

JOINT INSOLVENCY EXAMINATION BOARD

*Joint
Insolvency
Examination
Board*

Joint Insolvency Examination

Wednesday 5 November 2014

PERSONAL INSOLVENCY (3.5 hours)

ANSWER ALL FOUR QUESTIONS

EACH QUESTION CARRIES TWENTY-FIVE MARKS

SUBMIT ALL WORKINGS

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

Note: References to legislation are to that which was in force on 30 April 2014. References to 'the Act' are to the Insolvency Act 1986 as amended.

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

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

1. You are a Manager working for Mr Broughton who is an Authorised Insolvency Practitioner and a partner in a firm of Chartered Accountants.

A Bankruptcy Order was made against Cully Dixon (“Mrs Dixon”) on 31 January 2013 on a creditor’s petition. On 13 March 2013 Mr Broughton was appointed as Mrs Dixon’s Trustee in Bankruptcy. You have day to day responsibility for the case.

Mrs Dixon traded under the name Aspen Tallow Toys (“the Business”) which was closed down by the Official Receiver on the day that the Bankruptcy Order was made. The Business manufactured a range of toys from wood sourced exclusively from a local company, Binwell Sawmills Limited (“Binwell”). You have obtained several boxes of books and papers relating to the Business, which were sent to you by the Official Receiver shortly after your appointment.

After realising all of the assets, there is £150,000 available for distribution.

To date you have received 36 proofs of debt for claims totalling over £300,000. For the most part you have admitted the proofs as submitted, but there are seven proofs outstanding on which no decision has yet been made, as follows:

- HMRC has lodged a proof for £47,400. The supporting paperwork shows that the gross amount claimed is £54,500, comprising income tax assessments totalling £41,000 (raised in the absence of tax returns) and interest and penalties of £13,500. From this sum has been deducted a VAT refund due to the Business of £7,100.
- Shortly after Mr Broughton’s appointment you arranged for his interest in the lease of the small factory unit from which the Business operated to be disclaimed. The Landlord has lodged a proof claiming rent due of £19,500 from 29 September 2012 to 25 March 2022, being the date on which the lease was due to expire. Also included in the Landlord’s proof is an amount of £12,000 for dilapidations.
- Binwell is the largest creditor and has lodged a proof for £86,000. Correspondence to you from a solicitor, who was approached by Mrs Dixon in 2012, suggests that a number of the invoices submitted by Binwell were disputed by Mrs Dixon and that she had contemplated taking legal proceedings against Binwell. The grounds for considering proceedings are not entirely clear but seem to be based on (1) the supply of poor quality timber which led to excessive wastage and claims from customers, and (2) the consequential losses suffered by the Business.
- A proof has been received from a Mrs Stephens who is claiming £3,200, being the estimated cost of rebuilding her garden wall. According to Mrs Stephens, in November 2012 a van owned by the Business crashed into the wall causing significant damage. Mrs Stephens has tried to make a claim against her own insurers but they have declined to become involved and have instead suggested that she should make a claim in Mrs Dixon’s Bankruptcy.
- In 2011 Mrs Dixon started legal proceedings in the County Court against a customer of the Business seeking to recover an unpaid debt of £17,000. The claim was hotly contested by the customer who claimed that the toys supplied were unsafe. The case concluded in September 2012 when the Court found in favour of the customer and rejected Mrs Dixon’s claim. Mrs Dixon was ordered to pay the customer’s legal costs and, in February 2013, these were assessed by the Court at £9,500. A proof for this amount, plus statutory interest at 8% of £520, has recently been received.
- A proof for £13,300 has just been received from Mrs Dixon’s husband. You are aware that Mr and Mrs Dixon have separated but are not divorced. The supporting paperwork suggests that, in the past three months, Mr Dixon has made payments totalling £13,300 to four banks with which he and Mrs Dixon held joint accounts, all of which were overdrawn.

- Dunstan Boxes Limited (“Dunstan”) has lodged a proof for £38,000 for unpaid invoices relating to the supply of packing materials. According to the Official Receiver’s agents, a quantity of unused packing was returned to Dunstan when the factory unit was cleared. Mr Broughton has pointed out that Dunstan is a client of one of his audit partners.

Mr Broughton wishes a dividend to be paid to creditors as soon as practicable and has asked for a memorandum explaining what needs to be done to agree the outstanding claims.

Requirements

Draft the memorandum. Set out the steps that you would take to deal with the seven proofs. In each case explain the legal and/or other principles which you will need to apply and set out any further information which you will require.

(25 marks)

2. You are an Authorised Insolvency Practitioner.

Yesterday afternoon you were consulted by Ben Jones (“Mr Jones”) who is a director of Malham Cross Limited (“Malham”) which manufactures and sells designer handbags and other accessories to independent retailers.

Mr Jones told you that one of Malham’s major customers is Kate Wilding (“Kate”) who owns and runs a boutique selling women’s up-market fashion accessories. For some time Mr Jones has suspected that Kate might be in financial difficulties. Whilst payments have been received on a regular basis, the total due to Malham has increased over recent months and currently stands at £37,000. Mr Jones told you that yesterday morning he had spoken to Kate to tell her that Malham would not make any further deliveries until it receives payment of all overdue invoices.

Mr Jones explained to you that, within a few minutes of speaking to Kate, he received a call from an Authorised Insolvency Practitioner (“the IP”). The IP told Mr Jones that Kate is unable to pay her debts of around £140,000 and that recently he had advised her that she should propose an Individual Voluntary Arrangement (“IVA”). The IP further explained that Kate has provided some information to enable him to draft the proposals and that he expects to agree to act as Nominee next week. He stated that he does not consider it will be necessary for Kate to make an application for an Interim Order. He told Mr Jones that he should receive the proposals and Nominee’s report within about 10 days.

Malham has supplied Kate’s boutique for many years and it accounts for about 10% of Malham’s turnover. Therefore, Mr Jones is keen to help Kate if he can and, in principle, would support an IVA. However, he was adamant that Kate would only receive his support if he is convinced that she is being open and honest with her creditors.

Mr Jones asked you to write to him to explain how he will be able to satisfy himself that this is the case and that Kate is deserving of his support. You agreed to write to Mr Jones.

Requirements

Write a letter to Mr Jones. In your letter you should:

- (i) explain the role of a Nominee, the purpose of his report to creditors and the obligations placed on him by legislation, best practice and relevant case law. A listing of the contents of a proposal as prescribed by Rule 5.3 is not required. (20 marks)**
- (ii) set out your suggestions as to the steps that Mr Jones might himself take to be satisfied that he should support an IVA proposal made by Kate. (5 marks)**

(25 marks)

PLEASE TURN OVER

3. Last weekend a friend, George Bullard (“George”), came to see you. He explained that he faces financial difficulties because he is no longer able to meet the monthly repayments on debts of £65,000 which he incurred paying nursing home fees for his ageing parents. Sadly, both have recently died.

George told you that he has consulted an Insolvency Practitioner (“the IP”) who has advised that the best option would be for George to propose an Individual Voluntary Arrangement (“IVA”). However, before agreeing to act as Nominee, the IP wants to be sure that a small business owned and run by George will be able to continue to trade and will provide George with sufficient income to meet not only his personal living expenses but also a monthly contribution into the IVA. George has been asked by the IP to provide a cash flow forecast, prepared on a monthly basis, for the year ending 31 October 2015, together with a profit and loss account for the year ending 31 October 2015 and a balance sheet as at that date. George asked for your help in preparing these documents.

George has given you the following information:

- George’s business is called Bullard Prints (“the Business”). The Business buys unframed prints of well-known pictures, puts them into frames and then sells them either to the general public or to budget hotels, public houses and restaurants.
- In recent times the Business has consistently achieved sales of £20,000 per month and George expects this to continue up to and including April 2015, after which he is confident that monthly sales of £25,000 can be achieved. George estimates that 60% of sales will be to the public and 40% to the hospitality sector. George told you that, in addition to the expected regular monthly sales, a one-off contract (“the Contract”) has been signed with a chain of hotels under which an order with a sales value of £60,000 will be delivered in March 2015.
- Sales to the public are made from orders received through the Business’s website and payment is made by customers at the time that the order is placed. Orders received in this way are dispatched within 24 hours of being received. Sales to the hospitality sector are made on credit and customers typically pay in the second month following the month of the sale. The Business suffers negligible bad debts.
- The Business achieves a gross profit percentage of 50% on sales to the public and 40% on all other sales. Cost of sales comprises only the direct costs of buying in the prints and frames.
- The Business does not hold stocks of prints and frames but acquires these on a “just in time” basis from suppliers in the same month that they are sold by the Business. An exception to this will be the Contract: for this George will need to acquire the necessary prints and frames one month earlier than normal. Suppliers of prints and frames require their invoices to be paid in the month following the month of delivery.

- At 31 October 2014 the balance sheet for the Business was as follows:

	£
Fixed assets at net book amount	22,000
Debtors	16,000
Balance at bank	<u>7,000</u>
	45,000
Creditors for supplies	<u>(10,800)</u>
Proprietor's funds	<u><u>34,200</u></u>

- The Business's Bank is keen for the Business to continue. However, it has made it clear that it will not be willing to allow the Business's bank account to become overdrawn at any time. The Bank is not owed any money by George personally.
- The Business's fixed assets are depreciated at 25% per annum using the reducing balance method. George does not expect to buy or sell any fixed assets over the coming year.
- Other than the costs of buying the prints and frames, all the Business's costs are paid for in the month in which they are incurred. They currently amount to £7,500 per month, but George expects these to increase by £2,000 per month from May 2015.
- George needs to draw £2,500 from the Business each month to meet his personal living expenses. In addition, the IP has estimated that George would need to draw £500 each month to fund the contribution into his IVA.

Requirements

- Prepare a cash flow forecast on a monthly basis for the Business for the year ending 31 October 2015. Set out your supporting calculations and state clearly any assumptions which you have made. (12 marks)**
- Prepare a profit and loss account for the Business for the year ending 31 October 2015 and a balance sheet as at that date. Set out your supporting calculations and state clearly any assumptions which you have made. (8 marks)**
- Giving your reasons, set out the practical difficulties and risks facing George were he to continue to trade the Business in an IVA. (5 marks)**

(25 marks)

Note: Ignore all taxation, including VAT

4. You are an Authorised Insolvency Practitioner. Two days ago, on 3 November 2014, the Secretary of State appointed you Trustee in Bankruptcy of Daniel Scott (“the Bankrupt”). The Bankruptcy Order was made on 22 August 2014 on a creditor’s petition presented on 16 April 2014.

From the papers handed over by the Official Receiver it appears that the Bankrupt made an unsuccessful attempt to oppose the Bankruptcy Petition. Having failed to prevent the Bankruptcy Order being made, the Bankrupt informed the Official Receiver that he intended to propose an Individual Voluntary Arrangement (“IVA”). On 28 August 2014 the Bankrupt obtained a Court Order under Rule 6.34(3), preventing the Official Receiver from taking steps to advertise the Bankruptcy Order before 24 October 2014. The Bankrupt did not take any steps to propose an IVA and therefore the Official Receiver, who appears not to have done anything else, advertised the Bankruptcy Order and procured your appointment.

Yesterday, 4 November 2014, you and your property and chattels agent (“the Agent”) met the Bankrupt at his business premises. You ascertained the following:

- The Bankrupt owns a motor business called Badger’s Drift Garage (“the Garage”) which specialises in cars from the 1960s. For the most part the Garage is concerned with servicing and repairing but it also takes on longer term restoration projects and buys and sells a few vehicles. The Garage is still open for business, although only two vehicles are booked in for servicing over the coming month.
- The Garage leases the whole of a two storey building under a 25 year lease entered into 23 years ago when the Garage first opened. The whole building is in a very poor state of repair and the rent due in September 2014 has not been paid. During your visit you met the landlord, David Whitely, who handed you a letter from his solicitors holding you personally responsible for paying the rent and for clearing and renovating the building.
- The Garage trades from the ground floor of the building. The first floor has been divided into three bedrooms with a shared bathroom and kitchen. The accommodation and its contents are very dated. The Bankrupt told you that the hotel next door pays cash in advance to use the bedrooms as overspill accommodation for kitchen staff. Two of the bedrooms have been reserved for use this week.
- On inspecting the contents of the ground floor, the Agent discovered a rare Causton GT motor car which appeared to be in full working order and three other vehicles where restoration is in progress. He also found a large quantity of parts which, according to the workshop manager, are from vehicles which have been broken for spares. The paint shop contains a large quantity of paint. The yard behind the building resembles a scrap yard and in one corner is a shipping container holding rusty barrels of used engine oil and brake fluid. At the front of the building is a small forecourt where seven cars are displayed for sale.
- Your meeting with the Bankrupt was rudely interrupted by Olive Beauvoisin who announced that she had arrived to collect her prized Draycott XTC, which was nowhere to be seen. She explained that, in early September 2014, she had made an agreement with the Bankrupt for him to sell the vehicle in return for which he would receive a 10% commission. The Bankrupt confirmed that such an arrangement had been made, but told you that the vehicle had been sold two weeks ago and the proceeds had been paid into the Garage’s bank account.
- As you were about to leave the Garage the receptionist handed you a large pile of unopened mail. You opened a number of envelopes: each contained evidence of an outstanding creditor account, accrued from the start of 2014, right up to the current date.

This morning you met the Agent to consider what you had both found and to decide what immediate steps to take.

Requirements

- (a) What factors would you take into account in making the decision on whether or not to continue to trade? (5 marks)

- (b) Assuming you decide not to continue to trade, identify the issues to be dealt with and the actions that you and the Agent will need to take in the next week. In relation to each issue, state clearly the relevant law and any assumptions which you have made. (20 marks)

(25 marks)

