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Winter 2008

RECOVERY

Funding

With fewer funds around and higher rates, IPs will have to be seriously inventive

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Advice on aspects of ABL funding

Adapting to the economic reality
The challenges and opportunities for investments

Office-holders' conflicts
Conflicts of interest in formal insolvency

Don't forget about competition
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Editorial

Insolvency is the late ’08 buzzword. Regrettably, restructuring is becoming passé. This does not mean, however, that the European High Yield Association’s misnamed Insolvency Law Reform proposals are necessarily as ill-conceived as sometimes suggested in insolvency circles. When I interviewed Dan Hamilton, Chair of the EHYA’s European Insolvency Reform Committee, for this issue of *RECOVERY* (p54–6), he made it clear that the proposals are designed to affect financial creditors only and to apply only to restructurings with over £200 million of debt. In such cases, is a statutorily supported ‘New London Approach’ such a bad thing? It certainly won’t affect the general insolvency work that most of us undertake.

The world’s economic landscape has changed dramatically over the few weeks since articles began to be commissioned for this issue. Recession is upon us and the prospect of a significant upturn in formal insolvency appointments makes two of this issue’s articles especially timely. Richard Heis (p13–15) introduces the new code of ethics that comes into effect on 1 January 2009. His conclusion, that some might find the structure of the code confusing and that it merits careful study before it comes into effect, is concise and accurate. In a similar vein, Rupert Connell (p23–25) discusses officeholders’ conflicts, analysing the approaches of the courts as well as the RPBs. By illustrating the differences in those approaches he makes clear both that the courts have a distinct and separate view of conflicts from the RPBs, which practitioners therefore need to recognise and understand, and that practitioners must comply with the code of ethics and uphold the reputation, integrity and objectivity of the profession.

Chris Laughton is editor of *RECOVERY* and a partner at Mercer & Hole.

Reflections on our brave new world

Antony Fanshawe expounds on the monetary meltdown and the need to do more with less.

I am writing this on 8 October 2008. This morning Alistair Darling announced a £50 billion plus plan to inject new capital into four British clearing banks. Yesterday RBS fell to 90p, 76 per cent down from the six-month high of 384p.

At that level it must be a buy, was my first thought, particularly with government investment. At the time I did not know of the likely structure of the government's lifeboat for the banks but my first instinct was that they should offer to underwrite a rights issue not only to get some of the pain taken by the private sector but also to invest in ordinary shares with the upside of capital appreciation, voting powers and dividend income.

> These guys really need to start thinking like a turnaround fund. I wonder who is advising the government on this; not, it seems, IPs.

I was pleased to hear Jon Moulton echoing my thoughts this morning, when I heard that far from going for the ordinaries the government was going for the worst of all worlds: preference shares. All the risk of the ordinaries with none of the upside!

At least, I said to myself, why not look at the deal Warren Buffett did with Goldman Sachs and get a stonking coupon on the preference shares and either make them convertible or take an option on the ordinaries as well at the current market price.

Where were the IPs?

These guys really need to start thinking like a turnaround fund. I wonder who is advising the government on this; not, it seems, IPs.

I cannot think that the government had an IP helping to drive what became the Northern Rock debacle: months of dithering and then a botched nationalisation. Wouldn't it have been better to crystallise the position by appointing administrators to protect the position if necessary, with the government guarantee behind them. There were, at an early stage, a number of prospective purchasers who may have bought the business or parts of it from the administrators. The deals could even have been set up beforehand as pre-packs with some accelerated M&A work, so the transfer could have been seamless with no need to call on the government guarantees.

Shareholder claims would have been dealt with through the insolvency process without the need now for a share valuation, which will bring with it a prolonged period of wrangling and the potential for litigation at an inevitable further cost to the exchequer.

My colleague on R3 council, Mark Phillips, has expressed the view that perhaps we should change the name of administration to the French term, *sauvegarde*, (or safeguard to the monoglot English speaker). He feels that this would express the essential nature of the moratorium without the negative and, in some eyes, value-destructive connotations conjured up by the word administration.

> The challenge for us as a profession is to be quicker on our feet, to preserve value in goodwill and other intangibles and continue to deliver returns to creditors.

And he may be right; but whatever the name, it does seem strange that government should go to the trouble to invent a process and then seemingly turn a blind eye to it when the national interest is threatened.

At last though some practical lessons seem to have been learned as the banking crisis has developed. The split of Bradford and Bingley was a much more decisive operation, and the proposed takeover of HBOS is much more like what should have happened with Northern Rock. There are obvious similarities between these operations and the more common pre-pack administration sales as practised by IPs. Perhaps the government has been listening, and perhaps we have official sanction for pre-packs.

At the coalface

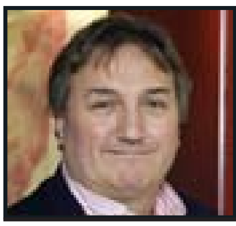
The implications for the wider economy are becoming obvious here at the coalface. In my office we have seen new instructions where banking facilities are not being renewed at all, or at a lower level than previously or only where supported by a personal guarantee.

The latter has certainly had the desired effect of concentrating directors' minds on whether they should continue to trade, and if the level of borrowing is more likely than not to increase, the answer is obvious.

Although the root cause of this recession (if I may call it that) is very different from the 1990 recession, the net effect is similar: costly money and not much of it.

The big difference this time round is the level of unencumbered assets in companies' balance sheets. In the early 1990s factoring and invoice discounting was in its infancy. Most SME funding was provided by overdrafts secured by fixed and floating charges and it was the accepted wisdom that book debts were a fixed charge. Now book debts are assumed to be a floating charge but often no longer belong to the company having been assigned to a factor or invoice discounter. Plant and equipment now also tend to belong to third parties, while real property is more often than not leased at full rents, rather than freehold, and office furniture and equipment has a derisory value.

The challenge for us as a profession is to be quick on our feet, to preserve value in goodwill and other intangibles and continue to deliver returns to creditors. This is what has primarily driven the rise of the pre-pack, which was largely unknown in 1990. It looks now as though it's here to stay, with government sanction.



Antony Fanshawe is a partner at Begbies Traynor.

President's column

Nick O'Reilly looks at the banking crisis and its impact on the insolvency industry.

The recent events in the financial world have taken place at an astonishing rate and it is a truly amazing time to be R3 president. Later in this issue you will see that we have given space to Angela Knight, chief executive of the British Banking Association (BBA) to give its views on the banking crisis. We at R3 have always been keen to listen to other stakeholders' views with regard to how they see business recovery and insolvency. It is no secret that R3 and the BBA have not always seen eye to eye, especially in the area of Individual Voluntary Arrangements over the last few years. Hopefully the IVA protocol, agreed by all stakeholders including the Insolvency Service and implemented in February 2008, will go some way to improving knowledge of our respective positions. That said, we will not shy away from making our members' views known to the BBA if we feel that any of its members are unnecessarily turning down viable voluntary arrangements for no logical reason.

Northern Rock

It is amazing to think that it was only in August 2007 that the credit crisis really entered the national consciousness when Robert Peston, BBC Business Editor, reported that Northern Rock had approached the Bank of England for emergency funding because their lines of credit had disappeared. We at R3 had also had our run-ins with Northern Rock in the period leading up to August 2007. We were very concerned when they made various public announcements that nine out of ten voluntary arrangements were, in their opinion, inappropriate. We felt that did a very big disservice to our members and complained immediately and asked for verification of that headline. No such verification was forthcoming. Even when people were queuing outside the branches of Northern Rock in August 2007 for the first run on a bank for many generations, no-one could have foreseen that just over a year later, the government would be needing to bail out institutions of the size of the Royal Bank of Scotland or that Lehman Brothers would have collapsed so spectacularly. In 20 years' time I wonder how history will judge the politicians involved and the chief executives, chairmen and boards of directors of the clearing banks of the UK. I am not sure that there will ever be the same level of trust in banks.

August 2007: the crisis begins

Icelandic banks

In May 2008 we held our annual conference in Cannes and Bjorn Gudmundson of Landisbankii gave us a presentation on how he saw the global economy at that stage. He also gave us a very short presentation on how Iceland had grown from being a small fishing community of 300,000 people to become one of the largest global players in the financial market. Even then a number of our members were astute enough to ask the pertinent question: 'Where has the money come from?' and, six months on, it is clear that it was all built on a house of cards. The national economy of Iceland will be paying for the follies of a small number of banks and entrepreneurs for many years to come.

All of the press coverage of the financial crisis and subsequent bail out by central governments has led some people to believe that everything will be back on track and there are no worries ahead. Unfortunately our members know that there is a time bomb out there in terms of the level of corporate failures and we expect to see quarter-on-quarter increases in the number of corporate insolvencies over the course of the next 18 months and perhaps longer.

Finally, we at R3 remain committed to providing thought leadership and engaging in high level discussions with government, the opposition, trade associations such as the BBA, the Insolvency Service and any other parties who we feel would benefit from understanding the difficult, technically challenging job that our members carry out at the coalface and the experience that they can bring to the discussions.

As I said at the start – an amazing time to be president.

R3 News

SPG Forum

The SPG Forum took place at Chesford Grange Hotel in Warwickshire on 16 and 17 October. It was a really lively conference, with a fantastic turnout. I think I personally enhanced the conference at the Gala Dinner by falling off the stage and taking one of the event's exhibitors, Richard Mitchell of C&V Data Management Services, with me. I would point out that no alcohol was involved in the fall and it just comes down to plain clumsiness on the part of your president.

> "I think I personally enhanced the conference at the Gala Dinner by falling off the stage.

Annual Dinner

It was nice to see so many members at the Annual Dinner at the Dorchester on 3 October 2008. I had personally chosen John O'Farrell as the after-dinner speaker as I have really enjoyed his books. He did an enjoyable presentation and came across as a thoroughly nice guy, and I am really pleased that the event was a great success. My thanks to Angela Laxton at R3 who does a sterling job in organising these events; the evening always goes off smoothly with Angela controlling operations.

Regional events

My diary continues to be a challenge to me in these busy economic times. During the next month I am attending the North West Regional Meeting, and the South West and Wales Regional Meeting as well as the Southern Region. The areas that I still wish to get to before my term ends are the Midlands Region, Northern Ireland and the North East and I am really looking forward to coming to events and hearing members' views on how the association is operating and areas of concern that they are facing.

Nick O'Reilly is client partner at Vantis.

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Burning platform

Have your shout. If you have comments about articles in *RECOVERY* or concerns about the industry we'd like to hear from you.

Dear Sir,

Banking Bill presents risks to bank creditors

It is surprising to see the government has imposed a condition on banks using the Bank Reconstruction Fund to keep lending availability to homeowners and small businesses at 2007 volumes; yet, at the same time, it is introducing measures that will make it more expensive for banks to lend.

Surprising, because it was the 2007 volumes of lending that helped to stoke the present crisis in the first place. And it could increase the cost of lending to or dealing with UK banks because their financial institution counterparties may have to hold more capital as a result of some of the proposals.

The restriction imposed on RBS, HBOS and Lloyds TSB paying dividends to shareholders has been widely criticised. It has been blamed for the banks' lower than expected share price, and it may increase their cost of capital.

Some provisions of the Banking Bill could make it more expensive for financial institutions worldwide to deal with any UK bank, not just those that use the Bank Reconstruction Fund:

- The Bill will take away the right of counterparties to call an event of default and accelerate a loan or other obligation based on a special resolution regime transfer order. It would not matter whether the affected contract were transferred or kept with a residual bank.
- The Bill may undermine set off and netting clauses. If implemented, the Bank of England may be able to cherry pick transactions (or even individual obligations from relationships that are structured as a single agreement) and transfer them to a private or public sector buyer. This would leave the creditor exposed to the weakened residual bank. Although under the Bill HM Treasury *can* make an order to preserve set off arrangements, it does not have to.

Up to now, financial institutions have only had to post capital to support net, rather than gross, exposures to counterparties. If the Bill were implemented as it stands, with no amendment to the capital rules, financial institutions dealing with UK banks would have to review their netting and collateral arrangements. They would have to assess whether they have to hold more capital if they could not be confident their close-out netting and set-off arrangements would work. This would probably be priced into any deal with a UK bank, and restrict the scale of dealings.

Rosali Pretorius is a partner in the Financial Markets and Regulation Group at Denton Wilde Sapte.

Obituary: Muir Hunter, QC

Muir Vane Skerrett Hunter, who died aged 95 on 18 October, took over as the head of 3 Paper Buildings in 1958. After a wide ranging legal career, insolvency had become his major focus, and the quality and quantity of work that his expertise attracted led his colleagues in Chambers to specialise likewise. The set subsequently relocated to 3–4 South Square, Gray's Inn, where it continues to be a leader in the field of insolvency and related subject areas.

Born in 1913, Hunter was educated at the Westminster School and read Classics at Christ Church, Oxford. After deciding to pursue a legal career, he was called to the Bar by Gray's Inn in 1938. His early career was interrupted by war service spent with the Royal Armoured Corps and in India, where among other things he judged anti-corruption tribunals.

Hunter became editor of *Williams on Bankruptcy* in 1948. His work on the title (and its successor, *Muir Hunter on Personal Insolvency*) marked the start of a distinguished academic career in addition to his career at the Bar, recognised by his appointment as visiting professor of insolvency law at Bournemouth University

in 1997 and by the University of Kingston in 2007. His final book, *Going Bust? How to Resist and Survive Bankruptcy*, was published in 2007.

Hunter was known for his integrity, professionalism and tenacious style of cross-examination. He took silk in 1965 and was made a bencher by Gray's Inn in 1975. In 1972, in one of the highlights of his career, he played an integral role in uncovering local authority corruption – and was uncowed by governmental pressure to soften his cross-examination of the then Home Secretary Reginald Maudling, who resigned as a result.

Hunter had strong humanitarian tendencies, as shown early on by his relief work during the Spanish Civil War. In the 1960s he worked with human rights organisation Amnesty International (of which he was a founder member), observing trials of alleged political dissidents in Turkey and the former Rhodesia, and in 1969 he co-founded a Neighbourhood Law Centre in North Kensington to offer help to people unfamiliar with the legal system. Hunter also joined forces with his second wife, a charity worker in palliative medicine, to found the Nairobi Hospice and the Polish Hospices Fund to provide training for Polish doctors and nurses in palliative medicine. The latter initiative eventually helped to revolutionise the field of palliative care throughout central and eastern Europe.

Hunter married his first wife, Dorothea Verstone, in 1939. After her death in 1986 he married Gillian Petrie. He is survived by Gillian and his daughter from his first marriage.

News update

SPG Forum members predict increases in corporate insolvency work

R3 members were asked in 2007 if they felt that their practices' earnings from personal and corporate insolvency work would increase, decrease or stay the same during the coming year.

At the SPG Forum in October 2008, over 180 delegates were asked the same questions to find out what had actually happened over the last 12 months, and to predict what would happen during the next 12 months. The charts show how remarkably close the predictions were compared with the figures for 2008.

Personal insolvency work

	2008 prediction	Actual figs for 2008	2009 prediction
Increase	26%	24%	36%
Stay the same	30%	25%	28%
Decrease	36%	37%	26%
Not relevant to me	8%	14%	10%

Corporate insolvency work

	2008 prediction	Actual figs for 2008	2009 prediction
Increase	54%	57%	78%
Stay the same	28%	21%	7%
Decrease	7%	11%	2%
Not relevant to me	11%	11%	14%

The future looks grim for retail sector

Statistics show that the retail sector is facing a hard time in the run up to Christmas and beyond. Companies need to consider their strategic options carefully and ensure they are diversified. The March issue of *RECOVERY* is on the theme of retail – so watch this space to find out what's happening.

Formal insolvency analysis

	Q4 07	Q1 08	Q2 08	Q3 08	July/Aug	Sept
Food & drink	14%	10%	8%	6%	7%	4%
Clothing & footwear	18%	27%	18%	19%	17%	23%
Furniture	9%	12%	19%	16%	17%	13%
Other household goods	4%	5%	8%	8%	9%	6%
Mail order	13%	8%	6%	6%	5%	6%
Non-specialised stores	17%	17%	8%	11%	11%	11%
Other specialised stores	21%	18%	28%	27%	25%	34%
Others	4%	3%	5%	7%	9%	3%
	100%	100%	100%	100%	100%	100%

IS investigations and enforcement operations

Grant Thornton has produced its final report on the Insolvency Service's investigations and enforcement operations.

An interim report was produced in April 2008 but, following discussion after its publication, additional data was sought to test further and provide more information for the emerging conclusions. On the strength of this, the conclusions and recommendations in the final report have been refined. The report is available on **www.insolvency.gov.uk/aboutus/reportweb.pdf**.

Thousands in debt missed off official figures

R3 estimates that around 600,000 people who are struggling with debt are being missed off official IS figures. These are people who have taken out debt management plans (DMPs) that have now become unmanageable. Unlike bankruptcy and individual voluntary arrangements, DMPs are not included in the statistics produced by the IS.

Stable PPF levy

The Pension Protection Fund (PPF) intends to keep its basic levy stable in 2009 but warns that the levy scaling factor, coupled with an economic downturn, could still combine to torpedo the UK's most vulnerable defined benefit schemes.

The PPF will not collect a levy from those schemes that have entered assessment at the start of the levy year. However, any waived levy will be recouped if the scheme in assessment is subsequently rescued.

In September, the PPF published *The 2009/10 Pension Protection Levy Consultation* document. It was available for consultation and all comments received by 23 October were considered. A summary of the responses and any changes was published in November on **www.ppf.gov.uk**.

Regulation of ratings agencies

Ratings agencies have come in for some stick lately and are likely to have to sharpen up their act. There are differing opinions on how this can be done. On 31 July 2008, the European Commission put out the *Proposal for Regulatory Framework for CRAs (credit ratings agencies) and Embedded Ratings Policy Options* for consultation. Standard & Poors agree with the EC's desire for greater oversight of ratings agencies and fully support CESR's (The Committee of European Securities Regulators) and IOSCO's (International Organisation of Securities Commissions) calls for greater transparency. However, S&P's president, Deven Sharma, has called for European policymakers to base their proposed system of supervising credit rating agencies on internationally accepted principles and standards in order to ensure a consistent approach globally and ensure ratings opinions remain comparable worldwide. For more information see **www.standardandpoors.com**.

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Legal update

In this time of economic turmoil, Peter Cranston questions whether pooling arrangements might return to traditional principles and, if so, whether this is desirable.

As this note is penned, the Icelandic banking crisis serves as a reminder of the collapse of the BCCI group 17 years ago. One of the legal legacies of BCCI was the clarification of the powers of liquidators to enter into compromise arrangements to produce the pooling or substantive consolidation of several connected insolvent estates into one. The primary drivers are the complexities of the cases, often impossibly entangled, diminution in the aggregate costs of administering the estates, and accelerated distribution of what is available; all obviously laudable aims.

However, a fundamental part of English insolvency law, indeed of practically all English corporate law, is that it operates at the separate entity level, with each individual company (and the assets in its liquidation) responding to the claims of those with claims against it. Departures from the single entity approach should require good reason and, as will be suggested, a more informed and positive assent from those who are affected than may be the received wisdom.

The position before 1992

Before the decision in *Re: BCCI SA (No 2)* [1992] BCC 715, the position in England was reflected in the words of Plowman J in *Re: Trix Limited* [1970] 3 All ER 397:

> *'It is elementary that if it is desired to distribute the assets of a company otherwise than strictly in accordance with the creditors' rights, the proper way to do it is by a scheme of arrangement… but the policy of the liquidators has been to avoid having a scheme of arrangement. Instead I am asked in effect to deprive the creditors of the protection afforded by [a scheme of arrangement], and to sanction a conditional agreement of compromise…'*

Since Plowman J's protest against pooling without using a scheme, effective group consolidation has been achieved through the use of interlocking CVAs under Part 1 of the Insolvency Act 1986. The need for a fully fashioned scheme of arrangement or CVA has also been tempered by the Court of Appeal's judgment in *Bank of Credit & Commerce International SA (No 2)* [1992] BCC 715, in which the court approved a compromise involving a variation of the rights of creditors in exercise of the powers conferred on liquidators (with court sanction) under section 167 and schedule 4 Insolvency Act 1986, to achieve a combined liquidation of two BCCI companies in Luxembourg and the Caymans. The Court of Appeal followed the Scottish decision in *Re Taylor, Noter* [1992] BCC 440 in departing from *Trix*. A similar outcome was also achieved in *Re Transocean Equipment Manufacturing and Trading Limited* [2004] All ER (D) 352.

What prompts a return to seemingly well established principles is the apparent convergence of recent views from the USA and Australia, which could signal a return to traditional principles in keeping with the more stringent approach of Plowman J.

Ireland and Australia

There is no statutory provision explicitly permitting pooling in English law unlike, for example, Ireland, where section 141 of the Irish Companies Act 1990 permits consolidation between related companies or, more recently, the introduction of section 579E into the Australian Corporations Act 2001, which received its first judicial consideration in *Allen* v. *Feather Products PTY Limited* [2008] NSWSC 259 in March 2008.

The Irish provision is headed *Pooling of Assets of Related Companies*, and confers a discretion on the court to order that two or more related companies may be wound up as if they were one, having regard to the several factors set out in section 141(4), including the extent to which the businesses of the companies have been intermingled.

> "What prompts a return to seemingly well established principles is the apparent convergence of recent views from the USA and Australia, which could signal a return to traditional principles in keeping with the more stringent approach of Plowman J."

The new Australian legislation also gives the court a discretion to make a pooling order in respect of a group of two or more companies. This would cause the several companies to be jointly and severally liable for the debts of and claims against each of them, with debts among the companies themselves being extinguished, so that the assets in each winding up become applicable towards satisfaction of the external debts of all of the companies together (as explained by Barrett J in *Allen* v. *Feather Products* at [7]).

The Australian requirements set out in section 579E(1)(b) are:

- that each company is related to the other group companies, or
- the companies are jointly liable for one or more debts or claims, or
- the companies jointly own or operate property that is or was used in connection with business, scheme or undertaking carried on jointly by the group companies, or
- one or more companies own property used by any or all of the group companies in connection with that joint enterprise.

The requirement was that each company was engaged in activities with the others that constituted a single business enterprise, with the focus being upon the actual state of affairs rather than the independent corporate capability of each of them. In *Allen* v. *Feather Products*, it was clear that the three companies involved met the requirements of section 579E. Feather Products itself manufactured goods using labour provided by the second company, and its finished products were then sold and marketed by the third. Physical assets were used jointly by the legal owner as well as the other two companies. What caused the court to reject the application, however, was that two of the companies had been in administration before liquidation, so that their liquidations were deemed to have commenced when the administration began, which was before the new provisions came into effect on 31 December 2007. Despite the obvious satisfaction of the requirements, the court had no jurisdiction to grant the pooling order, however meritorious it might otherwise be.

Black Stump

Prior to the new pooling order provision in Australia, applications by insolvent companies to propose pooling arrangements were not uncommon. In *Black Stump Enterprises* [2005] NSWCA 480, an application by the liquidators of the Black Stump group of companies was made for a pooling order by way of directions application. In *Black Stump*, Barrett J had set out several possible bases for the pooling order sought but, at the hearing, it was clear that none of the creditors had positively consented to pooling, nor had they been told their unanimous consent was required. Creditors' objections were invited, but Barrett J considered that this *nem con* approach was insufficient to enable the court to vary creditors' rights. In the event, the application was dismissed and pooling refused.

> "Practitioners should pause for reflection before resorting to pooling compromises as expedient alternatives to the normal (and) separate legal paths."

The liquidator's appeal failed. The court held it had no power to order pooling, no matter how expedient it might be. There was no evidence that the consents of creditors to alter their rights had been obtained, nor had there been a compromise between the creditors and the liquidators. Absence of objection was not sufficient. The liquidators' case was bound to fail, so much so that the court required the liquidators' solicitors to show cause why they should not bear the costs of the application and warned that the court

> *'is concerned about dividends to creditors in a winding up being whittled away by expensive legal proceedings that have little chance of success'.*

Ansett

The Ansett Airlines saga has featured consistently in the Australian courts since 2001. The Ansett companies were under deeds of arrangement (DOCAs). In 2005, the deed administrators applied for directions as to the conduct of creditors' meetings to consider variations to the DOCAs, proposing to pool all of the assets and liabilities of the Ansett group into a single entity and treat it as one. Goldberg J declined to grant the application (although he remained open to additional evidence that later enabled a meeting to consider the pooling scheme to proceed, notwithstanding his March 2006 decision). The principles set out in the judgment of Goldberg J in the Federal Court (*Ansett Australia Limited* [2006] FCA 277) are instructive, particularly as regards the comparative review of the US jurisprudence on substantive consolidation (found at [96] *et seq*). By contrast, there is no reference to any contemporary English authority, such as *BCCI No 2*, in his analysis.

> "The court held it had no power to order pooling, no matter how expedient it might be. There was no evidence that the consents of creditors to alter their rights had been obtained, nor had there been a compromise between the creditors and the liquidators."

Goldberg J commented on the effect of pooling upon creditors, especially as to the impact of the proposed pooling on individual creditors (some of whom would be worse off), and the lack of evidence about where the anticipated additional costs would be allocated if pooling was refused.

Pooling assets and liabilities was a well known concept. However, it did not appear to the judge that pooling had been approved where a number of the creditors of one or more of the companies had been disadvantaged by the pooling proposal, and those creditors had not unanimously consented to, or approved of, the pooling proposal itself.

Substantive consolidation

In *Ansett* Goldberg J reviewed the US jurisprudence on the doctrine of substantive consolidation, which was akin to pooling and, in particular, the recent restatement of the principles in the Third Circuit's decision in *Re: Owens Corning* (2005) 419 F.3d.195, that substantive consolidation was an extreme remedy to be used sparingly. Mere benefit to the administration of the various companies was not sufficient to warrant substantive consolidation.

The challenge to substantive consolidation in *Owens Corning* was made by its lenders, seeking to rely on subsidiary guarantees that would have been swept away in a consolidation. All other creditor constituencies (and the debtors) favoured consolidation. The Third Circuit reversed the District Court's approval for consolidation and made clear its rejection of a creeping liberal trend since 1980 towards substantive consolidation, verging on the routine and expedient in some cases, and questioned whether it was equitable to the creditors of each company. It emphasised that corporate separateness should be respected in the absence of compelling reasons, and then only after other approaches had been considered and rejected.

On co-mingling, Goldberg J in *Ansett* quoted the US court that

> *'…co-mingling justifies consolidation only when separately accounting for the assets and liabilities of the distinct entities, which will reduce the recovery of* every *creditor – that is, when every creditor will benefit from the consolidation. Moreover, the benefit to creditors should be from costs' savings that make assets available rather than from the shifting of assets to benefit one group of creditors at the expense of another; mere benefits to some creditors, or administrative benefits to the court, falls far short.' [98]*

Goldberg J considered that these principles applied and complemented the Australian principles. There was no >>

authority in support of the view that a court would pool in circumstances where a number of the creditors of one or more of the companies would be significantly disadvantaged (which troubled him in relation to the Ansett proposals). It was not sufficient for a pooling order that the administration or liquidation is complex, or that the identity of the creditors is difficult to determine. Those features may have a cost impact, but they were not, of themselves, determinative of the case for consolidation. The court was anxious to see liquidations conducted with commercial efficiency, and would not allow any technical rules to frustrate this. Goldberg J added that, although the pooling proposal was advantageous to most of the creditors from a practical point of view,

> *'I do not consider that one can disregard a corporate structure when one is seeking to exercise power under [section 447A of] the Australian Corporations Act, especially when the company has a group of clearly identified creditors, who may be disadvantaged by the exercise of the power. [It is not] open to an administrator to conduct the affairs of a company under administration in a manner detrimental to creditors.'*

The application by the Ansett administrators, albeit in good faith, and even though no creditor objected to the pooling proposal (other than the party appointed to argue against the administrators' application), was not determinative. The creditors who were adversely affected had not been put on notice of the monetary extent to which they may be adversely affected by the pooling proposal.

Ansett after *Allen* v. *Feather Products*

Does section 579E diminish the force of Goldberg J's judgment? *Ansett* was not referred to in *Feather Products* but *Black Stump* was. Barrett J noted [31] that the court in *Feather Products* recognised that there had been

> *'adequately informed assent by the creditors to a defined departure from the basis on which assets would otherwise be applied and debts and claims would otherwise participate in the respective windings up'.*

That seems wholly consistent with the views articulated in *Ansett*.

So what?

Indeed, you might ask. Pooling remains a minority pastime in English insolvency, and *BCCI SA (No 2)* amply justified the pooling compromise sanctioned because of the 'sheer complexity' thwarting 'any effort to proceed neatly along the normal legal paths' (per Nicholls V-C, at first instance, with whom the Court of Appeal agreed). However, the observations that pooling agreements are not conditional upon acceptance by creditors (*BCCI* at [1992] BCC 719F), or the compromise approved in *Transocean* without formal objection from creditors to save cost and to ease the administration of the estates, sit uneasily with the views of Goldberg J in *Ansett*. The complexity of corporate groups and their financial structures have certainly not diminished since the fall of BCCI. Practitioners should pause for reflection before resorting to pooling compromises as expedient alternatives to the normal (and) separate legal paths. They need to ensure that there will indeed be benefits to all creditor constituencies and that value is preserved for them by costs' savings, rather than rearranging legal entitlements.

Peter Cranston is a partner in the restructuring group at Eversheds.

Recent case summaries

Corporate and personal insolvency update from Martin Ouwehand.

Corporate insolvency

***In Re Beloit Walmsley Ltd* [2008] EWHC 1888 (Ch) (His Honour Judge Pelling QC)**

Facts: The company entered into administration on 17 November 1999 and then a Company Voluntary Arrangement on 17 April 2001. The administrators were also the supervisors of the CVA. The company had exposed its employees to asbestos. The Financial Services Compensation Scheme Limited (FSCS) had been required to meet a number of personal injury claims made by former employees. The FSCS took an assignment of these employees' claims against the company.

Some of those with personal injury claims, but whose symptoms had arisen well after the CVA, would not be party to the CVA under s5 Insolvency Act 1986 (as it was before the recent amendments) because they would not have been given notice of the meeting approving the CVA. The administrators applied to court because they wished to exercise a discretion under the CVA to admit any such additional creditors to participate in the CVA so long as they could show their injuries had arisen by 22 November 1999 (the date that a liquidation would have occurred).

> "The FSCS's application was dismissed. The court had no jurisdiction to order the administrators to make a distribution that would contradict the terms of the CVA or to do anything that would lead them to breach the trust created by the CVA.

The FSCS had had to meet the claims of a further category of contingent creditors whose claims were based in tort and did not accrue until after 22 November 1999. They therefore opposed the administrators' application because these claims would be excluded from the proposed distribution and the FSCS would be unable to recover all of its loss. Among other things, the FSCS sought an order that would make the CVA funds available to these contingent creditors as well as the others.

Held: the FSCS's application was dismissed. The court had no jurisdiction to order the administrators to make a distribution that would contradict the terms of the CVA or to do anything that would lead them to breach the trust created by the CVA.

Comment: The creditors with purely tortious claims accruing after 22 November 1999 could not be defined as creditors of the CVA. The FSCS, however, relied on a term in the CVA that allowed the administrators to take such action as they see fit in order to protect the best interests of those concerned in the CVA '*notwithstanding that such action may differ from the course of action anticipated* [in the CVA proposal]'. However, the judge found that, read as a whole, this provision could not authorise the administrators to make distributions to those not contemplated by the CVA.

He held that the court does not have the power to direct a variation to the terms of a CVA nor does it have jurisdiction to direct a course of action that would involve a breach of the terms. The judge held that, if he was wrong on this point, the court could not authorise what would amount to a breach of trust in respect of the CVA.

Personal insolvency

***Official Receiver* v. *Gary Lee May* [2008] EWHC 1778 (Ch) (Mr Christopher Nugee QC)**

Facts: Mr May acquired a new Yamaha motorbike on hire purchase from Close Motor Finance for £5,699. He later fell into financial difficulty and sold the motorbike for £1,250 in cash to pay bailiffs. He did so without informing Close Motor Finance and at a considerable undervalue. On 18 December 2006, Mr May was made bankrupt and Close Motor Finance was left with a debt owing to them of £4,066.

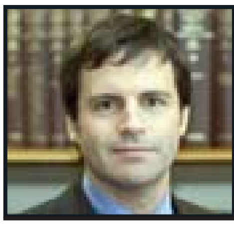
The Official Receiver applied to the Newbury County Court for a Bankruptcy Restrictions Order (BRO). Mr May did not dispute any of the allegations against him. The district judge found that his conduct was culpable but that it was an act of desperation and was unlikely to happen again. In those circumstances, she purported to exercise a discretion not to make the Order and Mr May was discharged. The decision was appealed to the deputy judge.

Held: Appeal allowed. The court had no general discretion as to whether or not to make a BRO once it concludes that the conduct of the bankrupt fell below the acceptable standard implicit in the statutory provisions.

Comment: The relevant provisions are contained in schedule 4A to the Insolvency Act 1986. Paragraph 1(1) provides that *'a bankruptcy restrictions order may be made by the court'*. Paragraph 2(1) provides that *'the court shall grant an application for a bankruptcy restrictions order if it thinks appropriate having regard to the conduct of the bankrupt (whether before or after the making of the bankruptcy order)'* .

The words *'if it thinks appropriate'* in paragraph 2(1) required the court to make a judgment by examining and evaluating the bankrupt's conduct to see whether it involved '*some element of misconduct or neglect or financial irresponsibility*'. Once this element was found then the use of the word *'shall'* in paragraph 2(1) compelled the court to make an order.

On re-hearing the application, the judge accepted that extenuating circumstances can be taken into account in evaluating Mr May's conduct, but found that it fell significantly below the appropriate standard: Mr May knew the motorbike was not his to sell and he exposed the finance company to the risk that they would recover neither their money nor the bike. In the circumstances, the deputy judge made an order for a period of two and half years.



Martin Ouwehand is a barrister at 11 Stone Buildings.

Legal Q&A

Kathryn Tait answers your insolvency queries.

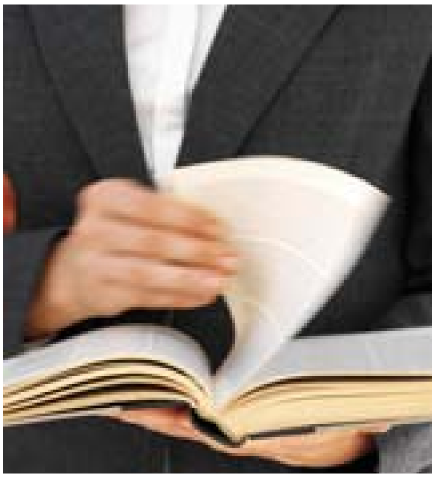
I was appointed as administrative receiver by a debenture holder; I have sold sufficient assets to repay the debenture holder and will be discharged shortly. However, a liquidator has now been appointed and has requested my files. Am I entitled to refuse?

The starting position is section 235 of the Insolvency Act 1986. As an administrative receiver you are obliged to give to the liquidator such information regarding the company and its promotion, formation, business, dealings or property as the liquidator may reasonably require. Further, you are under an equitable duty to account and provide information to the company, whether acting by its liquidators or not. Your failure to do so may entitle the liquidator to bring an application for an order under section 236 and/or a claim by the company for specific performance or damages for losses arising from your breach of the equitable duty. In either situation, you would be likely to face a costs' application if either succeeds.

To obtain an order for production of documents under section 236, the liquidator must show that the provision of the documents is necessary in the interests of the winding up and that production of

> "The judge was not persuaded that documents that had been paid for by the debenture holder should not be disclosed.

the documents should not be oppressive. It is established case law that the onus is on the liquidator to satisfy the court about the need for the documents. In situations where the respondent is an unconnected party the court will require more persuasion. However, in view of your fiduciary duties and statutory obligations to both the company and the liquidator, the court is likely to be willing to make the order. In *Re Pantmaenog Timber Company Limited* [2004] 1 AC 178, Lord Millett suggested that the only limitation in using section 236 is that it may only be invoked to enable the liquidator to exercise their statutory functions. If the liquidator can show that without the documentation they are unable to fulfil their statutory duties,



the court will probably make an order, unless the burden of providing those documents will be oppressive.

Will this include any documents relating to my fees and instruction I have received from the debenture holder?

This was one of the issues in the recent case of *Re Delberry* [2008] EWHC 925 (Ch). In this case the liquidator considered that the fees incurred in the administrative receivership were excessive and merited further investigation. During the course of that investigation other issues arose that required disclosure of various other documents. An application under section 236 was made, which the administrative receivers resisted on the grounds that the liquidator did not reasonably require the documents because they did not relate to Delberry's business and that the application was an abuse of process because an application to fix the administrative receivers' remuneration (section 36) was pending.

The judge was not persuaded that documents that had been paid for by the debenture holder should not be disclosed. Notwithstanding his observation, he did not agree that the identity of the person who bears the costs of preparing the documentation should affect the court's jurisdiction to make an order under section 236, so that this ground of rejection was refused by the judge.

I had understood that section 236 was not supposed to be used to put a liquidator in a better position in litigation, so that a liquidator would be unlikely to succeed if a decision to take court proceedings had already been made. However, I understand that in *Delberry* an application to fix the administrative receivers' remuneration had already been made. Is this correct?

This is correct. The administrative receivers argued that the liquidator wanted the documents simply to bolster the evidence in support of the application to fix the administrative receivers' remuneration. On the facts of *Delberry* the liquidator had written stating that, while the primary issue had been the remuneration, further investigations had disclosed other alleged failures by the administrative receivers.

The judge was clear in that although section 236 is not intended to give the liquidator special advantages in ordinary litigation, this principle is not a hard and fast rule. On this basis, in *Delberry*, the judge saw no reason why section 236 could not be used by a liquidator to support an application to fix the remuneration of the administrative receivers. The judge went further, referring to the expectation of the administrative receivers that they would have documents relating to the company's business and affairs and be under a duty to disclose them to a liquidator.

The judge distinguished the case of *Re Trading Partners Limited* [2002] BCLC 665, where it had been held that a liquidator should not use section 236 to obtain an insight into the strategic consideration for the receivership. In *Delberry*, the receivership was at an end and the liquidator wanted to investigate the circumstances of the sale of the company's business and assets by the administrative receivers. There were no competing claims by the administrative receivers or the debenture holder and, as the judge noted, it is important that the liquidator should have a comprehensive understanding of the company's affairs.

The overwhelming conclusion that is drawn from *Delberry* by administrative receivers, or indeed administrators, is that correspondence, communications, documents and notes of meetings must be prepared bearing in mind that they may have to be disclosed to a subsequent office-holder or indeed may come before a judge.

Kathryn Tait is a solicitor in the corporate recovery group at Boyes Turner.

Technical update

Richard Heis outlines a new code of ethics for insolvency practitioners and encourages IPs to study it before it comes into force.

On 1 January 2009 a new code of ethics will come into force for insolvency practitioners. The code has been produced by a sub-committee of the Joint Insolvency Committee, which represents all the insolvency regulatory authorities, and will replace the current *Guide to Professional Conduct and Ethics*. The production of the revised code has been a long and arduous process. Work began in 2005, and has involved extensive consultation with interested parties.

The need for a stand-alone guide for insolvency

The key feature of the new code is that it is based on, and follows the format of, the *Code of Ethics for Professional Accountants* produced by the International Federation of Accountants (IFAC). As all the UK accountancy bodies are adopting the IFAC *Ethical Code*, it was considered that this was the appropriate course to take. However, it did present the drafting committee with some challenges. As not all insolvency practitioners are members of one of the accountancy bodies, it was recognised that there remains a need for a stand-alone guide for insolvency. This raised the question of how the IFAC principles could be incorporated into such a guide in a way that would make them equally applicable to all insolvency practitioners while allowing the non-IFAC bodies to restrict their application to regulated work. At the same time, the guide would need to avoid unnecessary duplication and possible inconsistency with the IFAC *Ethical Code* adopted by the accountancy bodies. During the consultation, some respondents questioned whether the IFAC structure was suitable for the special circumstances of insolvency work at all.

The IFAC *Code* is a principles-based code, which adopts a framework approach. It begins by setting out a series of five fundamental principles to which all practitioners must adhere. The framework approach is a method that practitioners can use to identify threats to the fundamental principles and determine whether there are any safeguards that might be available to reduce or offset such threats.

The *Insolvency Ethical Code* attempts to deal with the problem of making this approach universally applicable by allowing alternative introductions for IFAC and non-IFAC bodies. For non-IFAC bodies the introduction sets out the five fundamental principles (which may be called the fundamental insolvency ethical principles, as in the current *Guide*) and discusses the threats and safeguards approach. An alternative introduction for the IFAC bodies would allow them to link to the main IFAC *Code* and set the remainder of the *Code* dealing with insolvency in the context of the main *Code*. The second part of the *Code* deals with the specific application of the principles in an insolvency context, with examples of circumstances that might give rise to threats and the safeguards that might be available.

Incidentally, the use of the word *code* to describe the document follows the terminology used in the main IFAC *Code*. However, the document does not constitute a set of rules and regulations, as the term code might imply. It is still essentially a guide, which sets out a series of directing principles and standards. Notwithstanding the adoption of the framework approach, the effects of applying the *Code* in specific circumstances are broadly the same as the effects of the current *Guide*.

> "The key feature of the new code is that it is based on, and follows the format of, the *Code of Ethics for Professional Accountants* produced by the International Federation of Accountants (IFAC).

The five fundamental principles

The five fundamental principles are:

- integrity
- objectivity
- professional competence and due care
- confidentiality
- professional behaviour

The *Code* explains these as follows:

Integrity: an insolvency practitioner should be straightforward and honest in all professional and business relationships.

Objectivity: an insolvency practitioner should not allow bias, conflict of interest or undue influence of others to override professional or business judgments.

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

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

Professional behaviour: an insolvency practitioner should comply with relevant >>

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

These are broadly similar to the fundamental insolvency ethical principles in the current *Guide*.

The *Code* then goes on to discuss the identification and evaluation of threats to compliance with the fundamental principles, which it divides into five categories:

- **Self-interest threats**: which may occur as a result of the financial or other interests of a practice or an insolvency practitioner or of a close or immediate family member of an individual within the practice
- **Self-review threats**: which may occur when a previous judgment made by an individual within the practice needs to be re-evaluated by the insolvency practitioner
- **Advocacy threats**: which may occur when an individual within the practice promotes a position or opinion to the point that subsequent objectivity may be compromised
- **Familiarity threats**: which may occur when, because of a close relationship, an individual within the practice becomes too sympathetic or antagonistic to the interests of others; and
- **Intimidation threats**: which may occur when an insolvency practitioner may be deterred from acting objectively by threats, actual or perceived

> Having identified and evaluated any threat to the fundamental principles, the practitioner should consider whether there are any safeguards that may be available to reduce the threat to what the *Code* calls an *acceptable* level.

Consider the safeguards

Having identified and evaluated any threat to the fundamental principles, the practitioner should consider whether there are any safeguards that may be available to reduce the threat to what the *Code* calls an *acceptable* level. The relevant safeguards will vary depending on the circumstances. Generally safeguards fall into two broad categories: safeguards created by the profession, legislation or regulation; and safeguards in the work environment. In the insolvency context, safeguards in the work environment can include safeguards specific to an insolvency appointment. In addition, safeguards can be introduced across the practice. These safeguards seek to create a work environment in which threats are identified and the introduction of appropriate safeguards is encouraged.

These issues are explored in greater detail in the second part of the *Code* dealing with its specific application in relation to insolvency appointments.

Generally, it will be inappropriate for an insolvency practitioner to accept an insolvency appointment where a threat to the fundamental principles exists or may reasonably be expected to arise during the course of the insolvency appointment unless:

- disclosure is made, prior to the insolvency appointment, of the existence of such a threat to the court or to the creditors on whose behalf the insolvency practitioner would be appointed to act and no objection is made to the insolvency practitioner being appointed; and
- safeguards are or will be available to eliminate or reduce that threat to an acceptable level. If the threat is other than trivial, safeguards should be considered and applied as necessary to reduce them to an acceptable level, where possible.

The *Code* then suggests various safeguards that might be considered, which might include, for example, the use of third parties on an assignment, Chinese walls, or terminating the relationship that gives rise to the threat. If the practitioner encounters a situation where the threat cannot be reduced to an acceptable level, he should not accept the appointment. Where an individual is specifically precluded by the *Code* from taking an appointment, a joint appointment would not be an appropriate safeguard, and consequently it would not be appropriate to accept the appointment.

IPs must be able to justify their actions

The *Code* goes on to discuss the obtaining of insolvency appointments (the payment of commissions remains prohibited), conflicts of interest, practice mergers, transparency, professional competence and due care, and record-keeping. It is important to remember that it will always be for the insolvency practitioner to justify his actions. He will be expected to be able to demonstrate the steps that he took and the conclusions that he reached in identifying, evaluating and responding to any threats, both leading up to and during an insolvency appointment, by reference to written contemporaneous records.

The *Code* deals with personal and professional relationships in some detail, but in a rather confusing way. One part of the *Code* deals in general terms with identifying relationships and evaluating whether they are significant to the conduct of an insolvency, while a separate part considers them in relation to specific circumstances. In this connection the concept of 'material professional relationship' has been abandoned and replaced with the concept of a 'significant professional relationship', the interpretation of which appears to be more subjective and open to the practitioner's own judgement. Although 'material' and 'significant' in normal parlance are often used synonymously, a subtle change has taken place. A practitioner's firm could have done a job for which they were paid relatively little, or indeed not at all, but that is still significant as it would have a bearing on their role as IP, for example, providing advice on wrongful trading. Similarly their firm could have done a much more remunerative exercise, involving something that is unlikely to have any bearing on the insolvency role and which had no connection to the reason for the company's predicament, such as a review of expatriate tax arrangements, and such a connection may not be deemed significant, even though it may previously have been seen as material. Some practitioners had already taken to thinking of 'materiality' in a wider sense, rather than focusing purely on size of fee, but the change provides a useful acknowledgement of this.

> The list of specific situations in which practitioners are required to decline an appointment, or are permitted to take an appointment in succession to a previous one, are broadly the same as in the current *Guide*.

The section of the *Code* dealing with the application of the framework to specific situations uses the framework approach to arrive at broadly the same conclusions as the annex of particular circumstances in the current *Guide*. For example, a practitioner should not accept an insolvency appointment where he or his firm have carried out audit work for the company within the previous three years. This is an example of a significant professional relationship that will preclude the taking of an appointment. Curiously, however, the *Code* does not discuss the provision of other types of services such as those which, under the current guidance, would give rise to a material professional relationship. Furthermore, the *Code* states that where audit work has been carried out more than three years previously, a threat to compliance with the fundamental principles may still arise, but it is for the practitioner to consider whether such a threat can be eliminated or reduced to an acceptable level.

As under the current *Guide*, appointment as an investigating accountant at the instigation of a creditor will not normally give rise to a significant professional relationship provided that there has not been a direct involvement by an individual within the practice in the management of the company or business, the practice has its principal client relationship with the creditor rather than with the company or proprietor of the business, and the company or proprietor of the business is aware of this.

The list of specific situations in which practitioners are required to decline an appointment, or are permitted to take an appointment in succession to a previous one, are broadly the same as in the current *Guide*.

Study the guide carefully

There is no doubt that there has been a need to review the *Ethical Guide* in the light of changes in the nature of the work undertaken by insolvency professionals. The adoption of a principles-based approach gives the *Code* the flexibility it needs for users to be able to apply the *Code* to the variety of situations they meet. However, there is a risk of confusion when familiar concepts are either rephrased or replaced with new ones, and the adoption of the IFAC structure, while understandable, does not always suit the circumstances of insolvency works.

Perhaps as a result of the IFAC provenance the *Code* is not a concise document and some might find its structure confusing. However, given the critical importance of getting the independence issues right, all members would be well advised to make sure they have read and digested the Code well before it comes into effect in January.

Richard Heis is a partner in KPMG Restructuring.

Technical Bulletin

Technical Bulletin 84 **was issued in October. Its contents included:**

- HMRC Claims Handling Unit – Change of Address
- New Address for VAT Returns and Payment – Deferred Implementation
- New Forms for Notification of Appointment of Liquidator – Northern Ireland
- Notification of Insolvency in Electronic and Other Media
- Display of Company's Name at its Registered Office and Other Locations
- Liquidator's Accounts – Scotland
- Administration Applications – Proposed Administrator's Statement
- Court Decides Between Competing Nominations for Administrator

Administrative Receivers' Duty to Obtain Proper Price
Availability of Orders for Disclosure under Section 236 of the Insolvency Act 1986
Annulment of Bankruptcy on Grounds of Payment in Full
Jointly Owned Property – Trustee in Bankruptcy's Right to Occupation Rent
Chapter 15 Recognition of Foreign Proceedings Denied by US Courts
Employers' Liability Insurance Policies
Federal-Mogul Aftermarket Judgment Now Reported

The banking industry is working to restore trust

Angela Knight maintains that lending is continuing but that the restoration of confidence and greater attention to risk management are needed to ensure a return to a more stable economic environment.

There are some mornings when it might be better not to switch on the radio. In fact just recently there have been too many mornings like that. We seem to wake up to fresh agonies every day, whether it is a bank going bust in America, Iceland grinding to a halt (the country that is), or here in the UK a massive state intervention to stabilise our banking sector.

Learning from our mistakes

In the UK we had an early indication of the problems to come when Northern Rock ran into trouble last September. Its business model relied too heavily on short-term borrowing from other banks, so when the inter-bank market dried up at the end of last summer it was left dangerously exposed.

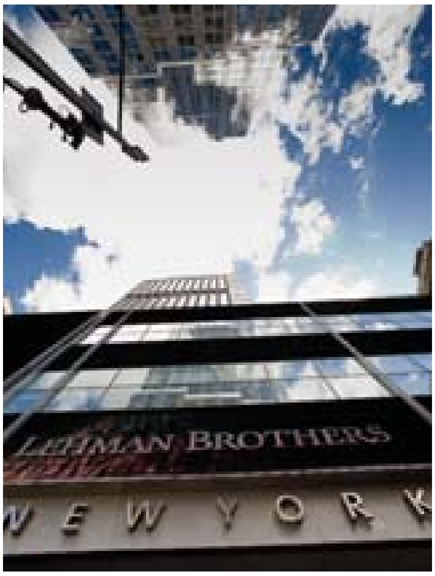
Following the run on Northern Rock, the UK authorities acted quickly to understand what went wrong and to put it right. And of course, since this is the UK, we did it all in public. No other country has addressed the issues facing the banking industry with anything like as much candour. All of us have learned a great deal in the process.

The economic downturn is a global phenomenon, and what we have seen in recent weeks is a concerted effort by the world's major economies to find a global solution. Much of this is yet to take place or has only partly been implemented, so time will tell how effective these measures will be.

Lending

But key among these measures for borrowers of all kinds – individuals and businesses – are the efforts to restore normal activity to that inter-bank market. The rates at which banks lend money to one another are still at historic highs, though they have been falling gradually at the time of writing. That cost of borrowing partly reflects and partly governs a bank's ability to lend to their customers, so much of the global activity at the moment is an attempt to drive these rates down.

All lenders have been affected by the credit crunch, but banks have continued to offer loans and mortgages more than many other lenders. Our latest figures show that the level of credit that banks have provided to small businesses has been holding up, while new mortgage borrowing has shrunk to around one-third of its usual size.



> "The banking industry is engaging actively to restore stability and confidence. The industry understands the concern and the worry and also what it needs to do to build back trust."

Over the 12 months to June 2008, figures from the main high street banks providing small business services show that term lending grew by 11 per cent to £44 billion and borrowing on overdrafts stood at £9.2 billion, some three per cent higher than a year earlier. Total deposits for small businesses stood at £54.5 billion, having grown six per cent over the year. Meanwhile new banking relationships had been established for 543,000 small businesses.

As part of its stability package for the banking sector, the government is requiring the banks in which it now has stakes to return lending to 2007 levels. If inter-bank borrowing costs continue to fall, good businesses will still be able to find competitive credit facilities.

But a full restoration of our economy is unfortunately some way off. We have lost what confidence we had in our institutions – in our banks, in our governments, central banks and treasuries, and in the international organisations who are supposed to be managing the accelerating globalisation of commerce. To restore that confidence will take some time and a great deal of effort.

Need to improve risk management

It is clear that one of the causes of the extraordinary events of these last 15 months is the failure by some in the banking industry to manage risk appropriately. But just because some banks have got into difficulty, certainly not all banks have and I know of no-one who works in the banking industry, or indeed in the financial services industry generally, that does not wish that situation had never arisen.

As the industry reviews both the causes and the consequences, it needs to ensure this type of problem does not happen again. The banks understand that there have to be changes in the way they do business and they are committed to making them. Some people ask why risks are taken at all. The answer is that all companies have to take risks, whether in banking or in any other area. It is about managing those risks well and making the key decisions – and also being prepared if something does go wrong.

It is the banking system that helps families buy houses, that helps businesses start and grow, and that is the fundamental pillar of economic development and prosperity. I quite agree that regulatory changes have to be made as the current regulations clearly did not spot the problems any more than some of the banks did. Equally as the changes take place it is also necessary to ensure they are proportionate and appropriate – over-regulation could constrain our economic recovery.

On all of this, the banking industry is engaging actively to restore stability and confidence. The industry understands the concern and the worry and also what it needs to do to build back trust.

Angela Knight is the chief executive of the British Bankers' Association.

Why is ABL attractive right now?

Peter Hayden explores the extent to which asset based lending (ABL) represents a highly appropriate source of finance in these difficult times and offers advice on the aspects that borrowers should concentrate upon when seeking such funding.

With the 20/20 clarity of hindsight, we are all by now deeply familiar with the severe consequences of the credit crunch and the significantly reduced availability of bank lending, which inevitably is matched by a flight to quality. Many customers in need of more funding will be all too aware that the credit bar has been raised. Until recently, an increase in facilities should not have been a significant problem for most businesses. Now the world has changed and banks are heavily constrained due to the hiatus in the inter-bank market.

The ever-tightening circumstances have driven liquidity down and expectations for credit quality and pricing markedly up. Some would say it was a long overdue correction and an example of a market simply reflecting the prevailing conditions. Others would argue that we are now enduring an over-reaction with otherwise healthy and solvent borrowers, be they personal or corporate, suffering unreasonably as a result of a broken, inefficient banking sector – all directly attributable to the excesses of the financiers over the last few years.

Why ABL is well suited to the present economic conditions

Figures recently released by the Asset Based Finance Association show that during the first half of 2008, the industry advanced over £17.3 billion against underlying security of invoices, stock, property and other trading assets worth a total of £31.2 billion. This represents a growth rate of 15 per cent. Traditional sources of funding grew by just 13.2 per cent in the same period. At present it is hard to gauge the effect that the recent disorder in the financial markets will have on the willingness of banks to lend in the medium term. Once the current disorder has abated and a more normal financial environment has been restored, it remains fair to say that the negative consequences of the current financial turmoil should be more muted among the asset based financiers (ABFs).

If existing or prospective ABL clients and their advisers understand why that should be, then they can focus on (and, wherever possible, strengthen) these key aspects prior to any negotiations with an ABF. This should maximise the chances of securing funding that might otherwise be unavailable to them.

Naturally, the ABL sector will not be immune since many players are bank owned and virtually all are dependent upon bank wholesale or back-to-back funding in one form or another. More acerbic commentators may wryly observe, perhaps with some justification, that over recent years prior to the onset of the current tightening of credit conditions some operators within the ABL sector have exhibited a degree of over-enthusiasm, in common with many others in the wider financial sector. This may sometimes have resulted in the provision of what may now appear to be very stretched facilities to corporate borrowers with a comparatively modest financial pedigree. Consequently, some ABFs may find themselves constrained in their ability to lend while they resolve the issues associated with such earlier lending but this observation does not apply to the majority of the companies in the ABL sector.

> “Figures recently released by the Asset Based Finance Association show that during the first half of 2008, the industry advanced over £17.3 billion against underlying security of invoices, stock, property and other trading assets worth a total of £31.2 billion.”

It is more important than ever to focus on the fundamentals

It is undoubtedly true that ABL has experienced similar challenges to those that have hit the other mainstream categories of UK lenders since the tightening of liquidity associated with the credit crisis first began to materialise in the third quarter of 2007. However, the ABL sector remains fundamentally sound as the facilities provided are asset linked, underpinned by professional valuations and protected to a greater extent by the more demanding collateral monitoring. As a result, ABFs remain vigorously active, although perhaps on a more cautious basis than a year ago. As a sector, ABL should not be as over-exposed, given the predominant focus on underlying asset values that sets ABL apart from mainstream business banking.

It is important to understand the drivers behind the changes that are now perceptible in comparison to last year.

Good quality book debts – the heart of most ABL propositions

It is important that the book debt is straightforward, allowing the lender to be confident that it will be readily collectable in the unfortunate eventuality of the borrower failing. The lender's confidence will be greatly enhanced if the assessments at audit reveal the book debt to be proven by a well organised documentation trail, including confirmation of delivery, and to be soundly administered by the receivables function within the borrowing business. Prospective borrowers will also receive more support from an ABF if their collection process is well established and stable, overdue debts are low and erosions resulting in the issue of credit notes are minimal. Timely submission of both invoices and credit notes and the regular reports required by the ABF have always been important but all the more so in today's market.

Poor debtor quality or over-dependence upon one or two customers, often referred to as excessive debtor concentration, may prove to be a significant barrier to a new borrower winning the desired level of support from an ABF. To illustrate this, if a business is reliant upon one debtor for, say, 40 per cent of its sales, should that business be lost or worse still the debtor fail altogether, the impact upon the ABL borrower will be profound. To some extent, trade credit insurance may serve to mitigate this concern but in today's market with insurers themselves experiencing some stress, it is reasonable to expect credit limits on troubled debtors to be reduced rapidly or pulled altogether. So credit insurance is helpful but cannot be a universal panacea to the challenge associated with a high concentration or an overall poor quality of debtors.

So the receivables element represents the most liquid, easily realisable of all ABL security and it is possible for borrowers to still enjoy a very full level of support from ABFs. As a result of the deterioration in the financial sector, and the likely knock-on effect in the wider economy, there may be some curtailment of the higher prepayment levels previously available on invoice discounting facilities. This probably will involve a shading of some five per cent down from the most aggressive levels available last year. There may also be a reduced willingness to grant overpayments unless supported by additional security or a very strong business case and appropriate fees commensurate with the additional risk undertaken by the lender in a very challenging credit market.

Taking stock

Turning to inventory (or stock) finance, the fundamentals are broadly similar but the parameters applied may be more cautious. Where last year there was a willingness to advance in the order of 70 per cent of the value of finished goods with some appetite to consider advances against raw materials (and even well understood WIP, in some instances) at present the approach may now be more cautious. Much will depend upon the confidence expressed in the professional valuation, especially where retail inventory and the ABL exit strategy will be directly related to the current state of the UK high street. Similar to receivables finance, a well administered stock control and integrated accounting system will be much better received than a business that is less rigorous in its inventory control.

Harder assets

The areas of plant and machinery and particularly property-related funding may potentially be more problematical as they are usually amortising facilities. As economic conditions continue to tighten, then the original valuations relied upon by ABFs may result in those property and P&M loans being overstated when the revaluations take place at the stipulated intervals. An ABF may seek an increase in capital repayments to bring the asset amortisation into line with any reduction in valuation perceived by the valuer. Naturally, this is a matter for discussion; rather than increasing monthly payments the lender may be willing to extend the period of the facility to avoid precipitating a cash-flow crisis that would not otherwise have arisen. Similarly, where a borrower is considering seeking replacement finance the issue of falling asset values may prove to be a hindrance as the levels of funding offered by an existing provider may be in excess of that offered by a prospective lender.

However, everything is negotiable. For the right covenant and if supported by a cogent and persuasive business case, cash-flow facilities or other forms of highly leveraged facility may well be available. Such a comprehensive ABL package may be crucial to fund a borrower through a seasonal downturn or to continue trading, notwithstanding the tough market conditions, but the availability of such additional ABL facilities may also be dependent upon the extent to which the current disruption in the global financial sector affects the wider economy.

“It is important that the book debt is straightforward, allowing the lender to be confident that it will be readily collectable in the unfortunate eventuality of the borrower failing.”

Some essentials

Notwithstanding current market conditions:

- The primary focus of an ABF is on the quality and adequacy of the underlying security.
- Incurring losses will not necessarily be a bar to a new ABL facility but, inevitably, sustained negative variance from plan will eventually impact upon an ABF's continued willingness to lend.
- Book debt represents the central, most attractive and liquid of all the usual ABL asset classes.
- Inventory remains similarly attractive although ABFs may be more cautious.
- Property and plant and machinery still represent sound ABL security, although the level of funding offered may be significantly lower than a year ago due to the fall in value of such assets.
- Refinancing may be difficult as a result of the fall in asset values as the existing borrowing may be too high.
- Sound administration combined with accurate and timely reporting will help strengthen the relationship with the ABF.

Money cost and fees are likely to be higher than a year ago, but may still represent good value if vital funding is secured in today's very difficult market.

While the availability of stretched facilities, over-advances or unsecured facilities will be curtailed, ABL should generate more funding than traditional sources of finance.

Peter Hayden is an asset based lending consultant working with MCR Corporate Restructuring.

The merits of private equity in an economic downturn

Private equity has responded to downturns before and has been successful in creating value. Simon Walker contends that the skills it brings to the table will be part of the economic future.

The private equity (PE) industry has gone through some major challenges and criticisms over the past year – like all industries in the limelight. But in the current financial and economic crisis, PE is one of the few sources of capital that is still investing and helping to keep the creaking economic machinery well oiled.

Private equity firms are still sitting on significant cash piles. According to Private Equity Intelligence, in the first half of 2008, global capital raised was almost unchanged at $232 billion (£184 billion) compared with the same period in 2007. A recent study by Preqin, the leading source of information for the alternative assets industry, estimates that buyout firms have some $450 billion of cash ready to invest.

Private equity success

Having worked through six downturns in economic cycles since 1978, PE has the ability to respond to changing market conditions; it is creative and flexible enough to keep re-inventing itself. It is one of the few sources of long-term capital that can be readily called on by companies in trouble – or can simply provide much needed liquidity. For example, in 1991 Cinven, the PE group, led the management buyout of Carpetland from the receivers of Lowndes Queensway. The company soon became profitable and in November 1993, with the help of further funding from Cinven's investors, it was able to merge with Allied Carpets, a larger operation than Carpetland itself, and part of Asda. Under the new name of Allied Carpets, the resulting group was the largest carpet retailer in the UK. The new company outperformed expectations and in July 1996 was floated on the London Stock Exchange. Only in February 2007 did Cinven's investors finally exit the company.

Private equity fixes and repairs companies. A recent example, occurred in the autumn of this year: MFI, the furniture retailer, was in financial trouble following the credit crunch. A deal was secured between MFI management and its owners, Merchant Private Equity (MEP). The buy-out was funded through a substantial cash injection from MEP, which secured deposits paid by customers. Most of the 2,500 jobs that were in jeopardy were also saved.

Longer term planning is important

To ride a period of economic downturn, it is important to plan ahead. And, it is a long-term investment that is best suited to those organisations such as pension funds, which always plan ahead. Many local authority pension funds have PE investments, as do a number of trade unions; one of the reasons why the TUC has issued advice on how to invest in PE. Private equity does not only bring cash injections to the table; it brings the right leadership for a company, provides strategic advice, shares their business know-how and contacts, and gives managers of their portfolio companies the freedom to get on with running and growing their business without the distractions of being a public company.

> In 2006/7 private equity-backed companies generated £35 billion in taxes – enough to pay for every nurse and police officer in the UK.

A study from June 2008 entitled *Corporate Governance and Value Creation – Evidence from Private Equity* by the London Business School and management consultancy, McKinsey, unveiled research on the creation of value in PE, based on a sample of 66 companies owned by 12 UK buy-out houses between 1996 and 2007. The research revealed that a deal's average internal rate of return was 35.6 per cent and more than half of this (19.5 per cent) was generated through operational improvement and a focus on margins and efficiency. There was no evidence that superior returns were achieved by asset stripping. Increase in capital expenditure was also demonstrated, as well as greater efficiency of capital employed.

More than this, the private equity industry contributes significantly to the wider economy accounting for £5.4 billion of the total revenue of the UK financial services industry in 2006/7. Private equity-backed companies generated £35 billion in taxes – enough to pay for every nurse and police officer in the UK – a fact highlighted in the BVCA's commissioned research on the *Economic Impact of Private Equity* launched in February 2008.

Future trends

Regarding trends of the future, distressed debt and turnaround funds are set to grow in importance. According to Private Equity Intelligence – global private equity funds raised $39.7 billion for distressed debt last year, more than ever before and this year's figures look set to beat that. It is estimated at the time of writing that close to $50 billion has been raised globally in 2008 for distressed debt funds.

Looking to the future, there is no doubt that the private equity industry will face a tough year in fundraising, as commitments to private equity funds are set to drop dramatically over the next 12 months as limited partners rebalance their portfolios and adopt a more cautious approach to investing following the turmoil that struck financial markets in September.

Whatever the turmoil still to come, given the magnitude of the current economic and financial issues, there is no doubt that the skills, discipline and capital that private equity brings will continue to be part of the economic mainstream in the UK, Europe and beyond.

Simon Walker is the CEO at the BVCA.

Adapting to the economic reality

UK mid-market or SME private equity investors recognise the reality of a sustained general economic downturn, which has yet to fully manifest itself. Michael Loizou explains the challenges and opportunities for existing and new investments.

While the challenges brought about by the credit crunch remain fluid, the past year has undoubtedly presented some common issues that impact on the private equity investor community. These include the weakening performance of underlying businesses (current and projected); the lack of availability and cost of debt funding; and a lowering of expectations on value and timescale of exit returns.

A downturn exposes weak businesses and funding structures, so the ability to recognise, control and improve the key income and cost drivers of the business as well as its working capital cycle become critical to riding the storm and future value creation.

The PE response

Some private equity (PE) investors will inevitably increase focus on their existing portfolio as previous unrelenting optimism is replaced with concerned attention to detail and micro-management. In some instances, the frantic search for a fallback begins. The experienced will promote a return to basics and focus on each investment's underlying core business, its reason for existence and how best to maximise its tangible opportunities. Investors may also pursue opportunities within their financially stronger portfolio companies, seeking bolt-on distressed acquisitions or increased market share from competitors submerged in crisis management. However, investors with businesses whose capital structure or business model are inappropriate face a period of nervousness as the lack of refinancing opportunities will lead to pressure to make additional equity injections, a possible distressed sale process or, in some instances, probable losses. Consequently, some PE investors will become far more cautious, retrenching and protecting existing investments and doing very little else until the worst blows over.

For equity investors who maintain an appetite and capacity to invest (and there are many), there should be a surfeit of investment opportunities, albeit with a recognition that a successful exit may require a more fundamental financial and operational focus than before. The difficulties in debt financing and the higher working capital requirements will lead to a greater equity requirement to fund an acquisition. Combined with the expectation that investors will need to hold the investment longer before any likelihood of a refinancing or exit, it is clear that the investment will need to be worked much harder to generate the returns needed to maintain targeted internal rate of returns. Added to the greater inherent business risk caused by the volatility of the economy, one can understand why there is a substantial fall in the value that investors are currently willing to pay for a business.

Investing in distress

Unsurprisingly, distressed investment opportunities are again in vogue. However, to deliver these, a PE investor must be more responsive to today's challenges, remaining enterprising and acting on opportunities speedily but with greater emphasis on managing commercial risk.

To invest successfully in distressed situations, improved internal discipline, processes and procedures within portfolio companies need to become part of the investor's day-to-day focus. It is vital that preventative and proactive measures in areas such as cash management, cost and asset appraisals are implemented, whether this is to achieve operational efficiencies or to dispose of non-core assets. The need for greater communication with key stakeholders of the business (and lenders in particular) is also important to maintain stability, support and find solutions to common interests.

> “To invest successfully in distressed situations, improved internal discipline, processes and procedures within portfolio companies need to become part of the investor's day-to-day focus.”

For many, the nuances of a distressed investment fall into the too difficult box. Due to the lack of time and reliable information available for distressed investments, together with the downside risk being too prevalent, it is often too easy for investors to say no to these opportunities. They may also recognise that they do not have the resources to be proactively involved in the investment. Additionally, institutionally raised funds not specifically focused on turnaround and distress may find their investment parameters prevent their participation. Thus investors in this area are more likely to be specific turnaround funds and high net worth individuals.

How can IPs help?

From our perspective, the merits of the hands-on active investor to complement a backable management team are obvious, as is the need to be able to obtain, where necessary, the specialist expertise of turnaround and insolvency professionals.

The constraint of limited time and information to the IP is understood by investors. However the earlier potential investors are shown distressed opportunities, the greater the chance that a deal can be done before the core business is beyond rescue. While a glossy information memorandum on a business is nice to have, getting a quick understanding of the detail, such as the cash requirement to normalise the business, the potential TUPE, pension, lease and other onerous obligations as well as access to management and key stakeholders, is far more likely to result in a successful purchase of the business and assets or of the debt. Some of the detail required by a distressed investor is little different to that of an IP deciding on whether or not to trade on an insolvent business.

We believe private equity should become an increasingly vital stakeholder in this downturn. It has been much maligned publicly during the boom times and perhaps now is the time for private equity to demonstrate more clearly its positive impact as a saviour of viable businesses, preserver of jobs and a key player in the underlying strength of the UK economy. With the help of the recovery fraternity, this is, in our eyes, an achievable and worthy outcome.

Michael Loizou is a partner at Ridgeway Capital LLP

Office-holders' conflicts

Rupert Connell maintains that the management of risk through the timely recognition and handling of conflicts of interest in formal insolvency procedures is all the more important in today's challenging economic climate.

The proper treatment and management of conflicts not only reduces the risk of office-holders and their firms being exposed to disciplinary action by their regulators, but it also reduces the scope for challenges and claims against office-holders personally, eg removal from office, damages, disgorgement of fees.

There is a heightened concern in today's climate, with more complex corporate structures and a greater diversity of stakeholders, that there will be a more aggressive approach to conflicts than has previously been seen. Conflicts can easily become an Achilles heel for office-holders and their firms if not properly dealt with.

A useful reference point is the challenge to the CVAs of the TXU Europe Limited holding companies. A group of bondholders applied to the court to have the CVAs of two of those companies set aside for unfair prejudice and their office-holders removed. They sought to make the issue of the prior advisory relationship of the office-holders' firm with the banks' steering committee, and the conflicts that existed between the group companies over which the office-holders were appointed, central to their applications.

In that case, reported as *Sisu Capital and others* v. *Tucker and others* [2005] EWHC 2170 (Ch), (*Energy Holdings*), Warren J decided that the conflicts facing the office-holders were not the central issue. And in juggling the unfair prejudice, removal and conflict arguments presented to him, he considered a number of judicial authorities on office-holders' conflicts as well as the confluence of those with the approach of the insolvency practitioners' licensing bodies (RPBs) to breaches of their own rules and guidance.

This article considers the conclusions that can be drawn from that case in the context of conflicts, and contrasts the different approaches of the courts and the RPBs.

The judicial approach

There is no shortage of examples of office-holders taking appointments over companies where their firms have previously advised creditors, eg banks, and one has to look back no further than the 1990s for some high profile examples of such cases. The propriety of appointments in these circumstances once again fell under the judicial spotlight in *Energy Holdings* where, not surprisingly, Warren J ruled that such a pre-appointment role should not, of itself, cause an office-holder to decline an appointment in respect of the debtor's group:

> *'It would be an overly strict application of the principles… to say that a professional who has previously advised a group of creditors about their position is thereby precluded from becoming an office-holder in any of the group of companies of which the debtor company forms part. The authorities show… that there is no such rigid rule and that there is a balance to be struck between the risk of bias and the advantages of having someone in office who is already familiar with the case, thus enabling a more efficient and less costly exercise to be carried out.'*

In reaching this decision, Warren J cited *Re Maxwell Communications Corporation plc* [1992] BCLC at 465, in which Hoffman J, commenting on the two eminent firms, Price Waterhouse and Touche Ross, stated that he had:

> *'no doubt that… office-holders appointed by the court … would in no way act in a way which favoured the banks at the expense of other creditors.'*

And referring to the judgment of Sir Andrew Morritt VC in *Re Barings plc* [2001] 2 BCLC 159, Warren J noted:

> *'…that conflicts within large insolvencies were common… and almost inevitable given* >>

the small number of large practices competent to deal with them.'

Moving on, it is possible, or even likely, that group companies over which office-holders are appointed will have claims against, or which compete with, one another. The treatment of these claims could materially affect the outcome for the creditors of each company *qua* that company. Some creditors, as in the case of *Energy Holdings*, may have claims against more than one company within the group. These may relate to the same debt, such as where a guarantee exists, or to different debts. Other creditors may only be interested in the office-holders achieving the right result for a single member of the group. See also *Re Bank of Credit & Commerce International SA (No 2)* [1992] BCLC 579 and *Re Esal (Commodities) Ltd* [1989] 59.

Over the years the court has shown that it is prepared in major or complex insolvencies to address conflicts such as these in a practical and commercial manner. The mere existence of intra-group conflicts should be no bar to an office-holder's appointment over several companies in the same group. At the outset it may not be practicable to assess what conflicts exist or how they should be managed. See eg Hoffman J in *Re Arrows Ltd* [1992] BCC 121:

'It is by no means uncommon in the case of the insolvency of a substantial group of companies for cross-claims and conflicts of interest to arise between companies in the same group.'

Indeed, in *Energy Holdings*, Warren J concluded that if, as was the case in *Re Arrows*, it was acceptable for the same individuals to act where there are potential conflicts, the existence of an actual conflict at the outset should also be no impediment to acting. This is subject to the proviso that the conflict is capable of being, and is, appropriately managed.

The proviso is important. See eg *Re Wallace Smith & Co Ltd* [1992] BCLC 970. In that case, the court declined to make an order that allowed the liquidators of one company to take an appointment over another member of the same group against which there was substantial litigation on foot. A further example can be seen in *Re Bi-Print Limited Ch* 22 June 1982 (unreported) in which Nourse J decided on the facts to make a winding-up order in respect of a company over which two partners of the same accounting firm had already been appointed liquidators by the creditors.

> "The mere existence of intra-group conflicts should be no bar to an office-holder's appointment over several companies in the same group. At the outset it may not be practicable to assess what conflicts exist or how they should be managed.

In both these last two cases there were substantial disputes as to claims between associated companies, more than just a prospect of a conflict, and the liquidators' role was to investigate or adjudicate those disputes that could lead, in effect, to them suing themselves.

It is therefore appropriate to distinguish between the position of an office-holder who has to determine a disputed debt between two companies of which he is an office-holder in a quasi-judicial capacity with that of an office-holder who, as in the case of a CVA, is merely putting forward proposals and who is not negotiating or agreeing anything. In the words of Warren J:

> "Conflicts can easily become an Achilles heel for office-holders and their firms if not properly dealt with.

'…an office-holder making proposals for a voluntary arrangement is not… adjudicating on the claims of creditors when putting forward proposals. True it is that he may, in the course of doing so, need to make some sort of assessment of the strength of competing claims in order to present a proposal which he considers to be fair. But it is for the creditors to vote on those proposals (so that, if anyone is making an assessment, it is the creditors) subject to the protection afforded by section 6 to a minority creditor.'

It would be over-simplistic to regard the treatment of the issues set out in this article as a panacea for every conflict situation. Ultimately cases will be decided on their own particular facts, but practitioners may be guided by points such as those touched on above.

The RPBs' rules and guidance

Of course, there are many other types of conflict that might affect an office-holder's ability to carry out his or her duties fairly and impartially. Insolvency practitioners will also need to consider their obligations under rules and guidance imposed by their RPB. The RPBs are required by s391 Insolvency Act 1986 to 'maintain and enforce rules' for the regulation of insolvency practitioners. This process is overseen by the Insolvency Service, an executive agency of the Department for Business Enterprise and Regulatory Reform (formerly DTI). The regime is underpinned by a Memorandum of Understanding setting out the principles and details agreed between the Secretary of State and the RPBs. This requires each RPB, among other things, to participate in the development of professional and ethical standards and best practice through the Joint Insolvency Committee (JIC). Once approved by the JIC, and adopted by the RPBs, these standards form the basis of the obligations expected of practitioners.

In *Energy Holdings*, it was argued that the office-holders were in breach of standards applicable at the time of their actions. The applicants also argued that this infected the process by which the CVAs (of two of the TXU Europe Limited holding companies, of which the Energy Holdings entity was part) had evolved. Consequently, they asked the court to find that such breach was sufficient, in itself, to render the CVAs unfair. However, the judge answered this question as follows:

'So far as concerns the CVAs, section 6 [Insolvency Act 1986] is the beginning and end of the case… The issue of conflicts and breach of ICAEW guidance come into the picture only insofar as (if at all) they are relevant to establishing unfair prejudice… I do not consider that the fact that an office-holder is in a position of conflict, even serious conflict, and that he is in breach of his professional rules are enough, by themselves, to establish unfair prejudice.'

The question… in relation to the CVAs is, ultimately, whether they unfairly prejudiced the applicants, not whether the process by which the CVAs were arrived at was fair.'

In *Re Polly Peck International plc* 3 February 1992 (unreported), Millet J drew a distinction between the interests of the court in the administration of insolvency processes and the rules and guidance of an RPB. He noted that the latter, by contrast, were concerned with the integrity and objectivity of the RPB's members. Also, in *Huxford* v. *Stoy Hayward & Co* [1989] BCC 421 Popplewell J stated:

'If as a result of a conflict of interest,

defendants were negligent in the advice they gave, then the plaintiffs have a cause of action as a result of negligence. … it is the quality of the [advice] not the reason behind it which is the question…'

Putting these two cases into the context of a CVA, Warren J said:

'In other words, the mere fact of conflicts does not necessarily result in unfair prejudice – indeed, if it did, any creditor would be able to block any CVA however reasonable it might be.'

So the existence of conflicts will always be a factor that the court will take into account which, as Warren J stated:

'may tip the balance where the court is uncertain whether or not the proposals are indeed fair.'

> Insolvency practitioners will also need to consider their obligations under rules and guidance imposed by their RPB.

But even if objection could properly be taken to an office-holder's appointment under a RPB's rules or guidance, it is clear from *Energy Holdings* that that would not, in itself, affect the validity of his appointment under the insolvency regime. Judge-made conflict rules, such as self-dealing or fair-dealing rules, must give way to the statutory regime of the Insolvency Act and the Insolvency Rules 1986 insofar as the validity of appointment is concerned. (Note, however, that the court may still make a winding-up order in relation to a company already in creditors' voluntary liquidation, as was seen in *Re Bi-Print Limited*, above).

The RPBs' approach

The RPBs might appear to be out of step, or even in conflict, with the courts, but, as Warren J identified, their role is not the same. The function of the RPBs is primarily to uphold the reputation, integrity and objectivity of the profession, so an office-holder could be exposed to disciplinary action even where the court has declined to disturb his appointment. So where, for example, a joint appointment might be acceptable to the courts as a way of managing a conflict, it might not, even with a practitioner from another firm, be enough to render an appointment acceptable to an RPB if a practitioner is specifically precluded under its rules and guidance from taking an appointment on an individual basis.

Breach of guidance will not always lead to disciplinary action, but insolvency practitioners who do not follow its provisions must be prepared to justify a departure. In the context of groups of companies, such grounds may, for example, in the case of ICAEW guidance in force at the time of the *Energy Holdings* case, be the recognition by the RPB that 'it may be impracticable for a series of different insolvency practitioners to act in the case of group situations where office-holders may encounter situations of conflict.'

Practitioners who may have placed some store on this example in the past will find it has not been carried into the new *Insolvency Code of Ethics* (*Code*) to be adopted from 1 January 2009 by all the RPBs to give uniformity to their approach to conflicts (see page 13). But while the *Code* provides some examples of what may constitute acceptable departures, it is left to every office-holder:

'to justify his actions… and to be able to demonstrate the steps that he took and the conclusions that he reached in identifying, evaluating and responding to any threats, both leading up to and during an insolvency appointment, by reference to written contemporaneous records… which should be sufficient to enable a reasonable and informed third party to reach a view on the appropriateness of his actions.' (Section 270).

In an interesting innovation, the *Code* suggests, as one of a number of safeguards to reduce the threats created by a conflict to an acceptable level, that an office-holder could seek the directions of the court. This raises a number of interesting points, not within the scope of this article, but more pertinently, on one view, assuming the court is prepared to give the desired directions, the *Code's* 'reasonable and informed third party' test (see above) would surely then be satisfied? However, the court seems unlikely to adopt an approach that would depart from its existing one as outlined above. Ultimately, therefore, the final decision as to matters touching the reputation, integrity and objectivity of the profession is likely to remain a matter for the relevant RPB, not the court, to decide.

> While the authorities show that the appointment and actions of office-holders need not be invalidated by the existence of conflicts, even where they might be in breach of the rules and guidance of their RPB, this does not mean that office-holders can ignore those standards.

Conclusions

The judicial authorities suggest a number of conclusions, which can be briefly summarised thus:

- there is a recognition by the courts that conflicts and cross-claims between group companies in large insolvencies are common;
- actual or existing conflicts are no bar to office-holders acting provided (a) the conflict is capable of being managed and (b) the management is put in place immediately;
- conflicts cannot be ignored. If something has been proposed as a result of decisions by persons in positions of serious conflict, it is 'even more important that the court is sure that there is no [unfair prejudice] if it is to refuse [the applicants] a remedy';
- resignation from one, or more, positions may not always be appropriate, for example, where a timely decision is required as to a complex and urgent matter;
- a number of different approaches may be appropriate depending on the facts, including, when a conflict is capable of being managed, the appointment of an additional partner from the same, or an independent, firm; obtaining separate independent legal advice; or seeking an appointment by the court of independent persons. The solution must be balanced by the need for the efficient and cost-effective conduct of the insolvency;
- in addressing a potential conflict the consequences of additional expense and delay must be balanced against leaving the matter to be dealt with when and if a potential conflict actually arises; and
- a conflict of interest may lead to a cause of action but it is not necessarily a cause of action in itself.

While the authorities show that the appointment and actions of office-holders need not be invalidated by the existence of conflicts, even where they might be in breach of the rules and guidance of their RPB, this does not mean that office-holders can ignore those standards.

The proper management of conflicts will remain a vital issue particularly for those concerned with insolvencies of groups of companies. This can be expected to become more acute in an environment where the role of financial stakeholders, each seeking to maximise their recoveries, is becoming increasingly prevalent.

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Don't forget about competition

IPs need to ensure they have a good understanding of merger control issues so that they can avoid competition issues when seeking to drive through a turnaround quickly.

Concentrate. Competition law issues may not immediately spring to mind when considering the potential pitfalls for a restructuring. Yet, merger control rules aimed at regulating the competitiveness of a given market can quickly become central to the success – or failure – of a deal. Without a basic understanding of when and how such rules might apply (and what you can do about it if they do), you may quickly find yourself experiencing delays or even, depending on the competition laws in force within a particular jurisdiction, the prospect of having to unwind a transaction. Ultimately, failure to appreciate the importance of merger control may present a stumbling block to the successful realisation of any remaining value in a distressed business.

Merger control rules require concentration

The purpose of merger control is to regulate the structure of a given market by ensuring that a concentration does not have anti-competitive effects. Broadly speaking, the concentration element required to trigger merger control rules is provided by a change in control or an ability to exercise influence. This will frequently be combined with a threshold test typically set on the basis of turnover, asset value, market share or a combination. Although the precise rules vary between jurisdictions, the potential application of merger control rules in contemporary restructurings should be clear.

Control does not necessarily require the acquisition of a majority shareholding. The UK merger control rules apply what is called a 'material influence' test involving an assessment of the acquiring party's ability to require the target's management to have regard to its interests. For example, a minority board representation or the acquisition of just a 15 per cent shareholding could be enough to confer material influence on an acquirer, particularly where the other shareholders are fragmented.

In a restructuring context, debt for equity swaps may require consideration of merger control rules. A lender may be looking for the potential upside should the restructuring prove successful. However, by swapping its debt for share capital (or some other form of equity instrument like a warrant or option), it may be acquiring control or the ability to exert influence over the debtor sufficient to trigger merger control rules. Even the enforcement of security may require attention if voting rights become exercisable as a result.

However, it is important not to overlook the preliminary step in any merger control analysis – that is to assess whether the rules of a particular jurisdiction actually apply. As the thresholds and tests differ, it is important to have a geographic breakdown of the target's turnover or whatever measure is applicable to the particular merger control regime. For example, China and Japan are among the few countries who apply an asset value test as the trigger – under the UK and US regimes it is the turnover of the entities involved. Further, it is just as important to recognise that the merger control regime of more than one jurisdiction may apply. Only after this analysis will the appropriate rules for the transaction become apparent.

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EC Merger Regulation and its one-stop shop

The EC Merger Regulation (ECMR) will have a role to play where the transaction concerns concentrations that have a community dimension. Even where there is no community dimension and the laws of a Member State apply, a national authority may decide to refer the matter to the Commission where it feels the concentration nonetheless affects trade between member states. This point could be overlooked, for example, where the assets of an insolvent UK company are divested to other UK companies.

Two sets of criteria must first be satisfied for the ECMR to apply:

> "Debt for equity swaps, insolvent business sales, changes to voting rights – the building blocks of many restructuring solutions – may all raise competition issues. However, the appearance on the horizon of merger control should not, if dealt with early and effectively, prevent the completion of a successful turnaround.

- an acquisition of control (the possibility of exercising 'decisive influence' over an entity); and
- the meeting of certain turnover thresholds.

The acquisition of control may even be triggered where sole control becomes joint control or vice versa. The decisive influence test is usually determined with regard to voting rights attaching to shares – either the acquisition of a majority shareholding (positive control) or the ability to veto or block a strategic decision (negative control). However, under EC competition rules there are no hard and fast rules and many of the tests are open to interpretation.

Concentrations with a community dimension will, however, benefit from the one-stop shop system – only the Commission's decision is required rather than clearance from the relevant authority in each member state. In a rescue situation, speed of implementation will often be vital in preserving value. The one-stop shop system may therefore be significant.

To notify or not to notify?

Some merger control regimes require mandatory notification to the competition authorities. The parties will be prevented from completing the transaction until they have received clearance from the relevant authority. Both the EC and US regimes are examples of a mandatory regime. Yet some regimes operate a voluntary notification regime – the UK is a rare example. Voluntary regimes allow the parties to complete the transaction in advance of (or even without having applied for and received) merger clearance. However, the merging parties run the risk of having to undo the transaction should it lead to competition issues. Particularly in a restructuring or insolvency context this would be disastrous.

The parties must generally notify the competition authorities where the transaction is likely to trigger merger control rules (unless it is voluntary to do so – although it will almost always be advisable). The timetable for this varies, as does the procedure. Under the ECMR, Form CO must be used. No implementation of the transaction can take place until the Commission gives clearance, which will require an extensive investigation. Failure to notify could lead to a fine of up to 10 per cent of the purchaser's worldwide turnover and, potentially, the transaction being unwound.

Once notified, the relevant authority may take a number of months to complete its investigation – this does not assist where time constraints can be so tight. Under the ECMR, the phase 1 investigation can take up to 35 working days with phase 2 taking up to 125 working days. So it is by no means a short period. It is easy, therefore, to see the importance of considering notification requirements early. In a restructuring situation, however, such time frames may sound the death knell to a successful turnaround. What can be done?

Getting around the issues

In some jurisdictions a 'failing firm' defence exists. This kind of defence allows a firm to merge with another where it either has failed or is about to fail, where no other purchaser provides a less anti-competitive alternative and where the assets would otherwise exit the market. It might be thought that this will assist. However, this defence is rarely successfully invoked and as such may be of little assistance.

Under the ECMR, in exceptional cases, the Commission will grant a derogation from the general suspension on implementing a transaction until clearance has been given. However, should there be a competition overlap between the acquirer and the target, for example where they are direct competitors, or even where the acquiring entity controls companies active in the same market, a derogation is unlikely.

Derogation in practice

Our own experience has shown the impact that merger control rules can have on an insolvency transaction. We acted for the purchaser in a pre-pack administration sale where it was necessary to obtain derogation from the obligation to suspend all dealings until we had clearance. We were successful in being granted the derogation within just three days of the application – apparently the fastest time derogation has ever been obtained. Our achievement in successfully cutting the time taken depended on the commitment of the case team involved and the manner in which they emphasised its urgency to the decision makers within the Commission. Although there can be no guarantee that the Commission will act as quickly next time around, given the right approach and contacts, it is now plausible to envisage a shorter timetable between notification and clearance.

In the particular case mentioned above, the Commission was adamant that the appointment of an administrator was not, of itself, sufficient reason for derogation from suspension to be given. The view was that derogation may be unnecessary since an administrator could sell the business as a going concern. However, we were able to convince the Commission that a going-concern sale would not be possible following the appointment of an administrator unless the sale could be conducted quickly – in effect, as a pre-pack, so as to avoid any adverse publicity. It was easy to envisage that should landlords, suppliers and customers of the company concerned become aware of the administration, this would have led to significant value destruction. The administrators would then have had to sell the business at break-up value only, leading to employee redundancies. Together with the fact that the business concerned owned very few real assets (for example it was trading from rented property), this helped convince the Commission that derogation was necessary so as to enable a quick, value-preserving sale.

Reaching the finishing line

Although merger control might at first seem an unlikely concern for restructuring and insolvency transactions, it should be clear that it would be unwise to ignore its importance. Debt for equity swaps, insolvent business sales, changes to voting rights – the building blocks of many restructuring solutions – may all raise competition issues. However, the appearance on the horizon of merger control should not, if dealt with early and effectively, prevent the completion of a successful turnaround. The key is to have a good understanding of the various merger control issues from the outset and to instruct advisers who have experience of dealing with the relevant competition authorities on a tight deadline.

You can stop concentrating now.

Tina Evans is an associate and Paul Sidle is a professional support lawyer in the Restructuring & Insolvency Group at Linklaters LLP.

You can bring that claim – with ATE insurance

Insolvency practitioners should reconsider the role that ATE legal expenses insurance can have in enabling them to pursue claims, as this can improve recoveries to the estate.

Funding an action

It is often the case that good claims cannot be pursued for lack of funding. This is particularly true in insolvency situations when there are insufficient funds in the estate and no creditors willing to fund claims from their own pockets.

To overcome this hurdle, a growing number of IPs have been working with specialist solicitors and counsel who are willing to act under a Conditional Fee Agreement (CFA), commonly known as a 'no win, no fee' agreement. A CFA effectively provides that the lawyer will not charge a fee if the claim is ultimately unsuccessful. If, however, the claim is successful, then the solicitor's fees and any counsel's fees are claimed from the loser (together with an uplift set at a rate that reflects the merits of the case and the risk that, if unsuccessful, the lawyers will not be paid). CFAs are permitted by the Access to Justice Act 1999 and regulations made under that Act.

Nevertheless, a CFA only helps with one part of the funding package: namely the IP's legal spend. The other part of the package relates to the costs of the opponent if proceedings are brought but the claim is unsuccessful – either because the case has had to be withdrawn or the case is lost at trial.

In litigation, the loser generally pays the winner's costs of any court proceedings. But having a CFA in place alone does not address the situation of the opponent's costs in the event that the claim is unsuccessful. If an IP brings a claim in his own name in his capacity as office-holder, he will be personally liable for such costs.

In order to complete the funding package where the IP's legal team are acting under CFAs, after the event (ATE) insurance can be taken out to cover the IP in respect of these opponent's costs. The IP should, however, check what is actually covered by the policy and the circumstances in which the policy will pay out (see point 2 below). ATE insurance can also cover disbursements associated with the claim, such as court fees.

ATE insurance can now usually be taken out without any money having to be found to pay for the insurance premium. The ATE insurer agrees, in the contract of insurance, that the premium is paid at the end of the case. Where the claim is successful, the Access to Justice Act 1999 allows the ATE premium to be recovered from the loser. Accordingly, the premium should be recoverable together with the solicitor's own costs, counsel's fees and other expenses associated with bringing the claim.

> "Where the claim is successful, the Access to Justice Act 1999 allows the ATE premium to be recovered from the loser. Accordingly, the premium should be recoverable together with the solicitor's own costs, counsel's fees and other expenses associated with bringing the claim.

If the claim is unsuccessful, then the premium – as one of the IP's expenses – is insured by the ATE policy. The net effect of this is that insurance protection can be obtained for the IP's claim without any financial outlay. This model has been used successfully for other types of litigation over the last nine years. It is a model that has been endorsed and approved by the highest courts, such as the House of Lords in *Callery* v. *Gray* (2002). In the case of *Rogers* v. *Merthyr Tydfil CBC* (2006) the Court of Appeal held that ATE insurance is a necessary expense that gives claimants access to justice and that any defendant seeking to challenge the level of premium charged would have to raise convincing arguments to do so successfully.

A typical case

Having investigated, an IP considers that there has been a transaction at an undervalue and that the opponent has the assets to meet any judgment and costs. Typically, the IP has no funds in the estate with which to bring a claim that would result in recoveries of around £150,000.

The IP and his solicitor agree that there is a good claim. The solicitor is obliged, both professionally and legally, to give advice in relation to the estimated costs of bringing the claim. This includes advising the IP about the consequences in the worst case scenario: namely of losing the trial. The IP is given an estimate of £50,000 for the solicitor's own costs and is advised that counsel's fees and court fees are likely to be an additional £20,000.

The solicitor then warns the IP that his opponent's total costs are likely to mirror his own of £70,000. Accordingly, if the case is commenced but is ultimately lost then the estimated downside is £140,000.

How to succeed

In such a case, no longer is an IP likely to throw in the towel. Today, given the merits of the claim, the solicitor is likely to be willing to act under a CFA and instruct counsel who is also prepared to do the same. Accordingly, there is no need to find the £70,000 for the IP's own legal team.

The solicitor is also likely to have an established relationship with an ATE insurer and will know that insurance can be secured with no financial outlay to his IP client. This cover will be for the opponent's costs to trial as well as for any expenses, including the ATE premium if the case is unsuccessful. Accordingly, the remaining exposure to opponent's costs and the premium is laid off by the ATE policy.

With this funding option, the IP is able to pursue the claim, if necessary by going to trial, and is likely to make a full recovery.

It can be seen that this business model enables the IP to run cases with limited or no funds at all. It unlocks litigation that otherwise would never be pursued because the financial outlay and the exposure to an opponent's costs are removed. IPs are not constrained by the traditional pay-as-you-go approach as they are offered as close to a 'no cost, no risk' solution as possible.

When considering whether to bring a claim, an IP needs to consider whether a CFA is appropriate (given the warnings of the judge in the recent case of *Segal* v. *Pasram*). However, it could be said, given his duty to maximise returns to creditors, that he now has a duty to consider whether any claim should be brought using a CFA backed with ATE insurance rather than on any other basis.

It should be noted that not all cases will be suitable for this business model. IPs also need to be aware that it is important to ensure that the proposed defendant has the means to meet any judgment and award for costs, as, in the event of a successful claim that turns out to be unenforceable (so a nil recovery) then the premium will usually remain payable (as, strictly speaking, do the solicitor's fees and uplift under the CFA).

Gaining the upper hand

Where a claim is funded by a CFA and an ATE policy, the claimant is obliged to notify the opponent of this. Tactically this has advantages for the IP. The opponent will know that the IP has the financial ability to run the case all the way to trial. This should give an opponent the incentive to try and settle early before the costs become too expensive.

However, opponents have tried to exploit the perceived weaknesses of the CFA and ATE insurance funding package in two ways.

1. Opponents would apply to the court in insolvency cases for a security for costs order, ie that the case should only proceed to trial if a significant sum of money (on average between 30–40 per cent of the defendant's estimated costs to trial) were paid into court. This can be an effective way for a defendant to stifle a case on the basis that it knows that the claimant does not have the funds to comply with any court order to pay over such security. Failure to comply with any security for costs order results in the action being stayed (ie held in abeyance) with the ultimate threat of the case being dismissed.

   In response to this need, a new policy now offers a bond (being as good as cash), which will allow IPs to comply with any such court order. The cost of the bond is only payable at the conclusion of the case. Once again, the IP's limited funds will not prevent him or her from obtaining the bond to see off this tactical challenge.
2. Opponents often try to see off a claim by issuing interim applications to the court in an attempt to secure a costs order against the claimant. These costs orders are normally payable within 14 days. Some ATE insurers only agree to pay the opponent's costs at the end of the case. This leaves the IP with the problem of finding the funds to pay any interim costs order and ensure the case proceeds. Ideally, cover for opponent's costs needs to include paying any interim costs order made in the defendant's favour as the case progresses to trial, as well as any final costs order that the defendant may obtain at the trial itself.

In summary

Historically, ATE insurance was associated with personal injury claims where claimants brought claims with their solicitor acting on a CFA.

As the market developed, ATE insurance changed and it is now available in relation to many more types of claim including mainstream commercial litigation cases and insolvency claims. Over time, through statute and case law, the process has been ratified and guidelines developed regarding the use of CFAs, the success fees payable under them and the level of the insurance premium that can be recovered from the losing party in the event of a successful claim.

The combination of a CFA backed with ATE insurance is, therefore, a valuable tool that IPs should ensure they understand and consider when deciding whether or how best to pursue claims with a view to maximising the return to creditors.

For IPs who are already using ATE insurance, it is probably worth comparing the policies now available as the market has changed considerably over the last two years and new products have been launched that are better tailored to meet their needs.

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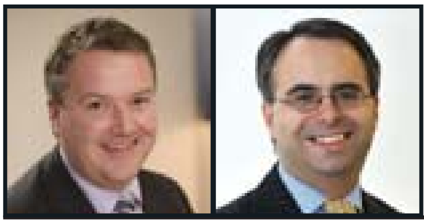


Theo Anderton (left) is a partner at Blake Lapthorn and Rocco Pirozzolo (right) is a solicitor and senior legal expenses underwriter at QBE Insurance.

Insolvencies of intermediaries and investment firms: The FSA's expectations

The FSA outlines what directors and IPs should do when authorised intermediaries and investment firms fail.

Since 2001, the Financial Services Authority (FSA) has been responsible for the regulation of the UK's financial services industry. The FSA's approach to regulation has regard to four statutory objectives: market confidence, public awareness, consumer protection and the reduction of financial crime. In the light of the current economic environment we think it's helpful to set out out our expectations when authorised intermediaries and investment firms fail. Similar considerations apply to all regulated firms.

The scope of regulation

To come within the scope of FSA regulation, a firm must first apply to be authorised in accordance with the provisions of the Financial Services and Markets Act 2000 (FSMA) and our Handbook requirements. As part of that process the firm must also apply for permission to carry on one or more regulated activities in accordance with Part IV of FSMA. Essentially, these Part IV permissions allow the firm to undertake certain types of financial services business. Before a firm is allowed to carry on a regulated activity we must be satisfied that it can meet and can continue to meet our minimum standards: Threshold Conditions and that the persons running the firm are fit and proper to do so. The firm and those running it should also have regard to our Principles for Business. These are a general statement of the fundamental obligations of authorised firms and reflect our four objectives.

Variation of permissions

Notwithstanding these objectives, the FSA does not purport to operate a zero failure regime. We recognise that actions taken by a firm may impact adversely on one or more of our objectives. By way of example, where a firm is deemed to be failing or likely to fail the Threshold Conditions then, unless the firm can rectify the situation, we will ask the firm to seek a variation of its permissions such that it is no longer permitted to carry on certain regulated activities. In the event there is resistance to a voluntary variation of permission then the FSA has the ability to compel a firm to vary its permissions. Alternatively, the directors or shareholders may decide, either of their own volition or through third-party pressure, that a firm is no longer viable or that they wish to withdraw from a particular sector of the financial services market.

For some firms this means that they will enter into an orderly wind-down on a solvent basis. (This is the preferred route from the FSA's perspective.) For others this is likely to mean that they have no alternative but to enter into some form of insolvency proceeding.

Formal insolvency proceedings

Where a decision is taken for the firm to enter some form of insolvency proceeding (including a members' voluntary liquidation) then the FSA should be notified prior to formal commencement. This is because the firm in question is still a UK-authorised firm and subject to our regulatory requirements. The nominee office-holder can verify if a firm is authorised by carrying out a search at **www.fsa.gov.uk/consumer**.

The point here is that Principle 11 of our high-level Principles for Business requires a firm to deal with us in an open and co-operative way. Compliance with Principle 11 includes, but is not limited to, giving the FSA notice of any proposed restructuring or reorganisation that could have a significant impact on the firm's risk profile or resources. (Our Principles apply to all regulated firms). The FSA should therefore be notified as soon as reasonably practicable of the proposed change to the firm's circumstances and certainly prior to taking any formal decision to appoint an insolvency practitioner (IP). Similarly where a firm is made the subject of a winding-up petition or is experiencing significant creditor pressure then the FSA would also expect to be notified of this and the steps being taken by the firm in mitigation.

Part XXIV of FSMA

The general law of insolvency applies to most financial services firms, however, Part XXIV of FSMA sets out the FSA's powers in relation to insolvency proceedings. These provisions establish, so far as is practicable, a common approach across all sectors. The FSA has the power to ask the court to initiate various insolvency procedures. It also has the right to be heard by the court in insolvency proceedings instigated by other parties and the right to receive information (including all notices or documents that are required to be sent to creditors) and to appoint a person to attend and make representations at creditors' meetings. How closely the FSA will want to be involved will depend on the seriousness of the situation for our regulatory objectives.

As the FSA has the right to be heard by the court in insolvency proceedings instigated by other parties, it has regard to the following matters in relation to the nominee office-holder:

- Do they have the right experience with regard to authorised firms?
- Do they have access to sufficient resource with the right level of experience?
- Do they have any conflicts of interest?
- Do they have the required level of integrity?

Notification

The proponents should therefore be prepared to explain to the FSA why a firm ought to be the subject of an insolvency procedure together with the reasons for the preferred choice of office-holder. Notification should be given to the firm's usual FSA relationship manager. Where the firm does not have a dedicated person in this role then, for investment and intermediary firms, notification should be given to the Firm Contact Centre in the first instance.

IPs are reminded that an administrator may not be appointed by the firm or its directors under paragraph 22 of Schedule B1 of the Insolvency Act 1986 without the consent of the FSA. The nominee administrator should therefore advise us of the proposed appointment, preferably in writing. Consent by the FSA must be given in writing.

Where a firm is to be put into an insolvency procedure we will need to give consideration to whether all or any of its remaining permissions should be removed in their entirety or have a limit or restriction put on them. Accordingly, where it is proposed to put the firm into administration then the FSA may want to understand why this is more appropriate in the context of its regulatory objectives than putting the firm into liquidation. For instance, will administration allow the sale of all or part of the business and thus minimise consumer detriment? In such a case, in order to facilitate the process the firm would need to retain one or more of its Part IV permissions. Alternatively, if there is no prospect of the firm continuing to trade then liquidation might be seen as the better option in which case the firm's permissions should be removed.

FSA building

Change of control procedures

A sale of all or part of the business by way of a transfer of shares will be subject to the FSA's change of control procedures. It may be possible to complete the change of control on an expedited basis provided the necessary relevant criteria can be met. This is of particular relevance where a sale (perhaps in a pre-packaged administration) is likely to mitigate loss and disruption to consumers. If an aset or share sale is a potential option this is should be communicated to us as soon as possible.

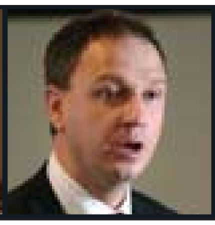
Where it appears that the insolvent firm has carried on a regulated activity when not authorised to do so, the office-holder must report the matter to the FSA without delay. By the same token, the insolvency practitioner must always ensure that the firm has the correct permission under FSMA to carry out a regulated activity before any business is continued. This is because, while the office-holder is personally exempt from sanction by the FSA and is not required to be an approved person, the firm remains subject to FSMA.

Notification of the FSCS

Where the failed firm has protected eligible claimants, then the Financial Services Compensation Scheme (FSCS) must be notified that the firm is in default and that it might be required to pay compensation (up to statutory limits) for any loss suffered. The FSCS in turn will have a claim in the insolvency in respect of any such amounts. Accordingly the IP will be required to liaise with the FSCS, although the FSA will also liaise with the FSCS about the conduct of the insolvency and expectations for claimants.

Once all assets have been realised (including by way of a sale of the books and records or through a change of control) claims adjudicated and a dividend paid (where there are funds available to do so) the office-holder can seek to be released, and should notify the FSA accordingly. This is so that any remaining Part IV permissions can be cancelled. Steps can then be taken to de-authorise the firm.

In summary, as soon as an IP becomes aware that a firm is contemplating an insolvency process, reorganisation or restructuring this should be communicated to the FSA forthwith having regard to the requirements described above. If there are any concerns about the steps to be followed then please contact the firm's usual FSA relationship manager or the Firm Contact Centre.



Beth Rees is a technical specialist and John King is manager at the Financial Services Authority.

Checklist of employment issues for administrators

Maya Cronly-Dillon **identifies the employment legislation that needs to be at the forefront of an administrator's mind.**

Adopting employment contracts

Should an administrator adopt any employment contracts? The administrator will be taken to adopt employment contracts if these are continued beyond 14 days after the administrator's appointment. Relevant considerations might be:

- Can a disposal be achieved within the 14-day period?
- If so, might some or all employees transfer to the purchaser automatically under TUPE (Transfer of Undertakings (Protection of Employment) Regulations 2006) thus avoiding the need either to dismiss or adopt at all?
- If not, how key are the staff to the value of the business and its recovery?
- The wages and salary of staff whose contracts have been adopted will have 'super priority' and rank ahead of outstanding claims for the administrator's own fees and expenses if unpaid when he or she leave offices. Will there be sufficient assets to meet both liabilities?

Evaluating the impact of TUPE

Understanding how TUPE applies to an insolvent business can be important in determining the price of assets and how they are marketed. If the business is subject to bankruptcy proceedings or insolvency proceedings, which are instituted with a view to liquidating assets, then a number of key provisions of TUPE (automatic transfer of employees/employment liabilities and automatic unfair dismissals) are disapplied making it possible to sell the assets alone.

However, in the case of an administration (assuming it is unlikely to have been instituted with a view to liquidation of the assets) the following applies.

- Employment contracts and liabilities will transfer but some of the existing debts to the employees are met by the Secretary of State out of the National Insurance Fund (subject to certain limits) rather than passing to the buyer.
- The usual restrictions on varying employees' terms and conditions in the context of business transfers are relaxed to a very limited degree.

Minimising employment liabilities

Consider how to avoid increasing employment liabilities where possible. Where these transfer to a buyer under TUPE, they will impact on the purchase price. If they remain with the company, unless they can be claimed from the National Insurance Fund, they will dilute the assets available for creditors generally. The main areas of risk are considered below.

Information and consultation

Identify what information and consultation obligations are relevant as significant sanctions can be levied for non-compliance with the requirements to inform and consult under:

- TUPE – about the impact of a business sale on employees before the transaction completes – the sanction for non-compliance is an award of up to 13 weeks' pay per employee, liability for which is joint and several as between transferor and transferee
- TULRCA – (Trade Union and Labour Relations (Consolidation) Act 1992) – where an employer proposes to dismiss as redundant more than 20 employees at one establishment within a 90-day-period – the award for failure is up to 90 days' pay per employee.

Consider what effect potential sanctions for non-compliance might have on the value of the business. This will depend on how many employees are affected and their salary levels. Consider what resources are available (eg are there experienced HR/communications people who can assist?). Check whether any competent consultative machinery already exists that avoids employee representatives having to be elected.

In light of any time constraints, how might these resources be best deployed? Would an attempt to achieve partial compliance with these obligations realistically reduce the maximum exposure? Provide as much of the required information in writing as soon as possible to appropriate employee representatives. If there are no post-transfer measures envisaged by a buyer, there may be no need to consult under TUPE.

Consider seeking an undertaking from a buyer not to claim the £500 minimum award per transferred employee to address any possible non-compliance with the obligation under TUPE to provide the buyer with 'employee liability information' at least 14 days before completion plus an indemnity if they were to claim.

Redundancies and unfair dismissals

Notify the Secretary of State within the time frames required by TULRCA where collective redundancies are contemplated to avoid criminal personal liability. Keep a written record of any procedural steps/relevant discussions and comply with appropriate dismissal procedures so far as possible to reduce the risk of unfair dismissal claims.

Keep a written record of the rationale behind any pre-transfer dismissal, especially where there is a proximate business transfer. This can bolster arguments that a redundancy was genuine and so not automatically unfair under TUPE. These records can be disclosed to a buyer during due diligence and may keep their assessment of employment exposures within realistic parameters.

Employment litigation

It is usual to consent to a request to lift the automatic stay in proceedings where a tribunal ruling is required for an employee to validate their claim in the insolvency unless the claim has no prospect of success.

Is it worth fighting proceedings where there is an arguable defence? Consider these points:

- The extent to which a successful claim might affect recovery for other claimants
- Whether the compensation recoverable by a successful claimant is less than the cost of defending a claim?
- Whether a low value claim might set an unhelpful precedent triggering more valuable claims?

Consider negotiating a temporary deferral of part of the purchase price rather than a reduction to address contingent employment liabilities that a buyer might inherit. Avoid giving advice to employees to avoid the risk of negligent misstatement.

Maya Cronly-Dillon is a senior associate in the employment group at Lovells LLP.


Wilsons Auctions' bespoke Mallusk site


Tractor auction

Auctioning of assets

The most transparent means of selling and the most efficient way to dispose of assets in today's economic climate.

The topic of the majority of conversations over the past number of months is the economic downturn and how hostile this is for businesses. With this severe change in the market we are seeing, and almost certainly will continue to see, an increase in the number of insolvency cases coming through. Businesses ceasing to trade is never a pleasant thing to experience, however, it is something that has to be dealt with and Wilsons Auctions know how to handle such cases to the highest possible standard. Whether it's a car, piece of machinery, a property or office furniture we know now, more than ever, is the time to be sticking to 'auctioning of assets'. Why is that? For a multitude of reasons.

Transparency

The most important of all reasons is the transparency that an auction provides. If an asset is put to public auction, it shows that it has reached the true market value on that particular day and every single member of the public has been given a fair chance to purchase the asset, therefore eliminating bias. No judge in the land can question that.

Rapid liquidity

The quicker that assets are transformed into cash the better as, in the downturning climate, the value of assets is constantly changing. Therefore an auction provides the ideal outlet to turnaround the asset into capital swiftly.

Competitive bidding

When an asset is put to public auction this means that it is open to everyone. Usually there will be more than one person interested in each lot on sale, therefore competitive bidding comes into play. This in itself has the potential to increase the selling price of the asset.

"Throughout all our branches in the UK and Ireland we provide the complete asset disposal service for all insolvency practitioners, whether it's a simple desktop valuation, securing an asset or the disposal of anything from 'property to the paper-clip'.

Pro-active marketing

The market today requires pro-active marketing, so for every single auction we hold we utilise our multi-functional marketing strategy. This means we promote to our vast national and multinational customer database to inform customers of the assets for disposal via e-mail, text message, bespoke website (**www.wilsonsauctions.com**), mail shot, national press, relevant asset-specific publications as well as direct customer contact.

By Roman times, the process of selling by auction had come to be recognised as the most convenient and equitable method of disposing of assets in the best interests of buyer and seller. We at Wilsons Auctions are still proving this to be the case.

In every auction we hold we utilise emotion, enthusiasm and psychology to generate excitement therefore heightening buyer interest to maximise the return to all our vendors. Modern auctions are no longer a sale of last resort – rather an efficient, proven marketing and disposal method.

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Rebecca Wilson is head of corporate services at Wilsons Auctions.

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The value of the insolvency industry

An R3-sponsored report demonstrates the important role played by the insolvency industry in the economy.

R3 has sponsored a report conducted by cebr (centre for economics and business research ltd) to evaluate the direct and indirect contribution of the insolvency sector to the United Kingdom's economy. Historically, the role and significance of the insolvency industry has been underplayed. Rarely has it been reported that the industry performs a vital wider role in creating an environment that balances the interests of creditors and debtors so as to be conducive to entrepreneurship and risk taking, as well as providing expertise and a service for businesses and consumers facing financial difficulty. The cebr report quantifies the number of businesses and jobs saved by the industry, and places the UK insolvency regime in a global context. In nearly all cases the findings were overwhelmingly positive.

What the statistics show

Beyond the traditional role of ensuring a fair, efficient and quick redistribution of assets, 67 per cent of insolvency practitioners' organisations are involved in the restructuring or turnaround of companies. The report also concluded that an insolvency practitioner, working on average 43 hours a week, will typically spend 20 hours (48 per cent of their working week) on formal insolvency procedures and 7 hours per week preventing insolvency.

The report estimates that the direct contribution of the insolvency sector is approximately 12,700 jobs, while its gross value added is £780 million per annum (0.08 per cent of the national economy). In addition, the insolvency industry's purchases from suppliers and spending by its employees accounts for a further £417 million of national output.

The indirect contribution is as significant, with the insolvency sector taking a key enabling role by encouraging entrepreneurship, balanced by safeguards for creditors. A functioning insolvency regime is essential to generate ease of doing business, which links to the prosperity of a country. Of all the 39 indicators reported on by the World Bank, the recovery rate when a business is closed (ie the pence in the pound recouped by creditors through the bankruptcy or insolvency proceedings) is the most strongly correlated to a country's prosperity (measured as gross domestic product per capita). The time it takes to close a business is also strongly related. Likewise, the recovery rate and speed of closure are also strongly correlated to rates of investment in an economy and overall rates of economic growth. These findings highlight the importance of the insolvency regime in delivering a robust economy.

Performance against other jurisdictions

The United Kingdom's insolvency regime performs well on these measures against other jurisdictions. The United Kingdom is ranked tenth out of 175 countries for the amount recovered for creditors when a business is closed; it is successful in recovering an average of 85 per cent of assets when a business closes. It is ranked ninth quickest in the time taken to close a business with the average time taken being one year. In both cases this is above the US.

Jobs saved

Media reporting on insolvency cases tends to focus on jobs lost rather than jobs saved in a business with financial difficulties. The report showed that the companies put through formal proceedings had an average of 25 employees before the process began and 18 employees when the process was completed; so, on average, 72 per cent of the workforce was retained (or saved) after formal insolvency.

This equates to a total number of jobs saved through formal insolvency proceedings of 312,000 in 2006 in corporations alone. A further 3,300 business were saved through rescue procedures in 2006. Although fewer firms go through rescue rather than formal proceedings, they are typically bigger. These companies have an average of 220 employees before the rescue procedure begins and, after the rescue has been completed, an average of 80 per cent of staff remaining in employment. The report estimates a total of 598,000 employees were saved through rescue procedures in 2006.

Considering rescue procedures, as well as formal proceedings, the cebr report estimated the industry was responsible for saving 910,000 jobs in businesses with a combined turnover of £132 billion per annum in 2006. Now that would be a headline: 'Insolvency practitioners save jobs'.

Amount recovered when a typical business is closed

(Top twenty out of 127 countries plus other key economies, 2007)

Rank	Country	Recovery rate (%)*
1	Japan	92.7
2	Singapore	91.3
3	Norway	91.1
4	Taiwan	89.5
5	Canada	89.3
6	Finland	89.1
7	Ireland	87.9
8	Belgium	86.4
9	Netherlands	86.3
10	**United Kingdom**	**85.2**
11	Korea	81.8
12	Australia	79.7
=12	Iceland	79.7
14	Hong Kong, China	78.9
15	Spain	77.6
16	United States	77.0
17	Sweden	75.7
18	Portugal	75.0
19	Austria	73.7
20	Denmark	70.5
…	…	…
28	Germany	53.1
32	France	48.0
49	Italy	29.7

Source: World Bank and cebr analysis, 2008

* Note: Recovery rates quoted are based on the outcome of a specific scenario developed and consistently applied by the World Bank. It is not a measure of average recovery rates across each jurisdiction. Indeed, we recognise that average recovery rates in the United Kingdom are much lower than this specific example.

Will Black is the communications manager at R3.

Tracking GB's personal debt

The *YouGov Quarterly Debt Tracker survey* is helping R3 to build up a picture of the reasons for personal debt, trends for the future and information about how people view DMPs and IVAs.

YouGov, the leading independent polling agency, in consultation with R3, has just completed major research into personal debt. Between 31 July and 5 August 2008 the 'debt tracker' surveyed a random sample of 3,329 adults, and a second group of 2,100 adults who said they were 'in financial difficulty'. The survey covered a very wide range of questions relating to their personal financial circumstances, including what borrowing they had, what they expected to have and, exclusively to R3, asked detailed questions to those in DMPs (Debt Management Plans).

DMPs and IVAs

The general attitudes to personal debt were illuminating and in many cases troubling (less than half of those in serious financial difficulty have sought professional help to sort out their financial problems for instance) but the work on DMPs was groundbreaking. For the first time ever, the survey indicates the high number of DMPs in Great Britain.

Based on the four per cent of respondents who said they were in a DMP and known official statistics for IVAs and bankruptcy, it was estimated that around 600,000 adults in Great Britain would currently be in a DMP. The four per cent who said they were in a DMP were four times the number who said they were in an Individual Voluntary Arrangement (IVA), and twice as many as those who said they are currently or have been declared bankrupt. R3 is concerned DMPs are being used as an out of sight 'parking lot' for debtors, and has long called for them to be included in official statistics.

Concerns about DMPs

'A DMP can be a good option for individuals who have manageable levels of debt, which can be paid off without entering into a formal arrangement. The benefit of the DMP is that it does not have as severe an effect on the person's credit rating. However, R3 has serious concerns as these plans can be prolonged,' explained Nick O'Reilly, president of R3.

Unlike an IVA or bankruptcy a DMP does not have a set duration. The survey reveals that 19 per cent of people currently in a DMP believe the arrangement will last over ten years, and an even more alarming 29 per cent do not know how long it will last.

There is cause for concern that these informal arrangements have the potential to turn into a life sentence. The desired outcome is to give people whose debts have become unmanageable a sense of control back. In the cases where individuals do not know how long the arrangement will last this goal does not appear to have been met.

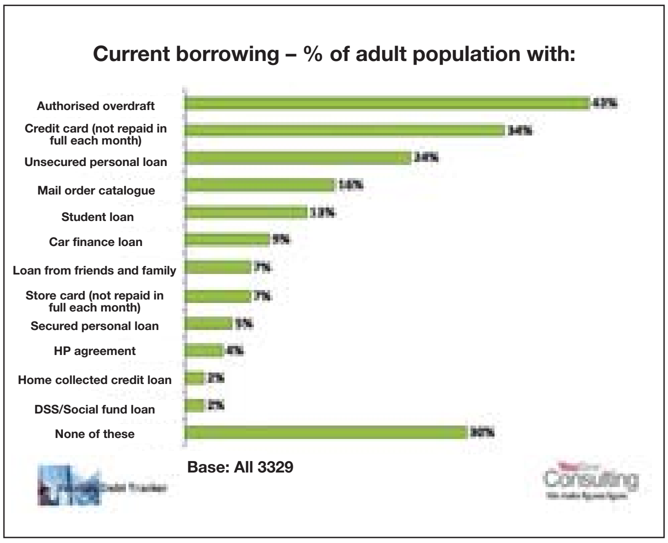
One third of DMP holders responded that they had not considered an IVA because they did not know what an IVA was. Everyone in a DMP should have had all of their options explained to them in order to ascertain the best arrangement for them.

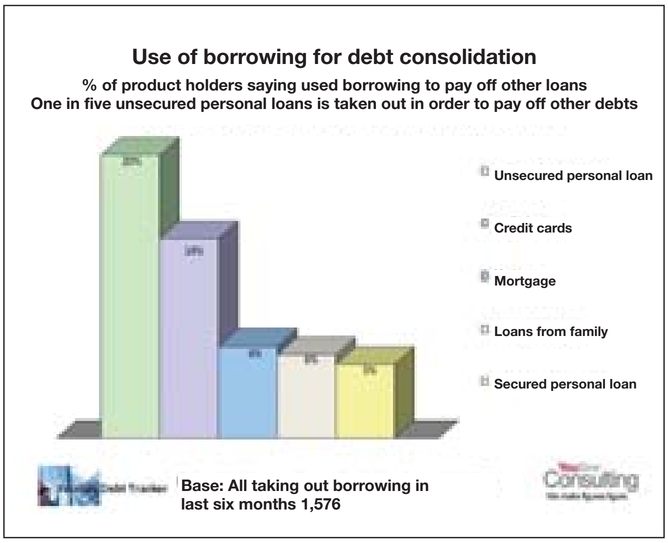
The top three causes of personal insolvency were seen as:

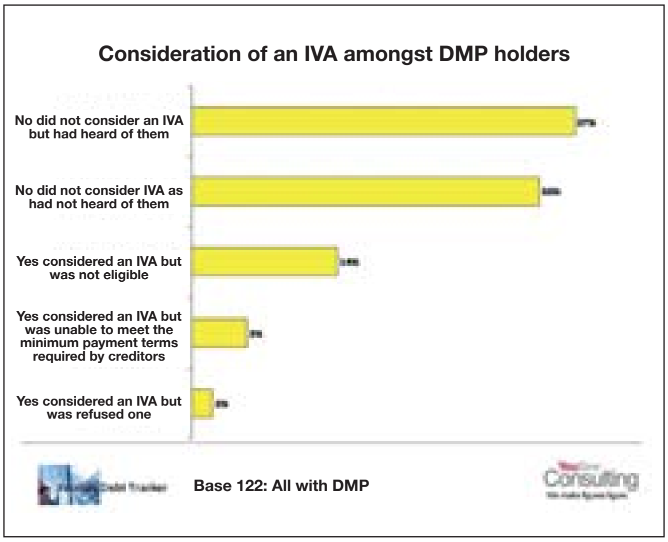
- misuse of credit cards
- borrowing without thinking about how to repay the money
- irresponsible lending by credit providers.

This largely coincides with the responses IPs gave when asked the same question in the R3 members' quarterly survey. The work with YouGov will be repeated quarterly to build a more sophisticated picture of personal debt in GB. These initial findings were written up in *The Times* on 25 September in an article entitled 'Management plans mask soaring level of debt'.

Will Black is the communications manager at R3.







R3 events, courses and conferences

Date	Event title	Venue
December		
1	North West Regional Meeting	
2	South West and South Wales Regional Meeting	
4	Southern Regional Quarterly Meeting	
9	Introductory Programme – Partnership Insolvency	etc Venues, London
9	Introductory Programme – Partnership Insolvency	Deloitte, Birmingham
11	Introductory Programme – Partnership Insolvency	Irwin Mitchell, Leeds
11	Employee Issues and Pensions	Thistle Hotel, Bristol
11	Buying a Business	Thistle Hotel, Bristol
January		
20	Introductory Programme – Introduction to Insolvency	etc Venues, London
20	Introductory Programme – Introduction to Insolvency	Deloitte, Birmingham
22	Introductory Programme – Introduction to Insolvency	Irwin Mitchell, Leeds
29	London Women's Group Talent Night	
31	Yorkshire Annual Dinner	
February		
3	South West and Wales – Regional Meeting	The Bristol Golf Club
5	Trading Insolvencies	Chase Hotel, Cheltenham
18–21	19th Annual Conference	Grand Hotel Kempinski, Geneva
24	Introductory Programme – Personal Insolvency 1	etc Venues, London
24	Introductory Programme – Personal Insolvency 1	Deloitte, Birmingham
26	Introductory Programme – Personal Insolvency 1	Irwin Mitchell, Leeds

For further information on R3 courses and conferences, please visit the R3 website **www.r3.org.uk**, where you can download the full 2009 programme. Alternatively, call the Courses team on 020 7566 4234 to request a programme by post.

regional events R3 events

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- an invitation to the R3 annual conference
- a copy of *RECOVERY* every quarter
- the 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
- access to the members' section of the R3 website.

Subscriber membership is open to people who are not insolvency practitioners, lawyers or students but who have an interest in the world of business recovery. Benefits 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
- a copy of the *R3 Directory*.

For more information on R3 membership, please call 020 7566 4238 or e-mail **membership@r3.org.uk**.

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

Sponsor of appointments' section: Michael Page.
Inserts: Sweet & Maxwell

Industry announcements

BAKER TILLY BOOSTS NORTHERN TEAM

Russell Cash and Don Bailey have joined the Manchester office of Baker Tilly's restructuring and recovery team.

Lindsey Cooper, restructuring and recovery partner at Baker Tilly in Manchester said:

"As well as complementing our existing offering, Russell and Don are both high profile figures with an excellent track record. With them both on board, I'm confident Baker Tilly's restructuring and recovery unit has a solid platform to realise the growth ambitions it has in the North West."

Russell moves to Baker Tilly as partner from PricewaterhouseCoopers where he spent the last 16 years working on turnaround and insolvency assignments across the North West. He has advised businesses from a wide range of sectors that have encountered financial difficulties. His main focus now is working closely with the region's banks and asset based lenders.

Don Bailey moves from the Manchester office of Begbies Traynor where he was a partner for eight years. Don, who trained with Ernst and Young before becoming a partner there in 1990, works closely with the intermediary market. He covers all aspects of corporate recovery and has operated across a broad range of industry sectors including manufacturing, construction, property, leisure, agriculture and nursing homes.

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About the role

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Corporate Recovery Partners / Directors
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This top independent firm already has a strong Recovery presence in London and the South and is now looking to build a national presence by establish operations in the North. They are seeking established Partners or Directors with proven business generation skills and strong local contacts. Ideal candidates will currently be working with a 'Big 4' or national practice and seeking a new challenge. Individuals or teams will be considered. Packages will reflect experience and are expected to at least match existing packages via a competitive base salary, equity and an open ended performance related profit share, together with usual compensation benefits.

Restructuring Senior Managers
Cayman $US 105-130,000 Tax Beneficial

What a great way to beat the winter and recessionary blues. This International firm offers challenging work experience, career progression and lots of sunshine to two Managers / Senior Managers who are likely to be qualified accountants with at least 5 years post qualification experience in Restructuring / Corporate Insolvency procedures. The roles will suit personable candidates with good commercial, technical and client relationship skills.

Corporate Restructuring Opportunities
Canada $Competitive

International firm seeks qualified accountants with Restructuring / Recovery experience at Assistant Manager, Manager and Senior Manager level. You will need specific Corporate Insolvency / Restructuring experience gained in a large firm environment. Opportunities in Toronto, Calgary, Montreal and Vancouver.

Corporate Restructuring Executive
Leeds Competitive

Excellent career opportunity in an international firm for a qualified accountant with previous Recovery / Restructuring experience and the ability to run own varied caseload. Friendly, growing department.

Recovery Manager / Senior Manager
Cambridge £Negotiable

Leading Recovery player offers a first class career opportunity to a qualified accountant and / or JIEB with several years' corporate insolvency experience. You should have strong management skills with experience of Business Review work to complement your case management skills. This all-round role will encompass casework, business reviews, budgeting, billing, compliance, staff management, marketing and practice development and represents a great opportunity for personal and professional development.

Corporate Recovery Manager
Birmingham £Negotiable

Leading national practice seeks a qualified accountant and / or JIEB with good all-round corporate recovery and insolvency experience to join its Birmingham office. They offer a good team environment with exposure to all types of cases and the chance to assist in marketing and business development initiatives.

Corporate Recovery Assistant Manager
London c£45,000

National practice offers a challenging opportunity to a newly / recently qualified ACA or ACCA with 3-4 years Corporate Recovery experience. You will gain excellent exposure to a variety of corporate cases and can expect good career progression.

Corporate Recovery Senior Administrators
London £30-40,000

This leading national practice is seeking two Corporate Recovery Senior Administrators who will be part or fully qualified accountants or CPI qualified who are able to work with minimum supervision on a varied caseload of corporate work.

Corporate Recovery Professionals
London £Competitive

This leading international boutique is expanding its Recovery and Corporate Insolvency team and is keen to recruit additional professionals with strong relevant experience gained in a 'Big 4', leading mid-tier or specialist Insolvency practice. Suitable candidates are likely to be qualified accountants and / or JIEB with 3-10 years Corporate Insolvency experience.

'Big 4' Recovery Opportunities Assistant Manager To Director Level
London / South East £45,000 – 6 Figures

As a result of the well documented economic conditions our client, a 'Big 4' firm, is experiencing significant growth in its Recovery practice and is consequently looking to make a number of key appointments to its team in London and the South East. They are interested in talking to dedicated specialists at all levels from Assistant Manager to Director. Suitable candidates will be qualified accountants, JIEBs or equivalent with a strong experience in Insolvency, contingency planning and independent and pre-lending business review work.

Senior Insolvency Administrator
Central London £30-40,000

Excellent opportunity for a part or fully qualified CPI or ACCA with at least 3 years Corporate Recovery experience to join a leading non 'Big 4' practice in Central London. You should be able to handle cases with minimal supervision. The successful candidate will benefit from a good range of Corporate experience in a friendly, supportive team environment with good ongoing career prospects.

Corporate Recovery Executive
Cayman $US Competitive

'Big 4' firm seeks a newly / recently qualified ACA, CA, ACCA or equivalent to join its Corporate Restructuring division in the Cayman Islands. You will need previous experience of corporate insolvency casework.

Restructuring Managers / Ads
Sydney / Melbourne AUS$ Competitive

Exciting opportunities for Chartered Accountants to join a leading international Corporate Restructuring team. You will be responsible for analysing the financial and operational influence of underperforming businesses and establishing valuable strategies to recover and re-establish successful company performance. The role is likely to suit a Chartered Accountants with a sound knowledge of Corporate Restructuring in a strategic advisory manner.

Corporate Recovery Director
South East England
Negotiable £6 Figure Package

Outstanding 'Big 4' opportunity for an ambitious Restructuring / Recovery specialist to 'make a name' for themselves in a 'Big 4' office in the South East of England. You are likely to be a qualified accountant and JIEB with at least 7 years post qualification experience and a specialist background in Recovery and Restructuring work, particularly for mid-market clients. You will need a strong history of successful delivery and a proven business development record. This role represents a great opportunity to be part of a growing national team.

Mid Markets Manager
Reading £50-65,000 + Car

International firm is expanding its Corporate Recovery operations in the South East and is able to offer a challenging and rewarding career opportunity in the Reading office for a Manager with around 2-4 years Recovery experience. Ideal candidates will be ACA / ACCA qualified with a range of Recovery experience gained in the Mid-Market sector.

Corporate Recovery Senior
Ipswich £Flexible

Leading professional firm offers a qualified accountant / CPI / JIEB the chance to work on a wide range of Corporate Recovery and Insolvency work and assignments including Receiverships, Liquidations, Administrations and Investigation work as well as the opportunity to become involved in marketing work.

Corporate Recovery Executives
'Big 4' London £40-46,000

'Big 4' City based recovery team seeks experienced Administrators for their thriving recovery department. You should have between 2-4 years varied corporate experience gained with a leading practice and excellent interpersonal skills. A market leading benefits package, a structured career path as well as an interesting and varied case load can be expected. Ideally you should hold an accountancy qualification or be studying towards one.

The best jobs:

Corporate Recovery Manager

Our client is a national firm with over 2,000 employees and more than 280 partners generating a fee income of over £204 million which positions them as one of the leading mid-tier accountancy firms. The Restructuring and Recovery department in Birmingham is looking to recruit a Corporate Recovery Manager who has review and insolvency skills, as well as knowledge of compliance. Ref MPRV13003663

Birmingham | £Excellent Package | Contact Lucy Williams

Corporate Recovery Senior Manager

The Restructuring and Recovery Department in the South West provide a full range of insolvency services including administration and receivership, liquidations and bankruptcy. Based in the Restructuring and Recovery department, the successful candidate will support the Partners by ensuring that each assignment is carried out efficiently and effectively and that statutory requirements are adhered to. Ref MPRV13016366

Bristol | Up to £60,000 | Contact Nick Jones

Insolvency Director/Partner Opportunity

Leading Scottish Accountancy Firm

A leader, a team player, and above all a confident director. You must have a good base of contacts and be able to leverage your new team into the market and lead them to success. JIEB qualified you should have full understanding of legislation and be confident in training your new team at all levels from Cashier to Senior Manager Level. Ref MPRV12993914

Glasgow | £Excellent Package | Contact Sandra McKinnon

Insolvency/Corporate Recovery Assistant Manager

This is a rare opportunity with fantastic progression to join this newly-formed team as Assistant Manager within this Top 25 practice. Experience of working within this discipline and a desire to succeed are key. There is no limit to where you could progress as there is only the Partner above you. Ref MPRV13014584

Reading, Thames Valley | c £45,000 | Contact Matthew Duquenoy

Corporate Recovery Associate

Our client is the world's leading specialist in corporate turnaround, restructuring and recovery. Due to an increase in work they are looking to recruit a Corporate Recovery Associate to work on a range of formal insolvency engagements. Successful candidates must have a corporate insolvency background. Ref MPRV13006716

Leeds | £38,000 – £40,000 | Contact Peter MacDonald

Corporate Recovery Senior Manager/Director

Providing you with a route to Partnership in 3-5 years. This firm has a superb reputation in their marketplace and are seeking a high calibre person experienced in bank/non-bank work and IBRs to manage a portfolio of high quality cases. Ref MPRV12996302

Leeds | £55,000 – £75,000 | Contact Peter MacDonald

Corporate Recovery Manager

Our client requires a Corporate Recovery Manager to manage a department of four (including an Assistant Manager) with a mainly corporate case load of c125 live cases. The successful candidate will require solid corporate insolvency experience as well as excellent communication skills and the ability to win work. Ref MPRV13017571

Manchester | Up to £45,000 + Car + Benefits | Contact John Wood

Corporate Recovery Director

There is an exciting opportunity to join one of the most dynamic and successful Corporate Recovery firms in London. As a Director you will be ready to put your experience of working on top level, big ticket administrations to good use in a highly commercial environment. With the enthusiasm and drive to help grow the business you will be ready to take the next step in your career in an entrepreneurial and high profile position. Ref MPRV12921918

Central London | Up to £110,000 | Contact Rachael Bunton

The best people:

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Michael Page
FINANCE

Interview with Dan Hamilton

Dan Hamilton, co-chair of the EHYA European Insolvency Reform Committee, explains that the EHYA proposals do not seek to introduce Chapter 11 to the UK: they are aimed at financial creditors only and at restructurings where there is over £200m of debt.

What are the EHYA proposals?

The proposals seek to create a new law for restructuring large companies in financial difficulties in the UK. This is not intended in any way to change our existing insolvency laws. It would be an additional procedure. The key features would be that large companies that propose to restructure, perhaps through a CVA or a scheme of arrangement, can apply to the court for a stay of enforcement from action by their financial creditors. The companies will have access to enough money to carry on their ordinary trading operations while they go through the restructuring procedure. They would apply to the court with a statement that they are unable or likely to become unable to pay their financial debts. They would have the bones of a scheme, and they would have a document from someone we are calling a monitor who will be an insolvency practitioner or maybe an experienced turnaround person, telling the court that the company has a reasonable prospect of achieving a restructuring. The role of the monitor is not to run the company and they are not there to negotiate the restructuring. They are there really to report to the court if they think there is any sort of abuse of the process or if they think it is unlikely restructuring will ever be achieved, just to make sure companies do not abuse the process and don't obtain a moratorium for ulterior purposes.

So effectively the monitor's role is reasonably similar to that of a nominee's in a CVA.

There are some similarities but if there is a CVA to be proposed the monitor will not be the same person as the nominee or as the supervisor of the voluntary

arrangement. It is key that their duty is to the court and that they don't owe a duty to the company in the way a nominee or supervisor might do.

And why is that?

The whole idea was that the monitor would not have any economic interest or any other interest in seeing the restructuring go through. They are meant to be someone who is overseeing the initial procedure, ensuring it is used properly and reporting to the court. We didn't want this procedure to become a new insolvency procedure displacing the directors, but we felt some protection would be needed for the creditors to be sure it wasn't abused and that it wasn't sought when there wasn't a real prospect of a rescue.

Is what we are talking about here just a pre-CVA, pre-scheme framework allowing greater predictability?

Yes, we suspect it will usually require a CVA or scheme.

> "The key features would be that large companies that propose to restructure, perhaps through a CVA or a scheme of arrangement, can apply to the court for a stay of enforcement from action by their financial creditors.

What else do you propose?

The second limb of our proposal is providing a better means for judicial resolution of valuation disputes in restructuring. There are two parts to this. One is that we would hope that by giving some guidelines in the legislation, the courts develop a new jurisprudence on valuation in restructuring. There is a tendency in the restructuring world to view valuation where restructuring is going ahead purely on the basis of what the business is worth in an immediate sale. While in some cases that may well be fair, in other cases that is going to mean junior creditors or shareholders will lose out on the future value of the business if it is successfully turned around. It is also there, however, to make sure that junior creditors cannot use the threat of a valuation dispute in order to disrupt a restructuring and perhaps get something that they are not entitled to. The company proposing the scheme or CVA would put in some valuation evidence when it files the scheme documents and if there was a valuation dispute the court could quickly give directions. Objecting creditors would either have to go to court, put their evidence of why the valuation is wrong and challenge at that point, or risk the court blessing the transaction and so removing the possibility of later arguments about valuation. We have all seen the situation where a small class of creditors who are completely out of the money managed to get themselves some part in a restructuring just through the threats of suing various parties for carrying out the transactions at the wrong values.

Once the company is insolvent, even just in terms of not being able to pay its financial creditors, why should 'out-of-the-money' junior creditors, or shareholders, share in post-turnaround future value?

There are many degrees of insolvency. Why should a temporary period of cash flow difficulty lead to whole tranches of a company's capital structure being disenfranchised? Our proposals are aimed at ensuring that a restructuring accurately reflects the real value of a business, and properly values and recognises each stakeholder's share. The aim is that junior creditors should not be able to get something for nothing as hold-outs, but equally should not be deprived of an interest by means of a valuation based on a narrow, snapshot liquidation valuation.

What else needs to be done to deal with 'out-of-the-money' stakeholders?

Schemes and CVAs will be able to cram down classes of creditor or shareholder where they genuinely have no economic interest in the matter. Although schemes of arrangement are a wonderfully flexible tool and you can carry out schemes of certain groups of creditors, ignoring a junior group of creditors and shareholders, the effect of that is merely that the scheme does not bind that group, it doesn't actually cram them down. We would suggest that if you get a proper valuation, you can have a proper cram down and continue to keep your corporate structures in place. This is the best way of ensuring that parties get what they are entitled to and hopefully reduce the culture of liquidations and pre-packs and allow more restructurings, which have been a very useful but sometimes rather crude tool.

Why does the corporate structure need to stay in place?

Our proposals will not necessarily mean that the exact corporate structure has to stay in place. What we are keen to see is that as much of the capital structure as is appropriate should continue to have a stake in the enterprise in question.

What else is central to the proposal?

Funding. What we have suggested is that in the appropriate circumstances a court should be able to remove a negative pledge or a restriction by junior creditors on further borrowing so that a company can borrow money as it goes through a restructuring. This is particularly important where you have a multi-layered financing with junior creditors who may be completely out of the money but have contractual rights to block the money going in at higher levels. The final little tweak is that we would add to the stay a provision that other commercial creditors could not terminate their contracts solely on the grounds that the company has applied for a stay. Obviously, if the company isn't paying its debts as they fall due or if there are other breaches the stay wouldn't prevent termination, but it would prevent the sort of blackmail where a supplier terminates the contract and demands double the fees solely on the ground of the stay. I have heard some insolvency practitioners suggest they would rather like such a change to the administration stay as well.

How relevant are your proposals given the financial crisis?

I think the proposals are hugely relevant and we all feel a little bit like Cassandra. Nearly two years ago our committee came forward with this proposal and the reaction we had from many was that we don't need this, it is not relevant, the economy is doing wonderfully thank you very much.

> "Monitors… are there really to report to the court if they think there is any sort of abuse of the process or if they think it is unlikely restructuring will ever be achieved.

We were hoping to anticipate the problems this time round rather than have all the pain that leads to the reform.

So this will be a contribution to the reaction to the current recession?

No, we hope that this can still be brought in in short order. Given that now the market seems to think we are potentially facing a worldwide recession that may be quite long, we feel it would make sense to be ready with a rescue procedure to deal with this over the next few years, not wait until we have gone through it.

What about liquidity? These proposals are not designed for where there is a shortage of liquidity but for where there is balance sheet insolvency, and today's problems are largely credit driven.

The amount of liquidity you need for a period while you restructure is proportionately rather smaller than the amount of liquidity needed completely to refinance a company. If we are looking at a long-term recession, restructuring doesn't just help the junior creditors and make sure that they maintain some stake in the business, it also preserves jobs and peoples' pension funds.

One of the issues about the proposals is that they were presented as insolvency law reform but what we've talked about so far is a precursor to any form of insolvency?

I think we initially called this insolvency law reform because part of what is in our Insolvency Act is expressed to be rescue procedures and legislation. However, in practice that is not how it is being used and I think it has been very difficult for people to get away from the insolvency taint of administration. You and I know that administration in theory can be used and in a few successful cases has been used very well as a rescue tool, but they are very much the minority of cases and it is difficult for this not to be seen as a failure and as a liquidation process. I am not one of those people who criticises the use of pre-pack administrations, but their predominance has tended to reinforce that it is in effect a liquidation procedure.

What makes you say that pre-pack makes administration a liquidation procedure?

Because you have liquidated the assets of the company and you are left with a shell, which means that a large number of the stakeholders have lost out.

In the restructuring scenario, aren't you saying something pretty similar, but just doing it through a different mechanism? You are saying that there is going to be a valuation and the people above the break can participate and those below it can't. Isn't that exactly the same thing?

I see a pre-pack as liquidation because it does simply leave behind the contractual rights and proprietary rights of creditors and stakeholders in an old company and because it can be driven by one class of creditors and takes value away from others. Sometimes administration can be used as a useful restructuring tool but it is rarely used as a tool for a conceptual restructuring where genuinely all of the classes have a right to participate. Also,

> "Our proposals are aimed at ensuring that a restructuring accurately reflects the real value of a business, and properly values and recognises each stakeholder's share.

current jurisprudence is that when an administrator sells an asset, his duty is only to achieve the price he can obtain for the business in the market at the time. It is not genuinely taking into account the long-term interests of the restructured business and potentially the rights of those subordinated creditors who are always investing for a long-term view rather than to get the immediate value of the business.

Are you arguing for something that protects against a dominance by the secured lenders in formal insolvency situations?

No, I think that is a whole different issue. What we are suggesting is that where there is a proposal for the business to be kept whole with some of the stakeholders remaining in the deal, it should be treated as a rescue and not as simply a liquidation. There will be cases where administration and a sale of a business is the only option and in many cases a pre-packaged administration is going to be the best way of getting value out of that. I am not sure it is always the best tool for a restructuring >>

within a group, and where it is used as a rather blunt instrument to exclude difficult junior creditors I am not sure it achieves equity or is the best way of protecting the interests of everybody.

Are you saying that this isn't really insolvency reform?

Exactly. I actually think the UK has some of the best insolvency laws in the world. I just don't think we have a useful procedure for restructuring and I don't think administration has been used in the way that it was intended to be used following the Enterprise Act reforms as a rescue for companies.

What size companies would the proposals apply to?

We are looking at companies at the larger end of the market who probably have multiple tiers of debt probably in excess of £200 million.

Are you intending to restrict it to companies with debt in excess of a particular amount or are you saying it is going to be generally available but that it is designed really only to apply to those high-end companies?

We think it is something that is lacking for larger, more complicated restructurings and initially we are proposing it just for them.

We have already got one of the most complex restructuring and insolvency landscapes in terms of the tools we apply. Now you are adding another one?

Really what we are seeking to do is to make slightly more formal the existing system of informal restructuring. We are really not changing the current way that they are done, except to make them more expedient and faster, and to remove the shareholder hold-out factor. We had the London approach and the INSOL rules on guidelines on restructuring but they are largely gone because the participants in the debt markets have changed so radically. We have managed in large restructurings, not because we have wonderful legal tools but because we have a very inventive and resourceful insolvency profession and restructuring advisory profession who have patched together restructurings with what tools are available. The use of schemes of arrangement has been very inventive, as has the use of CVAs. Both have gone beyond what they were originally intended and designed for, but it has worked. It is not necessarily a good thing from the point of view of selling the UK as an investment base that restructuring gets done because people are able to be inventive with the limited tools they have. It is much better to give them the better tool that means there is a degree of certainty in the outcome.

> "Given that now the market seems to think we are potentially facing a worldwide recession that may be quite long, we feel it would make sense to be ready with a rescue procedure to deal with this over the next few years, not wait until we have gone through it."

Is it correct to say that your proposal is not connected with ordinary insolvency, it is just connected with the huge multi-party restructurings that have proved very difficult without a formalised framework?

Correct. Restructurings that have proved difficult and which we think are going to be much more difficult given that the financial structures have become more complex. The financial markets have become a much broader church so we're not just dealing with a group of bankers who to a large degree know each other. We now frequently have transactions where you will have senior secured debt, second lien debt, mezzanine and high yield bonds and potentially some sort of PIK instrument at the bottom. Each of those held by potentially a different class of people. In the large transactions, as well as possibly the presence of credit default swap holders, a huge amount of the funds are no longer held by the banks that originated the deals, they are held by either distressed secondary investors or CDO and CLO funds who have very limited resources to engage in heavy restructuring.

> "Our committee is not proposing a wholesale introduction of Chapter 11. It is hoping our proposal will bring the best from various parts of the world's restructuring laws in order to make something that is an excellent English restructuring law."

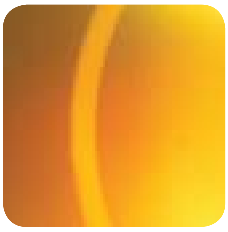
This summer, the Conservative party started talking about insolvency law reform and a lot of what they were saying seemed to echo parts of your proposal. Did you like what they said?

We would welcome in-depth discussion with the Conservative party on how their proposals would fit in with ours. We have only got an outline from them so far and I think they were referring on a number of occasions to Chapter 11 in the US. Our committee is not proposing a wholesale introduction of Chapter 11. It is hoping our proposal will bring the best from various parts of the world's restructuring laws in order to make something that is an excellent English restructuring law.

Where can a copy of the EHYA proposals be found?

www.EHYA.com

Chris Laughton is the editor of *RECOVERY* and a partner at Mercer & Hole.




Insolvency Specialists

Accountancy Practice

Manager – Business Review Team

£55,000 - £60,000 + benefits London

A Top 20 practice firm is looking to add to their growing Business Review Team, working closely with them on restructuring, turnaround and insolvency projects. ACA qualified and with strong insolvency experience. Strong independent business review experience will be key.

E: s3b.r3@witanjardine.co.uk (Ref: ATA54645)

Accountancy Practice

Business Recovery Manager

£45,000 - £60,000 + benefits London

This Big 4 firm is looking for an experienced Manager to join their Recovery Team. You will be able to demonstrate experience of working on large cases and the delivery of solutions to distressed businesses. Proven management skills as well as an accounting qualification are essential.

E: s3b.r3@witanjardine.co.uk (Ref: TP54076)

Accountancy Practice

Administrator

£15.00 - £20.00 per hour London

This Top 10 insolvency team is looking for an experienced Insolvency Administrator to assist them during a busy time. You will have broad corporate insolvency experience and be a competent user of IPS to take on this role, with caseloads including liquidations and administrations.

E: dar.r3@witanjardine.co.uk (Ref: TP53433)

Insolvency Practice

Senior Administrator

£28,000 - £34,000 + benefits London

A boutique insolvency practice is looking for an experienced Senior Administrator with an all-round background. This role will suit those who have mixed experience of both personal and corporate insolvency cases, are CPI qualified and are happy working autonomously when required.

E: s3b.r3@witanjardine.co.uk (Ref: TP54448)

Accountancy Practice

Insolvency Administrator

£25,000 - £32,000 + benefits London

A mid-tier insolvency practice is looking to add to its team. In the role, caseloads will predominantly be corporate cases, administrations, liquidations and some personal work. With a solid grounding in insolvency, you will be part or fully qualified with CPI to take on this challenge.

E: s3b.r3@witanjardine.co.uk (Ref: ATA54314)

Insolvency Practice

Insolvency Administrator

£13.00 - £18.00 per hour London

This South London based firm is looking for a temp to assist in a busy team. You will have experience of bankruptcy work as well as a good mix of personal and corporate case management. IPS experience will also be essential.

E: dar.r3@witanjardine.co.uk (Ref: TP54489)

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