RECOVERY

Data & cybersecurity

Intangible riches, tangible risks: IPRs
Most businesses will license or own intellectual property rights. How can you make the most of these intangible riches?

Fahrenheit GDPR – data destruction
Non-compliance with GDPR carries tough penalties. Find out how you should destroy, and record the destruction of, different types of data

Knowledge is your shield from online fraud
Fraud is a crime that can actually be prevented by knowing about it. The Met offers guidance on staying safe online

Pre-packs: best practice makes perfect
The code of ethics is there for a reason. Read up on best practice for this somewhat controversial procedure

Feet of clay: lessons from Carillion
Is administration out the window for large businesses in the wake of Carillion? Find out more about compulsory liquidation and why it was chosen for the business giant

An interview with… R3 president Stuart Frith
The association is going through a period of review and reform unlike any other. Find out what the future holds for R3 and the insolvency profession

Claims against IPs: the rising tide
What factors are behind the increase in litigation against IPs? Find out about the phenomenon and how best to combat it

Make yourself at home with the new rules for social housing providers
A special insolvency regime for social housing is now in force. Find out about the new duties for administrators

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What do you think? Readers' views are welcome. Have an opinion about a burning issue? Want to comment on articles or *RECOVERY* itself? Please contact me on **recovery@r3.org.uk**.

From the editor

As Chris Laughton is starring in this issue with an article about the regulatory side of pre-packaged administrations, the editorial board has asked me to be 'guest editor' for this quarter's publication.

The theme is data and cybersecurity, one of the various causes of the disruption and financial distress that we see in our market today. On that topic, we have Debbie Venn's piece covering the legal issues around the sale of intellectual property rights on page 17. Darren Bradshaw and Christopher Dunn explain that blockchain is becoming more relevant to our industry on page 20. On page 21, Mark Iwaszko highlights where insolvency practitioners now stand on data destruction post-GDPR. Finally, we have advice on how to avoid being the victim of online fraud from detective constable Callum Fraser.

In our legal update article and in one of our feature articles this issue (starting on pages 9 and 36 respectively), we hear about the reasons why claims against IPs are increasing and what they can do about it. Our technical update on page 12 is a helpful piece from HMRC detailing the teams within HMRC that IPs will interact with.

The biggest news stories in our industry this year have been retail CVAs, particularly following the landlords' aborted challenge of the House of Fraser CVA – and its subsequent pre-packaged administration – and the compulsory liquidation, as opposed to administration, of Carillion.

Our feature articles look at all three of these talking points. Phillip Sykes considers where CVAs currently stand as a restructuring tool on page 28. Chris Laughton looks at the regulatory regime and best practice for IPs in respect of pre-packs on page 30, and Alison Goldthorp looks at the Carillion compulsory liquidation on page 38. We also have an article on the new social housing administration regime on page 34.

When I joined the editorial board last year I naively asked what feedback we received from our readers. The response was that the board would love feedback, has sought it, but rarely receives it. This is your publication. Please tell us what you think of it and what you would like to see it cover. You can always send us an email to **recovery@r3.org.uk**. We can then ensure that it stays as relevant as it has always been.

Enjoy your end of summer reading!

Neil Smyth

NEIL SMYTH is part of *RECOVERY*'s editorial board and a partner at Mills & Reeve LLP.

WHAT YOU NEED TO KNOW

R3 Stats

22% British adults have had an outstanding credit card balance for at least six months, including the 4% of British adults who have had an outstanding balance for over five years.

34% of British adults are at least fairly worried about their current level of debt, while **34% say they sometimes or often struggle** to make it to payday.

26% of UK companies have suffered a hit to their finances following the insolvency of a customer, supplier or debtor in the last six months.

New R3/ICAEW research found that...

19% of 2013's CVAs have been fully implemented,

17% are ongoing, and

65% have been terminated – but that terminated CVAs may still be a better outcome for stakeholders than administration or liquidation.

Official Stats

Corporate insolvencies in Q2 2018 were

down 12% from Q1, but up 12% from Q2 2017.

Personal insolvencies in Q2 2018 were up 4% from Q1 and 27% up from Q2 2017.

Women are more likely to become insolvent than men, accounting for **54%** of personal insolvencies – **up from 30% in 2000**. 2017's personal insolvencies were again concentrated in coastal and industrial areas.

r3.org.uk/news-room

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President's column

Stuart Frith explains how R3 is taking your views on board as part of its strategic review.

On 20 July 2018, the R3 Council met to consider the findings of our strategic review and to plan the first steps of its implementation. This was always going to be at the forefront of my ambitions for my year in office and will no doubt continue into next year when Duncan Swift assumes the mantle. I have been an R3 member for the past three decades. There has been some introspection from time to time but I cannot remember a review as comprehensive as this one. We have put everything under the microscope to make sure R3 is fit for the future.

We have had some really constructive input from members – and non-members – as part of the review. This included thoughts from the 80 people from across the profession who have taken the time to sit down with our independent strategic review team, the delegates who provided feedback at our annual conference and the members and non-members who took part in our recent strategic review survey. Thank you to everyone who has taken the time to share their thoughts so far.

We are at the point now where we've identified key themes and work streams to be developed over the course of the rest of the year. R3 and the council will be setting up working groups of members and others in the profession to lead the implementation of changes in the coming months. The work of these groups will lead to some changes that will be seen by members and some which won't be as visible, while other parts will feed into a new R3 strategic plan.

Ensuring value for members

One key project for us is to look at which of our services are valued by members, where we can improve and what members want us to do less of. From our member survey, we know that our core services – including lobbying for members, technical and educational support, and thought leadership – are all highly valued by the profession and are good foundations for us to build on. Our work on 'member value' will support the rest of our strategic review work streams.

Among the more pressing issues for us to address as part of the review are R3's membership options and R3's larger events, such as the annual conference and the London & South East 'Ladies' Lunch'. On these issues, a number of things stood out from our member survey and stakeholder interviews, such as interest in the idea of corporate membership and in bringing the annual conference back to the UK. There is more we can do to support younger professionals too.

With 2019 membership renewals approaching and dates for key events already in the diary, we are working as quickly as we can to incorporate the member feedback in our planning. We do not want to rush into things though, so changes may be incremental, this year and next. Some ideas need careful analysis to make sure they are both commercially viable and fair to members across the profession.

> "I know the good work R3 has done to support our profession since it was founded. I want to make sure R3 has the same impact for years to come."

Another key part of the review is making sure R3 is relevant to those working throughout our profession – and trying to define exactly what 'our profession' is. This means representing insolvency practitioners, but also making sure turnaround and restructuring experts, and others, have a voice too. Encouragingly, respondents to our survey were much more likely than unlikely to feel that R3 does represent the 'whole spectrum' of the profession, from insolvency to turnaround; even more members felt that we *should* be doing this though, so there is work for us to do to close the gap between member expectations and what we deliver already.

What we know

As mentioned above, some of our core services are very highly valued by members: 95 per cent of our survey respondents said it is important that R3 lobbies for and promotes the profession; 94 per cent said it was important for R3 to provide technical, training, and educational support; and 88 per cent said it was important for R3 to play a thought leadership role. While R3 has a great track record on these functions, we can't be complacent. Our member engagement has already given us some great ideas about how to improve, including shifting the way we deliver courses, providing members with more opportunities to feed their concerns and views into our lobbying work, or simply improving how communicate what we do to members. All of our work in these areas will be looked at to make sure we're meeting member needs.

Finally, we will also have working groups looking at R3's member communications and corporate governance. It is important that members can keep up to date with what R3 is doing, and have plenty of opportunities to get involved.

Have your say

At the heart of the strategic review is making sure R3 responds to member needs and ensures members' voices are heard – and that goes for the review itself. Although our working groups are getting underway with their projects, it's not too late to have your say. Please do keep sharing your thoughts with me or R3 staff when you see us at R3 events, or by emailing in to **president@r3.org.uk**. Do keep an eye out for updates on the review as well.

I know the good work R3 has done to support our profession since it was founded. I want to make sure R3 has the same impact for years to come. This review will help R3 meet the needs of members now and in the future, wherever they work in the profession, and wherever they have got to in their careers. We have made a great start – and we are all set for the next phase.

Finally, at the council meeting we announced that Colin Haig of BDO will succeed Duncan as your President in 2020. I am delighted that Colin will be joining the executive committee immediately and will be assisting in carrying on the work that we have commenced. □

STUART FRITH is president of R3 and a partner at Stephenson Harwood.

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▶ If you are a lawyer and would like to write for Legal Q&A please contact: **matthew.jukes@groupgti.com.**

Legal Q&A

Andrew Robertson answers your insolvency queries.

Q I have been appointed administrator of a business that supplied goods and materials in the construction sector subject to retention of title (ROT) terms which have not been paid for. I understand that the purchaser is also in financial difficulty. What can I do in order to ensure the company gets paid?

A You must first establish that the company had a valid contract with the purchaser of the goods and materials that incorporates the ROT clause. It must be clear at the time that the goods in question were supplied, and that the parties were conducting business on such terms and no other terms. Ideally, this would be evidenced by a signed contract, or if there is no contract, an invoice attaching the relevant terms and conditions. Failing that, you will be reliant upon showing that the two parties had regular dealings, which meant it was clear the ROT terms should apply.

> There are a number of ways in which the purchaser, or an ultimate beneficiary, may be able to argue that the company's title in the goods and materials has been lost.

Assuming there is a validly incorporated ROT clause, you will need to check its terms to see whether it is a 'simple' or 'all monies' clause, and whether it provides any enhanced rights against the purchaser. A simple clause will reserve title in specific goods and materials until payment has been made for *those* goods and materials supplied. An all monies clause will reserve title in *all* goods and materials supplied until all sums due from the purchaser across a number of invoices have been paid. In addition, ROT clauses will often contain requirements on the purchaser to clearly mark the goods and materials as property of the company, segregate them from others and give the supplier a right to inspect and collect goods and materials if payment has not been made.

If you are satisfied that you have a valid ROT clause and identified its nature, you should write to the purchaser as soon as possible to put them on notice of the company's title to the goods and materials. If there are enhanced provisions regarding storage, you should also refer to these and put the purchaser on notice of its potential liability if it does not pay for the goods in full (or all sums due if the clause is 'all monies') or allow you to collect the goods and materials. If the goods and materials have ultimately been passed on to another third party (eg a developer/main employer), you should be putting them on notice of the same. The onus is on the company, as supplier, to positively assert its title.

Unfortunately, that is not the end of the story. There are a number of ways in which the purchaser, or an ultimate beneficiary, may be able to argue that the company's title in the goods and materials has been lost. This will depend on the nature of the goods and materials and how they were supplied. The main arguments are likely to be as follows:

- where goods and materials have been incorporated into works, title will be lost (this is known as the *quicquid plantatur solo solo cedit* rule). Whether goods and materials have been incorporated into the works will depend on the degree of annexation involved. For example, if bricks have been incorporated into a structure, they cannot be removed without causing damage and title in the bricks is likely to be lost. However, if carpets have been supplied, laid and incorporated into a building, it may be possible for them to be removed without damage and therefore, title may be retained;
- where goods and materials have been mixed with other supplies to the extent that they are no longer identifiable, title will be lost. For example, if paints are mixed to form a different paint, title in the original paint will be lost. Similarly, if resin or varnish is applied to wood, it will have become part of the wood and therefore title will be lost. It may also be harder to identify the same materials if they are provided by more than one supplier and are mixed; and
- if the goods and materials have been supplied by the company to the immediate purchaser pursuant to a contract for the sale of goods (but not the supply of services), and are then subsequently passed to a third party (eg a developer/main employer), if that third party has paid for the goods in good faith under its contract with your purchaser by way of a certified disposition (eg a certified payment under a construction contract) and without notice of the company's ROT rights, it will take possession of the goods and materials free from the company's title (section 25 of the Sale of Goods Act 1979).

Putting all parties on notice of the company's title in the goods and materials as soon as possible is the best way to protect its right to get paid in the circumstances. If the purchaser takes action to incorporate or mix the goods and materials while on notice of the ROT claim in an attempt to defeat it, they will be liable for conversion and damages. Similarly, if the ultimate beneficiary has not paid for the goods yet, putting them on notice now will prevent that party from relying upon section 25 of the Sale of Goods Act 1979 to defeat the ROT claim. However, you should also be aware that if the company owes or could owe the purchaser monies as a result of it entering into administration, you will likely still encounter resistance to payment and may have to agree a commercial settlement in order to resolve the matter. □

> Putting all parties on notice of the company's title in the goods and materials as soon as possible is the best way to protect its right to get paid in the circumstances.

ANDREW ROBERTSON is a senior associate at Pinsent Masons LLP.

Events, courses and conferences

Training and Networking

R3's national event programme offers an exciting and wide range of opportunities for high quality professional development for insolvency professionals at all levels of expertise and experience.

September

Practical Introduction to Insolvency Work – Personal Insolvency
6 September, London – *One day course*
The first day of this series will focus solely on practical Personal Insolvency issues. Visit the website for a full breakdown of topics and speakers.

Recent Challenges to Office-Holders' Conduct and Conflicts
13 September, London – *Breakfast briefing*
This briefing will focus on recent judgments concerning challenges to the conduct of insolvency practitioners and the difficulties surrounding conflicts.

Restructuring Day
13 September, Leeds – *One day course*
This interactive course will cover some of the common tools used to achieve a restructuring from out of court approaches to pre-pack administrations.

Directors' Duties
18 September, Birmingham – *Half day course*
With new and up-to-date content, this course will consider directors' duties from the perspectives of both the lawyer and the insolvency practitioner.

Practical Introduction to Insolvency Work – Rescue, including Administrations and CVAs
20 September, London – *One day course*
Day two will focus on an understanding of the key fundamentals of fixed and floating charges and the pitfalls of the administration appointment process.

Charities and Not-for-Profit Sector
26 September, London – *Half day course*
This course aims to help attendees understand some of the key features which mean charities cannot be treated as a standard insolvency process.

October

Insolvency Litigation
4 October, London – *One day course*
This year new topical sessions include court appointed receiverships, pre packs, CVAs and a session dedicated to litigation costs.

Practical Introduction to Insolvency Work – Liquidations I
10 October, London – *One day course*
The next two days will cover Liquidations in detail. Liquidations I includes DMPs for meetings, the preparation of the Statement of Affairs, and antecedent transactions.

Core Tax for Insolvency Professionals
18 October, London – *Half day course*
This course aims to bring insolvency practitioners and their relevant key staff up to speed with the world of tax as it interacts with restructuring and insolvency.

Insolvency: Blockchain & Cryptocurrencies
30 October, London – *Breakfast briefing*
An introduction to cryptocurrency and blockchain. What should the IP and/or solicitor do when an insolvent may or does possess cryptocurrency?

What's on in your region...

EASTERN

Golf Day, *6 September*
St Ives (Hunts) Golf Club
For Golfers & Non-Golfers! Play 18 holes or learn from the best followed by a social BBQ and prize giving.

Joint Regional Meeting
18 September, Bury St. Edmunds
Joint meeting held in conjunction with the ICAEW delivered by an excellent panel of speakers.

LONDON & SOUTH EAST

Evening Briefing
20 September, Brighton
"APNs/PPNs follower notices and EBTs – What to do with them when you encounter them."

Regional Meeting, *26 September, Smith & Williamson LLP*
"Current Issues in Insolvency Litigation Funding."

SCOTLAND

Golf Day, *11 September, The Renaissance Club, North Berwick*
Enjoy a round of golf, breakfast, lunch and full use of the club's leisure facilities.

Annual Dinner, *11 October, The Grand Central Hotel, Glasgow*
The famous R3 in Scotland Annual Dinner returns for an evening of good food and drink and entertainment.

NORTH WEST

Breakfast Meeting, *12 September*
Begbies Traynor, Manchester
Join the North West region for the second breakfast meeting of the year.

Afternoon Tea, *20 September*
Leaf, Manchester
The ticket price includes afternoon tea, a glass of prosecco as well as a tea masterclass talk.

SOUTH WEST & WALES

Comedy Gala, *13 September, Mercure Bristol Grand Hotel*
Don't miss the chance to attend the South West & Wales re-invented annual celebration for members. The event will be a spectacular evening of comedy, networking and food. Acts to be announced!

MIDLANDS

Golf Day, *25 September*
Edgbaston Golf Club
Teams of four will play a round of golf on this prestigious golf course before enjoying dinner and prize giving.

Afternoon Tea, *27 September*
Damascena Eatery, Birmingham
Join the West Midlands region for afternoon tea with a difference – 'A Taste of Arabian Nights.'

NORTHERN IRELAND

Golf Day, 4 October, *The Royal Belfast Golf Club*
Commencing with bacon rolls, play a round of golf or enjoy a 90 minute golf lesson with the club professional. The afternoon will be followed by a drinks reception, two course meal and prize-giving.

LONDON & SOUTH EAST

R3 LADIES LUNCH, *12 October, London*
Celebrating over 20 years of the Ladies' Lunch!
The 2018 Ladies' Lunch provides an opportunity to network with senior professionals and business leaders from across the insolvency, restructuring and turnaround world. With over 800 guests in attendance, this is the chance to mix with those who influence and shape our sector.

For more information on our training, networking and social events please visit www.r3.org.uk/events

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Recent case summaries

Latest insolvency update from **Katherine Hallett**.

PERSONAL & CORPORATE INSOLVENCY

***Pathania* v. *Tashie-Lewis & Okonye* [2018] EWHC 362 (Ch), [2018] All ER (D) 61 (May)**

The High Court held that a deputy master had erred in introducing a test of causation and declining to give a remedy pursuant to s423 IA 1986.

Although here the claimant was a creditor of the transferor of the asset, s423 is also a useful weapon for office-holders (both personal and corporate). The classic case is one in which a debtor transfers an asset (to a family member) in an attempt to avoid paying their debts.

The three criteria are: the transaction was at an undervalue; the claimant was a victim of the transaction in that it was at least capable of causing prejudice to him or her; and the purpose of the transaction was to put property beyond the reach of persons who may have a claim against the debtor.

> Although here the claimant was a creditor of the transferor of the asset, s423 is also a useful weapon for office-holders (both personal and corporate).

Frequently, it is the purpose criterion that is the focus of claims. It is the purpose of the debtor in entering into the transaction that is relevant, not the state of mind of the recipient of the asset. The latter may be relevant to the question of what remedy is available: this is discretionary and may not necessarily entail the reversal of the transaction. The jurisdiction is flexible.

In this case, the debtor borrowed money from the claimant in order to finance a building project. Without having repaid the claimant, the debtor disposed of the two houses by way of sales, one of which was to the second defendant, Ms Okonye. Although the sale price was realistic, the unpaid deposit was 38 per cent.

The deputy master found that the transaction was at an undervalue because the deposit had not been paid. The claimant was also a victim for the purposes of the statutory test. However, the claimant was denied relief. This was on the basis that a sale would have happened anyhow, because the debtor was in arrears with his mortgage lender, which was seeking a possession order. The deputy master held that the debtor would have then dissipated the sale proceeds without paying the claimant. Thus, he was no worse off.

The deputy judge reversed that decision. There was no justification for introducing a test of causation, which was inconsistent with the Court of Appeal's analysis in *Hill* v. *Spread Trustees* [2006] EWCA Civ 542. The key was the purpose behind the entry into the transaction: there was no further requirement that the transaction should actually have been detrimental to the claimant (only that it was capable of being so).

On the question of remedy, the deputy judge applied the reasoning from *BAT Industries* v. *Sequana* SA [2017] EWHC 211: when statutory criteria are established, the court will normally prefer the interests of creditors over the recipient and will fashion a remedy as appropriate. The deputy judge ordered that the sum of the undervalue (£55,102) should be paid to the claimant (there was no evidence of other creditors).

CORPORATE INSOLVENCY

***Ve Vegas Investors IV LLC & Ors* v. *Shinners & Ors* [2018] EWHC 186 (Ch), [2018] All ER (D) 34**

The registrar (now Insolvency and Companies Court judge) heard an application by creditors to remove from office administrators who had arranged a pre-pack sale of the company's business. The pre-pack sale had been to a NewCo connected to the company's management staff who had worked with the IPs to achieve the sale.

The creditors applied to the court on the basis that the pre-pack sale was in breach of the company management's duties to the business and that it prejudiced other bidders. Furthermore, there were grounds to investigate the administrators and their firm – the creditors argued that the administrators should be removed because of the conflict.

The application was successful, but only shortened the administrators' appointment by five business days because they gave notice of their intention to resign during the trial. The registrar found that there were a number of possible conclusions to draw from the facts: one was that the company management and the IPs' firm had done the best they could, with limited time, to achieve the only realistic sale and price available; another was that the company management took improper advantage of the circumstances, excluded others from the sale process and secured the purchase at an undervalue.

There were therefore serious issues to be investigated, which possibly included looking at the conduct of the company management and the IPs' firm. The administrators could not carry out that role. However, that did not necessarily mean that they had to vacate office: for instance, they could have worked in parallel with additional, non-conflicted administrators, who would have investigated the pre-pack sale. The registrar felt that the administrators had lost perspective on the claims that might be brought and on the conflict arising, once they became primarily concerned with defending any claim against their firm. He therefore exercised his unfettered discretion to remove them.

> The registrar felt that the administrators had lost perspective on the claims that might be brought and on the conflict arising once they became primarily concerned with defending any claim against their firm.

This case is important in highlighting (a) the potential conflict situations IPs may face in acting pre-appointment on sales and (b) the behaviour to be expected of office-holders once such conflicts arise. □

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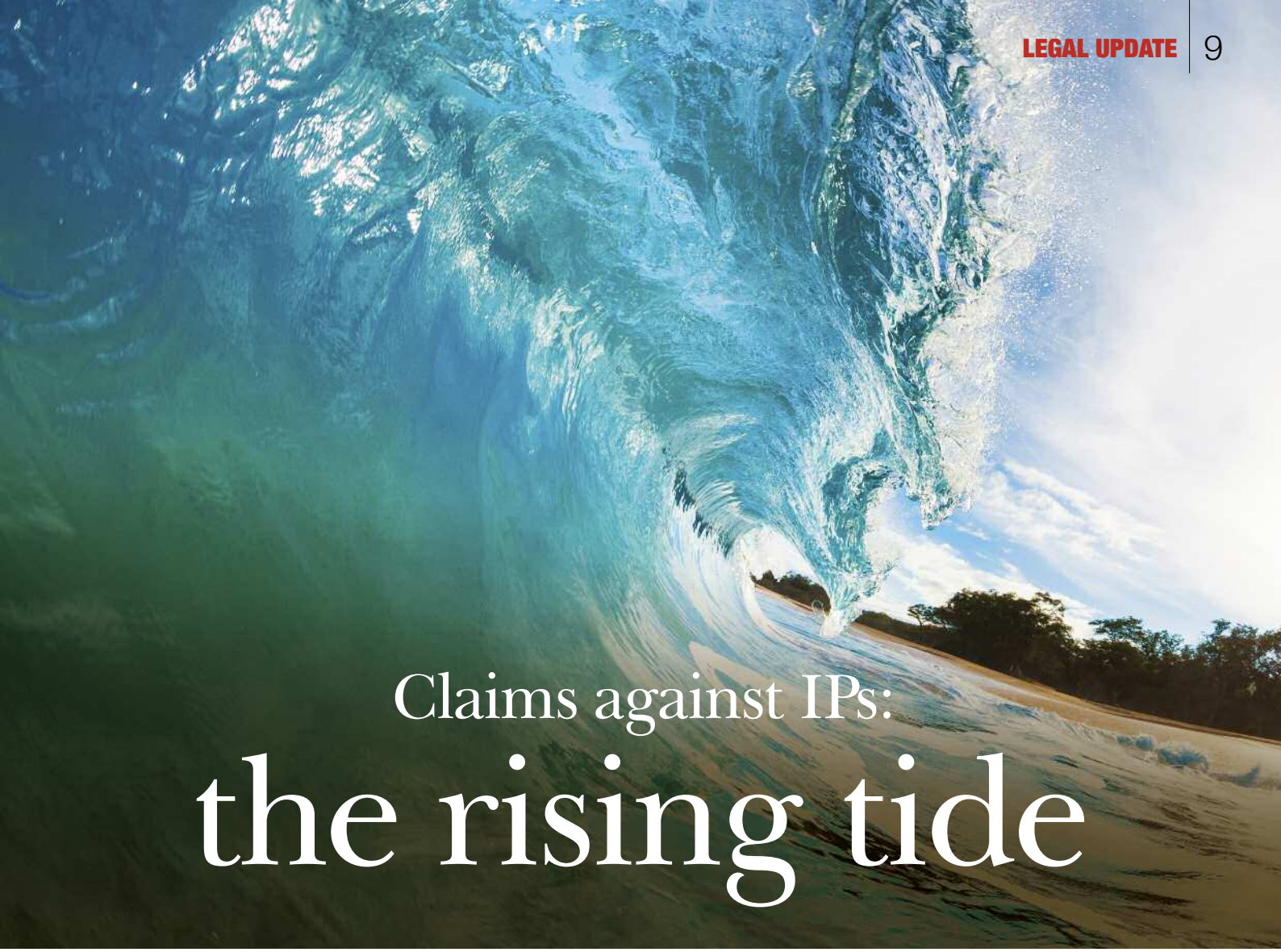

Claims against IPs: the rising tide

Helen Fairhead investigates the recent rise in litigation against IPs and considers what IPs can do when they are on the receiving end of such claims.

The role of an IP has always been challenging – taking control of a company in crisis, making swift decisions based on limited information and balancing the competing interests of stakeholders; all of this requires sound judgment, often under extreme pressure. It is no surprise that, when things go wrong (or perhaps more accurately when parties feel they have lost out), the IP can become the focus of blame, and their insurance policy an attractive target for 'last resort' litigation.

> **In the past few years, there has been a noticeable change in the type of claims brought against IPs and their firms, as well as a large uptick in their frequency.**

The traditional situation in which an IP finds themself the target of litigation is one where lenders have enforced personal guarantees against the company's directors or shareholders. Faced with the prospect of paying out under the guarantee, the director or shareholder responds with a cross claim against the IP[1], usually along the lines that the IP breached his/her duties by failing to realise the best price when selling key assets. In other words, a claim that the IP 'undersold' those assets[2].

However, in the past few years, there has been a noticeable change in the type of claims brought against IPs and their firms, as well as a large uptick in their frequency. Two main themes have emerged.

The first is that claims for 'underselling' are increasingly being brought as standalone actions, rather than as a defensive tactic to demands under a guarantee. See, for example, *AM Holdings* v. *Batten & LePage* [2018] EWHC 934 and *Davey* v. *Money & Another* [2018] EWHC 766 (Ch). Both of these claims were brought by the company or its shareholders as standalone claims that (*inter alia*) the IPs had undersold the company's assets. It is notable that both claims were brought after what would ordinarily be perceived as successful administrations – in *AM Holdings* the company returned to solvency, and in *Davey* unsecured creditors had received a significant dividend.

> **The litigation funding market has experienced exponential growth in recent years. Some estimates now value the market at £2.7bn – a tenfold increase since 2009.**

The second theme is the rise in claims based on economic torts – most notably claims for unlawful means conspiracy. The most high profile of these claims has arguably been *Premier Motor Auctions* v. *Lloyds Bank and PwC*, which was dismissed earlier this year, but there have been (and still are) many similar claims at various »

stages of proceedings. The typical allegation in such claims is that the IP or their firm unlawfully conspired with a secured creditor (usually a bank) to place the company into an insolvency process with a view to extracting the associated fees and (in the case of the bank) a discounted equity stake in the company.

In this article we look at a number of cases exemplifying these themes and consider: (i) what has driven the increase in them; (ii) what tactics IPs and their firms have used to defend them; and (iii) what the future holds for this type of litigation.

> One aspect that renders IPs particularly vulnerable to claims for unlawful means conspiracy is, of course, that they hold office personally and take appointments jointly with other IPs.

What is driving the increase in claims?

The primary, unavoidable factor behind the increase in claims is the growth of the litigation funding and after-the-event (ATE) insurance market. Most IPs will be familiar with these tools having used them to pursue claims against (for example) former directors in order to bolster the assets of the insolvent estate. However, as *RECOVERY* readers will no doubt be aware, the litigation funding market has experienced exponential growth in recent years. Some estimates now value the market at £2.7bn – a tenfold increase since 2009[3]. The sheer amount of capital that litigation funders have to invest means they have inevitably had to cast the net wider when funding claims. One consequence of this is that litigation funding has evolved from a tool that IPs utilise to bolster the insolvent estate, into a double-edged sword that may cut the wielder.

Add into the mix the 2014 report by Lawrence Tomlinson. Although the Tomlinson Report focused upon perceived failings in the way in which banks dealt with distressed businesses, it also made a number of allegations about the role of accountancy firms, pointing to what it perceived to be:

- the high potential for conflicts of interest when undertaking independent business reviews for banks, given the same accountancy firm was likely to be appointed to act as the business's administrator; and
- the *'unfair and opaque'* behaviour of administrators and receivers when in office.

The publicity surrounding the report, together with an increased appetite for litigation against large institutions following the 2008 financial crisis, has arguably created a significant impetus for those looking to pursue claims against banks, accountants and other financial institutions.

Conspiracy theory

The final and perhaps most interesting factor behind the increase in claims, is developments in the law of economic torts, in particular unlawful means conspiracy.

Unlawful means conspiracy occurs where two or more people act together unlawfully (the unlawful act can be civil or criminal), intending to damage a third party, and do so.

One aspect that renders IPs particularly vulnerable to claims for unlawful means conspiracy is, of course, that they hold office personally and take appointments jointly with other IPs. This, combined with the fact their firm often has a separate advisory engagement with the company and/or one of the company's lenders, means there are multiple parties over whom a claimant can make an allegation of conspiracy.

Furthermore, in 2007–2008, two House of Lords decisions clarified two key elements of unlawful means conspiracy and, as a result, made it much easier for claimants to pursue this course of action.

The first of these decisions was *OBG Ltd and others* v. *Allan and others* [2007] UKHL 21, which confirmed the level of intention that a claimant must demonstrate to establish unlawful means conspiracy. *OBG* confirmed that a claimant does *not* need to show that the defendant's sole or predominant purpose was to injure another person, only that it was one of the defendant's purposes. The result being that the relevant level of intention for unlawful means conspiracy can be established where injury to the target is a means to an end, rather than an end in itself[4], which is a much lower threshold.

This makes it easier for claimants seeking to plead unlawful means conspiracy. As an example, a claimant looking to bring a claim that an IP (or his or her firm) conspired with a bank to place a company into insolvency, does not need to demonstrate that the IP's sole purpose was to injure the company; he or she only needs to show that injury to the company was a means to an end; that end can, for example, be the professional fees the insolvency appointment would generate.

The second House of Lords decision was *Total Network SL* v. *HMRC* [2008] UKHL 19. Here, it was confirmed that the 'unlawful means' in question do not need to be something that is directly actionable by the claimant against the defendant. In other words, as long as there has been an unlawful action that is actionable by someone, even if not the claimant, then (providing all the other requirements are met) a claim for unlawful means conspiracy can be brought.

The fact the 'unlawful means' do not need to be directly actionable by the claimant has very wide implications in an insolvency context. In theory, it means individual creditors can bring claims for unlawful means conspiracy in circumstances where they would not otherwise have a cause of action. Take claims against administrators as an example. In an administration, absent special circumstances, the administrator owes his or her duties to the company, not to individual creditors[5]. However, if a creditor can establish that the office-holder has breached his or her duty to the company (ie the unlawful means), the requisite intention and the necessary element of combination (ie the conspiracy), then following *Total* it seems possible, in theory, for that creditor to bring a claim against the administrator (and others) for unlawful means conspiracy. At the time of writing this article, we are not aware of any such claims having been pleaded and whether such a case could ever proceed on policy grounds is debatable. However, with determined claimants pleading ever more creative causes of action, it seems only a matter of time before this is attempted.

> Where an IP or firm is confident that the merits are in their favour, the best option is likely to involve mounting a vigorous and robust defence and waiting for the claimant to run out of steam (or funding), or ultimately, vindication from the court by way of judgment.

RESPONSE ONE: early determination

Faced with a perfect storm of available funding, cultural impetus and claimant-friendly legal developments, it is no surprise that IPs and their firms have tried to dispose of such claims at an early stage, thus saving the time and cost of defending a claim to trial.

As seasoned litigators will appreciate, the English Civil Procedure Rules (CPR) provide certain mechanisms for the early disposal/determination of a claim, namely:

- an application for strike-out under CPR r3.4 on the basis that the statement of case discloses no reasonable grounds for bringing the claim or that it is an abuse of the court's process; and/or

- an application for summary judgment under CPR r24.2 on the basis the claimant has no real prospect of succeeding on the claim or issue and there is no other compelling reason why the case or issue should be disposed of at a trial.

In practice, applications made under these provisions are most likely to be successful where they are based on discrete points of law, contractual construction or procedure (eg limitation). In those cases, if the court is satisfied that it has all the evidence necessary to determine the question before it, then it is likely to 'grasp the nettle' and decide matters. IPs may therefore benefit from considering whether any such 'killer' points can be raised at the outset.

> It is perhaps of little comfort but, ultimately, where a claim that impugns the IP's integrity or professionalism fails, the IP can at least expect to recover indemnity costs.

Two recent examples where IPs have made successful applications to determine claims at an early stage are *AM Holdings* (see above) and *Fraser Turner Limited* v. *PwC and others* [2018] EWHC 1743 (Ch). In both cases, the court was prepared to deal with a short point of law or construction.

- In *AM Holdings*, the claim against the former administrators (for 'underselling' certain properties) was stuck out on a point of law – namely that the applicable provisions of Guernsey law governing the administrators' discharge precluded further liability to the company for breach of duty.
- In *Fraser Turner*, the claim for unlawful means conspiracy was struck out as the court was able to determine a short point of contractual interpretation – namely, whether the contract (a royalty deed) contained certain express or implied terms. The court held that the contract did not contain the terms alleged by the claimant, thus meaning there was no breach of contract, no unlawful act and the claim was therefore '*not maintainable*'.

RESPONSE TWO: play the long(er) game

Of course, an early application for strike out and/or summary judgment will not be an option in every case. Where there is no procedural or legal 'killer blow', and where the underlying evidence is contested and requires detailed analysis, then the claim is unfortunately likely to proceed to trial.

Underselling claims, by their nature, are likely to involve contested factual and expert evidence around the sale process and asset value. This means they can be very difficult to strike out, leaving the IP in question with the prospect of defending years of litigation to clear their name – the case of *Davey*, which involved a two-year wait for judgment, being a good example of this.

Claims for unlawful means conspiracy are also difficult to dispose of early because the allegations are rarely based upon direct evidence of wrongdoing – rather they are based upon inferences made from certain key (and largely uncontested) facts, which may be open to a number of interpretations. It is more difficult to convince a court at an early stage that such claims are 'fanciful' or stand 'no real prospect of success' as the court is likely to want to see and hear all of the evidence before reaching a decision.

IPs therefore face a longer game to try to defeat these claims. Where an IP or firm is confident that the merits are in their favour, the best option is likely to involve mounting a vigorous and robust defence and waiting for the claimant to run out of steam (or funding), or ultimately, vindication from the court by way of judgment. *Premier Motor Auctions* v. *Lloyds Bank and PwC* is a recent example of where such a case failed to last the distance. The claim against both defendants for (*inter alia*) unlawful means conspiracy in relation to the way in which the company entered insolvency was dismissed (effectively dropped) just weeks before trial.

Tactics for IPs

Clearly, each case will require its own unique tactics and IPs will need to consider their options carefully and with close input from their legal advisers. However, other tactics IPs playing the longer game may wish to consider might include:

- making early voluntary disclosure, especially where a claimant has pleaded a case '*pending disclosure*', to demonstrate that there is nothing in the allegations and the claimant should abandon the case; and/or
- making use of interim applications, such as security for costs, to protect their position and to increase the pressure on the claimants to obtain further funding and/or stronger ATE insurance. The *Premier* case is a recent example of where the defendants successfully applied for security for costs (see the Court of Appeal's decision at [2017] EWCA Civ 1872).

It is perhaps of little comfort but, ultimately, where a claim that impugns the IP's integrity or professionalism fails, the IP can at least expect to recover indemnity costs, the case of *Two Right Feet Limited (In Liquidation)* v. *(1) National Westminster Bank PLC (2) Royal Bank of Scotland PLC (3) KPMG LLP* [2017] EWHC 1745 (Ch) (where the claim was abandoned after disclosure and the defendants were awarded indemnity costs) being a good example of this.

Where next?

It remains to be seen whether the high-watermark for claims against IPs has been reached. What is notable is that none of the recent claims have resulted in a successful judgment for the claimants and that, where possible, claims have successfully been struck out at an early stage in proceedings.

> It seems inevitable that determined claimants will find new and ingenious ways to bring claims against IPs and their firms, as well as the means to fund them.

Perhaps, as a simple matter of economics, the more of these claims that fail – whether in the initial stages, or just before trial – the less appetite funders and insurers will have to invest in similar litigation in the future.

However, in the light of the contentious nature of insolvency work and the evolution of the law (particularly around conspiracy), it seems inevitable that determined claimants will find new and ingenious ways to bring claims against IPs and their firms, as well as the means to fund them. For now, these claims pose a real threat, and one which practitioners will be keen to avoid.

[1] And often also against the secured creditor who will be said to have influenced the insolvency practitioner.

[2] See *Ahmad & Ors v. Bank of Scotland, PwC & Ors* [2016] EWCA Civ 602 as a recent example. This claim was dismissed following an application for summary judgment.

[3] http://citywire.co.uk/wealth-manager/news/building-a-case-for-litigation-funds/a1033036

[4] Recent cases have gone even further and the Supreme Court recently stated that the requisite level of intention can be established where damage to the interests of others was merely a 'foreseeable consequence' of the act in question.

[5] See *Oldham v. Kyrris* [2003] EWCA Civ 1506.

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HMRC and insolvency work – our approach

Richard Hopwood from HMRC outlines a number of specialist insolvency functions within the department.

Insolvency work can be extremely complex and we want to make it as simple as possible for IPs to work closely with us. We have two overarching groups that IPs will predominantly interact with: customer services and customer compliance.

Customer compliance ensures HMRC successfully collects the correct amount of money due from UK taxpayers. Working closely with IPs is a vital part of this work. This article outlines some specialist compliance functions and how IPs can get in touch with HMRC.

> Customer compliance ensures HMRC successfully collects the correct amount of money due from UK taxpayers. Working closely with IPs is a vital part of this work.

Help in non-compliance cases

IPs may seek a nomination as liquidator or HMRC support in relation to cases where serious tax non-compliance is identified. Individuals and small business compliance (ISBC) deals with HMRC's largest and most diverse group of customers, and will consider supporting IPs who contact us directly seeking nomination or support (where there are compliance or insolvency risks identified and a clear benefit to the exchequer). If IPs are aware of insolvencies of this nature where HMRC is a significant or majority creditor, and there are potential claims against directors or others connected to the tax loss, then ISBC may consider taking the case up and supporting the request or will refer it on to the relevant HMRC team where appropriate – eg if funding is being requested. This also includes liaising with the Official Receiver (OR), who may retain the case where HMRC is not persuaded that there should be a change of IP. Should IP firms wish to seek support for nomination in the type of insolvency case referred to above then an initial referral should be sent to **isbc.insolvency@hmrc.gsi.gov.uk**.

If IPs are already appointed in a case and have seen indicators of deliberate evasion or tax fraud, then contact can be made with HMRC's fraud investigation specialists at **FIScivilrecovery.external@hmrc.gsi.gov.uk**.

Support for marketed avoidance

If IPs have cases where it is clear there has been marketed avoidance, then our counter-avoidance specialists are likely to have an interest. Counter avoidance's insolvency specialists aim to increase tax yield from insolvent users of avoidance products and to ensure insolvency is not seen as a way to escape avoidance debts. Where debts in an insolvency have arisen through marketed avoidance please email **ca.counteravoidanceinsolvencyexternal@hmrc.gsi.gov.uk** so we can support and assist you, whether that is in seeking your appointment as liquidator, or during a case you are already appointed to.

Customer services

Customer services, our second overarching group, supports millions of customers every year to get their tax, duties or tax credits right. Previous *RECOVERY* articles have outlined the work of customer services to better support IPs, eg the appointment of an insolvency customer service manager. There are also some specialist insolvency teams who can be contacted in customer services and who work with and support IPs (listed below).

> Counter avoidance's insolvency specialists aim to increase tax yield from insolvent users of avoidance products and to ensure insolvency is not seen as a way to escape avoidance debts.

HMRC's enforcement and insolvency service (EIS) is a team within customer service's debt management area. EIS is split into a variety of functions.

EIS Edinburgh

The Edinburgh service leads on debt enforcement and insolvency in Scotland and Northern Ireland, having responsibility for sequestrations, liquidations, debt arrangement schemes and trust deeds. EIS Edinburgh deals with all members' voluntary liquidations for the UK and can be contacted at: **eisw.mvl.team@hmrc.gsi.gov.uk**.

> There are also some specialist insolvency teams who can be contacted in customer services and who work with and support IPs.

EIS Newcastle

HMRC's insolvency claims handling unit in Newcastle lodges direct and indirect tax claims in IVAs, bankruptcies and sequestrations, administrative receiverships and liquidations (excluding MVLs). It prepares history reports for the Insolvency Service's director disqualification unit to support any action it may be considering. Contact: **insolvencyhelpdesk@hmrc.gsi.gov.uk**.

EIS Cardiff

Cardiff has responsibility for the majority of HMRC's company winding-up petitions for England and Wales. Contact: **teamc1.eisc@hmrc.gsi.gov.uk**. It now also works on new post-insolvency liquidations with support from EIS Worthing and a team is currently being trained to take over CVA and company administration work.

EIS Bradford

This service is responsible for applying for county court judgments. Additionally it now has responsibility for bankruptcy

Case studies – how HMRC works with IPs

A criminal investigation

The Fraud Investigation Service (FIS) civil recovery team's overarching objectives are to maximise recoveries, bear down on evasion and remove the profit from tax evasion. FIS manages HMRC's criminal investigations and its civil recovery team works closely with criminal investigators.

In one recent case, a company was criminally investigated in relation to a significant tax fraud through understatement of VAT. A criminal restraint order was granted over some of the company's assets.

During the course of the investigation, proactive civil recovery action was taken to prevent the company from causing any further VAT loss and to preserve and recover assets that fell outside of the restraint order. Those in control of the company failed in a court application to put the company into administration and it was placed instead into provisional liquidation and then liquidation. The liquidator worked closely with both HMRC's civil recovery and criminal investigators to pursue assets that had been transferred pre-liquidation. This resulted in over £5m being recovered, in addition to the criminal confiscation.

Marketed avoidance

A company went into liquidation after using tax avoidance schemes for the benefit of its two directors. The liquidator rejected HMRC's claim, which was brought from tax determinations raised against the schemes.

HMRC successfully challenged the liquidator's decision in court and, with its majority claim, replaced the liquidator. Working closely with the replacement liquidator, HMRC explained details of the scheme used by the company, the dates on which transactions had occurred and the amounts involved, as well as detailed information from the company's corporation tax returns. The liquidator considered the directors to have breached their fiduciary duties by allowing funds to flow out of the company for no benefit, incurring a tax debt as a result that rendered the company insolvent.

The liquidator issued letters before action, which resulted in the directors contacting HMRC to try to settle the company's tax liability directly in order to frustrate the liquidator's claim. HMRC refused and insisted that the matter be dealt with through the insolvency.

In the end a settlement was agreed amounting to the total tax debt plus the costs of the liquidation.

Compliance irregularities

An IP sought HMRC's support to be appointed in a compulsory liquidation case. The company owned a number of properties including a high value property that was sold for £600,000 shortly before the winding up. The IP identified a number of potential compliance issues:

- The sale occurred post issue of the winding-up petition and prior to the winding-up order being made. Therefore the sale appeared to be void under section 127 of the Insolvency Act 1986.
- The property was originally purchased for £250,000 and other properties had also been purchased and sold during the period of trading, giving rise to a suspicion that capital gains tax may be at risk because the company had failed to file company accounts for the two years preceding liquidation.
- Prior to the sale, a charge against the property had been taken out by another company registered in an offshore jurisdiction.

Following risk assessment within individuals and small business compliance (ISBC), a substantial tax debt was raised and a Secretary of State request was made, seeking appointment of the IP who had referred the case.

The IP instigated recovery action to overturn the sale of the property and bring a number of claims against the former directors, which saw HMRC and other creditors receive a dividend of 60 pence on the pound.

No grounds for appointment

An IP sought HMRC's support to be appointed in a compulsory liquidation case. The IP sought support on the basis that HMRC had been the petitioning creditor. No further details were provided highlighting either compliance risks or potential breaches of the Insolvency Act. The ISBC insolvency team advised that there were insufficient grounds demonstrated to warrant an intervention and they could not take up the case and provide support for the IP's appointment.

petitions in England and Wales and deals with annulment applications on those petition cases. Contact: **dm.insolvencytech@hmrc.gsi.gov.uk**

EIS Worthing

Worthing currently supports the debt enforcement work undertaken in Cardiff and Bradford. The team reviews and votes on individual and company voluntary arrangements where HMRC is a creditor, supporting viable proposals and businesses where published criteria are met. Together with EIS Cardiff, the team reviews all company administrations to ensure returns are maximised, with close monitoring of any new companies which may be connected to the one entering administration. It is also HMRC's specialist team dealing with rescission and annulment applications as well as fee resolutions on HMRC petition cases. All new work is being migrated to the EIS offices listed above with remaining legacy work to be moved by early 2021.

> Customer services, our second overarching group, supports millions of customers every year to get their tax, duties or tax credits right.

Key contacts: individual voluntary arrangements **eisw.vas@hmrc.gsi.gov.uk** and company voluntary arrangements and administrations **eisw.teamad@hmrc.gsi.gov.uk**.

Appropriate use of the above contacts should help IPs and HMRC work together more effectively to deliver lower costs and better returns to creditors, an objective I know that both HMRC and R3 members share. □

RICHARD HOPWOOD is head of the insolvency profession fraud investigation service at HMRC.

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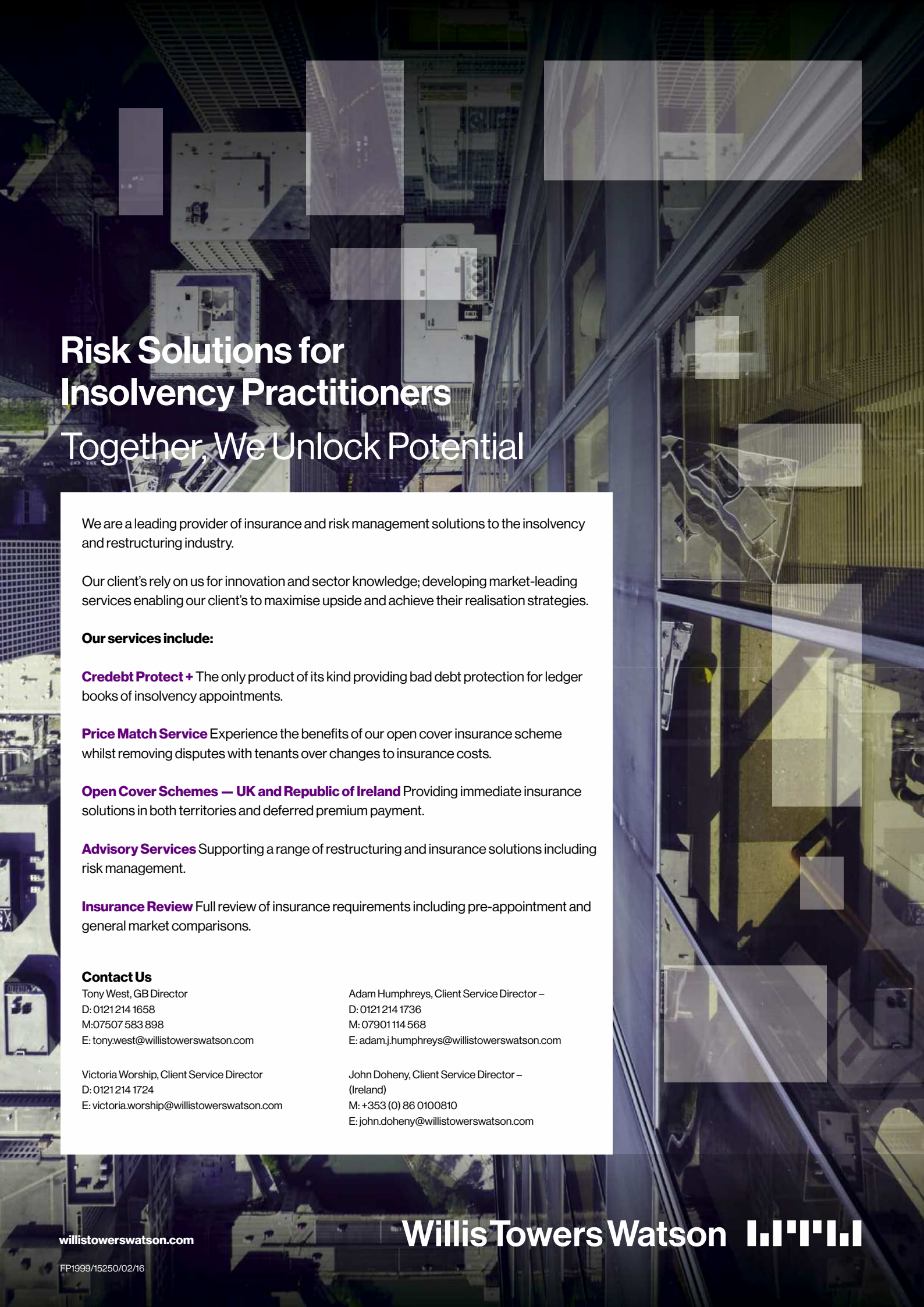

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Intangible riches, tangible risks: IPRs

Debbie Venn examines the legal issues relating to sale of intellectual property rights and databases from insolvent businesses.

Most businesses will own or license intellectual property rights (IPRs), including copyright, databases, brand names or other intangible assets such as software. Significant value can be derived from these assets, including goodwill attached to a brand, licence fees for selling software or manufacturing and selling invented products. However, businesses often fail to protect these intangible assets properly and realising value from them in an insolvency situation can cause problems.

How can IPRs be protected?

Some IPRs require registration (such as patents, registered trademarks or designs). It is easy for an insolvency practitioner to see if registered IPRs are protected, because the details will be on the applicable register. However, issues can crop up if the correct legal entity owning the right is not listed on the register. This can lead to concerns for purchasers over the rights that they might *not* receive if purchasing a registered IPR that has an inaccurate ownership record.

> If the business is 'IPR rich', there will be a huge amount of value placed on those assets.

Other IPRs exist automatically when they are created in a material form (and do not require registration), and allow the owner to stop others from copying those IPRs – eg copyright, unregistered trademarks, software or database rights. Some countries require the registration of copyright in order to enforce your right to claim damages for unauthorised use (eg the USA), but this is not required in the UK or Europe specifically for the IPR to exist as a protected right.

What might affect the value of IPRs?

IPRs can be vulnerable to a diminution in value because:

- The business entity may not be the sole owner – if ownership records for registered IPRs are not updated, then the registered owner might not be correct or there might be joint ownership issues to consider.
- If the business entity did not update its contact records, then notices of renewal may have been missed and registered IPRs may be revoked for non-renewal.
- If patent or trademark attorney fees »

have not been paid by the insolvent business (including any applicable renewal fees), then they might refuse to act until they are paid, which makes it difficult to get information relating to the registered IPRs already in place (or in the application process).
- If registrations are not complete, there may be problems with the continued prosecution of the registered IPR. Where this is only an application, the value of the IPR can reduce, particularly if it is quite early on in the application process. This means the IPR may be more vulnerable to not being granted or encountering registration issues along the way.

> Try to secure some written detail and explanation of know-how within the business to harness this and add to the value of the IPR asset list.

- Registered rights may also be vulnerable to revocation or attack from third parties where IPRs are not used for a significant period of time, eg five years. Evidence of use of the IPRs is helpful to show that the IPR is still valid and should not be vulnerable to attack.
- In terms of value of the IPRs, where a royalty or income connected to an IPR is payable, such payments may reduce over time. This is common where the product sold that is the subject of the IPR has a peak or short-term shelf-life.
- Is there any security granted over the IPRs specifically that needs removing prior to a sale? This needs to be considered and appropriate checks made at Companies House for any registered charges.

Sale of assets protected by IPRs

It is important to consider the type and nature of the business or assets that an insolvency practitioner might be seeking to sell. This is in order to determine pitfalls a purchaser would be aware of when looking at the business and its assets in respect of value and risk. If the business is 'IPR rich', there will be a huge amount of value placed on those assets. However, this can be diminished if the registration records for IPRs are not accurate, have been allowed to lapse or if contracts are (or are not) in place with other third parties involved in the development or commercialisation of the IPRs. This places restrictions or encumbrances on the IPRs, freedom to operate and realisation of the value in the asset. For example, if the business entity is a software licensor and has escrow arrangements in place with a third party so that in the event of a licensor becoming insolvent, its existing customers obtain release of source code from the escrow agent to the customer, then the value in the software is likely to reduce. The source code (although generally restricted to the customer's own internal use under licence in the event of such a release) will have been released and this may affect the ability for any purchaser to obtain similar value for licensing the software in the future.

Sale of databases

In addition to general potential IPR issues on a sale, databases throw up further issues. Where the data included within the database contains personal data or other commercially sensitive or confidential information, it may add further risk to the asset being used freely.

Database as an IPR: databases can hold significant value if, for example, it's a business' mailing list or customer records, as this will help build up value in the business and goodwill in connection with a business' revenue. If there is sufficient investment made in putting a database together in a systematic and methodical way, then the database may attract 'database right'. 'Database right' is an IPR and gives the owner a 15-year right to stop others from copying/reproducing all or a substantial part of the database.

If a database has been created using other third-party data, then a business will want some assurances from that third party that the data held within the database can be included for two main reasons: (i) to ensure that the data is not an extract from, or otherwise takes a substantial part of another third party's database; and (ii) if the database includes any personal data, then any relevant permissions or legal basis for processing that personal data by holding it within the database for a specific purpose have been obtained.

> IPRs can be difficult to put a value to, particularly if they have not been commercialised yet and there is no set royalty, licence fee or other income attached.

Data protection issues: when looking at a database, in addition to any database right, there is the possibility of the database including personal data or sensitive personal data about individuals. If it does, then the data controller of the data within that database will have responsibilities under the General Data Protection Regulation (GDPR) and/or the newly revised Data Protection Act 2018 (if the data relates to individuals in England and Wales). Purchasers generally want some reassurance that any personal data included within the database has been handled in accordance with applicable data protection laws. However, as an insolvency practitioner, you would not want to be giving any warranties or reassurances about this.

Where a database operated by an insolvent business entity is being sold, limited checks can still be made about how the personal data was dealt with – for example, checking what privacy notices or policies were in place when the data was collected and looking at the entity's record of processing activities to see how the data was used etc. This will show how the personal data was dealt with, will comfort a potential purchaser and will hopefully preserve value in the database itself, offering limited assurances in connection with the data included within the database.

Office-holder IPR checks

There are many assets in a business that include IPRs, but the following checklist will help insolvency practitioners gather relevant information pre- and post-appointment, as well as manage the assets during their appointment and any asset realisation arrangements entered into. Office-holders will need to:

- Review the assets of a company to assess how realisable they are and on what basis.
- Consider what IPRs the business actually owns (or licenses).
- Consider what intellectual property licences are in place and check the terms, ie,:
  - Licensing out its own IPRs to third parties; or
  - IPRs that the business receives a licence to use.
- Stress the importance of purchaser due diligence on any potential purchase of IPR assets due to the limited nature of an office-holder's position and ability to give any warranties relating to the assets, and their more limited knowledge around the development and lifetime commercialisation of the IPRs as an asset.

Checklist for IPs selling IPRs and databases

Registered IPRs will need to have up-to-date checks made on the relevant registers to see if the records are correct. It is sensible for an insolvency practitioner to contact intellectual property registers and direct all future communications to them (or continue through any appointed patent and trademark attorney), to keep records up to date. When a potential purchaser is found, any sale/purchase agreement for the IPRs includes a provision to place an obligation on the purchaser to undertake all relevant steps (at their cost) for updating the registers, as applicable.

Office-holders might be able to put the purchaser in touch with the patent/trademark attorney that has been dealing with any IPR registrations on behalf of the insolvent business to ensure this happens quickly, but also to try to get reassurance for the patent/trademark attorney that their fees will be paid by the purchaser moving forward (eg for renewals of registrations and any recorder fees for noting the transfer of ownership) to remove that cost from the administration and the practitioner.

> You should also be watching out for infringements of IPRs in your custody and bring proceedings where necessary to stop it.

There is a risk of *losing know-how* in the business where key personnel leave the business. Where possible, try to secure some written detail and explanation of know-how within the business to harness this and add to the value of the IPR asset list.

Although the office-holder is not going to be giving any warranties in relation to the IPRs being transferred to a purchaser, if there are any *ongoing legal proceedings* in connection with that IPR it may diminish the value of the IPRs.

IPRs can be *jointly owned, or licenced* to a business by a third party. If the IPRs have not been created by the business itself, or by contractors/third parties who have signed an assignment of IPRs to the business, then a purchaser will generally have concerns as to ownership of rights in the IPRs. Where possible, office-holders should try to gather evidence that the IPRs have been sufficiently handed over to the business entity, eg, by deeds of assignment of IPR or contracts. Joint ownership can also cause problems (1) if there is an agreement in place that allows the other joint owner to claim full ownership and terminate any joint commercialisation of the IPRs in the event that the other business entity becomes insolvent; (2) or generally in terms of value of an asset if any future commercialisation has to be done in conjunction with (and share royalties with) another joint owner.

Intellectual property valuation: IPRs can be difficult to put a value to, particularly if they have not been commercialised yet and there is no set royalty, licence fee or other income attached. You may have to instruct an intellectual property valuer in order to assess what value is attached to the IPR, in order to help ascertain value and a suitable sales price for the practitioner to set for a purchaser.

In the interim period of holding office, an insolvency practitioner should keep a *watchful eye on intellectual property* in their 'custody', ie, ensure the rights are renewed (where appropriate) so that registered IPRs do not lapse (and therefore lose value), including ensuring that any licensees are abiding by the terms of their licences and paying any ongoing licence fees. You should also be watching out for infringements of IPRs in your custody and bring proceedings where necessary to stop it.

On a practical level, any laptops, USB sticks or other files (physical and electronic) that contain details of the business' IPRs should be kept under control and ex-employees should be required to return such devices and delete all relevant information from any of their own equipment to protect the confidentiality of the IPR assets.

Risk and reward

IPRs can be an extremely valuable asset responsible for deriving a business' income. However, if a business has become insolvent and the assets are being looked at by an office-holder, it is important to consider the potential risks involved to understand how this might affect the achievable value of those assets in a transaction, and what you can do to help realise greater value while holding office. Particular care should be taken when looking at databases and it is important to consider potential legal pitfalls and what other rights might exist under data protection or other laws. □

> Particular care should be taken when looking at databases and it is important to consider potential legal pitfalls and what other rights might exist under data protection or other laws.

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Beating the bureaucracy: blockchain adoption

Darren Bradshaw and **Christopher Dunn** look at some of the changes blockchain is already bringing to transport and shipping.

There are a number of reasons an insolvency practitioner needs to understand the movement of goods in which an insolvent company has been involved. For example, there may be a suspicion that a logistics company or supplier has been involved in missing trader intra-community (MTIC) fraud. It may be necessary in a trading insolvency quickly to understand a company's trading and be able to continue to trade seamlessly. Or it might be necessary to establish the location of an item at the date of a company's insolvency to demonstrate that the company has title to that item.

Blockchain can assist in providing this information. Barely a day goes by without an announcement on the introduction of blockchain and traceability in insurance, supply chains and automating commercial processes. Maersk and IBM have partnered to introduce blockchain technology into the global shipping and transportation industry. DHL has issued a trend report in cooperation with Accenture on blockchain's potential to transform the logistics industry. However, the question remains, just what is it?

Shared platform

Blockchain is a distributed ledger technology platform designed to enhance the efficiency and security of global cross-border trading. Users log and process all elements of a shipment via the platform including data sharing, payments and documentation. Blockchain maintains records and authenticates data and transactions.

Speed, efficiency and savings are the primary reasons companies in the shipping and transportation sector are adopting the blockchain platform. At present, cross-border transportation of goods is subject to substantial amounts of hard copy documentation and bureaucracy that ultimately costs the end-customer. IBM estimates that the current system costs up to a fifth of the total expense of physical transportation in trade documentation, wasted time and inefficient bureaucratic systems embedded within the supply chain.

Blockchain seeks to eradicate these issues and modernise the transportation supply chain to the benefit of all users. The platform's ability to track freight and eliminate paperwork via a shared digital log will help to streamline the industry's practices and reduce administrative costs. It is hoped this will ensure a secure and seamless exchange of shipments between those within the supply chain.

Early adopters

Recent decisions to embrace technological and procedural change within the shipping industry have prompted calls to digitise processes and provide a secure platform to enable movement of funds and data between parties. This is not least in response to growing concerns over cyber-security and associated fraud. Blockchain purports to offer an IT system far better equipped to deal with and prevent these risks.

> **Participants within the industry will face pressure to subscribe to the blockchain system or risk being shunned in favour of dealing with those who already do.**

The decisions from industry giants such as Maersk will undoubtedly persuade others at least to consider embracing the technology. The Maersk-IBM venture proposes to sell software subscriptions to all participants within the supply chain. The costs of the subscription will be presented and justified as an overall saving when compared to the current costs incurred from the inefficiencies embedded within the supply chain.

Should the platform prove successful following its implementation, participants within the industry will face pressure to subscribe to the blockchain system or risk being shunned in favour of dealing with those who already do.

Maersk and DHL have recognised that the success of the platform will depend on the acceptance of all participants. It is currently being tested by various market players including DuPont, Dow Chemical, Tetra Pak and US Customs and Border Protection.

Ultimately, the blockchain venture is designed to achieve significant costs savings for all participants by reducing inefficiencies across the supply chain.

The new normal

Notwithstanding the reasons for the transport and logistics industry introducing these innovations, IPs can potentially take advantage of these technological advances to assist them with seamlessly continuing to trade when taking on a trading appointment, which can add value to a business or establish whether a company has title to particular items.

It would also provide a powerful tool in assisting the insolvency practitioner as to whether a company has been involved in, for example, MTIC fraud or to investigate the affairs of the insolvent company or the conduct of its officers.

While the benefit and impact of blockchain will take several years to emerge, the platform is not about experimentation. The level of investment in the technology is substantial and is likely to be a 'new normal' in the shipping and logistics markets in the not too distant future. IPs should be alive to the developments in this area now to fully understand how they might assist them in their insolvency appointments. □

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Fahrenheit GDPR – data destruction

Mark Iwaszko lays out the GDPR-compliant data destruction principles for insolvency related cases.

It has never been more important to handle data, books and records, and working data sets, in the correct manner. The GDPR and the new Data Protection Act 2018 (DPA18) have brought fresh challenges to the whole lifecycle of recovery and restructuring-related cases. There are now significant risks, potential reputational damage and large fines associated with non-compliance.

This article gives guidance on the current best practice for data destruction and retention policies relating to recovery and restructuring cases.

> The GDPR has focused people's minds on both new and historical obligations, highlighting the risks and penalties for non-compliance.

Seek and destroy?

The requirement to destroy records when they are no longer needed has been common practice since the Data Protection Act 1998 (DPA98), normally upon closure of a case. While most have adhered to destroying physical paper files and boxes, which reduces storage costs, few professionals concerned themselves with the destruction of electronic books, records, case and working data. This historically may have been overlooked because of the effort required to find, destroy and certify multiple low-cost electronic stores containing data.

The GDPR has focused people's minds on both new and historical obligations, highlighting the risks and penalties for non-compliance. The DPA98 definition of 'retention' has been replaced with the GDPR's 'principle [e]: storage limitation' and enshrined within the DPA18.

Recent Insolvency Service guidance in the March 2018 issue of '*Dear IP*' (number 80, chapter 10) helps here indirectly; it specifies that:

'When seeking information about an insolvent entity and to carry out an initial assessment, an IP is required to secure and list the books and records (in whatever form) in compliance with SIP2 and ensure that they are then used to discharge statutory duties placed upon them.'

Without accurate record keeping and documentation, certifying the deletion of both paper and electronic records is virtually impossible. Where books and records are to be collected these must be catalogued, risk assessed and stored separately from any working files or other unrelated case records.

These books and records have a data lifecycle from capture through to destruction, as do the associated working papers and data sets for a case. Correct categorisation of the case type and document contents allows a correct initial application of the relevant retention periods. This ensures the records are being handled according to all legal and regulatory requirements, and that they are meeting compliance obligations, particularly with respect to GDPR, DPA18 and insolvency regulations.

> Correct categorisation of the case type and document contents allows a correct initial application of the relevant retention periods.

Working files and additional copies derived from the original case data must then be tracked and categorised, giving a full picture or 'data map' of the evolution of that case data. This will ensure you can track a full data lifecycle when the time comes to destroy it. Final documentation »

can be added at the point of destruction to provide auditable proof that the records have been destroyed in the correct and compliant manner.

GDPR-specific items

The aforementioned GDPR storage limitation principle stipulates data should not be kept for any longer than is necessary. Data no longer required should be removed immediately. This includes captured books, records and subsequently created case working data sets. Therefore, it is best practice to perform regular and documented reviews of the data you hold to ensure you're not breaching your retention policies or GDPR guidelines.

> GDPR specifies you must establish, and have clearly documented, consistent data retention and destruction policy standards.

GDPR specifies you must establish, and have clearly documented, consistent data retention and destruction policy standards. The retention periods should also be individually specified for the different categories of information held. With respect to restructuring-related cases it is prudent to define these policies for each case type, such as administration, CVA and IVA. Furthermore, within each case type, policies should encompass more detailed definitions for the type of data handled, such as internal working papers and data sets versus original company books and records. The sensitivity of other documents' contents, such as medical records, should also be considered.

There may be an opportunity to destroy data at an early stage before it reaches its retention expiration. Your policy and systems should accommodate this option with, for example, the early destruction of duplicates of working files or records for investigations once no longer required. Where an earlier destruction date is agreed, this must be fully documented and approved by the office-holder, including the reasons behind the decision.

You should also be mindful of the new 'right to erasure' or 'right to be forgotten' principle. The Information Commissioner's Office (ICO) states that 'If a valid erasure request is received and no exemption applies, then you will have to take steps to ensure erasure from backup systems as well as live systems.' It would obviously be complex and time intensive to selectively delete records, so thought should be given as to the best way to achieve this in advance to avoid significant disruption during the management of the case.

GDPR goes beyond the original DPA98 in specifying that you can keep and maintain 'non-personally identifiable data' for as long as you want to. Keeping data for longer than you need may be unnecessarily expensive and increase other related risks. However, if the personal data you hold is sufficiently anonymised, or 'key-coded' (pseudonymised in GDPR terminology), to completely prevent identification, then it can be held securely and legally within systems, backups and archives.

This pseudonymisation, essentially overwriting personally identifiable information, allows for easily targeted specific personal data removal rather than bulk record deletions, and is GDPR and DPA18 compliant.

Destruction cost considerations

Costs of destruction are an expense of the estate. Recovery of these costs should be considered a part of the overall case strategy.

The time taken in logging and documenting the erasure of records, as well as the case closure workflow process, should not be underestimated. They should also be included in the cost of recovery. Where possible, storage and destruction costs should be recovered from the case, especially where this can be separately identified on a third-party invoice.

> Keeping data for longer than you need may be unnecessarily expensive and increase other related risks.

Data classes for retention and deletion

Consideration should also be given to the lifecycle of the different data and records depending on their origin and usage. Initially captured data will give rise to newly created data siblings and duplicates for various uses during the case process.

The primary sources of data relating to recovery and restructuring cases generally (a) company/debtor books and records (both paper and electronic) and (b) initial working documents created as part of the case setup.

Working files and copies of the original company records and accounts normally expand within the typical case lifecycle to build case-working data sets, which comprise all or some of the following examples. Each of these items will need to be tracked for retention and future erasure compliance:

- Working files and emails
- Original company or debtor books and records (along with second copies or backups)
- Servers, computers or data storage devices from the original company
- Creditor portal
- Data rooms
- Cash collection and case management platforms
- Investigation platforms
- Third parties (these may become data controllers in their own right, which means they will have their own retention policies and destruction obligations)
  - Lawyers
  - Valuers
  - Debt collectors
  - Other agents.

Exceptions

GDPR and the DPA18 allow exceptions to the documented retention and erasure policies under certain circumstances. These circumstances need to be justified and documented, taking into consideration the impact of data retention on an individual's privacy against its fair and lawful use.

An example of this would be personal data that might be required to defend a future legal claim or investigation. Relevant data should be retained until that investigation or claim is complete, however records or information not relevant to such a claim should still be deleted once the defined retention period has ended or it is no longer required.

GDPR specifies that information held for longer than is necessary carries additional risk and cost. As such the validity of any exceptions to the standard retention policies must be regularly reviewed and their suitability continued to be justified.

Expiration of retention period

Systems should be implemented that regularly check for the retention expiration of data. This can be automated or manual; however, automated diary reminders and data tracking systems are the most effective way of ensuring you are able to meet your data erasure responsibilities in a cost-effective manner.

Once a data retention point is reached, either as part of a review or as part of a case closure workflow, authorisation for the deletion of the associated data needs to be sought from the appropriate authority on the case. The approval for erasure must be documented before the deletion process is commenced, then subsequent auditable and documented proof of destruction recorded.

Destruction of data – company records and working data

Once data and records approach their retention expiration or the information is no longer required, predefined actions should take place to ensure that the data is securely destroyed or, where applicable, anonymised.

A workflow of case closure and the destruction process should include an erasure instruction validated by the IP or relevant case authority and should be

documented. Erasure instructions can then be given to storage agents, internal and external, to destroy both hard copy and electronic client data wherever it may be held for that case. Confirmation of the destruction of the record data sets must be obtained from each party and filed against the case along with disposal certificates and documented proof of destruction where applicable.

> If the electronic media is to be reused, it must be first wiped using multi-pass disk sanitiser software.

Simply taking data offline does not constitute secure erasure or deletion. While it reduces its availability and risk of misuse, you are still deemed to be processing personal data if you are holding or storing it and it is still protected by DPA18 and GDPR legislation.

Because of the various types of electronic storage platforms, the ICO recognised that it may not be possible to delete or erase all traces of data and records, but reasonable steps must be taken to put such data beyond possible use both on live systems and on back-ups and archives.

It is expected that expired data from live systems is deleted on or before the data retention period end point; however, data may remain in a backup environment for a short period of time until it is overwritten by a regularly scheduled process. However, even in these cases access to this data must be tightly controlled. There should be no intent for the data to be used for any other purpose to minimise the risk of breaching compliance. The ICO use an analogy of having a bag of shredded paper waste – although it may be theoretically possible to reconstitute the information it would be extremely difficult to do so.

There is a helpful ICO guidance document called 'deleting personal data', which will soon be updated for the DPA18.

Storage models for data deletion

There are many different storage models where electronic data is kept and different permanent deletion techniques will be required for each. Some common examples are given below:

Case management systems should be purged of all personally identifiable data. Anonymising or overwriting this data in place may be more suitable than trying to delete relational data records.

Emails – case-related emails should be stored as part of the working data set and should be deleted as part of the regular erasure process. While searches across email systems are possible, they are time consuming. Staff should be encouraged to move emails into a case management system.

Automatic email journaling of every message is not uncommon for disaster recovery or backup purposes; however, if you have this in place then you should consider how you delete these journaled emails.

Microsoft Office 365 – OneDrive keeps files in its first stage recycle bin for 90 days, then deleted files are migrated for a further 90 days in the second stage recycle bin. You can permanently delete files from within either recycle bin.

Google keeps files in its trashcan for 30 days. You can permanently delete an individual file from within the trashcan or empty your entire trash.

Dropbox permanent delete is achieved by opening the web client, showing deleted files and choosing the 'permanently delete' option. Dropbox keeps files in its trashcan for 30 days; if you sync Dropbox files to a local machine there is also a local cache where files may be accessible after 30 days.

Cloud Private, Azure, AWS – private, hybrid and public cloud offerings have their own particular backup, snapshot, retention and resilience policies. Each supplier should be contacted to ensure all copies of the data are deleted in a GDPR compliant manner.

Network attached storage (NAS) drives, USB devices, CDs, tapes and archives or other direct data storage media should be wiped using industry standard processes, detailed below.

Assets for sale or disposal

When an asset, which may contain electronic storage media, is sold or allocated for disposal, it must first be cleared of any residual data that may contain personally identifiable information.

Mobile phones, tablets and other mobile devices usually have a robust data wipe feature. It is advisable to ensure that the device is unlocked and that a linked Apple or Google account is removed before it is reused to prevent personal data from being transferred.

Smart devices beyond that of ordinary computers, tablets and phones are an additional consideration for data deletion on disposal or asset transfer. Personal data can also be stored within car computer storage systems as extensions of the driver's mobile devices, as well as holding its own personal and tracking data.

If the electronic media is to be reused, it must be first wiped using multi-pass disk sanitiser software and the wipe must be processed, verified and documented. Software, such as Active@'s *KillDisk*, destroys all data on hard drives or USB devices and provides erasure certification. *Darik's Boot and Nuke* is a free, open-source alternative data-wiping software tool. *Blancco* is a hardware device drive eraser, which can erase multiple drives at a time giving a digitally signed certificate of proof of secure erasure.

If the hardware is not to be reused, there are many companies offering secure collection and destruction of electronic media. Companies should meet the HMG Infosec Standard 5 for secure erasure as well as the WEEE – HSE standards for recycling and disposal.

The HMG Infosec Standard 5 is particularly applicable for GDPR compliance as the Infosec Standard 5 procedures specify that it is not sufficient to just sanitise the media, but the process must be auditable, and records must be kept.

Conclusion

To reduce risk and retain compliance with the legal regulatory frameworks of GDPR and the DPA18, data retention and destruction for recovery or restructuring-related case work must be handled in an efficient, considered and well-ordered manner.

> It is advisable to create a regular data retention review process and case closure workflow to document auditable proof of destruction.

Case or working data collected or created should be categorised to conform to a standard retention policy. At the point a data retention period requires review and destruction, most of the hard work will then already be done, resulting in time and cost efficiencies.

It is advisable to create a regular data retention review process and case closure workflow to document auditable proof of destruction and the authority under which it was carried out.

Adhering to the above will demonstrate that the utmost has been done to ensure records are being handled according to GDPR and DPA18 requirements, and meeting compliance obligations with respect to insolvency regulations.

MARK IWASZKO
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Knowledge is your shield from online fraud

Callum Fraser explains how the Met Police helps raise awareness of fraud and cybercrime, and offers up some perfect password pointers.

Knowledge is power. But is this always true? Knowing that someone has a knife to your throat doesn't stop a robbery. Hearing someone downstairs and knowing they're trying to steal your laptop doesn't stop a burglary. In fact, fraud is pretty much the only crime where knowing that it is happening stops it from happening.

Fraud requires a victim's willing (if duped) participation. Without that, the criminal fails. So how come 30 per cent of all crime in England and Wales last year was fraud?[1]

Sadly, that's a question to which there isn't a single, easy to find answer. But we can certainly try!

The Metropolitan Police Service FALCON (Fraud And Linked Crime ONline) unit has a team dedicated to preventing, and protecting, businesses and individuals from fraud and cyber crime.

How? Well, it involves three stages. The first stage is raising awareness: if you're aware that payment fraud, romance fraud or computer software service fraud are different methods that criminals use, then you're less likely to fall for them.

We raise awareness by reaching out to the community and telling as many people as possible. We've created a series of print booklets that detail the most common methods that criminals use. We call them the *Little Book of Big Scams* and the *Little Book of Cyber Scams*. They're free to download from the resources section at **www.met.police.uk/fraud**, and we can send out paper copies by the boxload for free.

We also have a series of videos, available in the same place, that describe some of the more common fraud types and give tips to keep you safe online. In addition, we can visit companies to give presentations or run table top exercises with Lego (yes, Lego!) to help raise awareness.

Once your awareness is raised, then comes the next part – behaviour change. Knowing that you ought to update your computer regularly is one thing, but how many people still click on the 'remind me later' button?

The third stage is changing the system. The latest advice from the National Crime Agency is that if you have a strong password, there is no reason to change it every 30 days. So why do many companies still have that as their security policy?

> "Fraud is pretty much the only crime where knowing that it is happening stops it from happening."

The essential password tutorial

With all of the above in mind, and painfully aware that I'm trying to cram an entire presentation into a magazine article, what tips can I impart to you to be safer online?

How about passwords and online security? Passwords are everywhere and often people use the same one for everything, or use a fairly simple one. Since it's usually the first line of defence, it's worth taking time to create one that's hard to crack but easy to remember.

Here is what we suggest. Take three random words. In our video example we use 'fish', 'boat' and 'tulip'. The next step is to put them all together and capitalise one letter in each. So, we now have 'fisHboaTtulip'. Then we pick an easy-to-remember number: 1995. We split that up and put 19 at the beginning and 95 at the end.

So, we're now at '19fisHboaTtulip95'. Let's put a couple of exclamation marks at the end, just to finish it off. So, we're now looking at a final password of '19fisHboaTtulip95!!' The password appears complicated, but, if you've followed the process, it's easy to replicate.

That's the example that we give in our animated advice videos, but as you're clearly an intelligent reader, I'm going to go one step further. Create your perfect password, and then never use it.

Crazy, right? But here's the trick. You can use the same base password, but change the beginning for each use. Need a password for Facebook? Try 'FB-19fisHboaTtulip95!!' LinkedIn? 'LI-19fisHboaTtulip95!!' The good thing about this is that if you want to write down your password, you can. As long as you miss out the '19fisHboaTtulip95!!' part, which clearly you've committed to memory, then no-one will ever work it out.

Multi-factor security

Finally, I'll briefly mention multi-factor authentication. Most secure systems allow access based on one of three things. Something you *have* (a card or token), something you *know* (a password) or something you *are* (fingerprints or facial recognition etc). The best security systems work on two or more of these. For example, you can't get into a police building if you've stolen my warrant card because you'll need my PIN. Seeing my PIN won't work without my card. You need both.

Many websites (Facebook, Gmail, Amazon, etc) have two-factor authentication. You can download an app onto your phone that will generate a code at random. Whenever you log in to these websites from a new location, you'll need to type in the randomly generated code from the app. No phone, no entry. In other words, if you don't have your phone you won't gain access – and neither can the criminals.

If you want to know more, or would like FALCON (or local officers) to come to your business, please get in touch by emailing **falcon@met.police.uk**. And please, check out the various resources online.

After all, knowledge might not always be power, but lack of knowledge is always a weakness. □

[1] *Crime Survey of England and Wales* – year ending December 2017.

DETECTIVE CONSTABLE CALLUM FRASER is a FALCON cyber prepare officer with the Metropolitan Police Service.

News affecting the profession

Kelly Tolhurst MP has been appointed as insolvency minister, following **Andrew Griffiths'** resignation from the role.

Recent public consultations affecting the insolvency and restructuring profession include: a BEIS consultation on **corporate governance**, a Treasury consultation on **tax abuse** and insolvency, DWP consultations on the **future of defined benefit pensions** and the **Pensions Regulator's powers**, a government review of **airline insolvencies**, the Treasury Select Committee's inquiry into **economic crime**, the independent review of the **Financial Reporting Council**, and a Labour party review of the UK's **financial and professional services regulation**. R3 has submitted responses to all of these.

'The government's 'insolvency and corporate governance' consultation proposals would fundamentally change aspects of the UK corporate landscape and culture, and would undermine the UK's attractiveness as a place to do business.' – R3 on the government's corporate governance consultation.

Since the last edition of *RECOVERY*, R3 has met **13** parliamentarians, including Chair of the BEIS Select Committee **Rachel Reeves MP**, and **5** journalists at national media outlets.

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are delighted to announce that

STEPHEN BAISTER

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CHIEF BANKRUPTCY REGISTRAR OF THE HIGH COURT

has joined Chambers' Mediation Group

Stephen will act as a mediator primarily in insolvency, insolvency-related and company law cases but will consider appointments in other commercial law disputes where appropriate.

Stephen was appointed as a bankruptcy registrar of the High Court in 1996, serving as chief registrar from 2004 until his retirement in 2017. He continues to sit as a deputy Insolvency Judge in the High Court. He is a Member of the Chartered Institute of Linguists, an honorary Member of the Insolvency Lawyers Association and an honorary Fellow of the Chartered Institute of Credit Management of which he is also president. He was made an honorary bencher of Lincoln's Inn in 2017.

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Insolvency dispute resolution: options for IPs

Mark Beaumont provides solutions for funding and insurance of medium-value claims.

In the last issue of *RECOVERY* I looked at lower-value claims and strategies to secure quicker settlements, especially the use of low-cost after-the-event (ATE) insurance to shift the perceived balance of risk away from the IP and onto the defendant.

Low-value cases are often the subject of discussion: there are more of them and they tend to be perceived as being harder to fund and insure, so it's important to educate practitioners about all of their options (and, just as importantly, the professional risks of not considering these options).

In this article I'll switch focus and look at some of the common mistakes made when securing funding and insurance for claims of £1m plus.

> "Insurance to protect from adverse costs risk is an obvious route to go and can also be useful in the event of a security for costs application."

Covering costs

Typically medium-value claims will run on conditional fee agreements (CFAs), whereby the lawyers defer their fees to the successful conclusion of the claim. Often, these kinds of cases would benefit from a sensibly priced, and sensibly staged, ATE policy. Given that ATE can be secured for zero upfront fees, this is a common route to go down and allows for the premium to be paid from a successful recovery upon conclusion of the claim. If the case settles early, then the premium to be paid would be very low (10–15 per cent of the level of costs cover sought). If the case runs all the way to trial, you would expect to pay in the region of 40 to 75 per cent of the amount insured (typically, the amount insured is your opponent's expected costs).

> "The best advice is to seek at least three quotes or risk exposing your practice to accusations of negligence further down the line."

Insurance to protect from adverse costs risk is an obvious route to go and can also be useful in the event of a security for costs application. Either the ATE itself can be put up as security, or the policy could be endorsed or bonded to provide greater levels of security to the defendants. This is a cost-effective way of dealing with security and can be considerably cheaper than fighting the application.

In addition to adverse costs risk and security issues, ATE can also be used as a way to protect the costs of your own claim: cover your owns costs with ATE and, in the event an unfavourable ruling in the case, the insurance would pay you the costs you've incurred in taking the case to that point. Insurance of this nature can protect lawyer's fees and disbursements, including investigation costs.

Once your 'own costs' are insured then it can be much easier for, as an example, a creditor to fund the claim as the decision to fund would no longer be so risky. If third-party funding is needed, then the existence of insurance can reduce the costs of funds from a multiple of 3 to a multiple of 0.5 (ie from 300 per cent to 50 per cent).

On larger cases, lawyers may be unable to carry huge amounts of work in progress (WIP) for extended periods and so funding of at least some of the legal fees may be necessary. In these circumstances it is often third-party funders that are approached directly. This is obviously good news for the funders, just as it would be good news for a buyer if you were selling a property and only approached one buyer and accepted their best price.

Example: a claim for £1.5m.

Own costs estimated at £300,000 to court, and similar for the defendants.
If the claim settled for £600,000 around the disclosure phase, the costs of the ATE would be £66,000 (22 per cent of the £300,000 adverse costs insured). If, however, the claim were to run all the way to trial and lose, the IP would pay nothing for the ATE and yet the insurance would cover the adverse costs of £300,000 awarded to your opponent.

Don't just take the first quote

The best advice is to seek at least three quotes or risk exposing your practice to accusations of negligence further down the line. In practice, this would mean having relationships with a wide range of funders, as it's unlikely the same three funders will be appropriate for every claim.

> "There is no reason for good cases to 'wither on the vine' any more, and there's certainly no good reason to pay through the nose for funding – simply explore the market and get the best options for your case."

Of course, many IPs may just rely on the solicitors to secure funding and insurance. Unfortunately, solicitors often have little experience in these areas too, and those that do may have 'pet' funders that they have reciprocal relationships with. I'm not sure how this would be viewed as in the best interests of creditors.

With well over 30 funders now operating in the UK market, and around 20 ATE insurers, there are a wide range of options for funding and de-risking insolvency disputes. There is no reason for good cases to 'wither on the vine' any more, and there's certainly no good reason to pay through the nose for funding – simply explore the market and get the best options for your case.

MARK BEAUMONT is co-founder of Annecto Legal Ltd, an FSA-regulated, full market broker accessing litigation funding and ATE insurance for a wide range of insolvency and commercial disputes.

GDPR… the initial repercussions

Lorraine Surlis says that GDPR is not a piece of new software to be used, but rather a series of continuous updates that will need to be regularly maintained.

The European Union's General Data Protection Regulation (GDPR) isn't a destination, it is a journey. An organisation could have been compliant on 25 May, but does it remain compliant over three months later? This isn't the end of data discussions.

The GDPR replaced the Data Protection Act 1998 this May. The length of time an organisation has to comply with a subject access, 'right to be forgotten' or personal data request will never be the same again. Below, I seek to answer the two questions that have regularly filtered through to me since 25 May.

- What has changed since the introduction of GDPR?
- What are firms doing to ensure they remain compliant?

What's changed?

Since the day GDPR came into force what has really changed? We have already heard that the Security of Network and Information Systems Directive is now in force and the ePrivacy Regulation is on its way. We are still receiving emails from various companies whose mailing lists we have possibly signed up to over the years: seeking approval to send newsletters, announcing changes to privacy policies, adding pop-ups and legal notices to sites and witnessing barriers being placed from (as yet) non-compliers. Some US-based sites have even blacklisted access by data subjects in the EU until they are GDPR compliant.

> **GDPR has given people in Europe more control over how organisations collect and use their personal data.**

GDPR has given people in Europe more control over how organisations collect and use their personal data. We've already seen how, on the first day of GDPR coming into effect, big names like Google and Facebook were hit with lawsuits and possible penalties of up to four per cent of global turnover. Both companies have released policies and functionality to comply with GDPR, but we can still see the areas where the collection of consent is a very 'all or nothing' move by the tech giants.

> **When we were preparing our GDPR readiness roadmap, we looked at every piece of personal data we collected and used, from our employees to our customers.**

Data security is at the heart of GDPR and it is always a good time for companies to look at their security hygiene. GDPR highlighted the need for us to be continuously monitoring our infrastructure. If personal data resides in our care, we need to be sure that the devices storing personal data are up to scratch. The task of identifying, locating and classifying data will help us to complete a data inventory.

GDPR references encryption as a means of protecting data, but encryption alone is not a solution. It is just one of many aspects that will help achieve compliance. Encrypted data breaches do not require a company to notify its supervisory authority – encrypted data is useless, and does not result in a risk to the rights and freedoms of individuals.

Information online is a borderless market, from larger companies to users of the dark web. We as data subjects put a lot of trust into organisations to use our data for the purpose for which it was acquired and to keep it safe and secure. Now, with GDPR, there is the creation of a trustworthy data protection culture.

Our continued GDPR efforts

At Vision Blue Solutions, when we were preparing our GDPR readiness roadmap, we looked at every piece of personal data we collected and used, from our employees to our customers. For our employees we looked at how our staff awareness programmes could benefit them, not just in how we as an organisation use their data, but also in how other organisations use their data, regardless of their location. We see this as a continuous effort and will ensure that we will:

- continue to encourage our staff to be aware of the data they deal with, their own data that we store and the data they provide to other organisations
- continue to update our policies with transparency in mind
- continue to add functionality needed by our customers who themselves navigate through their GDPR journey as data controllers.

> **Processes don't stay the same and over time neither does data. GDPR has highlighted the fact that we need to reassess at regular intervals.**

GDPR is a good thing that requires organisations like us, which assist our customers as data controllers in their processing activities, to protect any personal data that we come into contact with. As Vision Blue Solutions enters new jurisdictions, such as Canada and New Zealand, we welcome the GDPR framework. We are aware of the privacy regulations in other jurisdictions and, when required, we will be able to handle any clashes. We are actively monitoring our data privacy policies and storage of personal data in our efforts to continuously optimise our GDPR journey. Processes don't stay the same and over time neither does data. GDPR has highlighted the fact that we need to reassess at regular intervals. By doing so, it will help policies stick. □

LORRAINE SURLIS is the data protection officer at Vision Blue Solutions.

Lorraine managed the implementation of new functionality for Vision Blue's software and internal processes in order to comply with GDPR.

Are CVAs the answer?

Phillip Sykes reviews recent criticism and praise for CVAs to see where they fit in the current insolvency toolkit.

By the time this copy of *RECOVERY* reaches you, House of Fraser may well have collapsed following the challenge to its CVA by a group of unhappy landlords and the withdrawal of a proposed Chinese investor. The department store group is just the latest case in a raft of headline-grabbing CVAs to affect the retail and casual dining sectors.

This article is not going to conduct a detailed inquiry into the causes of distress affecting the businesses mentioned in the media. It is abundantly clear, though, that the high street has been hit by several disruptive factors at the same time. Retail has been increasingly affected by internet sales, casual dining is suffering from saturation due to over-supply and, to add to their woes, there has been a massive rise in business rates.

So, with the situation in context, is a CVA the answer to the present crisis on the high street? Is it what stakeholders want? Or does it interfere with the proper working of the market and is anti-competitive (as some have alleged)?

> The rather cynical view of a CVA back then [its introduction] appeared to be that if you have needed one, you probably didn't deserve one, so they were little used.

Shifting landscape

Recent R3 research into CVAs, which commenced in 2013, confirmed that two-thirds of CVAs fail – or more precisely, *'were terminated without achieving their intended aims'* (see table 1). This is not a great statistic so it is not surprising that CVAs have come to be regarded with a degree of scepticism.

But what do stakeholders really want from a CVA? When the Insolvency Act 1986 introduced the procedure there was initially virtually no take up.

The rather cynical view of a CVA back then appeared to be that if you have needed one, you probably didn't deserve one, so they were little used. If a retail chain ran into difficulties, a pre-pack administration was often seen as the most effective way to rescue the business, enabling the purchaser to cherry-pick the profitable sites and abandon the lossmakers.

Unsurprisingly, pre-packs tended not to be particularly popular with creditors generally, and landlords in particular, who found themselves having to negotiate new leases with the purchasers of the business at very short notice. Pressure from these stakeholders led to CVAs becoming more widely used in the healthcare and retail sectors, as they were perceived as providing a forum for negotiation between the concerned parties.

In more recent times, with wider use and increased publicity around household names using the procedure, came greater scrutiny. There were some high-profile failures of CVAs – for instance BHS – and the view of a number of stakeholders and commentators is that the procedure is just a deferral of the inevitable failure of the company – 'kicking the can further down the road'.

Tin-can football

But is 'kicking it down the road' actually such a bad thing? From some landlords' perspectives, probably not. Notification and implementation of a CVA gives landlords an early warning, and a sensible proposal may well provide a better alternative to immediate insolvency (even if only temporary). Generally speaking, landlords are not anti-CVA but they do want to feel they are being treated fairly.

In particular they want assurance that their economic interests are being properly reflected in the voting rights they are allocated for the purposes of the decision making process, as well as, in due course, agreeing any claims they may have. Voting rights are a bone of contention since some recent CVA proposals have tended to take a one-size-fits-all approach in valuing landlords' claims for voting purposes. This is clearly not always appropriate when evaluating the respective claims of, say, a landlord of a site in central London's Oxford Street, where they will be able to re-let fairly quickly, as against a landlord of a shed in a regional retail park location, where letting may take a lengthy period of time and their claim will be significantly greater.

This issue appears to have prompted the landlords' challenge in the House of Fraser case.

The British Property Federation (BPF) has just issued a voluntary protocol for IPs, which has the huge merit of being both short and comprehensible. It identifies the key issues that the BPF considers need to be addressed. These are set out in table 2 but include:

- basis of valuation proposed for the landlords' claims (and corresponding voting rights)
- basis for stratification for different properties
- termination provisions
- relevant antecedent transactions
- payment of rates
- clawback provisions for successful turnaround of business.

You can read the full protocol at: **https://www.bpf.org.uk/sites/default/files/resources/CVA%20best%20practice.pdf.**

None of this should come as a surprise to an IP trying to put together a proposal on behalf of a struggling business. Statement of Insolvency Practice 3.2 sets out clearly the behaviour expected of an IP and it is, after all, a requirement of the Insolvency Rules that *a proposal must explain why the creditors are expected to agree to a CVA* and, when reporting to the court on the proposal, the nominee has to state *why he/she considers the proposal does or does not have a reasonable prospect of being implemented*.

> The view of a number of stakeholders and commentators is that the procedure is just a deferral of the inevitable failure of the company – 'kicking the can further down the road'.

Although neither SIP 3.2 nor the legislation explicitly requires the company, the IP or the nominee to have made contact with the creditors, it is virtually impossible to satisfy the conditions above without having done so. And, in practice, extensive consultation has been undertaken in connection with the more well-supported CVAs such as New Look, Carluccio's and Aldo, all of which had well over 90 per cent voting in favour.

So the message is pretty clear – if you want your CVA to succeed you need to do a lot of homework with the stakeholders.

The question of rent

Even with stakeholder support, though, you may not get it away. There is a body of

TABLE 1
R3 research into CVA outcomes – May 2018

An analysis of the 552 CVAs commenced in 2013 involving companies in England and Wales showed:

- 18.5% were fully implemented;
- 16.5% were ongoing at the survey date;
- 65% were terminated without achieving their intended aims;
- 7% were terminated within the first 2 quarters;
- 24% were terminated between 4 and 6 quarters after commencement.

For the full report go to:
https://www.r3.org.uk/media/documents/policy/policy_papers/corporate_insolvency/R3_ICAEW_CVA_Report_May_2018.pdf

TABLE 2
British Property Federation CVA protocol

Key issues for landlords:

- The basis of valuation proposed for the landlords' claims (and corresponding voting rights)
- Payments in lieu of dilapidations, and basis for calculation
- The basis of stratification where different options are being offered, eg different properties continuing to trade or closing and/or different rental discounts being applied
- The ability, if any, for the landlord to terminate the CVA in the event of default
- Terms which enable the landlord or tenant to terminate the lease outside of any existing lease provisions, and any conditions attached
- If there have been previous failures, an explanation of the CVA stands a better chance of success
- Compensation offered
- As required by the legislation, an explanation of why the CVA is a better option for landlords than administration (particularly in terms of the number of stores likely to be closed)
- Relevant antecedent transactions
- 'Clawback' – any opportunity for compromised landlords to benefit from a successful turnaround of the business
- If relevant, the source of funding to make the CVA financially viable
- Rent repayments
- An explanation of why the business will be sustainable post-CVA
- The effect on any guarantors
- The justification for any differential treatment of critical and non-critical trade and other creditors
- Liability for rates
- Conditions for termination of the CVA, to include the treatment of the CVA and landlord compromises in the event of a subsequent administrator or liquidator appointment.

landlords who take the view that CVAs are potentially being misused. They are prepared to support CVAs that genuinely give breathing space to restructure and raise new funds. However, where the operating performance of a business is fine but its ownership structure has excessive debt, or management simply wants to improve its operating profits by reducing rents, they believe that the CVA process is neither fair nor appropriate.

There is another constituency that believes struggling businesses should be allowed to fail and the market be allowed to determine the rents achievable for a particular site, rather than have it imposed through a legal process.

It should not be overlooked that the process is causing real concern to overseas investors, both existing and potential, to whom it appears that the CVA process effectively enables tenants to tear up contractual agreements. In addition, solvent retailers are expressing annoyance when they see competitors apparently obtaining an unfair advantage through a reduction in costs. Some have called for 'CVA clauses' in leases to allow tenants to negotiate rent reductions where competitors/neighbouring stores have benefitted from rent reductions imposed through a CVA.

No such thing as a 'standard' CVA

Ultimately, though, CVAs are the symptom, not the cause. In many areas the high street and retail parks are struggling. From an economic perspective, a property can only generate a certain amount of income and if the government chooses to take a greater share by increasing business rates, either rents have to fall or businesses become less profitable. Where businesses are already struggling, insolvencies will follow.

> Generally speaking, landlords are not anti-CVA but they do want to feel they are being treated fairly.

So, yes, in the right cases, a CVA can definitely be the answer. But it has to be tailored to the particular situation and IPs must resist the temptation to roll out the same boilerplate pro forma proposal for each new matter. Furthermore, the proposals need to be very clear about the benefits for stakeholders and the way forward for the business.

Partly because some recent CVA proposals have been lengthy and complex documents, there have been calls for standardisation of CVAs in the belief that this would somehow improve fairness and transparency but, in my view, this would seriously undermine the procedure. A better solution is an executive summary which sets out in simple language the key proposals and issues.

> As the R3 research correctly concluded, the biggest strength of a CVA is its flexibility. In the right circumstances it can be a very useful procedure in the restructuring toolkit.

As the R3 research correctly concluded, the biggest strength of a CVA is its flexibility. In the right circumstances it can be a very useful procedure in the restructuring toolkit. IPs must always remember, though, that their role in a CVA is, first and foremost, to ensure a fair balance is struck between the company and its creditors – and also to make this clear to all involved. □

PHILLIP SYKES is head of London restructuring advisory at RSM.

Pre-packs:

best practice makes perfect

Chris Laughton explains essential best practice in relation to pre-packs and why they can sometimes be a controversial topic.

As a profession we have not been sufficiently successful in persuading creditors and the public that the benefits of the pre-pack mechanism outweigh the downsides. In individual cases we could do more to ensure that the relevant stakeholders appreciate that the pre-pack was the right thing to do.

Although pre-packs are used less often than the number of column inches devoted to the subject suggests, they are not uncommonly the subject of litigation and regulation, and the Insolvency Service is considering whether further legislation is required, potentially to limit connected party sales.

This article charts a course through the regulatory requirements and some of the litigation surrounding pre-packs. Compliance is a necessary precursor to stakeholder appreciation.

The IP's duties

An IP who acts in relation to a pre-pack has the common law duty of a professional person to act with reasonable skill and care in the conduct of their profession. The level of skill and therefore the extent of the professional duty is enhanced above that expected of a non-specialist corporate advisor or qualified accountant, because an administrator would be acting in their specialist capacity as an insolvency practitioner.

When a company is insolvent or there is a real risk of prejudice to creditors, its insolvency advisor should consider and act in the interests of creditors, and should advise the company and its directors accordingly. An administrator should similarly act in the interest of the creditors as a whole. Unless the IP's duties before and after appointment as administrator are consonant, he or she will be subject to a potentially irreconcilable self-review threat to his or her objectivity – a conflict of interests.

> "An IP who acts in relation to a pre-pack has the common law duty of a professional person to act with reasonable skill and care in the conduct of their profession."

This continuing responsibility to act in the interests of creditors is fundamental to the proper execution of a pre-pack. An area of difficulty arises in connected party pre-packs, where the company's management may be focused on the interests of the purchaser rather the company's creditors. It is for the IP to seek to ensure that there is appropriate segregation between the seller (acting in creditors' interests) and the purchaser.

Secured creditors

Another aspect of an administrator's duties to be borne in mind, from para 3, schedule B1 of the Insolvency Act 1986, is that an administrator cannot perform his or her functions with the objective of realising

Insolvency code of ethics – fundamental principles

An insolvency practitioner is required to comply with the following fundamental principles:

Integrity

An insolvency practitioner should be straightforward and honest in all professional and business relationships.

Objectivity

An insolvency practitioner should not allow bias, conflict of interest or undue influence of others to override professional or business judgements.

Professional competence and due care

An insolvency practitioner has a continuing duty to maintain professional knowledge and skill at the level required to ensure that a client or employer receives competent professional service based on current developments in practice, legislation and techniques. An insolvency practitioner should act diligently and in accordance with applicable technical and professional standards when providing professional services.

Confidentiality

An insolvency practitioner should respect the confidentiality of information acquired as a result of professional and business relationships and should not disclose any such information to third parties without proper and specific authority unless there is a legal or professional right or duty to disclose. Confidential information acquired as a result of professional and business relationships should not be used for the personal advantage of the insolvency practitioner or third parties.

Professional behaviour

An insolvency practitioner should comply with relevant laws and regulations and should avoid any action that discredits the profession. Insolvency practitioners should conduct themselves with courtesy and consideration towards all with whom they come into contact when performing their work.

property in order to make a distribution to one or more secured or preferential creditors if doing so would unnecessarily harm the interests of the creditors of the company as a whole. It is not a question of whether the administrator thinks such harm will be done. Whether unnecessary harm has been done to creditors' interests is a fact that will be determined if necessary by a court, with the benefit of hindsight.

> It is for the IP to seek to ensure that there is appropriate segregation between the seller (acting in creditors' interests) and the purchaser.

As Snowden J put it in *Davey* v. *Money*[1] (para 254):

'An administrator is required to have regard to the interests of all of the company's creditors, and he can only limit his ambition to seeking to realise the assets to repay the secured creditor if he thinks that it is not reasonably practicable to achieve anything else. Even then, he must not unnecessarily harm the interests of the creditors as a whole.'

Millett J in *Re Charnley Davies* (No. 2)[2] said (page 776a) in relation to the administrator's selling duty:

'It is not an absolute duty to obtain the best price that the circumstances permit, but only to take reasonable care to do so; and in my judgment that means the best price that circumstances ***as he reasonable perceives them to be*** *permit. He is not to be made liable because his perception is wrong, unless it is unreasonable.'* (Emphasis in original.)

Snowden J considers these two duties together, noting that (para 392):

'The administrator cannot simply decide to sell the company's assets at a time to suit the interests of the secured creditor, if by doing so he causes harm to the unsecured creditors, which is not necessary for the protection of the interests of the secured creditor.'

Pre-packs are often encouraged by secured creditors, who see them as a mechanism to generate the maximum return under their security. An administrator in such cases should take particular care not to cause harm to the unsecured creditors.

Code of ethics

The insolvency code of ethics applies to all IPs[3]. Its principles merit consideration and are shown in the box above.

At paragraph 400.37, the code requires that an insolvency practitioner should ensure that he or she is satisfied that he or she has considered obtaining knowledge and understanding of: the entity, its owners, managers and those responsible for its governance; its business, operations, relevant industries; and the specific engagement, purpose nature and scope of work to be performed.

Paragraph 400.38 of the code of ethics states:

'The fundamental principle of professional competence and due care requires that an insolvency practitioner should only accept an insolvency appointment when the insolvency practitioner has sufficient expertise…. Expertise will include appropriate training, technical knowledge and ***knowledge of the entity and the business of which the entity is concerned.***' (Emphasis added.)

It would be difficult and unusual to advise properly on a company's insolvency and a prospective administration without having obtained knowledge and understanding of the entity, its owners, managers and those responsible for its governance and business activities.

It would, I suggest, be impossible to advise properly on a company's insolvency and prospective administration or other solution without acquiring an appropriate knowledge and understanding of the nature of the entity's business and the complexity of its operations.

The code of ethics covers pre-packs specifically in paragraph 400.51:

'Where the assets and business of an insolvent company are sold by an insolvency practitioner shortly after appointment on pre-agreed terms, this could lead to an actual or perceived threat to objectivity. The sale may also be seen as a threat to objectivity by creditors or others not involved in the prior agreement. The threat to objectivity may be eliminated or reduced to an acceptable level by safeguards such as obtaining an independent valuation of the assets or business being sold, or the consideration of other potential purchasers.'

The code further requires (paragraph 400.74) the practitioner to justify their actions and demonstrate the steps taken and conclusions reached in identifying, evaluating and responding to threats, and that this is (paragraph 400.75) recorded to such a degree that a reasonable and informed third party would be able to reach a view on the appropriateness of their actions.

> Whether unnecessary harm has been done to creditors' interests is a fact that will be determined if necessary by a court, with the benefit of hindsight.

Ensuring that an administrator has the requisite knowledge, eliminating or reducing to an acceptable level any threats to objectivity, and maintains contemporaneous written records sufficient to enable a reasonable and informed third party to reach a view on the appropriateness of his or her actions, will go a long way towards ensuring that a pre-pack is executed properly.

Statements of insolvency practice

SIP 2 requires an administrator to investigate what assets can be realised. If he or she sells some of the company's assets on or shortly after appointment, the investigation should be done before appointment.

SIP 13 – disposal of assets to connected parties in an insolvency process – applies to the many pre-packs to connected parties. A detailed analysis of »

SIP 13 is beyond the scope of this article, but some key points from its introduction are that:

'Transparency in all dealings is of primary importance. It is equally important that the insolvency practitioner acts and is seen to be acting in the interests of the creditors as a whole and is able to demonstrate this.'

SIP 13 also includes (at paragraph 5) the principle that:

'When instructed to advise a debtor, a company or companies in a group, the insolvency practitioner should make it clear that the role is not to advise any parties connected with the purchaser, who should be encouraged to take independent advice. This is particularly important when there is a possibility that a connected party may require an interest in the business or assets.'

> An IP's principal objective in reporting to creditors must be to communicate effectively that the pre-pack was in the best interests of the creditors as a whole.

SIP 16 – pre-packaged sales in administrations – sets out detailed regulatory requirements for executing a pre-pack. Again, it is the introduction rather than the detailed provisions that merit attention in this article.

'The particular nature of an insolvency practitioner's position in [a pre-pack] renders transparency in all dealings of primary importance. Administrations are a collective insolvency proceeding – creditors and other interested parties should be confident that the insolvency practitioner has acted professionally and with objectivity; failure to demonstrate this clearly may bring the insolvency practitioner and the profession into disrepute.'

SIP16 also requires IPs to recognise the high level of public interest attached to a pre-pack administration and to plan for greater scrutiny.

When a pre-pack sale to a vehicle of, or connected to, the existing management is planned, even as one of a number of options, an IP would be expected to recognise the particular conflict of interests challenges that may arise. For example, he or she would have to be particularly careful to ensure that the buyers did not, at the expense of creditors, exploit knowledge and experience that they had obtained from the management with which they were connected and which the administrator would be unlikely to have in such depth. To do otherwise would ignore the guidance above.

Valuation

Paragraph 400.51 of the code of ethics explains that obtaining an independent valuation may eliminate or reduce the threat to objectivity inherent in a pre-pack. SIP 16 requires details of any valuation to be disclosed. If there was no valuation, it must be shown why not and how the administrator was satisfied as to the value.

A valuation is imperative when negotiating a single offer (not uncommon in pre-packs). Sometimes the excuse is given for no valuation that the market determines the true value and a valuation adds nothing. That may be the case if there is perfect marketing, but the best marketing strategy will be influenced by knowledge of the likely value.

Consultation with creditors about a pre-pack may be ineffective without a valuation.

All these points are likely to lead to a pre-pack with no valuation being a rare exception.

Marketing

The appendix to SIP 16 identifies marketing of a business as an important element in ensuring that the best available consideration is obtained for it in the interests of creditors and that such marketing will be a key factor in providing reassurance to creditors. SIP 16 specifies that marketing should be broadcast, not narrowcast; the marketing strategy should be justified; marketing should be independent; the business and assets should be publicised for an appropriate period; online communication should be the default, alongside other media; and any divergence from the requirements of the SIP should be explained in the context of how they have achieved the best available outcome for creditors as a whole in all the circumstances.

Consultation

One of the requirements of a SIP 16 report is for the administrator to report to creditors:

'Whether efforts were made to consult with major or representative creditors and the upshot of any consultation. If no consultation took place, the administrator should explain the reasons.'

Summary

Valuation, marketing and consultation, together with immediate and transparent reporting, constitute the heart of the regulatory mechanism to seek to overcome shortcomings in communication to creditors about pre-packs. It is worth IPs remembering that the key point here is communication, rather than a tick box approach to compliance. The regulatory requirements are set out and are not optional, but an IP's principal objective in reporting to creditors must be to communicate effectively that the pre-pack was in the best interests of the creditors as a whole.

Conflicts of interest

The recent case of *Re Ve Interactive Limited (in administration)*[4] is discussed elsewhere in this issue (page 8). For the purposes of this article there are two main points to take from that case.

Firstly there must be a 'serious issue for investigation' in order for a material conflict to arise in relation to an administrator considering his or her own pre-appointment conduct. In the event of such an issue having been identified, an appropriate remedy may well be the appointment of a conflict administrator to undertake the required investigation.

> Administrators executing a pre-pack need knowledge of the affairs, business and assets of the company so that they understand why that pre-pack was in the best interests of the creditors as a whole.

Secondly, the case makes clear that administrators executing a pre-pack need knowledge of the affairs, business and assets of the company so that they understand why that pre-pack was in the best interests of the creditors as a whole.

Conclusion

Through compliance with the law, regulation and professional guidance and through the all-important component of clear and effective communication, we should be able to continue to use pre-packs as a mechanism for preserving and realising value in an insolvent business. □

1 [2018] EWHC 766 (Ch)
2 [1990] BCLC 760
3 Each RPB has produced its own version of the code of ethics. They vary only in paragraph numbering. For convenience this article uses the numbering from the ICAEW code of ethics (part D).
4 [2018] EWHC 186 (Ch)

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– Nyla Yousuf, R3 Ladies' Lunch Committee Chair

Make yourself at home with the new rules for social housing providers

Louise Leaver, **Patricia Umunna** and **Marie-Louise King** explain the new special insolvency regime for social housing providers.

There are more than 1,700 registered providers of social housing in the UK, responsible for over 2.5 million units. Although there is strict regulation of the companies, registered societies and charitable incorporated organisations that provide social housing (referred to as registered providers), financial distress or insolvency is always a lurking possibility.

The societal importance of social housing, the perceived inadequacy of the powers of the Regulator of Social Housing (RSH) and public policy considerations specific to the sector were the catalyst for the establishment of a special insolvency regime. This was brought in via the Housing and Planning Act 2016 (the 2016 Act), the Insolvency of Registered Providers of Social Housing Regulations 2018, and the Housing Administration (England and Wales) Rules 2018 (together, the 2018 regulations and rules). Under this new special insolvency regime, the affairs, business and property of the registered provider are to be managed by an appointed housing administrator. The 2018 Regulations and Rules came into force on 5 July 2018.

The housing administration regime

The housing administration regime differs in significant respects from the 'ordinary' administration regime under schedule B1 of the Insolvency Act 1986 (IA 1986) and impacts on the secured and unsecured creditors of registered providers, as well as the registered providers themselves, in terms of the accessibility of the various insolvency and enforcement procedures.

> Under this new special insolvency regime, the affairs, business and property of the registered provider are to be managed by an appointed housing administrator.

In relation to registered providers:

- a housing administration order can be made by the court only; and
- an application for a housing administration order may be made by the Secretary of State or, with their consent, by the RSH only.

Any person who has appointed, or who is entitled to appoint, an administrative receiver of the registered provider, or who would be entitled to appoint an administrator of the registered provider by reason of being the holder of a qualifying floating charge, is entitled to notice of the application.

The court hearing the application may make the order sought, dismiss the application, adjourn it with or without conditions, make an interim order or may treat it as a winding-up petition. In the latter event, the court may make any order it would be entitled to make under s125 IA 1986. The court may only make a housing administration order if satisfied that the

registered provider is unable, or is likely to be unable, to pay its debts, or that it would be just and equitable in the public interest to wind up the registered provider.

Conversely, the court has no power to make a housing administration order in relation to a registered provider that is already in administration under schedule B1 or which has gone into liquidation.

Objectives

Once appointed, the housing administrator has two objectives:

- Objective 1: a 'normal administration' to (a) rescue the registered provider as a going concern; (b) achieve a better result for the registered provider's creditors as a whole than would be likely if the registered provider were wound up (without first being in housing administration); or (c) realise property in order to make a distribution to one or more secured or preferential creditors.
- Objective 2: keeping the registered provider's social housing in the regulated housing sector, namely its ownership by a private registered provider.

> Any application for an ordinary administration order must be dismissed if a housing administration order has been made or is in force.

The 2016 Act makes clear that while the housing administrator must, so far as possible, work towards both objectives, objective 1 (and, as with ordinary administration, in an order of priority) takes priority over objective 2. That means that in pursuing objective 2, the housing administrator must not do anything that would result in a worse distribution to creditors than would be the case if they did not need to pursue objective 2.

The housing administrator, who must be qualified to act as an insolvency practitioner, is required to aim to achieve the objectives of the housing administration as quickly and as efficiently as is reasonably practicable. The provisions of schedule B1 apply, with certain modifications, in relation to the conduct of the housing administration.

Secretary of State powers

Where a housing administration order is made, the Secretary of State has power under the 2016 Act to make grants or loans available to the registered provider to support the achievement of the objectives of the housing administration, to provide indemnities in respect of liabilities incurred or loss or damage sustained in connection with the housing administrator's carrying out of their functions, and provide guarantees in respect of financial obligations of the registered provider.

Restrictions on other insolvency procedures

The housing administration regime also imposes restrictions on other insolvency procedures.

The court may not exercise its powers on a winding-up petition unless at least 28 days' notice of the petition has been given to the RSH, who in turn must give notice to the Secretary of State.

A registered provider that wishes to pass a resolution for voluntary winding up requires the permission of the court to do so. As with winding up, at least 28 days' notice of an application for permission must be given to the RSH, who is in turn required to give notice to the Secretary of State.

Any application for an ordinary administration order must be dismissed if a housing administration order has been made or is in force. If a housing administration application or order has been made, or is in force, a person is not entitled to take any step to make an out-of-court appointment of an administrator under paragraphs 14 or 22 of schedule B1. In the event that an appointment is not precluded, an appointment of an administrator will not take effect unless at least 28 days' notice of the appointment has been given to the RSH, who must in turn notify the Secretary of State. In the case of an application to court for an ordinary administration order, the court must not exercise its paragraph 13, schedule B1 powers unless the RSH has been given at least 28 days' notice of the application. Moreover, the interim moratorium provisions of paragraph 44 of schedule B1 do not prevent the making of an application for a housing administration order before the appointment takes effect.

The requirement to give notice ensures that the Secretary of State (or, with their consent, the RSH) is afforded an opportunity to apply to court for a housing administration order before a winding-up petition, voluntary winding-up application or ordinary administration application is heard.

Impact on secured creditors and valuations

The restrictions on other insolvency procedures are extended into the area of enforcement of security. Security cannot be enforced over property of a registered provider unless at least 28 days' notice of the intention to do so has been given to the RSH who, in turn, must give notice to the Secretary of State.

The 2018 rules provide for the housing administrator to apply to court under paragraph 71 of schedule B1 for authority to dispose of charged property as if it were not. As in ordinary administration, such order as is granted would be subject to the condition that there be applied towards discharging the sums secured by the security, the net proceeds of sale and any additional money required to be added to such net proceeds so as to produce the amount determined by the court as the net amount, which would be realised on a sale of the property at market value. Part 5, chapter 2 of the 2018 rules contains provisions relating to the valuation and re-valuation of security.

> It remains to be seen whether the introduction of the housing administration regime will be reflected in a change in practice in addressing distress in registered providers.

From a valuations perspective, no real change is anticipated. As objective 1 will take priority and creditors' interests will therefore be protected, valuers have confirmed that the sector-standard market value subject to tenancy valuation can be retained.

Sea change?

To date very few registered providers have found themselves in financial difficulties and no funder in the housing association sector is believed to have suffered a loss.

It remains to be seen whether the introduction of the housing administration regime will be reflected in a change in practice in addressing distress in registered providers. The regime certainly gives the Secretary of State, or RSH, new powers, but will they wish to exercise them?

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Banks, blame and court claims

Simon Duncan explores recent cases where liquidators have brought proceedings against previously bank-appointed administrators.

The court may examine the conduct of a person who has been the administrator of a company on an application by the liquidator of the company, pursuant to schedule B1, paragraph 75(1) and (2) of the Insolvency Act 1986 (IA). However, an application may only be made in respect of an administrator who has been discharged, with the permission of the court, paragraph 75(6).

> Applications of this sort are becoming more frequent, particularly if it appears that the bank's appointees have done little more than look after the bank's interests.

The report of RBS Group's treatment of SME customers referred to the Global Restructuring Group (the GRG report), together with the Financial Conduct Authority's interest rate hedging product review (the FCA review), have shown widespread use of the administration process by banks from 2008 to 2013. Typically, the administrators will have been appointed from a small number of large insolvency practices that are 'bank panel' firms. Where the creditors of the companies pushed into insolvency are dissatisfied with the conduct of the banks' appointees, they can seek to restore the company into liquidation. They can then appoint an independent liquidator who can review the conduct of the former administrators. Applications of this sort are becoming more frequent, particularly if it appears that the bank's appointees have done little more than look after the bank's interests, rather than the interests of any other creditors, or the members.

One Blackfriars Limited

A good example is seen in the recent judgment of Mr William Trower QC, sitting as a deputy judge of the High Court, in *One Blackfriars Limited* [2018] EWHC 901 (Ch).

> It is incumbent upon the liquidators to show a reasonably meritorious cause of action which is reasonably likely to result in a benefit to the estate.

This was an application brought by the liquidators of the company for permission to bring proceedings against the former administrators for negligence. The administrators (from BDO LLP) were appointed by RBS in October 2010. The administrators sold the company's asset – 1–16 Blackfriars Road, London SE1 (the site) – for £77.4m in October 2011. This was not enough to pay the other secured creditors, one of whom restored the company and put it into liquidation. The liquidators allege that the administrators sold the site at an undervalue and by so doing were negligent. The claim against BDO is said to be worth £58m.

The former administrators were the respondents to the application and, in accordance with the Insolvency (England and Wales) Rules 2016 12.9(3), a copy of the application notice was served on the respondents. As a consequence, the application was listed for a day and hard fought by leading counsel on both sides. Permission to issue the negligence claim was granted.

In the past such applications have sometimes been made *ex parte*, without notice, the logic being that it is for the applicant to persuade the court to grant permission before a claim is issued. When the claim is served, the respondent can then be expected to answer the claim. Of course the target can be expected to oppose the application for permission because he or she does not wish to be sued, but where the rules require 14 days' notice

> There are likely to be more instances of liquidators being asked to review the conduct of a company's former administrators.

of the hearing of the application, and the former administrators are named as respondents on the application, notice should be given; to do otherwise risks an adjournment for this purpose.

Notice of the hearing of the application will also reduce the burden on the applicant to give full and frank disclosure of every fact germane to an application brought without such notice.

In *One Blackfriars* the court reviewed the existing authorities where permission had been sought from the court to bring a claim against former office-holders, post-release – in particular, against a former liquidator pursuant to section 212(4) IA and against a former trustee in bankruptcy pursuant to section 304 IA. Permission is required because the former office-holders have been discharged or released and no longer have the assets of the estate in their

possession from which to indemnify themselves against claims. In this sense the permission stage is a 'filter' to weed out unmeritorious claims.

However, how strong did the prospective claim have to be? Little more than a *bona fide* claim according to William Trower QC:

'It is incumbent upon the liquidators to show a reasonably meritorious cause of action which is reasonably likely to result in a benefit to the estate.' (paragraph 30.)

Contrary to what was said by counsel for the former administrators, this is not a high hurdle.

Somewhat surprisingly, in this application both sides had adduced expert evidence in support of their respective positions. The former administrators had argued that it was incumbent on those seeking to challenge the conduct of a professional person for allegedly selling a property at an undervalue to have obtained expert evidence *before* a claim is made. This argument prompted the liquidators to serve a draft expert report. However, the court held that there was no such obligation on the liquidators. There was sufficient evidence to support an arguable claim that there had indeed been a material loss sustained by the company.

Arthur Holgate and Son Limited (Holgate)

The Times and *The Sunday Times* (21 May 2018 and 1 July 2018 respectively) report that another similar application has been brought against Deloitte. Holgate is in liquidation. The joint liquidators' progress report, dated 26 October 2017, as filed at Companies House, contains their summary of receipts and payments that confirms receipt of approximately £10m, said by *The Times* to have been paid in an out of court settlement by Barclays. The joint liquidators have taken further legal advice about other potential claims and one of these is said to be against the former administrators, from Deloitte.

In order to bring such a claim, the joint liquidators are obliged to seek the permission of the court, pursuant to IA schedule B1, paragraph 75(6). The hearing of that application was listed for 5 July 2018. However, the hearing did not appear in the cause list. One might speculate that in light of the decision in *One Blackfriars Limited*, the application was conceded. As a result the court is likely to have granted permission 'on paper' having been satisfied that the liquidators had demonstrated that they did have a reasonably meritorious cause of action.

Conclusion

There are likely to be more instances of liquidators being asked to review the conduct of a company's former administrators.

Where a claim is identified, the application for permission need only evidence a reasonably meritorious cause of action that may reasonably be expected to benefit the estate. This is not a high hurdle. No expert evidence is required. The application ought to be served and as a consequence the court will list a hearing

> Where creditors of the companies pushed into insolvency are dissatisfied with the conduct of the banks' appointees, they can seek to restore the company into liquidation.

date. This does not oblige the respondent to file evidence and contest the application. Arguably, in view of the decision in *One Blackfriars*, the respondent would want to consider very carefully the costs risk attendant upon challenging the merits of the liquidator's claim at this stage. However, as a precaution, if the respondent does contest the application the liquidator may want to ensure that he or she has adequate adverse costs insurance in place before serving the application. □

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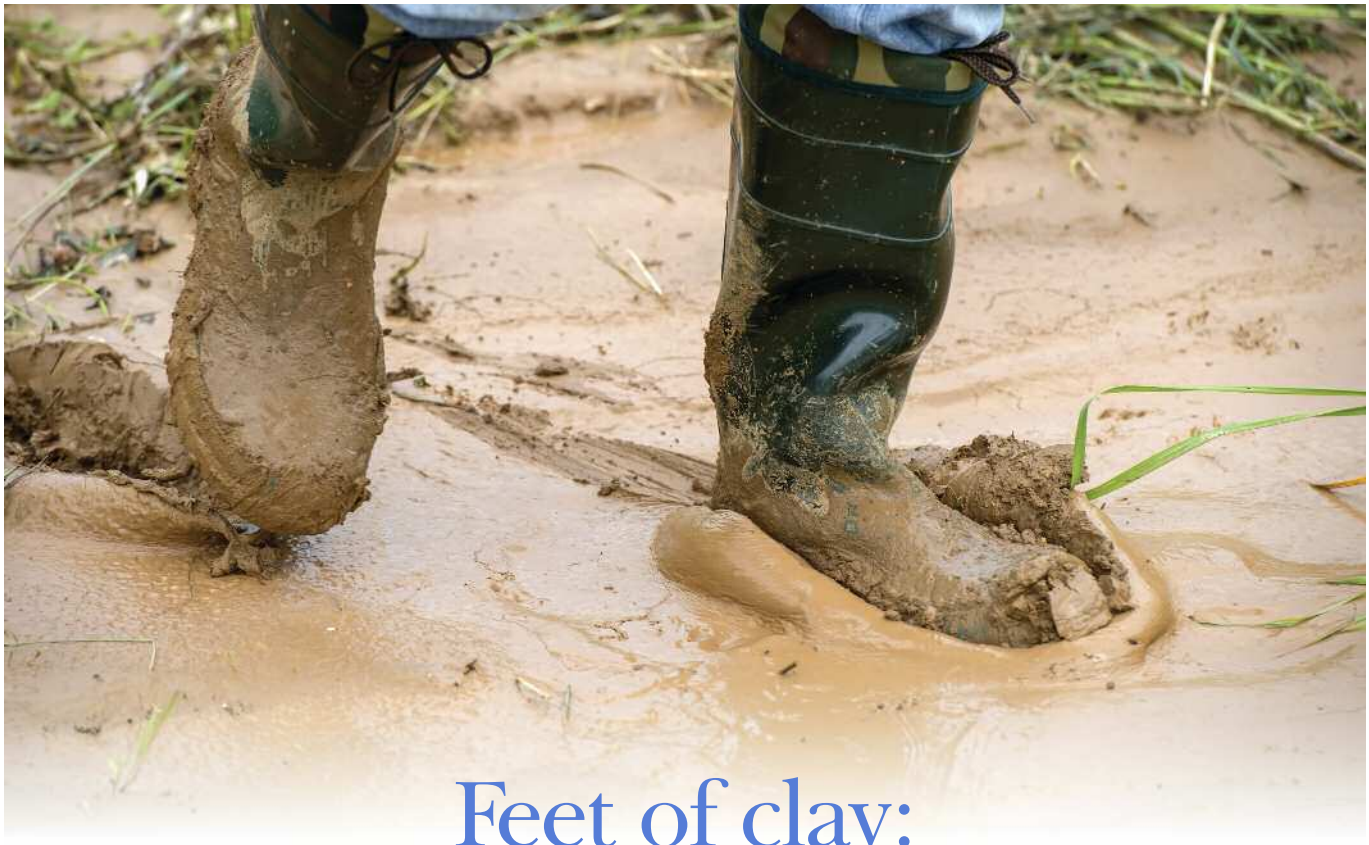

Feet of clay: lessons from Carillion

In the wake of Carillion **Alison Goldthorp** asks whether administration is no longer fit for purpose for larger businesses.

Carillion Plc and five of its subsidiaries went into compulsory liquidation at 6.40 am on 15 January 2018. Six partners at PwC were appointed special managers, and compulsory liquidation of many other companies in the group followed in the months since the first appointments. In this article we will explore the background to the compulsory liquidation and some of the legal issues that have arisen so far. Compulsory liquidation is rarely used in a trading situation, so a lot of the legal issues have involved looking at cases from the 1880s! No doubt there will be a spate of Carillion-related cases in the coming months that will set new precedents in this area of insolvency law.

The sheer scale of the Carillion business has provided numerous challenges for the UK insolvency process, which has been conducted under immense public scrutiny. Carillion was the UK's second largest construction and services business, with 43,000 employees globally and 20,000 of those in the UK. There were 2,000 apprentices and 7,000 subcontractors who were owed considerable sums, with payments being pushed out to them 120 days prior to the insolvency. The share price crashed by 90 per cent in the period from July 2017 and there had been three profit warnings. Carillion owed £1.3bn in senior debt, there was a pension deficit of £587m and it had just £29m in the bank on the date of liquidation. Up to 30,000 smaller firms were owed over £1.5bn and the knock-on effect for those businesses is only just starting to take effect. They will receive no payment as unsecured creditors, with recoveries for secured creditors being pennies in the pound.

> Compulsory liquidation is rarely used in a trading situation, so a lot of the legal issues have involved looking at cases from the 1880s!

The last filed accounts for the group were signed off on 1 March 2017 for the period to 31 December 2016. They showed total revenue of £5.2bn, which was up 14 per cent on the previous year, and proposed dividends for shareholders of 18.45p per share. The accounts reported a high quality order book of £16bn and a strong pipeline of contract opportunities worth £41.6bn. The summary refers to the intention to 'begin reducing average net borrowing over the medium term'. Yet, during 2017, Carillion was in negotiations with its lenders regarding the revision of terms and requests for further cash – which were ultimately refused – resulting in the appointment of liquidators in January 2018.

The collapse was very serious for the government in light of the contracts operated by Carillion in the public sector. It had contracts to maintain 50 prisons and provided services to numerous hospitals and medical practices, was part of a £1.4bn joint venture contract for HS2, provided meals for over 200 schools and maintained thousands of homes for military personnel.

On the construction side Carillion was involved in a number of very significant private finance initiative (PFI) contracts across the country including the Aberdeen bypass, the Royal Liverpool Hospital, the Midland Metropolitan Hospital, the Rotherham to Sheffield tram-train and the HS2 joint venture. There were reported delays, cost overruns and problems with three major UK public sector construction projects involving the £350m Midland Metropolitan Hospital, the £335m Royal Liverpool Hospital and the £745m Aberdeen bypass.

Select committee investigations

Since the liquidation began there have been inquiries by two select committees: the work and pensions committee and the business select committee, where further information has come out about the period leading up to the liquidation.

The investigations into the reasons for the collapse will no doubt be ongoing for several years, with yet further scrutiny of whether there should be changes to the laws relating to directors' duties, but in the meantime there has been some good news from the insolvency process so far.

Good news: jobs and contracts

The PwC website reports that, as at the end of July 2018, 11,351 jobs have been saved, which is 11 jobs for every 2 redundancies. As well as jobs transferred to other employers, 3,145 employees remain in the business and 1,094 have left through natural attrition (ie finding new work, retirement or other reasons) and 2,022 employees have been made redundant.

This is a great achievement given the position facing the Official Receiver and the special managers on 18 January. How has it been achieved?

> The investigations into the reasons for the collapse will no doubt be ongoing for several years.

The PwC website states that special managers assessed the options available in relation to the sale of the contracts of the Carillion companies and related assets, with the objective of delivering a smooth transition of the Carillion public sector contracts and realising the assets of the Carillion companies in a timely manner for the benefit of the creditors. They identified and offered for sale a number of contract packages and report on the completion of the sales of those various contract packages over the last few months. These packages include the sale of the facilities management contracts with corporate, governmental and public sector customers in the UK and Northern Ireland, the M40 maintenance contract, the SkyBlue recruitment business, the Network Rail contract, Carillion Advice Services and Carillion Fleet Management. Each of these sales of packages of contracts would have involved lengthy negotiations with the various contractual counterparties that were conducted without the benefit of the moratorium available in an administration, which prevents contracting parties from taking unilateral action adverse to the insolvent entity, for example, by terminating contracts and removing goods and equipment.

A large proportion of these contracts were PFI deals involving a complex web of contracts between a special purpose vehicle (SPV), a public authority, often a health authority or council, lenders, and shareholders who are often contractors at other levels in the project and the structure. A sale of that structure involves the novation of those contracts to the purchaser with the consent of the lenders involved and the public authority, which is no easy task and one that has taken a lot of negotiation for each PFI project involved. This would not have been possible without funding from the government, via the Official Receiver, of ongoing trading costs and fees. The special managers have sought to recover the running costs of each project from the commercial entities involved as part of the negotiations on the novations. They have also sought to collect in any monies due from any of the contracting parties to Carillion at the date of liquidation as part of the terms agreed in relation to the novations.

Inevitably, considerable numbers of people have been involved in the special managers' teams working on these negotiations, with over 250 staff from PwC at the start of the case. It was key to get the contracts transitioned as quickly as practically possible and to reduce the need for government funding on a daily basis. The costs incurred will be significant, but significant value has been added from transition of the contracts.

Not all contracts have been novated and some of the contracting parties decided to terminate their contracts with Carillion and enter into their own arrangements with new contractors without the involvement of the special managers.

Government support

From the outset the government indicated that the public services provided by Carillion would continue to operate with funding from the government if required. A statement was issued on 17 January 2018 confirming this support. This gave the special managers the ability to continue contracts involving public services while they sought to transition to new contracting parties. Services would be able to continue, but some contractual leverage was removed from the special managers in their negotiations to transition contracts to new counterparties as quickly as they could, to reduce the ongoing costs being paid by the Official Receiver and the government.

For other businesses affected by the collapse the government statement indicated that HMRC would give practical advice and guidance through its business payment support service. Business Secretary Greg Clark, Economic Secretary to the Treasury John Glen and Small Business Minister Andrew Griffiths met banks on 17 January to seek assurances that they would support small businesses affected by Carillion's liquidation and offer payment holidays, increased overdraft facilities and fee waivers as emergency measures. However, that support cannot continue indefinitely, and a wave of insolvencies of these businesses is likely to follow in the coming months.

Why liquidation and not administration?

The last big construction company collapse was Jarvis construction, which went into administration in March 2010. The administration moratorium was key to the administrators' ability to seek to transition as much of the business as possible to other contractors. So why did the Carillion companies go into compulsory liquidation rather than administration?

A key issue was the cost and risk of continuing to trade, which would result in significant administration expenses such as salaries, health and safety and environmental risk, and risks relating to the pension liabilities. Any administrators appointed would only have had the £29m in the bank present at the time of Carillion's collapse. The 'administrators in waiting' probably sought confirmation that they would be given an indemnity from the lenders and/or the government for those liabilities. They would also have been nervous of continuing to trade a loss-making business with very limited funding. The lenders were probably unwilling to write such a large 'blank cheque', and the government would be wary of underwriting the cost of public service contracts if there was a private sector administration appointment by the directors or the lenders, with no element of control for the government. The rare solution decided upon was compulsory liquidation for a trading business with the ability of the Official Receiver to ask the government for funding for ongoing trading expenses, and the possibility for the Official Receiver to provide an indemnity to the special manager for expenses incurred in his or her duties.

This put the lenders into a difficult position, as the Official Receiver/special managers did not have the benefit of the moratorium, in contrast to administration,

> The rare solution decided upon was compulsory liquidation for a trading business.

and it has been much more difficult for them to realise value for the lenders and coordinate stakeholder interests, because individual stakeholders have been able to deploy 'self-help' remedies and take unilateral action in their own interests.

As far as the contracting counterparties are concerned, they are in a stronger position with Carillion than in an administration (for example the position in Jarvis). Counterparties enjoy a better negotiating position on the terms of an assignment/novation of the relevant contracts and an acquisition of the related assets from the Official Receiver/special manager of Carillion. In an administration they would not have had immediate rights to terminate, or take enforcement action against Carillion. »

Another factor was that at the time of the appointment it was hard for an insolvency practitioner considering the appointment, without guaranteed funding, to be convinced that the purpose of administration could be achieved, and whether therefore administration was an option. For a company to enter into administration there has to be a reasonable prospect of achieving (i) the rescue of the company (ii) a better outcome for creditors than liquidation or (iii) a realisation for one or more secured creditor.

> This [compulsory liquidation] process usually takes several months… in the case of Carillion it was abridged to a matter of hours.

In addition, the power of disclaimer has been important in the case to bring to an end liability for many onerous contracts, for example leases, and this power would not have been available for administrators, but was available to liquidators.

Compulsory liquidation

It is worth commenting on the compulsory liquidation process as it is a process that not all practitioners deal with on a regular basis. The process can be commenced by a creditor or the company and involves the issuing of a petition, which is usually served on the registered office of the company and advertised in the *London Gazette*. There is then a hearing of the petition at court. This process usually takes several months, but it can be more flexible and in the case of Carillion it was abridged to a matter of hours (from the issue of the petition to the court hearing), and the requirements for service and advertising were dispensed with because of the urgency of the matter. The petition was heard in the early hours of Monday morning on 18 January 2018. The application was made by the directors for the appointment of the Official Receiver as liquidator.

The primary ground for winding up a company is that it is unable to pay its debts (section 122 Insolvency Act 1986 as amended), and the process is usually used by third-party creditors who are owed money by a company, often HMRC. The special managers have powers granted to them by the court, which are set out in the order appointing them. In this case the powers set out in the court order are comprehensive.

This process has been used by the Official Receiver previously on larger cases, often involving the public interest. It is also used in larger cases where there are potentially significant expenses or liabilities, which an independent insolvency practitioner acting as administrator or liquidator would be nervous of incurring, and would therefore decline the appointment. A previous example was SSI, the Redcar steelworks, where the potential employment, contractual, environmental and pension liabilities during the administration period were very significant and made administration impossible.

The Official Receiver and the special manager will usually have a protocol setting out how they will work together. The fees of the special manager require the approval of the Official Receiver and any creditors' committee if formed and, in the event of dispute, the court.

The Official Receiver takes control of the assets of the company and looks to realise them for the benefit of the creditors of the company, wind down the company and distribute the assets for the benefit of the creditors.

Compulsory liquidation differs from administration in a number of key ways:

a. It is usually a 'burial' rather than rescue procedure.
b. The purpose of liquidation is an orderly shutdown and winding up of the business. Administration has a three-part purpose – the rescue of the company, or a sale of the business as a going concern, or a distribution to one or more secured creditors.
c. A sale as a going concern usually involves a 'TUPE transfer' where the employees transfer to the purchaser who takes on their existing contracts and acquired rights in terms of length of service, employment terms and pension rights. The purchaser adjusts the price paid accordingly to reflect the assumption of these liabilities. The position regarding a TUPE transfer in liquidation is complicated, and rare, as the employees are usually dismissed on day one of the liquidation.
d. There is no moratorium in a liquidation preventing creditors from taking enforcement action against the company without the consent of the administrators or an order of the court.
e. The moratorium gives the administrators the chance to try to save the business in a restructuring or a sale as a going concern, without the interference of individual creditors seeking to take steps in their own interest.
f. Terminating contracts is arguably an enforcement step. Therefore in this situation, if there had been an administration, counterparties would have been forced to work with the administrator on solutions that they were driving in the best interests of all of the creditors.
g. Liquidators have the power to disclaim onerous contracts under the provisions of the Insolvency Act to stop the company in liquidation continuing to accrue liabilities under the contract. There is a detailed process set out in the Insolvency Act for disclaimer. Company searches of the Carillion companies show that the Official Receiver and the special managers have taken steps to disclaim a number of leases.

Employees in Carillion's liquidation

On the making of a winding-up order the contracts between employees and the company usually terminate. As a matter of practice employees are usually dismissed immediately. There is case law from the 1880s to support the position that automatic termination will usually be the case *unless the business is continued for the beneficial winding up of the company*. The position is not straightforward and it is unprecedented for a business of this nature to go into compulsory liquidation when it is intending to continue to honour and work on ongoing contracts and pay employees, so there are no recent cases on this point. Dusting off the 1800s cases the authorities are:

> It is unprecedented for a business of this nature to go into compulsory liquidation when it is intending to continue to honour and work on ongoing contracts and pay employees.

(1) the decision in *Oriental Bank Corporation* 1886 32 Ch D 366 says that the winding-up order would ordinarily have the effect of bringing the employment to an end. A person doing a couple of days' extra work, for example, would not constitute a waiver of that. However, the liquidator could waive the discharge of the employment contract and ask employees to accept that. The employment would then continue; and;
(2) the decision in *Re English Joint Stock Bank* 1866 VCW 341 indicates that if the company in liquidation is a continuing company then if there is work for employees to do, they would continue under their old contracts.

The Insolvency Service offers more information on the circumstances in which a special manager might seek to employ or retain staff for the business on its website.

The position regarding TUPE and whether there will be a TUPE transfer to a purchaser of part of the business, which is usually the case in the sale by administrators of a trading business, has been the subject of much discussion in this case by the purchasers of parts of the business.

The crucial question is the purpose of the insolvency proceedings. If the proceedings have been instituted with a view to the liquidation of assets of the transferor and the transferor is under the supervision of an insolvency practitioner (which is assessed at the point the proceedings are instituted), then, if subsequently employees are kept on and there is a transfer of an undertaking, certain provisions of TUPE are likely to be disapplied. The provisions of TUPE that are disapplied are the automatic transfer of employment contracts and protection against dismissal because of a TUPE transfer. However, the other aspects of TUPE will still apply including the obligation to inform and consult.

This means that if the compulsory liquidation has been instituted with a view to the liquidation of assets, but then subsequently other parties have stepped in to employ the employees and operate the contracts, then those employees will not have transferred under TUPE. They could, therefore, be put on new terms and conditions. However, if the transfer would amount to a transfer of an undertaking, then even though the transfer of the contracts themselves is excluded under

> The Official Receiver and special managers have made a success of the compulsory liquidation process in terms of saving jobs and transitioning contracts.

TUPE, then *continuity of employment* will be preserved. This is because of a separate provision in the Employment Rights Act 1996 (section 218(2)), which provides that continuity continues where an undertaking is transferred – and there is no provision disapplying this in the event of a compulsory liquidation.

Set-off and payments

Where two parties have financial claims against each other, a right of set-off allows them to deduct one liability from the other, so that only the balance is due. It enables a party to reduce or eliminate its liability to the other party.

A right of set-off may arise under a contractual term, and/or in accordance with various legal rules.

The result of exercising a right of set-off is similar to enforcing security. A right of set-off is, however, a personal right, which does not give an interest in the counterparty's property. This is in contrast to a security interest, which gives the secured party a proprietary right in the secured property.

(a) Legal set-off arises as a matter of English common law in relation to liquidated amounts claimed by a solvent entity. Insolvency set-off covers this for insolvent entities.

(b) Equitable set-off arises in certain situations in accordance with decided cases, where there are unascertained amounts.

(c) Set-off in administration and liquidation applies pursuant to the Insolvency Act 1986 as amended and the Insolvency Rules 1986 as amended. It applies automatically on liquidation under rule 4.90 which has recently been amended to rule 14.25. In administration it applies at the end of the administration.

Insolvency set-off

Set-off is important in an insolvency because in the absence of a set-off the debtor may still be obliged to pay the full amount of his or her indebtedness while only receiving back a partial amount, if any, of what is due to him or her as a creditor, by way of a dividend.

The set-off rules for liquidation are very different to those on administration. In Carillion unsecured creditors are likely to receive nothing and the payments to secured creditors are likely to be a small percentage of their debt. If a set-off is available, only the balance remaining after deducting one claim from the other would be payable.

The provisions of the contracts should also be reviewed to check on contractual set-off rights and any payments made expressly on the basis that rights to claim set-off are reserved and not waived.

> Administration will therefore remain the key rescue procedure, for most businesses, but we could see a push for reforms to the process as a result of Carillion.

Initial conclusions

The Official Receiver and special managers have made a success of the compulsory liquidation process in terms of saving jobs and transitioning contracts for essential services to new providers while collecting in significant amounts of debts due to Carillion at the date of liquidation.

This would not have been possible without the significant government funding of ongoing trading expenses, so this process is only likely to be successful to preserve jobs and businesses in larger scale insolvencies involving a public interest element where the government provides funding. Administration will therefore remain the key rescue procedure, for most businesses, but we could see a push for reforms to the process as a result of Carillion.

For the moment, we can only watch how the case progresses and the government reacts to the lessons learned. There are lots talking points arising from the case, which I have outlined in the box on this page. □

Questions from Carillion's fall yet to be answered

- The power of disclaimer has been useful for the liquidators in terms of limiting liabilities under onerous contracts, so should this be available to administrators?
- Should the rules on administration set-off be aligned with the rules on liquidation set-off? Or vice versa? The different rules are confusing for unsecured creditors.
- Do the rules on administration expenses and personal liability for administrators need revising?
- Do we need a court-based rescue procedure akin to Chapter 11 to deal with larger scale failures so the process could be more flexible in terms of liability and funding? R3 commented on this in the consultation on insolvency procedures prior to the last election and the government is due to look at this issue in the coming months.
- Will lenders look to appoint administrators earlier to avoid 'another Carillion' and improve realisations for secured creditors and give the company less time to look to restructure?
- Is there a need for reform to the law on directors' duties?
- What is the implication on the failure of Carillion on PFI as a model?
- Should the process for awarding public sector contracts consider whether the contracts will be profitable?
- What are the implications of a hard Brexit on public sector contracts already subject to very low profit margins?

ALISON GOLDTHORP is a partner at Addleshaw Goddard LLP.

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Is the fog lifting on data-handling in small cases?

Michelle Butler attempts to trim some of the thorny GDPR questions scratching at SPG members' skin.

The events surrounding the GDPR in spring determined one highly contentious question: how is an IP expected to deal with the GDPR requirements on a case with meagre assets, a disengaged director and indeterminate records? The answer from some – if we cannot be confident of managing GDPR-compliance on appointment, we should think twice about taking on the job – was jarring to a number of already hard-pressed ears.

Consequently, the 'FAQs on the GDPR: practical considerations for IPs' – a paper issued jointly by R3 and four RPBs – partly filled a desperate need. It doesn't answer all the questions, but it does attempt to recognise insolvency's practical realities.

> For an IP, the personal data of their employees and marketing contacts is by no means the riskiest part of their job.

How can SPG members with shallow pockets practically meet the GDPR's requirements? No doubt we have tackled the basics such as privacy notices, but what about the insolvency-specific challenges?

The power of policies

The GDPR demands several policy documents. For most businesses, off-the-shelf products work fine. However, for an IP, the personal data of their employees and marketing contacts is by no means the riskiest part of their job.

Unless policy documents have been designed with IPs in mind, they will need substantial reworking. For example:

- On appointment, how do you control access to, and maintain copies of, data?
- How do you decide what records (electronic and hard copy) to collect? What do you do with the remainder? How does your approach change depending on the different types of data involved?
- Do staff know what a data breach looks like in insolvency? Would they know what to do with one? How do you record your decisions and actions on a breach?
- What is your policy on leaving records with directors on MVLs?
- What are your archiving and destruction policies? What about the IPS (or equivalent) record? Do you restrict access to e-files on closed cases? When do you destroy files (electronic and hard copy)? What about case-related emails and cases that 'never were'?

Are these topics too detailed for a policy document? Not only does the ICO expect 'granular' documentation, but there is value in being detailed and specific because: (i) it forces you to justify standard approaches; (ii) staff are better equipped to do their job; and (iii) in the event of disaster, it will help you demonstrate that you took appropriate steps as an employer and data controller.

Answering the thorny questions

Does the GDPR require us to adjust long-practised pragmatic approaches? I had hoped that the FAQs would have provided clear direction, but, in the absence of answers from the ICO, it is not surprising that the RPBs/R3 have been cagey. Let's hope the ICO communicates soon so that we can stop sitting on the fence.

It would be foolhardy of me to step where the RPBs/R3 have feared to tread. However, the FAQs lead me to suggest the following:

Can records be left with a director in an MVL?

An IP's obligation to collect records to help with CDDA, SIP2 and creditors' claims is rarely relevant for small, very-solvent MVLs. Most directors are keenly interested in the success of the MVL. They may be a safe pair of hands, but it would be wise to ensure that they are committed to GDPR compliance and that they acknowledge the liquidator's rights to the records.

What records should be collected in insolvencies?

A general rule is that six years' worth of relevant records is sensible. In specific cases, there may be cause to stretch this timescale when dealing with, for example, controversial assets or liabilities or records with special retention periods – I would recommend R3's technical bulletin 104 as extremely helpful in this regard. It would also be wise to ask the directors or specialists when appointed over unusual or regulated businesses.

Am I expected to destroy records that I don't need? What if I no longer have access to the premises? What if former employees have laptops or worked from home?

The FAQs do not state that you must take extraordinary steps to gain access to and destroy unwanted records, but you 'need to take an informed view of the data risks as [you] must ensure the company's compliance with its obligations'. This certainly includes ensuring that computer equipment is wiped before disposal. It would also be wise to sever remote access and to instruct former employees to delete personal data permanently (after you have gathered what you need). Some have suggested that, on weighing up the risks of the likelihood and impact of a data breach occurring, there may be circumstances in which certain records may be abandoned.

> A general rule is that six years' worth of relevant records is sensible. In specific cases, there may be cause to stretch this timescale.

GDPR – just a storm in a teacup?

Some may wonder whether the ICO is only likely to take enforcement action against household names. Do SPG members really need to worry?

A recent ICO bulletin described a £100,000 fine on the Bible Society, a charity based in Swindon. The Society had been hacked and the ICO found that it had not taken appropriate technical and organisational steps to protect personal data.

Examples like these persuade me to take the GDPR seriously. Even if the insolvents had escaped attention, we cannot assume that SPG members are sufficiently insignificant to fly under the ICO's radar.

MICHELLE BUTLER is a partner of the Compliance Alliance and member of R3's SPG committee.

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An interview with…
Stuart Frith

The current R3 president speaks to *RECOVERY* about one of the biggest evolutions in the association's history.

Q What have been the highlights of your term as president so far?

A The major objective we are concentrating upon at the moment as part of the strategic review is to examine everything about the organisation and how it serves its members. I've been a member since 1989. There have been reviews conducted in the past, but this is the first time in my memory that R3 has conducted such a root-and-branch review of what the organisation does.

I have really enjoyed getting out and about and meeting members – I went to Manchester for a Members' BBQ, followed by the Eastern Region's annual dinner and then the President's Evening. It has been really full on. R3's Annual Conference this year was a particular highlight. We tried to ensure that this was a more informal event designed to entertain, educate and challenge.

> "This is the first time in my memory that R3 has conducted a root-and-branch review of what the organisation does."

The amount of lobbying that we have been involved in has also been very interesting. We've had round table meetings on CVAs and the latest corporate governance and insolvency consultation, as well as meeting with the insolvency minister and members of the House of Lords to get insolvency promoted up the Brexit agenda.

I spoke at the INSOL Europe R3 event in June. It was reassuring to hear that our European colleagues are entirely supportive in terms of what we are trying to do to maintain the European insolvency and judgments regulations, so that post-Brexit we are certain that we will be trading with Europe under whatever terms may prevail.

Q So there is less of a clash between British and European insolvency professionals over Brexit than there is between the politicians?

A The whole message we have for Brexit is 'if we're going to trade, it's nice to get paid now and again'. We have to ensure that there is an efficient method of getting paid in the first place, which depends in part on how you transmit goods across borders, and get paid for so doing, but there must be an efficient mechanism for the efficient resolution of any disputes and execution of judgments together with the mutual recognition of restructuring and insolvency processes.

If one mentions restructuring and insolvency to the government, it's difficult to get it promoted up the batting order for Brexit. However, if one says it is a fundamental component of any trading arrangement so as to save jobs, to get people paid for trading cross border post-Brexit, then that's a more relevant and less idiosyncratic concept to try to promulgate.

Q Is the corporate governance and insolvency white paper part of this too?

A We're still concerned about the consultation provisions being dealt with principally as a side show to several high profile bad cases. There is a »

Stuart Frith biography

● Stuart Frith graduated with a law degree in 1980 to fulfil a long-held desire to become a solicitor. He did articles in the north east, which involved assisting in dealing with noise-induced hearing loss claims for the Iron Trades Insurance Group with Middlesbrough law firm Jacksons Monk & Rowe (who featured in the eponymous Elvis Costello song). Stuart attended his first creditors' meeting in 1983 and found himself representing the director of an insolvent kitchen manufacturer in front of some of the glitterati of the Leeds insolvency community. From 1984 onwards he specialised in insolvency, even stepping out in the post-Christmas haze of 1986 to find a Glasgow bookshop that would sell him a copy of the freshly minted Insolvency Rules, which became operative on 29 December of that year.

● Stuart worked on the scandal-hit Barlow Clowes in the late 80s, during a busy period for law firms in Leeds. In 2009, he left Leeds to join Stephenson Harwood LLP, and has been involved in several sporting-related insolvencies, including the Glasgow Rangers liquidation and the last administration of Leeds United.

● Outside of work, Stuart divides his time between living in Harrogate and walking in the Yorkshire Dales with his wife Anne, and enjoying the cut and thrust of London life. He enjoys cricket (Yorkshire – obviously), plays golf (there are not many areas of Pannal Golf Course that he has not visited over the years) and, controversially, enjoys rugby union as well as rugby league.

saying that 'bad cases make bad law'. We chaired a round table event at the office of Pinsent Masons in June. Present were representatives from a broad range of organisations as well as members of the Insolvency Service. What was striking was the level of unanimity on the opinions expressed. We need to make better use of what we've got rather than wholesale new legislation to deal with specific high-profile cases. This includes advancing the 2016 corporate insolvency reforms, with the proposed moratorium, so that corporate entities other than small companies can make use of a moratorium in insolvency for turnaround and restructuring of the business. It would be helpful to ensure that our system is in the best possible shape post-Brexit because of the commercial and competitive challenges it will be confronted with. Initial impressions from government are that this message is clearly understood and any changes considered as a result of the recent consultation will be dealt with in unison with the 2016 proposals. We shall have to wait and see.

Q You mentioned one of your goals for this year was to highlight the role of the justice system and its interaction with insolvency. What does this involve?

A This involves working closely with the authorities, assisting them where we can and promoting new initiatives such as the fast-track trial system for insolvency. We enjoy a good relationship with the judiciary and both Sir Alastair Norris and Chief Insolvency and Companies Court Judge Briggs spoke at the R3 conference this year. Hearing views from IPs is useful from the judges' point of view, but IPs also hearing the judges' views on the difference between wrongful and fraudulent trading, pleading fraud in an appropriate way, and to learn about the circumstances where people may plead fraud when they don't need to were fascinating.

We have the LASPO Act review coming up and R3 will play a positive role in watching the reform of court use. We are lucky in London that we have a specialist court, but achieving consistency throughout the country is a challenge. District judges out of London have a much broader diet than the specialist insolvency judges in London and it's different in terms of approach. R3 may be able to assist with any issues that local judiciary may have and as court users we need to ensure that the relevant expertise is available. Overall efficient access to justice is the primary concern.

Q You also mentioned a drive for diversity back in April. How has R3 been working on diversity?

A It was interesting when we were arranging the conference: the organising committee consisted of a majority of women, but maintaining gender balance across speaking slots proved to be a challenge. We got a reasonable split, but there's much work still to do on that. Attitudes and professions around the world have been affected by the #MeToo movement, and these issues must be addressed.

This year R3 is celebrating 23 years of the London and South East Ladies Lunch. The lunch was started to provide a forum in which to promote women in the profession. Our profession has come a long way since the 1990s in terms of supporting women and providing opportunities for all to progress, but there is still much we can do. Fundamentally it's a case of making sure we pay the messages and knowledge forward in terms of the younger generation, whatever their gender.

> "It's a case of making sure we pay the messages and knowledge forward in terms of the younger generation, whatever their gender."

I went to my first conference in 1990 in Harrogate. I was about 32 years old at that stage and the profession seems to have aged with me. We need to give younger professionals the opportunity to develop and to see R3 as a go-to organisation that will allow them to form their own networks.

At the conference this year we sought to make the event as inclusive as we could. There was no 'top table' so that everybody was able to network throughout the evening. We had a very successful speed networking event that was tried for the first time. The aim was to put the networking opportunities more at the centre of the event. The feedback we received was very positive with regard to this initiative.

Q How else is R3 likely to evolve to meet the changes in society?

A R3 has got to listen to the members and what they want. That's what we've been doing through the strategic review. We've been encouraged by the responses we've received where we're doing things well and we've been challenged by responses where people think we can improve. We are definitely in 'listening mode'.

We have to make sure that the positive messages we get across about what our members do in terms of saving jobs is given equal measure to any issues that arise in relation to perceived regulatory issues imposed upon directors for extracting value in the twilight period of a company's life.

Pre-packs, for example, are perceived in certain quarters to be problematic. But they save a lot of jobs and businesses and they're a valuable tool for the profession. Promoting the 2015 Graham pre-pack reforms is on our agenda and, working with all stakeholders, we are looking at how those can be maintained, improved and kept at the forefront of the government's thinking as it considers whether or not to use its power to ban connected party sales from administrations.

The high profile cases always attract press attention. What you don't see in the press are the countless successful or efficient examples of a pre-pack which have created an opportunity to maintain employment or help a fundamentally viable business deal with a short-term shock. R3 should continue to promote successful cases via our contacts with the press and correct misunderstandings – ensuring that the press doesn't drive the government's agenda.

The other important thing is to maintain continuity from one presidential year to the next. This process was started by Andrew Tate and was pushed along by Adrian Hyde, who has handed the baton on to me. A cohesive strategy, running over five years plus, and implemented by a succession of presidents enhancing the progress every year, is important to ensure that we maintain this momentum.

Q To end on a lighter note: what would you have done if you didn't go into insolvency?

A I feel that any opportunity to score a century at Lords against the Aussies, to score the winning goal for Leeds United at Wembley and to win the Open Championship at St Andrews has receded. Perhaps I could have been the BBC's golf and cricket correspondent, with a specialism in rugby league. I'd like Jonathan Agnew's job, though I doubt he'd be willing to swap it for mine. □

MATT JUKES is publishing manager of *RECOVERY* magazine.

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