R3, the Association of Business Recovery Professionals | **www.r3.org.uk/recovery**

Spring 2014

RECOVERY

Professional service firms

including practice management

Technical update
The court's consideration of a trustee in bankruptcy's remuneration

Navigating the PI marketplace
Why professional indemnity insurance should be more a relief than an obligation

When firms need intensive care
A subject causing concern in the legal profession

Tips to survive and prosper in 2014
A solicitor's perspective on insolvent law firms

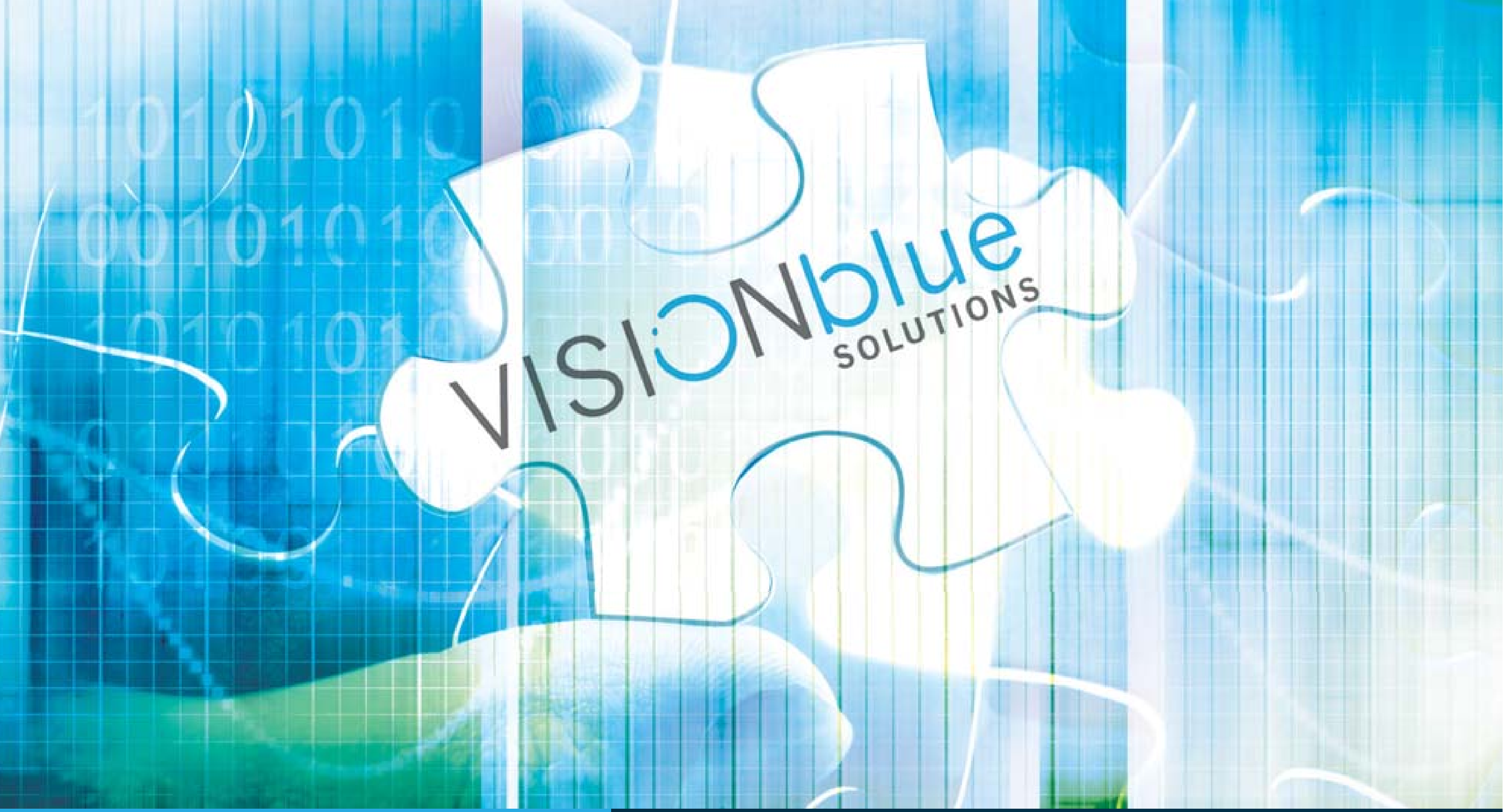
Limited Liability Partnerships
Is the LLP as safe for members as is assumed?

The proprietary claim minefield
The potential for problems and tips to avoid liability for conversion

Interview with…
Teresa Graham on pre-packs, why she wants information, not data and getting value for creditors

Careers and professional development supplement

JIEB 2013 examination results
A viewpoint from the new chair of the JIEB, Stephen Allinson



VISIONblue business solutions

VISIONblue is a software package designed by insolvency experts for use by insolvency professionals.

VISIONblue is designed to deal with the intricate requirements of all corporate and personal appointments from start to finish.

zero cost solutions

- **NO** annual site licences
- **NO** costs per user
- **NO** limits on the amount of users
- **NO** annual fixed overheads
- **NO** support maintenance costs

personal case types:

IVA • Bankruptcy • Trust Deed • Sequestration

corporate case types:

Administration • Compulsory Liquidation
CVA • CVL • MVL

reasons to use VISIONblue

- Simple cost model that is charged per appointment and is recoverable from the case as a category 1 disbursement.
- Detailed Diary for all assignment types.
- Comprehensive letter packs and forms that can be customised.
- Post receipts and payments in the Banking Module.
- Enter quick and easy relevant details into the Creditors Module, Debtors Module and Employee Module.
- Manage high volumes easily using VISIONblue's different bulk functionalities.

VISIONblue SOLUTIONS

t: (UK) 0800 072 0092 t: (Intl.) +353 1 685 4128 f: +353 1 685 4042
w: www.visionbluesolutions.co.uk e: info@visionbluesolutions.co.uk

R3 Association of Business Recovery Professionals

The Voice of Business Recovery

www.r3.org.uk

Education & Training
Conferences
Forums for debate
Social & networking events
Student support

Promoting the profession and enabling best practice.

R3 provides award winning education and training for insolvency and business recovery professionals. Its national course calendar keeps you up to date on the latest technical and legal requirements.

Forthcoming conferences
- R3 Annual Conference
- R3 & INSOL Europe International Restructuring Conference
- R3 Insolvency Conference
- SPG Forum

Courses this summer / spring
- Restructuring Day
- Charities and Community Interest Companies
- SPG Technical Review

Courses this autumn / winter
- Personal Insolvency
- Employee Issues
- Creditors Meetings
- Insolvency Litigation
- Insolvency Day
- JIEB Student Workshops
- Advanced Restructuring

Turn to **page 48** for more details

For more information on courses and conferences:
Visit www.r3.org.uk
Tel 0207 466 4234
Email courses@r3.org.uk

What do you think?

Readers' views are welcome. Got 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

Now the winter storms have receded we have a bumper spring issue of *RECOVERY* for you, packed with content focusing on professional service firms. Looking so close to home inevitably leads to consideration of the very pertinent current topic of the government's insolvency regulation and fees consultation. Our president, Liz Bingham, in her final column in office (page 6), leads the discussion.

The consultation is open until 28 March 2014, and I urge you to respond to it, individually, through your firm or by making your views known to R3.

The risk of failing to think carefully in advance about remuneration is easy to overlook, but Graham McPhie's article about *Secondus* v. *Atkinson* (p 10) holds a salutary lesson.

It has been suggested that the Office of Fair Trading conclusion on IP remuneration, which is clearly behind government thinking in its proposals on IPs' fees, was based on a false premise and questionable statistics. Professor Kempson's subsequent review of IP remuneration has been said to endorse the OFT position. It would seem to me entirely relevant for those earlier works to be scrutinised thoroughly as part of the exercise of addressing the government's proposals.

A major concern about the proposals is their over-focus on actual return to creditors, with apparently little emphasis being put on the value of an office-holder's work. Whether assets in a case should have realised £1m or £10,000, if the result is £100,000 the insolvency practitioner would earn the same. That cannot be right. It also seems to be entirely wrong that in the rather blunt instrument approach that the government proposals adopt, no account is taken of the statutory and compliance matters that need to be dealt with, whatever the return to creditors.

A further concern, as examination of the consultation documents shows, is that the law has already been drafted to put the government proposals into effect. A lot of thought has gone into the proposals and, without a lot of thought being put into, and delivered to the government on, alternatives, there is a real risk of their proposals becoming law – possibly as early as 2015.

Enjoy reading the rest of this issue!

CHRIS LAUGHTON is editor of *RECOVERY* and a partner at Mercer & Hole.

Regulars

Regulars

47
Interview with Teresa Graham

Legal update

Features

Professional service firms including practice management

26

R3 Matters

Book review

Advertising

Themes of *RECOVERY* 2014

SUMMER Not-for-profit organisations and insolvency

AUTUMN Business rescue including pre-packs and CVAs

WINTER The leisure industry

Features

RECOVERY

Editor
Chris Laughton, Mercer & Hole

Editorial board
Theo Anderton, Blake Lapthorn
Nick Cosgrove, R3
Simon Davenport, 3 Hare Court
Samantha Hawkins, Hawkins and Company
Alan Hudson, EY
Cynthia Matthews, R3
Kevin Murphy, Chantrey Vellacott DFK
Dan Redstone, Addleshaw Goddard
Graham Rumney, R3
Michael Rutstein, Jones Day
Bree Taylor, Memery Crystal LLP
Peter Thompson, HSBC

Publishing manager Sandra Kessell
Tel: 01491 828939, sandra.kessell@groupgti.com

Advertising manager Brendan McGrath
Tel: 01491 826262, Fax: 01491 833146
brendan.mcgrath@groupgti.com

Advertising executive Kym Freedman
Tel: 01491 828920
kym.freedman@groupgti.com

Art director Thomas Gray

Administration Eva Greenford, Paul Hinnell

Printed by Stephens & George

Forthcoming themes & advertising
www.r3.org.uk/recovery

RECOVERY is the quarterly magazine of R3, the Association of Business Recovery Professionals, 8th Floor, 120 Aldersgate Street, London EC1A 4JQ
Tel: 020 7566 4200, association@r3.org.uk, www.r3.org.uk

***RECOVERY* on the web**
RECOVERY is distributed to R3 members as part of their membership benefits. After an issue of the magazine has been sent to members, a PDF of the previous issue is uploaded onto the R3 website. This is so that the information may be disseminated to all the insolvency and restructuring community.
www.r3.org.uk/recovery

Published on behalf of R3 by
GTI Media, The Fountain Building, Howbery Park, Benson Lane, Wallingford, Oxon OX10 8BA
www.groupgti.com, Tel: 01491 826262

R3 Copyright Association of Business Recovery Professionals. No part of this journal may be reproduced, or transmitted, in any form or by any means, without the prior permission of the Association of Business Recovery Professionals. While every care is taken in its preparation, this journal is intended for general guidance only. Contributors' views are not necessarily those of R3 or GTI Media. References to any current matters in which the editor or any member of the editorial board is professionally involved are not to be taken to reflect the position or views of that person or his or her firm.

Sponsors

Willis

irs
the insolvency risk specialists

Two accountants gaoled

Two chartered accountants who pleaded guilty to fraud charges have received custodial sentences after the court heard that they had removed funds from struggling companies and covered their tracks to hide their wrongdoing from their business partners.

James Bradney, 48, from Kings Road, Headcorn, and Michael Worrall, 46, of Park Lane, Maplehurst, Horsham, received 42-month and 32-month custodial sentences respectively. Worrall was further banned from being a company director for five years and Bradney for seven years. At an earlier hearing they had pleaded guilty to conspiring to commit fraud by abuse of position of trust to the value of £825,000.

Bradney and Worrall committed the fraud while working at Bridge Business Recovery LLP. They removed funds from five struggling companies without the knowledge of other partners and insolvency practitioners and covered their tracks with false accounting documents. As a result, the companies forming part of Bridge Business Recovery LLP collapsed after failing to correctly register and pay their VAT and PAYE obligations. Around 40 people lost their jobs.

As chartered accountants, both men were in a position of considerable trust, the court heard. Bradney was the managing partner responsible for the business management of the Bridge business and he gained financially from the fraud through his additional drawings from the firm. Worrall was employed as the business accountant and carried out Bradney's instructions on the appropriation of funds and the preparation of the false accounts. Their offences began in January 2009 when £200,000 was dishonestly removed from the accounts of a company in liquidation with James Bradney. These funds were used to feed the Bridge Business overheads and were not disclosed to the other partners in Bridge or the creditors of the liquidated company.

In total, £915,000 was removed from different insolvent companies that James Bradney was winding up. Only £90,000 was returned and, on Monday 24 February, Worrall and Bradney pleaded guilty to one count of fraud by abuse of position of trust to the net value of £825,000.

Investigating officer Detective Sergeant Alec Wood said: 'This was not a simple case of putting your hand in the till and being caught with the cash in your pocket. Substantial police time was spent in the analysis of the bank accounts and tracing the flow of the money concerned. Furthermore, false management accounts were produced and passed to the other partners in Bridge to cover up the true position of the company.

'I would like to thank all the other witnesses both in the accounting profession and those former employees of Bridge who assisted in the investigation. I hope that these guilty pleas and sentences finally clear the reputation of Bradney and Worrall's former colleagues whose professional lives have been tainted by this gross abuse of trust.'

© Delta Whiskey

Internacionale to be wound down

Fashion business Internacionale has gone into administration for the third time since 2008. Unless a buyer can be found, its stores will be closed and jobs lost. The fashion retailer has 1,000 staff, including 200 in Scotland and 120 in Northern Ireland and it has 89 stores across the UK.

Administrators from PwC, Bruce Cartwright, Lyn Vardy and Toby Underwood, who are winding down the business, have indicated that the stores will continue to sell remaining stock as part of the process. The fashion chain was sold in a pre-pack deal last July.

Demolition company stays in business

Birmingham demolition and ground works contractor Democon has been sold in a pre-pack deal following the appointment of administrators at The P&A Partnership. Nineteen jobs have been saved in the deal, which will see a new company – Democon UK Limited – emerge from the rescue.

Gareth Rusling and Chris White, who acted as joint administrators, were appointed after Democon encountered difficulties collecting money owed and were left with suspended contracts despite posting a turnover of £2.75m last year. P&A is one of the longest established firms of business recovery and insolvency practitioners in Britain.

Unsecured creditors to receive £5bn surplus share

Administrators at PwC have announced that Lehman Brothers UK has a £5bn surplus with which to pay unsecured creditors. More than 500 PwC and former Lehman staff have been working on the administration since the investment bank's US parent company collapsed in September 2008. PwC is expected to recoup fees of £1bn as a result. In the latest update, PwC revealed that asset managers, hedge funds and major banks will be among the unsecured creditors to receive a dividend in what PwC partner Tony Lomas has dubbed a 'remarkable feat' and a lesson for regulators. Speaking to the Guardian's City editor Jill Treanor, Mr Lomas said regulators had been focusing on tackling the issue of balance sheet insolvency, with bonds that could be called upon, or bailed in, during times of difficulty.

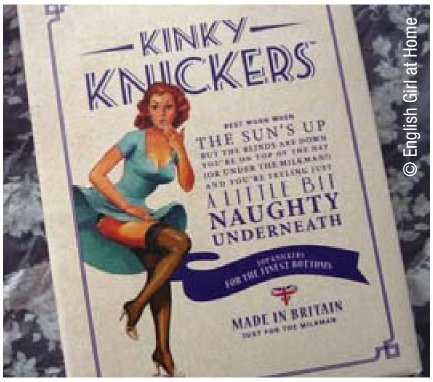
Government proposals for IP fees raise 'serious concerns'

R3 vice-president Giles Frampton has warned that new government proposals changing the way IP fees are calculated will have unintended and unwanted consequences.

'It would be the UK's creditor community that would lose out were they to be implemented,' he said as plans for improving regulatory oversight of fees and for boosting information for creditors were revealed.

'In practice, insolvency practitioners and creditors would find enforced fixed-fee caps or setting fees as a proportion of realisations unfair – indeed, the latter was abandoned as a standard practice decades ago. Arbitrary measures such as these are not always compatible with the unpredictable nature of insolvency work, and would routinely leave both creditors and insolvency practitioners out of pocket,' said Mr Frampton.

You can read up-to-date R3 news and press releases at the R3 website.
www.r3.org.uk/index.cfm?page=1008



© English Girl at Home

Kinky Knickers company rescued

Lingerie firm Headen & Quarmby, which featured in a television show fronted by retail guru Mary Portas, has been saved from administration by its management team. Director David Moore, whose grandparents started the Middleton-based business more than 75 years ago, said the firm still had a full order book despite a torrid time over the last few weeks. The Greater Manchester company called in administrators from BDO after bad debts ground production to a halt, threatening jobs and its future. Supportive suppliers and retailers, as well as staff and Mary Portas, have enabled the company to continue, however, and there are plans to get back into full production by the end of the year. In addition to Mary Portas's own Kinky Knickers label, H&Q have revealed plans to unveil a new line of vintage-inspired lingerie: Ella & Me.

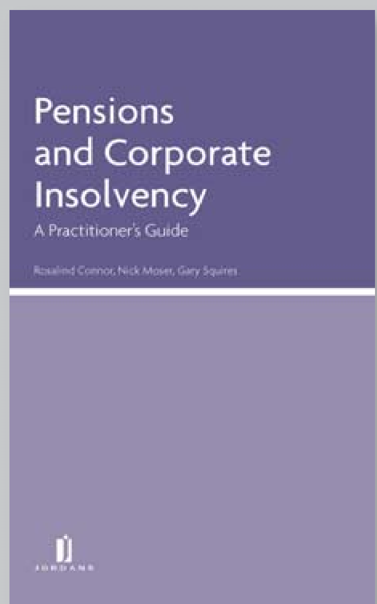
Obituary

Former R3 president, **Stephen Gale** 1957–2014

Stephen Gale, who was R3's president from 2000–2001 and a partner at Herbert Smith Freehills' finance offices in London and the Middle East, has died aged 56. He is remembered by colleagues and acquaintances as a hardworking and talented restructuring and insolvency practitioner. Described as a 'world class' restructuring lawyer by Chambers, his extensive international experience was built through working in Hong Kong, Europe, the Middle East and Africa.

Stephen advised on such high profile matters as the JJB Sports restructuring, Nortel's administration and acted for various Lehman creditors following that organisation's bankruptcy. Besides his roles at R3, he lectured on corporate recovery matters and was an honorary professor in the Faculty of Law at University College London and a member of the advisory board of the University of Sheffield, from which he graduated in 1979.

A longer obituary will appear in the summer edition of *RECOVERY* magazine.



- **Edition** First
- **Authors** Rosalind Connor, Nick Moser, Gary Squires
- **Publisher** Jordan Publishing
- **ISBN** 978 1 84661 555 9
- **PRICE** £110

Pensions and Corporate Insolvency: A Practitioner's Guide (first edition)

It strikes me that the insolvency and pensions professions have an awful lot in common. Both are high profile and highly regulated. Both deal with assets held on trust. Both are small, multidisciplinary, convivial worlds. And the two worlds are increasingly overlapping. Not just in respect of those employers with defined benefit pension schemes who face distress or insolvency. These remain a minority. But the skills of insolvency professionals are very much in demand advising on the majority of schemes where the employer is solvent. Services include employer covenant reviews, analysis of proposed transactions to determine detriment, advice surrounding granting of security and more.

> "It covers pretty much everything an insolvency professional needs to know about pensions."

This slim volume of some 250 pages is therefore a welcome addition to any firm's library. It covers pretty much everything an insolvency professional needs to know about pensions, whether advising the employer or advising trustees. It includes an introduction to pensions law, advice on dealing with the Regulator and the Pension Protection Fund (PPF) and background on financial support directions and contributions notices, regulated apportionment arrangements, and the PPF assessment period. All are covered in just enough depth. It also touches on some of the more complex areas such as Guaranteed Minimum Pension (GMP) equalisation. And the section on financial assessments will certainly help insolvency accountants who are considering diversifying into covenant reviews.

Congratulations to the authors. This reviewer recommends a 'buy'.

KEVIN MURPHY is a partner at Chantrey Vellacott DFK.

Fees and the squeeze on IPs

Six months after the Kempson report into insolvency practitioners' fees was published, we've finally heard from The Insolvency Service on their plans for updating how fees are set and regulated.

There are positives in what the government is suggesting, including efforts to increase creditor understanding. Modifications to how IPs are required to report to them will help, but government, and creditor and trade organisations could also do more.

There are also some interesting proposals regarding the role of regulators and fees, although placing the onus on regulators to run the rule over fees is easier said than done – were it that easy to implement, we may have seen it brought in before now.

However, the government's resistance to a time-cost basis for fees – in the absence of an engaged secured creditor or creditors' committee – is undoubtedly a problem. The enforced use of fee caps or fees as a percentage of valuations, as is proposed in these situations, would be unnecessarily inflexible.

A return to setting fees as a proportion of realisations would be a step back into the 1980s. Those of us old enough to remember how this worked – or didn't work

> "The enforced use of fee caps or fees as a percentage of valuations... would be unnecessarily inflexible."

– will know that setting fees in this fashion can result in fees that are wildly disproportionate to the work actually done.

And, although many IPs already provide a reasonable up-front estimate of costs, the diverse and unique aspects of each insolvency mean fees agreed in advance risk being unfair to either the IP or creditors, depending on the nature of the case.

There are other knotty issues elsewhere in the proposals: The Insolvency Service is reserving the power to create a single regulator if needs be, but it may be better served by looking closer at a unified regulatory process instead; there are also references to 'public interest' and 'public value' that require clarification lest they clash with IPs' existing obligations.

While we applaud the government's interest in improving the lot of the unsecured creditors, we are not convinced

that all of their proposals would achieve their goals. We're looking forward to working with the government to improve what's been suggested.

Following in the wake of the fees consultation is The Insolvency Service-sponsored pre-packs review. The review should be published by the end of the spring and, judging by what we've heard from the review team so far, it will make interesting reading – the preliminary proposals were subject to a very lively debate at Council in February!

Not to be outdone by The Insolvency Service in terms of changes to the profession, the Scottish Parliament is currently considering the Bankruptcy and Debt Advice (Scotland) Bill – the BADAS Bill, which could have a significant impact on the insolvency profession in Scotland.

The Bill risks worsening the conflicts of interest that already exist as a result of the Accountant in Bankruptcy's (AiB) role as government advisor and both supervisor and provider of debt management and relief solutions; it could make the bankruptcy discharge process more complex and expensive; and it proposes to remove powers from the courts – where they have been tried and tested – and hand them over to the AiB.

Working with ICAS, I'm pleased to say that R3's Scottish Technical Committee is starting to make some headway in unpicking some of the more concerning aspects of the Bill. We've met with the minister, the AiB, and the chair of the committee looking into the Bill to express our concerns, and hopefully we should see some of our public affairs activity bearing fruit soon.

Elsewhere, we have recently achieved some important 'wins' for our members that are worth mentioning: on consumer credit authorisations, for example, we've worked with the Treasury and Financial Conduct Authority (FCA) to clear up some of the confusion around whether or not IPs need consumer credit authorisation to offer debt advice once responsibility for regulating consumer credit moves from the Office of Fair Trading to the FCA.

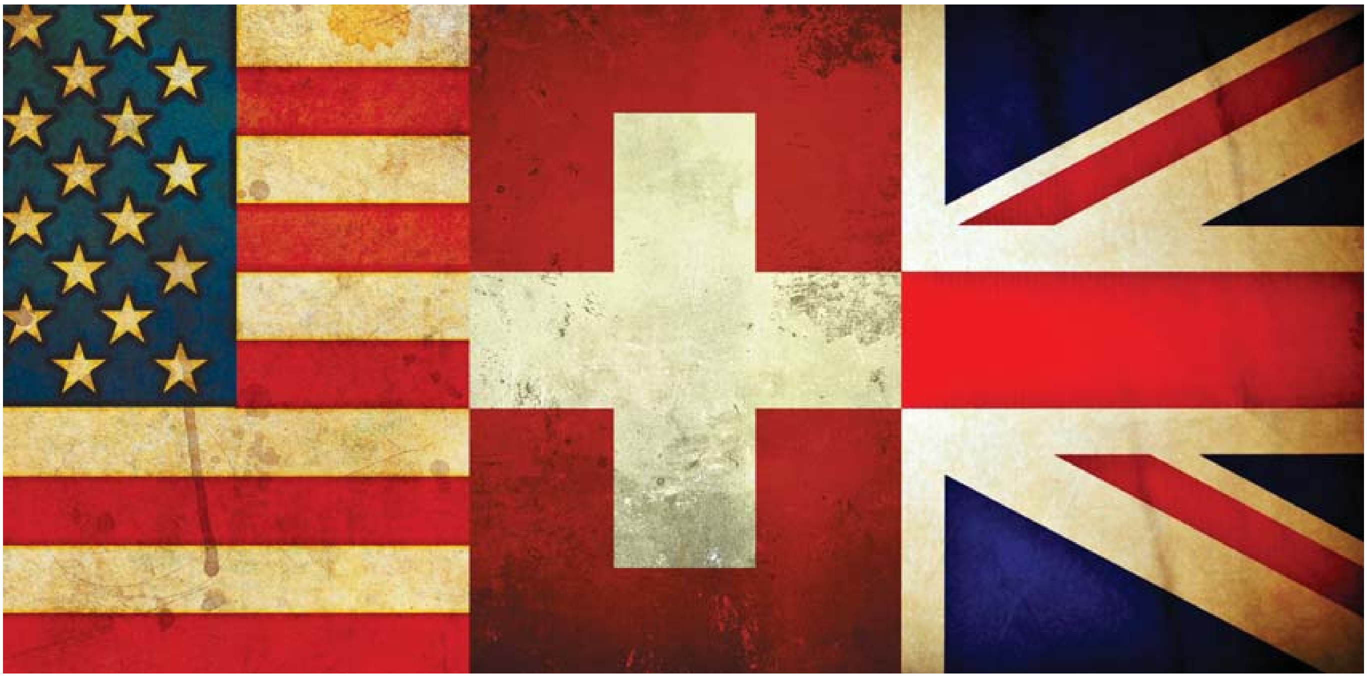
After providing feedback on several drafts of legislation, we're now at a point where IPs – and their staff – will not be required to obtain FCA authorisation to provide pre- or post-appointment consumer debt and credit advice (where appointments are those covered by the Insolvency Act), although there could still be one or two issues to clear up in Scotland.

> "The Bill risks worsening the conflicts of interest that already exist..."

Finally, as this is my last *RECOVERY* column as R3 president, I'd like to say what a pleasure it has been to have held the role over the last 12 months. It's been great to meet so many members up and down the country and to make the case on your behalf to MPs, journalists, and other organisations. Many thanks go to the team at R3 for supporting me throughout this busy, but enjoyable time, and my thanks also have to go to my assistant Sharon, who's been indispensable this year.

I'm very pleased that it's Giles Frampton, my excellent vice-president, to whom I will be handing the reins in April, and I'm sure he'll enjoy his time as R3 president as much as I have. You'll all be in safe hands. ◻

LIZ BINGHAM is president of R3 and a partner at Ernst & Young.



The raising of the Drawbridge?

John Verrill examines the complexities of foreign insolvency proceedings.

Cases from the United States

In judgments handed down in December, the US Court of Appeals for the Second Circuit and the US Bankruptcy Court for the District of Delaware reached opposite conclusions on the question of whether a foreign debtor must have assets located in the United States in order for a US Bankruptcy Court to 'recognise' its foreign insolvency proceeding under Chapter 15 of the US Bankruptcy Code. The Second Circuit judgment is important since it is to that Court that appeals from the US Bankruptcy Court for the Southern District of New York are made. The Southern District has so far experienced the biggest number of Chapter 15 applications of any court having federal bankruptcy jurisdiction.

Recognition

Chapter 15 of the US Bankruptcy Code enacted the UNCITRAL Model Law on Cross Border Insolvency in the US, its UK domestic parallel is the CBIR regime.

As with the CBIR, the authorised representative of a 'foreign proceeding' may file a petition requesting recognition of the foreign proceeding by a US bankruptcy court. The term 'foreign proceeding' is the same as the CBIR and extends to collective insolvency proceedings which can be either a 'foreign main proceeding', if opened in the country where the debtor's 'centre of main interests' is located, or a 'foreign non-main proceedings', if opened in a country where the debtor simply has an 'establishment'.

Similarly to the CBIR, an order recognising a foreign main proceeding automatically entitles the debtor to many of the rights and protections available to debtors in US Chapter 7 or Chapter 11 cases, including the automatic stay.

Drawbridge

In Drawbridge, the Second Circuit considered whether, in addition to satisfying the requirements of the definition of 'foreign proceeding', a foreign debtor must have assets located in the United States in order to obtain recognition. It involved an appeal of an order of the Southern District recognising an Australian liquidation as a 'foreign main proceeding', which had been opposed by Drawbridge Special Opportunities Fund. Drawbridge associated companies are defendants in a case brought by the liquidators in Australia and as foreign representatives they hoped to use Chapter 15 to get disclosure from the American directors of the defendants under the US equivalent of section 236 of the Insolvency Act.

> "The term 'foreign proceeding' is the same as the CBIR…"

Drawbridge argued that in addition to the recognition requirements of Chapter 15, a debtor must also satisfy the section 109(a) eligibility requirements of Chapters 7 and 11. The section provides that 'notwithstanding any other provision of this section, only a person that resides or has a domicile, a place of business, or property in the United States, or a municipality, may be a debtor under this title'.

When allowing Drawbridge's appeal, the appeal court stressed that there was no precedent controlling its conclusion 'that a debtor within the meaning of Chapter 15 is not required to have a domicile, residence, place of business or property in the United States'. It added that the issue was a matter of public importance and that finding otherwise would 'dramatically impact the jurisdiction of the United States bankruptcy courts and the use of Chapter 15 to assist in the administration of cross-border insolvency cases and the legitimate investigation of claims and assets in the United States'.

The Appeal Court concluded that Congress intended section 109 to be applicable in Chapter 15 proceedings. In so holding, it relied primarily on section 103(a), which generally provides that all sections of Chapter 1 of the Bankruptcy Code 'apply in a case under Chapter 15'. Additionally, the Second Circuit rejected the argument that section 109(a) was inapplicable because recognition of a foreign proceeding is sought by a foreign representative (which is not 'a debtor under this title', as such phrase is used in section 109).

Specifically, the court found that it 'stretches credulity' to argue that section 109 is inapplicable simply because a recognition motion is filed by a representative of the debtor and not the debtor itself, adding that 'the presence of a debtor is inextricably intertwined with the » very nature of a Chapter 15 proceeding, both in terms of how such a proceeding is defined and in terms of the relief that can be granted'.

Bemarmara Consulting

Six days after the judgment in *Drawbridge* a judge of the US Bankruptcy Court for the District of Delaware recognised a foreign proceeding as a foreign main proceeding and rejected the finding that section 109's eligibility requirements apply to Chapter 15 recognition applications. Bemarmara Consulting is in a Czech Republic insolvency proceeding and also a defendant in litigation pending in Delaware.

The plaintiff in the US state litigation, objected to a recognition application in the Delaware Bankruptcy Court, arguing, inter alia, that the proceeding should not be recognised because Bemarmara had no US assets.

> "Roughly 95 per cent of its assets, totalling over $7bn, were invested with Bernard L. Madoff Investment Securities LLC in New York."

The judge rejected this argument relying on the fact that Chapter 15 recognition is sought by a foreign representative of the debtor and not the debtor itself, a distinction the Second Circuit noted, but rejected as unsound in *Drawbridge*.

Conclusions

To be on the safe side it may well be necessary to open a bank account in the district of the Bankruptcy Court to which an application for Chapter 15 recognition is to be made, this is more particularly the case where procedural reliefs are sought, examination of witnesses and production of documents and so on.

Fairfield Sentry Limited

Fairfield Sentry was a company in the British Virgin Islands (BVI) and its registered office, registered agent, registered secretary and corporate documents were all located in the BVI. However, all of Fairfield's directors resided outside the BVI and its day-to-day operations were managed by Fairfield Greenwich Group in New York. Roughly 95 per cent of its assets, totalling over $7bn, were invested with Bernard L. Madoff Investment Securities LLC in New York. It was was the largest 'feeder fund' invested with Madoff.

On Madoff's arrest in December 2008, Fairfield suspended operations and began winding down its business. On July 21, 2009, the High Court of Justice of the Eastern Caribbean Supreme Court appointed a liquidator to Fairfield. Prior to the appointment of the liquidator, Morning Mist Holdings Ltd. (MM), a Fairfield shareholder, commenced a derivative action in New York asserting breach of duty claims against Fairfield's directors, management and service providers.

Almost a year after his appointment, the BVI liquidator petitioned under Chapter 15 seeking recognition of the BVI liquidation in the Southern District of New York. When determining Fairfield's COMI, the court looked at Fairfield's conduct during the period from December 2008, when it ceased business operations, up to June 2010, when the liquidator filed the Chapter 15 petition. The Bankruptcy Court determined that as of the Chapter 15 filing date, Fairfield Sentry had 'no place of business, no management, and no assets located in the United States'. Moreover, Fairfield's activities were limited to winding down its business from the BVI. The court held that Fairfield's COMI at the time of the filing of the Chapter 15 petition was the BVI and granted recognition to the BVI liquidation as a foreign main proceeding. Recognition triggered the automatic stay on any proceedings against Fairfield in the US including MM's derivative action.

MM appealed and argued that the court should have considered Fairfield's entire operational history in determining its COMI. Because Fairfield's operations in the BVI prior to December 2008 were minimal, adopting MM's approach could have allowed the court to decide that Fairfield's COMI was outside the BVI.

MM also argued that recognition was manifestly contrary to US public policy because BVI court records were not publicly available. The district court rejected both arguments and affirmed the Bankruptcy Court's decision. MM appealed.

The Second Circuit began its analysis by examining section 1517(b) of the Bankruptcy Code, which provides that a foreign proceeding shall be recognised 'as a foreign main proceeding if it is pending in the country where the debtor has' its COMI. According to the court, the use of the present tense indicated that the COMI determination should be made at the date of the Chapter 15 filing and not, as argued by MM, as of the date of the commencement of the foreign proceeding.

The Second Circuit also considered decisions from other courts, the vast majority of which had 'determined that COMI should be considered as of the time the Chapter 15 petition is filed'. Because a debtor's operations generally terminate at or around the time of the commencement of a liquidation, the court concluded that COMI should be determined as of the date of the commencement of the foreign proceeding. The Second Circuit rejected the Millennium approach, noting that Congress intentionally drafted Chapter 15 to reference 'COMI' rather than principal place of business.

Interestingly the court also considered the relevant European Union regulation and case law, but was not persuaded by the approach reflected in the EC regulation, which refers 'to a broader time frame for considering a debtor's COMI'. But it acknowledged that, the court should focus on whether a debtor's COMI is 'regular and ascertainable', not subject to tactical removal.

Ultimately, the court held that a debtor's COMI should be determined based on its conduct at or about the date of the filing of the Chapter 15 petition. Given the international focus on the regular and ascertainable nature of a debtor's COMI, it was held that 'a court may consider the period between the commencement of the foreign insolvency proceeding and the filing of the Chapter 15 petition to ensure that a debtor has not manipulated its COMI in bad faith'.

Because it determined that the Bankruptcy Court's factual findings were not erroneous and there was no evidence that Fairfield Sentry manipulated its COMI between the commencement of the liquidation in 2008 and the Chapter 15 filing in 2009, the Second Circuit affirmed the lower court's decisions.

The court then analysed the public policy exception to granting relief under Chapter 15. To trigger the public policy exception, an action must be 'manifestly contrary' to US public policy. The tribunal noted that this exception is to be invoked in limited circumstances concerning the most fundamental public policies of the US and would not bar an action that may merely conflict with public policy.

> "MM also argued that recognition was manifestly contrary to US public policy because BVI court records were not publicly available."

MM argued that recognition of the BVI liquidation was manifestly contrary to US public policy, because the liquidation was 'cloaked in secrecy'. The bench, however, was not troubled by the limited access to pleadings in the BVI, because (i) while the pleadings were under seal, public summaries were available, (ii) restricted access is not unusual in the BVI where only certain records are readily available to non-parties, and (iii) any non-party may apply for access to sealed documents. More significantly, it noted that public access to court documents 'is not an exceptional and fundamental' right. Indeed, it is not uncommon for documents to be sealed in US proceedings. Thus, '[t]here is no basis on which to hold that recognition of the BVI liquidation is manifestly contrary to US public policy'.

Conclusion

This judgment follows other courts that have narrowly interpreted the public policy


Bernard 'Bernie' Madoff

exception to relief under Chapter 15. The Second Circuit also joins the Fifth Circuit as the only other court of appeals that has addressed the timing of the COMI determination. By addressing the timing issue, the Second Circuit has resolved a split among the lower courts in the Circuit. It remains to be seen whether courts in other circuits will follow the Second Circuit or instead follow the rationale of Millennium.

Lehman in Switzerland

Most recently in *Enasarco* v. *Lehman Brothers Finance S.A. and Anor* David Richards J on an application by LBF's Swiss liquidators to stay proceedings concerning interpretation of an English law governed derivative contract on ISDA terms, refused the stay both under the Lugano Convention and under Article 20 of the CBIR.

The facts are complex but in essence Enasarco, as assignee of a company called ARIC's rights under the derivative contract where LBF was the counterparty, disagreed

> "Swiss law requires appeal against rejections of proof within 20 days, or the right to prove is lost."

with the Swiss liquidators' calculation of and handling of its proof in the LBF liquidation. Enasarco claimed to be owed $61.5m but the liquidators claimed that LBF was in the money for €43m. LBF consented to the lifting of the CBIR Article 20 stay so that the issues could be adjudicated by the High Court. In July 2011 Briggs J in effect rejected LBF's calculation method and ruled in favour of ARIC/Enasarco – their loss was to be the cost of a replacement transaction. There was no appeal.

Subsequently in April 2013 the liquidators rejected the ARIC/Enasarco claim and asserted that ARIC owed around $30.8m. Swiss law requires appeal against rejections of proof within 20 days, or the right to prove is lost. Enasarco appealed in time and indicated that it would seek a stay of the Swiss proceedings pending commencement in London to assert its $61.5m claim: it issued in London in August 2013, the CBIR stay having already been lifted. LBF then issued an application to stay the new proceedings and ARIC sought a declaration of non-liability to LBF.

LBF relied on the Lugano Convention arguing that its Article 27 required the English court to stay proceedings in favour of the court first seised. It was agreed that Switzerland was first. LBF also relied on discretions in both the Lugano Convention (Article 28) and in the Senior Courts Act 1981 (SCA). David Richards J held that the Swiss proceedings were closely connected with and directly derived from the Swiss bankruptcy proceedings. The Swiss proceedings therefore fell within the insolvency exclusion in the Lugano Convention – meaning there was no required automatic stay of the English proceedings. Further, David Richards J held there were strong grounds for refusing a discretionary stay of the English proceedings under either Article 28 of the Lugano Convention or the Senior Courts Act 1981. Accordingly, contractual issues under the English law governed derivative agreement fell to be determined in the English proceedings.

The judge acknowledged parallels between the Lugano Convention and the EC Judgments Regulation. In doing so he accepted that Virgos-Schmit Report and decisions of the ECJ on the nature and extent of the insolvency exclusion in the Judgments Regulation were of assistance in the interpretation of the Lugano Convention.

Referring to *Gourdain* v. *Nadler* (C-133/78) where the ECJ said that to fall within the insolvency exclusion, decisions must 'derive directly from the [insolvency] and be closely connected with the [insolvency] proceedings…' he concluded that at the heart of the case was whether the Swiss proceedings were sufficiently closely connected with and directly derived from the Swiss bankruptcy proceedings. If so the Lugano Convention, which would require an automatic stay of the English proceedings would be ineffective.

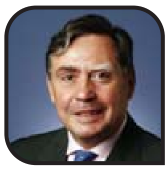
It was held that the Swiss proceedings clearly fell within the insolvency exclusion in the Lugano Convention (and by extension, the Judgments Regulation) because the proceedings arose, and could only arise, under Swiss insolvency law. They were an essential part of the Swiss bankruptcy proceedings, and the key driver of such proceedings, the distribution of assets to creditors, had to take place in the (Swiss) court dealing with the liquidation. The purpose of the proceedings was not simply to establish whether Enasarco had a valid claim, but principally to determine the quantum and priority of the claim for the purposes of the liquidation, solely an issue of Swiss bankruptcy law.

David Richards J expressed the hope that the Swiss court would be helped by having the judgment of an English court on matters under the ISDA form, given that it was governed by English law and he rejected the alternative argument that a

> "The English court was a better authority on English law!"

Swiss court could accept evidence on English law and reach its own conclusion. The English court was a better authority on English law!

Enasarco was not banned from the English proceedings simply because it had been forced to participate in the Swiss proceedings. Enasarco had no choice but to issue its challenge to the schedule of claims in Switzerland within the 20 days required if it wished to preserve any right it might have to participate in the distribution of LBF's assets. The choice of law was that of the liquidators when electing to exclude the claim from the list of participating creditors which compelled Enasarco to participate in the Swiss proceedings. That was not a wholesale submission to the jurisdiction for all purposes. ◻



JOHN VERRILL is a partner at Chadbourne & Parke (London) LLP.

How much in future?

Graham McPhie examines the court's consideration of a trustee in bankruptcy's remuneration.

On 17 May 2013, Mr Registrar Jones, delivered the judgment in the case of *Secondus* v. *Atkinson* [2013] BPIR 632. The application before the registrar was to annul a bankruptcy order on the grounds that the bankruptcy debts and expenses had all been paid or secured to the satisfaction of the court under s282(1)(b) of the Insolvency Act 1986. The difficulty that arose was that the expenses of the bankrupt had not been paid or secured and there was an argument whether statutory interest remained due on the petition debt – the only debt in this bankruptcy. The estimated payment in full calculation as at 31 March 2013 was £50,655. The bankrupt's case was that interest was not due to the creditor, the expenses claimed by the trustee were unreasonable and it was wrong for her to have to pay unreasonable sums to have her bankruptcy order annulled. Her position was that she would pay a reasonable total and the bankruptcy order could be annulled with the court to determine what that reasonable total would be.

The details

The bankruptcy order had been made on 1 March 2010, upon a petition presented on 19 April 2010. The petition debt was for unpaid service charges of £6,248.57. The bankrupt had her automatic discharge suspended.

By 13 August 2010, the mortgagee of the property had paid a total of £10,468.37 to the petitioning creditor and added that liability to the secured loan account. No doubt, that mortgagee was exercising its right to protect its security by making a payment to the landlord to prevent potential forfeiture of the lease.

The trustee in bankruptcy was appointed on 21 September 2011. It is not recorded in the judgment how that appointment came about but, as there had only been one creditor of the bankrupt who had been paid in full, presumably the appointment was by the secretary of state.

> "A trustee should not and cannot charge such high fees for a small and standard insolvency."

A notice under Section 283(a) was served upon the bankrupt on 28 October 2011 and on 18 November 2011, the bankrupt's solicitors wrote to the trustee's office identifying payments made to the long lessors of the property and raising an issue about whether she should have been made bankrupt. On 2 December 2012 the trustee agreed to hold the administration of the estate for two weeks.

On 30 December 2011 a creditors' meeting was held in which the trustee's remuneration was to be calculated on a time-costs basis. The registrar made the point that he was unclear who the creditors were when the petitioning creditor had been paid.

On 28 February 2012, the bankrupt's solicitors were provided with an estimated payment in full schedule that listed the petition debt plus statutory interest (£163.03), fees of £6,000 plus VAT, the Official Receiver's remuneration (£1,715), petition costs (£1,500 estimate), property insurance (£630), *ad valorem* fees (£5,420.88) and a total sum to be paid of £25,331.28.

On 12 March 2012, the trustee said that, although the petitioning creditor had acknowledged being paid in full, this was a preference and the trustee had a duty to have the amount refunded to the bankruptcy estate. The bankrupt was advised that the administration of the bankruptcy would continue within 14 days, which would include reclaiming the funds paid to the petitioning creditor and could lead to an application for an order of possession and sale against the property.

On 3 April 2012 the trustee said that payments of £10,468.37 could not be treated as payment to the petition debt because it was made after the bankruptcy order and therefore there were no grounds to annul the order except by payment in full. In addition the assertion of a preference was repeated as was the fact that the trustee considered statutory interest was due. At that point the estimated payment in full calculation was increased to £32,321.79. The trustee's fees had increased to £9,500 plus VAT.

On 31 August 2012 an application for possession was made.

On 27 November 2012, the bankrupt made an application to annul.

Preference regime

The court, rightly, gave the argument that the payment to the petitioning creditor was a preference short shrift. For some reason, perhaps it considered it did not need to do so, no reference was made to the fact that by s341 of Insolvency 1986, the preference regime is only applicable to a payment made before the presentation of the petition; the court decided the issue on grounds that the payment by a third party could not be a preference and nor could it be a void disposition under s284. The timing of the s293 notice by the Official Receiver is not recorded in the judgment and so it cannot be known whether s284 would have applied at all. However, for possibly the wrong or incomplete reasons, the registrar did rightly conclude that the payment could not be a preference.

The trustee had sought to argue that the bankrupt had used monies she wrongly raised upon security of her property but the court rejected this as an incorrect analysis. The payment had been made actually by the mortgagee and the fact that the mortgagee added the resulting debt to the loan did not alter that fact. As such, the trustee had been wrong to add interest to a debt that had been repaid. The registrar considered that the approach that a trustee should have adopted was that the only liabilities that needed to be paid were the expenses of the bankruptcy. On around 18 November 2011 (date of knowledge of the mortgagee's payment on part of the trustee) all the trustee needed to do was to obtain from the bankrupt, or realise from her estate, sufficient funds to pay the expenses of the bankruptcy.

The SIP 9 report

It is unclear from the judgment precisely what remuneration information the registrar had but the implication is that he was dealing purely with a SIP 9 report as he went on to state that it was impossible to identify from the SIP 9 report precisely how much of the trustee's costs were attributable to the error. He makes no reference to any other time-costs detail or summary of work carried out. There was no specific category in a SIP 9 report for work carried out in respect of the petitioning creditor and so the implication would seem to be that the registrar had no further remuneration information. In the context of this particular item, that may have made little difference to the outcome but the registrar did not know precisely what sums should be disallowed owing to the error that was made.

The registrar was particularly troubled by the issue of proportionality and the SIP 9 report totals were as follows:

Appointment formalities £1,268.50; statutory reporting £405; statutory review/case compliance £1,972; case accounting £137.50; fee and work-in-progress £114.75; dealing with the property £1,146; annulment application £668; dealing with possession and sale application £2,025; general administration £3,422; petitioning creditor/preference payment £330; total £11,788.75.

Turning to the breakdown of staff engaged, this was as follows:

Partner (2.8 hours), managers (5.8 hours), other professionals (43.16 hours) and support staff (0.70 hours). The rates being charged were £400 for partner; £270 for manager; £225 for an assistant manager; £150 to £160 for the administrator; and £175 for a cashier/case accountant.

No justification

The first issue the registrar raised was why the trustee was able to command such hourly remuneration after accepting an appointment for a bankruptcy with one creditor, debts of £6,248.57, possibly statutory interest £1,476.37, and the costs of the Official Receiver £1,715. There was apparently no answer or explanation provided in justification. The registrar considered that the charging rates were far too high as this was not a complex case. A trustee would normally charge fees at such a level when working for large insolvencies that inevitably required particular expertise and involved complex issues. A trustee should not and cannot charge such high fees for a small and standard insolvency just because that was the apparent normal charge out rate. The registrar considered that all of the other rates to be charged by the various categories were also too high. The registrar felt this was a team whose fee structure was good for substantial insolvencies and not standard bankruptcies with one creditor and a debt of £6,248.57.

> "The registrar felt this was a team whose fee structure was good for substantial insolvencies and not standard bankruptcies with one creditor."

The registrar considered that the rates should be: £200 for the partner; £150 for manager; £100 for assistant manager; £100 for the administrator; £100 for cashier/case accountant. Applying those rates produced a total of £5,796.

Guideline rates

The insolvency practitioners may be surprised about the court setting such rates but the Supreme Court Costs Office has been undertaking such steps for a number of years and the last guideline hourly rates for summary assessment of solicitors' costs produced in 2010 set rates for the following:

- **Grade A** – solicitors over eight years' qualified experience;
- **Grade B** – solicitors or legal executives over four years' qualified experience;
- **Grade C** – other qualified solicitors or legal executives;
- **Grade D** – trainee solicitors, paralegals or equivalent.

These gave guideline rates as follows:

- The Inner London EC postcode costs – Grade A £409; Grade B £296; Grade C £226; Grade D £138.
- The amounts allowed for London (W1, WC1, WC2, SW1) – Grade A £317; Grade B £242; Grade C £196; Grade D £126.
- For the Outer London three boroughs – Grade A £229–£267; Grade B £172–£229; Grade C £165; Grade D £121.

The guideline hourly rates for solicitors are not mentioned in the judgment and it can only be presumed that these were not referred to by either parties or the judge but practitioners should be aware that those who are assessing costs will be well versed in the summary assessment of solicitors' costs and these particular guideline hourly rates. It is, therefore, not an unusual exercise of the court's discretion to consider that the rate set by the party claiming the costs is not necessarily the starting point for the assessment of the costs but the judge's own considerations as to what he considers to be the amount properly chargeable with any guidelines being precisely that, merely guidelines.

Proportionality

The trustee early in the judgment, therefore, was in a position in which his remuneration claimed in the SIP 9 report of £11,718.75 had been reduced to £5,700.96 with the court having decided that he had been wrong in making assertions regarding payments to the petitioning creditors.

However, the issue that the court had to go on to consider was proportionality. The registrar went on to say that the figures as determined were still not proportionate. That may have been because the work carried out was more extensive than required. On the positive side, the registrar did recognise that there is work that any trustee must fulfil whatever the size of the estate.

The registrar summarised that the trustee had to:

1. Carry out the normal statutory duties required for each bankruptcy;
2. Check the petitioning creditor had been paid in full, including interest and costs;
3. Contact the bankrupt to inform her of the expense of the bankruptcy that had to be paid and in the absence of funds steps would need to be taken to obtain possession;
4. Instruct solicitors to deal with possession and sale;
5. Deal with the annulment application.

The registrar considered that these matters were nothing other than standard and they were far from complex.

The point was made by the court, decision in *Mirror Group Newspapers* v. »

Maxwell (No 2) [1998] 1 BCLC 638 that the time spent represents a measure of the service rendered and the cost of rendering it but not the value of the service. Remuneration should be fixed so as to reward value and not to indemnify against cost.

It is submitted that in this particular scenario of a bankruptcy estate with small sums of creditors, those creditors' claims being paid in full by a third party, any trustee in bankruptcy is going to be in difficulty in arguing what value has been produced to the estate once a creditor has been paid in full and the only action is for payment of remuneration and expenses.

> "Remuneration should be fixed to reward value and not to indemnify against cost."

Nevertheless that is a function that does have to be carried out. It would seem that the trustee would have to rely upon the fact of his appointment having prompted creditor payment. In this case, that had happened before the trustee was appointed although it seems no one was aware of that fact as the court accepted the trustee did not know until November 2011. It cannot be ascertained from the judgment whether or not the Official Receiver had been notified of the payment.

As regards the possession proceedings, on a further positive note, the registrar did make the helpful comments that, as the only source of funds available to pay the expense of the bankruptcy were the property or the bankrupt herself, as the bankrupt did not pay the trustee it was plain that the trustee had to realise the property.

The difficulty, however, was that the estimated payment in full schedule sent to the bankrupt had been incorrect because of both the unreasonable hourly rate and the misunderstanding concerning the petitioning debt. Possession proceedings are standard fare for insolvency practitioners and did not justify any increase in the hourly rates that had been identified. Turning to the trustee's fees in connection with the possession proceedings the court considered that:

- 7.7 hours for dealing with the property was excessive, even taking into account the trustee's explanation that he had to liaise with Land Registry because the Official Receiver had not entered a restriction because of the existence for a trust affecting the property and
- 13.5 hours for dealing with the possession and sale application was disproportionate when this was a straightforward application that had no unusual features and was prepared and dealt with by solicitors.

Those hours would be reduced by two-thirds.

Value and benefit

Turning to the annulment application, the court made a point that normal proceedings were issued in response to the possession claim. The total amount that the bankrupt was able to raise, it was said, was no more than £35,000. The inevitable conclusion the court reached was that the bankrupt was entitled to take objection to the totals in the estimated payment in full schedule and to ask the court to examine those costs. Turning to the question of value and benefit, the court considered this overlapped with the decision to reduce the hourly rates. That did reduce the remuneration but, taking the global approach, the court considered that 64.45 hours was too long for this bankruptcy. It would reduce the remuneration even further by taking into account the requirement for value to a figure in the region of £3,500. It was accepted that there had been the absence of a positive approach from the bankrupt by not making an early application for annulment or paying expenses that had to be paid and the administration of the bankruptcy would be more difficult than it might otherwise have been, which led the court to a conclusion that £3,500 was too low and that should be increased by £1,000.

Looking at the estimated payment in full calculation the registrar concluded as follows:

- The petition debt and statutory interest would be deleted;
- Trustee's fees incurred to date would be reduced to £4,500;
- Trustee's estimated fees to complete would be reduced to £1,000;
- Items for legal fees totalling £10,472.50 would remain subject to the bankrupt's rights to apply for taxation;
- The Official Receiver's remuneration of £1,715 would be allowed but may be recoverable from the deposit;
- Petition costs of £1,500 would be deleted as those had been paid; other fees or valuations, bond, advertising, Land Registry, the Companies House charges, insurance, bank charges would stand totalling £2,447.80;
- There was an issue whether or not VAT would be applicable owing to the location of the bankrupt abroad. A total of £18,520.30 was provided although the registrar did not make a final decision that this was the sum payable as there were still the issue of the VAT and *ad valorem* fees to be finalised.

A harsh lesson

The judgment highlights again the difficulties faced by trustees in bankruptcy in having costs assessed. The reduction in rates allowed is not unusual in the context of a court assessing costs and the key factors of proportionality and value will always be borne in mind in relation to any insolvency estate and the remuneration to be claimed.

The trustee's position was not assisted by the wrongful assertions of preference and interest remaining due on the petition debt and it can be seen that a judge could reasonably consider that those errors caused more work to be carried out than was properly required such that the remuneration should be reduced. The case is a harsh lesson of the need to ensure the legal accuracy of assertions made against any party by an office-holder and the trustee's role is not to seek to recoup monies at all costs when those monies are not properly recoupable.

Hindsight is, of course, a wonderful thing and the failure by the bankrupt to apply to annul the bankruptcy order when the petition debt (indeed the only debt in this bankruptcy) had been paid about four months after making the bankruptcy order did have an impact on fees being incurred but the court gave recognition to this by increasing remuneration by £1,000.

The only wise approach, it is submitted, that could be taken is for any trustee to consider at all stages in the administration of the bankruptcy the proportionality of the action that is being taken in relation to the level of the bankruptcy debts and the assets to be realised as well as the value that will be achieved for the estate in taking those

> "It was accepted that there had been the absence of a positive approach from the bankrupt."

actions. Further, if remuneration is an issue, we would urge that far more information is given to the court than is provided by a SIP 9 report. It would make sense for there to be full compliance with the practice statement on the assessment of office-holder's remuneration so the court has more details of the work carried out, the fee earners who carried out that work, the proportionality arguments and the value that has been achieved for the estate.

The writer suspects that the reality of the future for the assessment of trustee's costs is that this case and its like will be far more the norm and not the exception. The trustees will need to consider the value of the claims they are dealing with as well as assets to be realised in order to make a judgment call over what steps should be taken, the rate that needs to be applied per hour to this particular work and the amount of work required to bring the administration to an end.

GRAHAM MCPHIE is a partner at Moon Beever.

Recent case summaries

Daniel Lewis provides two personal insolvency case updates

Applications to annul bankruptcy orders will often provoke lively argument about the trustee's fees and expenses and who (if anyone) is to foot the bill. The fact that those fees and expenses will often have been caused by arguments about the reasonableness of the fees and expenses is a paradox often commented upon. Two recent decisions of the Court of Appeal provide some further guidance as to how the amount and liability for the trustee's fees are to be dealt with, in the context of applications under both sub-sections 282(1)(a) and (b) of the Insolvency Act 1986.

***Oraki* v. *Dean & Dean* [2013] EWCA Civ 1629**

Facts: In September 2005 and January 2006 respectively, Dr and Mrs Oraki were adjudged bankrupt on creditor's petitions presented by their former solicitors, in respect of a judgment for a payment on account of their professional fees. They obtained their discharge one year later.

In fact (unknown at the time that the bankruptcy order was made) the Orakis' 'solicitor' was no such thing. He was a convicted fraudster and was not properly qualified. It followed that the bankruptcy order should not have been made, since the petitioner was not entitled to any fees.

After a number of unsuccessful attempts to annul before the true position was known, on appeal the deputy judge annulled the bankruptcy orders on conditions, including a requirement that the Orakis meet their trustee's costs and expenses. In ordering the Orakis to pay the trustee's costs the Deputy Judge took into account the fact that the solicitors would be unable to pay. His order also gave the Orakis permission to apply to recover the sums paid in respect of their trustee's costs from their former solicitors (for what that was worth).

On appeal, the principal ground of challenge was that the deputy judge was wrong to order the Orakis to meet their trustee's costs when they were 'wholly innocent'.

Held: There was potential confusion in the use of the word "wholly innocent". A distinction was to be made as between the Orakis and their former solicitors and the position as between the Orakis and their trustee. As to the latter there was no clear disparity between the innocence of the two parties, such as to justify relieving the Orakis of the trustee's costs.

That the judge took into account the fact that the solicitors could not pay was also not faulted, since to make an order against the solicitors would not have been likely to result in any payment of the trustee's costs. The 'guiding principle' was that the proper expenses of the trustee should normally be paid or provided for before the assets are removed from him by an annulment order.

> "The 'guiding principle' was that the proper expenses of the trustee should normally be paid or provided for…"

***Hunt* v. *Salliss* [2014] EWHC 229**

Facts: A bankruptcy order was made against Mr Salliss in December 1993 on a creditor's petition presented by Barclays. Barclays was owed almost £2.5m but did not prove in the bankruptcy (despite being invited by the trustee to do so). Other creditors' claims amounted to approximately £14,000. The only asset in the bankruptcy were the pension plans, which were not drawn down until May 2007 (after the bankrupt had obtained his discharge). In order to receive the pension benefits, Mr Salliss needed to have his bankruptcy annulled. He paid off the claims of creditors who had submitted proofs, but not the Barclays debt. He then applied for annulment on the basis that the debts and expenses of the bankruptcy had been paid in full.

In the same application, Mr Salliss also challenged the trustee's fees. This challenge resulted in a substantial increase in the trustee's costs and expenses. The trustee applied to vary the basis of remuneration (having previously been fixed at £2,000 plus a percentage of realisations).

The deputy registrar refused to annul the bankruptcy, in particular because of the substantial, but unproved, debt to Barclays and the fact that there would be an insufficient return to meet the trustee's expenses. He granted the trustee's application to vary the basis of remuneration.

Held: The Barclays debt was irrelevant since they had been informed of the intended annulment application and had decided not to prove for the debt. This debt should not have been taken into account in dismissing the annulment application. That left as the only issue the trustee's remuneration in deciding whether or not the bankruptcy should be annulled. The question of the trustee's remuneration would have to be remitted, including the application to vary the basis of remuneration. It was only after these applications had been reconsidered (applying the principles in Part Five of the Practice Direction (Ch D: Insolvency Proceedings)) that the annulment application could be resolved. ◻

Practice points

- In the absence of conduct disentitling the trustee to his fees and expenses, these should be met by a party capable of paying, even if this means that the burden falls on the party against whom a bankruptcy order was wrongly made.
- Only proved debts count in determining whether the bankruptcy debts have been paid in full, providing that adequate notice is provided to creditors who have failed to submit proofs.
- In determining an application to vary the basis of remuneration, Part Five of the 2012 Practice Direction on Insolvency Proceedings should be applied.

DANIEL LEWIS is a barrister at 3 Hare Court.

WILLIS INSOLVENCY SERVICES

We provide specialist insurance solutions to insolvency practitioners and fixed charge receivers. Our market leading open cover scheme includes:

- Premium payment flexibility
- Pro rata premiums – you only pay for what you use
- 30 days automatic cover from date of appointment

Underwritten by an established scheme insurer and delivered by a team of experienced insolvency insurance professionals.

**FINDING BETTER WAYS.
WILLIS INSOLVENCY SERVICES.**

For further details on our Open Cover Scheme, Bonding, Health and Safety and Fire Management Services please contact:

Mark Sanderson
Managing Director
Mobile: +44 (0)7771 678571
Email: mark.sanderson@willis.com

Samantha Taylor
Deputy Managing Director
Mobile: +44 (0)7956 661162
Email: samantha.taylor@willis.com

Sadie Clarke
Client Service Director – North/Scotland/N.I
Mobile: +44 (0)7943 825923
Email: sadie.clarke@willis.com

Andrew McIntosh
Client Service Director – Midlands/South
Mobile: +44 (0)7944 918542
Email: andrew.mcintosh@willis.com

Alan Stockdale
Client Service Manager – North/Scotland/N.I
Mobile: +44 (0)7908 995891
Email: alan.stockdale@willis.com

Nick Christie-Rundle
Client Service Manager – Midlands/South
Mobile: +44 (0)7956 306416
Email: nick.christie@willis.com

Willis Insolvency Services is a trading name of Willis Limited, Registered number: 181116 England and Wales.
Registered address: 51 Lime Street, London EC3M 7DQ.
A Lloyd's Broker. Authorised and regulated by the Financial Conduct Authority for its general insurance mediation activities only.

FP1369/11456/11/13

Legal Q&A

Katie James answers your insolvency queries.

As the trustee in bankruptcy of a debtor who secured her business obligations by granting a charge over the jointly owned matrimonial home, I am seeking possession and sale of the matrimonial home. The husband is claiming the equity of exoneration – is he entitled to do so?

Where a charge has been granted by the joint proprietors of a property to secure the debt of only one of those joint proprietors, the other proprietor stands in the position of a surety. Once the chargeholder has been paid, the surety will be entitled to an indemnity from the debtor, but this indemnity is of little value when the debtor becomes bankrupt. The equity of exoneration was therefore developed so that the debtor's indebtedness is discharged from the debtor's interest in the property before the chargeholder can look to the other proprietor's interest for payment. This goes further as the equity of exoneration gives the innocent party a proprietary interest in the debtor's share of the property, making the innocent party a secured creditor of the debtor.

> "If the husband has no independent means of his own… the equity of exoneration cannot be applied."

However, much will depend on the intentions of the parties at the time the charge was created and whether the circumstances justify the inference that the parties intended the debt to be paid solely by the debtor.

If the indebtedness has been incurred so that a certain standard of living can be maintained for the benefit of both proprietors, it is unlikely that the equity of exoneration will be applied.

Do check to see if the sum borrowed was paid into a joint account, whether it was used for household expenses, holidays or to purchase other assets of which the husband had the benefit. If the husband has no independent means of his own, it is likely that he was reliant on the bankrupt's income so that the equity of exoneration cannot be applied.

These principles have recently been reinforced by Chief Registrar Baister in the case of *Lemon & Wood* v. *Chawda and Chawda* (2013) Nexis Lexis 88 and Mr Justice Morgan in *Day* v. *Shaw* [2014] EWHC 36 (Ch). The cases of *Bagot* v. *Oughton* (1717) 1 P Wms 347 and *Gray* v. *Dowman* (1858) LJ Ch 702 confirm that the equity of exoneration can be applied in favour of a husband as well as a wife.

I am acting as the liquidator of a group of companies, X Limited, Y Limited and Z Limited. All three owe significant sums to Bank A and there is also secondary lending to all three companies by Bank B. Only X Limited has granted any security. X owns four properties, all of which are charged to Bank A but only two of which are charged to Bank B. Who gets what?

Having obtained all of the documents from A and B, firstly confirm that there are no deeds of priorities or guarantees. If this is the case, as separate legal entities, all of the assets and liabilities of each company will be dealt with separately, notwithstanding the fact they form part of a group of companies.

X has four properties, all of which are charged to A (the A properties) and two of which are subject to charges in favour of A and B (the common properties). Subject to valuations, it is likely that A can be paid in full from the A properties, leaving B to be repaid from the common properties. However, if A enforces its security against the common properties, it is likely that B will not get anything. In this situation, the equitable doctrine of marshalling comes into play.

A creditor can take advantage of marshalling where:

- Its debt is secured by a second mortgage over a property;
- That property is also subject to a first mortgage in favour of a mortgagee that is also a creditor of the debtor;
- The first mortgagee also has security for that debt in the form of another property;
- The first mortgagee is paid from the proceeds of the sale of the common property;
- The second mortgagee remains unpaid; and
- The proceeds of the sale of the other property are not required to pay the first mortgagee.

The aim of marshalling is to ensure that the second mortgagee is not prejudiced by the arbitrary decision of the first mortgagee to enforce its security against the common property and it is particularly useful in insolvency situations, where it will maintain the position of the second mortgagee against unsecured creditors. However, it cannot be used to cause injustice to the debtor by increasing the amount owed, so that, in your case, there must be a valid debt owed by X to B for marshalling to take effect.

Once you have realised the properties, A can be paid from the A properties and B can be paid from the common properties. A and B will then be unsecured creditors of Y and Z.

However, if there is a contractual obligation on A to enforce its security against the common properties (e.g. because the other property is trading premises rather than investment premises) marshalling will not be available. Therefore the terms of the security and any deeds of priority should be checked carefully.

If there is a cross-guarantee between the three companies in favour of A (or indeed B), which is secured by the charges in favour of A, then as long as those obligations have become a debt owed by X to A, A will be entitled to payment of those sums as well from the proceeds of the sale of the A properties, and vice versa if the cross-guarantee is given to B. ◽

KATIE JAMES is an associate solicitor in the corporate recovery group at Boyes Turner LLP.

Intervention – a procedure in decline?

Fred Satow examines in detail what intervention is, how successful it is and asks how frequently it will continue to be used in the future.

There have been a number of high profile law firm insolvencies over the last few years, Halliwells (2010), Cobbetts (February 2013) and most recently Manches (October 2013). All were successfully rescued through pre-pack administrations, with value being obtained for their assets, including work in progress and debtors, their businesses preserved and employee jobs saved. However, unusually for a profession, the solicitors' regulator, the Solicitors Regulation Authority (SRA) can close down a solicitor's practice immediately through intervention, as described below, without the need for any insolvency procedure (the Council for Licensed Conveyancers has similar powers).

It is difficult to obtain hard numbers on law firm insolvencies but The Insolvency Service statistics for Q3 2013 show 716 creditors' voluntary liquidations and 59 compulsory liquidations among the professional, scientific and technical sector. It is likely that administrations will be more prevalent among larger firms, with liquidations prevailing among smaller firms.

> It is likely that administrations will be more prevalent among larger firms, with liquidations prevailing among smaller firms.

While interventions have decreased in number since 2011 (when there were 62) to 37 in 2012 and 47 in 2013, their cost has increased from £1.97m in 2011 to £3.11m in 2013. The forecast cost of intervening in Cobbetts was £4.3m. In the six months to October 2013, the Solicitors' Compensation Fund (the Compensation Fund), from where such costs are paid after the annual budget is exceeded, has reduced by a third to £45m, albeit a large part of this reduction is due to compensation paid in respect of one particular law firm[1].

So what is intervention?

In an intervention, the SRA closes down a solicitor's practice at once. The SRA (in tandem with its intervening agent, another regulated law firm, and with Capita, which deals with logistical aspects of the

intervention) takes all papers and documents relating to clients, including files and accounting records, as well as all the money held by the firm, including client monies. Each intervention is approved by the SRA's Panel of Adjudicators, who are operationally independent.

Thereafter the firm can no longer act for its clients, nor can it continue to trade. Depending on the grounds for the intervention, the practising certificate of the intervened solicitor(s) may be suspended.

The intervening agent then seeks to return live client files to clients (or to another law firm to act on behalf of the client). The SRA (or its agent) will also conduct an analysis of the monies held with a view to returning them to their rightful owners. This process can take some time.

Emergency funding

If the client matter is urgent, for instance completion of a conveyancing transaction, the intervening agent can act on behalf of the client – if needed the Compensation Fund can make emergency funding available for the transaction as client funds cannot be utilised until the analysis above is completed. In addition, any client can apply for a grant from the Compensation Fund, which can be paid if the client suffers or is likely to suffer loss as a result of the solicitor's dishonesty or loss and hardship from a failure to account for client monies. Generally the client will arrange for another firm to act on its behalf. Clients may make these claims while the analysis of the accounts is ongoing if they are unable to wait for their funds – once the accounts are able to be paid out, the Compensation Fund will then receive the money which was due to that client.

The SRA intervenes on a number of grounds, including:

- To protect the interests of clients, current, former or potential;
- If it suspects dishonesty on the part of someone at the firm;
- If the only solicitor at the firm has been made bankrupt, sent to prison or been struck off the roll of solicitors;
- The practice has been abandoned; or
- If there have been serious breaches of the SRA Code of Conduct or the Solicitors Accounts Rules.

Its purpose in intervening is to protect the interests of clients, the public and the solicitors' profession. One of the reasons intervention exists is that the SRA operates a Compensation Fund, designed to compensate clients where the solicitor has misappropriated capital entrusted to him or failed to account for those monies. Intervention has been described in the courts as being, in part, designed to protect the Compensation Fund. In this respect the profession differs from others such as

> Its purpose in intervening is to protect the interests of clients, the public and the solicitors' profession.

chartered accountants, although insolvency practitioners are of course required to have statutory fidelity bonding, which ensures funds are available to creditors in certain circumstances. The Compensation Fund is financed by an annual contribution, separate to the practising certificate fee, paid by each regulated solicitor in the UK.

The intervening agent does not deal with the employees of the solicitors' practice nor the trade creditors nor does it seek to obtain economic value for the client files it is handling.

A solicitor can apply to the High Court for an intervention to be withdrawn, but the application does not automatically stay the intervention. The costs of the intervention, which can comprise those of the intervention agent, the SRA intervention team and archiving costs relating to client files, become a debt payable by the solicitor to the SRA.

It will be apparent from the details given above that there have been fewer interventions taking place in recent years. The SRA only intervenes if it is judged necessary to do so to protect the interests of clients. One of the key drivers for intervention can be the issue of file archiving discussed below, particularly if there is no cash available to fund archiving. This is particularly the case in personal injury law firms, which have featured regularly among recent law firm insolvencies, but is also an issue with other firms.

How successful is intervention?

It will be apparent that intervention does not deal with the interests of key creditors such as secured creditors, employees, who rank as preferential creditors under UK insolvency law, nor trade creditors and other stakeholders. This is primarily

> “The SRA only intervenes if it is judged necessary to do so to protect the interests of clients.”

because it is not intended to do so by parliament and the powers given to the SRA do not include powers to deal with such assets and liabilities.

One of the biggest disadvantages of intervention is that it destroys all value for creditors of an insolvent law firm (including the SRA, which will be hoping to recover the costs of intervention from the law firm or the solicitors personally) by not obtaining economic value for that firm's debtors, work in progress and client list / goodwill. Indeed, it has the effect of largely reducing (or eliminating all prospect of) realisations, thereby increasing the probability that the costs of intervention will be paid from the Compensation Fund, rather than from realisations. It should, however, be noted that it is open to an intervened solicitor (or the IP) to raise bills and pursue outstanding costs following the intervention and the SRA will allow access to records and papers to facilitate this.

This is in contrast to the UK insolvency procedures mentioned below.

We have looked at realisations from a number of law firms that have suffered intervention and subsequently entered an insolvency process. In all cases, as you would expect, realisations have been negligible or apparently worse than could be achieved through a pre-pack administration.

Statutory trust

Another feature of intervention is that a statutory trust is created over the practice money (only the money, not other business assets) taken into the SRA's possession under the Solicitors Act 1974. These funds are held on consecutive trusts, the first for the use of the intervention powers, including the costs, and secondly for clients or anyone else with a beneficial claim. Arguably this first statutory trust ranks ahead of secured bank debt, if the business is an LLP or incorporated. While the matter has not been tested in the courts, this is hardly an encouragement to lenders to advance funds to law firms, at a time when specialist funders of work in progress and disbursements have largely left the market and when many law firms are in financial difficulties. It is, however, understandable that the SRA should seek to ensure that it recovers the substantial cost of intervention from the law firm concerned.

Another issue about which there is limited information is the extent to which clients are satisfied with the procedure. An SRA consultation paper has disclosed that only some 0.55 per cent of files it archives following intervention are ever accessed by clients (this is in contrast to live files, the majority of which are distributed).

Just as the UK appears habitually to 'goldplate' EU legislation when introducing it into the UK, there are a number of areas where solicitors impose upon themselves a higher regulatory and administrative burden than other professionals. One such example is the requirement for six years' run-off cover for Professional Indemnity Insurance (PII). Another is the practice of storing client files for seven years from the date of intervention, even if that file is long since closed. Intervention has the effect of prolonging the storage period in these circumstances. The SRA is quite rightly consulting currently on reducing this. It is also considering reducing compensation payable from the Compensation Fund.

In the case of *Atteys Limited*, which had a substantial personal injury practice and entered insolvent liquidation and was intervened after a failed pre-insolvency marketing campaign the directors' statement of affairs shows the SRA as a creditor (for intervention costs) for £1.1m. Most of this will be paid from the Compensation Fund, since the company's assets are insufficient. Intervention took place partly to deal with archiving of closed client files, but also to deal with many live files and in excess of £1m of client monies still held by the firm.

What are the alternatives?

Readers will be familiar with the formal insolvency procedures, which can be an alternative to intervention, such as administration, CVA, PVA, IVA or even creditors' voluntary liquidation and compulsory liquidation and bankruptcy.

These are discussed in more detail elsewhere in this issue, so are not considered here.

It is, however, worth noting that all these procedures will protect the interests of clients of a law firm and the SRA as regards client monies and client files.

The way forward

The SRA has made great progress over the last few years in becoming more sophisticated in dealing with troubled law firms, partly as a result of greater interaction with IPs, insolvency lawyers, turnaround professionals and others involved in the sector. As a result it is making greater use of existing insolvency procedures and professionals and restricting intervention to cases where the practice has been abandoned, dishonesty, where file archiving is an issue or other limited circumstances.

Readers may therefore wish to liaise with the SRA when dealing with troubled law firms, who may be prepared to take on the cost of dealing with closed files in return for some cash to fund such costs, which they argue they are entitled to under their statutory charge.

Another area the SRA should consider reforming is the successor practice rules which make it harder for other firms to buy law firms, reduce the prospects of realising value from a troubled or insolvent law firm, thereby reducing the amount that will be returned to creditors (and increasing the chance of a call on the Compensation Fund for intervention costs). A number of recent

> “While the matter has not been tested in the courts, this is hardly an encouragement to lenders.”

prospective sales of troubled law firms have failed due to these rules resulting in lower realisations for creditors, fewer jobs being saved and a greater call on the Compensation Fund.

Perhaps it should also consider the current method of funding the Compensation Fund and moving to statutory fidelity bonding such as the IP schemes. Could it then abandon intervention altogether? An opportunity for an entrepreneurial insurance broker perhaps, albeit a very large and challenging opportunity!

Many thanks to friends and colleagues, including those at the SRA, for commenting on and improving this brief article.

Note

[1] SRA closed consultations on meeting the costs of interventions from the Compensation Scheme.

FRED SATOW is a director at MHA MacIntyre Hudson.

When firms need intensive care

Christina Fitzgerald and **Steve Billot** revisit a subject causing concern in the legal profession.

Following our article in the winter edition of *RECOVERY* in 2011, which outlined the considerations when dealing with failing legal practices, as predicted we have seen many high-profile casualties in the UK legal sector, including Cobbetts, Dewey Le Beouf, Blakemores, Challinors, Atteys, Manches, HilliersHRW and Kaslers. However, there are many other firms in serious financial difficulty.

SRA financial survey

Last year the Solicitors Regulation Authority (SRA) engaged with over 2,000 law firms (which it assessed were 'high impact' firms, including the top 200), and asked for financial information. Many of these firms in need of intensive care have been assigned a relationship manager. This highlights the SRA's growing concern to maintain integrity and competence in the UK legal profession and ensures that firms can demonstrate financial stability.

SRA intervention

The SRA's intervention spend last year was £7m and the SRA is under pressure to avoid expensive interventions. The intervention cost in relation to Blakemores and Atteys was over £1m each. This added expenditure means that this year each solicitor will have to pay an extra £23 as part of their Solicitors' Compensation Fund contribution.

> "The intervention expenditure means that each solicitor will have to pay an extra £23 as part of their Solicitors' Compensation Fund contribution."

The SRA has stressed that it regards intervention as a last resort. It has engaged with many of the professionals in the sector, including lenders and insurers, and invited submissions on how to avoid intervention.

Therefore, when advising a distressed law firm, you need to ask if a relationship manager has been assigned, if the SRA has been notified of serious financial difficulties (which a firm is obliged to do under Outcome 10.3 of the SRA code of conduct) and also to see the financial information that the firm has given to the SRA.

Importance of early dialogue with the SRA

The SRA maintains that its primary role as

Regulator is to ensure that client monies and client files are protected. Early dialogue with the SRA is vital to ensure that a survival plan is agreed, or else, an organised wind-down is implemented.

The need for multiple advisors

Given the inevitably complex nature of a firm and the need to advise its members (or partners), the firm as an entity, the lenders and the SRA, it is difficult to see how one advisory firm can act independently. Therefore, it has become the norm in larger cases for multiple advisors to be engaged.

Focus on pre-packs

The SRA still maintains the requirement that if a law firm trades during administration, one of the joint appointment takers must be a Solicitor Licensed Insolvency Practitioner (SLIP). That SLIP will still be personally liable for any breach of undertaking in relation to that practice. This makes the taking of such an appointment very unattractive and a trading administration unrealistic. That is why we have seen so many pre-pack administrations. Submissions have recently been made again to the SRA for these requirements to be reviewed.

This has led to the appointment of solicitor managers, for example at Halliwells and Cobbetts. The SRA rules insist that only a solicitor can actively deal with client monies/files. Solicitor managers have been appointed on the bigger law firm failures to deal with these issues. However, there are no guidelines setting out the role of a solicitor manager and it is evolving on each occasion.

Who will be the successor practice?

The issue of who will be the successor practice for the purposes of professional indemnity insurance still remains live. This is particularly the case where a firm is being wound down with different parts of the business being divested into other practices. Many firms would be content in acquiring teams of solicitors from rival firms or for strategic gains, but will be reluctant to be determined as the successor practice as they would also adopt the professional indemnity liability of the practice.

Non-disclosure agreements (NDAs)

Make sure that any potential purchaser signs an NDA. Otherwise you could face a situation where the client names are stolen and misused. Also be careful about allowing any potential purchasers to see actual client files, particularly personal injury files. There are strict rules about confidentiality.

> "The SRA rules insist that only a solicitor can actively deal with client monies and files."

Valuing work in progress (WIP)

It can be very difficult to assess WIP. We work with professionals who are able to benchmark WIP for each sector of the legal market so that we can ensure full value for the stakeholders is obtained on any sale/merger.

Compliance with SIP 16

This has proven an issue on many cases. To what extent do you advertise the practice? Do you just approach local firms? How can you reach a wider audience of potential purchasers?

Help from specialists

The case remains that firms at risk need help from dedicated specialists before their condition becomes critical.

CHRISTINA FITZGERALD is a partner in the corporate recovery, insolvency and restructuring team at Matthew Arnold & Baldwin LLP.

STEVE BILLOT is a managing director at Duff & Phelps restructuring UK.

Payments, profits and problems

Steve Gale highlights the care needed when valuing work in progress.

It is very easy to come out with clichéd phrases such as 'cash is king' and 'turnover is vanity, profit is sanity'; the problem is that they carry a huge degree of truth.

Professional services firms are not complicated business models – their work doesn't involve the buying and selling of goods or stock, there is no manufacturing, no complicated machinery. At a basic level there are clients, people and premises. The clients pay for the service, the people are paid for their work, the landlord is paid the rent – what's left is the profit. As a certain meerkat might say, 'simples!'.

> "The temptation is to look at the book value of the unbilled work in progress."

But of course, it isn't that easy. For both firms of accountants and lawyers, the services performed for the client might not allow for payment for that work to match the outflows of the wages for the staff and drawings paid to partners (both paid monthly) or the rent (paid quarterly), so the practice needs an amount of working capital to fund the gap.

Assessment and valuation

Ultimately, the profit on an assignment will be certain when the job is complete and the cash received is compared to the cash spent on servicing the work. The problem, however, is that is not how firms are required to measure profit in their statutory financial statements and tax computations, where accounting standards need to be applied.

Accounting standards require work performed but not completed to be measured on the basis of the value of the 'right to consideration', crudely, its selling price – not how much has been billed or how much cash has been collected. For many of the different services performed by accountants and lawyers, the value of the assignment at any one point in time is measured by reference to the degree of completion method, ie estimating the total billable value of the assignment and applying an assessment of how much of the work has been completed. Where bills are raised for the work as it progresses then the valuation of contracts at the year-end for inclusion in the accounts becomes more straightforward but for certain assignment types, which include elements of insolvency work, this can provide something of a challenge.

When firms are preparing their year-end accounts, the temptation is to look at the book value of their unbilled work in progress (WIP) and then try to apply some form of 'recovery rate' to that WIP to end up with the selling price. What accounting standards actually require is a valuation of the contract assignment as a whole and the year-end balance is the difference between the value of the work performed up to the balance sheet date compared to amounts already billed. If the value earned exceeds the bills raised then there is accrued income, if the bills raised exceed the value earned there is deferred income. Critically, both of these impact fee income and profit for the year. One can have a situation where a firm has 'earned' money on a contract but not raised a bill. This amount will not only go to revenue but, critically, profit as well.

Slow progress, longer term

Insolvency work for both accountants and lawyers provides a particular challenge in that there may be considerable uncertainty over both the ultimate value of an assignment being undertaken as well as the time that it will take to complete. Making an estimate, therefore, of the value earned on such an assignment before it is complete can be difficult.

For insolvency work, the basis on which the practitioner may be remunerated will vary from case to case; some will be fixed fee, some time-based and some related to the value of the assets realised or distributed. It is also possible for a combination of all or any of the three to be applied to an assignment.

Insolvency assignments are generally over a longer term than many other types of assignments carried on by accounting or a law firms. This means that the estimates about the value of the work carried out are likely to have to be made at more than one year-end. There are some high-profile administrations and liquidations that have been going on for years.

Establishing greater certainty

Where circumstances change within an assignment this can lead to significantly different estimates being made that impact the value 'earned' on an assignment. These changes, ultimately, feed through to revenue and profit. It is not surprising, therefore, that insolvency practitioners are known for being 'cautious' when considering the revenue earned on

> "One can have a situation where a firm has 'earned' money on a contract but not raised a bill."

assignments. Recognising revenue and profit in one year only for that to reverse in a subsequent year leads to a risk that 'profits' are paid out when, ultimately, they are found not to have been earned. Generally, time will always help to establish greater certainty but when there is pressure for accounts to be finalised, it is a 'best estimate' at that stage which is required. Accounting standards do allow for uncertainty to be factored in when valuing revenue earned and for this reason it will normally be appropriate to exercise a greater degree of caution in the earlier stages of an assignment. Even where remuneration is based on the realisation of assets, not to recognise any revenue may be difficult to justify. Liquidators' fees have a priority and ultimately the assets will be realised even if the quantum and timing will be difficult to establish.

Coming back to that adage of 'turnover is vanity, profit is sanity' – perhaps we should exercise some caution…

STEVE GALE is a partner in professional practices at Crowe Clark Whitehill LLP.

The traditional approach is no longer enough

Tom Wood believes professional service firms should embrace change, or risk a challenging future.

Many firms need to improve their performance in order to achieve maximum profitability as we come out of what was arguably the first real 'white collar recession'. While well-run, forward-thinking firms can still be highly profitable enterprises, I believe some practices need to show increasing flexibility and customer focus in the way they operate.

> "It's important that firms can clearly set themselves apart from the competition."

This will mean major changes such as increased focus on marketing and brand, potentially moving out of high-cost London offices or using the internet and social media to bring in new business. Phone and tablet apps can be used to engage with younger or more tech savvy clients and can potentially begin new, long-term relationships.

Profit margins are under pressure from a number of directions. Among these are low interest rates and their effect on income from client balances, increasing competition, the compliance costs of meeting new legislation, client pressure for lower bills and an over-supply of lawyers. Firms therefore need to respond by taking a more flexible approach to what is no longer a safe and automatically profitable profession.

Stand apart from the crowd

As firms plan for growth, they should ask themselves a number of questions, including what is their niche or differentiator? Is it a particular area of the law, a geographical region or the way they deliver a product? It's important that firms can clearly set themselves apart from the competition. Likewise, understanding the competition is also key.

Another challenge is the balancing act of the need for firms to drive down their costs versus increasing client expectations. Many will have implemented the most obvious cost cutting measures, but if it hasn't been done, outsourcing some of the functions that firms currently carry out in-house could make a big difference.

Winning new business is obviously always a focus and firms also need to think about where and how they are going to find new clients and new revenue streams, beyond their usual tried and tested methods.

Look after your own

A firm is only as good as its people – so the business needs to do everything in its power to attract, develop and retain talent in the organisation and make sure that succession planning means the next senior position goes to the best candidate, rather than the next candidate in line. Another aspect to consider is whether the age profile of the firm is sustainable.

> "Every member of the team should contribute, not just to fee income but also to the wider business."

A 'performance scorecard' approach should also be used that ensures every member of the team contributes not just to fee income but also to the wider business, from enhancing the brand to chasing debtors due.

A flexible approach to staff will also pay dividends. The firm could, for instance, make use of talented and qualified parents who look after their children by day but are keen to pursue their legal career from home in the evenings.

Where work is allocated should also be looked at closely – how much work truly needs partner involvement? Could talented junior staff to do some of the work that partners are currently doing – and are they paid enough to make sure they stay?

An outside view

Would external advice be beneficial, perhaps by appointing a non-executive director or even by inviting the firm's banking relationship director to sit in on a board meeting and put forward ideas? Having a diverse management board can bring significant benefits and can lead to a more corporate, profit-based approach to leadership.

Keep a tight rein on finances

From a financial perspective, firms need to focus on reducing 'lock up' – the time between starting the clock and banking the cheque. Is this enough of a priority for every member of the team, including senior partners? Incentives could be introduced for those who improve cash flow in such a significant way.

Is the ratio of partner capital to external borrowing sustainable or is the firm in danger of finding themselves under-capitalised? How often is this reviewed?

Another key dynamic for professional services firms is understanding the end-to-end profitability of a piece of work. Clients increasingly want to see a fixed fee quote, something for which visibility of the cost to deliver is essential. A firm that can deliver legal work efficiently and in a cost-effective manner will ultimately grow market share.

> "A firm that can deliver legal work efficiently and in a cost-effective manner will ultimately grow market share."

If growth is the goal, how will it be achieved – organically or by seeking to merge with another practice? A merger should only be considered if there is a clear synergy between the merging firms and a clear competitive advantage, either created or enhanced, as a result of the fusion.

The client is king

It goes without saying that client relationships need to be at the heart of everything the firm does – how are they communicated with? For instance, are they being offered enough flexibility in the way they are expected to pay fees? Or is there a more customer-focused way in which that part of the relationship could be structured?

What is the firm's evolving and diverse client base looking for? Do they want quick and easy online access to services or are they driven by price or by easily accessible walk-in offices? Should the focus be on one category or mass appeal across the board? And above all – is the firm focusing on meeting clients' needs in a flexible and creative way?

The legal sector is going through unprecedented change, and this creates both opportunities and challenges for firms. Leaders must step back and re-assess their business, understanding the impact of sector progression and appreciate the future looks different. It is not an easy time to be at the helm, but innovation and a very close watch on cash, as well as profitability, will help firms succeed. ◻

TOM WOOD is head of professional services, Barclays.

Director's Loan Account

Breach of Contract

Government Compensation

Asset Recoveries

Breach of Directors' Duties

Difficult Debts

Fraudulent Trading

Misfeasance

Professional Negligence

Supplier Disputes

Transactions Defrauding Creditors

Transactions at Undervalue

Wrongful Preference

Illegal Dividends

Wrongful Trading

From £20k to £50m – talk to the Insolvency Litigation Financing Experts

MANOLETE PARTNERS PLC
ACQUIRING AND FUNDING INSOLVENCY LITIGATION

Contact: Steven Cooklin ACA ACSI CF – Chief Executive
steven@manolete-partners.com or telephone 01494 618520
www.manolete-partners.com

Navigating the PI marketplace

Why professional indemnity insurance should be more a relief than an obligation.

Professional indemnity (PI) insurance, also called errors & omissions insurance in North America, covers any negligent acts, errors or omissions in the service provided by you to your clients. In addition to this PI also satisfies the legal 'duty of care' that you owe your clients as a provider of your services.

Many industries that offer a professional service or advice will purchase PI cover to protect them from allegations or claims of negligence; however, the provision of this insurance can come in many forms.

More than a tick box exercise

Like many professional service industries, insolvency practitioners (IPs) are strongly recommended to have a robust insurance platform, however, not all policies are created equal.

> "The unfortunate reality for many IPs is that they, by the nature of their work, are often a high priority target for claims."

Law firms

In all parts of the UK it is compulsory for law firms, whether they are sole practitioners or top 100 firms, to have valid professional indemnity insurance with a participating insurer. The cover provided under the minimum terms and conditions are very generous to law firms, and these are some key features of the cover provided:

- The policy indemnifies innocent third parties against fraud.
- The policy wording provides automatic six years run-off period in the event of the failure or shutting down of a firm.
- The policy wording provides automatic worldwide cover in the event of a claim.

It is regarded as having the widest scope of cover of all the traditional professions, due to the overarching concern of protecting the general public.

Surveyors

It is compulsory for all Royal Institute of Chartered Surveyors (RICS) accredited surveyors to have valid insurance with RICS listed insurers. As with lawyers there are some unique features of provision of insurance. These include:

- As of 1 January 2014, any RICS listed insurer must have a minimum security rating, as graded by Standard & Poor and/or AM Best.
- The insuring clauses in the policy wordings are based upon civil liability rather than legal liability. This is generally viewed as providing a wider scope of cover for the profession.

Accountancy practices

The main regulator of accountancy firms, the Institute of Chartered Accountants of England and Wales (ICAEW), requires all practitioners and their member firms to purchase PI with an accredited insurer. Some of the benefits of this cover include the following:

- In the event that a practice cannot purchase PI through regular means, then there is an arrangement via the assigned risks pool, that firms can, for a limited period, satisfy their regulatory requirement for insurance.
- It is a requirement of the ICAEW that all policies provide retroactive cover for liabilities arising from work carried out in the previous six years, except for claims or potential claims known about at the time the insurance was first taken out.
- It is a requirement of the ICAEW that every firm returns a certification of compliance with the minimum terms and conditions to the ICAEW.

PI and other industries

The purchase of PI insurance is now commonplace in almost all professional service or advice industries in the UK. The list of industry professionals that purchase PI are varied and include the following:

- Patent agencies
- Testing and laboratory firms
- Actuaries
- Engineers
- Contractors
- Insurance brokers
- Independent financial advisors including mortgage brokers.

The list is far more extensive than this but in effect includes any profession where either a service or advice is being provided to a third party.

If it goes wrong, from the IP perspective

PI insurance protects your personal exposure from professional negligence, meaning that without comprehensive and reliable PI cover you may be required to pay claims through your personal assets. In the real world, failing to have a comprehensive PI policy in place can lead to a huge shortfall in cover following a claim. Defendants in this position often not only have to face the reality of having either to personally fund (partially or otherwise) any claims of negligence, but also have to face the potentially huge ramifications of the loss of reputation which can have far reaching effects even after the original claim has been resolved.

The unfortunate reality for many IPs is that they, by the nature of their work, are often a high priority target for claims. Emotionally charged owners/directors and severe financial strain on insolvent firms often cultivates an environment where claims (justly or unjustly) will appear. For many IPs the idea of facing a claim against them is more a matter of 'when' than 'if'. When a claim is lodged, having the knowledge that your PI cover is broad, your insurer is financially reliable and your broker is a specialist, can be a huge emotional relief, as well as a financial one.

Using a specialist

While navigating the PI marketplace can be a daunting task for any practitioner, utilising the skills and experience of a specialist broker will both reduce short term costs and improve the quality of your coverage. A specialist broker will have a dedicated team who handle all enquiries on a regular basis, keeping a close relationship with insurers to ensure the very best coverage, as well as market leverage to ensure competitive prices.

It's important to remember that while you, as an IP, will only deal with insurers once a year during renewal, a specialist broker will live and breathe your product. A good broker can (and will) inform you of market changes, premium fluctuations, policy trends and other influencing factors that affect your coverage.

LUKE HARRIS is a divisional director, Willis FINEX Global.

PAUL AFTENI is a divisional director, Willis FINEX Global.

Work in progress: a different, more friendly, beast

David Johnstone explains how to retain value when a claimant personal injury law firm seeks assistance from the restructuring and insolvency profession.

The last quarter of 2013 saw 136 firms close for a variety of reasons, many of them to do with the Professional Indemnity Insurance (PII) debacle. However, numerous others closed prior to the PII renewal date of 1 October. In all likelihood, 2014 will see that number rise significantly as the legislative changes that came into force in April last year start to bite.

Seeking advice

Change is difficult for most in any walk of life and while shock at the level of change in the legal sector is gradually translating to acceptance, a high proportion of legal practices remain in denial, failing to seek external advice early enough for there to be many options left for the business. Whether that trend changes remains to be seen. This year has already witnessed further activity in respect of formal processes and the number of strategic decisions to exit the personal injury (PI) market has risen.

The level of change and the very narrow and niche nature of claimant PI firms may influence earlier engagement.

> "A high proportion of legal practices remain in denial, failing to seek external advice early enough."

The legal press regularly carries features advocating early engagement and it is also promoted by the Solicitors Regulatory Authority (SRA).

Regardless of the timing of the approach for assistance, it is imperative that insolvency practitioners (IPs) have a clear understanding of the principle asset held by claimant PI law firms and PI departments within multidisciplinary firms' work in progress (WIP), if a sale or restructure at an undervalue is to be avoided.

Unlike WIP in a manufacturing scenario, WIP in a claimant personal injury file is a highly sought after commodity by firms that have invested in IT, processes and business structures they believe will allow them to remain profitable, despite the dramatic reduction in revenues achievable from new matters opened today. Albeit diminishing over time, the fact that a proportion of books of business transferred

will have pre-31 March matters within them, attracting remuneration under the old regime allows practices continuing in claimant PI to bolster the percentage of work performed at the old levels of remuneration.

When reviewing a balance sheet on a break-up basis, WIP is immediately discounted heavily, unless it involves raw material or finished goods. The general assumption is that if work is part way through a process, that process will be substantially unique to the business concerned and a market for something half-baked will be very restricted indeed. Claimant PI files, however, offer the opportunity to add value taking the matter to a conclusion. The processes and progression of such legal matters are fairly standard across the sector therefore, other than an investment in time getting up to speed as to where in the process the file is, the matter can slot into the firm's own case management systems. Value can be added by taking it to conclusion and the defendant then billed for all work, both pre- and post-transfer, performed on the case.

The contingent nature of the work – only having any value if concluded successfully, the mix of matter types, the assignability of Conditional Fee Agreements, client care around the transfer process, attrition rates and the different settlement profiles by matter type – does complicate the issues.

Risk equals discount

Other factors also come into play – successor practice issues, Transfer of Undertakings, Protection of Employment (TUPE) if the whole book is transferring to one firm, the quality of the work performed on the files, the lack of time to identify a purchaser, the covert nature of the tendering process. These factors, while justified, all play into the hands of the existing buying community. If the risks are not fully understood by the selling party, heavier than necessary discounts will be negotiated by the very experienced buying community.

Rather than fully discounting, there is a growing trend for work transferring on an earn-out basis. While this can improve the percentage of the WIP value that flows back in to the process, care must be taken to ensure visibility of case progression. In addition, agreements require tight drafting to ensure equitable apportionment of fees recovered. To be managed successfully there has to be investment in monitoring skills, as well as the demonstration to the buying party of a deep understanding of

> "There has to be investment in monitoring skills, as well as the demonstration to the buying party of a deep understanding of the processes."

the processes, if time delays and under-settlement on individual matters is to be avoided. As such cost/benefit analysis is required and sub-contracting to specialist providers needs to be considered in respect of the niche element of the work.

By understanding the risks, mitigating them and achieving full value for the WIP that will ultimately be liquidated, IPs can significantly improve the returns achieved for creditors where a formal process is required. ◘

DAVID JOHNSTONE is the managing director at Recovery First.

Recovering costs pre-, during and post-appointment

Tips on how to avoid the major pitfalls of an insolvency procedure when you're supposed to be doing the rescuing.

Costs are the price that creditors pay for an insolvency practitioner's (IP's) expertise and time in dealing with a trading bankrupt or insolvent business. However, where the assets are insufficient to meet the existing debts, the imposition of a practitioner's fees and expenses being paid out in priority can send some 'over the edge' and all practitioners have the scars to prove it. This article explores the developing general principles and major pitfalls and how to avoid them.

For the purposes of this article, we will focus on remuneration in the context of a liquidation. However, the principles are broadly similar for other trading insolvencies.

1. Fees and disbursements incurred prior to a formal insolvency procedure (FIP)

IPs are often instructed prior to an FIP, whether to provide advice to directors or assess whether a company is trading while insolvent. It may seem like an obvious point, but it is vital that before starting work an IP should seek an indemnity or some means of payment as an alternative to being paid by the company in question.

> Practitioners should beware the fast moving pace of FIPs.

If the work undertaken subsequently results in an application for an FIP then (subject to the indemnity) the IP is likely to want to apply for their costs for that work to be treated as an expense of the FIP. For work which is not referable to this FIP, or if the application for an FIP is refused then payment of fees is simply a matter between the company and the IP. Any fees outstanding will simply rank as an unsecured claim in the FIP.

Practitioners should beware the fast moving pace of FIPs or the difficulties of changing between two different FIPs (ie moving from an administration into a liquidation). The case of *Neumans LLP* v. *Androndikou and others* [2013] EWCA Civ 916 provides a stark warning of the danger of being caught out without an indemnity. In this case, a firm of solicitors were unsuccessful in striking out a winding-up petition against Portsmouth City Football Club Ltd (PCFC). While the appeal was

pending, PCFC's new owner appointed administrators out of court. After the administrator's costs had devoured all of PCFC's assets, PCFC was wound up on the original petition, leaving the firm of solicitors ranked as an unsecured creditor and facing the prospect of recovering none of its fees and disbursements of around £267,000.

Unsurprisingly, the solicitor's position attracted scant sympathy. There is of course nothing more ingenious or focused than solicitors seeking to recover their costs. They sought to claim that their fees should be treated as an expense in a subsequent out-of-court administration. The court rejected this and (with the benefit of hindsight) suggested that the solicitors should have sought third party funding or indemnities from the company directors.

Practice point:

Think about costs from the beginning and get an indemnity or third party funding.

2. Fees and disbursements incurred following an FIP

2.1 General principles: The Insolvency Rules 1986 (IR 86)

Unfortunately, IPs cannot fix their own remuneration and have no right to retain remuneration out of the assets if they are insufficient to pay other expenses of the FIP.

IR 86 provides for the remuneration of IPs (office-holders) and further important guidance is provided to the Court by *Practice Direction: Insolvency Proceedings* [2012] B.C.C. 265 (the Practice Direction).

Historically, remuneration had often been determined as a percentage of realisations and distributions. This changed with IR 86, which provided for an office-holder's remuneration to be determined:

- by reference to the time properly given by the insolvency professional; or
- as a percentage of realisations and distributions; or
- to be fixed.[1]

The decision as to which basis of remuneration to apply is made by the creditors' committee (the committee) or by a resolution of the meeting of the creditors. In making their decision, the committee shall have regard to the following matters:

- the complexity (or otherwise) of the case;
- any respects in which, in connection with the winding up, there falls on the IP any responsibility of an exceptional kind or degree;
- the effectiveness with which the IP appears to be carrying out, or has carried out, his duties as liquidator; and
- the value and nature of the assets with which the liquidator has to deal.[2]

> In the event of no determination, the office-holder will be entitled to remuneration on the 'official receiver's scale' both for realisations and distributions.

In the event of no determination, the office-holder will be entitled to remuneration on the 'official receiver's scale' both for realisations and distributions.

In the event that the office-holder considers that the basis of the remuneration fixed by the committee or by resolution of the creditors is insufficient or inappropriate, the office-holder may apply to court for an order changing it.[3] Recent case law, such as the *Neuman* case, suggests that the courts are adhering to the letter of IR 86 and the Practice Direction (see below). Therefore, an office-holder will maximise their chances of increasing their remuneration if they think about costs and apply the principles in the Practice Direction from the outset and have evidence to justify this, over and above basic time entries.

Editor recovery@r3.org.uk | Recruitment recovery@r3.org.uk/recruitment

Practice point:

Consider whether your existing time recording systems comply with IR 86 and the general principles set out in the Practice Direction to ensure that you can have easily accessible evidence to justify your remuneration.

2.2 General principles: The Practice Direction

The Practice Direction has been designed as a one stop shop for the principles, procedure and practice relevant to the fixing of an office-holder's remuneration by the court, including the information required.

> "The court should give weight to the fact that office-holders are members of a regulated profession."

The Practice Direction states that its objective is *'to ensure that the remuneration of an appointee [office-holder] is fair, reasonable and commensurate with the nature and extent of the work properly undertaken by the appointee in any given case and is fixed and approved by a process which is consistent and predictable'* (paragraph 20.2.1).

Under IR 86 a creditor may apply to the court for an order that an office-holder's remuneration be reduced on the basis that, in all the circumstances, the remuneration is too high.[4] Ordinarily all such applications will be heard at first instance by a registrar sitting alone. However, where it is sufficiently complex the court may direct that the application be heard by a registrar or district judge sitting with an assessor or a costs judge. In addition the court may direct that a report in respect of the remuneration be prepared by an assessor or a costs judge as an aid for the registrar.

As well as setting out the procedure for a remuneration application, the Practice Direction also sets out the court's guiding principles when fixing and approving remuneration:

- justification – the office-holder must justify his claim and be prepared to provide full particulars of the basis for and the nature of his claim for remuneration;
- the benefit of the doubt – if there is any doubt as to the appropriateness, fairness or reasonableness of the amount sought, such doubt should be resolved by the court against the office-holder;
- professional integrity – the court should give weight to the fact that office-holders are members of a regulated profession;
- the value of the service rendered – remuneration should reflect the value of service rendered, not merely reimburse time expended and cost incurred;
- fair and reasonable – remuneration should be fair and reasonable and represent fair and reasonable remuneration for the work properly undertaken;
- proportionality (both of information and remuneration) – this relates to the information to be provided by the office-holder in relation to his remuneration and to the remuneration itself. It takes into account the nature, complexity and extent of the work and the value and nature of the assets and liabilities involved. Consideration will also be given to the nature and degree of responsibility of the office-holder, and the nature and extent of risk to and the efficiency of the office-holder;
- professional guidance – regard can be taken of relevant and current statements of practice by relevant regulatory and professional bodies in relation to remuneration; and
- timing of application – remuneration should reflect whether any application should have been made earlier and the reasons for any delay in doing so.

The actual costs of and occasioned by an application for the fixing and/or approval of the remuneration of an office-holder are paid out of the assets of the estate unless ordered otherwise by the court.

Practice point:

Think about how you can justify costs to the creditors and court by reference to the general principles and record this in a contemporaneous note (ideally accessible to the creditors).

2.3 Disbursements

Solicitors and experts' fees should be treated as disbursements and not as part of an office-holder's remuneration. As such costs met by and reimbursed to the office-holder should be properly chargeable, ie appropriate and reasonable.

Where there is litigation, solicitors and experts' fees may be recovered (in part, at least) from the other side. However, where this is not the case and they are properly chargeable or incurred by the office-holder, disbursements are counted as an expense of the liquidation. As such, disbursements are paid out of the assets in the order of priority set out in r.4.218 IR 86, resulting in the payment of expenses prior to the payment of an office-holder's fees.

If prior sanction for actions such as litigation over antecedent transactions is not obtained from the committee/creditors, then those disbursements will not be treated as properly chargeable and therefore are not payable as an expense of the FIP. An office-holder may be left footing the bill personally.

Practice point:

Think carefully about whether disbursements are necessary and obtain prior sanction where appropriate.

Before accepting an appointment, an office-holder should consider carefully whether the company's assets will be sufficient to discharge the expenses of the FIP, including his remuneration, to avoid being out of pocket.

Conclusion

Given the dire consequences of failing to recover costs, IPs should consider costs and their recovery at the outset and keep them in mind throughout. IPs should consider whether third party funding might be available, or seek to negotiate indemnities

> "A clear approach to costs and transparent records, together with clear and quick legal advice, will go a long way."

from the directors of any potentially insolvent company. While these practice points may not be rocket science, these simple steps should save a lot of problems when it comes to remuneration from a limited pot.

The situations are myriad and the tactics sometimes Machiavellian, but a clear approach to costs and transparent records (together with clear and quick legal advice) will go a long way to prevent an IP from working without remuneration and at their own expense. ◻

References

1 IR 1986 r4.127(2)

2 IR 1986 r4.127(4)

3 IR 1986 R4.130

4 IR 1986 r4.131

ALEX FOX is a partner at Penningtons Manches LLP.

JAMES HARRISON is an associate at Penningtons Manches LLP.

LUKE CLEMENTS is a trainee at Penningtons Manches LLP.

Limited Liability Partnerships: individual profit without individual responsibility?

Alison Goldthorp and **Mark Jones** explore whether the LLP is as 'safe' for members as is assumed.

In his satirical lexicon *The Devil's Dictionary* (1906), the American author Ambrose Bierce defined a corporation as 'an ingenious device for obtaining individual profit without individual responsibility.'

The Limited Liability Partnerships Act 2000 (2000 Act) created a new form of business vehicle, the Limited Liability Partnership (LLP), with the intention of shielding individual members from personal liability for the acts of other members. In the years since 2000 the LLP has become the structure of choice for many professional service firms, widely perceived to be a 'safer' business vehicle.

> In partnerships every partner remains personally liable to contribute to the debts of the partnership if it fails.

Background

The 2000 Act was introduced after lobbying by the large accountancy firms, keen to reduce their exposure to negligence claims against partners. The resulting LLP is a body corporate, with its members' liability limited to the funds they agree, in the LLP agreement, to contribute. In contrast, in partnerships every partner remains personally liable to contribute to the debts of the partnership if it fails, and can be sued personally for breaches of contract by any party contracting with the partnership. Thus, at first sight, the position of individual members of an LLP is improved compared to that of partners in partnerships: the LLP, and not its individual members, is responsible for duties and liabilities.

As LLPs have become increasingly popular over the last ten years, so the transactions that they work on have become larger and more valuable, and the potential for negligence claims has increased. Since the onset of the current economic crisis in 2008 there have been a number of insolvencies and failures in the professional services sector. These have highlighted the differences between an LLP and a limited company and the ways in which members could have more exposure to personal liability than they might think.

Capital

The most obvious liability of individual members is for their capital contribution, often provided by taking out a professional practice loan (PPL) from a bank. Capital is sometimes mistakenly regarded by members as 'risk free', with repayment guaranteed by the LLP, and the LLP typically agreeing to repay the bank direct when the member retires from the LLP. But a PPL is a loan taken out by an individual member. Any guarantee is limited by the worth of the guarantor: the indemnity from the LLP is therefore worthless when the member most needs it, and the individual will still be required to repay the money borrowed to be introduced as capital.

> LLP members could have more exposure to personal liability than they might think.

The treatment of capital is particularly topical in light of HMRC's proposed changes to the taxation of LLPs, which are likely to require fixed share members to inject significantly more capital into the LLP if they are to continue to be treated as self-employed partners, and not employees, for tax purposes.

Tax

An LLP is tax transparent and the individual members are therefore personally liable to pay the tax on their share of the profits of the business. Often the LLP will hold in reserve the funds representing the tax payable by the member and pay HMRC direct when the tax falls due. In practice, those funds are used as working capital by the LLP and rarely, if ever, physically put to one side pending payment to HMRC. So what happens if there is an insolvency? The individual member remains liable to HMRC to pay their personal tax liability whether or not funds are available in the LLP to discharge that liability. Some individuals have therefore had a nasty shock when their LLP has gone into administration: HMRC has demanded the tax payable on previous profits, and there were no funds set aside for the member to use to pay that liability. Unless those funds were held on trust for that member, on terms that the administrator or liquidator accepted, the member's claim for repayment would fail. In our experience LLPs rely on the ability to use those funds during the year. If the funds were held on trust for the individual members, those LLPs would be under increased financial pressure and, in practice, it is not an option for the member to insist on a trust account if the LLP is to survive.

> "The treatment of capital is particularly topical in light of HMRC's proposed changes to the taxation of LLPs."

If an LLP does fail, however, the news for the individual member may not be all bad, as members have the right to claim for terminal loss relief. Depending upon the quantum of the losses of the LLP, that may enable members to recover, from HMRC, tax paid on profits made in earlier years prior to the insolvency.

Drawings

An LLP agreement will usually provide a mechanism for the division of the profits between the members of the LLP. Typically members are permitted to take monthly drawings ***on account of*** profits throughout the year, the final profit figures are determined at the year end, and then any profit to which a member is entitled in addition to the amount he or she has taken in monthly drawings is paid to the member over an agreed period. If the member has overdrawn, the agreement will typically set out how those overdrawings are to be repaid. In recent years, in a challenging market, with fees reducing and budget profit projections not achieved, overdrawing has become more common. Drawings taken on account of profit are precisely that: ***on account of*** a profit share which will not actually be finalised until the profits of the LLP are known at the financial year end. In the event of an insolvency, it may be the case that the LLP ceases trading and no profits are made in the final trading period. The administrator or liquidator will then ask the individual members to repay the drawings taken during the year on account of profits that were never made.

Claims by a liquidator of an LLP

Directors of limited companies are usually concerned to avoid wrongful trading under Section 214 of the Insolvency Act 1986 (1986 Act), which they often think is the only way that they can be made personally liable. Section 214 allows the liquidator to seek an order that the director contribute to the assets of the limited company. Section 214 applies to all members of an LLP as if they were all directors, and not just those members who sit on what is commonly described as 'the board' of the

LLP. The test for liability is an objective and a subjective one, so those involved in management will usually have more knowledge than an ordinary member of the LLP, but there is potential liability for all members of the LLP. Members of an LLP also have potential liability under Section 214A of the 1986 Act, which only applies to LLPs, and allows the liquidator to seek to claw back from members payments made to that member at a time when that member knew or ought to have known that there was no reasonable prospect of avoiding insolvent liquidation. The liquidator can look to claw back any payments made to the member during the two years prior to the commencement of the winding up, which could include drawings, or repayments of capital, or any other payments made to that member. The liquidator can also use the anti-avoidance provisions of the 1986 Act to seek to set aside payments to LLP members as transactions at an undervalue or preferences, using Sections 238 and 239 of the 1986 Act.

Directors' disqualification

The Company Directors Disqualification Act 1986 also applies to LLPs, and liquidators of LLPs are required to report on the conduct of the members of the LLP in the same way that they report on the conduct of directors. Again, as with Section 214, this applies to all members of the LLP, not just those who are on the 'board' of the LLP.

Conclusions

With profit comes responsibility. Members of an LLP have responsibility, and potential personal liability, for more than the capital they pay into the LLP, which is itself not 'risk free' if they borrowed that

> "Liquidators of LLPs are required to report on the conduct of the members of the LLP in the same way that they report on the conduct of directors."

capital. The perception of 'safety' can also lead to complacency and all members of an LLP should ensure that they maintain an active interest in the financial state of the LLP. In the unfortunate event of an insolvency they will then be better placed to defend any potential claims from a liquidator of the LLP for clawbacks or repayments. Even more importantly, however, given that many would say that there are cultural benefits to the partnership model and the 'glue' that joint and several liability creates, those benefits can better be reproduced in an LLP environment if the members behave cohesively and, together, take an appropriate interest in their business. More awareness of their potential personal risks could therefore help to improve the cultural cohesion of the business, reduce the number of failures in the future and achieve more successful restructuring when some form of failure does occur. □

ALISON GOLDTHORP is a partner at Addleshaw Goddard LLP.

MARK JONES is a partner at Addleshaw Goddard LLP.

irs
the insolvency risk specialists

Cows moo in regional accents...

Did you also know

We are experts in the complex language of insolvency insurance so no matter what the case or where you are based, we speak the lingo so you don't have to.

You are never too far from our regional teams of experts with extensive knowledge of the area and market in which you operate.

For more interesting facts visit
www.insolvencyrs.co.uk/facts

Experience the Difference

Insolvency Risk Services is a trading name of AUA Insolvency Risk Services Limited registered in England No. 6273355. Registered Office: St Helen's, 1 Undershaft, London, EC3A 8ND. Authorised and regulated by the Financial Services Authority. AUA Insolvency Risk Services is a wholly owned subsidiary of Amlin plc.

Recruit ■ Train ■ Retain **Careers and professional development**

RECOVERY SUPPLEMENT

R3, the Association of Business Recovery Professionals

Spring 2014 www.r3.org.uk/recovery

Career progress

Two of the 2012 JIEB award winners offer tips for study and talk about their career progression in the last 12 months.

Andrew Waudby

Since attaining his JIEB qualification last year Andrew has been made a partner at his firm, Clough Corporate Solutions. He won the R3 Smaller Practices Group (SPG) prize and the BPP prize, awarded to the candidate with the highest mark in the personal paper.

How important was the JIEB in your career progression?
Attaining the JIEB qualification was a huge step in my career as it allowed me to become a licensed insolvency practitioner. Furthermore, studying for the examination allowed me to gain a much broader and deeper technical knowledge of all aspects of insolvency, which has enhanced my ability to provide the best and most appropriate advice to all stakeholders and fully appreciate the circumstances surrounding each case.

The JIEB exams are notoriously tough – how did you juggle study commitments with maintaining work/life balance?
Obviously there has to be some give and take. I made sure that I still allowed myself some social time, but I had to adopt a more regimented approach to my time management. Work commitments can sometimes interrupt study, but you need to learn that one missed study session isn't the end of the world.

You need to be realistic about what you can do without tiring yourself out and need to allow yourself some well earned relaxation time. Earlier starts mean that you don't need to burn the midnight oil and can enjoy an evening with your feet up.

What advice would you give future students?
Start your study early. Having my revision notes completed by early August allowed me to move on to practising past exam questions and get to grips with what the examiners are looking for. Continuing to bulk up your notes as you do this allows you to incorporate key words and phrases in to your notes, which often come up over and over again in the past answers.

Gaining exposure to a broad range of case work prior to and during my studies gave context to the learning materials.

By working to a structured day plan in the last month of my study I could work for eight quality hours and always felt that I had a productive day. I was lucky enough that my employer allowed me plenty of time off before my exams to implement this plan.

What have been your year's highlights since learning of your success?
I became a licensed insolvency practitioner in 2013, which was the whole point of taking the exams! More recently I have been promoted to partner within my firm.

On a personal note I got engaged in May 2013 and am now planning for our wedding later this year. After a hard year of studying resulting in not seeing as much of each other as we would have liked, getting down on one knee was the least I could do.

What do you most enjoy about your job?
I enjoy the new challenges that each day brings. I feel that I am constantly learning and strive to constantly improve. The variety of insolvency work that I am exposed to within my firm allows me to test the scope of knowledge that I picked up while taking the JIEB qualification.

Have you taken up any new hobbies, now you're no longer studying?
During my exams I thought that it was important that I continued with my hobbies of football, squash and the gym, although I did have to compromise now and again. After my exams I allowed myself a bit of downtime and a few well deserved holidays.

Lorna Mode

Since winning both the ICAEW prize (awarded to the ICAEW member with the highest mark) and the PwC prize for second place overall, Lorna, who is assistant director of restructuring services at Deloitte LLP, has enjoyed refocusing on work commitments and home life.

How important was the JIEB in your career progression?
A lot of my day-to-day role involves technical compliance, so without the JIEB I would struggle to progress further. Ultimately I would like to take appointments and therefore it is a necessity. However, regardless of career progression I also wanted to pass the JIEB to achieve my own personal goals and it has given me greater confidence in my abilities.

The JIEB exams are notoriously tough – how did you juggle study commitments with maintaining work/life balance?
It becomes more of a work/study balance, and in my case I also have two young children so I needed to factor in some time for parenting as well! I had to be incredibly organised and disciplined with my study time. I had a study planner from the start of the year so I studied regularly rather than cramming at the end. This also enabled me to have every Saturday free to spend time with my family, and I relied heavily on my husband for support with the children. Deloitte also offers a very supportive study package so I was able to take the two months prior to the exams as leave.

What advice would you give future students?
Be realistic about how you personally study and tailor your study plan accordingly; have a study buddy; listen to your tutors; know the 'Book'; don't leave it to the last minute.

What have been your year's highlights since learning of your success?
Receiving my JIEB qualification and sailing to America on the QM2.

What do you most enjoy about your job?
I really enjoy the technical challenge of insolvency and the variety of work and cases. I'm currently working on Blockbuster and we also have Comet and HMV in my team, so there are lots of interesting issues to resolve. I also work with a great team of people.

Have you taken up any new hobbies, now you're no longer studying?
All the time I spent studying has now been refocused back on to my family, plus a few more sessions at the gym.

Joint Insolvency Examination – November 2013

Congratulations to all the successful candidates.

JIEB 2013 prize winners

Insolvency Practitioners Association Prize for First Place
Tim Armstrong

PricewaterhouseCoopers Prize for Second Place
Sarah England

Leonard Curtis Prize for Third Place
Lee Green

Association of Chartered Certified Accountants' Prize (awarded to the ACCA member with the highest mark)
Peter Anderson

ICAEW Prize (awarded to the ICAEW member with the highest mark)
Tim Armstrong

Insolvency Lawyers' Association Prize (awarded to the lawyer with the highest mark)
Laura Baker

Institute of Chartered Accountants of Scotland Prize (awarded to the candidate in the Scottish papers with the highest and sufficiently meritorious marks)
Adele Macleod

BPP Prize (awarded to the candidate with the highest mark in the Personal paper)
Sarah England

R3 Smaller Practices Group Prize (awarded to the candidate with the highest mark from a smaller practice)
Lee Green

A
Andersen (8272) Walton-On-Thames
Anderson P (8180) Macclesfield
Armstrong T (8261) Norwich

B
Baker L (8183) Altrincham
Baker N (8175) Oldham
Ball E (8143) Leicester
Baluchi S (8135) Shoreham-By-Sea
Bateson T (8265) Nottingham
Battrick D (8091) Epsom
Bingham L (8013) Motherwell
Bower E (8205) Sheffield
Brookbanks J (8051) London
Bucknall S (8102) Hove
Bulloss J (8216) Leeds
Burns J (8045) London

C
Camp J (8079) London
Carter M (8140) Cheltenham
Chan S (8238) High Wycombe
Childs A (8048) Oxted
Cooper P (8138) London
Culbert N (8030) Dromore
Curran R (8206) Pudsey

D
Dhalla S (8056) Ruislip
Diss C (8067) Chelmsford
Donacien F (8134) London
Donaldson J (8022) Belfast
Dowson C (8255) Sheffield
Dumville D (8071) Loughton
Dyer B (8263) Cambridge

E
England S (8050) Harpenden

F
Fletcher M (8073) Borehamwood
Fox T (8015) Clydebank

G
Gardner S (8234) Leeds
Glen J (8006) Glasgow
Goschalk J (8271) London
Green L (8262) Norwich
Gurung Y (8090) London

H
Hammond J (8229) Sheffield
Hargreaves G (8190) Altrincham
Harris N (8259) Exeter
Harris A (8087) St. Albans
Haughton K (8197) Bolton
Herridge K (8228) Leeds
Higham P (8176) Chorley
Holmes C (8040) London
Horner C (8252) Saltburn-By-The-Sea
Howells R (8168) Knutsford

J
James D (8231) Bristol
Jenkins M (8225) York

K
Keddie P (8039) London
Kelly J (8089) Gravesend
Kelsall D (8217) Leeds
Khaki A (8065) Northwood
Knight J (8068) Beckenham
Koumettou Y (8104) London

L
Lau S (8152) Birmingham
Lawson A (8109) George Town
Leach J (8060) Rickmansworth
Lee G (8244) Eastleigh
Luxford B (8108) Hornchurch

M
Macleod A (8009) Glasgow
Maisey G (8055) Welwyn Garden City
Mallatratt P (8267) Sidmouth
Manyande N (8113) Beckenham
Mcclenaghan L (8209) Leeds
Mehers A (8188) Bury
Mennim N (8001) South Queensferry
Monks M (8187) Stockport
Moulds V (8181) Salford
Myatt A (8208) Tadcaster

N
Nicholls P (8046) Guildford

O
O'Boyle P (8241) Reading

P
Parry C (8008) Glasgow
Patel S (8093) Aylesbury
Paxton A (8077) London
Poole V (8184) Prescot

R
Rawlings J (8235) Bristol
Regon D (8024) Belfast
Reilly A (8132) George Town
Robinson J (8213) Leeds
Ross M (8111) London
Rupping J (8128) Bedford

S
Sharp J (8127) Twickenham
Simmons A (8095) London
Stafford N (8232) Gloucester
Stanyon B (8085) London
Strowger J (8066) London

T
Taylor P (8182) Tarporley
Thompson O (8177) Manchester
Tomson J (8178) Preston
Townsend V (8076) London
Townsend I (8257) Northallerton

V
Venner L (8258) Crediton

W
Warnock D (8028) Belfast
Watkins A (8072) London
Watson P (8019) Belfast
West N (8156) Shrewsbury
Whalley K (8094) Egham

Y
Young K (8246) Alton

Analysis of November 2013 results

Papers sat	Papers passed				
	3	2	1	0	Total
3	51	23	11	13	**98**
2	–	26	29	31	**86**
1	–	–	44	33	**77**
Grand total	**51**	**49**	**84**	**77**	**261**

Do you know your WPSATC from your simple WP?

The world of 'litigation headings' made easy…

To non-lawyers, documents written by lawyers can often seem unnecessarily complicated, pernickety, convoluted and difficult to understand. Added to that, many documents are often headed with strange phrases such as 'Attorney-Client Work Product', 'Privileged', 'Subject to Common Interest Privilege', 'Without Prejudice', 'Subject to Contract' and so on. What do these mean exactly and why are they used? This short article will provide a quick and simple summary of each of the most prevalent of these phrases so that they can be better understood and used correctly by readers.

'Privileged' or 'subject to privilege'

The most common of these headings is an assertion that a document is 'privileged'. The effect of a document being 'privileged', once established, is that it does not have to be disclosed to the other side or to the court during legal proceedings (most commonly, during disclosure). Privilege is a very large topic of its own and this article can only deal with the subject in outline, but at its simplest there are two forms of privilege: legal advice privilege and litigation privilege. In brief, the first category covers confidential communications between lawyers and their clients, which are made for the primary purpose of offering legal advice; the second covers confidential communications between lawyers and clients or between lawyers or clients and a third party, which are made in connection with actual or imminent litigation. Adding the heading 'privileged' to a document does not actually make the document privileged but makes it easier to identify documents that are intended to be privileged. When assessing whether or not a document is covered by privilege, the court will have regard to its nature and purpose and will consider its actual substance rather than the label attached to it.

> "Adding the heading 'privileged' to a document does not actually make the document privileged"

'Without prejudice'

The label 'without prejudice' is only used when efforts are being made to settle a dispute between the communicating

parties (though there is no requirement for actual court proceedings to have been commenced). Labelling a letter or an email in this way provides a degree of protection for the writer insofar as any statements made in that correspondence (such as, for instance, a statement that could be construed as an admission of liability) cannot be used by the other party in any subsequent court proceedings. The reasoning behind the principle of 'without prejudice' communication is ultimately to encourage parties to make reasonable and realistic attempts to resolve a dispute as soon as possible. Parties are understandably far more incentivised to make an offer of settlement when they can be safe in the knowledge that there is no risk that the contents of their offer might be used to their detriment further down the line. To the extent that 'without prejudice' correspondence cannot be used by the parties in legal proceedings, it is said to be covered by 'privilege'.

'Without prejudice save as to costs'

In what can be viewed as an extension to the 'without prejudice' principle, it is also common for parties to mark certain correspondence as being 'without prejudice save as to costs'. As with correspondence simply marked with the shorter phrase, communications bearing this longer expression cannot be used in court or in an arbitration while the relevant dispute is being determined. However, such communications can be brought to the attention of the judge or arbitrator after the matter has been settled when he or she is making an order as to which party will bear the cost of the proceedings. Evidence of a genuine willingness to settle a dispute earlier can be very influential over a judge or arbitrator exercising his or her power to make an order for costs; to this end, 'without prejudice save as to costs' offers can potentially be of real benefit to any party who chooses to make one by potentially placing a risk of adverse costs being awarded against the other side. Again, the aim of their existence is to encourage active attempts to settle a dispute outside of court.

'Subject to contract'

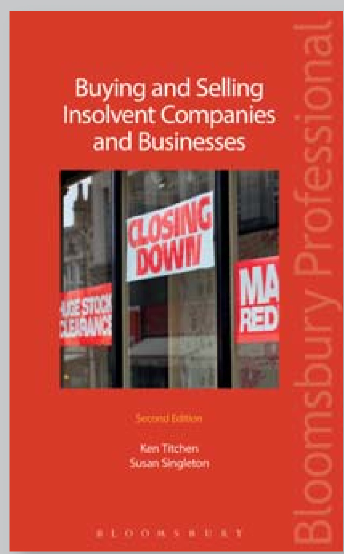
The phrase 'subject to contract' is often employed between parties in general commercial situations since it allows a greater degree of freedom when negotiating the provisions of a contract. For instance, the effect of labelling the proposed terms of a sale agreement as being 'subject to contract' is to ensure that neither party will be bound until a formal contract is executed. In a litigation context, for example, when negotiating a settlement agreement, the term can be used to ensure that the general terms of settlement that have been agreed are not binding on the parties unless they can agree the final form of a written contract of settlement. The matter is effectively deemed to be still under negotiation while this expression is used, meaning that either party could withdraw or alter its position without having the danger of incurring liability.

> "The aim… is to encourage active attempts to settle a dispute outside of court."

In addition to labelling their communications 'without prejudice', parties in a dispute may also choose to state them to be 'subject to contract'. As in the general commercial context, the use of such a label on a settlement offer means that the parties will not be bound by its terms until a formal agreement to that same effect has been entered into. Once again, the result is that disputing parties are in theory pushed to be more willing to explore alternative ways of resolving their issues without the need to resort to a judge or an arbitrator. ◻

DANIEL HENNIS is an associate at Jones Day.

Editor recovery@r3.org.uk | Recruitment recovery@r3.org.uk/recruitment



- **Edition** Second
- **Authors** Ken Titchen and Susan Singleton
- **Publisher** Bloomsbury Professional
- **ISBN** 978 1 78043 201 4
- **PRICE** £95

> “This book sits squarely within the category of academic text that serves both sides of the experience divide.”

Buying and Selling Insolvent Companies and Businesses

As any experienced restructuring practitioner will know, the sale of the business of an insolvent company has a number of nuances that do not arise in a solvent transaction. The ease in which a transaction is completed will often depend on the recognition of those nuances by the professionals acting on either side of the transaction. In this second edition of their book, Ken Titchen and Susan Singleton have sought to produce an authoritative text that deals with each stage of a sale and purchase transaction, with the law current as at 1 April 2013.

With the first chapter of the text dealing with basic corporate insolvency principals, it might at first appear that this text is pitched at the inexperienced, rather than the seasoned, professional. It is clear, however, from the remainder of the text that with issues such as financial support direction (FSD) notices being addressed (albeit in short form) that this book sits squarely within the category of academic text that serves both sides of the experience divide.

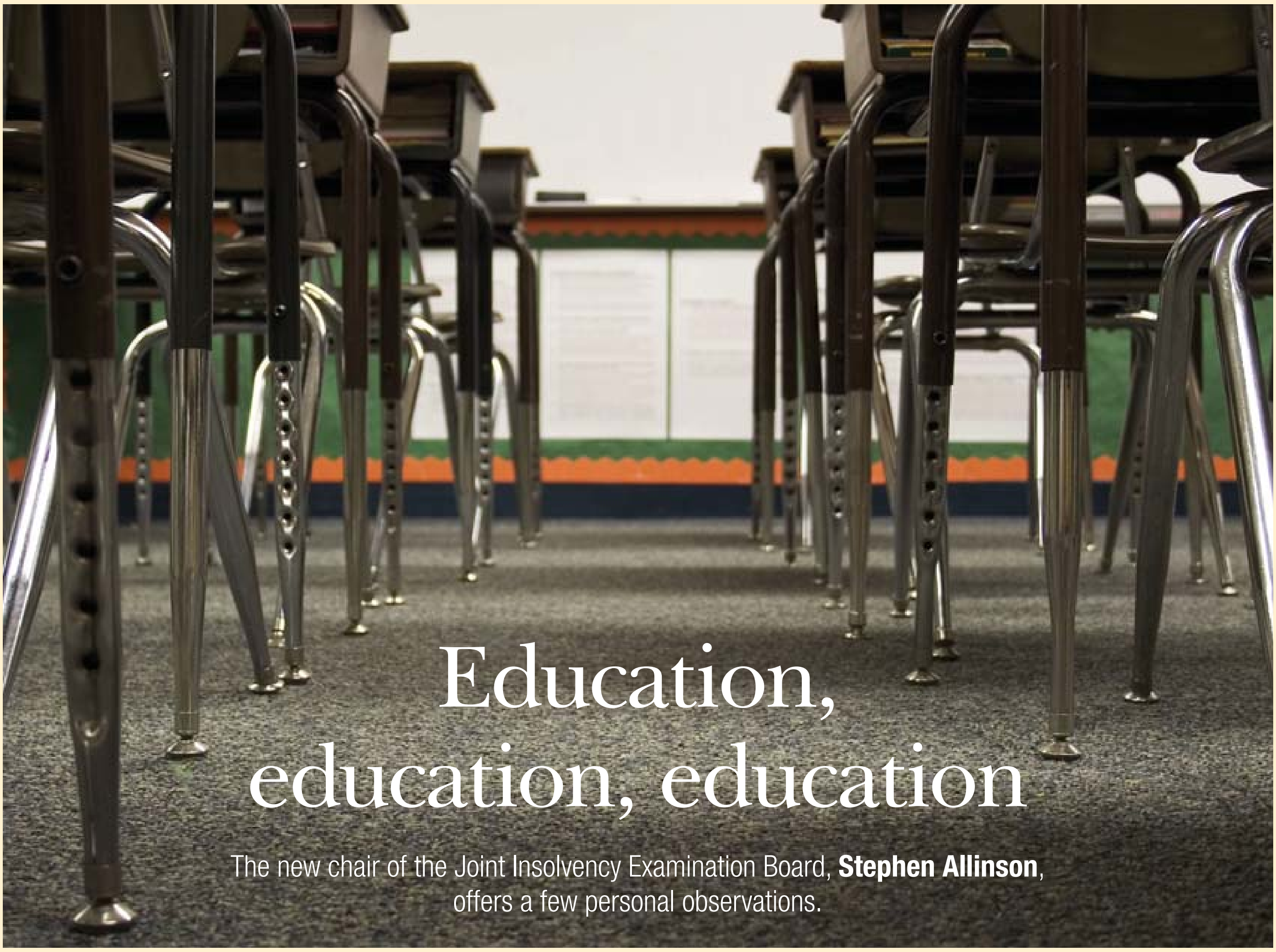
Topics covered include pre-pack sales, due diligence, security issues, employees, pensions, property matters and issues affecting particular classes of assets. Each chapter is thoughtfully set out and well supported by a good index.

Included within the appendices is a useful sale precedent and some common annexures, eg assignment of intellectual property rights (IPR) which have been adapted from practical law company precedents. For straightforward transactions, most issues have been well covered.

Needless to say, it is impossible to refer to all transaction eventualities in a text of this length. For the more complex transaction, reference may need to be made elsewhere for more detailed academic coverage. That said, there are plenty of pointers within this book to at least recognise that a more comprehensive analysis of a particular issue may be required.

Having set out to produce an authoritative text on the sale and purchase of the business of insolvent companies, Titchen and Singleton have done just that, certainly within the 'straightforward' category of transaction type. This book will serve as a useful resource for lawyer and IP alike, whether advising the acquirer or acquiree.

KEVIN HAWTHORN is an associate in the corporate recovery and insolvency team at DAC Beachcroft LLP.



Education, education, education

The new chair of the Joint Insolvency Examination Board, **Stephen Allinson**, offers a few personal observations.

As I write this article, those who sat the Joint Insolvency Examination Board (JIEB) exams at the end of 2013 are anxiously awaiting their results. The pass list is always scrutinised carefully not only by those who have taken the examination but also employers and prospective employers, and, no doubt, the JIEB tutors!

Passing the JIEB is, quite rightly, considered a significant professional achievement and the June graduation ceremony is always a celebratory event for those who have been successful. It is very pleasing to see the joy and obvious pride of the candidates as their names are announced and they collect their certificates.

Of course, given the ever-revolving circle of life, as one set of students await their results, another group is commencing the study and courses that are necessary for the 2014 examination and beyond. As the year draws on they will be cranking up their efforts towards that demanding week. That is as it should be, the examination is considered a tough one, and many war stories are told about it in smoke-filled rooms by disgruntled candidates (I couldn't, of course, possibly comment any further on that).

Challenges ahead

I feel very privileged to have been asked to be chair of the JIEB and am looking forward to the challenges that will bring. I have a hard act to follow in my good friend and colleague Peter Windatt, who has served us for a number of years, and we have all benefited from his quiet authority and wise leadership.

No examination of professional standards can stand still, however, and as I take over the reins, I realise that the board and I face some significant challenges ourselves. I welcome the opportunity through the pages of *RECOVERY* magazine to share some of those challenges with the profession and would welcome further dialogue and debate over the coming months and, indeed, years.

"Many war stories are told about it in smoke-filled rooms by disgruntled candidates."

Feedback and a forum

So, let's start with a bit of a hand grenade – is the examination the correct way to test a person's right to act as an insolvency practitioner? After all, this is a profession based upon pragmatism, practicality and judgements informed by experience. As such, it seems a fair debate to consider whether the examination should be more practically based – or should it have an element of continuous assessment or case study work in it? Should, for example, there be a practical exam to accompany it?

Before the jungle drums start beating that the qualification process is about to change, let me stress that no such changes are on the immediate horizon, but I do think it is right to discuss such questions and I would welcome a forum to consider these issues with relevant personnel from the regulatory bodies (RPBs). Perhaps this is something that R3 would wish to assist in facilitating?

These and many other questions are often fed back to those of us who sit on the board as, of course, we are the body which oversees the examination and the process surrounding it. Unfortunately, there are no easy answers. Nevertheless, I do believe the fact that the exams fuel an ongoing discussion on a number of fronts is healthy.

New faces

At the end of last year, we undertook for the first time an open advertisement and selection process to appoint a new senior moderator. Alan Katz has held that post for a number of years and has greatly assisted in ensuring that the process is very professional in its organisation and delivery. This article also gives me an opportunity to thank Alan and wish him all the best for his 'retirement'.

Two board members and I conducted

the interview and selection process and we were very impressed at the standard of applicants, and I am very pleased to welcome Steve Treharne as our new senior moderator. Steve will be well known to many of you as a former senior insolvency partner with KPMG and a very experienced practitioner.

We are always anxious to maintain the professional independence of the examinations team from the board, but similarly we meet regularly to ensure we are 'on the same page'. Again, if any reader wishes to discuss the opportunities that may exist to be part of the examinations team, please contact me at the email address below as we are adopting a streamlined process for future appointments.

New developments

The debates over how theory based or otherwise the examination should be does itself open several further branching debates and one element of this debate has even hit ministerial level. Last year, the insolvency minister Jo Swinson reignited the argument about whether there should be separate licences to practice personal and corporate insolvency. This then found its way into the draft Deregulation Bill and The Insolvency Service confirmed to me in January that it is very likely that these provisions will be passed into law.

On behalf of the JIEB, I submitted a response to the consultation that took place, but I also recognise that if this is the wish of parliament then the task of the board is to prepare an examination that reflects what is decreed. On this issue, I note that R3 has been campaigning diligently as well and there is no doubt that it is an important matter for our profession. We could, however, be seeing the introduction of these partial licences next year.

We do have firms that specialise in either personal or corporate insolvency solely, but I do still think that there is a core set of skills necessary for both, and so I am confident in saying that we will need to ensure that any new examination will need to reflect that fact.

There is no doubt that there is a move to increasing specialisation in our industry and, of course, the Insolvency Practitioners Association announced last year its new corporate insolvency examination, which is an equivalent qualification to the Personal Insolvency Certificate that it has run for a few years now. I am sure that the changes that may follow from separate licensing can also be very usefully discussed with the RPBs.

An even-handed approach

The truth is that we are meant to be all things to all men and women. We are expected to adopt this chameleon characteristic and act accordingly depending on the circumstances of the case and depending on for whom we are acting. Our approach is clearly different if we are acting for a debtor or a creditor and possibly also if we are acting for secured or unsecured creditors.

I feel that our skills are enhanced if we do have this mixed practice. As a very newly qualified solicitor I spent much time in the magistrates courts of the South West (purely professionally, you will understand) and initially it was before the advent of the Crown Prosecution Service, so I would be prosecuting one day and defending the next. I was always of the opinion that my abilities to do my best for my clients were enhanced by being on both sides of the fence.

Skills – soft, intellectual and ethical

If we are looking at examining the basis of an IP's work, then should we be looking at a 'soft skills' element of the qualification? Much of a practitioner's work requires people skills, and those skills at present seem to be learnt only through experience. Is this an area we need to develop for our future practitioners? If so, how should we go about it?

Perhaps it is not only professional knowledge and intellectual skills that should be measured. Other qualities go into the mix; for example soft skills in terms of empathy with those involved in the insolvency and recovery process. Again, a number of years ago a valued member of any insolvency team was the ubiquitous 'meetings man'. We would now know him as 'creditor services', I think. But this individual was often at the forefront of trying to develop client relationships for his or her firm through attendance at creditors' meetings and talking to other creditors and their representatives. Without doubt, in my opinion, people skills are a vital part of being a good practitioner. We can't easily measure that by examination, although in the JIEB it is recognised that we should try, wherever possible, to reward more than just academic and technical knowledge, and I hope we do that by the holistic marking process.

> "The profession has come a long way in terms of regulation and education."

Following through on some ideas of developing the scope of the examination should we consider a free-standing ethics paper in the JIEB suite? We do seek to examine such issues across all papers at the moment, but there is a strong argument for stating that ethics is the rock upon which all IPs must build their career and ethical principles are fundamental to every assignment undertaken, and possibly we need to think about giving these matters more weight.

The next generation

My final theme is the way that students are prepared for the examination. It is particularly pleasing to me to see that there is now a choice of training providers for students. That can only be a good thing, demonstrating that this is a qualification that merits organisations putting time and energy into the tutoring process. We meet annually with the tutors to discuss any concerns they may have and that dialogue has developed very positively in recent times.

I am conscious that perhaps the JIEB is not as visible as it should be. I am determined to develop that visibility in the near future. We are looking at ways we can use the internet and other communication methods to a much greater degree than we do at the moment. The profession has come a long way in terms of regulation and education. Especially given the big name insolvencies of recent years, we are in the public eye more often than not, and so the way new entrants to the profession are trained is not just important but vital in determining how we are viewed.

I want to see younger members of our profession being encouraged to qualify and provide us with the next generation of leading practitioners. I realise that is a challenge for firms, with many saying that they are seeing reducing work levels and facing other pressures in their practices. As someone who is now classed as an older practitioner, I realise the importance of being prepared to let go and accept that I have a crucial role to play in supporting more junior professionals. It is surely crucial for the future of our profession that senior professionals know when it is right to pass the baton on, and how satisfying it is to know that the profession is producing excellent new young practitioners.

I really hope that the JIEB can assist in that process and I am very excited at the part we can play. You can be assured that the board and I will work tirelessly to ensure the examination remains fit for purpose and an examination of which we can all be proud. ◻

The author is the first solicitor to be elected chairman of the Joint Insolvency Examination Board and can be contacted at **stephen.allinson@la-law.com**.

STEPHEN ALLINSON is a consultant solicitor and licensed IP with Lester Aldridge Solicitors.

Insolvency Practitioners Association (IPA) New Corporate Insolvency Exam

IPA has launched a new corporate insolvency examination and twice yearly sittings for its Certificate of Proficiency in Insolvency (CPI) suite of exams.

The IPA was established over 50 years ago to serve practitioners specialising in insolvency work and to advance knowledge and understanding of insolvency. Its CPI exams have been set annually since 1995 and enjoy strong brand recognition amongst students, employers and the wider profession as an intermediate test of competence and a valuable and worthwhile achievement. Feedback from member firms confirms that the mix of multiple choice, short form as well as essay style and longer computational questions provides an important boost to the skills and abilities of candidates conducting insolvency assignments in the workplace.

CPCI

Four years ago the IPA introduced the Certificate of Proficiency in Personal Insolvency (CPPI) for those focussing on this sector of the market. In August 2013 it launched a new equivalent paper for those whose work is primarily concerned with procedures for insolvent companies – a Certificate of Proficiency in Corporate Insolvency (CPCI). It is the first examination of its kind at this level and has been warmly welcomed by a number of leading firms.

Following a pilot paper for CPCI last December, all three papers (CPI, CPPI, CPCI) will be set this year both in June and December, with training providers offering tuition for both sittings. Results are now issued in the month following the sittings.

A new syllabus for the suite of exams has been published and is available to download from our website.

We are now accepting bookings for the June 2014 exam sitting. Please visit our website at www.insolvency-practitioners.org.uk to download your booking form, or call 020 7623 5108.

Tips to survive and prosper in 2014

Richard Preston offers a solicitor's perspective on insolvent law firms.

It has been widely reported in the legal press that there are currently law firms in the UK in serious financial difficulty.

High profile collapses of Halliwells, Cobbetts and more recently regional and niche practices, including Challinors and EOS Law, have meant that the once unheard of insolvency in law firms has become a realistic concern. Insolvency solicitors and insolvency practitioners who have been involved with insolvent law firms may have noticed a number of common trends.

Cash flow management

If a practice does not have sufficient available cash to meets its running costs there is a serious risk of the firm failing.

Lock-up of work in progress and firms working on conditional fee agreement and damage-based agreement can, if not managed properly, cause serious cash flow problems.

Many firms take more than 60 days to collect on invoices delivered. In common with any other business 'cash is king'. If firms run out of cash, insolvency may soon follow.

Professional Indemnity Insurance (PII)

On 29 December 2013, 136 solicitors firms failed to obtain qualifying insurance after the Extended Policy Period (EPP) and had to be closed down. Inevitably, this will lead to the insolvency of firms and partners alike.

Obtaining and retaining PII cover will be a serious issue for firms going forward, particularly with a number of the large rated insurers moving away from the small firm market. In 2014 and in the future firms that are unable to obtain PII insurance, or who face unmanageable premiums, are likely to have to deal with issues including insolvency.

New entrants to the market

The Legal Services Act came into force in 2011. Solicitors' firms cannot underestimate the changes to the landscape of the legal market now and in the future. Following the Co-op's entrance into law there are a number of insurers that have been granted alternative businesses structure (ABS) licences including Direct Line and Admiral. Also, household names in other sectors have entered the legal market, such as the AA and Saga. The new ABSs are offering services to their already-existing customer base. Fixed fees and easily accessible online products have and will drive down the cost of some legal services, particularly commoditised services typically offered by high street practices. Competition may mean loss of revenue. A loss of revenue to any business creates a greater risk of insolvency.

> "In common with any other business, cash is king."

Bank support

Historically, banks were keen to lend to solicitor partnerships. Low failure rates, high income, large client accounts and personal guarantees provided by partners meant that solicitors' practices were considered a 'good bet'.

More recently the insolvency of law firms, particularly high-profile casualties such as Halliwells, have affected banks' confidence in lending and support. It's not that the banks are not lending but they are much more careful about which firms they lend to and in which sectors the firm practises. Firms that are heavily engaged in personal injury or other forms of litigation on conditional fee agreements can have a long lock-up of work in progress. Banks may be reluctant to support firms practising heavily in these disciplines, increasing pressure on firms and their finances. Banks now have a keen eye on the legal market. A reduction in an overdraft or a facility could mean a once-healthy law firm is facing insolvency

Legal Aid cuts

Last year (2013) saw cuts to Legal Aid. Legal Aid is now rarely available for family, employment, personal injury and social welfare cases. Criminal defence work has seen reductions in the rates with fixed fees and means-tested applications reducing the volume and profitability of the work. Legal Aid income for criminal defence work is set to be reduced by 17.5 per cent in 2014/15. Firms undertaking Legal Aid will have seen a reduction in turnover. Unless addressed quickly in other areas and managed with reduced operating costs, reductions in the turnover of a practice will increase the prospect of the onset of insolvency.

SRA scrutiny

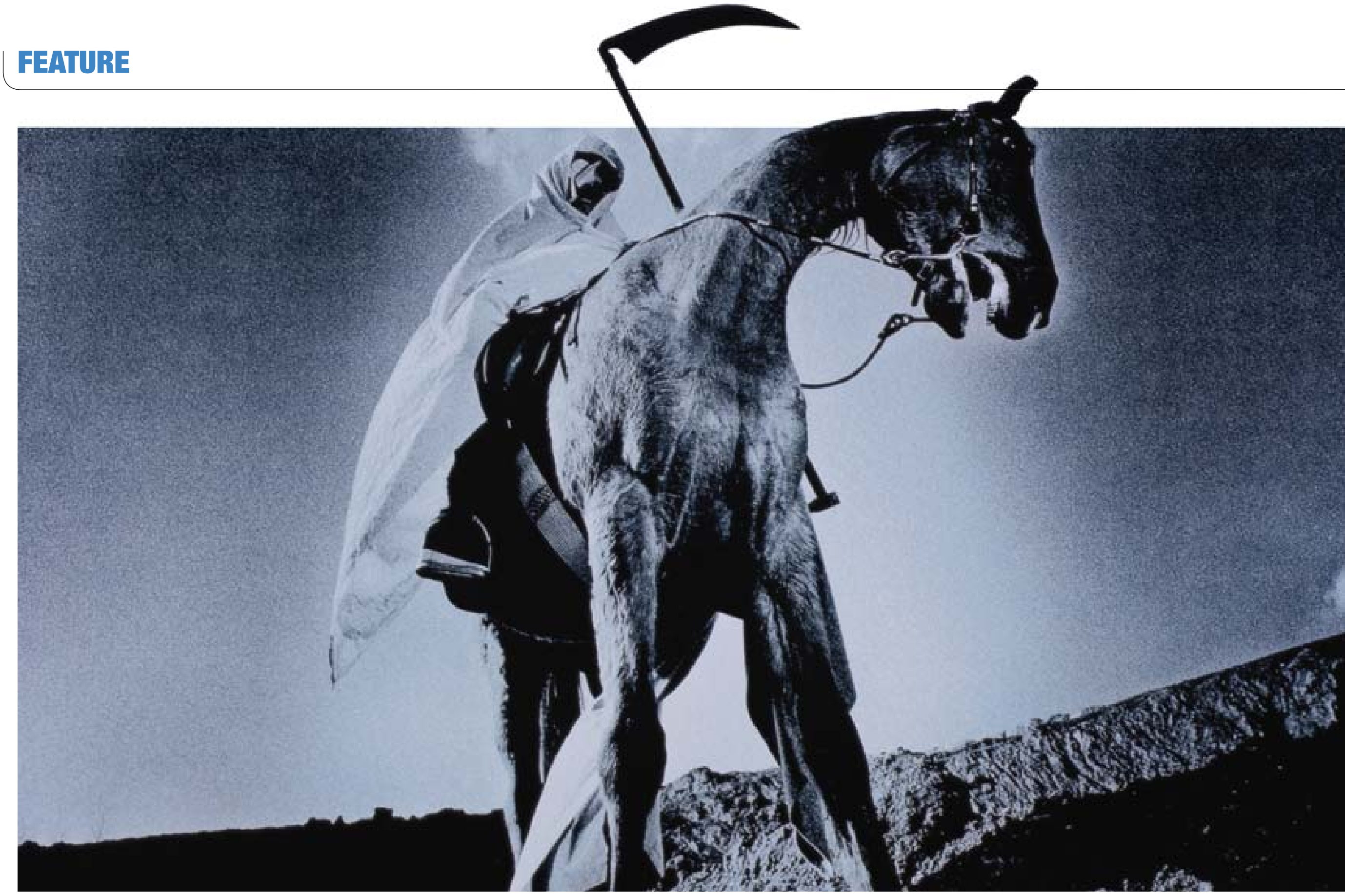
The Solicitors Regulation Authority (SRA) has confirmed that it will closely scrutinise law firms displaying signs of financial difficulty. If the SRA believes that clients are at risk it has the power to intervene. An SRA intervention immediately suspends a firm's right to trade often resulting in the firm's insolvency.

Expenditure

Glass-fronted offices and long expensive leases are not uncommon in law firm insolvencies. Landlords have been listed as creditors in a number of recent high-profile law firm insolvencies. If turnover is reduced, PII premiums are increased and bank support is uncertain, law firms need to be very careful when entering into leases with a rent that puts further pressure on the firm's finances and cash flow.

Law firms must be prepared to adapt, change and evolve to meet modern commercial demands. Good practice management, a tight control on cash and a clear vision of opportunities and risks must be at the forefront of a firm's management policies if it is to survive and prosper in 2014 and beyond.

RICHARD PRESTON is a partner at Beswicks Solicitors LLP.



The Model Law is dead? Long live the Model Law!

Ian Williams and **Professor Adrian Walters** ask if the game is up for the universalist faction.

In early 2013, the impact of the UK Supreme Court's decisions in *Rubin* v. *Eurofinance SA; New Cap Insurance Corpn Ltd* v. *Grant*[1] was being mulled over by practitioners. The *Rubin* decision in particular was met with differing emotions and much was written on the subject in the forthcoming months. The views of universalists on this side of the pond largely mirrored the views and concerns of US universalists following the 2007 decision *Re Bear Stearns High-Grade Structured Credit Strategies Master Fund, Ltd*.[2] Others took the view that the decisions restored certainty to the law on the recognition and enforcement of foreign judgments that the Court of Appeal's decision to the contrary in the same case threatened to undermine.

In *Rubin*, Lord Collins described modified universalism as 'a trend but only a trend'.[3] Others meanwhile regarded the *Rubin* decision as merely a blip in the otherwise relentless progress of international law towards its preordained universalist destiny. Those in the latter camp are therefore not unduly perturbed by the *Rubin* court's seemingly calculated attempt to undermine Lord Hoffman's philosophy of cross-border cooperation as embodied in the Privy Council's iconic decision in the *Cambridge Gas* case.[4]

Practitioners in the United States and the offshore jurisdictions have good reason to regard the Supreme Court's treatment of *Cambridge Gas* as unnecessary. Their Lordships in *Rubin* heard no argument and were not asked to rule on the correctness or otherwise of the Privy Council's decision on its own particular facts. They should have left well alone.

> "Practitioners tell us that in two of the cases the rulings helped prompt settlement between the warring parties..."

There is a principled case for the rehabilitation of *Cambridge Gas* and a narrow reading of *Rubin* and the need for such an approach may now be more pressing in the light of recent developments in the United States.

In this article, we discuss four relatively recent US cases which illustrate the ambivalence of the US courts towards the concept of modified universalism. In each case concerns for indigenous stakeholders and constituencies were to the fore. Given the current position in the UK and the recent decisions in the US together with the meagre take up of the UNCITRAL Model Law, we may question whether the game is over for the universalist faction and whether countries will increasingly prioritise the concerns of vocal indigenous stakeholders at the expense of promoting global solutions to international insolvencies.

It is not possible in the space available to set out in detail the particular circumstances of each of the cases we will refer to. It will be said in some quarters that they do in fact show the 'value of enforcement in friendly jurisdictions' but 'depending on the locale of a debtor's assets and operations, this is not enough'.[5] Practitioners tell us that in two of the cases the rulings helped prompt settlement between the warring parties but what of the 'big picture'?

The Four Horsemen of the Apocalypse?

Re Vitro,[6] *Re Elpida*,[7] *Re Qimonda*,[8] and *Drawbridge Special Opportunities*[9] have very particular facts and circumstances but together, in our view, show the continuing persistence of territorialism, some would say for credible and understandable legal, political and practical reasons.

Editor recovery@r3.org.uk | Recruitment recovery@r3.org.uk/recruitment

Re Vitro

Vitro was the largest glass manufacturer in Mexico. It had significant operations and subsidiaries in seven countries including the US. Its holding company had issued around $1.2bn of unsecured notes that most of its subsidiaries had guaranteed. The guarantees clearly stated that the subsidiaries' obligations would not be modified or released by any bankruptcy proceedings filed by the holding company. In 2010, the holding company initiated insolvency proceedings in Mexico but the subsidiaries did not. At the time of the Mexican filing, the holding company owed around $1.7bn, of which $1.2bn was owed on the unsecured notes.

Two of the directors were appointed by Vitro's board to be Vitro's foreign representatives for the purposes of a Chapter 15 case that was duly commenced in the Bankruptcy Court for the Northern District of Texas in 2011. The Bankruptcy Court recognised the Mexican proceedings as 'foreign main proceedings' and the two board appointees as 'foreign representatives'.

Later in 2011, Vitro filed a restructuring plan in the Mexican proceedings, the effect of which, as matter of Mexican law, was to extinguish the existing unsecured notes, to release the guarantor subsidiaries from liability, and restructure the obligations of Vitro and the subsidiaries so as to reduce the principal owing on the unsecured notes. The Mexican court approved the plan in early 2012 and the foreign representatives then filed a motion seeking to enforce the plan in the Chapter 15 proceedings with the aim of preventing the existing note-holders from pursuing their original claims against US based guarantor subsidiaries.

The Bankruptcy Court at first instance refused the foreign representatives' application for enforcement of the plan and they then appealed. The Fifth Circuit affirmed the Bankruptcy Court's decision and held that the plan was unenforceable under Chapter 15.

It is entirely clear that the court **could** have found a way under sections 1507 and 1521 of the Bankruptcy Code to give effect to the Mexican plan. However, it chose not to do so in part because it did not like the effect of the plan on the note-holders, a significant number of whom were US based. It is said that the decision to refuse enforcement focused the minds of the key parties and resulted in a settlement but in essence, the Fifth Circuit, in our view, simply found a way to circumvent giving effect to the Mexican court's approval of the plan. It is noteworthy that Vitro only succeeded in procuring approval of the Mexican plan because of the favourable votes of the guarantor subsidiaries, which were creditors by virtue of their holdings of inter-company debt. Indeed, the first instance court in Mexico initially denied the plan confirmation on the ground that the inter-company claims should not be counted towards the statutory threshold for creditor approval. However, the Mexican appellate court reversed that ruling and there was no further challenge to the plan approval in Mexico. The US note-holders clearly calculated (rightly as it turned out) that they were better off litigating their objection to the plan on US soil.

Re Elpida

This case involved the corporate reorganisation of a Japanese company under the Japanese Corporate Reorganisation Act. Elpida was an IT company that developed, manufactured and marketed dynamic random access memory. It was the third largest manufacturer in the world and held thousands of US patents.

Its authorised representatives filed Chapter 15 proceedings and in April 2012 they were recognised as foreign representatives and the Japanese proceedings were recognised as foreign main proceedings.

Japanese insolvency proceedings although modelled on the pre-1978 US bankruptcy law are significantly different from US proceedings particularly in terms of creditor participation and influence in the proceedings which is quite restricted by our/US standards. Furthermore, sales of assets in Japanese proceedings do not require public auction and typically occur privately with limited disclosure of information. These cultural differences were seized upon by the affected note-holders and clearly weighed heavily on the minds of the US judges.

> "In effect the US court replaced and supplanted legal standards reflective of Japanese business culture with its own standards."

In summary, in July 2012 Elpida publicly announced that it was to sell its assets to Micron Technology. The sale was to be incorporated into the plan of reorganisation. The structure of the sale, however, came as a surprise to Elpida's note holders who, from press reports, had been expecting significantly higher realisations from the sale.

The note-holders intervened in the Chapter 15 and asked the court to require that any sale impacting on the US assets should not be completed without notice to the US court and to all interested parties. Certain transactions affecting US assets had already been completed without recourse to the US courts, such transactions having been approved in Japan on an ex parte basis.

The US court did subsequently approve two of the transactions and although other similar disputes existed, the parties ultimately resolved their differences.

The interesting points arising from this case relate to the US courts' view on the importance of comity. Again, we believe the US court **could** have given effect to the Japanese reorganisation plan but it said '[t]here can be no doubt that promoting comity is a general objective of Chapter 15. But it is not the end of the statute. To require this Court to defer in all instances to [a] foreign court decision would gut section 1520'.[10] In effect the US court replaced and supplanted legal standards reflective of Japanese business culture with its own standards. Arguably, this is not what the UNCITRAL Model Law is designed to achieve unless there was something particularly repugnant to US public policy about Japanese reorganisation proceedings.

Re Qimonda

Qimonda AG was a German manufacturer of semiconductors that entered German insolvency proceedings in Munich. Its assets consisted mainly of patents, of which around 4,000 were US patents. The German administrator, Dr Jaffé, sought and obtained recognition of the insolvency proceedings as a foreign main proceeding in the US under Chapter 15. Dr Jaffé then moved to reject the US licence agreements by recourse to his statutory power in section 103 of the German Insolvency Code. His objective was to re-license the patent portfolio in a manner that would improve returns to Qimonda's creditors.

In US bankruptcy proceedings, the ability of a trustee to reject a patent licence is circumscribed by section 365(n) of the Bankruptcy Code. Under this provision, licensees can elect to retain their existing rights to the underlying intellectual property in return for making any required royalty payments. There is no equivalent provision in German law. The crucial issue therefore in *Qimonda* was whether US licensees could invoke US law protections to defeat what, as a matter of German law, was a clearly a legitimate exercise of the German administrator's powers.

The Fourth Circuit Court of Appeals affirmed the lower court rulings in favour of the US licensees. It was clear that under section 1521 of the Bankruptcy Code, the US courts could in their discretion give effect to Dr Jaffé's exercise of his German law powers in the US. However, the Fourth Circuit held that it was required by section 1522(a) to ensure that the interests of creditors and other interested entities were 'sufficiently protected'. Accordingly, the court concluded that it was entirely appropriate for any relief under section 1521 to be circumscribed by reference to section 365(n) so as to provide the US licensees with 'sufficient protection'.

The Fourth Circuit could have gone further and held (as had the Bankruptcy Court) that for the US courts to allow a German administrator to exercise his powers without affording the US licensees the protection of section 365(n) would be manifestly contrary to US public policy. »

Qimonda therefore illustrates that it is perfectly possible for local courts to protect local commercial interests from encroachment by foreign representatives without having to take the drastic step of invoking the public policy exception.

Drawbridge Special Opportunities

In this case, the Second Circuit Court of Appeals added an additional eligibility requirement for the filing of Chapter 15 cases. In simple terms, it ruled that a foreign entity is not eligible to be a debtor under Chapter 15 unless it has property in the US or meets the residence, domicile or place of business tests under section 109 of the Bankruptcy Code. This is not a problem in most cases and is generally thought capable of being easily remedied in any event. The Australian foreign representatives in this case, however, wished to use the Chapter 15 proceedings not for asset realisation but to institute discovery[11] against Drawbridge (to which it objected).

The foreign representatives argued that the definition of 'debtor' in section 1502(1) as 'an entity subject to foreign proceedings' meant that the requirements of section 109 did not apply. The court disagreed. It held that section 103(a), which invokes Chapter 1 of the Bankruptcy Code (which includes section 109), applies in a case under Chapter 15.

The argument that the application of section 109 would undermine the purpose of Chapter 15 was not accepted. The court held that 'It is true that the Model Law does not contain an express requirement akin to section 109(a)' but 'Regardless, the omission of section 109(a), or its equivalent from the Model Law does not suffice to outweigh the express language Congress used in adopting sections 109(a) and 103(a)'.

As we have said, this decision is unlikely to cause major difficulties and appears to be the product of a drafting glitch that could easily be fixed by legislative amendment. The case advanced by the foreign representatives was far from hopeless but once again the court found in favour of the US party.

Conclusion

The UNCITRAL Model Law and the concept of modified universalism have within them ample scope for balancing and in some cases prioritising local interests.[12] The problem for judges is that they are sitting in national courts rather than in some utopian international forum and, as they are branch of national governments, it may be said to be perfectly natural for them to favour their own citizens. Consequently there is plenty of scope for what may be pejoratively referred to as 'territorialist' tendencies.

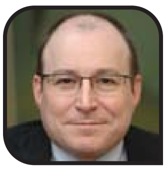
> "The world does not appear to be unfolding towards the glorious triumph of universalism..."

Ultimately, however, judges resolve disputes that the parties are unable to settle themselves, and it would therefore be wrong to suggest that decisions that are 'territorialist' in inclination are simply the product of judicial parochialism. Those professionals and stakeholders who 'play' in the international and restructuring arena clearly remain to be convinced that international cooperation will pay dividends, for example, in increasing trust between jurisdictions and in the expectation of reciprocal treatment. Of course this kind of reciprocity has been institutionalised in the Commonwealth through mechanisms such as section 426 of the Insolvency Act 1986 and its statutory equivalents elsewhere. The UK does not have that kind of framework with the US. In adopting the UNCITRAL Model Law as Chapter 15 of the Bankruptcy Code it could be said that the US was extending the olive branch that the UK accepted by passing the Cross Border Insolvency Regulations 2006. The *Rubin* and *NewCap* decisions, however, demonstrate that there is still a very long way to go before the 'new world' is afforded the same treatment as the 'old world'.

It is becoming clear that the UNCITRAL Model Law was essentially a modest development that has been incredibly over-hyped and promoted in some circles. The world does not appear to be unfolding towards the glorious triumph of universalism in international restructurings and insolvencies nor indeed, in the wider sense, does the concept of 'internationalism' seem to have any more supporters than it ever had. Maybe we should be content to accept that these cases simply show judicial pragmatism (which is clearly sanctioned under the Model Law) and shift the emphasis towards more structured engagement between stakeholders and their advisers.

References

1. [2012] UKSC 46; [2013] 1 AC 236
2. Nos. 07-12383 & 07-12384 (Bankr. S.N.D.Y Aug 30, 2007). See American Bankruptcy Institute Journal January and February 2008 'How the Assault on Offshore Havens in Bear Stearns undermines New Chapter 15' Timothy T. Brock
3. [2012] UKSC 46- page 8 paragraph 16
4. *Cambridge Gas Transport Corporation* v. *The Official Committee of Unsecured Creditors of Navigator Holdings plc* [2006] UKPC 26; [2007] 1 AC 508
5. American Bankruptcy Institute Winter Leadership Conference 2013 'Cross-Border Enforcement of Orders in Restructuring Cases' Mark W Devano and Mathew Cursio
6. *Ad Hoc Group of Vitro Noteholders* v. *Vitro S.A.B. de C.V (Re Vitro S.A.B de C.V)*. 701 F.3d 1031 (5th Cir. 2012)
7. *Re Elpida Memory, Inc.*, No. 12-10947, 2012 Bankr. LEXIS 5367 (Bankr. D. Del. Nov 16, 2012)
8. *Jaffé* v. *Samsung Elecs. Co. Ltd.*, No 12-1802. 2013 WL 6388591 (4th Cir. Dec. 3 2013)
9. *Drawbridge Special Opportunities Fund LP* v. *Barnet (Re Barnet)*, F.3d 2013 WL 6482499 (2d Cir. 12/11/2013)
10. Section 1520(a) applies other sections of the US Bankruptcy Code (notably section 363) that apply to a transfer of an interest of a debtor in property within the US
11. It is to be noted that they could also have proceeded under 28 U.S.C. 1782 which provides for discovery in aid of foreign proceedings
12. The concept of adequate protection in Article 21 of the Model Law and 'sufficient protection' in section 1521 of the US Bankruptcy Code sanction this.



IAN WILLIAMS is a partner, SGH Martineau LLP and a director of the American Bankruptcy Institute.

PROFESSOR ADRIAN WALTERS is a Ralph L. Brill Professor of Law at the Chicago-Kent College of Law and visiting professor at the Centre for Business and Insolvency Law, Nottingham Law School.

Tackling IPs' pensions auto-enrolment duties

David Pollard, **Harriet Sayer** and **Katharina Crinson** highlight the key issues to consider when seeking to comply with the auto-enrolment regime.

Under the Pensions Act 2008, employers are required automatically to enrol employees and workers into the central National Employment Savings Trust (NEST) or another qualifying scheme and, if a defined contribution (DC) arrangement is used, to make contributions on behalf of the members. This is being phased in from 2012 to 2018, depending on the number of employees. Insolvency practitioners need to check that companies going through an insolvency process fulfil their auto-enrolment duties.

The duty to enrol may have arisen before the company enters into a process, or may arise later, depending upon the employer's staging date.

If employees are enrolled on a DC basis and continue to be employed during the insolvency process, companies will be required to make regular payments into the scheme. These payments may have super-priority in the insolvency.

The penalties on employers for failing to comply with auto-enrolment legislation are serious, ranging from fines to criminal conviction. These penalties could apply to IPs managing insolvent companies.

How does the auto-enrolment regime affect IPs?

Between 1 October 2012 and early 2018, all UK employers will be required to start automatically enrolling most employees (and jobholders and workers) in the central NEST or another qualifying pension scheme. This could pose several issues for IPs:

1. **Timing:** The insolvent company may have ignored that its staging date (the date from which it is required to comply with the auto-enrolment requirements) has occurred, or may not know when it will occur.

> "The penalties for failing to comply are serious and could apply to IPs managing insolvent companies."

2. **Data:** The insolvent company may not have assessed its workforce to check who needs to be enrolled and what the value of their qualifying earnings is (the amount on which the value of the pension contributions payable is based).
3. **Access to qualifying scheme:** The insolvent company may not have existing pension arrangements in place that meet the standards set by auto-enrolment legislation. In this situation, the IP may need to make arrangements for employees to join NEST or another qualifying arrangement (such as a personal pension).
4. **Communication:** The insolvent company may not have provided the necessary information to the trustees/managers of its auto-enrolment scheme or its workforce regarding their auto-enrolment rights.
5. **Breach:** Through a combination of these factors, the insolvent company may be in breach of, or about to breach, its auto-enrolment duties. The IP may be held liable for any ongoing breach.

Who must be enrolled?

Pensions legislation requires employers to enrol any jobholder who meets the following criteria in a qualifying pension scheme:

- being aged between 22 and the state pension age (currently 65 but due to rise for most employees); and
- having earnings greater than the earnings trigger of £9,440 a year for tax year 2013/14 (ie the Pay As You Earn (PAYE) threshold). The Department for Work and Pensions has announced that the threshold for the 2014/2015 tax year is expected to be £10,000.

Jobholders are not just employees. The term includes anyone who has entered into an employment contract or any other contract with the company under which he or she agrees to perform services for the company, unless the company is a client or customer under the contract.

»

Opting in and opting out

Jobholders who are aged between 16 and 22, or between state pension age and 75, may elect to require the company to enrol them in a qualifying scheme. This is known as opting in.

Conversely, before or after having been automatically enrolled in a pension scheme, employees or workers may choose to stop participating in the scheme. This is known as opting out. If employees choose to opt out, the company must automatically

> "Jobholders are not just employees."

re-enrol them in a scheme once within the next three years (and each three years thereafter).

Staging dates

Employers will need to auto-enrol eligible jobholders from the employer's staging date. This depends on their size (which is assessed by the number of employees the employer had on its PAYE records on 1 April 2012). The Pensions Regulator (TPR) will twice notify employers in advance – 12 months and three months before the staging date.

An IP's need to consider a company's obligations under the auto-enrolment legislation will arise in two circumstances:

- from the insolvent company's staging date (if the company's staging date has not already occurred at the insolvency date), or
- as soon as the company enters the insolvency process (if that company's staging date has already occurred).

If employment continues after the insolvency starts, the insolvent company will usually continue to be the employer for auto-enrolment purposes, while the position of the IP is similar to that of a director. On appointment, the IP should therefore check whether a company's staging date has occurred, or when it is due to occur.

Postponement

In certain circumstances employers can choose to postpone auto-enrolment for some or all of their workers for up to three months, if they issue the relevant workers with a notice setting out prescribed information. This flexibility is intended to assist employers where they wish to align auto-enrolment with the employer's existing payroll processes.

However, it requires forward planning on the part of the employer, who will need to select its deferral date (broadly speaking, the last date of the postponement period, up to three months after the date employees would otherwise need to be enrolled) and issue a valid notice to employees one month following the day after the date from which the employer wishes to use postponement. This could limit its usefulness to IPs, if the insolvent company is not able to issue such notice in time.

What types of pension scheme can be used?

The company can choose whether the contributions are made to NEST or another pension scheme that meets the statutory requirements for a qualifying scheme.

NEST is a central DC scheme established by legislation aimed at low to moderate income jobholders. An employer may prefer to use its own existing occupational pension scheme (OPS) or a nominated personal pension (PP), in which case it will need to certify that such scheme is a qualifying scheme. Qualifying schemes can take the form of defined benefit (DB) schemes, DC schemes, or hybrid schemes (schemes that pay out both DC and DB benefits).

The company's auto-enrolment duties during an insolvency process will vary depending on whether the scheme is a DB scheme or a DC scheme, as explained in Table 1.

DB and hybrid occupational pension schemes

In general, where a company has complied with its auto-enrolment requirements using an existing DB (or hybrid) OPS, the scheme is likely to enter a Pension Protection Fund (PPF) assessment period on the employer insolvency starting, thereby freezing accrual of benefits under the scheme. This means that it will not, under the auto-enrolment legislation, have to continue to provide benefits to employees under the scheme for service after the insolvency process starts.

Schemes outside the PPF

The position of members of NEST, a personal pension or a solely DC OPS is different. For these schemes, no PPF

> "The company's auto-enrolment duties during an insolvency process will vary depending on the scheme."

assessment period comes into effect on employer insolvency, and so the Pensions Act 2004 does not prevent contributions continuing to be made. Similarly, the auto-enrolment duty will continue.

DC: super priority

The Pensions Act 2008 makes it clear that a jobholder does not have any right under the legislation to bring a claim against his or her employer for breach of statutory duty if the employer breaches one of its auto-enrolment duties. However, contracts of employment and announcements would need to be checked to see if a separate contractual right has arisen.

In practice, the contributions an IP pays to a DC scheme are likely to rank as an insolvency expense.

Arguably, these contributions (if contractual) could also be within the ambit of pay given super priority for adopted employment contracts in an administration or a receivership. Generally, the super priority only applies to sums arising out of, or under, a contract. Sums paid just to meet statutory requirements, such as the auto-enrolment requirements, probably do not qualify.

Contribution rates for defined contribution schemes

If the company chooses a DC arrangement (such as NEST), then once the company has enrolled the jobholders, it will need to pay contributions to that arrangement based on their qualifying earnings (being between £5,668 and £41,450 for the 2013/14 tax year, and expected to be between £5,772 and £41,865 for the 2014/15 tax year).

TABLE 1

Type of scheme	DC benefits?	DB benefits?	Potential for PPF entry? (so ongoing AE duty may end on the start of an insolvency process)
DB – OPS	No	Yes	Yes
Hybrid – DB and DC – OPS	Yes	Yes	Yes
DC – OPS	Yes	No	No
PP	Yes	No	No
NEST	Yes	No	No

TABLE 2

Transitional period	Minimum contribution of qualifying earnings (per cent)		
	Employer	Employer or deduction from Employee	Total
1 (Years 1–4)	1	1	2
2 (Year 5)	2	3	5
Steady state (Year 6+)	3	5	8

Contribution rates for DC schemes will be phased in over two transitional periods running over five years in total (see Table 2).

How are auto-enrolment obligations enforced?

Penalty notices

Pensions legislation prohibits conduct that will encourage employees to opt out of a pension scheme – for instance, suggesting to proposed candidates that opting out will be considered favourably or offering inducements to opt out. TPR is responsible for enforcing employers' automatic enrolment obligations and compliance

> "TPR has powers to issue compliance notices and fixed-penalty notices of up to £50,000."

with this prohibition. It has powers to issue compliance notices and, in more serious instances, fixed-penalty notices of up to £50,000 and escalating-penalty notices with an escalating daily penalty rate of up to £10,000. These can be issued against the employer (here the insolvent company) or a third party (where the employer failure is wholly or partly the result of a failure by the third party). An IP at fault is likely to be such a third party.

Following recent case law, it is however likely that such a notice against the company (but not a third party) will be caught by the moratorium on legal process against the company following the start of a liquidation or administration (*Hudson* v. *Gambling Commission* [2010] EWHC 1229 (Ch)). Note that the moratorium is subject to the IP or court giving consent to the process going ahead.

It is possible that such a penalty claim against the company could (if based on a notice given after the insolvency process starts) amount to an insolvency expense and so rank ahead of unsecured creditors and indeed the officeholder's own remuneration. Where a compliance notice is issued after the start of the insolvency but relating to non-compliance prior to insolvency, the compliance notice will rank as a provable debt following the recent Supreme Court decision *Re Nortel* [2013] UKSC 52. Where the non-compliance is due to the office-holder's own default, it is more likely to rank as an expense of the insolvency.

Third party compliance notices

TPR also has power to issue third party compliance notices . It can issue these if:

- an employer has breached one of its duties wholly or partly through a failure by a third party, and
- that failure is not itself a breach of an employer's duty.

It is conceivable that TPR could serve a third-party compliance notice on an officer (or IP) who has failed to ensure that the company complies with its auto-enrolment duties. The notice must specify a time-period carrying out an action. If the officer does not comply with the notice, TPR can issue a fixed-penalty notice.

Criminal offences

An employer will be guilty of a criminal offence if it wilfully fails to do any of the following:

- automatically enrol jobholders who satisfy the criteria for auto-enrolment;
- re-enrol opted out jobholders automatically once within every three years; or
- fails to allow jobholders to opt in to automatic enrolment.

Conviction for any of these offences carries a fine or a maximum sentence of two years' imprisonment. Directors, officers or managers at an employer can also be guilty of an offence if they consented to or connived in any of these offences, or if any of them was caused by their neglect (s46 PA 2008).

As with penalty notices above, criminal and penalty proceedings against the company for auto-enrolment-related offences are likely to be caught by the moratorium on legal proceedings following the start of a liquidation or administration.

> "It is likely that IPs are treated as managers and so officers of the company…"

It is likely that IPs are treated as managers and so officers of the company and can therefore be found guilty of this offence if caused by their consent, connivance or neglect (the moratorium would not apply to a case against an officer or an IP).

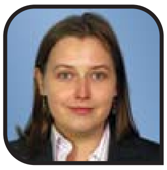
Compliance in insolvency

Breach of auto-enrolment legislation can be divided into three periods:

1. **Past breaches:** Breaches of auto-enrolment requirements relating to a period of employment prior to the appointment of the IP. The insolvent company and its officers (but probably not the IP) may face criminal charges, and the insolvent company may be made subject to a penalty notice.
2. **Breaches occurring during the adoption window:** Breaches of auto-enrolment requirements arising in respect of ongoing employment during the 14-day adoption window following administration.
3. **Breaches occurring after the adoption window:** Breaches of auto-enrolment requirements arising during the course of an administration or a voluntary liquidation or receivership in respect of contracts of employment that have been adopted by the IP that are likely to rank as an expense of the insolvency.

The IP will want to ensure that the company complies with its auto-enrolment duties for periods of service after the start of the insolvency process. However, this may not be feasible, particularly during the 14-day adoption window, if the insolvent company has not made the necessary arrangements already. The insolvent company may receive a compliance or penalty notice relating to this 14-day period.

DAVID POLLARD is a partner at Freshfields Bruckhaus Deringer LLP.



HARRIET SAYER is an associate at Freshfields Bruckhaus Deringer LLP.

KATHARINA CRINSON is a knowledge management lawyer at Freshfields Bruckhaus Deringer LLP.

The proprietary claim minefield

Bree Taylor explains the potential for problems if a third party claims to own some of an insolvent company's assets and offers tips to avoid liability for conversion.

Insolvency practitioners are often heard to say that one of the worst parts of the job is dealing with claims by parties alleging they have proprietary rights to assets in the possession of the company. The law is a minefield and there seem to be different views in practice as to the extent to which office-holders are protected from claims against them personally by s234 of the Insolvency Act 1986 (the Act).

> "Administrators have no right to dispose of assets belonging to third parties and must get permission."

One of the most common scenarios is as follows:

- Administrator is appointed.
- Administrator negotiates sale of company's assets.
- Administrator receives letter from person claiming to own some of the assets included in the proposed sale – commonly but not necessarily stock.
- Administrator then receives threats of legal action including claim for conversion if he/she does not allow the alleged owner to take back goods.

What are the danger areas for the office-holder? First points to bear in mind include:

1. Administrators have no right to dispose of assets belonging to third parties and must get permission under paragraphs 71 or 72 of Schedule B1 to the Act. In the case of ROT goods, the administrator will need to satisfy the court that the sale of ROT goods would promote the interests of the administration. Even where permission is granted, this does not override the owner's rights. Any proceeds of sale must be remitted to the owner.
2. Administrators are personally liable for torts they commit while in office. Conversion is a tort. This is *'an act of deliberately dealing with a chattel in a manner inconsistent with another's right whereby that other is deprived of the use and possession of it'* (Clerk & Lindsell on Torts, 20th edition at paragraph 17-07). Conversion of goods can occur by selling them to someone else or by wrongfully refusing the owner access to them.
3. The oft-cited s234 defence applies only to chattels (not choses in action such as book debts) and provides no defence where the office-holder has caused loss by acting negligently.

Before looking to guidance from recent cases, there is a distinction to be made between recognising a party's proprietary rights to goods and allowing the party to enforce those rights in an administration. Retention of title (ROT) claims fall within the moratorium provisions at s43(3) of Schedule B1 to the Insolvency Act 1986. Accordingly, an owner with a valid ROT claim will need the consent of the administrators or the permission of the court to enforce proprietary rights over ROT goods. For guidance on the principles applied when an owner seeks to enforce its rights against goods and the balancing exercise in relation to the owner's interests versus the company's interests, see *Re Atlantic Computer Systems Limited* [1992] Ch 505.

> "As a rule of thumb, if the company has not seen the terms at the time of agreeing to buy the goods, then the terms are probably not part of the contract."

What does an owner of goods need to establish to assert a claim to goods supplied under a retention of title contract (ROT goods)?

- The terms of the contract including the ROT clause relied upon. Does the clause form part of the contract? Has it been seen and agreed by the company or is it deemed legally to have been accepted by the course of dealing between the parties? An example of where the owner might have difficulty is where the ROT clause appears only in 'standard' terms and conditions printed on the reverse of invoices or on the supplier's website. As a rule of thumb, if the company has not seen the terms at the time of agreeing to buy the goods, then the terms are probably not part of the contract.
- That the ROT clause prevents the goods being on-sold by the company (or by the office-holder as agent for the company) or gives the owner some right to repossession. Some ROT clauses envisage the goods being on-sold in the ordinary course of business but provide that on certain events, the company's right to possession of goods may be terminated by the owner. Whether the office-holder may sell goods in this case depends on what exactly the clause says and whether the owner has in fact exercised contractual rights. For a recent example see *Sandhu* v. *Jet Star Retail Limited* [2011] EWCA Civ 459 where the ROT clause entitled the owner to terminate the company's right to possession on the happening of insolvency events. The administrators sold goods as part of a trading administration and then sold the business as a going concern to a third party. Despite sending letters via solicitors making various demands of the administrators for the value of the ROT goods (understanding the goods to have been sold), at no time did the owner actually terminate the company's right to possession under the relevant clause. Thus the administrators were therefore entitled to have dealt with the goods in the way they did.
- The identity of the specific goods to which the ROT clause relates. This is often one of the most difficult hurdles for the owners of goods, particularly where the goods are the sort of stock items that could have been supplied by more than one supplier, for example, books for supply to a book retailer. Notwithstanding the owner's difficulty in identifying the goods, office-holders do need to take care in cases where they are planning to sell the goods to the public. For an example of how administrators were found to have likely committed the tort of conversion of goods when running a trading administration of Borders book stores, see *Hachette UK Limited* v. *Borders UK Limited and others* [2009] EWHC 3487 (Ch).

> "Notwithstanding the owner's difficulty in identifying the goods, office-holders do need to take care in cases where they are planning to sell the goods to the public."

Top tips for avoiding liability for conversion

Exclude ROT goods from a business sale

It is possible for an office-holder to sell the business of a company without selling any ROT goods, even where the office-holder cannot specifically identify ROT goods. It has become common practice for administrators' sale agreements to contain clauses providing that any property to which an ROT claim is asserted is not included within the sale, notwithstanding that in practice, possession of the goods (although not ownership) may be transferred to the buyer. This option is not available for administrators selling goods to the public as part of a trading administration because in 'ordinary' sales of goods, it is clear that the seller is purporting to transfer ownership to the buyer.

Give owners a reasonable chance to identify their goods

Where an owner of goods asserts an ROT claim against goods, the onus is on that person to establish the claim including, most importantly, identifying the specific items to which he/she claims to have title. This is no easy feat, particularly where the goods are in the possession of the administrator (or sometimes in the possession of some third party at a warehouse or department store). It is common practice for office-holders to give owners an opportunity to attend the relevant site by appointment to see whether specific goods can be identified as his/her property. But in the scenario where office-holders have negotiated and are poised to complete a business sale by the time the claim letter arrives, this is often not practicable and in practice not done. This is where a well drafted clause transferring only such right title or interest as the company may have could save the office-holder from personal liability for conversion (see point above).

Apply to court under para 72 of Schedule B1

Mr Justice Sales was extremely critical of the administrators of Borders for carrying on with a trading administration without making any application under paragraph 72. The lesson is that faced with ROT claims, even if it is difficult or impossible to identify the goods that belong to a particular owner, make an application to court early with a proposal already worked out as to how to safeguard the owner's interests.

Get information from directors and employees – pay attention and take good notes

Not only will directors and employees be best placed to identify any goods or other property that might belong to third parties but the statements they make to you early on (and possibly even pre-appointment) could provide invaluable evidence in defence of any claim against you subsequently. It is therefore important to keep good records of what you are told whether formally or informally.

In the recent case of *Euromex Ventures Limited* v. *O'Connell and MacDonald* [2013] EWHC 3007 (Ch), various parties, including a Mr Bhabra, brought claims in conversion against the administrators following the administrators' sale of company assets including items alleged to have belonged to Mr Bhabra, members of his family and others. The administrators were vindicated in their actions in selling the property, because, among other reasons, they had taken and relied upon statements made by Mr Bhabra as to the ownership of the goods, and recorded the statements in a contemporaneous filenote. Later, when Mr Bhabra alleged that he and others owned that same property, Mr Justice Newey declined to accept this evidence. The administrators were found not have committed conversion and had a defence in any event under s234.

> "Have you weighed up the various interests fairly?"

Consider what the owner is demanding

Is the owner seeking consent to enforce an ROT clause within the terms of s43(3)? If so, what are the reasons for giving consent or not giving consent as the case may be. Are they justifiable reasons and have you weighed up the various interests fairly? Alternatively, is the owner merely asking you to set aside and protect goods to which it has a claim? It is important to look carefully at what rights are being asserted before responding. If it is unclear what you are being asked to do, clarify at an early opportunity and ask for any information you may need in support of the owner's claim. ◻

BREE TAYLOR is a partner at Memery Crystal LLP.

The use of English schemes of arrangement by foreign companies

Radford Goodman and **Helen Fairhead** look at an increasingly popular debt restructuring tool.

In recent years, a number of English schemes of arrangement have been sanctioned in respect of foreign companies – Primacom, Rodenstock, Telecolumbus, Metrovacesca, Vietnam Shipbuilding Industry Group (Vinashin) and Magyar Telecom, by way of some prominent examples. Companies using English schemes have come both from within the EU and outside, including Kuwait, Vietnam, Indonesia and the US. While it is recognised that English schemes can be cumbersome and costly, they have become increasingly popular as a debt restructuring tool, due principally to the following factors:

- schemes offer flexibility and certainty. The procedure is well-established and the terms of the scheme are reviewed and sanctioned by the court;
- it is possible to 'cram down' secured, as well as unsecured, creditors;
- schemes are not seen as an 'insolvency' procedure (even though they are used to restructure the debts of insolvent companies);
- many international financings are governed by English law and subject to the jurisdiction of the English courts; and
- the home jurisdiction of the company may not offer an equivalent or effective way to bind dissenting creditors.

In a series of recent decisions, the English courts have confirmed their jurisdiction to sanction schemes relating to foreign companies and continued to develop a coherent set of principles to govern the exercise of their discretion.

Jurisdiction

The jurisdiction of the English court to sanction a scheme in respect of a foreign company derives from the Companies Act definition of 'company', which includes 'any company liable to be wound up under the Insolvency Act 1986'. The Insolvency Act provides that the court can wind up any 'unregistered company' – which term includes foreign companies[1] – if:

(i) the company is dissolved, has ceased to carry on business, or is carrying on business only for the purpose of winding up its affairs;
(ii) the company is unable to pay its debts; or
(iii) the court is of the opinion that it is just and equitable that the company should be wound up[2].

There has been some debate as to whether a foreign company could be said to be 'liable to be wound up under the Insolvency Act' if it does not satisfy the criteria necessary for a court to exercise its discretion to make a winding-up order in respect of a foreign company – namely that: (i) the company has a sufficient connection with England and Wales; (ii) there is a reasonable possibility of benefit to creditors from the making of the winding-up order; and (iii) one or more persons interested in the distribution of assets are persons over whom the court can exercise jurisdiction[3].

> "Before the court will exercise its jurisdiction... it will need to be satisfied the company has a sufficient connection with England and Wales."

In *Re Drax Holdings*[4] it was held that these conditions go to discretion rather than jurisdiction and it is now clear that the English court does have jurisdiction to sanction a scheme in respect of a foreign company even if these conditions are not met. In *Magyar Telecom*[5], David Richards J confirmed that: *'The only jurisdictional requirement for a "company" is that it should be liable to be wound up under the Insolvency Act 1986… A foreign-incorporated company is so liable, even if its circumstances at the time of the application to the court are such that the English court would not at that time exercise its jurisdiction to wind up the company…'*

There has also been some debate as to whether the EC Regulation on Insolvency Proceedings[6] (the EIR), which has curtailed the jurisdiction of the English courts to wind up a company which has its COMI in another EU Member State[7], should, by extension, be taken to have restricted the jurisdiction of the English courts to sanction a scheme in respect of such a company. In cases such as *Re DAP Holding NV*[8] and *Re Rodenstock*[9], the English courts have held that the EIR was not intended to restrict their jurisdiction in relation to schemes[10]. In *Re Rodenstock*, Briggs J said: *'Given that neither of the two Regulations*[11] *appear on their face to have been directed at restricting the English court's international jurisdiction in relation to solvent schemes, and given that all company law consolidation since either of them was introduced as part of English law has re-enacted the "liable to be wound up" touchstone for jurisdiction in an unaltered form, it seems to me improbable on a purposive interpretation of those Regulations as part of English law that any such narrowing of the English court's jurisdiction was intended.'* This reasoning has been approved in the context of an insolvent schemes[12].

Discretion

Before the court will exercise its jurisdiction to sanction a scheme in respect of a foreign company, it will need to be satisfied that (i) the company has a *sufficient connection* with England and Wales and (ii) the scheme will be effective. The first condition is intended to ensure that the court does not exercise exorbitant jurisdiction and the second derives from the principle that the court will generally not make an order which has no substantial effect[13].

Many factors can contribute to a finding of *sufficient connection*, including the presence of assets, business interests or creditors within the jurisdiction, but crucially, in the context of schemes which are being promulgated in England because the finance documents affected by the scheme are governed by English law, it is now established that this alone can be enough to satisfy the test[14]. For example, in *Vinashin*[15], the company had no connection with England other than the fact that its loan facilities (which were the subject of a restructuring pursuant to the scheme) were governed by English law and subject to the non-exclusive jurisdiction of the English courts. David Richards J stated that: *'For good measure the non-exclusive jurisdiction clause also creates, in my judgment, a sufficient connection with the jurisdiction, but I take the view that the fact that the loan agreement is governed by English law is of itself sufficient to create that necessary connection.'*

The sufficient connection test may be more difficult to satisfy where creditors' claims are not governed by English law or subject to the jurisdiction of the English courts, as was the case in *Magyar Telecom*, where the company was incorporated in the Netherlands and the claims of the relevant creditors were governed by New York law and subject to the jurisdiction of the New York courts. In that case, a

Editor recovery@r3.org.uk | Recruitment recovery@r3.org.uk/recruitment

sufficient connection existed because the company had moved its COMI to England prior to promulgating the scheme.

In order to satisfy the second condition – effectiveness – expert evidence is usually deployed to demonstrate that the scheme will be recognised in those jurisdictions where it will need to be effective. This is likely to be easier in cases where the scheme creditors' claims are governed by English law because, as was observed by David Richards J in *Magyar Telecom: 'under generally accepted principles of private international law, a variation or discharge of contractual rights in accordance with the governing law of the contract will usually be given effect in other countries*[16]*'*. In *Magyar* itself, where the scheme creditors' claims were governed by New York law, sanction was achieved on the basis of expert evidence on US law which showed that it was reasonably likely that the scheme would be recognised by the US courts under Chapter 15 of the US Bankruptcy Code.

Interaction with European law

Two European Regulations are relevant. The first is the EIR and the second is the Regulation on Jurisdiction and the Recognition and Enforcement of Judgments in Civil and Commercial Matters[17] (the Judgments Regulation).

English schemes are clearly not within the scope of the EIR (at least, in its present form, and to the extent that the scheme is not promulgated in connection with insolvency proceedings that come within the scope of the EIR). There are conflicting authorities as to whether English schemes are within the scope of the Judgments Regulation, but in recent cases the prevailing view of the English courts has been that they are[18]. The Judgments Regulation applies to *'civil and commercial matters'* but *'bankruptcy, proceedings relating to the winding up of insolvent companies or other legal persons, judicial arrangements, compositions and analogous proceedings'* are excluded from its scope. On the basis that the two Regulations are designed to dovetail, it has been held that this exclusion should not be interpreted so as to encompass schemes. *'In other words, an order sanctioning a scheme between an insolvent company and creditors is subject to the Judgments Regulation, at least if the company is not subject to insolvency proceedings to which the [EIR] applies*[19]*.'*

Coming within the Judgments Regulation is a double-edged sword for English schemes. On one hand, it follows that, as far as the English courts are concerned[20], a scheme sanctioned in England should be recognised and enforced throughout the EU in accordance with Chapter III of the Judgments Regulation. This may be helpful in terms of fulfilling the second condition described above.

On the other hand, Article 2 of the Judgments Regulation provides that a person domiciled in a Member State should be *'sued'* in the courts of that Member State, unless one of several exceptions applies. Dissenting creditors domiciled in a Member State other than the UK may argue that the English courts do not have jurisdiction to sanction a scheme which purports to bind them. In practice, such an argument seems unlikely to succeed before the English courts, which have expressed doubts as to whether Article 2 can properly be said to apply to schemes and, even if it does, have in every case found that one of the exceptions applies – for example, the creditors were largely based in England (Article 6), the facility agreements provided for the jurisdiction of the English courts (Article 23) and/or the majority of creditors submitted to the jurisdiction of the English courts (Article 24)[21].

The future

Thus far, jurisdictional objections raised by dissenting creditors have largely been unsuccessful before the English courts and, in the process of resolving these disputes, the principles in respect of applications by foreign companies have evolved. These principles will continue to develop as more schemes, each with unique circumstances, come before the courts and questions which presently remain undecided (such as the applicability of Article 2 of the Judgments Regulation) are resolved.

> "English schemes are clearly not within the scope of the EIR – at least, in its present form..."

We expect foreign companies to continue to use English schemes as a restructuring tool for the foreseeable future, although there are challenges on the horizon. First, as described above, English courts will not sanction schemes if they are not satisfied that the scheme will be recognised in relevant jurisdictions. This may become more difficult to establish if foreign courts begin to refuse to recognise schemes in practice or the European Court of Justice rules adversely to recognition on some of the issues discussed in this article. Secondly, changes to European insolvency legislation may, at some stage, fundamentally change the market although, at present, proposals to include schemes within the EIR, which would have curtailed the jurisdiction of the English courts to sanction schemes in respect of foreign companies, appear to have been dropped. Thirdly, significant European jurisdictions have begun to implement their own pre-insolvency cram down procedures. It remains to be seen whether these will prove effective enough to replace English schemes for companies based in those jurisdictions.

1 Section 220(1) Insolvency Act 1986.
2 Section 221(5) Insolvency Act 1986.
3 *Real Estate Development Co* [1991] BCLC 210; *Stocznia Gdanska SA* v. *Latreefers Inc* (No 2) [2000] EWCA Civ 36.
4 [2004] 1 WLR 1049.
5 [2013] EWHC 3800.
6 Council Regulation (EC) No 1346/2000.
7 Article 3(2) EIR.
8 [2005] EWHC 2092.
9 [2011] EWHC 1104.
10 Note that the Insolvency Lawyers' Association has commented that this is an issue that would benefit from a detailed and reasoned judgment from a higher English court, as these first instance decisions were based on different reasoning and were not contested.
11 A reference to the EIR and the Judgments Regulation, as defined below.
12 see *Re Primacom* [2012] EWHC 164, at paragraph 61.
13 In *Magyar Telecom*, David Richards J pointed out that these two requirements may properly be understood as being aspects of the same question, or at least closely related.
14 *Re Primacom* [2012] EWHC 164; *Re Vietnam Shipbuilding Industry Groups* [2013] EWHC 2476.
15 [2013] EWHC 2476.
16 See also Article 12 of Council Regulation No. 593/2008 (Rome 1).
17 Council Regulation (EC) 44/2001.
18 *Re Rodenstock* [2011] EWHC 1104; *Re Magyar Telecom* [2013] EWHC 3800. Conflicting earlier authorities are *Re DAP Holding NV* [2005] EWHC 2092 and *Re La Mutuelles du Mans Assurances IARD* [2005] EWHC 1599. This is ultimately a question for the European Court of Justice.
19 Per David Richards J in *Re Magyar Telecom* [2013] EWHC 3800.
20 *Re Magyar Telecom* [2013] EWHC 3800. Courts in other Member States may take a different view. For example, in 2009 the German Regional Appeal Court held that an order sanctioning a scheme should not be regarded as a 'judgment' for the purposes of Chapter III of the Judgments Regulation.
21 In *Re Primacom*, Hildyard J favoured the view that Article 2 did not apply to schemes, which do not obviously involve anyone being 'sued' as a defendant in the traditional sense. In *Rodenstock*, Briggs J described this issue as a conundrum and in *Vinashin* and *Magyar Telecom*, David Richards J treated it as open question which did not require determination on the particular facts.

RADFORD GOODMAN is a partner in the business restructuring and insolvency group at Norton Rose Fulbright LLP.

HELEN FAIRHEAD is an associate in the business restructuring and insolvency group at Norton Rose Fulbright LLP.

It's not who you know – it's who knows you

The importance of networking and how R3 can help.

Someone once told me that people do business with those they like and trust but for a junior solicitor in the world of insolvency, where do you find such individuals?

With over 3,000 members, R3 represents over 97 per cent of all insolvency practitioners and the majority of lawyers, accountants and bankers in the profession – a good starting point for building your network. R3 does not only provide technical training and a forum for debate, but more importantly allows us the opportunity to meet fellow professionals. As networking is the most powerful marketing tool to achieve success, we should be jumping at the chance to attend the many R3 events that are organised throughout the year.

Get stuck in

When I left Birmingham in 2010 to move to Farrer & Co I did not know a single soul in the London legal market; that is until I discovered the R3 London and South East Women's Group. As the only female member of the insolvency team at Farrers, I was faced with the daunting task of attending an R3 event alone. Understandably, most people hate attending events by themselves, standing in the corner of a room watching as other guests move confidently from person to person as if they have all known each other for years. As intimidating as it was, I bit the bullet and got stuck in. To my delight, I discovered that all those in attendance were incredibly warm and welcoming. It did not take long before I had received a pile of business cards from juniors and partners alike, it being much easier to approach those in positions of seniority in a social setting than it would be at a conference or other formal event.

Truth be told, many of those who attend R3 events have known one another for years, but only because they have taken the time and effort getting to know their peers and, more importantly, keeping in touch throughout their careers.

From personal experience, there is nothing better than face-to-face networking events to raise one's profile. From the 'Bring and Buy' to the 'Hobbs Night' to 'Strictly Come Dancing' – I have attended them all, and soon I found the room was no longer full of unfamiliar faces; I was able to walk up to a group of ladies with the confidence of knowing at least one member of the group from a previous event. By year three, I was a 'Witch' on the organising committee of the infamous R3 Ladies' Lunch, following which, I was invited to join the R3 London and South East Women's Committee.

Ultimately, your career lies in your own hands. Even if you work for the most recognised insolvency firm in the country, it's not about who you are or even who you know, but who knows you! R3 sub-committees across the regions organise numerous events to encourage those within the profession (whether R3 members or not) to network. In an economic environment where firms have been forced to reduce marketing budgets and we work longer hours, simply wanting to rush home at the end of a long day, we must not forget the importance of getting out there and building a rapport with your peers who may one day be your clients. Building such a strong contact base will only serve you in the years to come – it certainly helped me when I was faced with a partner on the other side of a deal who recognised me from an R3 event.

> "Ultimately, your career lies in your own hands."

Future events

The R3 London and South East Women's Group have many exciting events lined up for those who wish to take advantage of the wonderful networking opportunities provided. As we go to press the committee is hosting a networking event at the offices of Farrer & Co where ladies are invited to network over a glass of wine.

For those who fancy something more glamorous, the committee is inviting women to the real ladies lunch with 'Lunch at The Langham' on 3 July 2014. Lunch at The Langham promises to be an exciting event with motivational speaker and comedienne Deborah Frances-White providing the entertainment and unlike the Ladies' Lunch at the Victoria Plaza, this truly will be a 'no Y chromosomes allowed' event.

A lot of hard work goes into organising these events, without which there would be no need for sub-committees. Gone will be the days of networking other than marketing to your client base. R3 provides us with the opportunity of widening our contact base and building relationships that will serve us as professionals throughout our careers. The opportunity is out there for the younger generation – we just need to grab it!

NYLA YOUSUF is an associate at Farrer & Co.

IP v. KPI – how do you know if you are a winner?

R3 SPG Committee member **Jeanette Brown** considers the importance and relevance of key performance indicators (KPIs) to those practising in smaller firms and suggests ways to get useful benchmarking information for your practice from R3.

The R3 SPG Committee may just have come up with the answer to the question *'where to get KPI information'* in the form of its recently redesigned membership benchmarking survey. It is hoped that, without a great deal of time input, the carefully formulated questions will help smaller firm members identify and compare key aspects of their performance from the survey results and practitioners can be reassured that all submissions will be kept in complete confidence by R3. The survey will be released later in 2014 and the members of your SPG Committee very much hope that you will be willing to take part, to the benefit of the whole smaller firm community.

So, with the benchmarking survey in mind, what are our KPIs and how can they be used effectively in practice management?

I was recently asked to present a seminar to first year business students at a local university entitled 'Managing performance in the real world'. Like much of my business life I found my audience divided into three distinct groups; the first group were attentive and engaging; the next group were tapping their electronic devices and the third group were simply not listening/asleep. What startled the latter two-thirds into paying attention, was when I told them about a piece of business advice that I received from an old Cumbrian farmer many years ago. Sadly through the medium of print I cannot convey the dialect of my region, but his words were, 'It's not turnover, lass, – it's left over'. I think this was my first lesson in assessing a KPI, albeit a very basic one of assessing whether or not the business had made any profit!

In my down time as an insolvency practitioner, I advise many professional practices on maintaining – and monitoring – their profitability, as well as being my own firm's 'in-house accountant'. I am therefore well used to producing and interpreting KPIs and if I could pick my top five KPIs for an insolvency practice (in no particular order) I would say the following:

1. Chargeability – ie the number of billable hours charged by each staff member as a percentage of their total time;
2. Recoverability – the amount billed in comparison to the time charged to the case;
3. Amount billed against a monthly billing target – billing targets should be set for each fee earner/department;
4. Age of work in progress (WIP) held at the end of each month – an analysis of the percentage split of time charged between 30/60/90 days and so on;
5. Staff costs as a percentage of turnover.

So why do I think these numbers are so important? Surely if the monthly management accounts show a profit, then the practice must be running effectively? Well not always, as in my experience, a reported profit can often hide a multitude of sins. It's only when you drill down into the figures that you really get an understanding of what drives the business – or holds it back.

> "It's only when you drill down into the figures that you really get an understanding of what drives the business – or holds it back."

Examining the examples above can illustrate any number of different scenarios. For example, a reduction in chargeable hours can mean that you've simply not got enough cases, or that staff aren't recording their time accurately. Recoverability problems mean there's not enough money in the pot to pay the fees and you are perhaps taking on the wrong type of cases. KPIs 3 and 4 tend to be interlinked. If billing doesn't happen, the time stays in WIP. The consequences of this are twofold – firstly, if you don't bill then the cash flow dries up and you can't pay the practice's running costs. The build-up of 'old' WIP over a lengthy period can lead to billing problems and ultimate write offs. Over-valuing work in progress leads to overstated profits, which in turn can lead to a nasty shock when it's ultimately written off. And finally if you're paying your staff more than your turnover, then there won't be any money 'left over' for the business owner (this could be you!).

I mentioned earlier that we review our KPIs on a monthly basis, but our targets are set from the perspective of an established business. We've been around long enough to understand our own market, and more crucially, the market around us. But what happens if you're on your own, perhaps in a new business with no established trends and no knowledge of whether your practice is over- or under- performing?

Talking to colleagues in similarly sized practices obviously helps. You can, of course, also make sure you appoint an accountant who specialises in professional practices and can give you this information as part of their annual accounts service, but without wanting to do the accountancy profession out of a job, perhaps in the early years of operation this extra expense may not be top of your 'shopping list'. This is, hopefully, where the R3 benchmarking survey can assist.

JEANETTE BROWN is a partner at Dodd & Co and a member of R3's SPG Committee.

SAVE THE DATE

18 September 2014
R3 Insolvency Conference
Crowne Plaza, Chester

16–17 October 2014
SPG Forum
Hilton Metropole, Birmingham

R3 events, courses and conferences

Month	Date	Event	Venue
March	4	Webinar – Insolvency Procedures in Jersey	Online
March	4	Yorkshire LinkedIn Seminar	Deloitte LLP, Leeds
March	5	Midlands Wine Tasting Event	Loki Wines, Birmingham
March	6	CVAs	Emirates Stadium, London
March	6	Football Finance	Emirates Stadium, London
March	6	London Football Networking Drinks	Emirates Stadium, London
March	7	East Midlands Excuse me Lunch	Trent Bridge Cricket Ground, Nottingham
March	13	Restructuring Solicitors' Firms in Financial Distress	The Met, Leeds
March	13	Pre-pack Administrations	The Met, Leeds
March	13	Scotland Question Time Event	The Lighthouse, Glasgow
March	13	London Women's Group Networking Drinks	Farrer & Co, London
March	18	Court of Appeal Decision in GAME – Breakfast Briefing	Berwin Leighton Paisner LLP, London
March	18	Introductory Series – Personal Insolvency 1	Deloitte LLP, Birmingham
March	18	Introductory Series – Personal Insolvency 1	Irwin Mitchell Solicitors, Leeds
March	18	Introductory Series – Personal Insolvency 1	Prospero House, London
March	19	R3 Annual Dinner	Lancaster, London
March	25	Northern Ireland Technical Update & AGM	The Merchant Hotel, Belfast
March	27	The Issues of Key Stakeholders in Insolvency	Copthorne Tara Kensington, London
March	27–28	Northern Conference	Oulton Hall, Leeds
April	3	North West Women's Group Space NK Event	Space NK Apothecary, Manchester
April	7	Eastern Regional Meeting & AGM	Ravenwood Hall, Bury St Edmunds
April	9	Thames Valley Meeting	Boyes Turner, Reading
April	24	Charities and Community Interest Companies	Marriot City Centre, Bristol
April	29	SPG Technical Review	Holiday Inn Bloomsbury, London
April	30	South West & Wales Regional Meeting	Bristol Golf Club, Bristol
May	1	R3 & INSOL Europe International Restructuring Conference	Tower Bridge Hilton, London
May	1	West Midlands Spring Ball	ICC, Birmingham
May	1	Yorkshire Regional Meeting	Crowne Plaza, Leeds
May	7	North East Regional Meeting	Tait Walker, Newcastle
May	14–16	R3 Annual Conference	Tivoli Marina, Vilamoura, Portugal
May	22	Restructuring Day	Holiday Inn Bloomsbury, London
May	22	South West Golf & Archery Day	St Pierre Hotel & Country Club, Chepstow
May	23	Eastern Golf Day	Diss Golf Club, Diss

Regional events

R3 events

For further information on R3 courses and conferences, please visit the R3 website **www.r3.org.uk**, where you can download the full 2014 programme. Alternatively, call the Courses team on 020 7566 4234 to request further details.

REGISTER TODAY courses@r3.org.uk or visit www.r3.org.uk

Association of Business Recovery Professionals
R3
Rescue
Recovery
Renewal

R3 ANNUAL CONFERENCE 2014

ANY PORT IN A STORM?

14–16 MAY 2014 · TIVOLI MARINA HOTEL
VILAMOURA, PORTUGAL

Portugal

Vilamoura

Navigate ahead of the challenges and chart the opportunities facing the profession.

Top insolvency and restructuring professionals will discuss the key issues of today, future trends and their implications.

9 HOURS CPD

PROGRAMME HIGHLIGHTS INCLUDE:

The economic outlook with William Keegan, Lord Nigel Lawson and Megan Greene

The new digital world with Stephen Mason exploring the emerging risks posed, the challenges faced and how to protect your business

Learning by example – how you can benefit from practitioners' experiences of managing stakeholders on a global basis

Scan the QR code for more information

SPONSORED BY:

BARCLAYS MAPS

R3, 8th Floor, 120 Aldersgate Street, London EC1A 4JQ
T: 020 7566 4200 **F:** 020 7566 4224 **www.r3.org.uk**

R3 contacts

President
Liz Bingham
lbingham@uk.ey.com

Vice-president
Giles Frampton
giles.frampton@richardjsmith.com

Deputy vice-president
Phillip Sykes
phillip.sykes@moorestephens.com

Administration

Chief Executive Officer
Graham Rumney
grumney@r3.org.uk

Assistant Office Manager
Tasneem Choudhury
tchoudhury@r3.org.uk

Smaller Practices Group; Personal Insolvency Discussion Group; Fraud Group

Assistant Director
Emma Hobson
ehobson@r3.org.uk

Finance

Finance Manager
Ryan Porter
rporter@r3.org.uk

Assistant Finance Manager
Alex Coles
acoles@r3.org.uk

Membership & Marketing

Head of Marketing & Member Services
Cynthia Matthews
cmatthews@r3.org.uk

Marketing Executive
Fareeha Afghan
fafghan@r3.org.uk

Regional Events Co-ordinator
Sara Calvert
scalvert@r3.org.uk

Database & IT Administrator
Samit Vadgama
svadgama@r3.org.uk

Membership & Marketing
membership@r3.org.uk
T: 020 7566 4238

Communications, Public Affairs and Policy

Director of Communications & Public Affairs
Victoria Jonson
vjonson@r3.org.uk

Communications Manager
Nick Cosgrove
ncosgrove@r3.org.uk

Communications Officer
Ryan McFadden
ryan.mcfadden@r3.org.uk

Public Affairs & Policy Manager
Alex Green-Wilkes
alex.green-wilkes@r3.org.uk

Education, Courses & Conferences

Training Director
David White
dwhite@r3.org.uk

Head of Courses & Conferences
Angela Stannard
astannard@r3.org.uk

Senior Courses and Conferences Manager
Natalie Harvey
nharvey@r3.org.uk

Courses and Conferences Marketing Executive
Kirsten Scully
kirsten.scully@r3.org.uk

Courses and Conferences Manager
May Ghaghda
mghaghda@r3.org.uk

Courses Administrator
Maggie Dean
mdean@r3.org.uk

Course Bookings
courses@r3.org.uk
T: 020 7566 4234 F: 020 7566 4225

Technical

Technical Director
John Francis
jfrancis@r3.org.uk

Technical Officer
Jonathan Ausena
jausena@r3.org.uk

Committee Chairs

Constitutional Adviser
Deborah Gregory, 020 7296 2000

Education, Courses & Conferences
David Chubb, 020 7583 5000

General Technical Committee
Mike Pink, 0207 311 1000

Membership & Member Services
Matt Dunham, 0161 953 6495

Policy Group
Steven Law, 01284 763311

Regional Communications Committee
Laurence Weeks, 01223 326600

Scottish Technical Committee
Eileen Blackburn, 0131 225 6366

Smaller Practices Group
Andrew Tate, 01634 899800

Regional Chairs

East Anglian
Shay Lettice, 01223 728222

London & South East
James Money, 020 7486 5888

Midlands
Richard Philpott, 0121 232 3000

North East
Allan Kelly, 0191 285 0321

North West
Richard Wolff, 0161 828 1990

Northern Ireland
Brian Murphy, 028 9043 9009

Scotland
Tim Cooper, 0131 222 9817

South
James Stares, 0208 038 1100

South West & Wales
Ross Connock, 0117 923 4274

Yorkshire
William Ballmann, 0845 437 4660

Regional Representatives on the R3 Council

Eastern
Laurence Weeks, 01223 423444

London & South East
Alison Goldthorp, 020 7606 8855

Midlands
James Martin, 0121 265 2522

North East
Linda Farish, 0191 256 9500

North West
Richard Wolff, 0161 828 1990

Northern Ireland
Joan Houston, 02890 918200

Scotland
John Hall, 0131 222 2460

Southern
Julia Branson, 0118 947 7823

South West & Wales
Richard Clark, 0117 939 2000

Yorkshire
William Ballmann, 0845 437 4660

Other Council Members

Louise Brittain, Alison Byrne, David Chubb, Simon Davenport QC, Christina Fitzgerald, Alan Hudson, Steven Law, Gareth Limb, Julie Palmer, Mike Pink, Elizabeth Pywowarczuk, Phillip Sykes, Matthew Tait, Andrew Tate,Cathryn Williams.

R3 membership categories

We continually strive to improve benefits for all members. Membership benefits across categories include:

- A copy of *RECOVERY* every quarter
- Attendance at regional meetings
- Priority bookings for R3 courses and most of its conferences
- Technical bulletins and releases
- Access to the members' section of the R3 website
- An invitation to the R3 annual conference
- Continuing professional education at discounted rates

Please see below for details of the different categories of membership:

Full members are invited to contribute to the development of insolvency, business recovery and turnaround professions at both local and national levels.

Benefits include: use of the designatory letters MABRP and a certificate of membership, inclusion in the *R3 Directory* and a copy of it, membership of INSOL International.

Associate members are individuals who do not meet the requirements for full membership but work significantly within the business recovery sector.

New Professional (Student) members are individuals preparing to take the Joint Insolvency Examination Board (JIEB), Certificate of Proficiency in Insolvency (CPI) or Certificate in Insolvency (ICAEW) qualifications. Pass students of the JIEB are eligible to apply for full R3 membership.

New Professional (Networking) members are individuals who have recently joined their firm, and/or are new to the business recovery sector and wish to network with R3 members. This category receives electronic copies only via access to the R3 website.

Advertisers' index

IBC = inside back cover
IFC = inside front cover
OBC= outside back cover

mgrappraisals

CHARTERED SURVEYORS • VALUERS • AUCTIONEERS

T: 0121 200 2206 e: info@mgrappraisals.com
www.mgrappraisals.com

WE UNDERSTAND YOUR BUSINESS!

With a wealth of knowledge in plant, machinery and property together with the important understanding of Insolvency, Business Recovery and Business Restructuring; MGR Appraisals is dedicated to providing a leading service to Insolvency Practitioners, Banks, Asset Based Lenders and Finance Companies to include:

- *Pre-appointment consultation*
- *Business asset valuations*
- *Property valuations & disposals*
- *Intangibles*
- *Online auctioneering*
- *Inventory*
- *Intellectual property*

Richard Mascall - 07801 306 587
richard.mascall@mgrappraisals.com

James Gregory - 07712 214 591
james.gregory@mgrappraisals.com

Jim Roberts - 07764 352 424
jim.roberts@mgrappraisals.com

Valuation Firm of the Year 2013

GLOBAL AWARDS 2013 WINNER

Surveyors, auctioneers & valuers

Empire Auction & Valuations! Tel: 0845 680 56 18
Property, Plant and Machinery, Chattels, Inventory
Valuation & Realisation of Assets

JPS Chartered Surveyors
Worth House, Unit 32 Stanley Road, Whitefield, Manchester M45 8QX
Tel: 0161 767 8001 www.JPSsurveyors.co.uk

If you're looking for unrivalled expertise across the full spectrum of services including asset-based lending, inventory and stock advice, corporate recovery and turnaround, talk to us.

As leading specialists in valuation and disposal of plant, machinery, business assets and real estate within Europe, we're the team you can trust.

Our team prides itself on delivering accurate, highly personalised and time-critical consultation, backed by a wide portfolio of corporate recovery programmes and disposal realisation services, using our market-leading on-line auction platform.

To find out more about GA Europe Valuations services, contact:

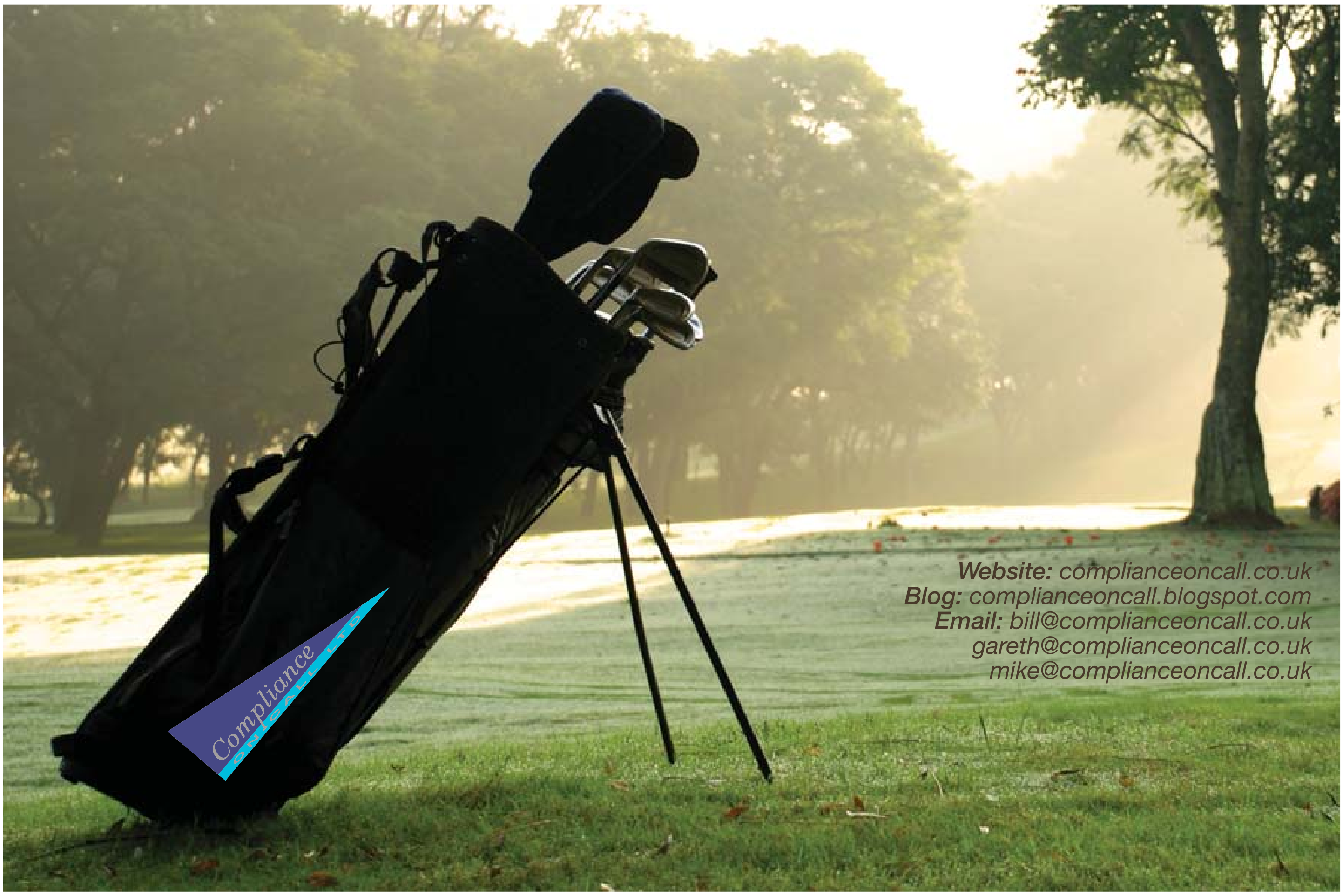
Gordon Titley	m: 0773 438 8785	e: gtitley@gaevaluations.co.uk
Dan Edgar	m: 0782 799 9332	e: dedgar@gaevaluations.co.uk
Peter Bache	m: 07774 174811	e: pbache@gaevaluations.co.uk

GA EUROPE VALUATIONS LIMITED.

14 Berkeley Street, Mayfair, London, W1J 8DX. t: 020 7318 0570 w: www.gaevaluations.co.uk
Offices in London, Birmingham, Milan and Munich.

On the move?
Promotion?
New business?
Announce it here!

Contact: Brendan McGrath
Tel: 01491 826262
E-mail: brendan.mcgrath@groupgti.com



Reach, recruit and influence recovery, insolvency and turnaround professionals in the UK

RECOVERY **is the premier quarterly business magazine for professionals working with underperforming businesses.**

Contacts:

Editorial: Sandra Kessell, GTI, 01491 828939, **sandra.kessell@groupgti.com**
Advertising: Brendan McGrath, GTI, 01491 826262, **brendan.mcgrath@groupgti.com**

Interview with…

Teresa Graham

Teresa Graham CBE has a string of honours and awards to her name. She has two main passions – assisting growing businesses and freeing them of red tape. She is currently heading up a government review into the use of pre-pack administrations, specifically looking at whether pre-packs encourage growth and employment and provide value for creditors. It is due to be published this spring.

Why did you go into accountancy?
I studied English linguistics at the University in Newcastle and wanted to go into HR. When the careers counsellor said I would have to move to London, which I wasn't yet ready to do, she asked if I fancied accountancy and I said yes, ok!

You didn't want to work with figures?
No, absolutely not, although in my holidays I worked at Ladbrokes the bookmakers. I was very numerate and rose to the rank of 'assistant bet settlor' but I didn't have any certification in maths at all.

I know you also worked in the family firm, so were you interested in business?
That was my entrepreneurial interest – I was always helping in the shops that we had, on the tills and around money. A dodgy accountant was responsible for my family going from riches to rags. It wasn't why I went into accountancy, but I certainly remembered that when I became an accountant. I wanted to be more of an adviser than a bean counter and that has coloured my approach to my client work. I want to make things simpler for businesses to understand, to get rid of all the technical obfuscation we wrap ourselves up in. A set of accounts is beyond the ken of most businesses.

> "Pre-packs seem to be akin to restaurants; you tell one person when you find a good one but 20 where you have a bad experience."

In small business it's important that you get paid and there's a good cash flow. Was your interest in small businesses one of the reasons you took on this job investigating pre-packs?
I have seen instances where pre-packs have caused harm to my clients but also instances where a pre-pack would have been a good solution but the clients said no because of the reputational damage they believed would tarnish and diminish them.

That's a shame. What comes to the fore most is the perception that it's a bad thing to be associated with or it's a quick fix. I want to try and put the record straight.

Your review is described as being in response to widespread concern over pre-packs. What is the evidence of this? How many cases are involved? What proportion of these concerns are in relation to disclosure and what proportion are in relation to some form of alleged impropriety?
That's a big question! Pre-packs have been hovering between 700 and 800 cases per year consistently since 2010, so not a huge number. This represents about 25–30 per cent of all administrations, and just two to three per cent out of the total 21,000 corporate insolvency interventions a year. Clearly there must have been some concern otherwise SIP16 wouldn't have been introduced.

Transparency and disclosure are, of course, issues; the first the unsecured creditors hear of the deal is after the event, so that causes a general unease among them. There is a lot of data out there but not very much up-to-date information. So, I've commissioned some academics to look at a few hundred pre-packs and I'm waiting for some solid information to act on. I want to know what I'm dealing with in order to answer the questions you've posed and that information will form an evidence base for my recommendations.

I know that IPs are increasingly reporting other IPs so there is, clearly, concern out there.

Do you accept that there can be good pre-packs and even good connected pre-packs?
There are times when a pre-pack is the best thing for creditors and that is what IPs are supposed to do; to work in the interest of all creditors. Pre-packs seem to be akin to restaurants; you tell one person when you find a good one but 20 where you have a bad experience. The danger is the noise from the bad pollutes people's perceptions of the good and all get tarred with the same brush. I'm not looking to reduce the number of pre-packs – I'm looking to eliminate the bad or, at least, minimise them.

Those I have spoken to have said that, where there is harm, it's in respect of connected pre-packs. What surprised me was that directors in any pre-packs aren't required to make any statement about the likely survival of NewCo; or what it is that they will do differently; whether the necessary capital is in place for NewCo to be successful.

> "You must aim for consistency between regulators otherwise IPs may then just pick the regulator that is more generous or regulates less well."

Speaking to stakeholders, it is pretty clear that it is unsecured creditors – the landlord, the trade creditors et al – who think they are losing out in some pre-pack cases, particularly in some connected party sales. Most accept that pre-packs can in the right circumstances be the best way to preserve value in the business – but they would argue they are being used, in certain cases, solely to dump debt.

I have commissioned research that will compare the returns to creditors between pre-packs and the closest counterfactual – a » trading administration – but it needs to be borne in mind that this will only provide broad comparison between the different procedures as the characteristics of the firms using both procedure may be different.

What *is* important is ensuring that pre-packing is used appropriately – that means that it should only be used where it leads to higher returns to creditors.

Everybody I've asked has given up their time to me: regulators, IPs, insurers, representative bodies, the legal profession, the judiciary… I've been to a great many meetings and met so many new people that I feel a responsibility to make a positive difference with any proposed recommendations.

How will you ensure that any changes proposed to address the concerns of those objecting to pre-packs (through various trade bodies, for example) won't disadvantage other bands of creditors?

I don't want any band of creditor or investor to be unfairly harmed by any of the recommendations I make. The research will show where the areas of likely abuse are.

A good business environment allows businesses both to succeed and to fail. The UK wouldn't be the success it is if it had an insolvency system that propped up businesses that were unable to adapt to changing conditions and stymied newer, nimbler businesses. However, there can be occasions when greater support is justified.

> "I want information; I don't want data."

I have come across examples in the automotive industry where small businesses are protected by larger corporate colleagues if the supply chain would be harmed by that business going under. I'd never come across that kind of industry self-help before and it was fascinating. The help may be financial, mentoring, some investment and even a take-over.

Do you feel the current range of regulatory penalties is sufficient to punish and deter IPs from breaching SIP16? Or do you think being given a bad name should be enough of a punishment?

A regulatory sanction is only good if it deters. So I would have to throw that back and say, is a £4,000 penalty likely to deter a firm if the job brought them in a fee of £100,000? If yes, then it worked, but if it doesn't, then that's not good enough. So, it is for the RPBs to decide whether the penalties are deterrent enough and if they want me to consult with them at a later date then I'm very happy to!

In addition each regulator currently publishes penalties independently of each other. I am aware, however, that there are plans in place to bring this all together on the Insolvency Service website, which will help with regulatory confidence.

You must aim for consistency between regulators otherwise IPs may then just pick the regulator that is more generous or regulates less well. You could pick the worst or the best for you, depending on your mindset.

Would you accept that the revised SIP16 has significantly increased the level of disclosure and hence transparency?

SIP16 MkII was a bit of an improvement on its predecessor, but it's still a statement. It might tell me *what* you've done but not *why* you've done it. I am not interested in box-ticking. I'm interested in understanding the process that led the IP to recommend a pre-pack to their clients. I want information; I don't want data.

> "I get fed up with the government always having 'to do something' – you've got to man up and do something yourself."

Is enough being done by the authorities, regulators and the industry (individual IPs and their firms) to crack down on those touting pre-packs, so-called 'ambulance chasers', where the aim or consequence of which turns out to be improperly disadvantaging creditors in an impermissible or unjustified way?

I was pleased to see the Secretary of State got rid of five or six of these last year – you've got to be ever-vigilant. IPs have shown me examples of letters companies receive after getting a CCJ and they're breath-taking: 'Do you want to dump your debt; do you want to keep your business? Ring me.' But an ambulance chaser is always going to need an IP to do the pre-pack so where do they find the accommodating ones? I get fed up with the government always having 'to do something' – you've got to man up and do something yourself. In my profession, I have a duty to report misconduct. I don't want my profession becoming scuzzy. To get a bad chartered accountant out of the profession, I would actively name, shame and be damned.

Can you share with us the kinds of self-help changes to how IPs work and/or report to creditors you think might result in fewer complaints and 'noise' over the pre-pack issue?

Transparency is important, but we were talking earlier about how information has to be relevant. It has to be concise. I went into the Royal Institution of Chartered Surveyors to introduce regulation for firms as well as for members and modernise as I went along – I replaced 60 pages of dense type with 6. It was principles based not prescriptive so you had to think hard about how to comply – no simple tick boxes. I will tell you to keep clients' money safe but not how to do it. If you can't keep clients' money safe you're an idiot – come on!

Do we need an easy to read and understand pre-pack impact assessment summary sheet that all IPs have to publish, ie something that shows who the winners and losers are, financially and otherwise? If so, will you be offering a template for such a report?

I don't see it as my place to suggest templates to a profession that should be able to use professional judgement in carrying out its regulatory and statutory responsibilities. If a regulatory body wants to devise a template then, feel free, and it should be copied if it works. We come full circle back to RPBs and consistency. I should be able to fear my regulator but to, at the same time, understand that I will be treated fairly. If that guy over there, while I'm doing my best, is flouting the law, I want my regulator to kick his a**e.

So, what do you think people outside the insolvency profession understand by the term 'pre-pack'? Do you think people would understand an energy efficiency-style report on the pre-pack, or something that shows it passes the kite mark?

Well, I guess what I'm trying to do with my report is to recognise where the harm is and to try to eliminate it; to go a long way to redressing the perceptions that all pre-packs are bad. And actually, that's not a bad place to end this interview! Thank you!

Teresa Graham CBE

Teresa Graham joined a Big 4 firm in Newcastle upon Tyne in 1977 and qualified as a chartered accountant in 1980 later moving to Baker Tilly where she held a board position for many years. In 1986 she was seconded to the government's enterprise and deregulation unit and in 1988 was named the Young Accountant of the Year in recognition of her contribution to the profession, the small firms sector and government.

She was named the 2007 Laureate under the ICAEW Award for Outstanding Achievement and serves on a number of advisory boards, small business service panels and SME boards in both the private and the public sectors.

Teresa was awarded a CBE in the 2007 New Year's Honours List for public service and an OBE in the 1997 New Year's Honours List for services to better regulation and the small firms sector.

SANDRA KESSELL is the publishing manager of *RECOVERY* magazine.

NEIL TAYLOR INSOLVENCY
INSPIRATIONAL TRAINING SINCE 1990

JIEB: Resits, Referrals And First Timers

Are You Sitting Any Of The Joint Board's Exams In 2014?

A New Approach To JIEB Exam Training Founded Upon Hugely Successful, Tried And Tested Joint Board Study Techniques.

- **New Ideas**
- **New Materials**
- **New Courses**

A Refreshing And Creative Approach, Built Around You - The Individual Who Deserves The Best Support

Resit And First Time Courses Starting Throughout The Year.

YOU MUST BE INSPIRED TO SUCCEED

www.ntinsolvency.com
enquiries@ntinsolvency.com
01962 77 21 81

Challenge

Satisfaction

Ethics

Recognition

Support

Collaboration

Growth

Training

Teamwork

Balance

Compensation

Success

Independence

Benefits

Integrity

Camaraderie

Analysis

Valuations

& YOU

POWERING SOUND DECISIONS

Here at Duff & Phelps, we know what it takes to power sound decisions. And we believe that behind every good decision, you'll find collaboration, valuable training and a dose of intuition. But ultimately, it comes down to the human element—our team of forward-thinking professionals—to make it happen.

That's where YOU come in—provided you're ambitious, disciplined and up for a challenge. We'll do our part, providing you with an environment where you can learn, grow and thrive—where you can make an immediate impact.

Following the successful recruitment of four new Restructuring Partners we are looking to continue to strengthen our National Restructuring Team at all levels.

Join our Restructuring team in **Birmingham, Leeds, London or Manchester** and together we will power the sound decisions that enhance value—yours and ours.

If you are interested in this exciting opportunity please call Toni-Marie Eakins on 020 7089 4841 or visit our website.

duffandphelps.jobs

DUFF & PHELPS

Financial Advisory and Investment Banking Services

All enquiries will be dealt with in the strictest of confidence.
Duff & Phelps is committed to equal opportunity and diversity, and recruits people based on merit.