JOINT INSOLVENCY EXAMINATION BOARD

DECEMBER 2007 EXAM (SCOTLAND)

EXAMINERS' REPORT AND MARKING PLANS

ADMINISTRATIONS, COMPANY VOLUNTARY ARRANGEMENTS and RECEIVERSHIPS DECEMBER 2007 (SCOTLAND)

EXAMINER'S REPORT

As with 2006, the reduction to four compulsory questions has provided greater focus to candidates and together with the separation of elements of the requirements into separate parts with marks allocated for each, again appears to have worked in the candidates' favour. As reported in 2006 the answers remain generally more concise, allowing candidates to demonstrate both knowledge and practical application in an easier format than writing letters or memoranda under exam conditions.

Those candidates who appear to have been able to summarise their thoughts in using the structure of the requirements and who focused attention on answering the question have generally scored well. There is less evidence in previous years of candidates treating the question as an invitation to write everything they know about a topic and/or copying out parts of the Acts and Rules.

The overall quality is somewhat spread with a cluster of candidates who, all else being equal, should pass the paper and showing a very clear divide between those who have struggled to demonstrate either the breadth of knowledge required overall, or the depth of knowledge to deal with the requirements of 30 mark questions.

I would suggest that the continued focus on using past exam papers and their marking schemes be emphasized to candidates in 2008 and subsequent years.

QUESTION 1

This question required candidates to identify compliance breaches prior to review in an out-of-court administration process, the statutory steps required to allow the administration to be completed and for the Administrator to vacate office. The question then further required candidates to prepare draft receipts and payments to accompany progress reports for each of the periods required by statute.

The most obvious failure in this question was that no candidate in Scotland dealt with the requirement for the extension properly, indeed very few candidates identified the need for an extension in their written response to Part B. As a result, candidates lost easy marks as a result of their failure to produce receipts and payments for the period required by the extension which could have been any date between 11 December 2007 (the date of the review in the question) and 1 January 2008. There are no transactions during this period in the question and the date chosen would not have affected the answer given.

Marks achieved in this question were largely therefore in Part A where a maximum of only 3 marks was available. As regards Part B, candidates did identify the need for a final progress report and reasonable knowledge was demonstrated of the requirements of that report and the parties to whom it was provided.

QUESTION 2

We might have expected Question 2 to have been performed less well in Scotland as it concerned a CVA proposal and previous exam questions on this topic have been poorly attempted. However, it is pleasing to note that several candidates achieved high marks.

The matters to be included in the CVA proposals were generally well done. The comparison of estimated outcomes between CVA best and worst case and liquidation best and worst case was particularly well attempted and well laid out by almost all candidates. Those candidates who could perhaps have got even closer to full marks failed to demonstrate their understanding as to the treatment of the group creditor and, from a practical point of view, that trading assets would be required to be used by the company in a CVA for its ongoing business (office equipment and stock) and therefore would not be available to be realised for the proceeds to be distributed amongst creditors. One or two candidates made simple arithmetical errors but this did not spoil their overall result.

In the liquidation worst case many candidates simply applied the costs of realisation per the amount in the question, not realising that this would need to be restricted to assets actually realised.

As responses were generally well laid out, candidates had little opportunity to hide or disguise their lack of knowledge.

QUESTION 3

This question required consideration of the factors that a bank would consider when deciding whether to appoint, or concur with the appointment of an Administrator or to appoint a Receiver itself. This part of the question was generally well done with most candidates demonstrating a reasonable knowledge of the points to be considered. There were surprisingly few candidates who mentioned the rates issue. More candidates, although still relatively few, mentioned the difference in tax treatment of trading profits and losses versus chargeable gains. The second part of the question was less well done. This required the candidates to outline steps that a board of directors should take to protect the interest of creditors pending the appointment of an Insolvency Practitioner and then to indicate the consequences if those steps are not taken.

The majority of candidates summarised the practical steps to be taken well. However, the section dealing with the consequences for the directors was less well done, with the majority of candidates using this as an opportunity to “brain-dump” everything they knew about CDDA. There was surprisingly little discussion around the type of antecedent transactions that may well apply in this particular case or of the sanctions available against a director found guilty of wrongful trading, fraudulent trading or preferences.

Finally, the question required candidates to detail the procedural steps required to appoint an Administrator. Very few candidates identified that an out-of-court appointment would not be possible as the winding-up petition had not yet been disposed of. Several candidates attempted to deal with this issue by opening dialogue with the petitioning creditor and asking it to withdraw the petition, which is clearly a practical solution. However, there was again (as with 2005) a clear lack of understanding on the candidates’ behalf as to the steps that require to be taken in applying for an Administration Order under the court route.

QUESTION 4

This was a relatively straightforward question requiring consideration of the factors to take into account when deciding whether or not a company should continue to trade and the practical measures and controls to manage post appointment trading. Finally, the question asked the candidates to outline the steps needed to market the business and assets for sale and the particular terms expected in a contract for sale by a Receiver.

This question was generally better attempted than Question 3 as a 30 mark question. However, candidates tended to score the most marks in Parts A and B where they were clearly more comfortable with the issues of trading and implementing controls over such trading.

The quality of answers in Parts C and D as demonstrated a lack of practical experience by candidates and again as with Question 3 demonstrated a lack of practical understanding of the issues to be considered.

JIEB ADMINISTRATIONS, COMPANY VOLUNTARY ARRANGEMENTS and RECEIVERSHIPS (SCOTLAND)

DECEMBER 2007

Exam Marking Plan

The marking plan set out below was that used to mark this question. Markers were encouraged to use discretion and to award partial marks where a point was either not explained fully or made by implication. More marks were available than could be awarded for each requirement. This allowed credit to be given for a variety of valid points which were made by candidates

QUESTION 1

(a) Identify the compliance breaches that had occurred prior to your review. (3 marks)

Notice of administrator's appointment not sent to the registrar of companies within 7 days
Proposals not sent to creditors and registrar of companies within 8 weeks of appointment
Progress report was not sent within six weeks of the end of the period to which it relates.
Progress report was apparently not sent to the court
Asset realisations made by agents on behalf of the office holder should be shown gross, before the deduction of costs of realisation. Costs of realisation should be shown separately as payments. Notice of appointment was not sent to the Keeper of the Register of Inhibitions and Adjudications Advertising could be " not as soon as reasonable practical" (award mark if discussed regardless of the conclusion)

(b) List the statutory steps that will need to be taken to complete the Administration and to enable the Administrator to vacate office. (5 marks)

Write to creditors for the purpose of obtaining consent for an extension to the period of the administration.
Consent may be written or signified at a creditors' meeting.
In this case consent means: Of each secured creditor and 50 % of the preferential creditors who take part in voting
The extension must not be for more than 6 months.
The request must be accompanied by a progress report for the period since the last report.
Consent will need to be obtained in this case no later than15 January 2008 (being the 12 month anniversary of the appointment).
Creditors must be given at least 14 days notice of a resolution to extend administration.
Therefore creditors must be in receipt of the progress report and ancillary papers no later than 1 January 2008.
When consent obtained, file notice of the extension with the registrar of companies and the court
Prepare a progress report for the period 16 July 2007 to 15 January 2008 and send to specified persons within six weeks
Prepare a final progress report for the period 16 January 2008 to 29 February 2008 and send to specified persons within six weeks
Persons to be sent progress reports are: The creditors The court The registrar of companies
Ensure creditors pass a resolution in favour of the administrator's discharge from liability.
File a notice of move from administration to dissolution (accompanied by final progress report) to The registrar of companies, and copy notice to The court The creditors

(c) Prepare draft receipts and payments accounts to accompany the Administrator's progress reports for each of the periods required by statute up to and including the proposed conclusion of the Administration on 29 February 2008. (12 marks)

There are three further discreet periods for which an abstract of receipts and payments must be prepared
First 16 July to the date of seeking the consent of the creditors to an extension to the period of administration.
The last possible day for obtaining consent to an extension is 15 Jan 2008.
Creditors require at least 14 days notice of a resolution to extend administration.
Therefore creditors must be in receipt of progress report and ancillary papers no later than 1 Jan 2008.
Therefore the period of account for a progress report in support of consent for an extension is from 16 July 2007 to any date between 11 December 2007 (date of review) and 1 January 2008. (Since there are no transactions during these later two dates, the period end date chosen should not affect the answer given.)
Cumulative account
Secondly 16 July 2007 to 15 January 2008
Cumulative account
Finally 16 January 2008 to 29 February 2008
Cumulative account

Q1 - RODRIGO WINDOWS LIMITED - IN ADMINISTRATION
ADMINISTRATOR'S ACCOUNTS OF RECEIPTS AND PAYMENTS

	ACTUAL	DRAFT		DRAFT 2nd 6 months		DRAFT	
	1st 6 months	In support of extension				Final period	
	R 2.47	R 2.112	SIP 7	R 2.47	SIP 7	R 2.47	SIP 7
	1	2		3		4	
	6 Months 16 Jan 07 - 15 Jul 07	Period 16 Jul 07- 11 Dec 07	Cumulative 16 Jan 07 - 11 Dec 07	6 Months 16 Jul 07- 15 Jan 08	Cumulative 16 Jan 07 - 15 Jan08	Final 16 Jan 08 - 29 Feb 08	Cumulative 16 Jan 07 - 29 Feb 08
	£	£	£	£	£	£	£
Assets Not Specifically Pledged							
Book debts	450,000	150,000	600,000	150,000	600,000		600,000
Retentions	150,000	100,000	250,000	100,000	250,000	50,000	300,000
Work in progress	400,000	0	400,000	0	400,000		400,000
Stock	95,000	0	95,000	0	95,000		95,000
Plant, equipment & vehicles	100,000	0	100,000	0	100,000		100,000
Interest received	5,000	10,000	15,000	10,000	15,000		15,000
	1,200,000	260,000	1,460,000	260,000	1,460,000	50,000	1,510,000
Payments							
Administrators' fees & disbursements	-70,000	-30,000	-100,000	-30,000	-100,000	-25,000	-125,000
Other professional costs	-50,000	-10,000	-60,000	-10,000	-60,000		-60,000
Direct labour	-80,000	0	-80,000	0	-80,000		-80,000
Other trading costs	-50,000	0	-50,000	0	-50,000		-50,000
Finance agreement settlements	-25,000	0	-25,000	0	-25,000		-25,000
Distributions					0		
Arrears of wages and holiday pay	-25,000	0	-25,000	0	-25,000		-25,000
Prescribed part of net property set aside		0	0	0	0		0
Floating charge holder - RHBC Bank plc	-750,000	0	-750,000	0	-750,000	-395,000	-1,145,000
	-1,050,000	-40,000	-1,090,000	-40,000	-1,090,000	-420,000	-1,510,000
Balance of funds held	**150,000**		**370,000**		**370,000**		**0**
	1,200,000		1,460,000		1,460,000	50,000	1,510,000

QUESTION 2

(a) List the matters required to be included in Nominees' comments on CVA proposals. (6 marks)

The extent to which the nominee has investigated the company's circumstances.
The basis on which the assets have been valued.
The extent to which the nominee considers that reliance can be placed on the directors' estimates of the liabilities.
Information regarding the attitude of the directors, with particular reference to instances of failure to co-operate.
The result of any discussions between the nominee and any secured creditors or other interested parties upon whose co-operation the performance of the VA will depend.
Information on the attitude of any major unsecured creditors which may affect the approval of the arrangement by creditors.
Details of any previous history of failures in which any of the directors have been involved in so far as they are know to the nominee.
An estimate of the result for the creditors if the VA is approved, explaining why it is more beneficial for creditors than any alternative insolvency proceeding.
The likely effect of the proposal's rejection by creditors.
Details of any claims which have come to the nominee's attention which might be capable of being pursued by a liquidator or administrator should one be appointed.
Where the following conditions have not been met (Re Greystoke v Hamilton-Smith & Others)
▪ The Company's true position as to assets and liabilities is not materially different from that which it has represented to the creditor to be
▪ The directors' proposal has a real prospect of being implemented in the way it is to be represented it will be.
▪ There is no already- manifest yet unavoidable prospective unfairness
If the nominee still recommends a meeting should be held, the reasons why he is making that recommendation and that the conditions have not been met is conspicuously brought to the attention of the court.
If not already dealt with in the proposal:
The source of any referrals to the nominee or his firm in relation to the proposed VA.
Any payments made or proposed to be made, to the source of such referrals.
Any payments made or proposed to be made to the nominee or his firm by the company whether in connection with the proposed VA or otherwise.
An estimate of the total fee to be paid to the supervisor together with a statement of the assumptions made in producing the estimate.
If the Company has in the previous 12 months put forward a proposal that has been rejected, a statement to that effect and why it is considered appropriate for the creditors to consider and vote on the new proposal.(Revised draft SIP 3 Sept 2006)

(b) Draft a comparative outcome statement, showing the estimated outcome of the proposed CVA on both a "best-case" and "worst-case" basis and also showing the estimated outcome of voluntary liquidation on both a "best-case" and "worst-case" basis. (14 marks)

Q2 - VIVID PLC

COMPARISON OF ESTIMATED OUTCOMES

	CVA Best case £	CVA Worst case £	Liquidation Best case £	Liquidation Worst case £
Assets not specifically pledged per statement of affairs				
Office equipment	0	0	5,000	5,000
Stock	0	0	15,000	15,000
R&D tax claim	260,000	0	260,000	0
Contribution to pay dividends and costs	40,000	100,000	0	0
Less costs of realisation and liquidation/CVA	-30,000	-30,000	-30,000	-20,000
Net assets available to preferential creditors	270,000	70,000	250,000	0
Preferential creditors	-20,000	-20,000	-70,000	-70,000
Surplus as regards preferential creditors	250,000	50,000	180,000	-70,000
Unsecured creditors				
Trade and expense creditors	-400,000	-400,000	-400,000	-400,000
PIT loan	0	0	-200,000	-200,000
Group creditor	-600,000	-600,000	-600,000	-600,000
	-1,000,000	-1,000,000	-1,200,000	-1,200,000
Total shortfall to unsecured creditors	-750,000	-950,000	-1,020,000	-1,270,000
Estimated dividend to preferential creditors (p in £)	100.0	100.0	100.0	0.0
Estimated cash dividend to CVA unsecured creditors (p in £)	25.0	5.0	15.0	0.0

QUESTION 3

(a) Outline the factors that the Bank would take into consideration when deciding whether to appoint, or to concur with the appointment of, an Administrator or to appoint an Administrative Receiver to the Company. (10 marks)

Appointment
The Bank can appoint a receiver in this case
The appointment of a receiver requires no prior notice to be given any person.
Company/directors' appointment -at least 5 business days notice of intention to appoint an administrator has to be given to any person entitled to appoint an administrative receiver or administrator
QFCH appointment-at least 2 business days notice of intention to appoint an administrator has to be given to a prior QFCH
Bank may to consent to directors' choice of administrator or appoint its own administrator or administrative receiver.
Moratorium
Receivership - no protection offered by a moratorium
Receivership may entitle landlord to irritate the lease
Relief against irritate on condition of payment of ongoing rent
Duties
Primary duty of receiver is to repay Bank and preferential creditors
Administrator owes duty to all creditors
Control
More difficult to remove bank appointed administrative receiver than administrator
Bank has more ability to influence administrative receivers' strategy
No requirement for receiver to report to creditors on a periodic basis
Administrator is required to seek approval to proposals from creditors
Administrator can sell business and assets subject to floating charge as if not subject to security
Secured creditor can apply to court to realise security
Period of administration only lasts 12 months without extension – consent of creditors/court required
Liability & Costs
Receiver's agency is terminated on winding up. An administrator's agency cannot be so terminated
Receiver's fees are controlled by the bank rather than the general body of creditors in the case of administration
There is a cessation of accounting period on entering administration and therefore a new tax period is created
Therefore trading losses cannot be offset against future trading profits and chargeable gains
Corporation tax arising post appointment ranks as an unsecured claim against the company in receivership but as an expense in administration.
Rates are payable as an expense of administration but not in receivership
Realisations
Directors' cooperation may not be forthcoming in receivership
Consequently book debts might be more difficult to collect without active director cooperation
Administrator can challenge antecedent transactions whereas receiver cannot
Other
Administration recognised but lack of recognition for receivership in other jurisdictions – EC Regulation
Potential adverse publicity associated with receivership compared to administration as part of the rescue culture

(b) Outline the steps that the board of directors should take to protect the interests of creditors generally, pending the appointment of an insolvency office-holder. Indicate the consequences that the directors may face if they do not take those steps. (10 marks)

Steps the directors should take
Since the Company is insolvent the directors' principal duty is to the Company's creditors.
The position of creditors whose debts have already been incurred should not be prejudiced in any way.
Any liabilities accruing due to creditors as a result of allowing the Company to continue to operate should be paid in full when due.
The value of the Company's assets must therefore be preserved
No assets should be disposed of below their market value. Therefore any disposal contemplated outside the ordinary course of business should be on the basis of professional advice.
Trading losses must be stemmed/eradicated since losses reduce available net assets.
Therefore any short term contemplated trading must be supported by a detailed cash flow and profit and loss account.
No payments should be made to exiting creditors.
This is to ensure that the pari passu principle, i.e. the equality of creditors as between themselves, is preserved
It also ensures that the assets of the Company available to pay creditor claims are maintained intact.
It will however be justifiable to pay an existing creditor if absolutely necessary for protecting the value of the business and assets and therefore the interests of the creditors as a whole.
If in doubt take professional advice.
All material decisions affecting the Companies assets, liabilities and continued trading should be adequately documented in the event of a challenge at a later date.
Consequences for directors of not taking those steps
A director who fails to take steps with a view to minimising the potential loss to creditors may be sued for wrongful trading by the liquidator if the Company goes into insolvent liquidation.
If the court finds for the liquidator the director can be made liable to make such contribution to the company's assets as the court thinks proper.
The level of that contribution is likely to reflect the addition losses sustained by creditors as a consequence of the director's failure. The court's jurisdiction is primarily compensatory rather than penal.
Failure to take steps to minimise the loss to creditors could lead to a finding that the conduct of a director of a company which has become insolvent makes him unfit to be involved in the management of a company
A disqualification order or undertaking has the effect that for a specified period the director shall not be a director, a receiver or be concerned in the promotion formation or management of a company without the leave of the court, nor act as an insolvency practitioner. The period specified may be between 2 and 15 years.
Where, in the course of a winding up, it can be shown that trading has continued with intent to defraud creditors or for any fraudulent purpose, any persons who were knowingly parties can be made liable to make such contribution to the company's assets as the court thinks proper.
A finding of fraudulent trading can also lead to criminal prosecution entailing fines and custodial sentences.
Where an asset is disposed of for less than its market value, a subsequently appointed administrator or liquidator may seek to recover the amount of undervalue transaction from the transferee.
In such a case of a transaction at an undervalue the directors responsible may, if the company is wound up, also be liable in misfeasance proceedings with liability to account or contribute to the assets of the company
This is particularly so where the transaction was with a person connected with the company – i.e. a director or an associate of a director.
Where a payment is made to an existing creditor without proper justification, a subsequently appointed administrator or liquidator may challenge the payment on the grounds that it was a preference – that there was a desire to put the creditor into a better position than they would have been on a winding up. The desire to prefer is assumed if the creditor was a person connected with the company.
In such a case of a preference the directors may, if the company is wound up, also be liable in misfeasance proceedings with liability to account or contribute to the assets of the company.
This is particularly so where the preference was given to a person connected with the company – i.e. a director or an associate of a director.

(c) Set out the procedural steps required to effect the appointment of an Administrator by the directors in the present circumstances. (10 marks)

Out of court appointment by the company or directors under paragraph 22 may not be made where a petition for winding up the company has been presented and has not yet been disposed of.
Therefore an application to the court under paragraph 12 for an administration order is the only route available to the company or directors
Pre-conditions to appointment of administrator are met, namely the company must not already be in administration, administrative receivership or liquidation nor has a provisional liquidator been appointed.
Application for administration order prepared which should state:
Name of company and address for service
Name and address of person(s) proposed as administrator(S)
An address for service
Consent to act from proposed administrator should be attached and should state
Details of any prior professional relationship he has had with the company
That in his opinion it is reasonably likely that the purpose of administration will be achieved
Note in support of the petition is prepared to contain the following information
A statement of the company's financial position
Specifying to the best of the applicant's knowledge and belief the company's assets and liabilities including contingent and prospective details of any security known or believed to be held by the company's creditors
Whether the secured creditor has power to appoint a receiver
Any maters which in the opinion of those intending to make the application for the order will assist the court in deciding to make such an order so far as lying within the knowledge or belief of the applicant
Whether in the opinion of the petitioner making the application, the EC Regulation will apply and if so whether the proceedings will be main or territorial proceedings
File application and supporting documents in court with sufficient number of copies for service
The court seals each copy of the application with date and time of filing and venue for the hearing and issues back to applicant sufficient copies for service.
An interim moratorium takes effect.
Notice of the petition to ber served by the applicant,, as soon as reasonably practicable
Any person who is or may be entitled to appoint an [administrative – this is the wording in the Scottish Rules]receiver of the company
Any such persons as may be prescribed
The proposed administrator
The company
Details of service and copy of application to be filed with court as soon as reasonably practicable [and not less than one day before the hearing- Roy is this right?]
Court hears the administration application
The directors as petitioners can appear or be represented
Court can make administration order only if satisfied that the company is or is likely to become unable to pay its debts and that the administration order is reasonably likely to achieve the purpose of administration.
Court issues sufficient sealed copies of the appointment to the applicant who sends one copy to the administrator as soon as reasonably practicable.

QUESTION 4

(a) Set out the factors that you should take into account when deciding whether or not to allow the Company to continue trading. (10 marks)

Confirmation obtained as to validity of appointment and capacity to deal with assets crucial to trading
Independent valuation of moveable assets shows a significantly higher value on a "going concern" basis compared to a "forced sale" basis.
Evidence of a reasonable prospect of realising value for goodwill, intellectual property rights or other intangible assets.
The likelihood of achieving a going concern sale of the business and assets.
A better prospect of maximising the value of book debts and/or work-in-progress
The ability to mitigate liabilities
The level of forecast profit/loss from continued trading
The level of funding required to support trading evidenced by a detailed cash flow forecast. The availability and cost of funding post-appointment trading
The level of employee actual and contingent claims and the impact of TUPER on a sale of business.
The impact of ROT
Ransom payments to suppliers/hauliers
Attitude of major customers
The terms on which existing customers are willing to transact including no set off
Credit-worthiness of customers to pay
The availability of raw materials/other inputs and the attitude of major suppliers
Evaluate environmental risks impacting on trading
Evaluate health and safety risks impacting on trading
Evaluate risks of claims arising by way of damages as a result of continued trading e.g. from arising out of product failures
The adequacy and attitude of the employees/labour force
Legal position re any necessary licenses
Adequacy of controls over trading
If leasehold property, the rent position and the ability to negotiate terms with the landlord
Where a factoring company is involved, confirmation that post-appointment sales will not form part of their security.
Confirmation that the directors support the decision for post-appointment trading
No significant production/process problems likely to affect production standards/quality
Obtain any necessary internal approval to trade e.g. following second/regional managing partner review.

(b) Outline the practical measures and controls that you should implement in order to manage post-appointment trading. (10 marks)

Purchases/payments
Establish new purchase order numbering system to distinguish receivership purchases from pre-appointment purchases
Review unexecuted purchase orders to determine whether the goods/services are still required. Cancel existing PO and replace with receivers' PO.
Review supplier terms and conditions
Receivers' PO to be countersigned by senior member of receivers' staff authorised for that purpose.
All goods inwards received after appointment to be verified against receivers' order prior to being accepted.
Ensure that purchasing system enables administrator PO to be matched to delivery note and invoice before payment is made.
All supplier payments to be approved by senior member of receivers' staff supported by PO, DN and invoice.
Overtime working to be approved in advance by receiver
Company credit cards/fuel cards and the like reviewed and either withdrawn or appropriate limits agreed.
Payroll to be scrutinised and authorised for payment.
Post-appointment trading performance to be reviewed in detail against forecasts at least weekly and any material variances investigated.
Take meter readings in respect of utility supplies at all locations as soon as possible.
Arrange a stock take as close to appointment as possible. Identify any potential ROT stocks and obsolete and slow moving stocks.
Establish any goods in transit

Sales/receipts
Establish new goods outwards record to distinguish goods supplied during administration. No goods to be despatched until proper cut-off established.
No goods to be despatched with external hauliers owed money until written confirmation received from them that they will not exercise a lien over goods.
Customers confirm that they will pay post appointment invoices without deduction, counterclaim or set off of any kind.
Review credit limits with customers
Analyse cheques received between pre- and post-appointment sales. Bank cheques daily/promptly
Review costing system/pricing policy if appropriate.
General
Ensure proper cut off of all pre-appointment accounting records
Review key holders and general security arrangements
Establish control over all incoming mail faxes and documents
Establish control over all outgoing mail, email, faxes and documents. Ensure statutory publicity requirements complied with – name of administrator and that the affairs, business and property are being managed by him.
All outgoing documents to state that receiver contracts as agent of the company without personal liability.
Ditto re Company website.
Arrange adequate insurance cover for the additional risks associated with continued trading – employee liability, fidelity, fire, theft, accidental damage and product liability. Consider terrorism damage.
Count petty cash and establish an imprest system.
Perform regular/weekly reconciliation of receivership cash book and bank statements

(c) Outline the steps that you should take to market the business and assets for sale. (5 marks)

Consult with the directors to the identity of the persons amongst the Company's competitors, customers or suppliers most likely to be interested in acquiring the business and assets.
Establish whether the existing management team is interested and if so how they propose to raise the necessary finance.
Review trade magazines, business directories and the financial press to add to the list of potential purchasers.
Consider engaging specialist corporate finance advisers to identify potential buyers. They will have access to databases of potential buyers as well as an extensive network of contacts.
Consider advertising the business and assets for sale in a publication appropriate to the business in question; specialist trade magazines and the Financial Times are frequently used.
Prepare a sales memorandum/ brochure containing essential information about the business and the nature of the assets for sale in order to spark interest on the part of potential purchasers. You should not at this stage disclose confidential information such as names of customers and pricing structure.
Send the sales memorandum to the list of potential purchasers inviting them to register their further interest with the receivers' office. Retain contact details
Maintain a schedule of contact details of all those parties expressing further interest.
Arrange for those expressing further interest to visit the principal trading site(s). Ensure adequate supervision of those visits.
Prepare a confidentiality/non-disclosure agreement whereby prospective purchasers undertake not to use or pass on any confidential information they are given about the Company or its business.
Provide further detailed information as requested to those interested parties willing to sign a confidentiality undertaking.
Set a deadline for the receipt of offers in order to draw matters to a conclusion.
Instruct solicitors to prepare a draft contract of sale.

(d) When instructing lawyers to prepare the contract for the sale of the business and assets, outline and explain the particular terms that you would expect them to incorporate into the contract, recognising this is a sale by an Administrative Receiver as opposed to a sale by a solvent company. (5 marks)

In addition to the Company (as Vendor) and the Purchaser, the receiver is also made a party to the transaction.
The Purchaser agrees to purchase such right, title and interest as the Vendor may have in the business and assets subject to the agreement.
Any failure by the Vendor to pass along any title, right or interest to or in any of the assets shall not be a ground enabling the Purchaser to rescind or treat the Vendor as in breach of the agreement or to claim a reduction of the price.
All sums payable under the agreement are to be paid to the receiver or their named solicitors.
All warranties as to title, merchantable quality, fitness for purpose and condition are expressly excluded.
Any provision for the Purchaser to indemnify the Vendor will also be extended to the receiver.
The Purchaser acknowledges that the terms and conditions are fair and reasonable in the context of a sale by a company in receivership and that the commercial risk to the Purchaser of such is reflected in the price, which would have been much higher on any other basis.
The Purchaser acknowledges that it places no reliance whatsoever on any representations by the receivers, their staff or their solicitors
The Purchaser acknowledges that it has relied entirely on its own inspection and enquiry as regards the assets to be transferred.
The receivers are given access to the business premises on reasonable notice and at reasonable times in order to complete the receivership.
The business records of the vendor will be available for inspection by the receiver whilst the receiver is in office in respect of the vendor.
The receivers are acting only as agents for the Vendor and without personal liability on their part.
Signed by named receivers(s) on behalf of the Vendor. Also signed by named receiver as receiver on behalf of joint appointee (unless the joint receiver also signs personally).
No title guarantee given in respect of business premises

LIQUIDATIONS (SCOTLAND) DECEMBER 2007

EXAMINER'S REPORT

General Comments

General presentation was fairly good and the quality of writing and presentation was much improved from past years

Candidates generally kept to the specifics of the question. The level of digression from the question asked was substantially less than previously seen. This may be due to the questions being set in a more sectional manner but thelevel of improvement generally reflects on the candidates addressing and recognising the technical specifics of the question. Candidates must not ignore the obvious simple answer. The questions are not set to trick, but to examine basic understanding of matters involved in aspects of the liquidation process. The examiner cannot allocate marks on a presumption that because a candidate ignores the very basic points and answers the more complex that the candidate actually knows the basics. Candidates also need to look at the number of marks available in each section of a question and appreciate that they require to provide a full enough answer to obtain marks in line with the available marks.

QUESTION 1

The question posed a range of unrelated problems that an IP may face. The question tested candidates' familiarity with a number of issues arising in separate cases.
Part (a) which dealt with an insolvent members' voluntary liquidation and the issues which arose as a result of that discovery. The question was generally well answered.
Part (b) dealing with double proofs was generally well answered and candidates did pick up the main issues involved.
The answer to part c was mixed with some candidates' failing to recognise the potential alienation of the assets at a low value.
Part (d) was varied with some candidates failing to attempt any answer. The majority of the candidates appreciated the basics and saw the potential of appointing a provisional liquidator to protect the position.

QUESTION 2

The main part of the question was to address the organisational aspects of case progression and delegation and then look at the steps which were required to close a case.

The answers to this question were of a high standard and candidates clearly demonstrated a firm grasp of basics. Closure of cases is an area where historically candidates have shown a lack of practical experience, presumably due to the use of "closure departments" in some firms. The depth of some of the candidate's answers clearly indicated that previous comments in this area have been fully addressed and that there has been practical exposure to this important area of practice.

The final part of the question which looked at a potential claim was not well answered. The issue of asbestos and contaminated land is one which is becoming more problematic and candidates should be aware of the actions which they require to take to protect both themselves and also the estate with which they are dealing.

QUESTION 3

The thrust of this question was to have the candidate address and identify potential solutions to a variety of issues arising in a liquidation.

Answers were variable depending on how the candidate identified the issues involved in each part of the question. No particular deficiencies were noted during the marking process though candidates do need to ensure that they do answer the question asked which in this case was to consider advantage and disadvantage of certain actions and to give reasons for those views.

QUESTION 4

The question was divided into three distinct parts.

The first part asked candidates to state the main purpose of a creditors' voluntary liquidation, and to set out the factors when deciding whether to commence an investigation. The answers were somewhat mixed and many candidates appeared to place a greater importance on the availability of funds to carry out an investigation rather than address the requirements as set out in SIP2.

The second part asked the candidate to consider information which had become available on the liquidation of a parent and subsidiary. This part of the question was particularly well answered by some candidates and issues were addressed in a logical manner.

The third and final part asked candidates to consider the matters, in addition to the legislation, which a Liquidator is required to report under the Directors' Disqualification Act 1986 and to address matters which may hinder reporting. SIP 4 was the key to this question and where candidates found that connection they scored well. A number of candidates appeared to miss the point of this section of the question but this may have been due to time constraints rather than lack of knowledge.

LIQUIDATIONS DECEMBER 2007

Exam Marking Plan

The marking plan set out below was that used to mark this question. Markers were encouraged to use discretion and to award partial marks where a point was either not explained fully or made by implication. More marks were available than could be awarded for each requirement. This allowed credit to be given for a variety of valid points which were made by candidates.

QUESTION 1

(a) Set out the immediate steps that you, as Liquidator, should take. Set out the consequences for the Liquidator. (4 marks)

Practical steps
Verify claim. – Do directors' accept validity of claim? How was it omitted from the declaration of assets and liabilities? Do directors have reasons for omission?
Discuss with directors.
Was there an indemnity from the parent – is the indemnifier prepared to make up the deficit? Discussion.
The declaration of solvency will have been signed by the directors (or if over two directors the majority) (IA 1986 s89 (1)) and that it is an offence to make a declaration without having reasonable grounds for the opinion that the company will be able to pay its debts in full, together with interest at the official rate, with the period specified and the directors are liable to imprisonment or a fine, or both. (IA 1986 s89(4)).
If claim is correct, the directors may wish to mitigate the risks which could arise and it may be possible that they directors will agree to pay some/all of the shortfall.
Legal steps
If correct and the company is unable to pay its debts and the interest (IA 1986 s189)on them [within the time stated] in the Declaration of Solvency (IA 1986 s89) (max one year), the liquidator must call a creditors' meeting within 28 days (IA 1986 s95(2)(a))
Creditors must be given 7 days notice of the meeting (IA 1986 s95(2)(b))
Notice of the meeting must be advertised in Edinburgh Gazette and two local newspapers in which the company's principal place of business was situated in the 6 months before the start of the liquidation (s95(2)(c).
Before the creditors' meeting the liquidator has to provide creditors free of charge with such information concerning the company's affairs as they may reasonably require (IA 1986 s95(2)(d)) and this duty must be stated in the notice to the meeting.(IA 1986 s95(2))
At the meeting, the liquidator must act as chairman (IA 1986 s95(3)(c)
Prepare and present to the meeting a statement of affairs on Form 4.18 (IA 1986 s 95(3)(a), (b) and IA Rules 1986 Sch 4). The statement of affairs must be at the date that the liquidator formed his opinion that the company would not be able to pays its debts in full within the period stated in the declaration of solvency.
With effect from the date of the creditors' meeting, the liquidation will be a CVL ((IA 1986 s96(a))
The creditors' meeting will be treated as though it were the first meeting of creditors convened in a CVL (IA 1986 s96(b)) and so it will be able to appoint a liquidator in place of the members' appointee (IA 1986 s100(2)) and appoint a liquidation committee (IA 1986 s101(1))
Consequences for liquidator
The replacement of the liquidator by the creditors appears to be a removal by a general meeting of creditors for the purposes of IA 1986 s173 and, unless the creditors have voted against it, he will obtain his release when notice that he has vacated office is given to the Registrar of Companies (IA 1986 s173(2)). If the creditors vote against his release he will need to apply to the Secretary of State (IA 1986 s173(2)(b).
The MVL liquidator will not be able to take appointment as CVL liquidator if he was auditor, but also even if he was not auditor he will be conflicted from taking appointment as CVL liquidator, as the advice that he gave the company when entering into MVL will need to be investigated.
If there were no reasonable grounds for signing the declaration of solvency, the creditors' liquidator will have a duty to report the circumstances of the liquidation to the DTI under the reporting provisions of the CDDA 1986 and so disqualification proceedings may also follow.

(b) Reply to the solicitor's letter explaining, with reasons, whether or not the solicitor's proposition is correct. (4 marks)

Answer in form of letter to Bob from liquidator.
Rule against double proof is a common law principle that there cannot be two proofs in respect of the same debt.
A guarantor cannot prove in the liquidation, as a contingent creditor or otherwise, unless the principal debtor has not or is no longer entitled to prove (e.g. because the guarantor has paid him in full). Until that happens, no right of subrogation arises.
See Re Fitness Centre Ltd [1986] B.C.L.C. at 521, per Hoffmann J.
The test to be applied when deciding whether or not the rule against double proof applies is a broad one, and is simply whether the two competing claims are in substance claims for payment of the same debt twice over. It is necessary to look at the substance of the transactions which have given rise to the potential application of the rule to determine which claimant has the better right. Barclays Bank Ltd v TOSG Trust Fund Ltd [1984] A.C. 626, applying Oriental Commercial Bank, Re (1871) L.R. 7 Ch. App. 99
As a general proposition, the rule against double proof is going to apply wherever the existence of one liability is dependent upon and referable only to the other liability. To allow both liabilities to rank independently for dividends would produce injustice to the other creditors. The rule is designed to prevent a distortion of the pari passu principle, which would occur if both proofs were admitted in full.
If Bob does not accept the Liquidator's explanation of the legal position and wishes to continue with his claim then, subject to further evidence or explanations which Bob may wish to submit, within say 10 days, the liquidation will have no alternative but to formally reject the proof (he must prepare a written statement of his reasons and send it to the claimant whose proof has been rejected. B(S)A S49(4).
In these circumstances, if Bob is dissatisfied with the liquidator's decision he may apply to the court for it to be reversed or varied within 2 weeks of the rejection.
B(S)A S49(6)

(c) Set out the issues to be considered and the remedies that are available to the Liquidator. (4 marks)

Carroty Ltd
The main issue for the Liquidator to consider is the sale of the business so soon before the CVL:
Discussion required, including:

- Was the consideration at market value?
- Was the deal structure intended to leave some creditors (HMRC and landlord) behind? Or was this unavoidable because of the requirements/demands of the purchaser?
- Could the directors have achieved a better deal?
- Did the directors treat all creditors fairly and equally in proportion to their claims?

If the assets were not sold for the market price (and the liquidator should take steps to ascertain whether or not this was the case) – there may be a remedy for a transaction at a gratuitous alienation (IA 1986 s 242). Note a preference may also be an alienation.
Note for marker: The strict legal effect of a purchaser taking over some liabilities and not others is the same as if the vendor company has received the amounts of the liabilities taken over as part of the consideration and had itself then paid off those liabilities from those amounts to the creditors taken over. The short circuiting of the mechanics of payment as in the scenario did not have the effect of taking the transactions out of the preference position.
If the assets were not sold at a market price the liquidator may also have an action against the directors for misfeasance (IA 1986 s212)
If the business and assets were sold at market price – there will have been no alienation or misfeasance. Did company become insolvent as a result of the transaction or was it already insolvent? Was the value correct?
In this case, there may be a possible action for preference (IA 1986 s243) but the directors could argue that the deal was imposed upon them by the purchaser (i.e. commercial pressure) and they were not desiring to prefer any particular creditors.
May be a claim against the directors for fraud.

(d) Advise Hubert on the immediate actions that Smog can take to prevent Mistier's assets from further dissipation and the procedures involved. Explain the risks to Smog of taking immediate action. (8 marks)

Petition for winding up order (IA 1986 s124) – on grounds either that the company is unable to pay its debts (s123(1)(e)) (note - there is no mention in the question that a demand was made for the arrears).
Petition must be advertised.
On hearing the petition the court can make .."any order it thinks fit." (s125)
Apply to court for a provisional liquidator in order to protect the assets/records in the company's possession or under its control, s135
An application for a provisional liquidator can be made at any time between the presentation of the petition and the making of a winding up order (s135(1)).
The applicant must normally show:

- why the appointment should be made (that otherwise the company's assets would be dissipated in this case)
- who is proposed as provisional liquidator
- that the person proposed consents and is a qualified insolvency practitioner
-
- whether a scheme of arrangement has been proposed or is in force
- whether an administrator or administrative receiver is acting
- whether a liquidator has been appointed for the company's voluntary winding up
- the estimated value of the assets over which the prov liq will be appointed

The Creditor, as creditor or as petitioner, may apply for the appointment.(R4.1(1)).
- the court order appointing the liquidator will specify the functions he is to carry out
Adequate security needs to be provided to support the appointment (R4.1(2)
The provisional liquidator must be an insolvency practitioner and is an officer of the court
If necessary, a provisional liquidator can appoint a special manager
Other remedies (non-insolvency):
- freezing order
- seize and search
- order in relation to property (preservation or sale)
- order to deliver up goods

Risks to creditor
Cost/benefits
- a licensed insolvency practitioner will be appointed
- court may not make an appointment if it considers that there are insufficient reasons for taking control of the company's affairs away from the directors before making the winding up order.
Maybe better to talk to insolvency practitioner before application to explain Creditors/applicant's position.
- costs:
- need to consider whether there are sufficient assets to recover, after costs of provisional liquidation.
The remuneration of the provisional liquidator is set by the court (R4.5)
In many practical situations the provisional liquidator may waive a fee if there are no assets
Or restrict his fee if the assets are limited
Provisional liquidation may cause business to close
May not get money back there may be a quicker way to settle the dispute.

QUESTION 2

(i) State the problems that are caused by the backlog of insolvency cases, using the above scenarios as mere general examples. In relation to delegation and control of cases handled by the insolvency practitioner firm, state the main points that are recommended to be addressed in the published guidance. (6 marks)

(20 marks)

Guidance on procedures for delegation and control of cases may be found in the Insolvency Guidance Paper – Control of Cases

Delegation

Note this is a small firm and the requirements to delegate work needs to be considered accordingly.

Delegation can take on a number of forms, including:

delegation of work to staff in the practitioner's own office, or to subcontractors;

delegation of work to staff within a firm but in another location;

taking a reduced role on an appointment taken jointly with an Insolvency Practitioner in the practitioner's office;

taking a reduced role on an appointment taken jointly with an Insolvency Practitioner within the same firm but in another location;

allowing a specialist Insolvency Practitioner within a firm to take responsibility for all work of a specific type;

allowing a specialist within a firm to handle work of a specific type (e.g. tax);

sharing work on an agreed basis on an appointment taken jointly with a practitioner from another firm;

employing another firm to give specialist advice (e.g. tax), or to undertake specific work (e.g. an investigation); and

allowing a practitioner in a former firm (following either the practitioner's move to another firm or retirement) to take responsibility for appointments for a short time pending the transfer of cases.

For each of the above examples (and in other circumstances where delegation takes place), the practitioner must be satisfied at all times

that work is being carried out in a proper and efficient manner, appropriate to the case.

Control

In determining the procedures to be put in place to ensure that an appropriate level of control can be established in relation to delegated work,

it is recommended that a practitioner have regard to the following matters:

the structure within a firm, and the qualifications and experience of staff;

the need for the practitioner to be involved in setting case strategy at the outset, depending on the nature, size and complexity of the case;

the procedures within a firm to ensure consultation by joint appointees, other practitioners, and staff;

the extent to which levels of responsibility are defined, and the circumstances in which a reference to, or approval by, the practitioner is required;

whether there are clear guidelines within a firm to deal with the administration of cases at locations remote from the practitioner;

the ways in which compliance and case progress are monitored, and then reported to the practitioner;

the frequency of case reviews, and who carries them out;

the systems for dealing with correspondence received and, in particular, complaints;

the process by which work is allocated on a joint appointment with a practitioner from another firm, the rationale for that split, and the controls to be put in place, subject always to statutory requirements; and

the way in which specialist advisers (including agents and solicitors) and sub-contractors are chosen and engaged, and how their work is monitored.

Insolvency Practitioners are aware that they may be required to justify their decisions and demonstrate that appropriate levels of control

have been established. It is recommended that for firm wide procedures, guidance is set out in writing, and that on a case by case basis,

contemporaneous working papers or file notes are prepared.

Illustrate/discuss answer by referring to scenarios in the question – including:

- Was Joe sufficiently briefed?
- There is no evidence of case strategy and of how staff were briefed when taking over the files (especially as there seems to be a high staff turnover)
- How experienced was the staff?
- Were there enough staff?
- Should the joint appointee have had more involvement in the case with the lead partner?

ii. Set out the practical, legal and regulatory steps that need to be taken to close Platus Ltd. (11 marks)

Needs to **declare and pay dividend**.
The liquidator has a duty to declare and distribute dividends when sufficient funds are available, subject to the retention of such sums as are necessary for the expense of the winding up.
Prepare a projection account showing how it is proposed to distribute the available funds, making such reserves as are appropriate and necessary.
Ensure that full provision is made for the expenses of the winding up.
Before paying a dividend to creditors of any class, ensure that all creditors of prior classes have been paid or provided for in full.
Before paying any dividend, the liquidator must provide for:-

- Any debts due to persons who might not have had sufficient time to tender and establish their proofs.
- Any debts, which are the subject to, claims which have not yet been determined.
- Any disputed proofs and claims.

Where any assets remain unrealised at the time of a dividend payment, ensure that the above calculations take into account future potential costs that might arise in making the further realisations.
If not already done, advertise for claims before any distribution being made. Rarely done by public advert, normally by circular.
Always record circulars by way of certificate of postage, showing whom the circular was sent to.
Make formal adjudication of claims and,
Advise creditor of right of appeal to court. To be made within 2 weeks of adjudication.
Where a creditor assigns his debt, he must first give notice of this assignment to the liquidator, who must then pay the dividend to the assignee.
Where a proof is altered after the payment of a dividend the creditor is not allowed to disturb the distribution but is entitled to be paid, out of any money for the time being available for the payment of any further dividend, any dividend(s) which he has failed to receive. In this instance the dividend will be a “first and final”.
Where a proof has been received from secured or partly secured creditor, seek confirmation before any distribution is made whether or not the creditor wishes to
revalue that security.

Payment of dividend

When paying the dividend:
Many IP’s request a signed receipt from the creditor prior to sending the dividend cheque. If that method is used file the receipts in the sederunt book.
If no receipt is requested retain a copy of the cheque and the accompanying letter in the sederunt book thus evidencing the payee.
Maintain a bank reconciliation showing the clearance of the payments.
Consign any unclaimed dividends, uncashed cheques or cheques returned marked “gone away”, to Royal Bank of Scotland with details being sent to Accountant in Bankruptcy.
- two employees cheques not cleared. If not cleared within 6 months, the Liquidator may take some steps to ascertain their whereabouts. One course of action is to use the Department of Work and Pensions forwarding service – as long as you know the employees’ NI numbers.

Closing

Take steps to deal with the remaining funds and ensure all bank accounts are closed.
Obtain confirmation from agents and advisors that there are no outstanding matters.
If appropriate, call a final meeting of the liquidation committee
Once the company’s affairs have been fully wound up the liquidator must call general meeting of company and meeting of creditors and lay a final account before them, 28 days’ notice is required. (s106)
Advertise meetings in the Edinburgh Gazette at least one month before. IA 106(2)
The report shall contain a statement as to the amount paid to unsecured creditors by virtue of application of s176A
Note quora need not be present, unless resolutions are to be passed. S106(5)

Within one week following the meeting, send to the Registrar of Companies: A copy of the final report and a return of the holding of the final meetings or a statement that the meetings were duly summoned but at one or both of them no quorum was present. S106(3), S106(5)
Prepare final report. This should include a summary R & P, narrative description regarding asset realisations and costs, appropriate SIP 9 disclosure. S106(1)
Send final report, final meeting notices, proxy forms, receipts and payments account and authority forms, together with any Notice of Dividend, to creditors and members.
Send copies of final report, final receipts and payments account etc to directors, liquidator's agents, solicitors, bankers and guarantors for information.
Obtain consent to chair meeting if necessary. IA 106, R 4.56
Take minutes of final creditors' meeting. IA 106
Place copy of Minute in sederunt book.
Within one week following the meeting, send to the Registrar of Companies: A copy of the final report and a return of the holding of the final meetings or a statement that the meetings were duly summoned but at one or both of them no quorum was present. S106(3), 106(5), Form 4.17
The liquidator obtains his release when he vacates office by filing the returns of the final meeting with the Registrar (provided the creditors have not resolved against his release). S171(6)(b), S173(2)(e)
Close estate accounts
Withdraw name from any display at Jones & Smith registered office on dissolution (3 month after final meeting).
Advise bordereau provider of termination of case.

(b)
iii. Set out the issues Joe should consider on the basis of this information (3 marks)

Possible asbestos claims

The Liquidator has not been advised of any formal claim and is incapable of valuing the potential claim. A protective action could be taken by a potentially affected creditor or a body representing creditors. The question is whether any party has yet suffered any damage and does not therefore, at that time, have a cause of action against the company.

This gives the Liquidators practical problems – should, and how much, funds should be reserved to distribute for claimants who have not yet suffered any damage?

A possible course of action is to take expert advice on the likelihood of the factory's asbestos harming the former employees and making an assessment of the amount of damages that may arise.

The Liquidators could keep the case open and wait for claims or could set up a trust fund for future claimants?

The court has power to fix exclude creditors not proving in time – s153. Presumably the court will wish to be fair to all creditors.

Also Liquidator can seek court directions – s112.

See Turner & Newell case.

QUESTION 3

For each of the issues, i to vii, which have arisen after your appointment, state the legal and practical steps that you, as Liquidator could take. If there is more than one possible course of action, explain the advantages and disadvantages of each option and state, with reasons, which option you prefer.

(30 marks)

i. Flexible package patent

Main issue is whether or not to abandon the interest in the patent and associated licence agreement or whether to spend more funds and sell the patent.

There may be a funding issue – consider whether deal could be done to sell the patent to the licence holder.

Is there a value in the patent which may be realisable from another party? May need to seek advice from a patent agent.

The terms of the licensing agreement need to be examined to ascertain whether insolvency is covered and also whether there are any rights attaching in the event of failure to maintain the terms of the licence.

A liquidator should ensure that he is not seen as personally adopting the licensing agreement albeit he has taken possession of it, endeavoured to sell it, or otherwise exercised rights of ownership in relation to it.

Stripey could be in breach if they fail to pay licence fees.

There is an issue as to whether monies due under the terms of the licensing agreement can be offset against losses incurred due to the product failure.

There is an attraction in trying to sell the patent to Stripey as this would protect the liquidator from funding any further development and also issues relating to breach of the licensing agreement. Stripey would clearly consider those matters when considering its offer for the patent.

Stripey Limited, if they fail to acquire the rights and should the agreement be terminated can prove in the liquidation for the amount of loss suffered by them as a result of the insolvency.

ii. Payments out of bank account

The commencement of the liquidation is the date of the petition.

IA 1986 s127 states that in a winding up by the court, any disposition of the company's property made after the commencement of the winding up is void unless the court orders otherwise.

To have validation there must be value given and received. (Re Grey's Inn Construction Co Ltd [1980] 1 WLR 711 – where the company is insolvent the main purpose of s127 is to ensure all creditors are paid pari passu),

A transaction is likely to be validated if the assets company have not been depleted by the transactions, for example if continued trading has resulted in no loss to the creditors,

A transaction is not likely to be validated if there has been some preference – eg if there was a guarantor.

A transaction which has depleted the assets will not be validated.

Re Grey's Inn Construction Co Ltd [1980] 1 WLR 711 – it made no difference whether the bank account was overdrawn or in credit for a disposition to have occurred. Although this has since been criticised for being too wide.

These funds cannot be recovered from the bank.

Bank of Ireland v Hollicourt (Contractors) Ltd [2001] 1 WLR 906 – The Court of Appeal held that payments made by cheque out of a company's bank account to a third party involve no disposition of the company's property to the bank – which just acts as the company's agent in making a disposition in favour of the third party – and that this is so whether the account is in credit or overdrawn.

If there has been a disposition, the liquidator needs to look to the suppliers.

iii. Employment of staff

Court winding up acts to automatically terminate employment (Re Reid v Explosives Co Ltd (1887) and re Measures Bros (1910))

But if the Liquidator wishes to continue the business of the company and employ certain employees for this purpose, the notice of dismissal constituted by the winding up order can be waived in which case the employee's employment continues under his existing contract (Re English Joint Stock Bank Ex p. Harding (1867) L.R. 3 Eq. 341)

If the Liquidator is not trading but wishes to retain some employees, their employment contracts will have been broken. McEwan v Upper Clyde Shipbuilders Ltd (1972) 7 I.T.R. 296; Day v Tait (1900) 8 S.I.T. 40; Golding and Howard v Fire Auto and Marine Insurance Co [1968] I.T.R. 372

Liquidator can pay employees and the Secretary of State normally treats the redundancy as occurring at the time of the eventual dismissal by the Liquidator

For the avoidance of doubt, if employment continued should be in name of company to ensure that there is no doubt that the subsequent redundancy costs are costs of the liquidation.
Liquidator should write to employees informing them that it is the company in Liquidation that is employing them.
TUPE Regs SI2006/246 - applies to Liquidator selling business and not to Liquidator (in any case continued employment is unlikely to be regarded as a transfer because a court winding up will be a relevant insolvency proceedings opened with a view to Liquidation of the assets).
Liquidator will need to pay the arrears of the staff he is keeping on (as an expense of the Liquidation), otherwise they probably won't agree to work for him).

Claims for unpaid stocks (iv, v, vi)

iv. Linear Ltd

Generally for ROT:
Need to ascertain if there is a valid retention of title clause and, if there is, do the circumstances of this claim comply with it.
Need to obtain a copy of the terms and conditions of trade, a copy of the Company's acceptance of those terms and details of the balance due.
If the Company has accepted the terms, the Liquidator needs to ascertain the precise nature of the conditions.
The clause may be
"simple" – reserving the supplier's title to particular goods until they are paid for or
"extended to secure the price of all goods supplied, or all monies due, or it may expressly claim the proceeds of sale or manufacture of the goods supplied or
It may do both.
- any dispute will turn on the precise conditions agreed. Welsh Development Agency v Export Finance Co [1992] BCLB 148 – the court held that it had to examine the agreement as a whole to determine if it was a sale of goods, charge or mortgage.
Generally, claims to recover the goods supplied will often succeed, but claims to proceeds or products can usually be resisted.
The Liquidator should beware that he may face claims that he is personally liable if he resists the suppliers' valid claims.
The supplier must establish that the retention clause is part of his contract with the Company.
- the clause may be resisted if it has not been agreed by both sides
- the timing of the clause is also important – if the invoices are endorsed with the clause, this will be ineffective in relation to contracts already raised but may be effective for subsequent invoices.
The status of an extended retention of title clause securing payment for all goods supplied or of all moneys owing is not settled.
The Sale of Goods Act does not restrict ROT conditions but it also does "not apply to a transaction in the form of a contract of sale which is intended to operate by way of mortgage, pledge, transaction in the form of a contract of sale which is intended to operate by way of mortgage, pledge, charge or other security."
- the clause must retain the full legal title to the supplier (Re Bond Worth [1980] Ch 228).
- retention clauses on stock confer authority on the buyer to resell the goods in the ordinary course of business, expressly or by implication.
The onus will be on the supplier to establish the amount of the buyer's debt, in the case of an "all goods" or "all monies due" clause this will be similar to the amount of the buyer's debt. A simple retention clause may be more difficult and, unless there is a running account (when the rule in Clayton's Case may be used) it will be necessary to establish the extent to which the supplier accepted particular payments as discharging particular debts.
- it may not be commercially expedient to pursue the case, so need to look at the amount of what is disputed compared to the costs.
An effective "all monies clause" can be created – Armour v Thyssen Edelstahlwerke AG [1990] All ER 481)
If there is a valid ROT clause:
Can outstanding amounts be traced to invoices? (may need to carry out Clayton's Case type exercise. It may also depend upon how good the Company's accounting records are.
Can invoices be traced to the specific goods. This may depend upon how the goods are identified – eg are batches of chemicals identified by serial numbers and are these numbers on the invoices?

v. Wavier Ltd

- **Mixed goods -** if the goods supplied have been mixed with goods from other sources (as in this case), it may be that the Company has "disposed" of his own stock first.

- generally, where the purchaser mixes the supplier's goods with others to form a composite amalgam in which the supplier's goods lose their distinct identity, and can no longer be returned in an "as received" state, title otherwise retained by a supplier will be lost. Borden (UK) Ltd v Scottish Timber Products Ltd [1979] 3 WLR 672 chemicals were mixed to form new chemical compounds. The Court of Appeal held that the supplier had no proprietary claim against the insolvent purchaser's manufactured products, and that any interest retained or acquired by the seller in those products would have amounted to a registrable charge.

In the absence of an express contractual provision, it can be argued that either
- title to manufactured products will vest in the purchaser, regardless of whether any of the materials were supplied by him,
    - or the supplier and purchaser become co-owners of the mixed product

(discussion required)

Clough Mill v Martin [1985] 1 WLR 111 – buyer and seller can agree as a matter of contract where title to contract vests. The contract may provide that seller and buyer be tenants in common of the co-mingled goods to the extent of their respective interests. But a term to the effect that product would remain the seller's property until raw materials were paid for was struck down in Clough Mill as a registrable charge. The relevant term provided that:
"If any of the material is incorporated in or used as material for other goods before [payment in full] the property in the whole of such goods shall be and remain with the Seller until such payment has been made, or the other goods have been sold … and all the Seller's rights … in the material shall extend to those other goods."
The Court of Appeal held that this clause created a charge over the products, which was void for non-registration.

The courts are generally reluctant to apportion ownership of product between supplier and manufacturer eg Modelboard Ltd v Outer Box Ltd [1992] BCC 945.

[Re London Wine Co (Shippers) [1986] PCC 121 – the court held that each category of wine held for customers remained the property of the Company. The contention that the Company held the bulk wine as a whole on trust for each customer failed as to create such a trust it must be possible to ascertain with certainty not only what interest of the beneficiary was but also the property attached to it.]

See also, he Sale of Goods Act 1979 which provides:
- if there is a contract for a sale of a specified quantity of unascertained goods in a deliverable state forming part of a bulk which is identified by the parties, and the bulk is reduced to (or less than) that quantity, and there is only one buyer to whom goods out of that bulk are due, the goods are appropriated to the contract at the time the bulk is so reduced and property than passes to the buyer.
- A buyer of goods forming part of a bulk which is identified by the parties, who has paid some or all of the purchase price in advance, is to be an owner in common of the bulk, and that property in an undivided share of the bulk is transferred to the buyer.
- A person who has become an owner in common is deemed to consent to dealings with the property by other owners in common.

vi. **Parallelogram Ltd**

Parallelogram's claim will depend upon the nature of the contract with the Company.

E Pfeffer Weinkellerei-Wieneinkauf GmbH & Co v Arbuthnot Factors Ltd [1987] BCLC 522: the buyer assigned to the seller future book debts payable upon resale of wine but then re-assigned those debts to secure finance from a factoring company. The seller's claim to book debt proceeds were bound to fail since the factoring company had given first notice of its rights to sub-purchasers. The judge also had regard to the fact that the seller's claims against book debts were expressed to be defeatable upon settlement of the buyer's debts. The terms relied upon were therefore indicative of a registrable charge.

nb Detailed knowledge of this case is not required, rather a reasoned argument on what happens once funds received from factoring company and possibility of the clause being a registrable charge.

vii. **Petitioning creditor's costs**

R4.66/4.67 – petitioning creditor's costs must be paid in the priority indicated – and

The costs should relate to the preparation of the petition and court fees.

The Liquidator should ask for an analysis of the costs to ensure that they are in respect of the preparation of the petition and the court fees.

If the Liquidator believes that the costs are too high, for example, the solicitors' hourly rates, he could ask (as a matter of negotiation) the petitioning creditor to submit a more reasonable fee.

If the petitioning creditor and the Liquidator do not agree on the quantum, the Liquidator may ask for the costs to be taxed by the Court

The creditors or the committee can require the Liquidator to have the costs taxed

QUESTION 4

a. State the main purpose of a Creditors' Voluntary Liquidation. Set out what factors should be considered when deciding whether to commence an investigation into the affairs of a company in Creditors' Voluntary Liquidation. (5 marks)

A procedure for winding up or bringing the affairs of a company to an end in circumstances where the company is insolvent (unable to pay its debts within the meaning of s123).
See s107 - to realise the company's assets and
- after the payment of costs, to distribute the proceeds among the creditors (and shareholders) according to their respective rights and interests (pari passu)
Following from this:
- duty to identify and recover the assets
- to determine the property (as defined in section 436 of the Insolvency Act 1986) and liabilities of the company and to identify any actions which could lead to the recovery of funds.
- to identify and agree creditors' claims
To carry out investigations to at least SIP2 standards.
There is a further purpose, imposed by the Company Directors' Disqualification Act, to report on the conduct of directors (but not to investigate that conduct).

(b) Taking into account the circumstances of the Parent's Liquidation and the information that has come to light since your appointment, set out the practical and legal steps that you, as Liquidator, may take to investigate the Parent in order to achieve the main purpose of the Creditors' Voluntary Liquidation. (15 marks)

Practical steps (before using any legal measures) include:
- request statement of affairs/if not forthcoming prepare estimated statement of affairs
- compare statement of affairs/estimated statement of affairs with last audited accounts and last management accounts
- prepare deficiency account
- search Companies House register
- search Isle of Man Companies Register
- Write to Heureux Ltd requesting details of how the debt arose.
- Review company records for availability of cars in the period when it was claimed no cars were available.
- send questionnaire requesting details of Company's dealings to directors and key staff.
- seek to interview directors and staff
- seek to interview Company's professional advisors, including auditors/accountants
- analyse Company's bank accounts for unusual transactions.
- talk to subsidiary's liquidator to ascertain if there were any unusual transactions with the Company, ascertain the inter-company balance and the reasons for it.
- ask creditors for information (should have done so at s98 meeting) and write to creditors, usually in first letter to creditors, requesting information.
- read Company's minutes/minutes of management meetings
SIP 2 – need to consider which directors and company staff need to interview
Legal steps
Rights of action include (see SIP 2):

Insolvency Act 1986
Section 76 Redemption or purchase of own shares
Section 127 Avoidance of property dispositions etc.
Section 128 Avoidance of attachments etc.
Sections 150 and 165 Uncalled capital
Section 212 Misfeasance and misapplication etc. of property
Sections 213 and 215 Fraudulent trading
Sections 214 and 215 Wrongful trading
Section 242 Gratuitous alienation
Section 243 Unfair Preferences
Section 244 Extortionate credit transactions
Section 245 Avoidance of floating charges
Companies Act 1985
Sections 135 to 141 Unauthorised reduction of capital
Sections 151 to 181 Unlawful assistance/redemption in the purchase of own shares
Section 277 Unlawful distributions to members
Sections 320 - 322B Unlawful property transactions
Sections 330 - 341 Unlawful loans
S134 – getting in company's property (any person has in his possession or control any property, books, papers or records to which the company appears to be entitled) – liquidator has to apply to the court to require person to deliver, convey, surrender or transfer the relevant property. The liquidator should probably write to the person first: requesting the property and also stating that he can ask the court to order the person to deliver up the property.
S235 – duty to cooperate with office holder, includes:
S235(2) – duty to give information about the company and its promotion, dealings and affairs or property as liquidator may at any time reasonably require and duty to attend on liquidator as he may reasonably require
S235(5) penalty for non-compliance – can be fine, or daily default fine for continued non-compliance
S235(3) – those who must co-operate include: officers of company; employees, former employees (up to one year); directors/officers/employees of another company (within one year) which is an officer of that company. No court order is necessary.
S236 – court, on application of liquidator, can summon to appear before it:

- any officer
- any person known or suspected to have in his possession any property of the company or supposed to be indebted to the company or
- any person who the court thinks capable of giving information concerning the promotion, formation, business, dealings, affairs or property of the company (s236(2)

s236(3) – the court can require the person to submit an affidavit containing an account of his dealings with the company or to produce any books, papers or other records in his possession or under his control relating to the company

This is a private examination (compared to a public examination under s133 which is not available to a liquidator in a CVL).
The court may order the costs of proceedings, under s235, 236, be paid by the respondent, if the court considers that the examination was made necessary because information had been unjustifiably refused by the respondent.
Where court makes an order under 237(1) (to deliver up property in his possession which belongs to the insolvent) or s237(2) (to pay any amount in discharge of a debt due to the insolvent) – the costs of the application for the order may be ordered by the court to be paid by the respondent.
Otherwise, costs shall be paid out of company in liquidation.
Note main purpose of investigation is to recover assets and so consider costs and benefits before entering into any investigation, especially if there are court appearances which may be costly.
Generally when trying to obtain information from the directors
- should ask them first and so write with either specific questions and/or, through the use of a questionnaire
If fail to submit statement of affairs – note powers of compulsion
S235 – duty to cooperate with office holder. Have an meeting with individual directors, if possible have in attendance shorthand writer to take notes of meetings
If all informal means have failed – the liquidator can apply for the court to examine the directors. This is more likely to be necessary when requesting information from the Parent's auditors, the liquidator of the Subsidiary, the former wife of D and her business associate.
Note also, if suspect any criminal wrongdoing – duty to report to Lord Advocate(IA 1986 s218)

Also, duty to report offences to NCIS under Money Laundering Regulations.

Transaction with IOM company
- use s235 to question Dick and, if necessary, other directors
- use s236 to question Freda and Graham
May have difficulties of examining Isle of Man residents under s236 – Re Seagull Manufacturing Co Ltd – an application under s236 is territorially limited to persons within the jurisdiction of the English court. Otherwise the liquidator may need to seek the co-operation of the Isle of Man Court under s436.

Amount due from Subsidiary
As this is now in liquidation, the Liquidator needs to consider whether he can trace the funds going out of the Subsidiary, ie was it used as a means of transferring the funds elsewhere.
Will need the assistance of the Subsidiary's Liquidator and/or the Official Receiver (who has power to investigate the affairs of the Subsidiary).
Should write to subsidiary and its Liquidator and request information.
May use s236 to question the auditors and s235 to question directors and former employees.
Note – SIP2 – liquidator needs to satisfy himself as to the validity of transactions with connected companies/associated persons.
Heureux Ltd
- there may be wrongdoing/criminality and so it may be necessary to inform Lord Advocate/NCIS.

(c) In addition to the matters listed in the legislation, what are the other main matters that a Liquidator is required to report under the Company Directors' Disqualification Act 1986. Explain the issues that may hinder any reporting. (10 marks)

Main issues to be reported
These are in addition to the matters contained in CDDA 1986, Sch 1 – Matters determining unfitness – which are explicitly not required here.
- SIP 4 – the Liquidator should include other matters which he believes to be relevant.
The Disqualification Unit attaches particular importance to the following:
attempted concealment of assets or cases where assets have disappeared or a deficiency is unexplained
appropriation of assets to other companies for no consideration, an undervalue, or on the basis of unreasonable charges for services;
preferences;
personal benefits obtained by directors;
overvaluing assets in accounts for the purpose of obtaining loans, or other financial accommodation, or to mislead creditors;
loans to directors in making share purchases;
dishonoured cheques;
use of delaying tactics;
non payment of Crown debts to finance trading;
phoenix operations;
misconduct in relation to operation of a factoring account;
taking of deposits for goods or services ultimately not supplied; and
cases where criminal convictions have resulted.
Practitioners should not take a pedantic view of isolated minor compliance failures, but should form an overall view of a director's conduct when deciding whether report is appropriate.
Details of the conduct giving rise to the decision to submit a report should be included, and specific examples of alleged findings should be given wherever possible. It is recognised that in some cases substantive information not be available, but the report, in the light of other information already held by the Disqualification Unit in deciding whether to recommend to the Secretary of State that it is in the public interest for an action to be brought in the event of the director being involved in other insolvencies.

The following matters should be dealt with within the body of the report:

· the position on any civil recovery actions;
· the adequacy of the accounting records;
· evidence available in support of insolvent trading;
· professional advice taken by the directors, and specific correspondence which sheds lights on directors' conduct, for example with banks, solicitors, accountants or creditors.

Where the practitioner has been unable to quantify, or otherwise comment on the amounts involved in the alleged conduct due to cost or other considerations then an explanation to that effect should be included in the

Matters hindering reporting

Any concealment/misconduct is just speculation at this stage but must report (or submit interim report) within 6 months (Disqualification Unit must bring proceedings within 2 years of date of liquidation and so there is a need to report speedily).

He is probably better to submit an interim report at this stage

- Liquidator needs to ensure that there are no defamatory statements in the report, especially when reporting suspicions. He needs to be aware that the report may be discoverable in any proceedings

PERSONAL INSOLVENCY (SCOTLAND) DECEMBER 2007

EXAMINERS REPORT

QUESTION 1

Background details were provided regarding an existing trust deed and candidates were asked to prepare an initial statement of affairs and likely financial outcome at the commencement of the trust deed (June 2006). Candidates were then asked to prepare a memorandum of issues that require to be discussed at a meeting with the executors and the proposed method of dealing with points which had been identified during the course of the trust deed process. Most candidates prepared a reasonably accurate initial statement of affairs with care being taken regarding layout. However, confusion appeared to arise in dealing with the likely financial outcome and candidates were unsure where to show future contributions, with some scripts showing the likely financial outcome as at December 2007 rather than June 2006. Candidates securing most marks were those who dealt with each item in turn rather than trying to address several issues at the same time.

In terms of preparing for the proposed meeting with the executors, it was curious that one or two candidates suggested that the executors were under an obligation to continue paying contributions on behalf of the late debtor. A number made assumptions regarding the life policy, pension policy and title deed position which hampered their ability to provide a full answer. There seemed to be a view that the late debtor's spouse would be able to answer questions regarding her husband's affairs which would not necessarily be the case, and whilst a number of candidates said that issues should be referred to a lawyer for advice, it is the knowledge of each candidate that was being sought rather than that of a third party. Several candidates were not aware that a trustee acting in a trust deed can petition for sequestration if the terms of a trust deed have not been met and there was misunderstanding about the trustee's ability to use trust deed funds to pay funeral expenses.

The question was answered reasonably well by most candidates and one suspects that, given more time, the layout and numerical calculations would improve.

QUESTION 2

The question sought an explanation of the process of electing a commissioner and scheduling the principal duties and requirements of such individual with regard to election in a sequestration.

The process of election was answered in a competent manner. Despite numerous sections in the Bankruptcy (Scotland) Act 1985, schedule 6 and SIP15 which deal with the duties/role of a commissioner, the second part of the question was not handled well. A significant amount of writing was required which created a disadvantage for those with bad handwriting and poor grammar. A candidate mentioning a section rather than detailing the contents of such section lost marks and a number of candidates failed to deal with issues such as the trustee resigning, death of a trustee, removal of a trustee whose actions are inappropriate, and whether or not the commissioner could be paid and/or recover travel expenses.

Again, layout and clarity did not seem to be uppermost in the minds of candidates and this detracted from many answers.

QUESTION 3

The question set out details regarding a recent sequestration appointment and asked candidates to prepare draft sales particulars, a letter of confidentiality and thereafter explain the steps to be taken by a trustee in order to validate the decision to sell the business when a number of low offers had been received.

The answers demonstrated that several candidates had dealt with the preparation of sales particulars before and were able to show a logical approach in addressing key issues such as employees, assets, occupation of premises, background to business, current business conditions, competitor and trustee details. Some scripts tended to spend more time discussing the preparation and validity of future trading forecasts, essentially a matter for a purchaser, rather than detail recent/existing financial performance. Also, it was surprising how many candidates wanted to disclose independent valuation details to potential purchasers.

Many candidates were unsure of what a letter of confidentiality contained and who would sign it.

In terms of validating the decision to sell a business, quite a few candidates did not mention the potential liability on the trustee for ongoing trading although most were quite clear about the requirement to consult with the independent valuer and accountant in bankruptcy/commissioner(s). A number of candidates became embroiled in considering dividend prospects which was not required and relatively few mentioned issues such as TUPE and communication with suppliers/customers. The question showed that candidates had a general knowledge of the issues but the lack of detail in many answers suggested that the knowledge was gained more from study than practical experience.

QUESTION 4

This question required the calculation of various claims and preparation of a claims' adjudication, followed by a requirement to explain the key issues in paying a dividend to creditors.

The question was designed to be fairly straightforward in terms of claim calculation and it was surprising how many candidates used the date of appointment of the trustee to calculate claims rather than date of sequestration. As a result, PAYE, NIC and VAT up to 19 October 2005 were all accepted as a valid claim rather than calculating the position as at 1 October 2005. There was clear knowledge of the £800 limit but confusion as to whether it applied to employees or the Redundancy Payments Office. Many candidates were able to gather marks by including detailed workings and hence, even where the wrong answer was obtained the correct thought process could be displayed. A few were unable to convert Euros into Sterling correctly, whilst the arrestment on 3 September 2005 was deemed (incorrectly) to be of no consequence.

Layout was important in terms of both the answer and workings and it was disappointing to see a number of scripts which were almost impossible to read.

Conclusion

In general terms, the legibility of handwriting proved a challenge when reading the scripts. Those candidates who had practical experience of the issues raised in various questions were able to display such knowledge to good effect.

PERSONAL INSOLVENCY (SCOTLAND) DECEMBER 2007

EXAM MARKING PLAN

QUESTION 1

(a) Prepare the initial statement of affairs and likely financial outcome that reflected the position in June 2006. (5 marks)

Protected trust deed for the late Tom Stewart

Estimated outcome as at 19 December 2007
(date of meeting with executors)

	£	£
Assets		
Heritable property in Plockton owned joint with spouse estimated to realise	200,000	
Less: secured borrowings	(120,000)	
Potential equity	80,000	
Whereof, one half to debtor		40,000
Contributions collected up to date of debtor's death (June 2006 to June 2007: 13 x £500)		6,500
Ford Fiesta vehicle, estimated to realise		1,500
Shareholding in Unilever plc, estimated to realise		18,000
Pension policy proceeds		40,000
Life assurance policy proceeds		-
Total assets		106,000
Liabilities		
Unsecured creditors		(76,000)
Net surplus		30,000
Provision for future payments		
Trustee's fees to date	5,000	
Trustee's fees to close	3,000	
Trustee's outlays	1,000	
Statutory interest on creditors' claims to, say, 15 December 2007 (18 months @ 8%)	9,120	
		(18,120)
Surplus funds to executors		£ 11,880

Matters to consider :

1. The debtor died after date of the trust deed, trust deed and thus, monies cannot be utilised to settle funeral expenses. This means that the debtor's spouse/family will be required to fund them from personal resources.

2. The trustee will have recorded his interest in the pension policy in June 2006 in terms of protecting the death benefit included therein.

3. If the trustee had been made aware of the term life assurance policy, he would have recorded his interest therein as a precautionary measure.

   It is noted that the policy is written in trust for the debtor's only grandchild and thus may be outwith the reach of the trust deed estate. In order to clarify the position, the trustee should write to the insurance company in order to ascertain the date that the policy was written in trust for the debtor's grandchild.

   If the instruction was within the five year period prior to the date of the debtor signing the trust deed, the trustee may challenge the transaction as a gratuitous alienation.

   For the purpose of preparing the statement of estimated outcome, it has been assumed that the policy was written into trust at inception of the policy and thus, excluded from the trust deed process.

4. The trustee will take steps to sell the shares in Unilever plc for the benefit of creditors.

5. Notification of the trust deed should be sent to the pension provider together with a certified copy of the death certificate in order that the death benefit may be obtained for the trust deed estate. Need to check for any specific death payment provisions i.e. to spouse, with pension provider.

6. If the vehicle is valued at less than £1,000, it is likely to be excluded from the trust deed estate on the grounds of materiality.

   The debtor's vehicle was valued at over £2,000 in June 2006 and he was allowed to retain it in order to travel to work such that contributions could be paid. No further contributions will be received in view of the debtor's death, and the trustee should take steps to obtain fair value for the vehicle. This can be provided by family members if they wish to pay fair value.

7. A fresh independent valuation of the property should be instructed and a current redemption figure for the secured borrowing obtained. The potential equity available in the property can be calculated.

   Check for existence of special destination clause.

   If no clause, the debtor's spouse should be invited to purchase the debtor's one half share of the equity at fair value. In this regard, fair value may be deemed to be less, perhaps up to 10/15%, than the arithmetical calculation in order to secure a prompt realisation and to reflect the spouse's cooperation.

   Alternatively, Mrs Stewart could be asked to allow the property to be placed on the open market for sale, and leave voluntarily when an acceptable offer is received.

If the debtor's spouse does not wish (is not able) to purchase the property and will not agree to the property being made available for sale, the trustee will have to consider whether it is appropriate to petition for the sequestration of the late Tom Stewart.

Once sequestrated, the property would vest in the permanent trustee who could seek court approval in order to progress an action of division and sale and evict the debtor's spouse from the property.

8. The debtor's spouse should be encouraged to seek independent legal advice.

9. On the basis that funds are received by the debtor's grandchild from the assurance policy, it may be that the debtor's grandchild is willing to release funds to the trust deed: perhaps in return for a standard security over the heritable property. This would avoid the debtor's spouse having to fund the purchase of the debtor's equity or consider selling.

(b) Prepare a memorandum setting out the issues that will require to be discussed at the meeting and note how you propose dealing with them. Include calculations to demonstrate the position. (15 marks)

INTERNAL MEMORANDUM

To: Insolvency practitioner

From: Insolvency manager

Subject: Notes for meeting with executors
Protected trust deed for Tom Stewart

At commencement of the trust deed process, 16 June 2006, the debtor's estimated statement of affairs and likely outcome was as follows:

Trust deed for Tom Stewart

	£	£
Assets		
Heritable property in Plockton (owned jointly with spouse) estimated to realise	160,000	
Less: secured borrowings	(120,000)	
Potential equity	40,000	
Whereof, one half to debtor		20,000
Ford Fiesta, not subject to finance	2,000	-
Debtor's contributions (36 x £500)		18,000
Total assets		38,000
Liabilities		
Unsecured creditors		(76,000)
Estimated net deficiency		£(38,000)

The debtor's assets and future contributions are forecast to be sufficient to pay a dividend of 50p in the £ to unsecured creditors.

The debtor has retained the car for work purposes and hence, agreed to pay a reasonable contribution to his estate from earnings.

The foregoing statement is subject to the costs of realisation of assets and the trust deed process.

In view of the debtor's death and the estimated outcome is as follows:

QUESTION 2

(a) Briefly explain the process of election of commissioners and detail who may and may not act as a commissioner. (4 marks)

ELECTION OF COMMISONER(S)

- Commissioners are normally elected at the statutory meeting of creditors but it is competent for the creditors to elect commissioners at any subsequent meeting. Nominations will be tabled at the meeting where the election takes place.

- The minimum number that may be elected is one and the maximum is five.

- A commissioner must be a creditor or an authorised mandatory of a creditor and can only be elected if a permanent trustee has been elected.

- The following individuals cannot act as a commissioner
    a) The debtor
    b) A person who holds an interest opposed to the general interests of the creditors
    c) An associate of the debtor or the trustee

- Two classes of creditor are not entitled to vote at the election of commissioners
    a) Anyone who acquires the debt, other than by succession, after the date of sequestration and
    b) A postponed creditor

Election is confirmed by votes at the meeting: one pound equals one vote, and each commissioner must agree to act.

(b) Schedule the principal duties, requirements and powers of a commissioner. (16 marks)

PRINCIPAL DUTIES, REQUIREMENTS AND POWERS OF A COMMISSIONER ELECTED TO ACT IN A SEQUESTRATION

The Bankruptcy (Scotland) Act 1985 provides that the general functions of commissioners are to supervise the intromissions of the trustee once appointed/elected in respect of the sequestrated estate and to advise him as required e.g. asset disposal, legal action etc. Whilst instructions/requests from the commissioners are persuasive, the trustee would normally require a good reason to ignore them.
The principal functions include the following:

- The commissioner(s) may inspect the record of intromissions of the trustee with the sequestrated estate at all reasonable times.

The commissioner(s) may offer advice to the trustee. The trustee will have due regard to such advice but there is no legal obligation upon him to accept/follow it but acting in a different manner would require to be based on good reason.

- The commissioner(s) to audit the trustee's periodic accounts and approve his outlays and fee claim(s). The trustee submits his accounts to the commissioner(s) within two weeks after the end of each six month accounting period and the commissioner(s) are required to audit such accounts and approve the outlays and fee claim within six weeks after the end of the accounting period. Thus, such accounts are likely to include all vouchers, bank statements etc. in order to allow the process to be undertaken.

The commissioner(s) will be invited to grant consent to the trustee before he pays the preferred claims against the sequestrated estate.

- If the trustee deems it inappropriate to pay a dividend to creditors in accordance with their legal ranking following the audit of each of his periodical accounts e.g. the estate has insufficient funds, the commissioner(s) can consent to postpone payment of a dividend. Similarly, should the trustee wish to accelerate the payment of a dividend he may do so with the written consent of the commissioner(s).

- When fixing the trustee's remuneration for the final accounting period in the sequestration, the commissioner(s) can adjust the remuneration which has been fixed for any earlier accounting period.

- When an offer of composition is made to creditors and such offer has been accepted, the commissioner(s) will be invited to audit the trustee's accounts and fix his outlays and remuneration for the period in which he has been acting.

- As soon as possible after the issue of an act and warrant from court, the trustee is required to consult with the commissioner(s) with regard to the recovery, management and realisation of the debtor's estate. This is normally done as part of the first meeting of commissioners. All matters discussed are wholly confidential. The commissioner(s) cannot impose instructions on the trustee [but they are entitled to make application to court for general or specific directions to be given to him: an unusual occurrence].

- The commissioner(s) is required to provide consent to the trustee if the trustee wishes to perform any of the following functions which he considers would be beneficial for dealing with the debtor's estate:

  (a) carry on any business of the debtor
  (b) bring, defend or continue any legal proceedings relating to the estate of the debtor
  (c) create a security over any part of the sequestrated estate
  (d) make payments or incur liabilities with a view to obtaining any property which is the subject of a right, option or power for the benefit of the creditors.

  The commissioner(s) may request the trustee to apply to the sheriff for an order for the public examination of the debtor, or of other relevant persons.

- Where a creditor wishes to submit a claim on the sequestration the normal procedure requires him to submit a statement of claim in statutory form, suitably supported by accounts/vouchers. The trustee may dispense with any part of this requirement with the consent of the commissioner(s).

The trustee is under a duty to retain certain documents in the sederunt book but is not bound to insert therein any document of a confidential nature. Nevertheless, the commissioner(s) can see any such document if desired.

- If the trustee wishes to submit an issue to arbitration or to agree a compromise with a creditor relating to a claim, he is required to obtain the prior consent of the commissioner(s).

- Where an offer of composition is made by the debtor, or on his behalf, the trustee will submit such offer with a report thereon to the commissioner(s). If the commissioner(s) consider that the offer will be implemented timeously, that it will secure payment of a dividend of at least 25p in the pound to ordinary creditors, and they are satisfied with certain other matters specified by statute, they are required to recommend that the offer should be placed before the general body of creditors for consideration.

- A trustee may make application to court for permission to resign prior to conclusion of a sequestration. In such circumstances the commissioner(s) will convene a meeting of the creditors for the purpose of electing a new trustee not more than 28 days after the existing trustee has resigned. If the trustee dies the commissioner(s) will convene a meeting of creditors for the election of a new trustee as soon as they are aware of the death.

- The commissioner(s) may apply to court for the removal from office of the trustee upon just cause being shown. The court may grant the order or make an alternative order, in which case there is a right of appeal by the commissioner(s).

- In the event of removal from office of the trustee, the commissioner(s) will convene a meeting of creditors for the election of a new trustee. The meeting is to be held no more than 28 days after the date of removal.

- If circumstances arise whereby the trustee is unable to act for whatever reason, or if he has so conducted himself in a manner that shows he should no longer continue to act, the commissioner(s) can apply to court to declare the office of trustee vacant and to make any necessary order to enable the sequestration to proceed or to safeguard the estate pending the election of a new trustee. The commissioner(s) would then convene a meeting of creditors for the election of a new trustee not more than 28 days after the court's declaration.

- The commissioner(s) can request the trustee to convene a meeting of creditors and the commissioner(s) can convene a meeting of creditors as long as appropriate written notice has been served to the trustee. The person calling the meeting is required to give not less than 7 days' notice to every creditor and to the accountant in bankruptcy specifying the date, time and place fixed for holding the meeting and the purpose of such meeting.

- The commissioner(s) may also instruct the trustee to convene a meeting of commissioners. If the trustee fails to do so the commissioner(s) may convene such meeting. The rules for commissioner(s) meetings are set out in part III of schedule 6 to the Bankruptcy (Scotland) Act 1985.

Commissioner(s) are not permitted to purchase anything from the debtor's estate.

QUESTION 3

(a) Your principal asks you to prepare draft sales particulars together with a letter of confidentiality. Detail the items which might be contained in the sales particulars and the key issues that a letter of confidentiality will include. (20 marks)

Information included in the Sales Particulars will include the following:

Details of the permanent trustee
- name
- address
- date of appointment
- agent(s) acting on his behalf
- telephone number, fax number and e-mail address

Financial information
- date of commencement of trade, type of trade and area covered
- major customers and details of any contracts in place
- summary of the key accounting information: turnover, gross profit and net profit. Most recent annual and/or management accounts would be useful.
- notice that further financial information can be made available to serious interested parties after viewing

Employees
- number of employees and whether they are paid weekly or monthly
- weekly/monthly payroll expense
- employee names, addresses, job title, date of commencement and hours of work
- copy contract of employment for each category of employee
- details of any Union involvement
- details of any special agreements with all, or some, employees

Trading premises
- location
- proximity to contract work
- details of communication links
- whether the premises are leased or owned
- the size of the premises
- if leased, date of expiry of the lease and details of the current lease, including any rent arrears
- rates obligation

Assets
- stock summary: value, key items, ROT issues
- an inventory of all moveable assets available for sale
- assets which are subject to finance (but may be purchased directly from the finance company)
- reference to any goodwill and intellectual property rights related to computer software, training aids etc
- details of factor (if book debts factored)

Standard terms
- sales particulars do not constitute an offer or invitation to the public of any jurisdiction
- the trustee is under no obligation to allow the potential purchaser to undertake further investigation into the business affairs nor to provide any additional information or otherwise negotiate with or deal with the potential purchaser
- sales particulars shall not constitute the bases of any contract that may be concluded
- the trustee has not carried out any audit or verification of the information contained in the sales particulars and accepts neither responsibility nor liability for negligence or failure to exercise reasonable skill or care in connection with the information contained in such particulars
- no representation or warranty is made in respect of any statement or opinion in the sales particular and the trustee contracts without personal liability
- closing date for offers

Confidentiality Agreement

a confidentiality agreement should be attached to the sales particulars and should be completed and returned to the permanent trustee if an interested party wishes to pursue their interest
information that might be included in the confidentiality agreement relates to:
the company
the permanent trustee
the potential interested party ("the recipient")

The recipient

a) undertakes that he will hold all information provided in confidence and will not directly, or indirectly, disclose any information to any third party at any time without the prior written consent of the trustee which must be obtained specifically on each occasion.
b) will use information only for the purpose of evaluating the debtor's business and assets with a view to determining whether or not to purchase or otherwise deal with such assets, and that he will take no action otherwise to use or exploit the information without specific prior written approval of the trustee.
c) will use his best efforts to maintain confidentially of all information provided.

It should be noted that the undertaking will not apply to any debtor information which at the time of disclosure is in the public domain or subsequently comes into the public domain through no fault of the recipient and not in breach of this agreement or was already known to the recipient at the date of disclosure to him by the trustee, or becomes known to the recipient after the date of disclosure to him by the trustee from a third party who did not acquire it directly or indirectly from the trustee.
Further, the recipient undertakes and agrees:

a) not to make copies or extracts of any written or other record of any debtor information provided.
b) that within seven days of termination of the agreement or within seven days of written request from the trustee, the recipient shall return to the trustee all debtor information in his possession.
c) that he will notify the trustee forthwith upon becoming aware of any disclosure or use of any debtor information.
d) to provide the trustee with all assistance reasonably required for the purpose of preventing or containing any leakage of debtor information under the agreement.
e) to indemnify and hold the debtor and the permanent trustee harmless in respect of any breach of the agreement by the recipient, including any costs in enforcing the agreement.

It should be noted that either party may terminate the agreement on thirty day's written notice to the other.

The confidentiality agreement should make it clear that it would take effect under, and be interpreted in accordance with, Scots law.
The letter should provide for signature by the trustee and an authorised signatory of the interested party and all signatures witnessed by a third party.

(b) What steps should be taken by the trustee in order to validate the decision to sell, and in anticipation of the day of handover? (10 marks)

The trustee should instruct a fresh independent valuation of the tangible assets. Forced sale and going concern values can be compared against the sum being received.

Review of the accounting information in order to establish the potential value of the business should be undertaken and benchmarking review used to compare key performance figures.

The trustee should liaise with the commissioner and/or the accountant in bankruptcy.

The trustee should review trading results since he assumed control in terms of determining if he has incurred a profit/(loss) and if the price being obtained ensures no overall loss to creditors. If a trading loss has been incurred under the trustee's stewardship, he should prepare a schedule to demonstrate that overall, he has generated a higher return for creditors compared with closure at date of appointment and disposal of assets under forced sale conditions.

Collate and provide to buyer all leases, finance agreements, customer contracts and asset ownership documents.

Prepare letter to customers to advise of sale.

Prepare letter to employees to advise of sale.

No VAT chargeable because it is the sale of a going concern.

Ensure all suppliers aware of date that trustee is ceasing to trade in order to invoice accordingly.

Cancel any trading/operating insurance cover and consider if increase in caution is required.

Take meter readings and advise utility providers, rates department and landlord of date of cessation of trading by trustee in order that final accounts can be prepared.

Collect all financial information (or copies) likely to be required to continue sequestration process

QUESTION 4

(a) Prepare the draft claims adjudication for presentation to your principal. (20 marks)

SEQUESTRATION OF GENEVIEVE DEAUVILLE FORMERLY T/A SCENT FROM FRANCE

PERMANENT TRUSTEE'S ADJUDICATION OF CLAIMS

Creditor: Name	Note	Amount of Claim £	Claim admitted: Preferred £	Claim admitted: Ordinary £	Claim Rejected: £	Reason(s) for rejection
HM Revenue & Customs (PAYE)	1	30,000		22,800	7,200	Debt incurred after date of sequestration
HM Revenue & Customs (NIC)	2	22,500		17,100	5,400	Debt incurred after date of sequestration
HM Revenue & Customs (VAT)	3	15,300		11,500	3,800	Debt incurred after date of sequestration
French company	4	1,503		1,503		
Former employee claims for unpaid entitlements:						
Arrears of wages	5a	17,100	6,400	10,700		
Holiday pay	5b	3,944	3,680	264		
Redundancy	5c	11,042	-	11,044		
Redundancy	5c	792	-	792		
Notice pay	5d	6,000		6,000		
ROT supplier	6	6,200		400	5,800	Cost of goods returned to supplier
Personal pension plan provider	7	750	750	-	-	
Arresting creditor	8	6,000	-	6,000	-	
Trade creditors	9	130,000	-	130,000	-	
		£251,131	£10,830	£218,103	£22,200	

Submitted by:

I M A Practitioner
Address
Date

(b) Explain the procedure that your principal will require to undertake in order to effect a distribution to creditors. (10 marks)

1. The claim submitted by HM Revenue & Customs for PAYE is afforded an ordinary ranking. The level of the claim is as follows:
   From 5 August 2005 to 19 October 2005 (date of award of sequestration) = 75 days
   From 5 August 2005 to 1 October 2005 (date of sequestration) = 57 days

   The date of sequestration constitutes the date for calculating claims and thus, the claim that will be admitted in the sequestration for HM Revenue & Customs is £30,000 ÷ 75 x 57 = £22,800.

2. The claim submitted by HM Revenue & Customs for NIC is afforded an ordinary ranking. The level of the claim is as follows:
   From 5 August 2005 to 19 October 2005 (date of award of sequestration) = 75 days
   From 5 August 2005 to 1 October 2005 (date of sequestration) = 57 days

   The date of sequestration constitutes the date for calculation claims and thus, the claim that will be admitted in the sequestration for HM Revenue & Customs is £22,500 ÷ 75 x 57 = £17,100.

3. The claim submitted by HM Revenue & Customs for VAT is afforded an ordinary ranking. The level of the claim is as follows:
   VAT due for the period from 1 October 2004 to 30 September 2005 is £11,500.

   VAT incurred subsequent to date of sequestration is a rejected claim.

4. It is noted that a French company supplied goods to the debtor on 2 September 2005 and has an outstanding balance due of €2,210.
   Section 49(2) of the Bankruptcy (Scotland) Act 1985 indicates that any claim stated in foreign currency should be converted into sterling at the rate of exchange prevailing at the close of business on the date of sequestration.

   Therefore the claim that would be admitted in the sequestration would be based on the rate of £1.47/Euro which produces a claim of £1,503.

5. The claim submitted by the former employees are as follows:

   (a) Arrears of wages
   4 (£1,400 x 2 months)
   = 4 x £2,800
   = £11,200

   2 (£900 x 2 months)
   = 2 x £1,800
   = £3,600

   2 x (£575 x 2 months)
   2 x £1,150
   = £2,300

   Total claim for arrears of wages = £17,100

   Limit of £290 per week = £1,256 per month for RPO purposes, and total amount of preferential claim limited to £800 per employee. Thus the claim would be calculated as follows:

	Total Claim	Preferred	Ordinary (RPO/employee)
	£	£	£
4 employees @ £1,400/month =	11,200	3,200	8,000
2 employees @ £900/month =	3,600	1,600	2,000
2 employees @ £575/month =	2,300	1,600	700
	£17,100	£6,400	£10,700

(b) The amount of accrued holiday pay is preferential in its entirety, although the Redundancy Payments Office will only pay up to £290 per week. The balance would be a preferred claim in the sequestration. The claims would be as follows:

	Claim	Preferred	Ordinary
	£	£	£
4 employees x (2 x 1,400 x 12/52) = 4 x (2 x 323 per week) =	2,584	2,584	-
2 employees x (2 x 900 x 12/52) = 2 x (2 x 207.7 per week) =	830	830	-
2 employees x (2 x 575 x 12/52) = 2 x (2 x 132.7 per week) =	530	530	-
	£3,944	£3,944	£ -

(c) Redundancy pay is afforded an ordinary ranking.

Redundancy – 4 x (6 x 290) = 6,960
2 x (6 x 207.70) = 2,492
2 x (6 x 132.70) = 1,592
£11,044

Additional element due to higher paid employees (4 x 6 x (£323 - £290)) = £792

(d) Payment in lieu of notice is afforded an ordinary ranking, and subject to adjustment depending upon each employee's income position during the period of notice.

6. The supplier will be required to deduct the cost of the goods which were returned to him under the terms of the retention of title clause. Therefore, the net sum due to the supplier is £400 (£6,200 less the cost of the goods £5,800).
7. Part 4 of schedule 3 of the Bankruptcy (Scotland) Act states that any sum which is owed by the debtor to an occupational pension scheme is afforded a preferred ranking.
8. Section 37 of the Bankruptcy (Scotland) Act 1985 deals with the effect of sequestration on diligence. The arrestment was served in the hands of a customer on 3 September 2005 and subsection 4 of section 37 indicates that no arrestment of the estate of the debtor within the period of 60 days before the date of sequestration shall be effectual to create a preference for the arrestor. Therefore, the permanent trustee would take steps to collect the sum of £3,000 from the customer and the creditor would have an ordinary claim in the sequestration for £6,000.
9. The other trade creditors claims will be afforded an ordinary ranking.
10. The debtor's spouse's claim in respect of a loan provided to the debtor for business purposes would constitute a postponed claim in terms of section 51(3)(B) of the Bankruptcy (Scotland) Act and as such would only be payable if all other creditors' claims together with statutory interest at the prescribed rate, had been settled.