

## **Joint Insolvency Examination 2022**

15 NOVEMBER 2022

3.5 HOURS

### **CORPORATE INSOLVENCY** (Scotland)

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

**References to legislation are to that which was in force on 30 April 2022. References to ‘the Act’ are to the Insolvency Act 1986 as amended.**

**References to Sections, Schedules and Rules are to Sections and Schedules of the Act and to Rules of the Insolvency (Scotland) Rules 2018.**

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

#### **Important Information:**

Please read the instructions on this page carefully before you begin your exam

1. Click on the **right arrow** in the header to begin the exam. The exam timer will begin to count down
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. A warning is given five minutes before the exam ends. When the exam timer reaches zero, the exam will end. To end the exam earlier, navigate to the last question and click the right arrow button. Click the **Submit** button to close the exam
4. Click on the **right arrow** in the header to begin the exam. The exam timer will begin to count down..
5. When the exam timer reaches zero, the exam will end. To end the exam earlier, navigate to the last question and click the right arrow button. Click the **Submit** button to close the exam.
6. You may use a pen and paper for draft workings. Any information you write on paper will not be read or marked
7. You must make sure your answers and workings are clearly visible in the word processing area when you submit your exam. **Only your answer in the word processing area will be marked.** You must copy over any data from the spreadsheet area to the word processing area for marking. The

examiner will **not** be able to expand rows or columns where content is not visible.

8. The examiner will take account of the way in which your answers are structured. Respond directly to the exam question requirements. Do not include any content or opinion of a personal nature, this includes your name or any other identifying content.

## Question 1

You are a partner in a firm of accountants and an Authorised Insolvency Practitioner. You have been approached by one of the firm's clients, Buddrose UK Limited ("Buddrose"). Buddrose is seeking advice in relation to one of its customers, Currie Commercial Limited ("the Company").

As a result of an overdue debt of £350,000, several months ago Buddrose ceased to provide its services to the Company. Due to the criticality of the services provided, it quickly became clear that the withdrawal of Buddrose's services had created a significant issue for the Company and, as a consequence, it was facing closure. To avoid this situation, the parties agreed that Buddrose would continue to supply the Company on the condition that it received weekly payments of £100,000 to cover the full cost of ongoing supply and a contribution towards reducing the arrears.

The first payment was made on time; however no further payments were received. After chasing the Company and once more ceasing the supply of its services, Buddrose discovered that the Company had sourced an alternative supplier. The Company subsequently made a revised offer to make weekly payments of £2,000 to Buddrose.

The Company now owes Buddrose £400,000, comprising the original debt and additional services rendered, less the £100,000 payment received. The Directors of Buddrose are aggrieved that Buddrose's exposure has increased and that, based on the level of proposed weekly payments, it will take several years to repay the debt.

### Requirement

- (a) Set out the key steps that Buddrose would take to place the Company into compulsory liquidation.**

**(5 marks)**

Shortly after the presentation of a petition for a winding up order, Buddrose was notified that the Company had been placed into Administration by its Qualifying Floating Chargeholder. It was informed that, immediately following this appointment, the business and its assets were sold to Hemphill Limited, a company connected to the Company by virtue of having common directors and shareholders.

Buddrose is concerned as to the turn of events and the actions of both the Company's Directors and the Administrators. Despite being the largest creditor, Buddrose was not consulted in relation to the sale process and its Directors believe that very little marketing was undertaken. The Directors of Buddrose have expressed a preference for you to be appointed as Administrator in place of those already in office.

### Requirement

- (b) Explain how you would respond to this request.**

**(5 marks)**

Having decided not to pursue your appointment as Administrator, four weeks later Buddrose receives a copy of the Administrators' statement of proposals. The Administrators are not seeking approval of the proposals as they consider that Paragraph 52(1)(b) of Schedule B1 applies.

Buddrose is astounded as to the level of fees already incurred and expected to be incurred by the Administrators as set out in this report and, as they have not been asked, are confused as to how these have been approved.

**Requirement**

- (c) Explain to Buddrose the circumstances in which they would have been asked to approve the remuneration of the Administrators and, given the circumstances, set out what action they can take if they are dissatisfied with the level of the fees charged.**

**(5 marks)**

Due to issues with their replacement supplier, several weeks later Hemphill Limited approaches Buddrose seeking a quote to use its services. Having lost a significant amount of money as a result of the Company's failure Buddrose is keen to avoid making the same mistake again.

**Requirement**

- (d) Explain how Buddrose could protect itself from another bad debt arising in the event that Hemphill Limited were to fail to pay.**

**(5 marks)**

**Total: 20 marks**

## Question 2

You have been approached by Mrs Butani who wishes to place Kurtz Brewer LLP (“the LLP”) into Creditors’ Voluntary Liquidation.

The LLP was formed in 2018 and traded as a firm of industrial architects, concerned in the design of commercial food processing factories. Its financial difficulties started in early 2021 following the loss of a key account and, after an unsuccessful year trying to replace this customer’s business, the members of the LLP concluded that they should try and sell the practice. Unfortunately this was also unsuccessful and the business closed on 30 September 2022 as it was unable to meet the £50,000 monthly payroll for its 10 members of staff.

Mrs Butani, who is an architect by trade, wishes to engage your firm to assist her in the preparation of the relevant documentation to place the LLP into liquidation. She is one of 3 members of the LLP, having been appointed to this role in 2021. Following the LLP’s closure, she and her fellow members have found employment elsewhere.

In order to prepare the statement of affairs, Mrs Butani has provided a copy of the balance sheet from the most recent management accounts prepared by the LLP up to 30 September 2022 together with some notes relating to its contents.

	£	Note
Fixed assets		
Leasehold improvements	75,000	1
Office equipment	25,000	2
	<u>100,000</u>	
Current assets		
Work in progress	60,000	3
Debtors	150,000	4
Prepayments and other debtors	40,000	5
	<u>250,000</u>	
Current liabilities		
Bank overdraft	(50,000)	6
Trade creditors	(50,000)	7
Deferred income	(75,000)	8
Finance leases	(15,000)	2
HMRC	(70,000)	9
Other creditors	(70,000)	10
	<u>(330,000)</u>	
Net assets attributable to members	<u>20,000</u>	
Loans and other debts due to members	<u>20,000</u>	11

### Notes:

1. The LLP occupied an office under a 10 year lease, paying rent, which Mrs Butani believes was market rate, of £30,000 per annum, payable in advance on the normal quarter days. As at 30 September 2022 there were 6 years remaining on the lease and the members handed the keys back to the landlord when the business was closed. The leasehold improvements relate to a mezzanine floor that the LLP built at the property: however, under the terms of the lease the LLP is required to reinstate the property to its original condition at the end of the lease. The cost of doing so is estimated at £30,000.

2. Of the office equipment, £20,000 relates to specialist Computer Aided Design equipment that was returned to the finance lease company immediately following closure. The finance company has sent a letter to Mrs Butani requesting payment of the remaining liability under her personal guarantee. Mrs Butani has paid the sum of £10,000 representing the final amount due under the terms of the agreement. The remaining office equipment was considered valueless and has been disposed of.

3. There were two projects underway when the business closed and the work in progress balance was an estimate as to the proportion of work that had been undertaken. Project Pumpnickel accounted for £40,000 of the balance and was 60% complete. The other project, codenamed Project Penguin involved the design of a refrigeration plant and was 40% complete. As the LLP was unable to complete these projects, and to ensure the customers were not let down, Mrs Butani and one of the other members plan to complete Project Pumpnickel and Project Penguin (respectively) at their new employers.

4. The trade debtor balance relates to invoices raised during the 2 months prior to the LLP's closure. Of these there is one particular customer, Hill Snacks Limited, that has raised some concerns regarding the service provided by the LLP. This customer owes £50,000 and Mrs Butani expects that only half of this will be collectable. Of the remaining balance, she anticipates that the liquidator will be able to recover 70%.

5. Within this balance is a deposit provided to the landlord representing 6 months' rent. In addition there is a balance of £10,000 relating to a professional indemnity insurance policy and the remainder relates to pre-paid marketing events, of which Mrs Butani expects 50% to be recoverable.

6. The bank overdraft is secured by a floating charge over all the assets of the LLP.

7. Included within trade creditors is the landlord's invoice for rent due in September 2022.

8. Due to concerns regarding the LLP's cash flow the members took the decision to, where possible, seek payment in advance for its services. £40,000 of this balance relates to Project Pumpnickel and the remainder to clients where work has yet to commence.

9. HMRC's debt comprises:

	£
VAT (Quarter to September 2022)	30,000
PAYE deductions	15,000
Employer National Insurance	15,000
Employee National Insurance	10,000
	<u>70,000</u>

10. The other creditors balance comprises a holiday pay accrual for the LLP's employees and arrears of pay. These employees were made redundant on closure and were owed a further £150,000 of redundancy pay and £100,000 in relation to notice pay.

11. Under the terms of the LLP agreement Mrs Butani is entitled to 25% of the profits of the LLP subject to a minimum annual payment of £50,000 per annum. Since being appointed as a member she has received payments of £60,000 and the LLP has retained £15,000 as a personal tax provision.

## Requirements

**Draft a statement of affairs for the LLP as at 30 September 2022, together with relevant notes explaining to Mrs Butani how the figures have been determined. Explain what other information you will require in order to finalise the statement.**

**Total: 20 marks**

### Question 3

You, an Authorised Insolvency Practitioner, have been approached by Mullens Baank (“the Bank”) who currently provides funding to Alexis Containers Limited, (“the Company”).

The Company was formed in 2018 and is a logistics company owning a fleet of specialist shipping containers that are designed to reduce the forces exerted on the cargo carried in them. These containers are used for the transportation of delicate and sensitive equipment by sea or road where any in-transit damage could easily occur or would result in high costs.

In terms of its operations the Company will typically receive an order to transport one of its containers containing the customer’s goods from one location to another, usually over long distances. It does not own its own transport fleet and therefore subcontracts the road and sea travel elements to third party hauliers or shipping companies. The Company charges a per day rental for its specialist containers and also adds a profit margin onto the costs it incurs for transportation. Established customers are invoiced following delivery of the goods, whereas others may be required to make payment in advance or during the shipping process.

Whilst it provides its services internationally and to locations as far away as China and New Zealand, the majority of orders involve the UK as either the origin or destination of goods. Its customers are primarily based in Europe and they will place orders several weeks in advance so that the Company can plan the associated logistics most efficiently.

The Company has over 300 live customers but 3 account for almost 50% of the Company’s turnover, all of which are on long term supply contracts. One of these customers is a road haulage business that has an agreement to simply hire the container for use by its own customer. The Company also utilises the haulage business’s road services to transport containers for some of its own customers.

The Company owns 1,000 containers each costing approximately £8,000 and when not in use these are located in warehouses across the world depending on their previous destination. However, at any point in time there are typically 200 empty containers at the Company’s UK leased warehouse.

The Bank provides funding to the Company in the form of a term loan, used to fund the purchase of the shipping containers. In addition, the Company has an overdraft facility. The Bank has a floating charge over all the Company’s assets.

The Company wishes to expand its operations and intends to purchase an additional 200 containers. It has asked the Bank to provide the funding to enable it to do so.

The Company has been profitable in the past but increasing transportation costs have placed pressure on it due to some fixed price contracts. As a result it is under-performing compared to its forecasts and the Bank is concerned that additional debt may lead to it struggling to meet its debt servicing obligations and potentially to its failure.

As part of the credit approval process the Bank’s underwriters have asked for a report to be prepared by a firm of insolvency practitioners setting out, in the event of an insolvency process, what key issues the insolvency practitioner may face when realising the assets of the Company and how this may affect realisations and the Bank’s recovery.

#### Requirements

**(a) Provide a summary of the issues that may affect the value of the Company’s assets and the Bank’s recovery, specific to the circumstances set out above and in the event the Company entered an insolvency process.**

**(12 marks)**

**(b) In the event that the Bank wished to appoint you as Administrator of the Company, set out the key considerations and legal and practical steps that you would take prior to**

**appointment. It is not necessary for your response to cover issues identified in requirement (a).**

**(8 marks)**

**Total: 20 marks**



#### Question 4

Roland Products Limited (“the Company”) has recently experienced a number of financial issues that has resulted in creditor pressure.

The Company has approached you for advice given that creditors are now threatening legal action. The Directors have undertaken a full review of the Company’s financial performance and are certain that it can afford to repay these debts should it have the breathing space to do so. The Directors believe that the Company’s secured lender Levy Funding plc (“the Bank”) will be supportive of such an approach.

Given the level of creditor pressure, the Directors think that to rescue the Company it needs a moratorium on legal action and time to restructure its debts.

#### Requirements

- (a) Explain the principal differences between an Administration moratorium and a moratorium under the provisions introduced by the Corporate Insolvency and Governance Act 2020.

4 marks

- (b) Outline the procedure necessary to obtain a moratorium under the provisions introduced by the Corporate Insolvency and Governance Act 2020

5 marks

Prior to taking any steps to obtain a moratorium, the Company established that it is in a worse financial position than it originally thought. As a consequence, the Company’s Directors now believe that a rescue will not be possible and that the business should be sold. The Bank broadly supports this strategy.

Due to increasing supplier pressure, the Company needs protection from creditor action, in particular its landlord, and therefore it is proposed to place the Company into Administration imminently. The Bank has indicated that it may be willing to provide funding to the Administrator to allow the business to continue to trade, provided it is likely to enhance overall realisations.

The Company has provided you with the following information:

- **Sales:** the Company’s Sales Director has provided an estimate of the sales (net of VAT) achievable over the next 6 weeks, as set out below. On average the Company achieves a (materials only) gross margin of 35% and customers pay 2 weeks after delivery of the goods. The existing debtor book is subject to a debt factoring arrangement and it is anticipated that there will be no surplus over the amount owed to the lender. The factoring company has agreed that any sales made during the Administration will not be factored.

Week	Net Sales (£)
1	150,000
2	200,000
3	175,000
4	150,000
5	250,000
6	225,000

- **Stock:** the Company is a 'Just in Time' manufacturer and currently holds only a low level (£50,000) of stock. This is not subject to reservation of title as all recent deliveries have been made on a proforma payment basis, an arrangement which is expected to continue.
- **Delivery costs:** the Company uses a third party supplier who charges the equivalent of 5% of the net sales value. It is anticipated that this supplier will agree to being paid 1 week in arrears.
- **Production staff:** these employees are paid weekly, 1 week in arrears. The total payroll cost is 10% of sales and, of this total, National Insurance and PAYE account for 30% and employer pension contributions 5%. It is anticipated that gross arrears of £20,000 will have to be paid as normal to secure the employees' cooperation.
- **Office staff:** the Company employs 20 salaried office staff. The staff are paid at the end of each 4 week period and they have just been paid. The current salary costs are £40,000 every 4 weeks and, of this total, National Insurance and PAYE account for 35% and employer pension contributions 5%. It is anticipated that on appointment of the Administrator 5 staff on an average annual salary of £24,000 each will be made redundant with the remaining staff retained.
- **Other costs:** the landlord is paid £25,000 per month and other costs, expected to be paid on a proforma basis, amount to £5,000 per week.

### Requirement

- (c) **Using the above information, and assuming trading ceases at the end of week 6, set out an 8 week cash flow forecast. Identify the peak funding required from the Bank, the point at which this funding can be repaid and the overall benefit to creditors of continuing to trade.**

**(18 marks)**

Following your appointment as Administrator, the business was sold and the assets of the Company are now realised. Due to the complexity of the situation you are now only 5 weeks away from the second anniversary of the Administration, having already extended it for 1 year by creditor consent. The level of realisations is such that there is an amount to be distributed to the unsecured creditors in accordance with Section 176A of the Act. You have not commenced any steps in relation to distributing these funds.

### Requirements

- (d) **Set out the key steps required to distribute the prescribed part to unsecured creditors.**

**(8 marks)**

- (e) **In these circumstances, explain how you would ensure that there is sufficient time to arrange for the remaining funds to be distributed and the steps you would take in this regard.**

**(5 marks)**

**Total: 40 marks**

**Note: assume a VAT rate of 20%**