

Tuesday 12 November 2019

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## CORPORATE INSOLVENCY (3.5 hours)

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This exam consists of **four** questions (100 marks).

### Marks breakdown

|            |          |
|------------|----------|
| Question 1 | 20 marks |
| Question 2 | 20 marks |
| Question 3 | 20 marks |
| Question 4 | 40 marks |

1. Please read the instructions on this page carefully before you begin your exam. If you have any questions, raise your hand and speak with the invigilator before you begin.
2. Please alert the invigilator immediately if you encounter any issues during the delivery of the exam. The invigilator cannot advise you on how to use the software. If you believe that your performance has been affected by any issues which occurred, you must request and complete a candidate incident report form at the end of the exam; this form must be submitted as part of any subsequent special consideration application.
3. Click on the **Start Test** button to begin the exam. The exam timer will begin to count down. A warning is given five minutes before the exam ends. When the exam timer reaches zero, the exam will end. To end the exam early, press the **Finish** button.
4. You may use a pen and paper for draft workings. Any information you write on paper will not be read or marked.
5. The Examiner will take account of the way material is presented. Candidates should answer the questions set: marks will not be awarded for extraneous material.
6. Ensure that all of your responses are visible on screen and are not hidden within cells. Your answers will be presented to the examiner exactly as they appear on screen.
7. References to legislation are to that which was in force on 30 April 2019. References to 'The Act' are to the Insolvency Act 1986 as amended.
8. References to Sections, Schedules and Rules are to Sections and Schedules of the Act and to Rules of the Insolvency (Scotland) Rules 1986.
9. References to Sections and Rules of other Acts, Regulations and Orders will mention the Act, Regulation or Order.

## Question 1

You are an Authorised Insolvency Practitioner in a medium sized firm of accountants and are considering taking the following appointments.

- (a) You are Administrator of Doodah Signs Limited and your proposals, approved by creditors, stated that the Administration would exit into Creditors' Voluntary Liquidation and that you would act as Liquidator. Subsequent to your proposals being accepted you have received a complaint from a relatively small creditor of the company stating that they believe you were negligent in selling the trade and assets on deferred terms, given that the acquiring company has gone into Liquidation leaving the majority of the consideration unpaid.
- (b) You were engaged by Molinaro Equipment Limited to undertake an accelerated sales process of its trade and assets in the expectation that the sale would be completed by an Administrator. Despite your best efforts, the Directors were not particularly co-operative during the process and did not allow the business to be marketed widely. The Directors have made an offer for the assets in line with agent valuations, to be concluded immediately following the appointment of an Administrator. If the sale does not complete the business will close and realisations will be significantly lower than if the Directors' offer is accepted. You have consulted with the major creditors and they have agreed that, given the circumstances, a sale to the Directors should be completed. It is proposed that you should act as Administrator.
- (c) Deagle 2007 Limited was a tax client of your Firm until it was placed into Members' Voluntary Liquidation with a Partner in a local firm of Insolvency Practitioners acting as Liquidator. Your tax colleagues had assisted Deagle 2007 Limited in relation to the company's corporation tax returns and you prepared the Declaration of Solvency for the Directors based on information the Directors had provided.

At the date of liquidation, the company's Declaration of Solvency stated that it had over £10 million of cash at bank and its only liability was a £1 million intercompany debt. Since the Declaration of Solvency was signed a significant complex liability involving a large number of claimants has been identified in relation to potential mis-selling claims and the Liquidator believes it is necessary to 'convert' the Liquidation to a Creditors' Voluntary Liquidation.

Due to the complexity of the situation, the existing Liquidator does not believe that he has the required expertise available to him and has suggested that you should be appointed in his place. Your Firm's Managing Partner is keen for you to accept the appointment as it is estimated that, due to its complexity, the Liquidation fees going forward will be in excess of £1 million.

## Requirements

**For each of the three situations described, set out the relevant ethical considerations and explain what safeguards could be put in place in relation to your proposed appointment. In each case state, giving your reasons, whether you think it would be appropriate for you to accept the appointment.**

- (a) 4 marks
- (b) 7 marks
- (c) 9 marks

**Total: 20 marks**

## **Question 2**

You, an Authorised Insolvency Practitioner, will shortly be appointed Administrator of Fountaine Tots Limited (“the Company”).

The Company currently provides day time childcare to children between the ages of two and four at three sites in the Elgin area. Of the premises two are owned, subject to mortgages, and the other is leased under a recently signed 10-year lease.

You have agreed, in principle, a sale of the trade and assets of the Company to a third party; however, as their regulatory registration may take several weeks to be granted it is your intention to trade the business until such a time that the sale can complete. The proposed third party acquirer has not confirmed whether it wishes to retain the leased premises.

### **Requirements**

- (a) Set out the key practical tasks specific to these circumstances that you would seek to undertake prior to your appointment. (10 marks)**
- (b) Explain how, in these particular circumstances, the leased property may be dealt with. (10 marks)**

**Total: 20 marks**

### Question 3

Due to the unexpected illness of a colleague you have recently been appointed as the case manager in relation to the Administration of Benarty Cakes Limited (“the Company”). The Company was placed into Administration on 30 September 2019 and two partners from your firm act as Officeholders. In their statement of proposals, it was stated that Paragraph 52(1)(b) of Schedule B1 of the Act applies.

A sale of the Company’s trade and certain assets was completed two weeks into the Administration to an unconnected third party, Oxenton (2005) Limited (“Oxenton”).

Prior to her departure your colleague provided you with a summary of several outstanding matters for you to deal with:

#### (a) Reservation of title claim

Immediately following the appointment of Administrators, Birdlip (Foods) Limited (“Birdlip”) made contact to claim title to goods remaining on site. A stocktake, undertaken on the day of the Administrators’ appointment, identified that there were 50 x 25Kg bags of Dark Chocolate and 100 x 25Kg bags of Molasses all unopened and clearly marked with Birdlip’s name.

During the course of the Administration and prior to the business sale, half of this stock was used. Oxenton has subsequently used the remaining stock.

Several weeks after the stocktake Birdlip provided information to support its reservation of title claim including a statement showing the following transactions since the start of its trading relationship with the Company as follows:

|                          |                            |                 |                 |
|--------------------------|----------------------------|-----------------|-----------------|
| <b>Total outstanding</b> |                            |                 | <b>£22,750</b>  |
| <b>Delivery date</b>     | <b>Description</b>         | <b>Quantity</b> | <b>Value £</b>  |
| 01/09/2019               | Molasses (25Kg bags)       | 200             | 6,000           |
| 09/09/2019               | Molasses (25Kg bags)       | 175             | 5,250           |
| 15/09/2019               | Dark Chocolate (25Kg bags) | 100             | 11,250          |
| 22/09/2019               | Molasses (25Kg bags)       | 250             | 7,000           |
| 28/09/2019               | Dark Chocolate (25Kg bags) | 100             | 11,250          |
| <b>Payment date</b>      |                            |                 | <b>Amount £</b> |
| 12/09/2019               |                            |                 | 6,000           |
| 20/09/2019               |                            |                 | 12,000          |

Birdlip has provided a copy invoice which has the following clause printed on its reverse:

“Notwithstanding delivery and the passing of risk, property in and title to the goods shall remain with the seller until the seller has received payment of the full price of (a) all goods and/or services the subject of the contract and (b) all other goods and/or services supplied by the seller to the buyer under any contract whatsoever.”

Birdlip is now chasing for return of their goods.

**(b) Outstanding customer debt**

You have received correspondence in relation to a £100,000 debt owed to the Company by Crickley (UK) Limited (“Crickley”). Crickley has written to you in response to a letter chasing for payment of the outstanding amount stating that it is subject to a Company Voluntary Arrangement and therefore will not be paying the outstanding amount.

**(c) Items in the possession of a former Employee**

Robert Smith was made redundant by the Administrators. Following this, a letter was sent to Robert requesting the return of certain Company owned items including a laptop (containing customer details), a mobile phone, samples pack and a petty cash float of £235.

Robert has responded stating that he is owed a month’s salary, redundancy and notice pay, that he is unwilling to repay any float and that it is his intention to sell the other items to recoup some of his losses.

**(d) Accounting information**

The Company used a web based accounting system and following the Administrators’ appointment the supplier suspended access to the data. Access to the system and data is required so that investigations can be conducted.

**Requirements**

**Set out the steps you would take to deal with each of the four matters.**

- (a) 7 marks**
- (b) 6 marks**
- (c) 4 marks**
- (d) 3 marks**

**Total: 20 marks**

## Question 4

You were appointed Liquidator of Fescue Products Limited (“the Company”) on 2 September 2019. Up until recently, the Company had been profitable, having reported a consistent annual profit before tax of £300,000 in its accounts for many years. However, year to date losses amount to £600,000 due to the unforeseen loss of a major contract.

Following an organised wind down of operations, the business closed on 5 August 2019 at which point the remaining 3 employees were made redundant by the Director, Mr Augustine. Shortly thereafter you were instructed by Mr Augustine to help him to place the Company into Creditors’ Voluntary Liquidation. A fixed fee of £25,000 was agreed in relation to your remuneration as Liquidator.

At the date of your appointment the Company’s assets were limited to some residual book debts and a freehold property. The collection process in relation to the book debts has now been completed: however, the amount recovered was only 60% of the total balance. A sale of the Company’s freehold property is expected to complete tomorrow for the sum of £250,000.

Your Receipts and Payments account to today’s date shows the following:

| RECEIPTS       |                | PAYMENTS                      |              |
|----------------|----------------|-------------------------------|--------------|
| Description    | Amount<br>£    | Description                   | Amount<br>£  |
| Book debts     | 135,000        | Liquidator’s disbursements    | 300          |
| Cash at bank   | 100            | Property valuation fee        | 3,000        |
|                |                | Legal costs - debt collection | 2,500        |
| Total          | <u>135,100</u> | Total                         | <u>5,800</u> |
| Represented by |                |                               |              |
| Estate account | 128,800        |                               |              |
| VAT receivable | 500            |                               |              |
|                | <u>129,300</u> |                               |              |

The Statement of affairs detailed the following creditors:

| Creditor                              | Security                              | Amount owed £ | Note |
|---------------------------------------|---------------------------------------|---------------|------|
| Trustees of the Fescue Pension scheme | Standard Security                     | 200,000       | 1    |
| Mr Augustine                          | Standard Security and Floating charge | 175,000       | 1    |
| HMRC                                  |                                       | 75,000        | 2    |
| Employees                             |                                       | uncertain     | 3    |
| Suppliers                             |                                       | 50,000        | 4    |

Notes:

### **1. Secured creditors**

On 2 June 2017 the Director, both personally and through his Executive Pension Scheme, lent money to the Company on a secured but interest free basis. There is a priority agreement in place stating that the debt due to the Pension Scheme ranks first.

### **2. HMRC**

The Company's liability to HMRC comprises £50,000 PAYE accrued in the lead up to the liquidation and £25,000 being a residual Corporation tax liability in relation to the previous tax year liability. All other HMRC debts including VAT had been settled in full.

### **3. Employees**

In the lead up to the closure 30 staff were made redundant and entered into settlement agreements in relation to termination payments. All of these payments were settled prior to liquidation.

Two of the employees remaining at the point of closure had only worked for the Company for 8 months prior to being made redundant and were paid up to the date of termination including notice pay.

The third employee remaining, Mrs Bahia was an office manager who had worked for the Company for 7 years after leaving college at the age of 18. She was entitled to a salary of £52,000 p.a. and her contract provided for 3 months' notice of termination. As she was paid through a different payroll when she was made redundant she was owed 2 weeks' pay but had been paid her holiday pay entitlement.

Mrs Bahia has made a claim against the Redundancy Payments Service and has now been paid accordingly.

You have recently received notice of an Employment Tribunal claim in which Mrs Bahia claims she received no notice or consultation from the Company prior to 2 September 2019 and is seeking a Protective Award. Your solicitor has reviewed the claim and has advised that there is no defence to put forward and it is virtually certain that Mrs Bahia will obtain the maximum award.

Since she was made redundant Mrs Bahia has been unable to secure employment elsewhere and is receiving £73.10 per week by way of Job Seeker's Allowance.

### **4. Suppliers**

The balance in the Statement of Affairs accurately reflects claims.

### **Requirements**

- (a) Briefly explain and quantify the claims that the Liquidator could make either to minimise the amount due to HMRC or to recover funds from HMRC for the estate. (10 marks)**

- (b) Calculate and set out the employee claims, clearly indicating the extent to which they are preferential and the amounts that would be paid by the Redundancy Payment Service. (8 marks)
- (c) Set out how the existing and any future funds will be disbursed from the estate, making it clear in your answer the priority of entitlement for each creditor and the expected return to each. (10 marks)
- (d) Explain how your answer to part (c) would differ had the priority agreement stated that Mr Augustine's standard security ranked first. (3 marks)

You subsequently identify that the Company was mis-sold an interest rate hedging product and agree a settlement with the bank concerned. This settlement results in a refund of £300,000 into the estate.

- (e) Explain how you would deal with this situation assuming that you distribute funds to creditors on 1 September 2020. (9 marks)

**Total: 40 marks**

### **Assumptions**

- Corporation tax rate of 20%
- VAT at 20%
- 52 weeks in a year