite the question clearly requesting this in the requirements.

Q3c required candidates to consider the options for the director who had a statutory demand he couldn't satisfy served on him and was testing candidates' personal insolvency knowledge and its impact on holding a directorship of a company. Most candidates scored very poorly if they attempted the question at all.

Question 4

- a) Prepare a Statement of Affairs (11 marks)**
- b) Prepare a distribution statement (3 marks)**

In preparation for your meeting with Blake and Miranda tomorrow, write a file note explaining:

- ci) the purpose of the statement of affairs (3 marks)**
- cii) the practical steps a Liquidator should take if Blake and Miranda request an early distribution (3 marks)**
- d) State what matters you should consider before accepting an appointment as Members' Voluntary Liquidator to the Company (5 marks)**

This MVL and ethics question related to a sawmill company which the directors wished to wind up solvently.

Q4a and Q4b required candidates to prepare a statement of affairs and distribution statement. The Statement of Affairs was generally done well, with some easy marks available.

Q4ci required candidates to set out the purpose of the statement of affairs and was answered fairly.

Q4cii asked candidates to set out the practical steps of an early distribution and was answered fairly well. Candidates failed to focus on practical considerations, for example seeking tax clearance or taking security on the cottage.

Q4d was an ethics question, asking candidates to identify the matters to be taken into consideration before accepting an appointment as Liquidator. This question was answered well with candidates recognising the need to identify significant professional relationships, and the restrictions if the practice or proposed Liquidator had previously undertaken audit work.

EXAMINER'S MARK PLAN

LIQUIDATIONS (SCOTLAND)

NOVEMBER 2016

Question 1

Requirements

(a) Write a file note of the practical and legal steps you need to consider in the Liquidation to resolve the issues you have identified. You should make reference to relevant legislation and case law.

(21 marks)

File note layout
Cessation of supply from software supplier: Insolvency (Protection of Essential Supplies) Order 2015, s233 applies to IT suppliers of software. Contact supplier and advise of your appointment Provide personal guarantee for costs incurred after appointment (nb insolvency related terms in the contract (e.g. higher tariffs) can still be relied on and exercised as company is in CVL) Calculate how long you will need services for and remember to withdraw undertaking once services no longer required
ROT: <i>Blue Monkey Gaming Ltd v Hudson & Others [2014]</i> onus is on the claimants to locate and identify ROT goods. Only obligation on the office holder where a potential claim has arisen is to provide supervised access to alleged owner for purposes of identification and then to adjudicate claim. Liquidator to consider if Mallera has unequivocally demanded return of goods and revoked express or implied right to sell. Liquidator to advise Mallera need to identify goods (do they have a local agent?) Review documentation, establish if valid ROT claim and value, consider contract law jurisdiction, consider if you need the helmets or can return them. Consider whether original state has changed. If co-mingled goods and not uniquely identifiable, vendors have interest in single bulk as tenants in common, review contract to see if have express contractual provision as to where title rests.
Deposit: Identify whether bank account is overdrawn, if not charity could use tracing argument. If bank account is overdrawn charity is an unsecured creditor Consider how charity paid deposit - if by credit or debit card consider claiming under s75 Consumer Credit Act Consider CDDA if took deposit knowing couldn't provide goods.
Health and safety issue re contaminated waste: Can use s178 to disclaim onerous property. Consider costs of cleaning up site v value of lease. Review lease and get lease valued. Part2A of the Environmental Protection Act 1990, office holder not personally responsible for remediation unless contamination is as a result of any act done or omission made by him that it was unreasonable for a person acting in that capacity to do or make
Licence contract: consider whether value in licence and is it assignable. If so continue to pay and use brand rights to maximise value of stock. Seek premium for assignment of IP rights? Consider whether you can sell branded goods if in breach. Consider terms and conditions of ski holiday competition, if can't be withdrawn, winner will be treated as unsecured creditor re the debt as the company became subject to the debt after the date of appointment by reason of an obligation incurred before that date.
Fees: Committee to fix the basis of your remuneration (I(S)R4.32, R4.68 and s53 B(S)A) and Liquidator will need to call committee meeting to obtain approval. Per SIP 9 need to disclose to committee their rights under the insolvency legislation. Liquidator to provide committee members with copy of SIP 9 and R3 Creditor Insolvency Guide. Liquidator to provide fee estimate (unless already presented at creditors meeting)
When requesting approval of fees Liquidator should provide the following information; work done and why necessary split into common areas of activities; actual costs of the work including any expenses incurred in connection with it; whether the work has provided a financial benefit to creditors, and if so what benefit (or if the work provided no direct financial benefit, but was required by statute). Also consider complexity, exceptional responsibility, effectiveness and value and nature of assets Liquidator to chair the committee meeting and all committee members to vote on fee and disbursement resolutions, resolutions passed if majority are in favour. Appeal periods when writing to creditors advising what has been agreed by committee
Joint Liquidator retiring: s171 and I(S)R4.23 (call a creditors meeting, 28 days' notice, prepare progress report, consider if Joint needs to be replaced).

Consider release I(S)R4.25

(b) Set out the issues arising from the EC Regulation on Insolvency Proceedings that you may encounter when dealing with the French distribution centre.

(4 marks)

Apply to Court I(S)R4.84 to confirm EC Regs apply and give notice to creditors in EC states (other than UK) (Article 40 and 42). UK CVL is then recognised as main proceeding and governing law automatically covers all assets in France (Article 4) (except for employees and ROT assets).
Do you need to open formal secondary proceedings in France, can only do so if there is an establishment i.e. Skiiz carries out non-transitory activity, evidence suggests it does
If there is an establishment UK Liquidator (i.e. member state liquidator) could appoint French liquidator. This would safeguard French property, governing law would be French (Article 8).
To avoid opening secondary proceedings, give undertaking to French employees to pay them in accordance with French law (Collins v Aikman). French law applies (Article 10)

Question 2

Requirements

Write a file note for the Liquidator setting out:

(a) The duties and powers the Liquidator has to investigate the affairs of the Company.

(5 marks)

File note layout

SIP2:

Duty to investigate what assets there are (including potential claims against third parties including the directors) and what recoveries can be made

Investigations to be proportionate to the circumstances of each case, steps and outcomes to be reported clearly

Write to creditors inviting them to bring any relevant matters to your attention; question officers; compare statement of affairs with last audited or management accounts; secure, list and review books and records from last 6 months

Duty to document at the time, initial assessments, investigations and conclusions

s235 duty of directors to co-operate with Liquidator and attend on him to provide information. This would apply to all current and former directors, not Loretta or Hank

s236 allows Court to summon before it any person (i.e. Loretta, Hank and solicitor) capable of giving information or require them to produce property of the company.

[Re Harvest Finance [2014]] if the solicitors have a public duty to comply with the request Court unlikely to award costs under IR9.6 (4)]

s234 obtain court order requiring solicitors to deliver up books and records

(b) The actions the Liquidator could take to recover assets for the creditors.

(11 marks)

Dixienotes bank transfer: Were the dividends paid out of distributable reserves? If not Dixienotes can be required to pay back under s847 CA06. Could also be a preference under s243

s213 Fraudulent trading, has the Company made that payment as a means of putting assets out of the reach of creditors? S213 has extra-territorial effect and can also be used to bring proceedings against Dixienotes [Jetivia SA v Biltta (UK) Ltd [2015]]

s213 also applies to diversion of cash receipts and assigned book debts

Flat disposal by Loretta/assigned book debt: s242, gratuitous alienation. Loretta acquired the flat for significantly less than the flat was worth within 2 years of date of liquidation. Loretta is a connected party as the former wife of Hank (s435) so insolvency will be presumed. Defence unlikely to be successful.

S242 also applies to assigned book debt

Under s242, Court can make order restoring the position, but won't prejudice interests of third party who acquired property in good faith and for value. Can therefore pursue Loretta for profit made on sale
Consider if the nightclub is also owned by the company and therefore could sell to realise assets for creditors

Mary loans: s244 extortionate credit transactions, consider whether risk justified interest rate. Loan made within 3 yrs. of liquidation date. Remedy is to set the transaction aside and recover interest
S245. Floating charge is invalid except to the extent of the aggregate of any fresh consideration given for it. Creation must have been within relevant time period. Here is Mary connected, if yes then relevant time is 2 years, if not relevant time is 12 months. However, s245 doesn't apply to June 2014 loan as made over 2 years ago and outside of relevant time
Jan 2015 loan with charge created Feb 2015, consider if charge has been registered. If not registered within 21 days then charge is invalid. Also consider Re Shoelace Ltd 1993 If charge registered consider s245. Mary resigned 30 Jan 2015 so not a de jure director at the time the charge was created/registered. However evidence suggests she is a shadow director therefore she is still a connected person (s249), insolvency is presumed and charge created within relevant time period of 2 years. Remedy is that assets are no longer covered by the security and are all available for the creditors Can Mary rebut presumption that company wasn't insolvent at the time as company was able to pay debts as they fell due, because of her loans? [Bucci v Carmen Re Casa Estates (UK) Ltd (In Liquidation) [2014]] held that if a company is only able to pay debts by incurring further debt, in any commercial sense it was insolvent.
Inability to pay suppliers: s214 wrongful trading – remedy is for directors to contribute to assets of the company, potentially £250k being the amount the creditors increased by between July and October – could they argue thought business would survive with planned music promotions
Solicitors: s246 Solicitors can't hold a lien over books, papers and records
Wanda in Spain: What are her assets, consider if it's worth pursuing her in Spain? Take local legal advice
Mary personally liable for debts of the company incurred whilst acting as a director, despite being disqualified from doing so
s212 recover funds from directors for misfeasance

(c) who should be included in your Director Conduct Report and on what basis.

(4 marks)

<p>Need to consider all directors ("any person occupying the position of director, by whatever name called" (s251)) in 3 yrs. preceding date of appointment</p> <p>Wanda - de jure director. Properly appointed in accordance with articles of association and registered at Companies House and in the PSC Register</p> <p>Earl – could argue either de facto or shadow director "person in accordance with whose instructions the directors (Wanda) of the company are accustomed to act" (s251)</p> <p>Hank - non executive director is a de jure director</p> <p>Mary - de facto director. Acts as a director and is treated as a director by the board despite a lack of formal appointment. She was also a director in the last 3 years</p>

(d) The steps the Liquidator should take to deal with the letter received this morning from Mary.

(5 marks)

<p><i>Insolvency guidance paper: dealing with complaints</i></p> <p>Follow own internal formal complaints procedure</p> <p>Acknowledge complaint promptly</p> <p>Make Mary aware of the steps you are taking to review and respond to her complaint and the likely timetable for your response</p> <p>Ascertain background facts as quickly as possible and seek additional information from Mary as required</p> <p>If you feel the complaint is unjustified, provide Mary with a clear explanation of reasons for that conclusion e.g. the relevant legislation affecting your duties as a Liquidator</p> <p>Notify Mary that she can refer her complaint to the Insolvency Complaints Gateway who will then pass to your authorising body for further enquiries</p> <p>Notify your internal risk team of the complaint and consider whether your professional indemnity insurer needs notifying</p> <p>Consider whether the complaint should be reviewed by another insolvency practitioner in your firm or an independent practitioner</p>
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Question 3

Requirements

Draft a letter to Pierre setting out:

(a) the consequences on the above matters of the winding up petition being presented and how these can be managed. Make reference to relevant legislation and case law.

(12 marks)

Letter format
Bank account will be frozen once bank hears that winding up petition has been issued, this will prevent Furnichere trading.
Other creditors could become aware of the petition and support it
s127 IA86 states that dispositions of company property (i.e. payments out of the company's bank account) made after the date of the presentation of the petition (31 October 2016) are void unless the court orders otherwise. If wanted to sell Stirling store would need to apply to Court for a validation order consenting to the sale. Court would normally approve property sale if no prejudice to creditors i.e. transaction is made in good faith, at arm's length and at fair market value [Re Wilson v SMC Properties Ltd [2015] Therefore in order to make payments out of the bank account the company or a creditor will need to apply for Court permission to exempt either a transaction or class of transactions Permission will be granted if the payment is unlikely to have the effect of reducing the assets available to the creditors (Re Grays Inn Construction) The Court will refuse to validate payments in the ordinary course of business if the company is making losses and trading on is unlikely to benefit the creditors (Re A Company (no 007523 of 1986)) Court will agree to pay wages which would have to be paid in any event (Re Web Electrical) or to pay a supplier to maintain supplies essential to trading on (SA and D Wright Ltd [1992]) If Furnichere believes company will survive he should apply to Court for a validation order for classes of transactions If validation order obtained he will need to notify the bank
Winding up petition and/or order doesn't affect rights of secured creditor to repossess the Stirling store Notice of enforcement: Would want to inform the Glasgow landlord that a winding up petition has been issued. Pierre needs to check whether he has received this notice from the Edinburgh landlord, which can be served by post, fax, e-mail, by hand or personal delivery to the tenant or registered office. Notice can only be served if Furnichere is already in rent arrears equal to or exceeding seven days rent. Pierre needs to check the rent arrears position on the Glasgow and Edinburgh stores. Confirm whether there are any rent deposits in place that could be used to settle the rent If the company wanted to settle any arrears they would need permission from the Court under s127

(b) the other options which are available to the Company to enable it to continue trading, and how these would be achieved given the outstanding winding up petition. State which option you would recommend and why.

(9 marks)

Disputed debt: Company can apply for an injunction restraining the petitioner from advertising the petition As the advertisement is a pre-condition for making the winding up order, this will prevent the winding up taking place (Court Rules) Grounds on which Furnichere could apply for an injunction would be debt genuinely disputed, Furnichere able to pay its debts, or there is a counter-claim or set off which would extinguish the debt Here, Furnichere states debt is disputed. Furnichere's solicitor should speak to creditor's solicitor to see if a settlement can be reached
CVA: Company could consider a CVA. Company will either need to get creditor to withdraw the petition or persuade the Court to grant an adjournment to the winding up hearing in order to achieve this option If creditor agrees to CVA proposal, if petition served but not advertised – petitioner must apply to Court to withdraw petition (IR4.15). If petition served and advertised, petitioner must apply at hearing for petition to be withdrawn (s125). If the petition has already been advertised, Company could also file witness statement opposing petition not less than 5 business days pre hearing (IR4.18) stating intend to propose CVA

Pierre should consider whether a CVA would be accepted by the creditors, on what terms and whether it would be achievable before he takes any further action
Special Manager: Could apply to Court for Provisional Liquidator to be appointed, and then in turn appoint a Special Manager to trade the business (s177). Candidate should discount this, as not practical given circumstances
Administration: Court could grant administration order instead of winding up order (s125), need to ensure could achieve administration purpose
Recommendation: Candidate to state sensible recommendation

(c) the options available to Pierre for dealing with the statutory demand served on him personally. Explain how each option could affect his directorship of the Company. State which option you would recommend and why.

(4 marks)

Sequestration: If Pierre takes no action and can't pay then he will be made bankrupt. Can't be a director of Furnichere
Trust Deed: Could still be a director of Furnichere
Debt Arrangement Scheme (DAS): Need to have a proposal that would pay all debts off in a period of 10 years or less. Could still be a director of Furnichere
Consensual: Find alternative funds to settle rent. Pierre would become a creditor of the Company (assuming it enters a form of insolvency)
Recommendation: Candidate to state sensible recommendation

Question 4

Requirements

In preparation for tomorrow's meeting:

- (a) prepare a statement of affairs for the Company as at 31 October 2016, stating any reasonable assumptions that you make. (11 marks)
- (b)

Hornbeam Sawmill Ltd (In MVL)	Note	Book Value £'000	ETR £'000	Ref
Statement of Affairs as at 31 October 2016				
Section A – Summary of Assets				
Assets subject to securities				
Land and buildings	1	355.0	450.0	a
Less due to Bank	9	(50.0)	(50.0)	
Surplus		305.0	400.0	
Hire purchase assets	3	15.0	15.0	
Less due to HP company	3	(10.0)	(10.0)	
Surplus		5.0	5.0	
Floating charge assets				
Intangible assets	4	20	25	b
Stock	2	50.0	45.0	c
Work in progress	5	75.0	35.0	
Trade debtors	6	200.0	160.0	d
Other debtors	6	40.0	32.0	e
Plant and machinery	3	185.0	252.0	f
Fixtures and fittings	2	30.0	9.0	
Cash in hand		15.0	15.0	
Surplus from Landlord buildings		305.0	400.0	
HP asset surplus	3	0.0	5.0	
Section B – Summary of Liabilities				
Available for preferential creditors			973.0	
Less preferential creditors	10		(14.5)	g
Net property			963.5	
Prescribed Part			0.0	h
Available for floating charge holder			963.5	
Less due to Bank			0.0	
Floating Charge Surplus			963.5	
Less unsecured creditors	7, 11, 12		(331.5)	i
Surplus after creditors paid in full			632	
Shortfall re Bank			0.0	
Shortfall re unsecured creditors			0.0	
Available to members			632.0	

Workings

Ref	Note
a	Sawmill (£335k) and cottage (£115k)
b	Patent etr £25k (patent legally belongs to the Company if developed in the ordinary course of directors employment).
c	90% recovery (£50k*90%)
d	80% recovery (£200k*80%)
e	80% recovery (£40k*80%)
f	NBV is net of HP assets (£200k-£15k), ETR specialist kit net of auction costs =£252k (£280k-£28k)
g	Occupational pension
h	Bank paid in full therefore security settled, no Prescribed Part
i	Trade creditors £58k, other taxes and social security £25k, directors loans £79k. Need to include additional liabilities (CCL tax £17.5k (gas) and £17.5k (electricity), plus contract termination charges £29k) redundancy pay £105.5k

(c) prepare a distribution statement for each shareholder, stating any reasonable assumptions that you make.

(3 marks)

Hornbeam Sawmill Ltd (In MVL) Distribution Statement

Blake

	£k
Members surplus	379.2
Total	<u>379.2</u>

Assumptions

Blake owns 60% of the Company

Patent belongs to the Company

Assume Company settles Blake's directors' loan of £29k prior to members distribution

Miranda

	£k
Distribution in specie	115.0
Members surplus	137.8
Total	<u>252.8</u>

Assumptions

Miranda owns 40% of the Company

Miranda receives managers cottage valued at £115k as distribution in specie

Assume Company settles Miranda's directors' loan of £50k prior to members distribution

(c) write a file note explaining:

(i) the purpose of the statement of affairs.

(3 marks)

File note layout
Detail the company's assets and liabilities (present, contingent and future) to evidence that the company is solvent and thus supports the Declaration of Solvency
Statutory requirement s89(2)(b) IA86
Provides the Liquidator with details of all the company's assets together with current valuations, and provides details of all liabilities to settle
Calculates the estimated return to the members.
Provides creditor and shareholder details so the Liquidator can obtain details of their claims.

(ii) the practical steps a Liquidator should take if Blake and Miranda request an early distribution.

(3 marks)

Advertising for claims
Obtaining tax clearance
Carrying out an assessment of the business and make a provision for any debts, liabilities or expenses that haven't been agreed
Assessing any potential health and safety claims
Reviewing the indemnity - if they are emigrating to Australia is it worth anything? Consider taking security over the manager's cottage or obtain an indemnity from a third party

(d) state what matters you should consider before accepting an appointment as Members' Voluntary Liquidator to the Company.

(5 marks)

Significant Professional Relationships ("SPR") – identify if you or your Firm has any SPR with the Company, the directors or any other connected parties – conflict checks
Can take appointment if practice or proposed Liquidator has previously carried out audit work within the previous 3 years, but consider whether there are any other circumstances that give rise to an unacceptable threat to compliance with the fundamental principles
Identify your client and carry out anti-money laundering checks
Agree engagement letter and fees
Consider obtaining an indemnity from the directors
Confirm that Declaration of Solvency is likely to be substantiated by events (especially if previously been auditor)
Consider whether have sufficient experience and staff to take appointment

JOINT INSOLVENCY EXAMINATION BOARD

ADMINISTRATIONS, COMPANY VOLUNTARY ARRANGEMENTS AND RECEIVERSHIPS (SCOTLAND)

EXAMINER'S REPORT AND MARK PLAN FOR THE NOVEMBER 2016 SITTING

General comments

There were a number of candidates that did not fully address all parts of the question requirements or who extended them to a subject that they were more comfortable answering, wasting time and effort. Candidates should start tailoring their answer to the specific circumstances and what question is asking instead of "dumping" everything they know on a topic in the hope of picking up marks.

With two large numerical questions there was an opportunity for candidates to score a lot of marks for what should have been relatively straightforward questions however there is still a clear lack of understanding when it comes to preparing financial statements, especially on calculating and presenting the costs/expenses.

Generally questions that required thought and practical experience were not answered particularly well by a significant proportion of candidates. Candidates are also failing to provide opinions where questions are asking for them and therefore missing the overall point of the question.

Calculation of trading figures, VAT and corporation tax still present a considerable challenge for candidates with the majority unable to demonstrate even a basic understanding of their impact on financial reports.

Question 1

This question focused on the end stages of an administration where exit would be via dissolution.

(a) Draft an expected final receipts and payments account for the Administration period. (15 marks)

Generally this part of the question was well answered with one candidate almost scoring full marks. The majority of candidates presented their account in an appropriate format and included the key items split between fixed and floating charge assets.

Candidates were required to calculate two employee claims and the majority of candidates successfully established the relevant preferential liability. A few candidates struggled to calculate the employees' weekly wage from an annual salary; dividing this figure by 12 and then 4 rather than using 52 weeks.

Very few candidates stated their assumptions in relation to VAT and on occasion presented a mix of figures including and excluding VAT. Few candidates demonstrated any understanding of the relevance of VAT to the question.

The deduction of the Administrator's fees from the prescribed part seemed to cause most candidates a problem, with most simply not recognizing that these would be deducted directly from the prescribed part funds.

The better candidates identified that as a final receipts and payments account the cash balance at the end of the period should have been nil.

(b) Assuming that you have completed your distribution, set out the key steps to finalize the Administration. (10 marks)

Most candidates were able to list the legal steps to finalize and Administration but surprisingly very few were able to list practical steps.

The better candidates recognized that the company would move to dissolution and were therefore able to list the correct steps to achieve this.

Question 2

This question was split into two areas – part (a) focused on a CVA and part (b) on two relatively complex reservation of title claims.

- (a) **(i) Set out for the Directors how such situations can possibly be resolved without the need for the Company to enter Administration and provide an overview of the process that would typically be followed. (6 marks)**

The majority of candidates identified that a variation could potentially be used to deal with the situation but there was a clear lack of practical understanding of the process to be followed.

- ii) Explain your key ethical considerations as to whether you could accept the appointment as Administrator. (4 marks)**

Generally candidates understood the key ethical principles that would need to be considered however very few applied these to the specifics of the question when answering and simply listed what the principles were.

- (b) **Set out any additional information you would seek from the parties claiming ownership of the goods concerned. Based on the information provided, summarise the extent to which you think the suppliers will have a valid reservation of title claim and, assuming they do, how you would deal with the situation. (15 marks)**

Generally the answers were poor, the better candidates picking up marks for logically thinking through the issues and making practical suggestions as to how the situation could be dealt with. Most candidates tended to write down everything they knew about ROT which ultimately led to answers going off at tangents. There was a lot of duplication on answers across both claims i.e. send questionnaire, do stock take, rather than focusing on the specifics of the question and trying to think through logically and practically how they would deal with that claim.

Only a few candidates provided an opinion on whether they believed the claims were valid and again demonstrates candidates are failing to read the question fully and understand what they were being asked to provide as an answer.

Most candidates were able to pick up marks for stating basic information required to establish whether the creditors have a valid claim.

Question 3

- (a) **Set out and explain the key concerns that the Administrator would have and the issues she would face trading the Company in Administration. (15 marks)**

Candidates were required to identify risks from the given scenario of an electroplating business supplying the medical sector.

Generally most candidates were able to identify a few issues that could be relevant to the circumstances but there were few comprehensive responses with a lot of candidates tending to go off track by trying to answer how they would trade a business in Administration.

The requirements asked for concerns and issues, however many of the candidates produced long lists of questions that, whilst indicating they had some understanding of the problem, did not explain why it was a concern.

- (b) **Briefly explain the options available to the funder and/or Administrator in order to recover the debt from Mr Crinkle. (10 marks)**

This part of the question was aimed at testing the candidate's knowledge of debt recovery techniques including the existence of personal insolvency processes. Most candidates missed the point and whilst

some candidates were able to state a few basic options there was a clear lack of understanding and practical knowledge in this area.

Most candidates tended to focus on a couple of options and then write down everything they knew about this i.e. bankruptcy, rather than simply stating what the options were.

Only one candidate recognised that it would likely be the funder taking action.

Question 4

This question required the production of an outcome statement.

Draft an Administration estimated outcome statement, clearly showing the priority of payment. (25 marks)

Overall, this question was poorly attempted. Most candidates were able to deal with the property sale and debtors calculations and input this correctly into the EOS however beyond this most candidates struggled to deal with more complex calculations and some even struggled with layout and flow.

Whilst most candidates were able to distinguish between fixed and floating charge assets and payments no candidates were able to prioritise payments as requested within the question. This is important point to note especially as most candidates seemed to think that the deduction of the corporation tax liability was to be deducted from the secured proceeds. If candidates had opened Butterworths to the relevant rule then this would have been straightforward to answer and list.

The calculation of profit was not handled well with only one candidate working out the correct sales price of the stock.

Some candidates did not recognise that the prescribed part would be capped at £600k. No candidate attempted to offset the bad debt relief against the HMRC and some included as a realisation.

As with corporation tax, VAT was not handled well with many candidates including a mixture of gross and net figures in the outcome statement.

EXAMINER'S MARK PLAN

ADMINISTRATIONS, COMPANY VOLUNTARY ARRANGEMENTS AND RECEIVERSHIPS (SCOTLAND)

NOVEMBER 2016

Question 1(a)

Receipts and Payments account for period to [end of administration]

Estimated to realise	6 months to 11 August 2016 £	To end of administration £	Cumulative £	
Secured assets/assets specifically pledged/pledged charge assets				
Asset realisations/Receipts				
Freehold property	-	250,000	250,000	
Cost of realisations/Payments				
Agent costs - property	-	5,000	5,000	(see workings below)
Legal costs - property	-	10,000	10,000	(see workings below)
Insurance	1,000	250	1,250	any reasonable value to end of administration
Administrator costs - property	-	9,900	9,900	
Irrecoverable VAT	-	4,980	4,980	Discretion as to whether fixed or floating (see workings below)
Fixed chargeholder claims	-	218,870	218,870	See workings - £nil if VAT recoverable
	1,000	249,000	250,000	See workings - £223,850 if VAT recoverable
Floating charge assets/assets not specifically pledged				
Asset realisations/Receipts				
Plant and Machinery	50,000	-	50,000	
Office equipment	4,000	-	4,000	
Debtors	35,000	30,000	65,000	
Stock	85,000	-	85,000	
Customer contracts	1,000	-	1,000	
Cash at bank	55,000	-	55,000	
	230,000	30,000	260,000	
Cost of realisations/Payments				
Legal fees	25,000	-	25,000	
Tax advisors	-	1,000	1,000	
Agent fees	15,000	-	15,000	
Administrator's remuneration	30,000	-	30,000	
Administrator costs - balance	-	33,000	33,000	(see workings below)
Insurance		-	-	
Misc disbursements	1,500	-	1,500	
Corporation tax	-	10,000	10,000	
Total costs	71,500	44,000	115,500	
Preferential creditors	-	(1,741)	(1,741)	(see workings below)
Assets less costs subtotal	157,500	(14,741)	142,759	(needed for prescribed part)
Administrator costs - prescribed part	-	(10,800)	(10,800)	Can appear above prefs (see workings below)
Unsecured creditors				
Prescribed part	-	(20,752)	(20,752)	(see workings below)
Floating chargeholder		(111,207)	(111,207)	(see workings below)

157,500	(157,500)	-
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Represented by		
VAT receivable	14,300	-
Estate bank account	<u>143,200</u>	<u>-</u>
	<u>157,500</u>	<u>-</u>

SPECIFY VAT ASSUMPTION - GROSS OR NET. If gross as sale of business as a going concern the receipts would not attract VAT.

Fixed chargeholder payment

	If VAT Irrecoverable*	if VAT incidental*	Difference (irrecoverable VAT)
Sale proceeds	250,000	250,000	
Legal costs	(12,000)	(10,000)	
Agent costs	(6,000)	(5,000)	
Insurance	(1,250)	(1,250)	
Administrator costs	<u>(11,880)</u>	<u>(9,900)</u>	
Available to charge holder	<u>218,870</u>	<u>223,850</u>	4,980

*Assumed that VAT is irrecoverable as no VAT charged on property sale. Discretion if candidates have stated that they have assumed that VAT would be recoverable due to 'incidental nature'

Administrator's remuneration

To date	355	180	63,900
Charged			(30,000)
To completion	50	180	<u>9,000</u>
Total expected	(This excludes the remuneration relating to the prescribed part (see below))		<u>42,900</u>
Property related (see above)			9,900
Balance			<u>33,000</u>
			<u>42,900</u>

Preferential creditors

	Salary	Weekly	Weeks	Arrears	Arrears	Holiday
					Limit to £800	Days
Employee						
Mr Arnold	18,000	346	2	692	692	2 138
Miss Beach	28,600	550	3	1,650	800	1 110
					<u>1,492</u>	<u>248</u>
TOTAL PREFERENTIAL					<u>1,741</u>	Assumed 5 day week

Prescribed part

Amount available after preferential creditors		
Receipts		260,000
Payments		(115,500)
Preferential creditors		<u>(1,741)</u>
Amount available for prescribed part		<u>142,759</u>
First £10,000	50%	5,000
Balance	20%	<u>26,552</u>
Prescribed part		<u>31,552</u>
Cost of distributing prescribed part		(10,800) (60 hours at £180 per hour)
Amount distributed		<u>20,752</u>

Floating charge holder

Available for prescribed part	142,759	See above workings
Prescribed part	<u>(31,552)</u>	See above workings
Available for floating charge holders	111,207	
CHECK: Shortfall from fixed charge		
Bank debt	380,000	
Secured creditor distribution	<u>(218,870)</u>	
Outstanding	<u>161,130</u>	

Question 1(b)

Practical steps

- Pay any accrued outstanding costs
 - Administrators
 - Professionals; legal and agents
 - Other costs of administration
- Review and finalise any tax matters including PAYE/NI, VAT and Corporation tax
- Ensure all insurance aspects have been dealt with
- Ensure that unclaimed dividends are dealt with
- Ensure forms submitted in relation the directors' conduct
- Release bond (once end confirmed)
- Ensure that appropriate records are retained in accordance with Regulation 13 (as amended by the IP (Amendment) Regulations 2015).
- Ensure that provisions are in place regarding storage of company and other records
- Close administration bank accounts

Procedural steps

- Dissolution most likely exit
- Establish position regarding discharge from liability
 - If necessary seek approval from committee or secured creditors
- Final progress report prepared
- Notice of end of administration completed
- Notice sent to Registrar of companies with final progress report
- 2 copies of notice filed in court
- Court sends one sealed copy to administrator
- Within 5 days administrator sends notice of end of administration to creditors
- Notice can be placed in the Gazette

2a) (i) Alternative to administration

Variation – if proposals provide for such an eventuality.

Could be used to reduce contributions to an affordable level

Process outlined in proposal followed. Typically

- Determine what the Company can afford to pay and for what period
- Compare this to alternative outcome; produce an EOS
- Discuss with significant creditors; secured and unsecured
- Convene a meeting of creditors to consider the variation
- Meeting held and creditors vote; approval % required determined by existing CVA proposal
- If approved new terms take effect
- In rejected then it may be necessary to appoint Administrators
- Notify creditors of outcome

Other alternatives:

- could propose a new CVA; would bind new and 'old' creditors
- Third party funds
- Discretion in proposal to reduce or suspend contributions

(ii) Ethics

Code of ethics: Insolvency Practitioner may normally accept an appointment as administrator or liquidator.

However the Insolvency Practitioner should consider whether there are any circumstances that give rise to an unacceptable threat to compliance with the fundamental principles.

Self review threats – any actions as supervisor that would be reviewed by Administrator

Conflict of interest - Dealing with the assets and claims over them; the spare machine could create a conflict.

Views/opinion/perception of creditors

2b) ROT

General (applicable to both)

- ROT questionnaire completed
- Proof/copy of ROT clause
- Proof ROT clause incorporated into contract
- Consider course of dealings if terms on post contract documentation
- Confirmation of outstanding balance
- Re Atlantic; are the goods required for the administration
- Explain impact of moratorium
- Seek legal advice in relation to the validity of claims
- Invite creditor to identify goods

(i) Stickle

Information required/considerations

- Evidence that the motor can be identified; e.g. serial number
- Can the motor be removed without damage to the rest of the unit – if replaced it suggests that this is possible
- Is there any value to settling the outstanding balance – does this result in better realisations
- Obtain a valuation for the compressor with and without the motor
- Whichever way it is considered at least part of the motor has been paid for but not all of it

Motor likely to be easily removed and identifiable, therefore claim likely to be successful

How deal with situation

- Negotiate with creditor in relation to the money paid by the Company – it has effectively paid for the labour and part of the cost of the unit; can the creditor recoup more than their loss?
- Consider settling the outstanding balance if the valuation suggests that it is beneficial to do so.
- Reject the claim if the creditor is unable to establish validity.

(ii) Blencathra

- Evidence money outstanding
- Details of historic amounts invoiced and paid
- Do any other suppliers supply these packs – if so how can they be identified to the specific supplier
- Type of ROT clause – simple or all monies
 - If all monies - account ever reached zero
 - If simple – how can the packs be identified to specific invoices; appears that this will not be possible if only contains a code
- Establish impact on value of completed packs if screw packs removed; is it appropriate to agree commercial settlement for these items?
- Loose packs of screws in box likely to be easily removed; but cost of doing so may be prohibitive to creditor.
- Assuming clause and claim exists likely to have a valid claim;

Dealing with situation

- Commercial settlement regarding those within boxes due to cost of removal and impact on sales price.
- Potentially agree for the removal of the items at the creditors' cost
- Discuss selling the completed items to the creditor taking account of the ROT claim
- Broker a deal between a purchaser of the entire finished goods and the supplier
- If parts required and cannot agree with Blencathra; are there alternative suppliers

3(a) Concerns regarding trade

- Environmental; chemicals may pose a contamination risk.
- Health and safety; acid - risk to employees would be high.
- Are there any licences associated with its activities that would affect the ability to trade – e.g. medical sector
- Insurance; may be difficult to obtain in administration;
 - could the existing policy continue
- Warranties; administrator would not normally provide but nature of equipment likely to require them.
- Quality; customers would need to be confident as to quality and disaffected employees could impact on this.
- Loss making; does the prospect of enhanced realisations compensate possible trading losses, is it possible to reduce costs to bring administration trading into profitability or obtain an indemnity from secured creditor
- Achieving a purpose; does the trading support the purpose of administration
- Lack of funding; will the administrator be able to fund trade, via existing lenders, new lenders, suppliers etc.
- Customer contracts;
 - do these terminate on administration?
 - would the customers want to continue trade with the Company?
 - Payment terms; would these need to be changed
 - Does continued trade protect the existing debtor book
- Key employees;
 - are there any key employees that are required for trade
 - The director may be uncooperative; is the MD key/required and what impact would this have
 - will it be possible to retain these given the uncertainty of administration.
 - Would it be necessary to pay arrears
- Key suppliers;
 - would the administrator be able to obtain new supplies,
 - would the supplier require any arrears paying
 - Is reservation of title an issue
 - Would prices remain the same or could they increase affecting possible losses
- Landlord
 - Will there be any issues with the landlord regarding access
 - Will the landlord position affect the possibility of a sale of the business
- Purchaser
 - Is it likely that a purchaser as a going concern will be found
 - Does the increase in value offset the above risks; does it benefit creditors overall?
 - Will a purchaser be willing to take on warranty and environmental risks
 - Will a purchaser want to take on the TUPE liability

3(b) Recovering debt from sole trader

- Funder likely to own the debt until repaid and debt reassigned to company
- Therefore funder likely to have to take action
- Options
 - Chasing for payment; attempts should be made to obtain payment
 - Consider meeting to discuss the situation and agree settlement
 - Consider instructing collection agents/solicitors
 - Could sell the debt to a third party
 - Could sell the debt as part of a sale of the business
 - Issue a statutory demand
 - Could consider mediation if dispute involved
 - Bankruptcy; debtor could be made bankrupt in which case assets would be realised for their creditors including the Company
 - Court Judgement; the claim could be taken to court; debtor may defend the claim.
 - Enforcement of court judgement
 - Repayment arrangement; could seek court involvement to make debtor provide details of income and expenditure
 - Charging order over property or land could be sought
 - Could seek order for possession and sale
 - Attachment of earnings order from court to obtain a deduction from wages if applicable

- Third party debt order; against debtor's bank or another third party who may pay the debtor. Funds held and court decides if funds should be paid to the creditor.

Question 4

Estimated Outcome Statement

			Book Value £'000	Estimated to realise £'000	
Assets subject to fixed charge					
Trade debtors	See workings (d)		6,600	5,280	
Collection charges	See workings (d)			(104)	
Amount due to Bank	Per question		(6,000)	(6,000)	
				<u>(824)</u>	
Property	Per question	2,500	1,500	2,500	
Agent costs	2%			(50)	
Agent costs - valuation	Per question			(15)	
Solicitors	Per question			(18)	
Administrators' costs	Per question			(15)	
				<u>2,402</u>	
Total available to bank				2,402	
Amount due to Bank	Per question			(5,500)	(5,475) If cash at bank subject to set off
Shortfall from debtors	From above			(824)	
				<u>(3,922)</u>	
Shortfall to fixed chargeholder	Carried down to floating charge			(3,922)	
Assets subject to a floating charge					
Plant and Machinery	10%	3,500	4,500	3,500	
Trading	See workings (a)			3,000	
Sale of residual stock	See workings (b)		3,000	240	
Director loan account (other debtors)	Per question			25	
Cash at bank				-	Assumed used prior to appointment (discretion if assumed subject to bank set off)
Floating charge realisations				<u>6,765</u>	
Costs associated with QFC appointment	Per question		Priority c	(10)	
Statement of affairs	Per question		Priority d	(3)	
Corporation tax payable	See workings (c)		Priority f	(19)	
Legal fees	Per question		Priority f	(130)	
Agent fees - realisation	6%		Priority f	(210)	
Agent fees - valuation	Balance from Fixed		Priority f	(20)	
Pre-administration costs; Legal	Per question		Priority h	(12)	
Pre-administration cost; Administrators	Per question		Priority h	(8)	
Administrator's remuneration - floating charge plant	Per question		Priority h	(10)	
Administrator's remuneration	Per question		Priority h	(150)	
Administrator's remuneration - to completion	Per question		Priority h	(30)	
Chargeable gain	500	19%	Priority j	(95)	
Available for preferential creditors				<u>6,068</u>	
Preferential creditors					
Arrears of wages	as average arrears £250 assumed all pref			(75)	
Holiday pay				(20)	
Pension scheme contributions				(10)	
Surplus after preferential creditors				<u>5,963</u>	
Prescribed part	Or identification that not relevant as floating chargeholder will be paid out			(600)	
Available for floating chargeholder				<u>5,363</u>	
Floating chargeholder	Shortfall from fixed charge			(3,922)	
				<u>1,441</u>	
Prescribed part				600	

Available for unsecured creditors				2,041
Pension scheme	8,000	2	s75 double per question	(16,000)
Redundancy	Per question			(280)
Notice pay	Per question			(150)
Protective award	Per question			(150)
Trade creditors	Per question			(8,000)
HMRC	See workings (e)			(1,080)
Other creditors	Per question			(600)

Overall shortfall to creditors (24,219)

Distribution rates				
Secured creditor				100%
Preferential creditors				100%
Unsecured creditors				8%

Workings (a) Trading

Profit calculation

Stock cost	2,600	
Margin	35%	
Sales	<u>4,000</u>	
Stock cost	(2,600)	
Direct costs	(1,000)	
profit	<u><u>400</u></u>	

Realisations for EOS

Sales	4,000	
Direct costs	<u>(1,000)</u>	
	<u>3,000</u>	

Workings (b) Residual stock	p in £	60%	
Total stock	3,000		
Used in trading	<u>(2,600)</u>	(See workings (a))	
Residual	<u>400</u>	60%	<u>240</u>

Workings (c) - Tax on profits

Tax on stock			
Profit from above	400		
Loss on residual stock	<u>(160)</u>	(residual cost price - 60p in £)	
Taxable profit	240		
Less allowance	<u>(140)</u>	(per question)	
Taxable	100		
Tax rate	19%		<u>19</u>

Workings (d) - Trade debtors

BV	6,600		
Realisation rate	80%		
Collected	5,280	5,280	
Uncollected	1,320		
Charges			
	3,000	1%	30
	2,000	3%	60
	280	5%	14
	<u>5,280</u>		<u>(104)</u> (104)

Invoice finance (6,000)

Workings (e) - HMRC Unsecured debt

Per question 1,300

Bad debt relief on debtors

Uncollected debts	1,320
VAT rate	20%
Net amount	1,100

VAT

220

(220)

1,080

Assumed that no bad debt relief claimable as a realisation - instead subject to set off.
[insufficient information to calculate if would result in realisation but discretion over treatment if assumed realisable]

JOINT INSOLVENCY EXAMINATION BOARD

PERSONAL INSOLVENCY (SCOTLAND)

EXAMINER'S REPORT AND MARK PLAN FOR THE NOVEMBER 2016 SITTING

This year the paper examined dealing with a buy to let property portfolio, preparing an estimated outcome statement, providing initial advice and finally, the remedies available to a creditor if not satisfied with the progress of the sequestration.

These questions were straightforward and the initial advice and estimated outcome statement, in particular, have been examined on a number of occasions before. It was pleasing that candidates did well on these questions

Again this year, candidates in general, spent less time writing pages full of irrelevancies and handwriting was all legible, which have all been issues on previous exam sittings.

Question 1

This question explored the topical question of a debtor with what appears to be a portfolio of buy to let properties. The sequestration award follows a creditor petition, information is limited and there are indications that the debtor may prove to be unco-operative.

The question asked the candidates to explain the information they would obtain to identify the extent of the portfolio and then outline the steps they would take to secure the Trustee's interest. The final part of the question considered what advice should be given to tenants.

This question was poorly answered, with the average mark being well below a pass mark.

This possibly reflects a lack of experience of dealing with this type of case in practice. Candidates also almost universally assumed or didn't question that the portfolio would have equity in it. Ultimately, establishing the value within the portfolio was the point of part (a) and would then dictate the actions required in part (b).

Requirements

- (a) Explain what enquiries you would make and what records you would keep in the first month following your appointment in order to establish the extent of the property portfolio and the current position regarding each property. (15 marks)**
- (b) Describe the practical steps you and your team would take to secure your interest in the property portfolio for the benefit of the sequestrated estate. (4 marks)**
- (c) Explain the position regarding the payment of rent by tenants of a landlord who has been made bankrupt and what you would say to the tenants who have called. (6 marks)**

Total: (25 marks)

Most candidates were able to achieve marks for identifying that searches should be done on the Land Register, the secured lenders should be written to and to a lesser extent that valuations would be required. Most appeared to assume the co-operation of the debtor.

While lots of suggestions were made about information which could be gathered, candidates' knowledge of how to obtain this information was patchy and in some cases unrealistic. Few made meaningful comment

about the need to establish the extent of the equity, which will determine the value of the various parts of the portfolio to the estate and the need to set a strategy for the case.

The secured lender's position was largely ignored.

Few candidates were aware of the Tenancy Deposit Scheme.

No candidates mentioned the need to consider the future Capital Gains Tax position and tax planning.

All candidates were of the view that there was no question that the Trustee should take the rental income and in most cases unhesitatingly assumed that he would take the landlords obligations.

Some candidates were able to make helpful practical suggestions about what tenants should do if the debtor continued to pursue them for rent.

In the main candidates kept to the issues in question. However, there remains an issue with a small number of candidates hoping that "opening a sederunt book" or "opening a case file on the computer system" is worth mentioning. Detailing these points before giving any consideration to the much wider issues in the case or the case strategy does not inspire confidence and is reflected in a poor Holistic Assessment.

Question 2

This question considered a case which had reached its first year anniversary and required candidates to comment on the basis of the Trustee's remuneration and how it should be approved and asked them to prepare a fairly straightforward Estimated Outcome statement. This question was generally answered well.

Requirements

- (a) **Prepare a briefing note for Samuel outlining what steps need to be taken, and when, in order to obtain approval for the basis of his remuneration. Your note should include details of the different bases upon which his remuneration can be calculated. (7 marks)**

This part of the question was answered well. Candidates who answered it in the context of the question, for example, with reference to the accounting periods in this case, generally provided the most meaningful responses.

- (b) **Clearly stating any assumptions that you have made, prepare an Estimated Outcome Statement and calculate the likely dividend to creditors. (18 marks)**

This part of the question was also generally answered well with most candidates able to produce a well presented Estimated Outcome Statement which covered the main points.

Some of the presentation was overly convoluted, however, the majority of candidates understood what they were required to calculate.

Generally asset realisations, the trustees, fees, outlays, Audit fees and irrecoverable VAT were dealt with well.

Only one third of candidates mentioned the Trustee's liability for Capital Gains Tax and of those none of them treated it correctly.

Surprisingly the calculation of statutory interest proved challenging, with both the period of interest and compounding being an issue.

Candidates should remember to conclude their calculations as marks were missed where it was not clear to the Examiner what candidates had concluded.

Question 3

This question required you to advise a contact about the issues they should be concerned about as a creditor in a sequestration which on the face of it didn't seem to be well administered by the Trustee.

Overall, this question was not well answered although there was a broad range of marks.

Requirements

- (a) **Based on the information provided to you, prepare a structured list of issues and questions that you would like to discuss with George. (18 marks)**

Most candidates were able to recognise the fairly obvious issues of the abandonment of a property which now appeared to have equity, the absence of a DCO and the motor vehicle and other assets.

Better candidates, also identified that large sums had been paid to Mary and sought explanations of what had been done to investigate this.

Few candidates had any issues or concerns about the debtors conduct/discharge.

Whilst candidates commented on the amount of the fee paid for preparation of a Statement of affairs, worryingly no candidate identified that it is not permitted to make payment to a third party for the preparation of a statement of affairs in a sequestration case.

Some candidates appeared to forget that they would be attending the meeting with and on behalf of a creditor. Some of the information which they suggested should be requested was extremely unlikely to be provided and if they adopted the strident tone of some of the suggested questions and statements made then the meeting would be fairly short.

Some of the suggestions made by one candidate were disproportionate, vindictive and unprofessional.

- (b) **Outline the steps which Thomas could take if, following the meeting next week, he remains dissatisfied with the progress of the Sequestration and the actions of George. (7 marks)**

This part of the question was answered better, with most candidates being able to offer Thomas sensible suggestions about the routes he could pursue should he wish to complain about George's conduct. Not all candidates recognised that as a creditor Thomas had a potential remedy in the ability to secure the appointment of an alternative Trustee.

Question 4

This question presented a scenario that an IP might be expected to see on a daily basis and required candidates to comment on the options available to someone to resolve their financial difficulties based on a limited amount of information.

The perhaps unusual aspect of this question was that on paper the client was not balance sheet insolvent.

Overall this question was answered well.

Requirements

- (a) **Set out the ethical and regulatory matters that you would need to consider before accepting any instructions to advise Abigail. (4 marks)**

Most candidates were able to comment on the ethical principals and the threats that Abigail (or her company) being a client of their Firm may represent.

No candidates offered any comment on whether the advice which Abigail required would be covered by your insolvency permit or whether regulation by the FCA would be required.

(b) Explain the various statutory and non-statutory procedures that might be available to Abigail to resolve her difficulties. (14 marks)

Candidates generally recognised that Abigail was not insolvent and sensibly offered a variety of options that she could consider as an alternative to a formal debt solution.

Most candidates commented on the options available with reference to the context of the question and made their answers relevant to Abigail. However, some spent considerable time providing a list of features of some of the statutory solutions, which were not relevant or of interest to Abigail.

There was limited consideration given to the student loan, only a few candidates recognised that it represents low cost credit and would not be written off in a formal debt solution.

(c) Advise Abigail which procedure is most likely to be applicable to her. You should explain what further information you would require in order to advise her more fully and set out any assumptions which you have made. (7 marks)

Most candidates were able to make a sensible recommendations to Abigail. Though it is concerning that at least one candidate strongly recommended a statutory insolvency procedure, which would be unlikely to be acceded to by creditors, in the knowledge that the debtor was not insolvent.

To be able to advise Abigail properly considerable further information would be required particularly about affordability for debt repayments based on her income, the completeness of her creditors and her attitude towards remaining in her property.

However, candidates generally missed marks here, perhaps in fairness because it was the last question in the paper.

EXAMINER'S MARK PLAN

PERSONAL INSOLVENCY (SCOTLAND)

NOVEMBER 2016

Question 1(a)

Explain what enquiries you would make and what records you would keep in the first month following your appointment in order to establish the extent of the property portfolio and the current position regarding each property. (15 marks)

Enquiries you would make/information to obtain

General

- Ask petitioning creditor to provide you with any additional relevant information they have about the debtor's assets and liabilities or alternative names/aliases;
- Write to the debtor at his last known address and advise him of sequestration appointment and arrange to meet with him as soon as possible to discuss his sequestration.
- Attempt to find telephone contact details either online or through any paperwork that the petitioning creditor has provided and make contact to arrange an interview;
- If the debtor is prepared to co-operate with you a full interview should be completed to establish the extent of his assets, the sums secured over them and the likely equity position.
- You also need his assistance to quickly establish which properties are tenanted, the agreed rentals, the terms of any leases and whether any are in arrears;
- If contact details are not available, instruct a tracing agent;
- If debtor fails to respond consider serving correspondence requesting the above by Sheriff Officer
- Could consider an application to court for the private examination of the debtor but this depends on the extent to which you consider it cost effective depending on the extent of the information you can obtain elsewhere.
- Write to HMRC, invite claim and get copy tax returns (if any);
- Identify any sources of income declared on tax returns;
- Credit rating agency search – to identify credit card, bank accounts etc and thereafter make enquiry of these financial institutions, obtain and review copy statements etc
- Internet search – social media etc
- Companies House search – directorships/shareholdings etc, might give property addresses or details of share ownership

Heritable Property

- Carry out name Search on Registers on any addresses identified in your investigations
- Carry out name searches in any areas where you believe the debtor may own property
- Obtain copy of searches for any properties identified

Secured Lenders

- Write to all secured lenders identified and ask them to note your interest. Ask them to confirm the extent of their indebtedness, whether mortgage payments are being maintained and whether they have any intention to repossess. Ask them if they have obtained recent valuations for the properties in their portfolios.

Valuation

Make initial enquiries regarding the value of each property identified. Valuations:

- Drive by
- Internet values

Are any already on the market?

- Right Move searches
- Call local agents
- Instruct your own agents to make enquiries on your behalf

Once you have a broad idea of the equity position, or otherwise on the portfolios consider the most appropriate way to confirm the valuation. If all that is required is a broad indication of value eg negative equity desk top/drive by valuation (above) may be sufficient. If any action is likely to be taken eg sale/legal proceedings an internal valuation and Home Report may be required. Where properties are tenanted this

will require the consent of the tenants. There should be provision to obtain access in the lease upon giving required notice to tenants.

Disposal strategy, ie sell as portfolio or gradually and impact on value – discuss with surveyor. Also seek recommendations on whether portfolio should be tenanted to sell or vacant

Tenants

- Write to all known properties, either to known tenants or “to whom it may concern”
- Request details of tenancy/copy agreement
- Rental income – amount/frequency/how paid When tenants call ask them to confirm the rental they pay, the property address and how they historically paid the rent whether via a letting agent. If they paid the debtor directly, did they do so in cash or, if they paid by Bank transfer, can they provide details of the account to which they made payment. This will direct your enquiries to that Bank.
- Establish if the tenants paid a deposit to the landlord, if so how much. Have these deposits been placed in the government supported tenancy deposit scheme and are any of the tenants aware of which one.

Local Housing Authorities

- Write and request if they hold any information regarding tenants of the debtor who are on housing benefit.
Provide debtor’s name and list of properties.

Tenancy Deposit Scheme

- Write to the appropriate fund noting your interest and asking them to confirm the funds they hold and for which properties/tenants. Secure their agreement that they will not release deposits without your agreement.

Other - property

- Information to enable you to assess any CGT liability on disposal, purchase price (from search) likely selling price, and if known the extent of any improvements.
- Consider reinstatement value of properties for insurance purposes
- If properties are factored establish ongoing maintenance/factoring charges for each property
- Ascertain whether there are arrears to factors and whether these are secured by NOPL on the title which could affect equity position
- For properties disposed of and where debtor has not provided this information consider requesting state for settlement from solicitor who dealt with sale to consider where there has been any transfer at under value.

Bank accounts

- Write to high street banks
- Enclose copy of Award of Sequestration
- Request information regarding any accounts in debtor’s name – entitled to information pursuant to s38 and will make application if bank is unwilling to provide information
- Request bank to freeze account, not allow withdrawal of funds
- Request copy statements – review to identify potential assets (e.g. via direct debits)

Records you would keep

Use the information obtained above to continue to build a complete picture of the portfolio of properties owned by the debtor. Create a list/database of:-

- The number and location of each property;
- Whether it is solely or jointly owned;
- Whether occupied and if so by whom and on what basis;
- The likely selling price and the impact on that price if the property is tenanted and the likely impact of a disposal of all properties at once;
- The sums secured against it;
- The equity position;
- The rental stream and offsetting costs, letting agents fees, maintenance and factoring;
- Any property where repossession proceedings have been raised by the secured lender.

- Any Capital Gains tax liability which would be likely to crystallize for the Trustee if the property was disposed of by the Trustee or the secured lender.
- Properties which have previously been owned and disposed of and whether further investigation is required.

1(b) Describe the practical steps you and your team would take to secure your interest in the property portfolio for the benefit of the sequestrated estate. (4 marks)

Practical Steps

- Practical steps will depend on extent of the value to the estate and the Trustee's disposal strategy.
- Specifically in relation to the debtor's home if this is a family home put joint owner/entitled spouse notice of your appointment and seek their proposals for any equity.
- Where properties are jointly owned and have equity, the joint owner will have to be aware of your strategy. It may be more cost effective to give them the first opportunity to purchase your interest.
- Serving notice on tenants to secure vacant possession – input from legal agents;
- Consider use of letting agent if need to manage portfolio in short to medium term to secure the best price.
- Take advice from Estate Agents about the extent of any cleaning/clearing works which would improve the marketability of the properties (cost vs benefit).
- Where the properties have a value to the Estate obtain open cover insurance. If there is no value to the Estate then advise the secured lender that they are not insured (assuming debtor is not insuring);
- Put Secured lender on notice that Trustee is going to sell properties if this is the strategy to be taken forward (s39) .
- Where any doubt about the value to the estate of portfolio, consider need to ask secured lender to underwrite costs of disposal.
- Trustee can act on behalf of secured lender but they need to underwrite costs and provide a benefit to the Estate. The benefit can be the reduction of shortfall claim to secured lender.
- Landlord regulation – Trustee may have to register with the Local Authority as landlord. The Local Authority may be prepared to dispense with this requirement but this is not guaranteed.

Capital Gains tax planning – for example, abandon the Trustee's interest in any properties with limited value to the estate and where there is a significant tax liability. Assuming you believe that there will be funds available for distribution to the unsecured creditors this will protect the residual estate from CGT liabilities

1(c) Explain the position regarding the payment of rent by tenants of a landlord who has been made bankrupt and what you would say to the tenants who have called. (6 marks)

Position regarding rent

The Trustee is entitled to collect the rent as this can be regarded as income arising from the Estate which is vested in the Trustee – Section 32(1) of the Bankruptcy Scotland Act.

However, if the Trustee collects the rent then they could be deemed to have adopted the tenancies (even if they have not adopted the lease) and therefore adopted the landlords obligations. Accepting rental payments will also place reputational/moral obligation on the Trustee.

You need to consider in view of all of the information gathered above whether you are likely to abandon your interest in these properties (no equity/significant CGT or other liabilities) and whether in those circumstances you are prepared to take the landlord obligation of receiving the rent whether legal or simply moral.

Until the position is established, and given that the debtor is showing signs of being un-cooperative, it is appropriate to ask the tenants to:

- Hold rent to order, or pay to trustee/solicitor
- Do not pay to debtor

- Cancel direct debits
- But if he issues threats etc, call police but don't put themselves in a position of physical danger
- Keep records of any amounts that they do pay to him

Where there is value in the portfolio and you want to manage its disposal in an orderly way then you may well want to retain the tenants as part of that strategy. Take legal advice on lease and whether to issue new short term assured tenancies.

Consider use of letting agent to collect rent and manage maintenance.

Depending on your approach you will:-

- either be abandoning interest and telling the tenants that the Trustee does not have an interest in the rental;
- OR
- advise them to make payment to the Trustee/your letting agent and providing your Bank account details.

Tenant will be concerned about their deposits and whether they are held securely for them. You should attempt to quickly ascertain whether these funds are secure as required by Legislation in a Tenancy deposit scheme, or whether they will simply have an unsecured claim in the sequestration. You should resist any attempts to withhold rent in order to recover the deposits.

If any tenants are in arrears, you also need to address this in the context of your overall strategy of either retaining the tenants or securing vacant possession.

Tenants will be concerned about whether they can stay in the property in short/medium term. Your answer will depend on the strategy determined.

Question 2

Requirements

- (a) Prepare a briefing note for Samuel outlining what steps need to be taken, and when, in order to obtain approval for the basis of his remuneration. Your note should include details of the different bases upon which his remuneration can be calculated. (7 marks)

Memo

Section 53(4) of the Act states that the basis for fixing the amount of remuneration payable to the Trustee, may be a **commission** calculated by reference to the value of the debtor's estate but in any event should take into account (a) **the work** which, having regard to the value of the estate was undertaken by the Trustee and (b) the extent of the Trustee's responsibilities in administering the Estate.

In accordance with **SIP 9** the Trustee's remuneration should be appropriate, reasonable and a commensurate reflection of the work necessarily and properly undertaken by the Trustee.

In **practice**, in a bankruptcy, the basis of the Trustee's remuneration is likely to be either, time on line or a fee based on the level of assets realised or a combination of both.

In this case the first accounting period ended on 2 November 2016 and within **two weeks** of this 16 November (ie 1 week from today) you need to prepare your account for the first accounting period. This account should include a **claim for Trustee's remuneration**. It appears that there are significant funds on hand and that creditors' claims have been agreed. If so it would be appropriate to prepare a **Scheme of Division** account which would propose an interim dividend to creditors, after provision for the costs incurred to date and future costs.

The file needs to be checked to see if Commissioners have been appointed either at the first meeting of creditors (if held) or at any meeting since. If **Commissioners** have been appointed then they can audit the account and claim for remuneration. If there are no commissioners then the account and claim for remuneration must go to the **AIB** to be audited.

The Commissioners or the AIB have **6 weeks** from the Accounting period end to issue a determination fixing the Trustee's remuneration.

This determination will be issued and any party with an interest, the Trustee, creditors or the debtor (if he can show that he has a financial interest in the outcome) can **appeal** to the AIB (if the determination was issued by the Commissioners) or to the Sheriff (if issued by the AIB).

The Trustee must **not draw** any remuneration from the Estate until a determination is issued by the Commissioners or the AIB and it would be prudent not to do so until the appeal period has expired.

The request for remuneration this should be prepared in accordance with SIP 9. SIP 9 states that requests for remuneration and reports to creditors should where remuneration is being requested on a time cost basis provide an **explanation of the Trustee's firms' time** charging policy including stating the units of time charged, grades of staff used and their charge out rates and the policy on charging support staff time. The report should also provide a **description of the work** carried out. **A time charge out summary** should be provided in an appropriate format.

In this case, time costs incurred are £5,940 to date. Time still to be incurred in quantifying and agreeing the CGT liability with HMRC, collecting the remaining payments under the DCO, paying an interim distribution and at conclusion of the 48 month period paying a final distribution and closing the case. It is possible that time costs by that stage will exceed £10,000.

In this case it would be appropriate to use the format provided in SIP 9 for cases where total remuneration is likely to be between £10,000 to £50,000. This would show the grades of staff, their rate and the area of the case worked on.

The AIB's NFG state that sufficient information should be provided to allow them to determine if the request for remuneration is reasonable and should explain what has been achieved in the case to date and how.

An application under section 63 would be required if the account and claim for remuneration is late.

(b) Clearly stating any assumptions that you have made, prepare an Estimated Outcome Statement and calculate the likely dividend to creditors. (18 marks)

Sequestration of John Proctor
Estimated Outcome Statement

Notes

Assets

Equity in family Home		55,000	
Income Payments			
received to date		3,500	
future receipts	1	<u>13,300</u>	
			16,800
Interest received on funds in hand	2		<u> </u>
Total asset realisations			71,800

Costs

Legal costs		1,200	
Trustees fees	3	9,315	
Outlays	4	400	
Statutory Fees	5	454	
AIB audit fee issuing determination	6	1,870	
Capital Gains Tax	7	5,012	
Irrecoverable VAT	8	<u>2,137</u>	
			<u>20,388</u>

Available for creditors 51,412

Creditors

Bank overdraft		1,410	
Credit cards (x3)		17,360	
Utilities		235	
Loan from parents		20,000	
Shortfall to mortgagee		<u>6,400</u>	
			45,405

Statutory Interest - to interim	9		4269
Statutory Interest - to final			4312

Shortfall on Statutory Interest			<u><u>-2,574</u></u>
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Note 1 10 payments made, 38 future payments @ £350 = £13,300
 Last payment Jan 2020 (if made on due dates).

Note 2 A small amount of interest is likely to be received - not material

Note 3 Trustee's fees assume time costs

Current = 44 x £135	5940
Future - estimate 25 x £135	<u>3375</u>
	9315

Alternative assumptions: fixed fee, % etc. Credit for reasonable estimate

Note 4 Outlays to date 400

Assume Registering Award and Supervision Fee already incurred

Sederunt book Fee	36
Distribution Fee (x2)	138
Supervision Fees 4 remaining	<u>280</u>
	<u><u>454</u></u>

Note 6 17.5% of Fees and outlays (excluding stat fees) 17.5% * (£9,315+1200+(400-20-210))

Note 7 Sale Price	98000
Purchase price	<u>65000</u>
	33000
Less: sale costs (estimate)	<u>-4000</u>
Net Gain	29000
Less: annual exemption (2016/17)	<u>-11100</u>
	17900
CGT at 28% (assume higher rate)	5012

CGT will be payable despite the fact that the property was sold by the secured lender

and that the estate got no funds from the sale.

In order of priority it will be paid after outlays and remuneration but before unsecureds

18% if assume lower rate. However. Debtor is making income payments of £350 per month, £4,200 per year. It is reasonable to assume that his taxable pay, plus the gain of £17,900 will take him over the basic income tax rate band of £31,785, thus CGT is charged at the higher rate

Assume no CGT on realisation of family home as PPR

Note 8 As not VAT registered, VAT is irrecoverable.

Solicitors fees	1200
trustees fees	9315
disbursements - current	<u>170</u>
	10685
VAT @ 20%	2137

Note 10

1. Creditors would be entitled to interest calculated at 8% from date of award to the interim distribution and then at 8% thereafter on any sum not paid.

Date of Award of seqn:	03-Nov-15	
Date of dividend - 2 months	05-Jan-17	Can't distribute until 8 weeks after Accounting period end (falls in Xmas/NY) say 5 Jan
No. days for interest calc	429	
$\text{£}45,405 * 8\% * 429 / 365$	4269.31	

Interest of £4,269.31 will have accrued by the time of the first distribution. Assume that you make an interim distribution

of £30,000

Interest to final distribution

Date of Award of Seqn	03/11/2015	
Date of final distribution	03/05/2019	38 months + 4 months
No of days for interest calc	1277	
$(45,405 - 30000) * 8\% * 1277 / 365$	4311.71178	

Question 3

Requirements

- (a) Based on the information provided to you, prepare a structured list of issues and questions that you would like to discuss with George. (18 marks)

Issues to raise with George on Thomas' behalf regarding the sequestration of Mary

General

A family member appears to have paid the sum of £5,000 to pay for a Private Trustee to administer the sequestration. Whilst there is nothing in legislation or guidance to prevent this, and there could be a good reason for it, it raises the question of why the debtor/family member would consider it necessary. The debtor's application could have been submitted without nominating a Trustee and the default position would have been that the Accountant in Bankruptcy could have been appointed as Trustee. If there were no realisations, the Public Purse would have met the costs of sequestration.

The following issues should be discussed with George:-

Surplus Income

Mary appears to have a well paid job, however, there are no income contributions on the R&P. What steps has the Trustee taken to secure a DCO ? The AIB would have set a DCO when the Award of Sequestration was made based on the information provided in the Debtor's application. As this is not mentioned in the Statement of Affairs it is possible that it was set at nil. However, if the debtor's circumstances change then the ability to pay a contribution should be reviewed using the CFT and the DCO varied as appropriate. The payment of a contribution over a period of 48 months could generate significant funds for the Estate.

Bramble Cottage

It would appear that the Trustee has accepted a nominal sum to formally abandon his interest in this Cottage. This is supported by the £500 receipt on the R&P and the outlay of £15 to Registers of Scotland which is likely to be for the Registration of the Form 22 – Form of Abandonment of Heritable Property. The SOA states that a 90 day ERRV valuation has been obtained. What is George's rationale for using this valuation, particularly as there is a significant difference, of £100,000 between this and the Home Report valuation. There is a concern that the Trustee has effectively ignored value of c£90,000 which could have been realised for the benefit of creditors.

The outlay shown on the R&P for the valuation of £45, would suggest the valuation obtained was a desk top or drive by. It is certainly unlikely to have been an internal valuation, which is concerning in view of the variations in value.

Retail Units

There is no mention in the SOA of a valuation having been obtained for these units. There is also no outlay on the R&P. Who has provided the value of £270,000. Has George obtained his own valuation and if not does he intend to obtain a valuation and pursue the equity, if any in these units, or if there is no equity, seek a nominal payment.

Are the retail units occupied by tenants, if so, what arrangements are in place regarding the rental income. There are no receipts on the R&P.

Vehicle

A Range Rover Evoque is likely to be worth more than £3,000 and therefore if owned by Mary would vest in the sequestrated estate and should be realised by the George. Even if Mary requires a vehicle for her employment this is arguably a more expensive vehicle than she needs (also at the present time she doesn't appear to be making any contribution, so this is arguably not generating any value for the estate). Has the Trustee checked with the DVLA who owns the vehicle or if it is leased?

If it is subject to HP or finance, what is the outstanding finance?

Check with Thomas if he knows what the treasured number plate is in order to obtain an indication of the value. These are not often cost effective to recover however, you would expect George to ask for a proposal for his interest to be realised.

In practice an internet valuation can usually be obtained.

What actions has George taken to assess the value and realise it?

Other assets

It is clear that considerable sums were given by Thomas and members of his family to Mary, £86,000 by Thomas alone. Unsecured creditors are noted as £30,000. It is also concerning that this is a round sum figure. Did Mary disclose the sums due to Thomas and his family on her application, or subsequently. Thomas should ensure that he has an acknowledgement of his claim from George, if this has not already been received.

As Thomas has made George aware of the sums due to him, what explanation has Mary provided for how she utilised these funds and what steps has George taken to verify the accuracy of this. Has the trail of these funds been followed. As a minimum, did George carry out a sweep of the UK Banks to identify any balances held by Mary?

Mary appears to spend considerable time in Spain, has George taken any steps to establish whether Mary has assets in Spain, for example, where does she stay when there? Have appropriate property searches been carried out.

Specific questions on R&P

Unless it has been shortened the first accounting period will be 12 months ie to 30 October 2016. Has the Trustee submitted his accounts to the AIB. If so what was his proposed remuneration for the first year? The Receipts and Payments account suggests that payment was made to a third party for work done to prepare the statement of affairs. Notwithstanding that the amount of work which appears to have been done does not justify £850, it is specifically against the Ethical code to make such a payment in a sequestration appointment. It is likely that this outlay will be rejected by the AIB in any event, when they audit the account; There is no outlay shown for the bond in this case – has it been bonded, and George's firm settled this directly;

There is no interest on the R&P, even at currently very low rates, there should be a little. Are the funds properly being held in an interest bearing account?

Debtor's Conduct

Thomas has concerns about the conduct of Mary in taking sums from him and his family which she failed to invest or return to him. You should ask whether:

Mary has been asked to complete a course of Financial Education;

Whether Mary has been reported to the Accountant in Bankruptcy's Bankruptcy Restrictions Team for a possible BRU/BRO in relation to her fraudulent activity prior to the sequestration.

Whether George is satisfied with Mary's conduct during the sequestration and has recommended granting her personal discharge at the first year anniversary, the Trustee has to prepare and send the report to the AIB (section 54 of BSA) at a point after the 10 month anniversary of the appointment with Appendix N (Trustee Report for debtor discharge)

If she has not co-operated with him, has he considered asking her to attend either a Private or Public Examination in front of a Sheriff;

Whether criminal proceedings have been brought against Mary. If so, has any Proceeds of Crime Order has been made against Mary and if so the date of the order to determine whether the Order or sequestration would rank first in relation to sums recovered.

(c) Outline the steps which Thomas could take if, following the meeting next week, he remains dissatisfied with the progress of the Sequestration and the actions of George. (7 marks)

Steps which Thomas could take

On the face of it, there are issues which appear not to have been addressed by the Trustee for example, the potential equity in Bramble Cottage, a DCO from Mary as a minimum. It is also very concerning that there is no clarity over what has happened to the significant sums of money given to Mary by Thomas and his family. Thomas has two priorities, firstly, ensuring that realisations are now maximised going forward for the benefit of creditors and secondly to ensure the conduct of both the Trustee and debtor are addressed.

Accountant in Bankruptcy Guidance suggests that a first step is to speak directly with the person administering the case, Thomas will have done this during the meeting.

Following the meeting it would be advisable to write to George and based on the information or explanations provided at the meeting, outline the areas of concern that Thomas would like to be addressed and ask for an urgent response.

If this is not responded to or, if Thomas is still not satisfied with the response, he should consider whether it would be appropriate to secure the appointment of an alternative Trustee.

He would need to secure another Insolvency Practitioner who would consent to Act. Depending on the extent of future asset realisations, it may be necessary for him to be prepared to underwrite the costs of this process. He should therefore obtain indications of cost.

If an IP will consent to Act then Thomas should write to George and request that he call a Meeting of Creditors ("MOC"). Since we have to assume that Thomas and his family represent more than 1/3 in value of the creditors the Trustee would be obliged to call a MOC within 28 days of a request to do so. 7 days notice of the meeting would have to be given.

It would appear that Thomas is not currently a Commissioner, it would be prudent to become a Commissioner at the same time as nominating an alternative IP as Trustee. This would give him better access to information regarding the sequestration going forward. It would also help to reduce costs, as the Commissioner can audit the Trustee's accounts which would save on the AIB's supervision fee.

Whilst replacing the Trustee will give Thomas more confidence that matters are being dealt with it does not address the loss that the creditors may have suffered as a result of George's actions to date.

Thomas should consider putting his concerns to George's Recognised Professional Body. This can be done by writing directly to the RPB noted on the Trustee's letterhead or through the Insolvency Complaints Gateway.

It is also worth raising his concerns with the Accountant in Bankruptcy's office as they have the ability to issue direction to a Trustee at any time (this power is used infrequently).

In due course, depending on the findings of the new Trustee, Thomas should consider whether it can be demonstrated whether he and the other creditors have suffered a loss as a result of George's actions or lack of them as a claim against George's professional indemnity insurance may be required.

Thomas should also be aware that if his debt has been incurred as a result of fraud, then the debtor will not be discharged of this debt when the current Sequestration is concluded. If for example, there are assets which have been abandoned by the Trustee in this sequestration and are no longer available to creditors, then Thomas could benefit from these through a subsequent award of sequestration.

Question 4

Requirements

- (a) Set out the ethical and regulatory matters that you would need to consider before accepting any instructions to advise Abigail. (4 marks)**

Ethical and Regulatory Matters

You need to consider whether there is any conflict of interest in you providing advice to Abigail regarding dealing with her personal debts. You need to establish the nature of the advice given to Abigail by your Partner (tax) and who his client is ie the Limited Company or Abigail or both.

You should consider the ethical principals and the nature of any threats to these. The threats likely to be relevant here are, self interest, self review, familiarity, advocacy and intimidation.

You should consider what safeguards you could put in place to mitigate these threats.

You should also consider if you decide to act in relation to an insolvency appointment for Abigail the requirement to disclose the previous client relationship to creditors at the outset.

Assuming you think there is no conflict and that you can act, to the extent that this has not already been done by your Firm you would need to carry out money laundering (Know your client checks) to confirm her identity whether through verification of her passport/utility bills or by using a third party system.

You also need to be comfortable that the advice which you are providing falls within that permissible by your insolvency permit. Insolvency Practitioners can provide what would otherwise be considered to be Debt Counselling services under their insolvency permit, if it is provided in contemplation of an insolvency appointment. However, insolvency practitioners no longer have an exemption in relation to acting as a Continuing Money Adviser under the DAS. If you wish to act as CMA then you would require to fall within the definition of a Money Adviser or to be regulated by the FCA.

Likewise will you would be able to sign post to solutions such as a consolidation loan, you will not be able to offer this product and advice unless appropriately authorised.

(b) Explain the various statutory and non-statutory procedures that might be available to Abigail to resolve her difficulties. (14 marks)

General

Abigail has assets of £55,500 plus any value in her shareholding. This compares to unsecured debts of £23,550. Based on the information provided, she is not balance sheet insolvent. However, she has sought advice in relation to her debts which suggests that with her current income, she is unable to meet the statutory payments on these. The existence of the equity in Abigail's property means that Abigail does not require debt relief (and indeed should not be able to obtain it). However, it appears that she does need time to pay her debts.

An assessment of her income and expenditure is required (see additional information below) to understand the level of debt repayment currently being made and establish the level of funds Abigail could have to service her debts on a monthly basis whether as part of a refinancing or a statutory debt solution. A significant amount of Abigail's debt is her student loans, since 2008/10 (depending on the type of loan) these are no longer able to be written off through insolvency proceedings.

Student Loans in Scotland need to be repaid when Gross Income > £17,945 and then you repay 9% over £17,495. Abigail is likely to be paying Student Loans £585pa which is c £50 per month. This is not a loan on commercial terms and will be relatively cheap debt. Payments will increase as income increases. Abigail is also the director of a limited company she should be aware that she will be unable to continue to act as a director if she was sequestrated.

The options available to Abigail include:

Informal solutions

Income maximisation – is her company able to sustain an increase in her salary?

Expenditure review – Does Abigail need her car, could she run a cheaper one, does she want to stay in her property, could she take in a lodger to offset some mortgage cost.

Additional borrowing/consolidation loan – consolidate all of her debts into one loan which is potentially secured against the equity in her property. This depends on the level of income which Abigail has to service the loan.

Consider remortgaging and using some of the equity in her property to pay off unsecured debts – again dependent on level of income to support increased mortgage payments and that the student loan is relatively cheap debt;

Assistance from ***family member/friend*** who could help her clear the most pressing debts.

Releasing Assets – would she consider encashing premium bonds, selling car to reduce her indebtedness.

Informal agreement with creditors/Debt Management Plan. Neither of these options would provide debt relief, or freezing of interest and charges or any real protection from creditors.

Debt Arrangement Scheme. This would provide Abigail with protection from her creditors, the ability to freeze interest and charges (provided that she maintains her payments) while she repays her debt in full. If Abigail could afford to pay around £300 per month then the period of the DAS would be around 6.5 years.

Abigail would be required to repay 100% of her debts, however, the costs of the payment distributor would be deducted from that 100%, so that the creditors receive less than 100%. Interest and charges would be frozen and there would be no statutory interest required. Abigail could obtain the services of a Money Adviser for free (and you are obliged to tell her this) or she could pay for these services which is likely to increase the payment term.

The equity in Abigail's property is unaffected by the DAS. Although she could consider releasing some equity or cashing in her Premium Bonds to make an initial payment to her DAS which would reduce the payment term (potentially by around 25% from the value of her premium bonds). Creditors have the right to object to the DAS and request that the DAS administrator consider the fair and reasonableness test. In this case creditors may argue that with this level of equity, it is unreasonable that they do not receive payment in full (and are required to freeze interest and charges in the meantime) for over six years.

Reducing the payment term by releasing funds from the equity or the bonds could reduce the likelihood of this.

Comment on whether Student loan included – yes ?

Trust Deed or Bankruptcy. As Abigail has the means to pay her debts in full, she would be required to do so in either scenario. In a Trust Deed an agreement would be reached about the level of contribution to be paid and how and when the required equity in the property would be released. Some practitioners may consider accepting an additional years contributions in lieu of the equity if Abigail cannot release it. However as she is solvent, the creditors are likely to object to this approach. Similarly, the creditors are unlikely to agree to a property exclusion. It would be important for Abigail to understand the Trustee's Costs and also the extent of the statutory interest which would be applied to her debts at 8%. This could be significant depending on the timing of when creditors were able to be paid. Sequestration would also require sufficient funds to be realised from the equity and contributions to pay the creditors in full plus interest and costs. Sequestration would have the additional important implication for Abigail that she would not be able to act as a company director while an undischarged Bankrupt. Discharge is possible after 1 year assuming that Abigail does co-operate and has made a full and fair surrender of her estate. However, this would present a practical, problem for the limited company and the solution would need to be carefully considered. It is also worth noting that the Trustee in Sequestration has more powers to investigate antecedent transactions should this be a concern for Abigail.

(c) Advise Abigail which procedure is most likely to be applicable to her. You should explain what further information you would require in order to advise her more fully and set out any assumptions which you have made. (7 marks)

Recommendation and information required from Abigail

I would **not recommend** that Abigail embark on an insolvency solution as it is not appropriate in her circumstances. The implications of insolvency and the additional costs would make it a costly way to pay her debts in full. I would **recommend** that Abigail explore the steps such as income maximisation and reviewing her expenditure together with realising assets to help reduce her debts in the first instance, if this has already been done, or does not manage the creditor pressure, assuming that there is a reasonable surplus income to allow Abigail to pay her debts in full within a reasonable timescale as estimated above, I would **recommend** that she make an application for a DPP under the Debt Arrangement Scheme. If she is prepared or able to do so then cashing in the premium bonds/releasing some equity in the value of the property or shares would reduce the payment term for her.

Comment on the impact of each option on credit rating.

Any of the statutory solutions available would require Abigail to make a contribution of her full surplus income for a period of 48 months or until her debts are paid in full. An assessment of Abigail's Income and Expenditure and therefore surplus monthly income using the Common Financial Tool is required. It is also important to understand the level of surplus income that is available each month to service a consolidation loan/remortgage. What does Abigail's gross income of £2,000 per month equate to in net terms ? What are her outgoings, for example, mortgage, council tax, utilities, travel costs and housekeeping ? How does Abigail foresee the income which she is able to draw from the company changing is this stable or likely to increase or decrease in the short to medium term.

If Abigail were to progress any of these solutions then verification of her income would be required (3 months payslips and or Bank Statements) and her monthly outgoings would also have to be evidenced.

Value of her 100% shareholding in the limited company. What do the last set of accounts show in terms of shareholder value – copy of most recent set of accounts. Would she want to realise any of this value and is there any means to do so, for example an employee, or colleague who would want to acquire a share in the business. Check Memorandum and Articles to establish whether/how the shares could be sold, assuming this was appropriate.

Check that any part of Abigail's Student Loan is not a Graduate Endowment this is the only type of student loan which would be discharged in a bankruptcy.

Is this list of creditors complete, does Abigail have any additional debt? For example is she on her company payroll or does she owe HMRC any sums. Does she have Council Tax arrears. Does she have any other secured lending for example, a second security on the property or a loan secured on her car?

How accurate is the equity figure ? Is it based on a recent valuation and redemption statement. There is a general presumption that Abigail will not want to sell her home, but is this actually the case and would she consider selling/downsizing to address her debts.