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RECOVERY

Employment issues

Perfect harmony How can cross-border coordination be improved?

Exploring new waters
An in-depth look at handling insolvency in the energy sector

The key link between insolvency and HR1 The full story behind city link and the importance of HR1

Employment and insolvency – strange bedfellows?
What IPs need to know about bridging the gap between the two

Brexit strategy
The potential impact on insolvency law without oversight from Europe

Mis-sold down the river?
A forensic approach to the matter of IRHP mis-selling

Overt intelligence
The IP's guide to using social media and online tools in an investigation

An interview with… Sarah Albon
The inspector general and chief executive of The Insolvency Service speaks to *RECOVERY* about the challenges The Service is facing and how it is changing the way it interacts with the profession.

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

From the editor

When you receive this issue of *RECOVERY*, the time for voting in the EU Referendum will be approaching fast. So what then do we have to help the undecided reader – or perhaps to persuade the decided! Diving into the debate on p28–30, Jamie Leader considers the legal effects of Brexit on restructuring and insolvency, concluding that whatever the outcome of the referendum, practitioners cannot simply assume a continuation of the status quo. That is underlined in our technical update on p13–15 where Chris Parker and Catherine Burton explore the harmonisation of insolvency laws both within Europe and through the workings of UNCITRAL Insolvency Working Group V.

Two books on the European Insolvency Regulation (original and recast) are reviewed on p6 and, linking to our employment theme, Barbara Rumora-Scheltema explains on p22–23 how TUPE and pre-packs work in The Netherlands.

The conflict between insolvency and employment law is explored on p24–25, where Simon Kerr-Davis and Philippa O'Malley consider how IPs might deal with the risks the conflict creates. One such risk is the filing of HR1 forms, which Amanda Rowe addresses in some detail on p19–21 by reference to the City Link case. Another issue is explored by Paul Marsh on p26 – how employees of a partnership (not an LLP) can fall outside the Redundancy Payment Scheme.

There is much more to stimulate and inform you in this larger than usual issue. Our new President, Andrew Tate writes his first column on p7 and we are delighted to carry an interview with Sarah Albon, inspector general and chief executive of The Insolvency Service on p50–52. You should make a point, however, of reading Mike Pavitt's plea as a creditor's lawyer (and vice-chairman of R3's Southern Region Committee) encouraging genuine engagement with creditors – it will raise a smile.

C. Laughton

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

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RECOVERY

Editor
Chris Laughton, Mercer & Hole

Publishing manager Matt Jukes
Tel: 01491 828939, matthew.jukes@groupgti.com

Advertising Will Nevill
Tel: 01491 828920, william.nevill@groupgti.com

Art director Thomas Gray

Administration Jack Roberts

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Tel: 020 7566 4200, association@r3.org.uk, www.r3.org.uk

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Austin Reed finally threadbare

Luxury tailor and suit retailer Austin Reed, that once catered to clients such as Winston Churchill and the Beatles, has collapsed into administration citing 'challenging retail market conditions' as the reason for the insolvency. Profits had been declining for the suit retailer since 2011, when it was forced to move out of its flagship Regent Street store. It closed a further 31 unprofitable stores as part of a company voluntary agreement last year. Administrators from AlixPartners were appointed at the end of April.

AlixPartners stated that Austin Reed would continue to trade while options were explored for the business, including whether parts or the whole of the business could be sold. So far it is believed that around 50 offers have been received. The retail group employs more than 1,000 staff in the UK in around 100 stores and 50 concessions.

Just two days prior to the Austin Reed announcement, high street behemoth BHS announced that its attempts to avoid insolvency had been unsuccessful. An estimated 350 retail stores have gone into administration since 2007.

Source: The Guardian

Harkand no longer shipshape

Oil and shipping group Harkand has gone into administration following the global downturn in oil and gas prices. Administrators from Deloitte were called in at the beginning of May 2016 to wind up its European business. Senior staff at Harkand's US business, led by managing director A J Jain, agreed to a management buyout, which has allowed joint administrators to sell the US and Africa parts of the business successfully, preserving around 100 jobs.

Harkand began operating in 2013, providing subsea services to the energy industry, including surveying and dive support operations, and had received contracts from major names in the industry including BP, Apache and Maersk. The group, which has bases in London and Aberdeen, has an estimated turnover of £357m and employs 400 staff. It is estimated that around 170 jobs will be lost, predominantly in Aberdeen. *Source: BBC*

Digital dilemma for Omnifone

Omnifone, a B2B digital music firm with a licensed library of 35 million tracks that catered to companies such as Spotify and Sony, has been placed into administration. Just two months prior to the move, the company had appointed a new CEO. Post-tax losses in 2014 had reached £6.9m, up from £6.1m in 2013, with the company failing to file figures with Companies House for 2015.

Joint administrators have been appointed from Leonard Curtis to take Ominfone Ltd and its subsidiary Omnifone Group Ltd through the process. Around 120 staff were employed by the business, with 50 expected to be retained to continue operations in the meantime. *Source: Music Business Worldwide*

Shining a light on BHS

The Insolvency Service will bring forward its investigation into the collapse of BHS by order of the Department for Business, Innovation and Skills. Business secretary Sajid Javid said that he had asked the investigation to be brought forward and that any issues of misconduct [among BHS' directors] would be taken very seriously. Under normal circumstances, The Service would wait for a final report by administrators before taking action. The investigation will examine the most current directors of the company, led by Dominic Chappell of Retail Acquisitions, as well as their predecessors led by Sir Philip Green.

The company's pension scheme is also currently under investigation in relation to a pension deficit of £517m, while the Serious Fraud Office is reportedly examining the flow of money in and out of BHS. Negotiations for the sale of more than 150 BHS stores is ongoing.

Source: The Guardian

Trying time for steel producer

A Nottinghamshire steel fabrication company has entered administration following the death of its director. Steelworld Fabrications Ltd formerly catered to automobile makers such as Jaguar and BMW. Following the death of its sole director, administrators from Wilson Field were called in April to handle the company. Eight redundancies have been made so far.

Source: Insider Media

Rerun for printing group

Elements of a major UK printing group have recovered from, then returned to, administration after one of their biggest customers declined to renew its contract. Parts of the Polestar printing group had been saved as part of a £65.9m pre-pack deal in April. However, the loss of the major customer, believed to be DMG Media – a newspaper publisher – has threatened the viability of the business. Administrators from PwC are handling the case.

Source: Insider Media

Motorcycle bust up

A motorbike dealership in the Midlands that went into administration, and was generating a profit of £73,000 in the months before closure, collapsed due to a shareholder dispute, according to *Insider Media*. Derbyshire's Bikers Motorcycles closed at the beginning of this year. A shareholder dispute caused director Ian Smith to resign, taking with him £28,000 in repaid investment. A reduction in the company's overdraft and a reluctance to take new orders put the business into distress.

Source: Insider Media

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- **PRICE** £175.00

> "Insights from contributors closely involved in development of the new legislation are invaluable."

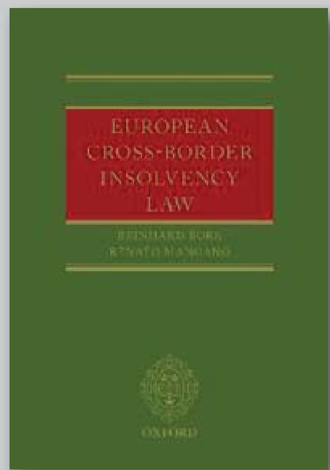
The EU Regulation on Insolvency Proceedings

The third edition of this familiar and authoritative work achieves two things. Firstly, it updates its predecessor for developments to Regulation (EC) 1346/200 (the 'original Regulation') over the seven years to early 2016. Secondly, it analyses Regulation (EU) 2015/848 (the 'Recast Regulation'), which was published on 20 May 2015 and will come fully into effect on 26 June 2017. That it does both superbly well should not be a surprise, given its pedigree and the skills and experience of its contributors and its renowned editors.

For many, this book is the first place to go when seeking assistance with the original Regulation, as it explains the history and legal basis of the Regulation before going on to discuss: scope and jurisdiction; choice of law rules; recognition and enforcement; cross-border security; and financial institutions. The chapter on financial institutions has been rewritten in light of the significant developments in the various directives that apply to financial institutions excluded from the Regulation. Finally, chapter eight analyses the original Regulation article by article over some 140 pages, 470 paragraphs and 550 footnotes. The full text of the original Regulation and that of the *Virgos-Schmit Report* (a widely used aid to interpretation in the form of an explanatory report on a preceding proposed convention, which became the original Regulation with only a few amendments) are included in two of the book's main appendices. The detail in this work often means that the reader need look no further when seeking an explanation of a point in the Regulation.

Each of the book's chapters also addresses the Recast Regulation to a greater or lesser extent in the context of their subject matter so, for example, pre-insolvency proceedings and synthetic secondary proceedings (both newly addressed in the Recast Regulation) are touched on in the chapter on scope and jurisdiction. The final 100 or so pages of chapter eight analyse the Recast Regulation article by article. Naturally, there are fewer footnotes than mentioned above as there are no decided cases. Nevertheless, the insights from contributors closely involved in development of the new legislation are invaluable.

If you practise European cross-border insolvency, you should have this standard text close at hand. ◻



- **Edition** First
- **Authors** Bork and Mangano
- **Publisher** Oxford University Press
- **ISBN** 978 0 19872 909 9
- **PRICE** £125.00

European Cross-Border Insolvency Law

This slimmer but equally authoritative volume concentrates on the Recast Regulation and is introduced by a slightly broader consideration of European insolvency law and the development of that topic. It brings a continental European perspective to analysis of the Regulation, its distinguished authors being, respectively, professor of civil procedure and general litigation at the University of Hamburg and professor of commercial law and insolvency law at the University of Palermo. Each has also been a visiting fellow at Oxford University.

The book neither analyses the Regulation article by article nor includes the text of the Regulation. Rather it discusses the Regulation's key subject areas: scope; jurisdiction; applicable law; recognition and enforcement; information and cooperation; secondary proceedings; and group insolvencies (with the principal author of each chapter noted in the page footers). As might be expected, it does so by reference to case law from the Court of Justice of the European Union (CJEU) and from a variety of member states, and it contains a full academic bibliography. While noting that the quality of some of the provisions in the Recast Regulation is debatable, the preface identifies the book's objectives as 'seeking to explain the system of the [Recast Regulation] to both academia and practitioners… and offering a reliable overview of the case law of the CJEU.'

To this English practitioner it appears to have met those objectives fully and to have done so usefully from a standpoint that is not wholly familiar. For those seeking a deeper understanding of the Revised Regulation, it is a valuable reference work. ◻

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

President's column

Andrew Tate takes the helm and lays out R3's goals for the coming year.

I've been writing this column as preparations for R3's annual conference in Budapest are wrapped up. By the time you read this, the conference, the culmination of 12 months' work, will be over for another year. I hope you enjoyed it if you were there.

Despite being involved with R3 since 2011, first as Smaller Practices Group chair and then as deputy vice-president, it's not been easy to truly appreciate the amount of work that goes on behind the scenes at R3 to put the conference together until I've sat in the presidential hot seat myself.

One of the major themes at this year's conference was the IP's skillset, something else where there is much more going on than meets the eye of the casual observer. The changing nature of the insolvency profession – whether it's the type of work we do or the rules that underpin that work – is going to be the main focus of my year as president.

IPs and the public

Understandably, 'insolvency practitioners' can be pigeonholed as dealing only with formal insolvency appointments. With this assumption in mind, companies and individuals can make the mistake of leaving it until there is no choice but entering an insolvency procedure before seeking help from an IP. As you and I know, the earlier an IP can offer their help, the better; and in many cases, avoiding an insolvency procedure altogether is the best outcome. Insolvency practitioners are about much more than just formal insolvency processes! Getting this message across is one of the goals I have set myself for my year as president.

The IP's skillset, while built on formal insolvency work and requirements, is incredibly versatile and equips the profession for work well outside the confines of liquidations, administrations, bankruptcy or voluntary arrangements. Many of us have developed skills that extend way beyond the Insolvency Act and rules.

While our formal insolvency work is subject to much regulatory scrutiny, legislation or public attention, the breadth and depth of the profession's restructuring and advisory work is under-explored. There is a lot of catching up to do. With major lenders doing much more when it comes to supporting struggling debtors, formal insolvencies, on the corporate side at least, are unlikely to return to historic highs and advisory and restructuring work will continue to grow in importance. For larger firms and others, the importance of advisory and restructuring work is already well established.

Increasing the understanding of what the profession can do away from formal appointments will involve work both inside and outside of the profession. Of course, it will be important to speak to stakeholders and policymakers about what the profession can do; but there is educational work to do inside of the profession, too. For more traditional practices, in particular, help to understand and offer advice on refinancing options, for example, could be useful.

Legal landscape

We will keep an eye out for any legislative reforms that might be needed, but given the scale of change already in the pipeline we believe that any new reforms would have to be absolutely necessary.

Indeed, helping the profession adapt to recent changes – and ensuring the government is aware of the impact of the reforms – is another other item high up on my to-do list. There will be a lot of things to digest: fees, pre-packs, creditors' meetings, investigations work, and more have all recently changed or will be in the process of changing by the time I hand over to Adrian Hyde this time next year. The government's change in tack on collective redundancies – resorting to criminal charges to tackle compliance issues – is another challenge, but one where R3 is leading the way for reform. In May, R3 and Stephenson Harwood hosted a round table to discuss ways forward that brought together regulators, government, and the insolvency profession.

Whatever we think about the necessity or appropriateness of some of these changes, it is vital that each of them enhances rather than undermines the UK's insolvency regime and our ability as IPs to get on with the job of rescuing businesses and jobs, returning money to creditors and helping financially struggling individuals onto their own two feet again.

Writing as a former Smaller Practices Group chair, I also believe it's important the government keeps a close eye on the impact of its reforms on smaller firms and smaller businesses in particular. While formal insolvency work needs to be uniformly tightly regulated, maintaining a one-size-fits-all approach can lead to practical problems for IPs, typically smaller firms, dealing with small or micro-businesses with few assets. When it comes to insolvency, the government's traditional maxim of 'think small first' doesn't always seem to apply.

R3's influence will be crucial for making sure the government understands the profession's concerns. As vice-president and deputy vice-president, I've seen first-hand how R3 was able to moderate the changes to which we now are adapting – a fees estimate is preferable to a blanket ban on time-costs, for example – and I will try to shed some light for members on the work R3 does on their behalf over the next 12 months. I can understand that the scale of the recent changes is overwhelming and it can seem that the views of R3 and the profession are not taken on board, but I can assure you that nothing is further from the truth.

Please do read the monthly eBulletin and these columns for updates, and remember that getting involved with your own regional committee is another great way to keep up to date with what R3 is up to. In the same way that there is more than meets eye when it comes to IPs' work, the scope of what R3 gets up to on your behalf might surprise you.

Looking to the future

As well as the changes already announced over the last 18 months, we know that more planned legislation is in the pipeline. At the time of writing, the government is yet to publish its much-trailed plans for a reformed moratorium for companies from creditor action but an announcement is imminent. We'll do our best to ensure that any resulting legislation matches the business rescue moratorium proposal published by R3 in April and, at the very least, is a workable tool for IPs – and businesses.

By the time we meet again in Dublin for the 2017 R3 conference, the insolvency regime will look different. As well as the changing type of work we do, there will be legislative and regulatory change, too. As your representative I will fight to make our voice heard and our value and our contribution to the economy recognised. And, above all, I will fight to make sure that a 'different' insolvency regime is a 'better' insolvency regime. □

ANDREW TATE
is president of R3 and a partner at Kreston Reeves LLP.

Sucked into the (creditor) portal

Mike Pavitt writes about why creditor portals do not equal creditor engagement.

So-called 'creditor portals', and other similarly titled electronic platforms through which insolvency practitioners typically circulate meaningful information to creditors about insolvent estates, have been a bugbear of mine ever since they were first used a little while ago. Don't get me wrong; I absolutely applaud the attempt that they represent to minimise the amount of unnecessary paperwork in circulation and the savings of cost that they bring to the administration of insolvent estates – where the cost of copying and posting alone would be absolutely frightening today. I don't even object to the quality of the software *per se*, although some are much better than others. No, what I object to is the seemingly (and yes, I know there will often be good reasons for this) 'lazy' way in which a significant cross-section of the insolvency profession make use of them, such that the 'Holy Grail' of genuine creditor engagement (which the insolvency profession always claims it wants more of) gets further and further out of reach.

> Given that the vast majority of reports to creditors enter the public domain, I have to query why we need ridiculously complex passwords as if we were trying to access an MI6 database.

A hard life of hard copies

Take this week as an example: as lead corporate restructuring and insolvency partner at a busy firm of solicitors, I will typically receive on my desk perhaps half a dozen to a dozen hard copy letters from insolvency practitioners with sticky labels on them proudly announcing that they have been sent *'to all known creditors'* of XYZ Limited or Mr John Jones (in bankruptcy) etc. What these labels almost always omit to say, however, is whether we are receiving them because we (as a law firm) are a creditor, or because one of our clients is a creditor, or (heaven forbid) who our client actually is (who is or may be a creditor). The idea of there being a client or matter reference anywhere on the address label is positively risible. Alright, so perhaps that is too much to expect. It takes a bit of time, but we can generally work out who the alleged creditor is, and if we are lucky we will also be able to see how the creditor's claim arises. So far, so okay.

Then we look at the substance of the letter. This varies, with some IPs deigning to tell us why they are writing to us in the letter itself (tick, tick), others alerting us to the fact that we have to do something by a certain date (half a tick), and still others simply putting the name of the debtor in the header alongside the words 'in administration' or 'proposed corporate voluntary arrangement' and expecting us to work out the rest (big cross).

Data entry for the overworked

So then what? Ah, to read on we need to log on to a web address. This will normally be an http address carrying at least 30 characters, various slashes and dots etc, which we have to magically transcribe into our browsers – making no doubt several missteps of our fat fingers on our tiny laptops along the way. Having done so we are then invited to do the same with a 'case code' (typically long numbers – yuck, we are wordsmiths not mathematicians) and (horror) a password. Given that the vast majority of reports to creditors enter the public domain at some point, I have to query why we really need to be issued with ridiculously complex passwords as if we were trying to access an MI6 database. Remember, this is a hard copy letter; we cannot (without scanning the letter and using some clever tool at any rate) just copy and paste these passwords as we would do with emails from online providers.

And then, finally, we are in. Oh wait, no we are not. We cannot get in at all. The http address on the letter was wrong. It should have been 'Blahblahblahcorporateportalthingamy/reports/morereports/highsecurity.com' instead of 'Blahblahblahdebtorportalthingamy/reports/theonethatonlyworksforbankruptcyreports.net'. The case code or password were mistyped and have disappeared accordingly. Perhaps there was a dash on the letter when it should have been a hyphen. So we wind up ringing up the nominated case administrator and/or emailing them (perhaps there is more than one, because the letter and the attached notice do not agree). And what do they do? Of course, very naturally and helpfully they offer to email you the report. Then you either have to hope they make an accurate note of your email or make sure you have sent them an email to reply to.

> So, please, please, insolvency practitioners everywhere, take a moment before you send your report notifications.

Let's say after all this effort we finally do get sight of the report we've been so anxious to read. What is it? Oh – it's a progress report on a creditors' that liquidation (CVL) that commenced four years ago, only there have never been any assets in the liquidation for distribution to anyone let alone unsecured creditors, because, you see, there was a prior company voluntary arrangement (CVA),

and all of the company's assets were pledged in trust to the CVA creditors, and the only reason we're keeping the CVL open and sending you this pointless report is because we have to until the CVA supervisors have finally lost the will to live.

So long, and thanks for all the paper

Well, thank you insolvency profession. You have just wasted a good chunk of my day. Thank you very, very much. And am I then going to move on to the next such letter, knowing full well that this one might be offering me a chance to vote on proposals within a short timescale, which vote if cast

> Well, thank you insolvency profession. You have just wasted a good chunk of my day. Thank you very, very much.

could be to everyone's advantage if only you had the requisite majority? No, I am not. I am going to throw the second letter away, or place it out of reach for a (very) rainy day and get on with something more profitable.

I cannot be alone in this frustration. Corporate creditors with massive post rooms must absolutely despair at the amount of such mail that they receive, particularly those who are not used to it and have not appointed some poor, underpaid soul to the made up role of 'orphan post management operative' or similar. This surely cannot be what the insolvency profession hopes to achieve? Disengagement? Resentment even? An impression that you're just there to generate information you don't want anyone to read so you can be paid for it? No, I am convinced that is not what you are about. I am not just saying that as vice-chairman of R3 in the South, but as one who frequently advises creditors who I genuinely want to play an active part in helping you to deliver returns and to maximise the value that we all look to bring to the British economy by turning these matters around as quickly as possible.

A final plea

So, please, please, insolvency practitioners everywhere, take a moment before you send your report notifications. Give some thought as to whether they need urgent attention, why they might genuinely be of interest to the recipient, and put at least a flavour of this in your covering letter, starting with when you were appointed so we at least know if it's current and urgent or old and potentially stale. Consider also whether, on this occasion, you might be better off actually sending the whole thing out, perhaps with the appendices and other bulky documents on the portal for those who want or need to see the full detail. Oh, and don't ever send me a portal link to a CVA proposal without actually telling me that's what you've sent me a link to! Period. Save us all a lot of time in the long run, and a lot of anguish, and you might just achieve the creditor engagement you always say you desire!

> The idea of there being a client or matter reference anywhere on the address label is positively risible.

Oh, and one last word to the wise. If you know my firm acts for a creditor whose vote is important to you for whatever reason, don't throw yourself on the lottery of a chance of my having the time and inclination to access and read your report before it's too late: give me a call!

MIKE PAVITT is lead corporate restructuring and insolvency partner at Paris Smith LLP and is vice-chairman of the R3 Southern Region Committee.

IPs: are you ready for the new PSC regime?

Rebecca Jarvis, **Richard Bussell** and **Paul Sidle** outline what you need to know about the PSC regime and how it might be relevant to you.

As part of the government's ongoing drive to improve corporate transparency and tackle corruption, the UK recently became the first G20 country to establish a publicly accessible central registry aimed at showing who really pulls the strings behind UK companies. Effective from 6 April 2016, Part 21A of the Companies Act 2006 (CA 2006) requires most unlisted UK companies to maintain a register of its people having 'significant control' – or 'PSCs'. The PSC regime also applies to LLPs and *Societates Europaeae* (European public limited liability companies).

How the PSC regime might affect you

Scenario 1...

You are appointed over a UK company obliged to maintain a PSC register. Do you need to go on its PSC register?

A company's PSC register must include any person who has 'significant control' over it (they may be an individual or a company). Given the public nature of insolvency proceedings, it would not be particularly problematic if an IP were a PSC for the purposes of the regime and had to include their details on the PSC register of the company over which they have been appointed. However, it could potentially expose an IP to criminal liability given the obligations that can fall on a PSC.

> "Apply the five tests in the box on this page to establish whether a person is a PSC."

Applying the five tests in the box on this page to establish whether a person is a PSC, it is clear that an IP should not need to go on a company's PSC register.

	Condition	Application to IPs
1	Directly or indirectly holding more than 25 per cent of the shares in the UK company	• N/a
2	Directly or indirectly holding more than 25 per cent of the voting rights in the UK company	• Liquidator/administrator – n/a • A document charging shares in a UK company may give a receiver the right to exercise voting rights on enforcement. Even so, a receiver will not be a PSC unless there are unusual circumstances. • Para.23 of schedule 1A to the CA 2006, confirmed by BIS guidance, ensures that for the purposes of the PSC register, the rights would continue to be held and controlled by the chargor even though they could be exercised (eg by the lender/receiver on enforcement) for the purpose of preserving the value of the security or of realising it. The same analysis would apply if, on enforcement, a receiver were able to exercise any board appointment/removal rights for the purposes of condition 3. • If a receiver had more extensive rights and powers than it would do ordinarily or there were other unusual circumstances (eg they exercised voting rights over a lengthy period of time), then it is possible they could become a PSC but this would not be common (and a question of fact to be considered at the time). • The same points would apply to lenders and security agents.
3	Directly or indirectly holding rights to appoint or remove directors with the majority of board level voting rights	• Para.22 of schedule 1A to the CA 2006 provides generally that rights exercisable by an administrator while a company is in administration are not to be taken into account. Accordingly, while para.61 of schedule B1 to the Insolvency Act gives an administrator power to remove and appoint directors, it will not trigger condition 3. • Para.22 does not cover liquidators or receivers. But, a liquidator does not have the same power to appoint and remove directors and the analysis referred to on para.23 above would apply to receivers.
4	Otherwise having the right to exercise, or actually exercising, 'significant influence or control'	• Statutory guidance provides a non-exhaustive list of roles and relationships which would not, on their own, result in a person being considered to be exercising 'significant influence or control'. For example, a lender would not typically be a PSC for these purposes, as dealings under a third party commercial or financial agreement are not caught. Where a person 'exercises a function under an enactment' they too would not satisfy this condition and the guidance expressly notes a liquidator or receiver. This would also cover an administrator.
5	Having the right to exercise, or actually exercising, significant influence or control over the activities of a trust or firm which is not a legal entity and which meets any of the above conditions	• N/a

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

Scenario 2...

You are appointed over a UK company obliged to maintain a PSC register. Do you or the company still need to comply with the information gathering requirements of the PSC regime?

Under the PSC regime, a UK company has:

- a general duty to take 'reasonable steps' to find out if it has any PSCs and, if so, to identify them
- specific duties to issue certain information gathering notices (eg to anyone it knows, or has reasonable cause to believe, is a PSC or has information on anyone who may be a PSC).

There is no exemption from these information-gathering duties for a company in liquidation or administration. Failure by a company to comply with its PSC investigatory obligations is a criminal offence – for more, see the box on this page.

Where wholly owned by another UK company, a company can easily identify its PSC. Other situations, for example where there are multiple shareholders, may be more complex and require greater time and resource. For example, there may be shareholder agreements to review. Alternatively, it may be necessary to investigate voting patterns suggesting parties are acting together. A non-UK company cannot be included on a company's PSC register (unless the non-UK company has voting shares listed on certain markets and is subject to its own disclosure requirements). Instead, the UK company must 'look through' the non-UK company to find a relevant person or entity (if there is one).

What steps should a company take once insolvency proceedings have begun?

- **PSCs already identified**: a company should already have taken steps to identify its PSCs and, from 30 June 2016, will need to file with Companies House an annual confirmation statement (replacing the annual return) with information taken from its PSC register. Accordingly, in most cases, IPs should not need to do anything further.
- **PSCs not yet identified**: what further steps would be 'reasonable' will depend on the circumstances. For example, in most cases, it would not seem reasonable for a company in liquidation to need to incur any expenditure on compliance. What constitutes compliance for a company in administration will be a judgment call – depending, for example, on whether the company is likely to exit administration or whether it will continue trading for some time – but typically is unlikely to extend beyond issuing any information gathering notices.

Scenario 3...

You are appointed over a UK company that is a PSC on another UK company's PSC register. Do you or the company need to notify it of any information?

Where a company is a PSC of another company and on its PSC register, it is under an obligation to notify that company of any change in the 'required particulars' stated in the PSC register so that the company can update its PSC register accordingly. A company in liquidation or administration is not expressly exempt from this obligation.

The required particulars do not include whether the PSC is in any form of insolvency process and so you would not be required automatically to notify the UK company of your appointment. However, if you change the registered office of the company, you would need to notify the company so that it can update its PSC register. This would need to be done within two months of the day on which the change occurred.

Similarly, if you receive an information gathering notice from the UK company (eg to update its PSC register), the obligation to respond within one month remains applicable.

Failure by a company to comply with its PSC notification obligations or to respond to an information gathering notice is a criminal offence – for more, see the box below.

Ultimately, it may be preferable to provide the requisite information if that is not likely to prejudice creditor recoveries due to the cost involved or if failure could put at risk a transaction relating to the shares, as discussed in scenario 4. »

Could you be liable for any non-compliance with the PSC regime?

While noting the comments made in scenarios 2 and 3 about what steps would be needed to comply with the PSC regime once a company enters a formal insolvency process, failure to comply with the PSC regime's investigatory and notification obligations is a criminal offence. The offence is committed by the company and 'every officer'.

Criminal liability of the IP?

The key issue is whether an IP would be an 'officer' for the purposes of the PSC regime. In *Re Powertrain Ltd* [2015] EWHC B26 (Ch), the High Court was asked to consider, among other matters, the scope of the relief available under s1157 of the CA 2006. It held that, for the purposes of that section, the liquidators fell within the meaning of 'officer' – as somebody holding an office in relation to the company. But, the decision (which was unopposed) does not mean that a liquidator or administrator would always be treated as an 'officer' for the purposes of the Companies Act legislation. Notably, where a provision is looking to impose criminal liability on an 'officer', as in the PSC regime, that term should be given its ordinary, narrow meaning – ie as referring to a director, manager or secretary of the company – and not an extended meaning as to apply to an IP.

That is substantially different from a provision like s1157 which provides a remedy in the form of relief from civil liability and which, on the facts in *Powertrain*, operated in favour of liquidators looking to conclude a long-standing liquidation, distribute monies in their hands and protect themselves from remote product liability claims which could, in theory, arise in relation to a short period of trading which had taken place over nine years ago in an earlier administration.

Treatment of any fines

A fine referable to non-compliance after insolvency proceedings began would likely be treated as an expense in line with the decision of the Supreme Court in *Re Lehman; Re Nortel* [2013] UKSC 52.

The rationale for the PSC disclosure requirements is to combat abuse of corporate structures for illicit purposes. In general, there would be little benefit in prosecuting a company in administration or liquidation, or an IP, for any technical offence committed during the course of the insolvency process. Nevertheless, IPs should be careful to comply whenever possible to do so.

Scenario 4...

You are looking to carry out a share sale pre-pack of a UK company subject to the PSC regime. Does the PSC regime matter?

If a person fails to respond to an information gathering notice within one month, the requesting company may issue a 'warning notice'. This will inform the person that, unless it responds to requests for information within one month, the company may issue a 'restrictions notice' in respect of the relevant interest it believes makes the person a PSC (that is, the shares in the company, voting rights or rights to appoint/remove any member of the board of directors). A company is not obliged to issue either a warning notice or restrictions notice, although it may be advised that only by doing so can it discharge its duty to take reasonable steps to identify its PSCs.

> "If shares in a company cannot be realised and that is likely to delay creditor distributions, that could make the issue of a restrictions notice unfair."

Where a restrictions notice is issued, any transfer of the shares in the UK company, agreement to transfer the shares or exercise any rights in respect of them (including, for example, any entitlement to dividends or the exercise of any voting rights) will be void. Knowingly acting in breach of a restriction is a criminal offence.

Accordingly, when selling the shares in a UK company subject to the PSC regime you should check its PSC register to see if there are any outstanding information gathering notices or whether it has issued a

restrictions notice. Until 30 June 2016, you will need to ask the company for a copy of its PSC register to search it. After that date, a company may elect for Companies House to keep its PSC register on the central public registry, so you can search it by carrying out a full company search.

See the box on this page for what you should do if there are restrictions in place.

Para. 1(6) of schedule 1B of the CA 2006 provides that in deciding whether to issue a restrictions notice, the company must have regard to 'the effect of the notice on the rights of third parties' in respect of the relevant interest. BIS guidance adds that the company must consider whether the effect would be 'unfair' and, if so, provides that the company should not then impose restrictions. Further, if such a company were to issue a restrictions notice, para. 11(c) of schedule 1B provides that it must withdraw it if it discovers that the rights of a third party in respect of the relevant interest 'are being unfairly affected' by the restrictions notice.

In practice:

- a UK company whose shares are subject to security should not issue a restrictions notice in respect of those shares, or if it does it must withdraw it, because it would be unfair for a restrictions notice to prevent a secured lender from exercising its right to enforce its security (eg through a share sale pre-pack)
- similarly, if shares in a company cannot be realised and that is likely to delay creditor distributions, that could make the issue of a restrictions notice unfair or require its withdrawal if already issued.

What should you do if shares are subject to PSC restrictions?

If there are restrictions on the shares, you will not be able to proceed with the share sale until the restrictions are lifted.

You will need to ask the company to withdraw the restrictions notice. If it refuses to do so, the simplest solution may be to comply with any outstanding information gathering notice, as that will require the company to withdraw any restrictions notice under para.11 of schedule 1B of the CA 2006. Alternatively, you could suggest there is a 'valid reason' justifying the company's failure to respond. If satisfied, the company must withdraw the restrictions notice. Mere entry into an insolvency process is unlikely to suffice, although your lack of specific knowledge might be worth highlighting. As discussed, you could also point out that the rights of creditors are being unfairly affected such that the company is required to withdraw the restrictions notice. Finally, if all that fails, you will need to apply to court under the provisions of schedule 1B asking it to relax the restrictions and approve the sale. Clearly, this will have consequences for the timing of any share sale.

Scenario 5...

You want to make a distribution to shareholders but the shares are subject to a restrictions notice. What can you do?

If shares are subject to a restrictions notice under the PSC regime that would prevent any PSC from benefitting from their interest (eg by way of a dividend). However, there is an express carve-out for distributions to members made in a liquidation – these are not prohibited by any restrictions affecting the shares.

Conclusion

The PSC regime raises plenty of issues but with the right understanding should not cause IPs too much trouble. While the PSC regime certainly has its limitations, in time, as PSC registers are completed, it may turn out to be helpful in some insolvency situations, notably as an additional tool to help IPs identify shadow or de facto directors or to assist with conducting investigations.

REBECCA JARVIS (left) is a partner and global co-head in the restructuring and insolvency group at Linklaters LLP.

RICHARD BUSSELL (middle) is a partner and global co-head in the restructuring and insolvency group at Linklaters LLP.

PAUL SIDLE (right) is a senior PSL in the restructuring and insolvency group at Linklaters LLP.

Perfect harmony?

Chris Parker and **Catherine Burton** consider measures to address the harmonisation of substantive insolvency laws and the better coordination of cross-border group proceedings.

Despite an increasing move towards the globalisation of businesses, laws around the world primarily address insolvency by reference to single corporate entities. The challenges associated with the insolvency of businesses operating across borders are well known and, in the absence of tailored legislation, judges, insolvency practitioners and key creditors developed their own solutions to recognise the interconnected nature of cross-border insolvencies.

International bodies responded with treaties, protocols and two key legislative instruments: in Europe, the EC Regulation on Insolvency Proceedings (No 1346/2000) (the regulation); and internationally, the UNCITRAL Model Law on Cross-Border Insolvency (model law). Neither sought to harmonise substantive laws nor to provide tools specifically designed to look beyond the individual corporate debtor despite its positioning within a corporate group.

Those two limitations are now in the spotlight for legislative reform.

The European Commission

After ten years, and following extensive consultation, the EC regulation has been revised and on 26 June 2015 the recast regulation came into force. The majority of the provisions of the recast regulation will apply to proceedings opened on or after 26 June 2017. For the purposes of this article, key among those provisions are the introduction of:

- 'group coordination proceedings' where any office holder appointed to a company forming part of a corporate group can request that separate group coordination proceedings are opened; and
- a new standard claim form for all proceedings falling within the scope of the regulation. This is a significant first, admittedly small step towards introducing harmonised provisions affecting the underlying insolvency laws of each member state.

The recast regulation group coordination proceedings

While the recast regulation continues to respect the separate legal identity of each company in a corporate group it focuses on measures to enhance the coordination of the separate insolvency proceedings and cooperation and communication obligations between the different insolvency administrators and courts. Any court seized of insolvency proceedings in respect of a member of a group of companies can be requested to appoint an independent group coordinator whose role includes seeking to propose a comprehensive group coordination plan. The coordinator can mediate disputes between office holders of separate group companies, request information from such office holders, appear in each group member's insolvency proceedings and » request that the insolvency of any group member be stayed for up to six months. Participation in the group coordination proceedings is voluntary – office holders of each group company can opt out of the proceedings at any time and are obliged to consider, but not to follow, the recommendations of the group coordination plan.

The relevant court must be satisfied that (i) no group member that is likely to participate will be financially disadvantaged; and (ii) the proceedings are appropriate to facilitate the effective administration of the insolvency of the different group members.

> The most significant point to appreciate when considering reforms proposed by UNCITRAL and those proposed by the European Commission, is that only the latter has legislative powers.

The court will decide on the cost estimate and the share to be borne by each group company. The coordinator's remuneration is to be adequate and in proportion to the tasks he fulfils and to reflect reasonable expenses. The scope for duplication of work, interference in an office holder's independent decision-making process and, particularly, the imposition of a new layer of costs are likely to deter the commencement of group coordination proceedings. The costs may prove difficult to allocate across group companies, particularly when each member's office holder can elect to opt out and then back in again during the period from formulation to full implementation of the proposed plan. However, the possibility of appointing an independent professional to mediate inter-company disputes may provide a cost-effective solution enabling office holders who cannot find an acceptable negotiated settlement to avoid litigation and move swiftly to being able to concentrate on a recovery plan.

Harmonisation of insolvency laws across Europe

On 12 March 2014 the European Commission issued a recommendation asking member states to introduce national measures with a view to harmonising insolvencies and restructurings throughout the EU. The recommendation had no direct legislative effect. A few member states implemented reforms along the lines of the recommendation but the response was generally disappointing.

In December 2015 the Commission created an expert group consisting of 22 professional and academic advisers to prepare a potential legislative proposal containing minimum standards for a harmonised restructuring and insolvency law in the EU.

In March 2016, in line with the Commission's capital markets union action plan, the Commission launched a 12-week public consultation seeking stakeholders' views in relation to common principles and standards:

- which parties should be empowered to open proceedings;
- at which stage in the debtor's cycle should it be possible to open protective proceedings;
- the extent to which the absence of harmonised substantive laws affects the functioning of the internal market and the prospects of saving viable businesses;
- which minimum standards should be applied to harmonise avoidance actions; and
- whether there should be minimum standards of qualification for office holders dealing with cross-border cases.

Those bodies calling for greater harmonisation of insolvency proceedings across Europe will welcome this opportunity to explore the scope for greater harmonisation. AFME High Yield Division's view is that differences between national insolvency and restructuring regimes create uncertainty and increase costs for issuers and investors, discourage cross-border investment and often lead to liquidation rather than providing an opportunity to restructure a distressed company.

UNCITRAL

For most practitioners, UNCITRAL means the model law, now adopted in 41 member states. However, the other, key works of UNCITRAL's Insolvency Working Group (WGV) are equally important and an understanding of their role and effect is helpful before proceeding in this article to explain the current work of WGV.

- UNCITRAL's Legislative Guide on Insolvency Law is intended to assist lawmakers around the world by providing a statement of the objectives and principles that should be reflected in a state's insolvency laws. It is divided into four parts:
  - parts 1 and 2 discuss the objectives and key features of an efficient insolvency law;
  - part 3 addresses the treatment of group insolvency proceedings both domestically and internationally; and
  - part 4 focuses on measures to incentivise management and directors to act responsibly.
- UNCITRAL's Practice Guide on Cross-Border Cooperation supplements the model law by illustrating how issues arising in cross-border cases might be resolved by cross-border cooperation, in particular through the use of cross-border insolvency agreements and protocols.
- UNCITRAL's Judicial Perspective on the Model Law offers guidance, from a judge's perspective, on the issues relevant to deciding applications for recognition, based on the intentions of those who crafted the model law and the experience of its use in earlier cases.

Current work of UNCITRAL WGV

WGV comprises representatives of UN member states and its meetings include observers from leading international insolvency bodies. Three projects are currently being considered:

- facilitating the cross-border insolvency of multinational enterprise groups
- cross-border recognition and enforcement of insolvency-related judgments
- obligations of directors of enterprise group companies in the period approaching insolvency.

Facilitating cross-border group insolvency

In 2013 WGV agreed to continue its work on cross-border insolvency of multinationals by developing provisions on a number of issues including to extend the existing provisions of the model law.

The most significant point to appreciate when considering reforms proposed by UNCITRAL and those proposed by the European Commission, is that only the latter has legislative powers. Issues incorporated in European

> Creditors tire of the myriad of different insolvency proceedings that exist around the world and are often surprised by the divergence of approaches that still exists within the European Union.

regulations automatically become law in participating member states. UNCITRAL has no direct legislative power.

WGV is preparing draft text (the text) to provide group resolution tools that are sufficiently attractive to encourage members states to introduce them, while at the same time not give rise to concerns about the sovereignty of local courts being overridden by foreign courts. WGV agreed to introduce two overriding, fundamental principles into the text:

- the jurisdiction of the courts in the state in which a group member's COMI is located is and remains unaffected; and

- the remaining principles of the text do not replace or interfere with any process or procedure required by the jurisdiction in which the COMI of a group member is located.

The text is at a relatively early stage of drafting but its terms suggest that subject to these overriding principles, it should be possible to capture a generally acceptable procedure whereby:

- If an insolvency proceeding has been commenced in state A for a group member (X) whose COMI is in state A, any other group member (Y and Z) (whether their COMI is in state A or not) may participate in that proceeding to develop a group solution.
- Group solution is defined as proposals for the reorganisation, sale or liquidation of all or some of the operations or assets of more than one group member.
- Y and Z will not be allowed to join X's proceedings in the absence of consent of their home-COMI state.
- X's proceedings should not become the main coordinating proceedings unless it is considered that X would be a 'necessary and integral part' of a group solution.

"In the absence of tailored legislation, judges, insolvency practitioners and key creditors developed their own solutions to recognise the interconnected nature of cross-border insolvencies."

- Once an additional group member has been joined to X's proceedings, the court may appoint a group representative whereupon the proceedings become known as planning proceedings.
- The group representative's role is to seek to develop a proposed group solution, which can then be recognised in foreign courts.
- The group representative may seek to participate in any foreign proceedings relating to a participating group member, including to apply for appropriate relief to help implement the proposed group solution (such as the granting of a stay or moratorium).

The proposal may change significantly as it is further debated by WGV. Among the issues that will need further discussion are: (i) whether it should be possible for solvent group members to join the planning proceedings; and (ii) how any plan that forms part of the proposed group solution

should be voted upon – whether by applying each group member's local laws but allowing them to vote in the foreign planning proceedings according to those laws, or simply to take the plan to each member's home COMI courts, which can then arrange for approval and implementation.

WGV continued its discussions in New York from 2–6 May 2016. The group is considering ground-breaking proposals. Those with a keen interest in cross-border group insolvency solutions will be eager to learn how ambitious member states' delegations are prepared to be, as the text is further refined to clarify the various options available for implementation.

Conclusion

Harmonised laws Creditors, particularly those based in the USA familiar with Chapter 11 of the US Bankruptcy Code, tire of the myriad of different insolvency proceedings that exist around the world and, in particular, are often surprised by the divergence of approaches that still exists within the European Union. While fundamental differences in the law of secured transactions would need to be addressed before complete harmonisation could be achieved, there is a large selection of issues that could be harmonised across Europe (by the legislative force of the Commission) and more widely (by the choice of individual countries) such as the timescale for submitting claims, the definition of 'insolvent', and in time perhaps even consistent claw-back periods, and tests for reviewable transactions. The potential risks posed by harmonisation include the imposition of common standards which ultimately prove to be unhelpful, and the removal of compelling incentives to find better solutions. The European Commission is embracing calls for harmonised laws and the outcome of the current public consultation will inevitably prompt further work in this area.

"The possibility of appointing an independent professional to mediate inter-company disputes may provide a cost-effective solution enabling office holders to avoid litigation and move swiftly to being able to concentrate on a recovery plan."

Group insolvency The European Commission has already introduced its first proposed solution to the challenges of cross-border group insolvencies. We now have to wait and see how effective its solution proves to be, once group coordination proceedings take full legal effect in June 2017. UNCITRAL's proposals lack the force of a legislative body to impose them on member states. The proposals that its insolvency working group are now considering are therefore all the more ambitious. However, WGV's delegates will be well aware from member states' uptake of the model law that adoption can be slow. Ambitions may need to be tempered in order to arrive at a text that is sufficiently valuable to provide workable solutions and yet, at the same time, sufficiently attractive to incline member states to choose to adopt it in local laws. These are exciting times.

CHRIS PARKER (far left) is partner in the International Restructuring Group at DLA Piper.

CATHERINE BURTON (left) is head of restructuring knowledge management at DLA Piper.

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

Recent case summaries

Latest insolvency update from **Rowena Page**.

COMPANY INSOLVENCY

Re Longmeade Limited (in liquidation) [2016] EWHC 356 (Ch)

The joint liquidators of Longmeade Limited (the company) sought directions in relation to a potential claim against the secretary of state for business innovation and skills. The liquidators had been advised that the claim had good prospects of success and a litigation funder had offered finance. However, some 99 per cent of the company's creditors opposed the proposed litigation.

Since 26 May 2015, changes to the Insolvency Act 1986 brought about by the Small Business Enterprise and Employment Act 2015 (SBEE) had removed the need for a liquidator to obtain sanction before causing the company to commence or defend legal proceedings. However, in the face of such substantial opposition to the proposed claim, the liquidators sought directions as to how to proceed.

Snowden J summarised the changes to the law following the amendments introduced by the SBEE. He held that the removal of the need to obtain sanction did not of itself signal a change to the established approach of the courts to the exercise by liquidators of their powers that did not require sanction. The judge emphasised the court's reticence to become involved with, or interfere in, the process of commercial decision-making that liquidators face as a necessary incident of their office.

Summarising the application of these established legal principles against the modified regime post-26 May 2015 the judge held at [66] that:

- *A decision by liquidators appointed by the court as to whether to commence proceedings in the name of the company is essentially a commercial decision which the liquidators are entrusted to take without obtaining sanction;*
- *In taking the decision, the liquidators should act in what they believe to be the best interests of the insolvent company and all those who have an interest in its estate;*
- *The liquidators may, but are not obliged to, consult the creditors (or contributories) who have an interest in the estate;*
- *The liquidators should normally give weight to the reasoned views of the majority of such creditors (or contributories) provided that they are uninfluenced by extraneous considerations;*
- *If all those who are interested in the insolvent estate are fully informed and are unanimously of the same view, the liquidators should ordinarily give effect to their wishes;*
- *The court should not generally become involved in giving directions to liquidators as to how to make commercial or administrative decisions; and*
- *The court should not generally interfere with a commercial or administrative decision of liquidators after the event, unless it is a decision that was taken in bad faith or was a decision that no reasonable liquidator could have taken.*

Applying these principles to the case, Snowden J noted that the joint liquidators were not required to summon a meeting of creditors to vote on the proposed litigation, nor (even if they did choose to call such a meeting) would they be bound by the creditors' votes. The liquidators would be entitled to discount the views of the two largest creditor groups who were 'plainly influenced' by extraneous and individual considerations (in the case of the principal creditor, HMRC, a concern over suing another government limb and depleting the public purse; in the case of another substantial creditor, Lehman Brothers Holdings Inc, the risk of bad publicity).

Notably, and in express recognition of the highly unusual facts of the case, the judge also gave 'reassurance' to the liquidators, stating that if, following further enquiries, it emerged that there remained a creditor or creditors in favour of the litigation or not opposed to it who would lose the opportunity for a materially increased distribution if the proposed claim were not pursued then a decision by the liquidators that the company should pursue the claim would be within the range of decisions that a reasonable liquidator could properly take.

Finally, by way of postscript and without deciding the issue, Snowden J cast doubt on the impact of *Re Oasis Merchandising Ward* v. *Aitken* [1998] Ch 170 on the liquidators' ability to assign the claim if they so chose.

PERSONAL & COMMERCIAL INSOLVENCY

Stratford Edward Hamilton (1); James Ashley Dowers (2) (as joint trustees in bankruptcy of Charles Newell Brown) v. *Maureen Frances Brown (1); C&MB Holdings Ltd* [2016] EWHC 191 (Ch)

The petitioners were the trustees in bankruptcy of Mr Charles Brown, husband of the first respondent (Mrs Brown) and former director and shareholder of the second respondent (the company). Upon the petitioners' appointment in June 2014, Mr Brown's shares in the company had vested in them automatically pursuant to s306 Insolvency Act 1986. They had not been registered as shareholders, however, until 26 March 2015.

The petitioners sought (a) relief under s994 Companies Act 2006; alternatively (b) an order winding up the company on just and equitable grounds. This case update examines the winding up aspects of the case only.

Mrs Brown argued that the petitioners lacked standing to bring the petition given that, under s124(2)(b) Insolvency Act 1986, Mr Brown's shares in the company had not been held by them and had not been registered in their name for at least six months during the 18 months prior to the commencement of the winding up (being June 2015, the date of presentation of the petition).

The registrar rejected Mrs Brown's opposition. Drawing on the definition of 'member' in s250 Insolvency Act 1986, he noted that 'member', when used in s124(2)(b) is defined to include a person to whom shares in the company have been transferred or transmitted by operation of law. The definition of 'member' within s74 Insolvency Act 1986 (on contributories' liability) and of 'contributory' within s79 Insolvency Act 1986 would include the wider definition of 'member' set out in s250, notwithstanding that the name of the receiving party had not yet been entered onto the company's register of members.

The court held that between June 2014 and March 2015 the petitioners were to be regarded both as 'a member' of the company for the purposes of s74 and a 'contributory' for the purposes of s79. On that basis, and taking account of the s250 requirement for s124(2)(b) to be *'read accordingly'*, the court held that the petitioners should be treated as being registered for the period during which they were *'regarded… a member'* pursuant to s124(2)(b) and that they did therefore have standing to present the winding up petition. The fact that the word 'contributory' was used in s124(2)(b) and not 'member' did not change this conclusion. ◻

ROWENA PAGE is a barrister at Enterprise Chambers.

Legal Q&A

Emily Lockhart answers your insolvency queries.

Q I am the liquidator of a company in CVL. The creditors have made a requisition for a creditors' meeting to replace me as liquidator. What do I have to do and on what grounds would the creditors be successful if they applied to court for me to comply with their requisition if I refused to comply?

A Pursuant to section 171(2) of the Insolvency Act 1986 (IA), in a creditors' voluntary liquidation (CVL), a liquidator may be removed from office only by an order of the court or by a general meeting of the company's creditors summoned specially for that reason in accordance with the insolvency rules 1986 (IR).

In accordance with 4.114 of the IR, a meeting held under section 171(2)(b) for the removal of the liquidator shall be summoned by the liquidator if requested by 25 per cent, in value, of the company's unconnected creditors.

Provided the creditors who requisition the meeting are more than 25 per cent in value of the unconnected creditors of the company, then this constitutes a valid requisition. Although there is no specific definition of connected in the IR, it would seem reasonable to work on the basis that the definition of connected, as set out in s249 and s435 of the IA, would also apply in these circumstances.

If you refuse to comply, the creditors can apply to court under section 112 of the IA for an order directing you to convene a meeting in accordance with their valid requisition.

The case law on such applications has historically been in the context of compulsory liquidations and bankruptcy where the court has overridden the IR and directed that liquidators are not obliged to comply with valid requisitions for creditors' meetings.

In *Re Barings plc No 1* [2001] 2 BCLC 159, the court considered whether, if the meeting requisitioned was held, it would be conducive to both the proper operation of the liquidation and to justice between all those interested in the liquidation. In this case, the court held that the requisitioned meeting would not be conducive to the proper conduct of the liquidation or to do justice to all of the parties interested in the liquidation and the liquidators were

> **“You ought to consider complying or face costs consequences from the court if you are later ordered to comply.”**

granted an order directing that they did not have to convene a creditors' meeting.

However, in the recent case of *Re Overfinch Bespoke Vehicles Limited, Autobrokers Limited & Ors* v. *Dymond & Ors* (2015) [EWHC] 2691 (Admin), the court found that those tasks outstanding in the liquidation would not be substantively impacted on by a change in the liquidators. Furthermore, there was no suggestion of an improper motive. For these reasons, and considering the creditor-led nature of a CVL, the court ordered that the meeting should be held so that the creditors could determine the issue, especially given that the requisition had been validly served under 4.114 of the IR.

A CVL is a very creditor controlled process and as such the courts are unlikely to interfere with their decision making or deprive them of their voting rights under the IA, unless the exercise of such rights would be detrimental to the ongoing liquidation.

In the circumstances, unless you can say that the creditors' exercise of their rights would not be conducive to the proper conduct of the liquidation or to do justice to all the parties interested in the liquidation, you ought to consider complying or face costs consequences from the court if you are later ordered to comply.

Q Can a redress payment for swap mis-selling be paid direct to the former administrators of a now dissolved company to cover unpaid time costs?

A In accordance with paragraph 99 of Schedule B1 to the Insolvency Act 1986 (IA), where a person ceases to be the administrator of a company, the former administrators' remuneration and expenses shall be charged on, and payable out of, property of which he had custody or control immediately before cessation.

This question was considered in the recent case of *Walker and another* v. *National Westminster Bank Plc and another* [2016] EWHC 315 (Ch). In the *Walker* case, the court held that in circumstances where the bank was prepared to offer a company a redress payment as compensation for mis-selling interest rate swaps, conditional on the company being restored to the register – until and unless the company was restored to the register – there was no party capable of accepting the bank's offer of a redress payment. Furthermore, the court had no jurisdiction to order a payment unless some right had been successfully asserted against it by or on behalf of the company or it entered into a settlement agreement.

Even if there had been a right of payment capable of being enforced, the court was unconvinced that the former administrator's paragraph 99 charge could attach to it, as it was a voluntary payment that was not at that point due to the company. In the alternative, if the redress payment was an asset of the company, it would be payable *bona vacantia* to the crown to be dealt with in the normal way via restoration.

In the circumstances, it would be advisable to restore the company to the register and appoint an independent liquidator to accept the redress payment and enter into a settlement agreement and adjudicate on the competing claims to the redress payment in a distribution. At best the paragraph 99 charge could be considered an equitable mortgage but that would not equate to legal ownership and an order of the court would be required before the payment could be dealt with by the former administrators. ◻

EMILY LOCKHART is a business support and restructuring associate at Addleshaw Goddard.

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Mark Sanderson, Managing Director
T: +44(0)7771 678571
E: Mark.Sanderson@willistowerswatson.com

Samantha Taylor, Deputy Managing Director
T: +44(0)7956 661162
E: Samantha.Taylor@willistowerswatson.com

Damien Frost, Sales Director
T: +44(0)7342 089761
E: Damien.Frost@willistowerswatson.com

Sadie Easdown, Client Service Director – North, Scotland & NI
T: +44(0)7943 825923
E: Sadie.Easdown@willistowerswatson.com

Andrew McIntosh, Client Service Director – South & Midlands
T: +44(0)7944 918542
E: Andrew.Mcintosh@willistowerswatson.com

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The key link between insolvency and HR1

Amanda Rowe unravels the full tale of City Link and examines when the HR1 form should be submitted.

There has been significant press coverage surrounding the responsibilities of directors and administrators where redundancies are contemplated following the administration of the courier business, City Link Limited, and the subsequent legal action taken against the directors of the company. This highlights the increasing scrutiny that directors and insolvency practitioners are coming under to comply with the letter of employment law when already under considerable commercial and other legal pressures.

Background

City Link was founded in 1969, delivering parcels in the UK. By the end of 2014 it was an established national courier service operating from 53 depots and four hubs in locations across the UK.

The business had been suffering from sustained losses over a significant period of time. In April 2013, it was acquired by one of the Better Capital funds. Better Capital injected £40m into the business and provided management support for plans to turn it around.

While losses were reduced, by late summer 2014 it was becoming clear that additional funding would be required to enable the business to continue to trade. The directors therefore approached Better Capital to obtain the additional funding to finance a revised turnaround plan.

The City Link management team and their advisers produced an initial proposal for consideration by Better Capital, which they continued to refine. They confirmed, as far as they could, that various assumptions were reasonable and developed the plan further for the solvent restructuring of the business. At the same time the directors also considered a number of alternative options, including a sale of the business and a company voluntary arrangement. On 1 November 2014 a competitor made an indicative offer to acquire City Link Limited and a period of exclusivity was entered into for due diligence purposes.

> If the employer fails to undertake an information and consultation process, or fails to do so properly, a recognised trade union or employee representative can apply to the employment tribunal for a protective award.

On 18 November 2014 the period of exclusivity expired. Following due diligence, the potential purchaser withdrew its indicative offer to acquire City Link and said it was only interested in acquiring certain assets out of an insolvency process. This left the turnaround plan as the only solvent option.

Further refinements of the turnaround plan were presented to Better Capital with the final one on 19 December 2014. Throughout this period the directors were taking regular professional advice. They considered that the turnaround plan provided a reasonable prospect of avoiding insolvency and that it was in the best interests of City Link Limited and its creditors to continue to trade and pursue the plan.

By this stage a trade competitor who had been contacted previously had revived its interest in the business and was seeking further information. Ultimately this interest fell away following City Link entering administration.

On 22 December 2014 Better Capital advised the directors of City Link Limited that following presentation of the final turnaround plan it was unable to justify the investment required compared to the prospective return and risks involved. Following receipt of this information a decision was taken on 22 December 2014 by the board that City Link Limited should be placed in administration.

Following professional advice it was concluded that it was in the creditors' interests for trading to continue until Boxing Day to allow parcels in the system to be delivered and avoid significant liabilities arising from the disruption to direct and indirect customers. Substantial payments were made to unsecured creditors during this four-day period to ensure that their financial loss did not increase.

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The appointment of the joint administrators was to take place just before commencement of business on 26 December 2014. However, on the morning of 24 December 2014 an email was circulated by the National Union of Rail, Maritime and Transport Workers (RMT) to its members stating that City Link Limited was already in administration. This email was factually incorrect and put the business and assets of City Link Limited at risk. It was therefore decided that the appointment should be accelerated to protect the assets of City Link Limited. Accordingly, at 7.00 pm on 24 December 2014, City Link Limited entered administration and R H Kelly, C G J King and T Lukic of Ernst & Young LLP were appointed as joint administrators.

> "The learning point from these cases is that the government is not willing to see insolvency used as a defence for employment law non-compliance."

Legislation

There are two separate legal processes that must be undertaken when making large scale redundancies.

HR1 – Advance notification of redundancies

Under the Trade Union and Labour Relations (Consolidation) Act 1992 (TULRCA), advance notice must be given in writing to BIS by completing form HR1, if an employer proposes to dismiss 20 or more employees as redundant at one establishment within a period of 90 days or less. An employer must submit the form before giving notice to terminate an employee's employment and at least 30 days before the first of the dismissals takes effect where it is proposing to dismiss 20 or more employees as redundant; or at least 45 days before the first of the dismissals takes effect where it is proposing to dismiss 100 or more employees as redundant.

Failure to comply with the notification obligation is a criminal offence and the employer and the responsible director, manager, company secretary or other officer of the company will be liable on summary conviction to a fine. Since 12 March 2015 the fine is unlimited (before that date the maximum fine was £5,000 per breach).

A copy of the HR1 form must also be sent to any recognised trade union and elected employee representatives.

Collective redundancy consultation

Collective redundancy consultation obligations are triggered when an employer proposes to dismiss 20 or more employees as redundant within a 90-day period at one establishment. TULRCA requires that employers inform and consult on proposals for collective redundancies with unions or representatives of the affected employees. The consultation process must begin in good time and, in any event, at least 30 days before the first dismissal takes effect where 20 or more redundancy dismissals are proposed; or at least 45 days before the first dismissal takes effect where 100 or more redundancy dismissals are proposed.

There can be difficulties in determining what triggers the information and consultation obligations – they must begin when the employer's redundancy proposals are still at a formative stage and not when the employer has taken a decision to make redundancies or when the employer has taken a decision (such as a site closure) that will inevitably result in redundancies. However, the proposals need to be sufficiently advanced to have meaningful consultation.

Under the information and consultation process the following information must be provided as a minimum by the employer:

- the reasons for the proposed dismissals;
- the number and descriptions of employees whom it is proposed to dismiss as redundant;
- the total number of employees of any such description employed by the employer at the establishment;
- the proposed method of selecting employees who may be dismissed;
- the proposed method of carrying out the dismissals including the period of time over which the dismissals may take effect;
- the proposed method of calculating the amount of any redundancy payment to be made (over and above the statutory redundancy payment);
- details about the numbers of agency workers working temporarily and under the supervision of the employer, where they are working within the company and what type of work they are carrying out.

The information and consultation process must include consultation about ways of:

- avoiding the dismissals;
- reducing the number of employees to be dismissed; and
- mitigating the consequences of the dismissals and shall be undertaken by the employer with a view to reaching agreement with the appropriate representatives.

If the employer fails to undertake an information and consultation process, or fails to do so properly, a recognised trade union or employee representative can apply to the employment tribunal for a protective award. If there are no recognised trade union or employee representatives, individual affected employees can make applications to the employment tribunal. The award can be for up to 90 days' pay for each affected employee. The purpose of the award is to penalise the employer for its failure to comply with its obligations rather than to compensate the employees.

The legislation therefore raises a number of questions, including:

- At what point does the legal duty to consult arise?
- If the duty to consult is triggered, at what point must collective consultation commence?
- At what point is the duty to notify the secretary of state about collective redundancies triggered?
- If the duty to notify the secretary of state is triggered, when should he be notified?

These may seem like straightforward questions; however, the legislation and case law makes the answers less than clear.

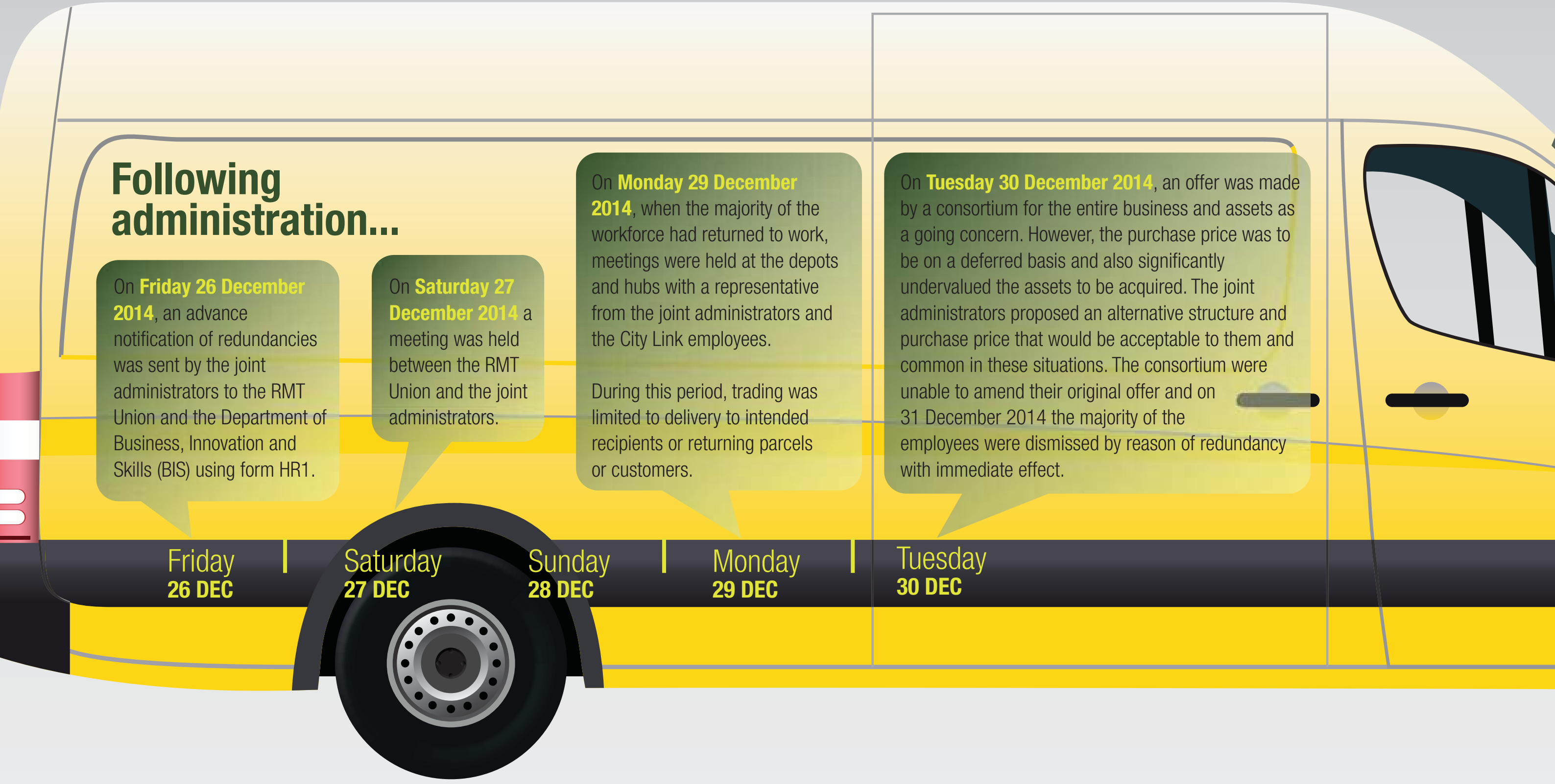
Legal action

In 2015 BIS commenced criminal proceedings against the three directors of City Link Limited for failure to notify BIS of proposed redundancies. This was the first time BIS has taken such action. BIS alleged that the directors should have concluded that redundancies were inevitable on 22 December 2014 and that the duty to notify the secretary of state and commence collective redundancy consultation began on that date. The directors presented arguments that there was no proposal to make redundancies or corresponding notification obligation on 22 December 2014. It is important to highlight that this was only two days prior to the appointment of administrators, so the prosecution was pursued for a relatively short period of alleged inaction.

> "There was certainly no precedent set to clarify exactly when the obligations to inform and consult appropriate representatives and notify the secretary of state are triggered."

It is also interesting to note that in this instance BIS chose not to pursue an earlier date when the turnaround plan was still being refined.

This action through the courts is a change of approach by BIS in bringing criminal proceedings against directors under Section 194 of the TULRCA for failing to give BIS advance notice of redundancies. This perhaps should not have been seen as surprising given the 2015 call for evidence on collective redundancy consultation for employers facing insolvency, with the government seemingly keen to ensure that employment



law is adhered to or that the courts clarify the timing questions raised earlier in this article.

As a result of the City Link Limited redundancies, the RPS has paid out (to date) over £7m in statutory redundancy pay, payments in lieu of notice, holiday pay, arrears of overtime and commission payments to former employees of the company. The criminal proceedings against the directors signify greater interest by BIS in large scale redundancies involving insolvent companies.

The prosecution arguments centred on the contention that the directors should have seen that redundancies were inevitable given the company's financial circumstances and the number of alternative options that the directors had already considered. The arguments also included the fact that the duty was an absolute one with no time delay allowed. In the court hearing against the City Link directors, judge Goodman concluded that the directors had genuinely believed a sale of the business was not only possible but quite probable. Goodman J said *'Retrospective use of a crystal ball is a concept I struggle at the time to understand. A director cannot be expected to put a crystal ball on his or her desk at a time of huge shock and turmoil and predict the likely consequences of an action, unless a consequence is either the only foreseeable one or is the only consequence that can be reasonably envisaged'.*

Subsequently the case against the directors was dismissed (Goodman J did not make comment on, or allowance for, reasonable administration or practical time delay period before beginning consultation and not informing the secretary of state).

This conclusion has to be considered against the backdrop of the previously failed sale process, one potential interest at the date of administration and, ultimately, the administrators receiving only one offer that was ultimately deemed to be unviable. This showed that in the City Link case there was still uncertainty on the outcome for the business and whether redundancies would ultimately be made. The directors were also able to show that they had taken proper professional advice throughout the process and had acted on the advice given.

> **By the end of 2014 City Link was an established national courier service operating from 53 depots and four hubs in locations across the UK.**

Following his decision Goodman J stated that *'I would add only that no employer should take these findings to be a precedent that an employer can avoid its responsibility under section 193 (of TULRCA) by simply going into administration. My finding in this case that no proposal [to make collective redundancies] had been made is based on the evidence in this case, not a general principle in relation to administration generally.'*

While directors may take some comfort that if they act in good faith always balancing the interests of all stakeholders the courts will take a balanced view on the challenging situation they face, there was certainly no precedent set to clarify exactly when the obligations to inform and consult appropriate representatives and notify the secretary of state are triggered.

Case against the company director and one of the joint administrators of USC

In a similar case BIS have also commenced criminal proceedings against the director of West Coast Capital (USC) Limited (a subsidiary of Sports Direct) for failure to notify BIS prior to redundancies made in January 2015.

One of the joint administrators has also been charged with the same offence in that the HR1 form giving BIS advance notice of the redundancies was not submitted until after the redundancies took place. This is the first time an IP has been prosecuted for this type of offence.

The legal issues hearing was held in the middle of March 2016 with the judgment reserved until 27 April 2016. The substantive hearing is due to be held in early summer.

Conclusion

The learning point from these cases is that the government is not willing to see insolvency used as a defence for employment law non-compliance and will bring criminal proceedings against individuals as well as companies. Directors, managers, company secretaries and other officers and their advisers must make sure they are aware of their employment law obligations and bring them to the front of their plans to avoid personal liability.

AMANDA ROWE is an assistant director in restructuring at EY.

Pedalling through Dutch pre-packs

Barbara Rumora-Scheltema explains the situation for the protection of employees' rights and pre-packs in the Netherlands.

European Directive 2001/23/EC (the directive) relating to the safeguarding of employees' rights in the event of transfers of undertakings provides in articles 3 and 4 that the transferor's rights and obligations arising from employment agreements or employment relationships existing on the date of a transfer shall, by reason of such transfer, be transferred to the transferee, and that the transfer of the undertaking shall not constitute grounds for dismissal by the transferor or the transferee. A transfer under the directive is a transfer of an economic entity that retains its identity, meaning an organised grouping of resources, which has the objective of pursuing an economic activity, whether or not that activity is central or ancillary.

> Silent trustees have mostly been utilised in recent years – and not always without controversy – for the preparation of an asset sale.

Pursuant to article 5 of the directive, and unless member states provide otherwise, articles 3 and 4 do not apply to a transfer of an undertaking where the transferor is the subject of bankruptcy proceedings or any analogous insolvency proceedings which have been instituted with a view to the liquidation of the assets of the transferor and are under the supervision of a competent public authority (such as an insolvency practioner authorised by a competent public authority).

Bankruptcy without TUPE

The directive has been implemented in the Dutch Civil Code (DCC) in articles 7:662 through 7:666. Article 7:666 DCC prescribes that the rules relating to a transfer of undertakings do not apply if the employer has been declared bankrupt and the enterprise forms part of the bankrupt estate. Under Dutch law, there are two types of bankruptcy proceedings for enterprises: bankruptcy (*faillissement*) and suspension of payments (*surseance van betaling*). A bankruptcy affects all creditors of the debtor (although the effects for secured creditors are limited) and in most cases leads to liquidation of the assets and dissolution of the debtor company. A suspension of payments only affects non-secured and non-preferred creditors (although there may be limited effects for secured creditors) and is aimed at a restructuring of the debtor. The employee protection under the directive applies to bankruptcy proceedings only, and not to suspensions of payments.

Bankruptcy over a company is a court decision, following an application by the debtor or one or more of his creditors. The court appoints one or more bankruptcy trustees and a supervisory judge. The court has full discretion as to whom it appoints as bankruptcy trustee and is not bound in any way by requests or suggestions from either the debtor or the creditors. As a consequence of the bankruptcy, the debtor loses all powers to manage, and dispose of, his assets. In case the debtor is a company, its management can no longer represent the company in the management and disposal of assets of the company. Management and disposal of the assets that form part of the bankrupt estate lie with the bankruptcy trustee, who requires approval from the supervisory judge for certain acts. Such approval is required, among other things, for selling or transferring any assets out of the bankrupt estate. Although the bankruptcy trustee acts for the benefit of the joint creditors, the formal role of the creditors is limited. A creditors' committee, although possible, is not required and in practice is appointed by the court only in exceptional circumstances. Even where a creditors' committee has been appointed, its powers are of an advisory nature only. In particular, a bankruptcy trustee does not require the approval of the creditors or creditors' committee for selling assets from the estate.

Typically, a bankruptcy trustee will try to sell the enterprise of the bankrupt debtor quickly in order to preserve value. And so, during the first days and weeks after the bankruptcy, the trustee will spend most, if not all, of his time trying to find a buyer for the debtor's assets. The purchaser of these assets will not have to worry about the Transfer of Undertakings (Protection of Employment) Regulations (TUPE) arising from the directive and its implementation into Dutch law. He can offer a new employment agreement to anyone, and is in principle not obliged to take on the same number of employees (or the same employees). However, the trustee will try to get not just the best price for the assets, but also a buyer willing to enter into employment contracts with as many of the debtor's employees as possible. Although to some extent it depends on the type of business conducted by the debtor, a general rule is that the sooner the trustee is able to sell the assets, the higher their value and also the higher the number of employees that a purchaser is willing to take on board.

> In the past five years or so a practice has grown whereby a sale of assets is prepared even before the debtor is declared bankrupt and a bankruptcy trustee is appointed.

A Dutch pre-pack

It is because of this economic reality that in the past five years or so a practice has grown whereby a sale of assets is prepared even before the debtor is declared bankrupt and a bankruptcy trustee is appointed. This practice is commonly referred to as a Dutch pre-pack. The court is requested by the debtor to disclose beforehand whom it would appoint as bankruptcy trustee in the event that the debtor would apply for bankruptcy. Most, although not all, courts will oblige and will appoint what is called a 'silent trustee', on the basis that preparations for a bankruptcy by the debtor, together with the silent trustee, will be in the interest of the joint creditors and will lead to higher proceeds for the estate.[1] There are usually a number of conditions attached to the appointment of a silent trustee. For example, the debtor will have to disclose any and all information that the silent trustee needs, and will have to cooperate fully with the silent trustee. Failure to do so may cause the court to appoint a different person as bankruptcy trustee when the application is made. Once appointed, a silent trustee may do a number of things. He will usually start by familiarising himself with the case and study the financial information available. He may try to prepare an asset sale, but he could also try to secure financing post-bankruptcy, or both. If the debtor is in the healthcare business, the silent trustee will probably want to take measures in order to avoid emergency health issues (which could for example be caused by suppliers seizing their stocks).

“A general rule is that the sooner the trustee is able to sell the assets, the higher their value and also the higher the number of employees that a purchaser is willing to take on board.”

Silent trustees have mostly been utilised in recent years – and not always without controversy – for the preparation of an asset sale, whereby a sale of part or all of the enterprise of the debtor is prepared prior to bankruptcy and the transaction itself is effectuated shortly – usually within hours – after the court has rendered the bankruptcy decision. In such a Dutch pre-pack, the silent trustee will, together with the debtor, pursue the best possible asset sale both in terms of proceeds as well as number of employees being able to keep a job. The purchaser, usually a special purpose vehicle, will sign a purchase agreement with the bankruptcy trustee immediately after the bankruptcy and take delivery of the assets he has purchased. He will have committed to offer new employment contracts to a specified number of employees of the debtor.

A look at cases

From an investigation of 48 appointments of silent trustees, one author concluded that the average percentage of employment that had been safeguarded through a pre-pack was 68, versus 24 per cent of employment safeguarded following an asset sale post-bankruptcy that had not been pre-packed.[2] These successes, along with the call from insolvency practitioners to codify the practice of the appointment of silent trustees, has led the legislater to introduce a proposal for an amendment to the Dutch Bankruptcy Act that is currently pending before parliament.[3] However, pre-packs have been criticised by some of the unions, who fear that bankruptcies may be abused as a means to get rid of expensive employees. The unions have initiated litigation against the buyers in two pre-packs, namely Heiploeg (a processor of shrimps and related products) and Estro (a childcare organisation). In the Heiploeg case, all claims of the unions were rejected at first instance[4], and the case is currently before the appellate court. In the Estro case, however, the court has asked the European Court of Justice (ECJ) to advise on questions about prejudice.

The Estro pre-pack took place in early July 2014. Smallsteps, a newly incorporated entity owned by some of the lenders/shareholders of Estro, acquired about two-thirds of Estro's childcare locations within hours after Estro had been declared bankrupt. It offered employment to approximately two-thirds of former Estro employees, but did not take over the exact same (or exact same number) employees. FNV (the Dutch Federation of Trade Unions), along with four former employees who had not been offered a job by Smallsteps, initiated proceedings against Smallsteps, arguing that articles 3 and 4 of the directive did apply in a pre-pack and claiming a declaration of law that all employees who had previously worked at Estro locations that had been acquired by Smallsteps had, in fact, as a result of the transfer of enterprise, become employees of Smallsteps. FNV argued, among other things, that the bankruptcy of Estro was not instituted with a view to a liquidation of its assets and therefore that the exception of article 5 of the directive did not apply.

In its interim decision of 24 February 2016[5], the court wondered whether the exception of article 5 of the directive indeed applies to a pre-pack, and considered that questions should be asked from the ECJ before a decision could be taken. These questions have now been published by the ECJ[6], and aim to find out whether articles 3 and 4 of the directive apply in situations where a transfer of an undertaking (or part thereof) has been prepared prior to a bankruptcy but effectuated only after bankruptcy as is the case in Dutch pre-packs. While these questions are pending, there remains uncertainty about the consequences of a restructuring through a pre-pack as has become practice in the Netherlands. □

“One author concluded that the average percentage of employment that had been safeguarded through a pre-pack was 68, versus 24 per cent of employment safeguarded following an asset sale post-bankruptcy that had not been pre-packed.”

1 The courts of Middle-Netherlands (Utrecht), Overijssel and Limburg do not appoint silent trustees because of their consideration, briefly put, that such an appointment requires an explicit basis in law.
2 Source: J.R. Hurenkamp, 'Failliet of fast forward? Een analyse van de pre-pack in de praktijk' ('Bankrupt or fast forward? An analysis of the pre-pack in practice'), TvI 2015/50.
3 Proposal for Act number 34,218 for 'Amendment of the Bankruptcy Act in relation to the appointment by the courts of an intended trustee in order to advance the handling of a possible bankruptcy and the increase of the chances of continuation of an enterprise or a restructuring of viable parts of a company', commonly referred to as Act for the Continuation of Enterprises (*Wet Continuïteit Ondernemingen*) or WCOI.
4 District Court Overijssel 28 July 2015, ECLI:NL:RBOVE:2015:3589 (FNV et al./Heiploeg).
5 District Court Middle-Netherlands, location Almere, 24 February 2016, ECLI:NL:RBMNE:2016:954 (FNV et al./Smallsteps).
6 Case number C126/16, to be found at http://eur-lex.europa.eu/legal-content/NL/TXT/?uri=CELLAR:efcf473c-168c-11e6-ba9a-01aa75ed71a1.

BARBARA RUMORA-SCHELTEMA is a lawyer and partner in NautaDutilh's Restructuring and Insolvency department. She has acted as lawyer for Smallsteps in the case referred to in this article.

Employment and insolvency – strange bedfellows?

Simon Kerr-Davis and **Philippa O'Malley** explain the key issues for practitioners when employment law and insolvency meet.

In a recent response to its call for evidence, the Department for Business, Innovation and Skills (BIS) concluded that there is no conflict between insolvency and employment laws. Yet despite this conclusion, the two regimes continue to live uneasily together and raise particular difficulties for insolvency practitioners. Perhaps this is unsurprising, given the inherent conflict between the intention and purpose underlying the two sets of legal provisions: employment law is designed to provide protection for employees, whether by making certain dismissals unlawful, ensuring continued employment in particular circumstances or requiring consultation before decisions can be taken. This can often be at odds with the underlying purposes of insolvency law, particularly those aspects that aim to rescue businesses, often requiring speedy action to be taken to preserve value, and equally speedy decisions to close down uneconomic parts of the business and overall to ensure fairness among creditors of all types. This article considers the key employment issues that are likely to arise for an insolvency practitioner and ways to deal with the potential risks.

Making redundancies

Redundancies are often necessary at an early stage in an insolvency, whether due to overstaffing, a reduction in work or the closure of the business. Redundancy is a potentially 'fair' reason for dismissing an employee, but employees must be fairly selected for redundancy and a fair process must be followed, which includes consulting with the employees. Failure to do so could result in a finding by an employment tribunal that the employee has been unfairly dismissed or discriminated against. Discrimination in this process should be of particular concern to insolvency practitioners – while liability for the majority of employment claims would sit with the insolvent employer (or with the Redundancy Payments Office), individual administrators can be liable for discrimination against an employee.

> "Discrimination in this process should be of particular concern to insolvency practitioners – individual administrators can be liable for discrimination against an employee."

Where a large number of employees are to be made redundant, the situation is more complicated. Legislation known as TULR(C)A (the Trade Union and Labour Relations (Consolidation) Act 1992) requires a collective consultation process to be carried out where an employer proposes to dismiss as redundant 20 or more employees within a 90-day period. This process includes electing employee representatives (if there is no existing body of representatives or recognised trade union), giving information about the proposed redundancies to the representatives and consulting about ways of avoiding redundancies or mitigating the impact.

Where 20 to 99 redundancies are proposed, dismissals cannot take effect until 30 days after the start of the consultation process (although notice of dismissal can be given before the 30 days are up). Where 100 or more redundancies are proposed, this increases to 45 days. This time restraint can be at odds with the realities of an insolvency situation, where it may be considered necessary to make redundancies quickly to preserve value and prevent ongoing costs being incurred. Further, administrators will be conscious that 14 days after their appointment the employment contracts of employees who are still employed will be adopted, with ongoing employment liabilities becoming an expense of the administration. This creates a clear conflict between the TULR(C)A time periods and the needs of an administrator to minimise expense.

Failure to comply with collective consultation requirements can result in an employment tribunal claim for failure to inform and consult, for which a protected award may be made of up to 90 days' pay per employee.

Filing form HR1

When an employer is proposing redundancies which would trigger the collective consultation, the employer is required to file the statutory form HR1 informing the government of this proposal. The failure to file the necessary form carries a criminal penalty, an unlimited fine, which has recently been brought to bear in a number of insolvencies, either as a failure of the directors of the company concerned, or as a failure of the administrators after an administration has begun. Filing a timely form HR1 and updating it as necessary has therefore become a necessity in any insolvency where job losses are contemplated.

Sale of the business

If the insolvent business, or part of it, is sold, the Transfer of Undertakings (Protection of Employment) Regulations 2006 (commonly known as TUPE) may apply. This will depend on what is actually being sold.

TUPE will apply when there is a transfer of all or part of a business sufficient to constitute an 'organised grouping of resources', which retains its identity post-transfer. Assessing this test requires a detailed review of the type, nature and amount of assets being transferred.

If TUPE does apply, the usual rules are that the employment of the employees who are wholly or mainly assigned to the business will transfer automatically to the purchaser, together with almost all rights and liabilities relating to their employment. In addition, liabilities in relation to employees who were dismissed shortly before the transfer can also transfer. This can be a significant concern for potential purchasers, who could find themselves liable for employees who were made redundant before the sale. Further,

> **Filing a timely form HR1 and updating it as necessary has therefore become a necessity in any insolvency where job losses are contemplated.**

dismissals because of the transfer will be automatically unfair and changes to terms and conditions of employment because of the transfer will be void. It is not possible to contract out of TUPE, but the parties can agree who will bear certain liabilities through indemnification.

In an insolvency situation the usual TUPE rules will be modified, but the extent of the modifications depends on the type of insolvency procedure. Where there is 'bankruptcy or analogous insolvency proceedings' (most obviously a liquidation), there will be no automatic transfer of employees to the purchaser. However, where there are 'relevant insolvency proceedings', which are not opened with a view to liquidation, a definition which has been held to include administrations (whether pre-pack or otherwise), the relaxations of TUPE are very limited. Employees will still transfer but liability for certain debts will not: this includes up to eight weeks' arrears of pay; six weeks' accrued holiday payment in lieu of notice and a statutory redundancy payment. Instead, these amounts will be payable from the National Insurance Fund. There is also some flexibility when it comes to changing the terms and conditions of employment of transferring employees, provided that terms are being varied with the intention of safeguarding employment.

TUPE imposes information and consultation requirements on both the seller and the purchaser of the business. The purchaser will need to inform the seller about any measures that it intends to take post-transfer in relation to the employees, such as redundancies or changes to working conditions. The seller must then give representatives of affected employees certain information about the transfer and consult about any measures (the same obligations apply to the purchaser if it has any employees who will be affected by the transfer). As with collective redundancy consultation, if there are no existing representatives and no recognised trade unions, representatives will have to be elected. Again, the election and consultation process can be difficult in an insolvency situation where time is limited and the business may not have the resources to support a lengthy process. However, a failure to do so could result in an employment tribunal claim for failure to inform and consult, for which a protected award may be made of up to 13 weeks' actual pay for each affected employee, such an award being payable to the employees themselves.

Tips for insolvency practitioners

- Be careful when making dismissals to ensure that there is no discrimination.
- File an HR1 at the earliest opportunity when redundancies are contemplated (even if other options, such as sale, are still being considered).
- Some degree of redundancy or TUPE consultation is better than none. Making attempts to consult, even if for a limited time, will help minimise potential liabilities and be welcomed by any purchaser of the insolvent business.
- On a sale, consider what indemnity protection is necessary from the purchaser to ensure that all claims and potential claims will be liabilities for the purchaser rather than for the insolvent estate.
- Before terminating outsourcing agreements consider who, if anyone, will provide the services going forward and whether there is a risk of employees transferring under TUPE.

In addition to giving information to representatives, the seller needs to notify the purchaser of 'employee liability information'. This information must be given at least 28 days before the transfer, unless this is not reasonably practicable. Failure to do so could result in potential compensation of £500 per employee, the compensation being payable to the buyer.

Terminating outsourcing and service agreements

TUPE does not just apply on the sale of a business, but also when a 'service provision change' occurs. A service provision change means a situation in which a service is outsourced, moved to a new outsourced provider or taken back in-house from an outsourced provider.

There are also certain conditions that must be met. Immediately before the change, the employees who are performing the activities (which must not consist wholly or mainly of the supply of goods) must be organised in a grouping that has the provision of those activities as its principal purpose. Further, post-change the activities that will be carried out must be fundamentally the same as the activities pre-change.

> **TUPE imposes information and consultation requirements on both the seller and the purchaser of the business.**

Where these conditions are met, TUPE will mean that employees who were performing the activities will transfer to the new provider, together with the rights and liabilities outlined above. For an insolvency practitioner, this can mean that when an outsourced service (for example, for cleaning services) is terminated, there is a risk that employees will transfer from the service provider to the insolvent business if the services are brought in-house. Even if the services are not brought in-house, the service provider and its employees may claim that there has been a transfer and dealing with such claims can be time consuming and costly.

SIMON KERR-DAVIS is counsel at Linklaters LLP.

PHILIPPA O'MALLEY is a senior associate at Linklaters LLP.

Best-laid schemes

Paul Marsh looks at how employees of an unlimited partnership can fall outside of the remit of the Redundancy Payments Scheme.

Owners and managers should be well informed as to the financial status of their business and, as a consequence, be aware of impending insolvency. Often they instigate the formal insolvency procedure themselves. For employees, on the other hand, the failure of their employer more often than not comes without warning and can leave them ill prepared to face the consequences.

For this reason, the Employment Rights Act 1996 (ERA) provides that if an employer becomes insolvent, certain debts owing to employees, including outstanding wages and redundancy payments, may be paid by the secretary of state from the National Insurance Fund.

A safety net for employees

The Redundancy Payment Scheme (the scheme) ensures that sums due to employees, albeit capped at the statutory rate, can be paid to them quickly in the event of the insolvency of their employer business. The scheme provides a safety net and a degree of protection from the employer's failure. The secretary of state, in turn, can seek to recover payments on a subrogated basis from the insolvent business.

However, the scheme does not apply to all insolvencies and as such there are categories of employee that are not afforded protection. For the purposes of the scheme, section 183 of the ERA defines 'insolvency' in terms of formal insolvency proceedings. Employees of businesses that are subject to administration, liquidation, bankruptcy or voluntary arrangement are all afforded protection. However, the employees of an unlimited liability partnership, subject to a winding up order, where no bankruptcy orders have been made against the individual members, are not afforded protection by the scheme.

In theory, this makes perfect sense. In an unlimited liability partnership, the members of the partnership are the employers of the staff. As such, even when the partnership has been wound up, the staff are able to apply to the members directly, as the employer, for payment of wages, and any other monies they are entitled to arising out of their employment. In addition it avoids a scenario where the secretary of state, and therefore the taxpayer, makes payments under the scheme in circumstances where members of the partnership may not be insolvent.

> In an unlimited liability partnership, the members of the partnership are the employers of the staff.

Falling outside the lines

Although the approach adopted by the scheme is technically correct, its application in practice can be harsh. I have been involved in a case recently where an unlimited liability partnership was wound up by the court. Upon liquidation of the partnership, it ceased to trade. As a consequence, its entire staff became redundant. Had the staff been employed by a company, the staff would have been entitled to make immediate claims to the scheme seeking to mitigate their losses. However, in this case, the position adopted by the secretary of state was that the employees were not entitled to benefit from the scheme until such time as bankruptcy orders had been made against each of the members, or they had entered into voluntary arrangements. Most individuals who need to rely upon the scheme are unlikely to be able to afford the costs of issuing and prosecuting bankruptcy petitions, especially against a large number of individual members. In reality most employees do not have claims that satisfy the bankruptcy threshold. As such, the employees often need to rely upon further action by a creditor or upon the members seeking to place themselves within the insolvency regime. Even if employees are in a position to petition for the bankruptcy of the members, there is invariably a significant delay. In some parts of the country many months can elapse between the presentation of a petition and the making of a bankruptcy order by the court. As a consequence, in the case of an unlimited liability partnership the protection for employees envisaged by the scheme, does not, in practice, exist.

In the case that I dealt with, the liquidator stepped in and issued petitions against the members with a view to accelerating the employees' ability to make claims under the scheme. However, inevitably, there was a delay, which would not have been faced by employees of a limited company.

The flaws of partnership

In practice, this situation can be avoided if concurrent action is taken in relation to the members, either by way of bankruptcy or voluntary arrangements. In fact it would be unusual, where the process was driven by the partnership, for the individual members not to be tied into insolvency proceedings that would satisfy the criteria of section 183 of ERA. While this may be feasible in those cases where the formal insolvency action is being driven by the partnership itself, it is less certain when the formal insolvency procedure is being driven by a creditor. Many creditors will target the partnership without seeking to place the underlying members into the insolvency regime. In those cases, the liquidation of the partnership will inevitably result in the cessation of trade and the redundancy of the employees. In the absence of further action against the individual members it appears that the employees are deprived the protection afforded under the scheme to their counterparts in insolvent limited companies. □

PAUL MARSH
is a partner at Hillyer McKeown.

Changes on the horizon in Guernsey's insolvency regime

Guernsey is about to embark on a wholesale revision of its personal and commercial insolvency regime, which will have wide-ranging repercussions for those involved in the Guernsey restructuring market.

Ben Rhodes, Licensed Insolvency Practitioner and a Director of Grant Thornton's Channel Islands practice, has been engaged to advise the States of Guernsey's Commerce and Employment Department (C&E) on the changes. Ben is a member of the ARIES Legal & Regulatory Committee in Guernsey, and is currently involved in the drafting of Guernsey Insolvency Practice Statements (GIPS).

Background

Guernsey's insolvency regime has remained largely unchanged for many years. The law is slim and deficient in a number of areas. While Guernsey has the benefit of a flexible and pragmatic court, and has been able to successfully navigate significant cases, there are nonetheless areas of uncertainty and unpredictability.

Reform of Guernsey's insolvency regime is long overdue. The last significant update to the commercial regime was the introduction of the Administration procedure and the Scheme of Arrangement procedure in 2008. The personal regime has had no substantial reform for more than half a century, and is largely governed by the customary law procedure of désastre and saisie.

Working group and consultation

In 2013, C&E established a working group to advise on the reform, consisting of restructuring professionals from the legal and accounting professions, representatives of HM Sheriff's office and the GFSC.

Following input from the working group, C&E issued a consultation paper in 2014. The consultation paper covered 40 topics in total, both personal and commercial, including a mixture of detailed proposals and higher level questions regarding the general legislative framework.

I was engaged to assist in analysing the consultation responses and to set out recommendations for consideration by C&E.

Consultation response document

A consultation response was issued in February 2016 setting out the proposals to be taken forward, with prioritisation as either a first or second phase of work. There are over 20 changes to be introduced in the first phase alone.

Personal insolvency

The first phase involves the introduction of a 'Low Value Debt Relief' order, available for individuals with limited means who satisfy certain criteria. They can apply to Court to have their debts frozen and written off. This is similar to the 'Debt Relief Order' in the UK, and to the 'Viscount's Remission Order' currently being considered in Jersey.

Commercial insolvency

There are a large number of changes to be introduced including the following:

- Insolvency rules will be introduced to offer guidance on procedural matters, such as the calling of creditor meetings or reporting suspicions of misconduct. C&E considers that a rules committee, including industry practitioners, would be best placed to draft and update the rules.
- There will be greater protection for creditors in insolvent voluntary liquidations. Liquidators will be required to give notice to creditors of the liquidation, and will be required to report to creditors and hold a meeting of creditors. There will also be a requirement that liquidators be independent, in an insolvent voluntary liquidation, in order to avoid potential conflicts of interest.
- Office holders will be required to report to relevant authorities, if they find or suspect misconduct on the part of the directors or officers of a company.

Full details are available at **www.grantthorntonci.com/en/News-Centre/rr/states-of-guernsey-commerce-and-employment/**

BEN RHODES,
Director
T: +44 (0)1481 753431
E: ben.rhodes@gt-ci.com

Next steps

The proposed changes will enhance Guernsey's reputation as a safe place to do business. Many are in line with other jurisdictions with well-developed insolvency regimes such as the UK.

While there has been significant progress, it is likely to be some time before the changes become effective. There are significant resource implications for C&E in developing the policy and drafting the legislation. Change to the corporate insolvency regime is an important issue for Guernsey's financial services industry and broader business community and political endorsement is key.

The next stage is for detailed proposals for the first phase projects to be included in policy letters for consideration by the States of Deliberation.

In the meantime ARIES, the Channel Islands chapter of INSOL International, is drafting the equivalent of UK Statements of Insolvency Practice, which its members can follow on a voluntary basis. These are being drafted by the ARIES Legal & Regulatory Committee in Guernsey, where Guernsey practice requires it. These will focus on key areas including office holder investigations; creditor meetings in voluntary liquidations; and pre-pack sales of business. C&E has agreed to consult with ARIES where topics overlap with the proposed insolvency reform.

Grant Thornton

Brexit strategy

Jamie Leader looks at the potential future for insolvency and corporate restructuring post-June.

By the time that this issue of *RECOVERY* is published, the referendum on whether the UK should leave or remain within the EU will be almost upon us, and a long and bitter campaign almost over. If the UK votes 'leave' on 23 June, it will mark the start of a significant period of uncertainty while the terms of our future relationship with the EU are worked out. From a legal point of view, there would be a huge amount of work to do in disentangling EU and English law, and deciding which provisions derived from EU law a post-Brexit UK should keep and which it should discard. What cannot be denied is that the effects on all areas of business in the UK would be substantial.

Although the immediate economic effects of Brexit could certainly be relevant to restructuring and insolvency practitioners, this article focuses on the possible legal effects; in particular:

- the recognition of cross-border insolvency proceedings;
- the use of English schemes of arrangement to restructure European companies;
- the restructuring and insolvency of credit institutions and insurers; and
- other EU laws that directly or indirectly impact on restructuring and insolvency.

> "A vote to leave the EU would create considerable uncertainty regarding the future landscape for multi-jurisdictional insolvencies."

What do we mean by Brexit?

One of the difficulties with the Brexit debate is that no-one knows what type of relationship the UK would have with the EU if it left. As there is no comparable precedent to provide guidance, most commentators agree that a bespoke arrangement would be negotiated to provide for the terms of the UK's continuing relationship with the EU. As a minimum, this might include a free trade agreement providing for the free movement of goods between the UK and the EU, but all would depend on what the EU would require in return as part of the negotiation and the political stance taken by a post-Brexit government in the UK on key issues such as immigration.

The media has presented the Swiss and Norwegian EU arrangements as possible model examples for a future UK/EU relationship. However, neither is attractive; the UK Government has indicated that the Norwegian model is not favoured (although a post-Brexit government might take a different view), and the EU seems unlikely to offer the Swiss model given its complex and cumbersome nature.

Cross-border insolvency

Currently, insolvency proceedings commenced in any member state of the EU (with the exception of Denmark) are subject to the EC Regulation on Insolvency Proceedings (the EC regulation). The EC regulation does not harmonise European insolvency laws; rather it imposes a clear framework of rules governing where insolvency proceedings may be opened, the laws applicable to matters arising in such proceedings (eg security, setoff and antecedent transactions) and the recognition of the proceedings in other member states.

Unless some alternative arrangements were agreed, if the UK were to leave the EU then the EC regulation would cease to apply to it automatically. The result would be that EU insolvency proceedings would no longer benefit from automatic recognition in the UK, and UK insolvency proceedings would no longer benefit from such recognition in the EU. Furthermore, the ‘safe harbour’ provisions of the regulation (that apply the parties’ choice of governing law in priority to any rules of local insolvency law – for example, in relation to employment contracts under article 10 or detrimental acts under article 13) – would cease to apply to English law.

The detrimental impact upon the administration of cross-border insolvencies would be significant, and would create more difficulties for the UK than the EU. That is because, unlike most member states, the UK has implemented the UNCITRAL Model Law on Insolvency, in the form of the Cross-Border Insolvency Regulations 2006 (CBIR 2006). Insolvency office holders from the EU who required recognition in the UK could therefore seek it under CBIR 2006, which, although not automatic, would bring many of the benefits of recognition under the EC regulation. UK office holders would not find matters so easy: other than the UK, the only member states that have implemented the UNCITRAL Model Law are Greece, Poland, Romania and Slovenia. Elsewhere, UK office holders seeking recognition would have to rely either on obtaining recognition under local law (which may be difficult or even impossible) or seek the opening of territorial insolvency proceedings; neither is likely to be particularly attractive.

“The detrimental impact upon the administration of cross-border insolvencies would be significant, and would create more difficulties for the UK than the EU.”

In the circumstances, in the event of Brexit it would be in the interests of both the UK and the EU to reach an agreement whereby UK proceedings would benefit from some recognition under the EC regulation, and vice versa. The precise form that such an agreement would take is, however, a matter of conjecture. Extending the application of the EC regulation to a third party state would represent a significant departure from its current structure and other member states (some of which have long been suspicious of certain aspects of English law, such as out-of-court appointments and schemes of arrangement) might see a Brexit as another opportunity to recast the regulation in a form more sympathetic to their own national interests. In general, in view of the asymmetric recognition landscape in the event that the UK leaves »

Other EU law

It is, of course, not only the law specifically relating to insolvency that affects restructuring and insolvency practice; many other areas of law have a significant impact on how and whether a business can be restructured, and many of those other laws could be affected by a Brexit. For example:

- **Employment law:**
  If the UK remained in the single market it would probably be obliged to retain EU employment law, but even if it did not a Brexit would be unlikely to precipitate immediate and major changes to employment law policy. The EU-derived provisions of greatest relevance to restructuring and insolvency are perhaps the Transfer of Undertakings (Protection of Employment) Regulations (TUPE) and the rules relating to collective redundancy consultation. Both are now such well-established aspects of UK employment law that it might be politically unattractive for any government to abolish them, although minor changes might be made.

- **Financial services law:**
  European financial markets are governed by an extensive body of EU legislation, much of which is relevant to insolvency. Perhaps most important are the measures that aim to avoid the smooth operation of the financial markets being interrupted by rules relating to insolvency, such as the Settlement Finality Directive and Financial Collateral Arrangements Directive (although the practical significance of the latter to UK professionals is currently limited by the way it has been implemented into domestic law – see *Gray* v. *GTP Group Ltd* [2010] EWHC 1772). Much of this legislation applies to the EEA, and so would continue to apply to the UK if we remained in the EEA. Even if we left the EEA, however, it seems unlikely that there would be any significant political will to abandon these rules following Brexit, because of the unobjectionable policy aims behind them and because many are ultimately derived from non-EU sources in any event.

- **State aid:**
  EU law prohibits member states providing financial assistance to companies in a way that could distort competition. In the event of Brexit these rules would cease to apply, leaving the UK government free (in principle) to provide rescue finance to distressed British companies or industries. Whether it would do so in practice is perhaps another matter: a cynic might suggest that the state aid rules provide a welcome pretext for avoiding bail-outs that the government would not make in any case.

the EC regulation, the EU might feel that the UK had more to lose than it did in any negotiation.

If it proved impossible or impractical to extend the EC regulation, an alternative could be for the UK to negotiate bilateral agreements with member states. It goes without saying that this could be a slow process, and results could be considerably more complex than the current framework.

Schemes of arrangement

Schemes of arrangement occupy a unique position: although used for some of the most significant restructurings of European companies, schemes do not fall within the ambit of the EC regulation. Indeed, the fact that the EC regulation does not apply to schemes gives them an unrivalled flexibility and has been a crucial factor in their development. That is not, however, to say that schemes are not subject to EU jurisdictional rules: judicial opinion is divided regarding whether they are covered by the judgments regulation. Although the point remains undecided, in recent schemes the English court has considered it necessary to establish that, if the judgments regulation did apply, the particular scheme before the court would be recognised abroad under it.

> "It would be in the interests of both the UK and the EU to reach an agreement whereby UK proceedings would benefit from some recognition under the EC regulation."

If the UK were to leave the EU, and thus the judgments regulation, the question of whether schemes are subject to that regulation would naturally fall away – with the result that it should, in principle, become easier to persuade an English court that it has jurisdiction to sanction a scheme in relation to a foreign company. Jurisdiction alone is insufficient, however; it is also well established that, before the English court will exercise its discretion to sanction a scheme, it must be satisfied that the scheme will be recognised in those jurisdictions where creditors might challenge it. If the judgments regulation did not apply, it might become harder for such companies to satisfy the court that such recognition will be granted: in effect, the applicant company will need to show that the scheme would be recognised under the rules of private international law of the countries in question. The Lugano Convention, which provides for mutual recognition of judgments between EU and EFTA countries, may be of assistance in this respect. The existing authorities suggest that, in many cases, it is likely to be possible for the scheme company to satisfy the court that the scheme will be recognised even if the judgments regulation does not apply, so that Brexit would not seem to threaten a knockout blow to the use of schemes for restructuring EU companies. A greater threat to the dominance of schemes may be rival procedures adopted by other member states (for example, the Netherlands).

Credit institutions and insurers

Certain classes of entity are expressly excluded from the EC regulation: insurance undertakings, credit institutions and certain investment undertakings. In place of the EC regulation, insurance undertakings and credit institutions are subject to specific EU directives (there is no equivalent for investment undertakings that, from an insolvency point of view, therefore fall outside the EU jurisdictional framework altogether).

The EU directives relating to insurers and credit institutions have also been adopted by the European Economic Area (a grouping that includes Iceland, Liechtenstein and Norway in addition to the member states of the EU: EEA). As a result, if the UK remained in the EEA then UK insurers and credit institutions would still benefit from them and the UK would be obliged to retain the provisions of English law that implement them: the Insurers (Reorganisation and Winding-up) Regulations 2004 and the Credit Institutions (Reorganisation and Winding-up) Regulations 2004.

If the UK left the EEA as well as the EU, those regulations (as provisions of English domestic law) would not automatically cease to have effect; it would be a matter for the UK government to decide whether to repeal, amend or retain them – whereas the equivalent legislation in the remaining member states of the EU would cease to apply to UK banks and insurers automatically.

A post-Brexit UK government that had decided to leave the EEA would be making a major break with Europe, and it seems unlikely that European regimes for recognition of the insolvency of banks and insurers would be a priority. In contrast to many other sectors, the international operations of the UK's banks and insurers are, to a great extent, not conducted in the EU and it seems probable that, in the event of Brexit, UK banks that intended to conduct retail business in the EU would hive the relevant business down to subsidiaries based in Frankfurt or elsewhere (leaving UK retail and investment banking in London). If, therefore, the regulatory 'price' sought by the EU for mutual recognition of bank and insurer insolvency was perceived to be too high, the UK government might conclude that it would be preferable to 'go it alone' or to seek agreements with other key international markets rather than with the EU.

Conclusion

As UK insolvency legislation is not derived from EU law, the effect of Brexit on the insolvency of entities domiciled and trading only in the UK, and upon domestic insolvency case law, would be limited. A vote to leave the EU would, however, create considerable uncertainty regarding the future landscape for multi-jurisdictional insolvencies. Whereas, in other areas, the Vote Leave campaign argues that leaving the EU would deliver advantages to the UK, it is not obvious how such advantages could arise in the narrow field of cross-border restructuring and insolvency. Although the current system is certainly not perfect, it does generally deliver clarity and predictability, and thus reduces costs and maximises value for creditors. In the event of a Brexit vote, the UK's priority in this area should therefore be to retain as much of the current system as it can.

> "The fact that the EC regulation does not apply to schemes gives them an unrivalled flexibility and has been a crucial factor in their development."

It is also important to note that there are changes on the horizon even if the UK votes to remain in the EU. Under the European Commission's Capital Markets Union initiative, the Commission has made clear its intention to commence a process of harmonisation of EU insolvency laws, with the first legislative proposal to be issued during 2016. Due to the sophistication of the UK's restructuring and insolvency market, such harmonisation is likely to bring greater change to other member states, but the UK will undoubtedly face changes too. Indeed, the UK government is already considering proposals for a pre-insolvency moratorium, in what appears to be, at least in part, a pre-emptive response to the Commission's proposals.

Whatever the outcome of the Brexit vote, practitioners cannot simply assume the continuation of the status quo.

JAMIE LEADER is a partner at Eversheds LLP.

Mis-sold down the river?

Rob Miller offers the forensic view of how IPs can deal with mis-sold interest rate hedging products.

Claims arising from mis-sold interest rate hedging products (IRHP) have been the bane of many insolvency practitioners' lives over the past few years, especially those who are on bank panels or were appointed by the banks. Often, there is a clear disparity between their objectives and those of the previous shareholders or directors.

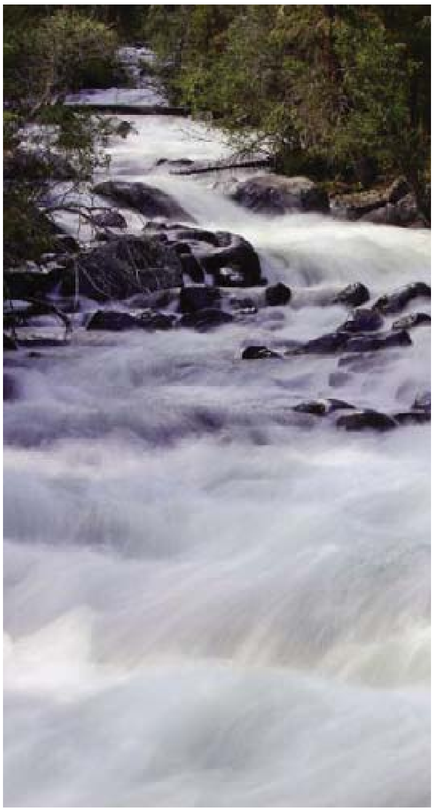
IRHP claims are complex, and can lead to expensive litigation that, for the most part, insolvency practitioners are reluctant to take on unless it can be done without risk for them.

> "In my view, if the debt is likely to be paid in full by settlement of the claim, it should be ignored in calculating the losses."

Here I will look at the support a forensic accountant can offer to insolvency practitioners in these situations.

The insolvency practitioner will usually ask three key questions:

- What is the value of the claim?
- Is there any evidence that the mis-sold IRHP caused the losses?
- How can the claim be funded?



Valuation

The claim's valuation is usually a straightforward exercise where a company is in liquidation. Ultimately, if it can be proved that the mis-sold IRHP caused the business to go into administration or liquidation, the figure will be calculated by reference to the value of the business were it not for insolvency proceedings. For many firms affected by IRHPs, the losses will be claimed as a premature sale of properties or an undervalued sale.

In the case of *MMP GMBH* v. *Antal International Network Ltd*, the High Court judge Mr Justice Flaux said: *'If the effect of the breach of contract had been to put the company out of business then since, by definition there are no future profits (or losses) against which to compare the profits (or losses) which the company would have made had the breach not occurred, then it is not possible for the court to assess damages on the basis of a loss of profits in the normal way.*

It seems to me that it is only in such situations that the court will fall back on… seeking to value the company as at the date of the breach, both because it is that value of which the claimant has been deprived by the breach and because it is only by such valuation that the court can arrive at a "proxy" for the loss of profits.'

The question then arises: how to deal with the debt? In my view, if the debt is likely to be paid in full by settlement of the claim, it should be ignored in calculating the losses. This is because it is the same in the 'actual' and 'but for' scenarios. However, where there has been some debt forgiveness, credit should be given for this to take account of the benefit obtained by the claimant.

IRHP and losses

Question two is the most important. Can it be proved that the losses were caused by the mis-sold IRHP? More often than not it is difficult to pinpoint a single reason why a company enters into insolvency proceedings. However, by examining its cash flow and loan covenants (especially in regard to the undisclosed contingent liability created by the IRHP), a clear link often emerges between the IRHP and the company's demise. You simply cannot underestimate the impact of a mis-sold product on cash flow and a firm's ability to borrow.

Additionally, it is not always the case that the value of redress provided by the Financial Conduct Authority's review process provides a good measure of whether the business concerned has suffered a loss. While £50,000 is unlikely to make a big difference to, say, a large property company, to a small bed-and-breakfast concern it is a significant sum, which would undoubtedly have led to some kind of loss.

Funding a claim

When it comes to question three and the subject of funding, many options are available. Understandably, most insolvency practitioners will seek a risk-free, zero upfront cost model.

> "It is useful for an insolvency practitioner to obtain the view of an independent third party on the cause of losses."

While lifting the LASPO exemption from insolvency proceedings in March may have an impact on the claim value, many solicitors are still looking to take on strong claims with a 100 per cent conditional fee agreement (CFA) or damages based agreement (DBA). Others may be willing to take on a hybrid, discounted CFA with the base costs met by a litigation funder.

It is useful for an insolvency practitioner to obtain the view of an independent third party on the cause of losses, which can prevent any future accusations of a conflict of interest. The landscape is certainly changing, and insolvency practitioners are likely to come under increasing pressure to make claims as alternative, risk-free, fully funded solutions come on to the market. ◻

ROB MILLER is founder and director of Inquesta.

Going, going, gone?

Mark Weston brings the hammer down on the topic of online auctions and what their rise means for IPs and the future of asset sales.

The importance of value when disposing of assets in insolvency cases is one that weighs heavy on the insolvency practitioner's mind.

It goes without saying that you appoint agents with expertise in a given field to gain the best market price for the chattels and achieve a return for creditors. Surveyors with experience of an industry will have not just the knowledge, but also the insight and contacts to generate the highest possible price for sellers across a number of platforms. Based on a wide range of factors including demand, condition, location and estimated value, they may use those relationships to arrange a private sale, or they may opt to sell at auction.

Once upon a time 'best market price' could be gained at traditional English auctions, using specialist auctioneers, who knew their market, knew their product and used their skill and the live atmosphere of the room to their advantage.

However, in some sectors, live auctions are becoming a thing of the past. There is a way now of selling goods that offers greater convenience, enables a bigger market of buyers and therefore can attract higher prices. Across the country, agents involved in insolvency have moved towards online auction portals to sell off assets, offering tangible benefits for IPs.

Clicks of the trade

Specialist auctions have been held across the UK for many years, giving buyers the chance to bid for equipment in person or via the telephone or internet. It is not just business assets of course; every week in the UK an estimated 75,000 lots go under the hammer across a network of 300 auction houses, with around 60,000 of those being sold.

However, these numbers are falling. As the internet became commonplace at the end of 20th century, buyers soon realised that they didn't need to attend the auction at all. 'Webcast bidding', where people place bids on lots via the internet, became more popular and saleroom numbers were dwindling. This trend has continued since, boosted by the rise of smart phones and handheld internet connectivity.

With this in mind, surveyors have moved to introduce online platforms for industrial machinery and business asset auctions. Similar to mainstream consumer auction sites such as eBay, these online auction platforms open up the sale to a wider audience, allowing increased competition and the opportunity for a higher price. Previously, of course, auction lots were

restricted to a small number of buyers in the auction room, or any offers made in advance in the form of a sealed bid tender.

Online platforms

Online auctions offer the same functionality as traditional live auctions, including the ability to place maximum bids in the same way as a conventional commissioned bid.

Viewings can usually be arranged as part of a pre-arranged viewing day, although many buyers may not bother thanks to the level of detail that can be provided in online auction catalogues compared to conventional paper catalogues.

An auction is typically held via a third party site such as **bidspotter.co.uk** and interested parties can view the catalogue either through the surveyor or Bidspotter websites. All lots are available to view online, along with auction details, terms and the full catalogue available to download as a PDF. The auction will run for a specified time and bidders must sign-in and register in order to place a bid.

Promotion of the auction is not too dissimilar to promotion of a traditional auction. Relationships remain a key part of any agent's repertoire and word of mouth continues to be a strong tactic to encourage interest, especially for niche, sector-specific auctions such as food manufacturing or demolition equipment. Any good agent will know who to tell in order to get the right interest at auction.

The auctions are also advertised in advance, while PR and advertising is often used to promote auctions in trade magazines. This can be a particularly effective tool to promote sector-specific auctions directly to that audience.

What does the future hold?

Of course, there are some challenges. There are legal considerations to take care of – any equipment sold via online auctions is subject to distance selling regulations. This means it is necessary to supply lengthy condition of sale documents and it may be worth spending a little money on professional photography for very detailed items. Consumer rights issues must also be taken into account, especially when items have not been viewed in person.

While it is clear the industry must embrace technology like any other, it is also fair to say the introduction of online auctions has been a challenge for many surveyors. Auctioneering is recognised as one of the oldest trades in the world and generations of professionals have thrived on the buzz of the auction room, so for those who trained before the advent and exponential growth of internet, online auction portals may be difficult to comprehend.

There is romanticism about live auctions and there is no doubt the desire and passion to stage them will linger within the profession. In certain sectors the drama and excitement of the auction room is still drawing crowds and specialist collectors from around the world.

But for most, there is no doubt that online auctions have quite literally changed the face of auctioneering; in many cases buyers no longer have a face, just an online ID.

Online platforms will continue to thrive as another method for disposing of assets. They are easier to host, quicker to arrange and more convenient for buyers. Certainly, when dealing with insolvency, it is the potential for increased financial realisation made possible by online platforms that means this method will continue to prosper. □

MARK WESTON is a machinery and business assets partner at Sanderson Weatherall.

Exploring new waters

Chad Griffin and **James Terry** look at the first exploration and production administration to take place in the current cycle.

Prolonged weakness in the commodity price environment, particularly with respect to oil prices, has given rise to significant restructuring activity, and the start of a potential wave of insolvencies, with respect to exploration and production (E&P) companies operating on the UK North Sea Continental Shelf.

The first of these insolvencies involved the Iona Energy group, a Canadian-parented and listed group with oil and gas assets in the North Sea. FTI Consulting and Akin Gump had initially been retained in early 2015 by Nordic Trustee ASA, on behalf of senior secured bondholders, to negotiate a debt restructuring. Although a restructuring was substantially agreed and close to being implemented, further downward pressure on oil prices led to a key investor pulling out in late 2015 after a year of restructuring efforts, and in January 2016 joint administrators from FTI Consulting were appointed over the UK companies in the group.

We should expect to see more E&P restructurings and insolvencies over the near-term. This article highlights some of the key issues to be aware of for lenders and investors who are looking at contingency planning and potential insolvencies in distressed UK oil and gas situations.

> "The insolvency of an operator can potentially be far more complex than the insolvency of one of the other partners whose involvement is principally financial."

Background

Iona Energy ran into difficulties in late 2014, brought on by production problems at its main producing field (Huntington), a delay to the timetable for its key development project (Orlando), a need for additional development funding, a reduction in oil prices and looming decommissioning costs.

The focus of the restructuring efforts centred around the Orlando field, which was the principal asset in the group. Orlando was a development project, meaning that exploration test wells had been drilled, but various development steps were required to bring the project to 'first oil', originally hoped to occur during 2016. These development steps carried significant capex costs relating to the retention of a drillship to undertake further drilling, the purchase and development of the subsea infrastructure required to safely operate the wells, and the infrastructure required for the offtake and transport of the oil and gas hydrocarbons once the field became operational and went into production. Although the project had already received significant funding through equity raises and the bond issue, up to a further \$80m-100m (£55m–£68m) was required.

The company undertook fund-raising efforts, which might have involved any number of solutions from M&A, equity investment, new super senior debt » financing and/or restructuring of the existing financial debt. Ultimately, an innovative restructuring was developed through a combination of capex savings, deferrals from key Orlando project suppliers (who in the current environment were highly incentivised to see the field becoming operational), a debt for equity swap to reduce the level of bond debt and future cash interest costs, and a farmout with an industry player. A farmout involves a new partner (typically another E&P company) coming into the field project and taking on a share of that project, usually by becoming responsible for an equivalent share of future costs (and by definition, future revenue once the field goes into production). This can be a very effective way to reduce costs (and associated risk) for existing field partners that are unable or unwilling to bear their current share of the future burden of concluding development of an oil field.

> There has been little track record to date of distress in the E&P industry and therefore many of the default provisions in joint operating agreements have not actually been tested in practice.

However, in late 2015, the proposed farmout partner for the Orlando field pulled out after its parent elected to restrict capital allocation to its upstream operations. This had been a key component in the restructuring, and without it the restructuring could not proceed. The focus therefore shifted to preparing for an administration, and realising value through individual asset disposals.

The administration strategy involved effecting certain pre-packaged transactions for bids that had been negotiated during the M&A process, winding down operations and exiting from other licence interests where no bids emerged. A key question in this would be the impact of the administration on the continuation of the licence for the Orlando field.

Key issues

There are some significant industry, regulatory, operational and tax issues to be aware of in undertaking contingency planning for (and then administrations of) E&P companies, many of which have featured in the case of Iona Energy. We set out some of these below:

Understanding the assets

E&P companies range from large scale operators of producing oilfields to exploration focused companies, and their business models are vastly different. A thorough understanding and risk assessment is needed, as this will drive the appropriate strategy.

The assets themselves tend to comprise certain key components, each of which needs to be reviewed and understood. These tend to involve a government-issued oil licence; a joint operating agreement, and potentially also additional royalty entitlements and lifting entitlements (ie right to oil sales) that may have historically been negotiated between field partners. At the root of it all are the well inventories themselves, which dictate the expected production levels and life of the field, and therefore its ultimate value.

The joint operating agreement is usually the key contractual document. This regulates the rights and rules between the various field partners, and in particular the basis on which the field will be operated on a day-to-day basis by one of the joint venture partners who will act as the 'operator'. In the case of Orlando, Iona was the operator of the field. The insolvency of an operator can potentially be far more complex than the insolvency of one of the other partners whose involvement is principally financial. However, the level of complexity will depend on the extent to which the field is already operating, and the status of any wells that have been drilled.

Also relevant is the creditworthiness of other field partners. If one of the field partners fails, the other partners need to decide whether to abandon the field venture in its current form, or whether to take on the non-performing partner's share of the field. While in the long run this route will provide access to an increased share of revenue, prior to production it also involves the performing partners bearing an increased level of the development costs, for which they may not have budgeted. Although joint operating agreements are often based on an industry standard form, there has been little track record to date of distress in the E&P industry and therefore many of the default provisions in joint operating agreements have not actually been tested in practice. It should be assumed that major oil companies in particular will be keen to adhere strictly to the provisions of the agreement, not least given the concern to establish a strict precedent across all of their other field ventures.

All of these items need to be reviewed in detail to understand entitlements, the impact of operational and financial defaults, and points of leverage.

Particular focus is needed on decommissioning – the requirement once a field becomes operational to post security for the ultimate close-down of the field at the end of its life. Decommissioning liabilities can involve significant up-front payments. They will be of significant importance to regulators, as well as potential bidders. An in-depth understanding of the development

infrastructure in place on the seabed, including suspended wells, is crucial.

Health and safety and emergency response arrangements

Membership of the Offshore Pollution Liability Association (OPOL), an industry organisation that administers a voluntary strict liability compensation regime, is mandatory for operators of oil licences. This imposes certain obligations on members including financial and operational capability in the event of an emergency pollution incident.

> Specialist energy policies are not covered by standard open cover and it will be important to liaise with the insurers to ensure continuity and availability of cover.

It is important to review insurance arrangements. Specialist energy policies are not covered by standard open cover and it will be important to liaise with the insurers to ensure continuity and availability of cover.

A risk assessment should be undertaken for health and safety executive (HSE) issues. This is not an area to be overlooked, however low the perceived risk. Key staff with health and safety and emergency response responsibilities should be identified and retained. Certain standby contracts may also be needed to ensure appropriate incident readiness.

Role of the regulators

From April 2015, UK North Sea oil and gas companies have been regulated by the Oil and Gas Authority (the OGA). It is an executive agency of the Department of Energy and Climate Change (DECC) and is principally focused on licensing. Early engagement with the OGA is important in distressed situations given licence defaults upon insolvency, development obligations and the OGA consent requirements for disposals. It should be remembered that prior to 2016 there has only been one formal insolvency of an E&P company operating in the UK North Sea, namely Oilexco. To that end, recent events are making yet new ground, and requiring the OGA to consider their strategy in an environment where multiple licensees could be in financial distress. It is important to have an open and constructive dialogue with the OGA. The OGA is acutely aware of the difficulties facing many struggling oil and gas companies and can play a key role in providing flexibility and support where needed.

Experience to date has shown the OGA to be practical and commercial.

The Petroleum Act 1998 affords the secretary of state for the DECC wide ranging powers to serve notices on parties in connection with decommissioning and well abandonment. These parties can include group companies, shareholders owning in excess of 50 per cent, former owners and potentially directors and officers.

Specialist E&P legal advice is important in this area. Insolvency practitioners will wish to make appropriate arrangements with the OGA and DECC ahead of any insolvency, in particular in relation to managing potential risks of claims against them for decommissioning and abandonment.

Asset realisation and the importance of tax

With depressed oil prices, disposal processes will prove challenging. It must be recognised that purchasers interested in development assets, or operating assets with capex requirements, will face significant funding requirements. It is important to explore creative payment structures on the sale of assets, including the possibility of upside sharing through deferred consideration to drive superior recoveries.

Most distressed oil and gas companies have significant pools of tax losses. These are typically available to shelter future trading profits on licences but are not capable of being sold separately. It is also key to drive value from these attributes.

> “It is important to explore creative payment structures on the sale of assets, including the possibility of upside sharing through deferred consideration to drive superior recoveries.”

Given high corporation tax rates for UK North Sea oil companies, most interested parties look for an acquisition of companies to preserve the tax loss pools, rather than business and assets, which would result in the tax losses being unavailable.

Consequently, efforts should be taken to achieve a financial restructuring that enables the sale of companies as going concerns, meeting the administration first purpose. This may involve a company voluntary arrangement (CVA) to restructure unsecured creditors' claims in an efficient way. The recent introduction of the corporate rescue exemption may also be of benefit in restructuring secured debt in a tax efficient manner.

With tax being such a large value driver for bidders, it is important to seek tax advice early, to develop a value maximising approach to disposals.

Optimising the overall outcome

E&P restructurings and insolvencies present a unique set of challenges. Given the benign oil environment in recent years, there are few precedents to follow. It is important to assemble the right team with the requisite experience, who can step up immediately and drive an optimal recovery.

JAMES TERRY (far left) is financial restructuring partner at Akin Gump, London.

CHAD GRIFFIN (left) is senior managing director at FTI Consulting, London.

Equity rich protected trust deeds – *for the benefit of the creditors?*

Roy Roxburgh writes on the potential ethical and professional dilemmas that can arise for IPs dealing with trust deeds in Scotland.

As a member of both the R3 Scottish Technical Committee and the Joint Insolvency Committee, I have become aware of what I consider to be a serious misunderstanding of the law relating to trust deeds for creditors in Scotland. This is causing competition issues for IPs since my advice to solicitors, if I were asked, would be that the trustee should not in normal circumstances be doing what is happening and would likely be in breach of his fiduciary duties by doing so, leaving him open to action by his Recognised Professional Body (RPB) and the Accountant in Bankruptcy.

> It is similar to going to a Rolls-Royce garage with enough money to buy a small second-hand car and insisting a new Rolls-Royce is to be sold to you.

What is the problem?

The mischief starts with the IP considering that a trust deed is in effect the Scottish equivalent of an individual voluntary arrangement (IVA). That is a fundamental misconception, even if they are functional equivalents. A trust deed is a creature of the common law of Scotland. It is just like any other trust in Scotland, albeit subject to some statutory influence under insolvency legislation.

The Insolvency Act 1986 Part VIII (individual voluntary arrangements) provides a process for a debtor to make a proposal to his creditors for a composition in satisfaction of his debts as a voluntary arrangement and its implementation is supervised by a nominee (an IP).

The Bankruptcy (Scotland) Act 1985 s5(4A) defines a trust deed as 'a voluntary trust deed granted by or on behalf of the debtor whereby his estate (subject to a caveat which does not apply to this article) is conveyed to the trustee for the benefit of his creditors generally.' The trustee holds the estate on behalf of the creditors and not on behalf of the granter (debtor). *(McBryde – Bankruptcy) (Stair Encyclopaedia Vol 24 p13).*

Following the granting of the trust deed, the trustee will seek the status of a protected trust deed (PTD) in accordance with The Protected Trust Deeds (Scotland) Regulations 2013 (the regs). If more than half of the creditors in number or no fewer than one third in value object it will not be protected, but creditors who do not reply are treated as if they had agreed, as a matter of public policy, resulting in most trust deeds gaining protection. A PTD gives protection and relief from all creditors (save certain ones carved out and not relevant to this article).

Mischief arises

To avoid problems where heritable estate (property) might increase in value, again as a matter of public policy, the property is valued on the date of signing of the trust deed and that is the value used in any negotiations the trustee may have with the debtor. In terms of the regs the trustee can reach an agreement with the debtor in relation to the property and it is here that the mischief is arising. The regs (reg 15) provide that at the date on which the trust deed was granted the trustee may agree, subject to the conditions in reg 15(3), in form 1B:

(a) not to realise any specific property of the debtor which has been conveyed to the trustee, and
(b) to relinquish the trustee's interest in respect of such property.

The reg 15(3) conditions are that the debtor must:

(i) pay any amount determined by the trustee by the date determined by the trustee, and
(ii) following any monthly payments in the normal course of the trust from income, pay a monthly amount determined by the trustee for a period determined by the trustee.

> The obligation of the trustee is to the creditors primarily and that is the common law position not contradicted or qualified by any statutory provision.

Such payments by the debtor must be 'determined in accordance with a valuation made by a chartered surveyor or other suitably qualified third party of the debtor's property as at the date of the grant of the trust deed'.

Well that seems reasonably straightforward and the process fully set down. So what's the problem?

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

Following protocol

It appears to flow from the IVA standard protocol, whereby after the 48-month contribution period, an additional 12 monthly contributions are paid towards the equity and such a proposal in an IVA is often accepted with the equity being 'retained' by the debtor (which is unlike Scotland where the property is transferred to the trustee on day one). This is clearly part of the IVA proposal and the creditors at a meeting have positively approved it. There is no equivalent of the IVA standard protocol with trust deeds. In Scotland there is no need for positive approval since an independent IP is appointed as trustee for the creditors and the protection to the PTD (as noted above) can be obtained by deemed approval (ie either of the relevant percentages not objecting).

> The mischief is the signing of the form 1B after appointment.

So let's look at an actual trust deed example from the Accountant in Bankruptcy. An individual approaches an IP seeking a trust deed saying he has equity of £209,000 in a property, less than £11,000 of creditors and is prepared to pay £105 a month for an additional year (£1,260 in total). He cannot obtain a re-mortgage due to his age. The IP agrees to be appointed trustee, the trust deed is signed, and a form 1B is signed agreeing that the trustee will relinquish his interest in the property once the £1,260 is paid. The creditors receive less than 20p in the £1 and the debtor keeps over £200,000 of equity.

Striking a balance

Creditors operate under non-statutory 'treating customers fairly' provisions and accordingly rarely object to trust deeds becoming protected. They are probably aware that if the relevant percentages of creditors do nothing they are deemed to agree, they may not want to tarnish their image by treating debtors differently under the two systems or to create difficulties for the debtor since the trust deed will continue to exist even if not protected. Anyway, the trustee is appointed to ingather and realise the estate and has a fiduciary obligation to the creditors and them alone. The debtor has a radical right to any estate not distributed to creditors and the trustee needs to consider the debtor's position, but that is against the background of the trustee being appointed *'for the benefit of (the debtor's) creditors generally'*. SIP3(3) may state 'If a trust deed is proposed, an IP should ensure that a fair balance is struck between the interests of the debtor and those of the creditors' but that has no statutory basis. The obligation of the trustee is to the creditors primarily and that is the common law position not contradicted or qualified by any statutory provision and the SIP needs to be read against the background of the legal position.

With regard to timing, before the trust deed is signed the IP has no status since he becomes the trustee only once the trust deed is signed. Accordingly the IP can enter into no arrangement binding on the trustee before the trustee and the trust exists. On appointment he must act 'for the benefit of the (debtor's) creditors generally'. On the basis that the trustee can only sign the form 1B after he has been appointed, can it really be in compliance with a trustee's fiduciary duties *at that time* to accept £1,260 (in over 48 months' time) on behalf of the creditors in exchange for a property independently valued at £209,000? I cannot believe that it is.

A PTD requires all of the debtor's estate as would vest in the trustee of a sequestrated estate (subject to the caveat noted above) to be conveyed to the trustee. Is that the case here? Probably, I would suggest, since the property is transferred when the trust deed is signed and no understanding between the prospective debtor and the prospective trustee is binding on the trustee once appointed, even if there may be an understanding that the form 1B will be signed by the trustee. The mischief is the signing of the form 1B after appointment. This creates a conditional realisation of a valuable asset for a nominal sum, but it is done after the trust deed becomes effective. On appointment the trustee needs to satisfy himself, objectively, and not simply by accepting the debtor's word, that he cannot obtain any mortgage, that the form 1B agreement is a reasonable conditional realisation of the value of the property and he can only do that after considering the debtor taking out a mortgage (whether on high street terms or not) or downsizing. He is obliged, under the regs, to ensure that the proposed payment is *determined in accordance* with the professional valuation. Our example shows that the payment is in no way linked to the valuation but is based on what the debtor can pay. That is similar to going to a Rolls-Royce garage with enough money to buy a small second-hand car and insisting a new Rolls-Royce is to be sold to you.

I am not suggesting that the regs do not allow an agreement of payments during an extended period to be entered into, but such agreement must be *determined in accordance* with the valuation and the fiduciary duties to the creditors and not based on what the debtor can pay alone.

Ethical dilemma

There may always be exceptional circumstances, but the number of cases coming through appears to reflect a mischief rather than increased exceptional circumstances.

Can an IP reach agreement with the debtor in advance of the entering into of the trust deed on the basis of the above example and be in compliance with the ethical code? Again, I think not.

Three of the fundamental principles come into play, namely (a) integrity, (b) objectivity and (c) professional competence and due care. The code states that

'The practitioner must always be satisfied as to the actual objectivity which he or she can bring to their judgement, decisions and conduct, but also must be mindful of how they will be perceived by others.'

The IP is anticipating taking an appointment on behalf of the creditors generally, but prior to doing so is entering into an arrangement with the prospective debtor, the party in direct conflict with the creditors to whom the trustee has a fiduciary duty, which on the face of it appears to be completely at odds with the interests of the creditors. The whole structure of trust deed law and practice with the conveyance of the estate to the trustee at the start, and the deemed consent provision is predicated, as a matter of public policy, on the independence of the IP as trustee and the ability of the creditors to have absolute faith in the integrity of the trustee acting throughout in their best interests. In an administration if a pre-pack along the lines of the above example were proposed, would the pre-pack pool be satisfied? Surely not! As noted above the role of a nominee in an IVA is fundamentally different from that of a trustee in a trust deed.

> Creditors operate under non-statutory 'treating customers fairly' provisions and accordingly rarely object to trust deeds becoming protected.

If it is known that an IP would be prepared to countenance such arrangements, this has the effect of giving him a competitive advantage over other IPs who would not consider the arrangement to be compatible with their fiduciary duties. This must be of concern to all the RPBs.

ROY ROXBURGH is a member of R3's Scottish Technical Committee.

Overt intelligence

Dr Stephen Hill snoops around the essentials of open-source intelligence and social media for use in modern investigations.

Open-source intelligence (OSINT), for most purposes, refers to a broad array of information and sources that are generally available. This includes information obtained from the media (newspapers, radio, television, etc) professional and academic records (papers, conferences, professional associations, etc), and public data (government reports, demographics, hearings, speeches, etc).

It has been estimated that roughly 90 per cent of valuable intelligence comes from open sources compared to traditional covert intelligence. According to the CIA, open sources often equal or surpass classified information in monitoring and analysing issues including terrorism, proliferation and counterintelligence. To an internet-savvy user, OSINT provides access to a plethora of intelligence, which, if knowing where to look and how, can be the life blood of a modern-day investigation.

To most, searching the internet is simply about using a search engine such as Google, or rival Bing, to run a keyword search. This type of search, and the site that provides it, are typically referred to as the surface or visible web. In simple terms the surface web is a portion or segment of the World Wide Web that is indexable by a search engine such as Google. Surface search engines typically construct a database of the web by using programs called *spiders* or robots (web crawlers). The spider gets a copy of each page and indexes it, storing useful information that will let the page be quickly retrieved again later. Google uses a slightly more refined approach using what is commonly termed the 'page rank algorithm'.

Online investigation toolkit

When it comes to searching online there are many tools available, but some are more popular than others. So which are the most effective for the online investigator? This is a difficult question as it depends on many circumstances based on the type of search being carried out. However, the following section explores some of the options available to the online investigator when exploring the world of social media.

> "Protect your ID when online by using an anonymous browser and when asked for personal details."

The main surface search index tools include Google and Bing, with both having the ability to filter text, images, video and offer the investigator the ability to filter by time, location, site or related pages. Both have good advanced features and offer the ability to translate (although this is very basic). While both these search engines are good they do not cover every possible angle of searching that some investigators have come to expect. One weakness is that by default they do not automatically search the vast wilderness of social media including everything from blogs, photos, videos and geo-location data among other things.

Social media investigations

Social media has opened up numerous opportunities and is a key component to profiling the subject of an investigation. The pool of information about each individual can form a distinctive social signature.

Twitter, Facebook and LinkedIn, to name but a few, have embedded themselves in people's lives. Postings to walls, tweets, video and image updates are emerging as a new trove of intelligence.

Social media evidence can be a valuable addition to an investigation, revealing the kind of information that, years ago, would have been difficult, if not impossible, to find. But it has to be gathered in a way that will hold up in court. Because it's such a new source of evidence in investigations, case law is developing rapidly. A forward-thinking investigator would be well-advised to stay on top of the latest legislation both locally and internationally.

Once the access to social media information has been secured, either through court order or simply due to public accessibility, evidence must be gathered in a way that is legal and useful. Collecting evidence from social media sites can be challenging for several reasons.

The world of social media is constantly changing, and users can easily update and delete material that could be evidence in a case. However, once a user is aware of an ongoing investigation, he or she is under an obligation to preserve social media evidence just as if it were any other type of evidence. Deleting photos, posts and other information is akin to shredding documents and the courts have been clear about the consequences, handing out hefty fines and sanctions for spoliation.

There are a series of specialist search tools available, which offer options to the online investigator especially as these tend to excel in searching social media. The sites listed in the box each have their own unique strengths – whether it is looking at photos, finding user profiles or even establishing geo-social footprints – collectively they provide a powerful toolkit to the online investigator.

Dark net search

The dark net has been in the headlines over the last couple of years because of its association to nefarious activities and it being 'hidden' from plain site. Websites such as Silk Road and other associated activities operated under the anonymity of the dark net.

Access to this dark net is possible through services such as TOR or I2P. With more and more online users worried about privacy and possible intrusion into their online life, downloads of TOR have increased substantially over the last few years. However, the dark net has proved attractive to not only the typical user worried about security, but also to the criminal wishing to hide their identity. The dark net serves as a platform for the cyber-criminal to become anonymous since it not only provides protection from unauthorised users but also, in many cases, uses encryption to prevent monitoring. TOR (The Onion Router) is one such anonymous network with access granted via the TOR browser that was developed by the US Naval Research Laboratory for communicating online anonymously.

So where would you start when trying to unlock this dark net information? The first and most crucial part is to understand how, when conducting an online investigation, can the investigator go untraced and fall under the radar – in other words how do they hide their own digital footprints?

> Deleting photos, posts and other information is akin to shredding documents and the courts have been clear about the consequences, handing out hefty fines and sanctions for spoliation.

Anonymity comes from the Greek word *'anonymia'* referring to the state where one's personal identity is not publicly known. To allow this anonymity online, the internet investigator should look to disguise their digital footprints by hiding their IP address. The TOR client allows this to happen by routing internet traffic through a worldwide volunteer network of servers hiding the user's information and eluding any monitoring.

Onion routing is a technique for anonymous communication over a computer network. Messages are repeatedly encrypted and sent through several network nodes called onion routers. In the same way someone may peel the layers of an onion, each onion router removes a layer of encryption to uncover routing instructions, and sends the message to the next router where the process is repeated. This gives the internet investigator the level of protection required as this technique prevents intermediary nodes from knowing the origin, destination and contents of the message.

Go forth and search

There is no right or wrong way to carry out an internet search but it is a good idea to familiarise yourself with a selection (toolbox) of search engines and specialist sites to use during an online investigation. When conducting a straightforward keyword search, experiment by adding and taking away words and try using the 'advanced search' option on the chosen search engine.

Remember, information is power and having access to the most accurate, up-to-date and relevant intelligence is vital to a successful investigation. Knowing when to stop searching is also a key skill so practice good discipline by setting a time limit and remember that a good investigation is based on quality not quantity.

One final point to remember – protect your ID when online by using an anonymous browser and when asked for personal details, if for example accessing a Gmail account or social media profile, then use details not associated to you or your organisation. Also consider using a search engine that doesn't track you, giving better privacy, such as DuckDuckGo **duckduckgo.com** or StartPage **startpage.com**. ◻

Useful sites:

Echosec www.echosec.net
Echosec is a location-based search platform that provides public safety, security, journalism and intelligence professionals actionable knowledge based on social media and other information. By typing a postcode into the search bar of the online application this site will bring up the location on a digital map and when the user highlights a square of the area, around a building, for example, social media posts and images taken and published in that location start popping up beneath the map. Sites searched include Facebook, Twitter, VK, Instagram.

Geofeedia geofeedia.com
Geofeedia is similar to Echosec allowing the user to search the globe and draw a perimeter around any location of interest displaying all geotagged social media posts from Twitter, Facebook, Instagram, YouTube, Flickr. Geofeedia's visual and analytics tools make it easy to discover, monitor and filter social data, on a real-time basis.

Social Searcher www.social-searcher.com
Social Searcher is a specialist social media search engine. It allows the user to search for content in social networks in real-time and provides deep analytics data. Users can search without logging in for publicly posted information on Twitter, Google+, Facebook, YouTube, Instagram, Tumblr, Reddit, Flickr, Dailymotion and Vimeo. Users can also save their searches and set up email alerts.

DR STEPHEN HILL is director of data and intelligence at Absolute Partnership Ltd and founder of Snowdrop Consulting Ltd.

Can directors defend the 'sin' of wrongful trading?

David Towers and **Tim Lees** analyse the three key issues considered in the *Re Ralls Builders Limited* proceedings.

In a recent decision,[1] Snowden J considered a company whose directors had continued trading profitably after they knew or ought to have known that there was no reasonable prospect of avoiding an insolvent liquidation. Receipts were used to discharge the company's secured overdraft, leaving unsecured trade creditors in a worse position than they would have been had the company filed for administration or liquidation at an earlier stage, or if the directors had taken steps to protect trade creditors (as they had been advised to do). Snowden J found that the directors had committed a 'sin' by worsening the position of trade creditors, but he was unable to require the directors to make a contribution to the company's assets for wrongful trading in circumstances where the company itself had suffered no loss.

> Snowden J found that the directors had committed a 'sin' by worsening the position of trade creditors.

Background

Ralls Builders Limited had fallen on hard times. The directors obtained advice from an insolvency practitioner in late July and early August 2010. The directors were advised that the company had a net asset deficiency of £1.4m, and that realistically it could not become solvent by trading alone. The directors had, since April 2010, been in discussions with an investor regarding an investment in the company's parent, which might have enabled a turnaround. The insolvency practitioner advised that the directors should only allow a limited period for discussions with the investor to continue.

The directors in fact continued to trade until 13 October 2010. By this point the investor had apparently[2] not kept a number of assurances that funds would be forthcoming, in circumstances where it must have been plain such funds were urgently needed. The company was placed into administration, and subsequently entered liquidation. The directors continued to hold discussions with the investor, even after the company was placed into administration.

The company traded profitably between the dates at which the directors sought advice and the date that it entered administration. However, the company's bank had restricted payments from the company's overdrawn account. Consequently, receipts from trading were used to discharge the company's overdraft (which was secured by a debenture) in full, while, for the most part, trade creditors were not paid. The insolvency practitioner had advised in August 2010 that the company should seek confirmation from its bank that specific payments would be made, or else set aside money to pay trade creditors in a separate account (albeit in breach of its existing obligations to the bank). This advice was not followed.

The company's joint-liquidators made an application, under s.214 of the Insolvency Act 1986 (IA 1986), for an order requiring the directors to make a contribution to the company's assets for having wrongfully traded the company either from 31 July 2010 (immediately after they took advice from the insolvency practitioner) or 31 August 2010 (one month thereafter).

The decision

In deciding the liquidators' application, the court needed to consider three key issues: reasonable prospects; the 214(3) defence; and quantum of contribution.

Reasonable prospects

Section 214(1) provides the court with a power to require a director of a company in insolvent liquidation[3] to make 'such contribution (if any) to the company's assets as the court thinks proper', ie an order for 'wrongful trading'. Section 214(2) qualifies this by providing (insofar as material) that an order for wrongful trading shall only be made where the court is satisfied that 'at some time before the commencement of the winding up of the company, that person knew or ought to have concluded that there was no reasonable prospect that the company would avoid going into insolvent liquidation continued to trade after the point at which they knew, or ought to have known, that there was no reasonable prospect of avoiding an insolvent liquidation'.

On the evidence, the company's prospects were dependent on concluding a suitable transaction with the investor.[4] No such transaction was in fact concluded, and so the critical question was whether, by 31 July or 31 August, the directors knew (subjectively) or ought to have concluded (objectively) that there was no reasonable prospect of concluding such a transaction.

Snowden J found that the directors subjectively believed that the investor could be persuaded to invest even after the company entered administration. He also considered, from an objective standpoint, that the directors were not unreasonable for continuing to trade as at 31 July 2010 while discussions with the investor were ongoing – they had been advised that they could allow such discussions a limited period to continue. But by 31 August 2010 the investor had not kept a number of apparent assurances that he would invest, and the directors had made only very superficial enquiries into the investor's real means and intentions.

> In deciding the liquidators' application, the court needed to consider three key issues: reasonable prospects; the 214(3) defence; and quantum of contribution.

Snowden J considered that there was no longer 'a rational basis upon which to expect that the investor would provide the necessary money that the company urgently needed', and that the directors should therefore have concluded that there was no reasonable prospect of avoiding an insolvent liquidation.

The s.214(3) defence

Section 214(3) provides a defence to a wrongful trading claim, where a director can show that he 'took every step with a view to minimising the potential loss to the company's creditors as (assuming him to have known that there was no reasonable prospect that the company would avoid going into liquidation) he ought to have taken.'

The directors sought to rely on the s.214(3) defence, on grounds that they had continued to trade during a profitable period with a view to minimising creditors' losses. The liquidators contended that the s.214(3) defence was not available, as the benefits of trading were disproportionately received by the company's bank, and not by other creditors. Contrary to the advice they had received, they had not set aside any money for such other creditors or taken other steps to secure their payment.

> Snowden J considered that this was not a particularly 'harsh' conclusion to reach, particularly in light of the advice that the directors had received.

Snowden J sided with the liquidators on this point. The wording of s.214(3), which refers to 'every step' was clearly intended to set a 'high hurdle', and in order to avail of the defence under s.214(3) a director would need to 'demonstrate not only that continued trading was intended to reduce the net deficiency of the company, but also that it was designed appropriately so as to minimise the risk of loss to individual creditors'.[5] Snowden J considered that this was not a particularly 'harsh' conclusion to reach, particularly in light of the advice that the directors had received.[6]

Quantum of contribution

The directors had traded the company after they ought to have concluded that there was no reasonable prospect of avoiding an insolvent liquidation, and were not able to avail of the s.214(3) defence. The court therefore needed to consider the appropriate quantum of any contribution that the directors might be ordered to make.

In previous cases the quantum of the contribution to be made by directors has been set by reference to the loss suffered by the company (and not individual creditors) as a result of its continued trading.[7] Here, the company had traded profitably, such that there was no loss towards which the directors could be required to contribute. The liquidators therefore contended that these cases were wrongly decided, or that in any event they could not survive the coming into effect (after the cases cited were decided) of s.176A IA 1986,[8] which requires that a 'prescribed part' of secured asset realisations be set aside for the benefit of unsecured creditors.

However, Snowden J considered that requiring a contribution for wrongful trading in circumstances where the company had suffered no loss would be liable to produce a windfall in favour of creditors who had not extended additional credit.[9] He therefore followed the earlier cases in finding that the proper basis for quantifying any contribution was the loss suffered by the company. The directors had committed a 'sin' by increasing trade creditors' losses, but Snowden J was not able to order any contribution because the company had suffered no loss. Snowden J suggested this might be a 'shortcoming' in section 214 but it would be for Parliament, not the courts, to remedy it.[10]

Lucky directors; unlucky trade creditors

The directors in *Re Ralls Builders* were fortunate that notwithstanding that they were potentially liable for wrongful trading, the company had traded profitably. This was also a fortunate result for the bank, but by the same token was an unfortunate result for trade creditors. It will be interesting to see what amendments (if any) are considered by Parliament with a view to resolving the apparent 'shortcoming' this case identified.

Snowden J's finding that the s.214(3) defence requires the interests of individual creditors to be taken into account appears to stand in contrast with the decision of Registrar Jones in *Brooks* v. *Hardy*,[11] where it was said that 'the minimising loss defence must be judged by reference to the body of creditors as a whole because it is they as a class who are protected by s.214, not individual creditors.'[12] *Brooks* v. *Hardy* was a case where the directors had continued to make payments to trade creditors by not making payment to certain other creditors (including the company's landlord and HMRC), resulting in an overall increase in the company's net asset deficiency. It was said that 'the fact that trade creditors were paid cannot mask the fact that the liabilities of the creditors as a class were increasing'[13] – which is surely right. The decision in *Re Ralls Builders* clarifies that directors cannot seek to minimise losses to creditors irrespective of how that result is achieved. A director who fails to take account of losses to individual creditors, while taking steps to minimise losses overall, will not have taken 'every step he ought to have taken'.

More broadly, this decision is a reminder of the importance to directors of distressed companies making frequent and realistic assessments of key issues – most importantly of all, the decision to continue to trade – in light of appropriate advice. It is significant that both the questions of whether the directors ought to have concluded that the company had reasonable prospects, and whether they could avail of the s.214(3) defence, were framed partly by reference to the advice the directors had received. One can only speculate as to what might have occurred had the directors followed that advice more closely and/or taken more fulsome advice on their negotiations with the investor, but it seems far less probable that the liquidator would have brought proceedings against them.

> The decision in *Re Ralls Builders* clarifies that directors cannot seek to minimise losses to creditors irrespective of how that result is achieved.

1 *Re Ralls Builders Limited (in liquidation)* [2016] EWHC 243 (Ch). The hearings took place in June 2015, but judgment was only handed down in February 2016.
2 The investor was not called to give evidence, and so his version of events remains unknown.
3 And now, insolvent administration – see s.246ZB IA 1986, in force from 1 October 2015.
4 At [186].
5 At [245].
6 See at [247].
7 *Re Purpoint* [1991] BCC 121 and *Re Continental Assurance* [2001] BPIR 862 were considered in Snowden J's judgment.
8 This came into effect on 15 September 2003 (and was amended on 5 April 2008).
9 See at [249]-[251].
10 See at [279].
11 [2015] BCC 661 – the case was heard at around the same time as *Re Ralls Builders*.
12 Ibid at [276].
13 Ibid.

DAVID TOWERS (far left) is a partner in the restructuring and insolvency group at Clifford Chance LLP.

TIM LEES (left) is an associate in the restructuring and insolvency group at Clifford Chance LLP.

PAPER TRAIL

Mark Beaumont asks whether the Panama Papers could be positive for practitioners pursuing assets.

Mainstream reporting of the 'Panama Papers' has understandably focused on the tax affairs of wealthy individuals and international organisations: the papers name 128 politicians and public figures from around the globe, including 12 national leaders with links to the Panamanian law firm Mossack Fonseca (MF).

In case you missed it (or get your daily news from the quarterly *RECOVERY* magazine!) this was the largest leak in history, with 2.6 terabytes of data leaked to German newspaper *Süddeutsche Zeitung*. The files have been reviewed for the past year by almost 400 journalists from 76 countries, in 25 languages, under the banner of the International Consortium of Investigative Journalists (ICIJ).

> IPs could have the opportunity to re-open certain settlement agreements… with a rather fuller picture of the true asset position at the time of settlement.

The 11.5m documents cover a 40-year period up to December 2015 and shed light on how a global industry of law firms and big banks sells financial secrecy to politicians, fraudsters and drug traffickers, as well as billionaires, celebrities and sports stars. They include at least 33 people and companies blacklisted by the US government because of evidence that they'd been involved in wrongdoing, such as conducting business with Mexican drug lords, terrorist organisations such as Hezbollah or rogue nations like North Korea and Iran.

The leaked files show how prime minister Sigmundur David Gunnlaugsson and his wife secretly owned an offshore firm that held millions of dollars in Icelandic bank bonds during that country's financial crisis. Icelanders took to the streets in protest and he has since stepped down.

At this point I should highlight that MF has released statements saying it has operated 'beyond reproach for 40 years' and never been charged with criminal wrong-doing. In fact, as most people are fully aware, the services the offshore industry provides are legal if used by the law abiding. However, the documents show that banks, law firms and other offshore players have often failed to follow legal requirements to make sure their clients are not involved in criminal enterprises, tax dodging or political corruption. The files show that in some instances offshore middlemen have protected themselves and their clients by concealing suspect transactions or manipulating official records.

ICIJ will release the full list of companies and people linked to them in early May, after this article goes to press.

Lessons to learn?

This massive leak should be a wake-up call for all businesses to treat their cyber-security with the same stringency as their regulatory, financial, legal and operational risks. The latest 'Government Security Breaches Survey' found that 74 per cent of even small organisations reported a security breach in 2015; an increase on both the 2013 and 2014 surveys. According cyber security firm Symantec, more than half of 'spear phishing' attacks in the final quarter of 2015 were against SMEs, not large corporates.

The insolvency angle

Aside from the clear dangers of cyber crime, the Panama Papers will peak the insolvency practitioner's interest for a number of other reasons. IPs could have the opportunity to re-open certain settlement agreements, now that additional information may reveal, shall we say, a rather fuller picture of the true asset position at the time of settlement.

There will also be insolvencies and investigations worth re-examining in the light of new information. Have there been cases in recent years where there was a reluctance to fund investigations or pursue actions because it seemed assets were going to be difficult to access? Perhaps there looked to be a decent claim, but it appeared the perpetrator had hidden assets through offshore companies or trusts. Meritorious actions can become disproportionately costly in such circumstances, but the information leaked could reveal the location of accessible assets and bring costs down considerably.

For example, journalists have already revealed 200,000 offshore companies for which MF acted as registered agents, and 2,800 companies linked to title deeds of 6,000 UK properties, with a total value of over £7 billion. Will a potentially clearer picture of ownership give new impetus to previously abandoned investigations and actions?

There are clearly going to be some interesting avenues for asset tracers, HMRC and IPs to explore – away from the salacious headlines. Given the current boon in litigation funding and 'early case investment' there could also be new funds available to follow-up on these new lines of enquiry.

> This massive leak should be a wake-up call for all businesses to treat their cyber-security with the same stringency as their regulatory, financial, legal and operational risks.

Insolvency litigation funders (and there are many) can be encouraged to speculate on potential claims, where a relatively small investment of tens of thousands of pounds could open the door to recoveries in the hundreds of thousands, or even larger.

The funding market is evolving and it's common now for IPs and their lawyers to get investment at pre-action stage to allow further investigations, without the returns to funders being prohibitive. The Panama Papers are just one more reason to think carefully about potential claims and the value in exploring all avenues to recover funds – oh, and change your password!

MARK BEAUMONT is co-founder of Annecto Legal Ltd, an FCA-regulated broker of after-the-event (ATE) legal expenses insurance and non-recourse litigation funding that allows meritorious insolvency claims to be pursued without cost and risk to the IP.

R3 contacts

R3, 8th Floor,
120 Aldersgate Street,
London EC1A 4JQ

T: 020 7566 4200
F: 020 7566 4224
www.r3.org.uk

R3 Executive

President
Andrew Tate,
andrew.tate@krestonreeves.com

Vice-president
Adrian Hyde, ahyde@cvr.global

Administration

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

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

Smaller Practices Group; Personal Insolvency Committee; Regional Communications Committee and R3 Regional Network

R3 Director
Emma Hobson, ehobson@r3.org.uk

Finance

Finance Manager
Ryan Porter, rporter@r3.org.uk

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

Membership & Marketing

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

Marketing Executives
Fareeha Afghan, fafghan@r3.org.uk
Marek Nusl, mnusl@r3.org.uk

Membership Officer
Shemin Karim, skarim@r3.org.uk

IT Manager
Samit Vadgama, svadgama@r3.org.uk

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

Communications, Public Affairs and Policy

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

Senior Communications Manager
Nick Cosgrove,
ncosgrove@r3.org.uk

Communications Officer
Orla Hennessy,
ohennessy@r3.org.uk

Senior Public Affairs & Policy Manager
Georgina Waite, gwaite@r3.org.uk

Public Affairs & Policy Officer
James Jeffreys, jjeffreys@r3.org.uk

Education, Courses & Conferences

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

Courses & Conferences Organiser
Catherine O'Mara,
co'mara@r3.org.uk

Senior Courses & Conferences Marketing Executive
Kirsten Scully, kscully@r3.org.uk

Courses Administrator
Maggie Dean, mdean@r3.org.uk

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

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

Technical

Technical Director
Caroline Sumner, csumner@r3.org.uk

Technical Officer
Jonathan Ausena, jausena@r3.org.uk

Committee Chairs

Education, Courses & Conferences
Adrian Hyde, 020 3794 8750

General Technical Committee
Mike Pink, 0207 311 1000

Membership & Member Services
Matt Dunham, 0161 837 1870

Personal Insolvency Committee
Stuart Frith, 0207 809 2379

Policy Group
Giles Frampton, 01752 690101

Regional Communications Committee
James Martin, 0121 543 1900

Scottish Technical Committee
Eileen Blackburn, 0131 225 6366

Smaller Practices Group
Simeon Gilchrist, 0207 691 4166

R3 in Scotland

Chair & Representative on the R3 Council
Tim Cooper, 0131 222 9817

Regional Chairs

Eastern
Frank Brumby, 01603 611370

London & South East
Nick O'Reilly, 020 7186 1144

Midlands
Chris Radford, 0115 983 8200

North East
Neil Harrold, 0191 2328345

North West
Richard Wolff, 0161 828 1990

Northern Ireland
Michael Neill, 028 9031 4466

Southern
Andrew Watling, 023 8033 6464

South West & Wales
Alan Bennett, 01392 337000

Yorkshire
Adrian Berry, 0113 243 9021

Regional Representatives on the R3 Council

Eastern
Andrew Turner, 01502 563921

London & South East
Stuart Frith, 020 7329 4422

Midlands
James Martin, 0121 543 1900

North East
Kelly Jordan, 0191 211 7904

North West
Richard Wolff, 0161 828 1990

Northern Ireland
Joan Houston, 07799 581 528

Southern
Duncan Swift, 023 8033 0116

South West & Wales
Richard Clark, 0117 939 2000

Yorkshire
William Ballmann, 0845 437 4660

Other Council Members

Alison Byrne, Eileen Blackburn, Louise Brittain, Frances Coulson, Matt Dunham, Christina Fitzgerald, Giles Frampton, Simeon Gilchrist, Adrian Hyde, Jamie Leader, Gareth Limb, Nick Pike, Mike Pink, Liz Pywowarczuk, Phillip Sykes, Matthew Tait, Charles Turner, Laurence Weeks, Cathryn Williams.

R3 membership categories

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

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

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

- **Full members** are invited to contribute to the development of insolvency, business recovery and turnaround professions at both local and national levels.
- **Benefits include** use of the designatory letters MABRP and a certificateof membership, inclusion in the R3 Directory and a copy of it, membership of INSOL International.
- **Associate members** are individuals who do not meet the requirements for full membership but work significantly within the business recovery sector.
- **New Professional (Student) members** are individuals preparing to take the Joint Insolvency Examination Board (JIEB), Certificate of Proficiency in Insolvency (CPI) or Certificate in Insolvency (ICAEW) qualifications. Pass students of the JIEB are eligible to apply for full R3 membership.
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Change is a constant

Simeon Gilchrist reflects on the continual developments in the profession and how the modern practitioner adapts to them.

David Bowie was a musical genius and one of my personal heroes. Constantly evolving, the living musical embodiment of the maxim that the only constant is change. Superlative in each professional iteration: as Ziggy; as the Man Who Fell to Earth; as the Thin White Duke; as a Young American. All, however, ruthlessly discarded on his way to elder statesman of the music world. Bowie evolved not so much as a response to his market, but primarily as a catalyst that drove and created his market. I was struck while watching a rerun of a most excellent biopic that Bowie's professional development was the perfect, albeit perhaps laboured, model for the approach that we must all adopt in our evolving professional environment; and is the approach that SPG members must take in meeting the landscape challenges that are now before us. Either that, or the thought was a sad reflection of my inability to leave the market behind at the office!

I gazed a gazeless stare

Pausing to consider why I might be trying subconsciously to ruin a great hour and a half in front of BBC4, safely insulated from the real world with the help of a glorious glass of red, I found myself disappearing down the professional rabbit hole and preparing a list of the present-day drivers for change. With profound apologies to the Man Who Fell To Earth, this is what I came up with.

Although The Insolvency Service's quarterly statistics had not at the time of musing gone to press, it seemed pretty clear that the recent trends would continue – there is a shrinking market in 'traditional' personal and corporate insolvency work. We have been living in an unprecedented era of record low interest rates and quarter on quarter the statistics seem to suggest that practitioners have to work harder to source and secure appointments. It is certainly the case that the distribution of appointments in personal insolvency cases remains a challenging environment for SPG members, and one in which there are calls for increasing transparency.

To be an office holder at all requires bonding and, from members' feedback, the days of low-cost bonding could be most firmly behind us. It would also seem that the renewal process is becoming more complex and more time-consuming with, in some instances, a greater requirement for disclosure of a member's monitoring

history than ever before. Whether complexity and cost are a function of the rise of the successor office holder per se, or a consequence of a rise in claims made by successor office holders, is a question for a long and more studious examination, but the challenges facing the bonding market certainly seem to coincide with the emergence of successor claims, whether or not those claims result in better returns to the creditor body.

As with the bonding market, also with the regulatory landscape, which would also seem to be in line for development; the Small Business, Enterprise and Employment Act 2015 not only brought into play substantive amendments to the 1986 Act, but also brings forward the prospect of a single regulator with, in the interim, a renewed set of regulatory objectives for RPBs. Whether the market is better served, and whether members would secure from a single regulator greater, more consistent outcomes of inspection, control and sanction would also seem to be a series of questions calling for greater and very much more serious examination.

Then, of course, we have the framework supporting the 1986 Act; the 1986 insolvency rules have undergone – or suffered – many changes over the years, as anyone with a subscription to the 'blue book' will know. Many and varied were the occasions for debate over the meaning of terms and expressions used in different parts of the rules, with different processes apparently in place in different parts of the rules for ostensibly the same end. The insolvency rules committee is seemingly still wrestling with the challenges of reforming thirty years' worth of plumbing, just as you and I are most probably wrestling with the draft format of the 2016 rules (my iPad copy runs to 387 pages) if indeed that is what they will be when released to us.

Stepping through the door

What seems certain is that we will have a view on 'Brexit' before we have the 2016 rules, at which point there will be a particular prism through which to view the calls for insolvency law harmonisation emanating from certain of our European colleagues. We had, I suppose, been practising within the framework of the EC regulation, assuming that if we all understood that there are rules for the attribution of work between the member state jurisdictions, competent and mature bodies of law and ways of doing things could coexist. There seem, however, to be voices to the contrary, which, should we stay, will need to be met. Does remaining 'in' necessarily mean harmonising? We will see.

Introducing an element of granularity into my train of thought, I had reason to reflect on the everyday nuances: SIP 9; SIP 16 and the pre-pack pool; FCA authorisation; and, of course, the evolving jurisprudence, with any number of cases worth mentioning this year alone, whether to do with the unassuming form that has unintended consequences (the HR1) or to the interaction between bankruptcy and pensions, there is no standstill option; the practitioner must be informed and up to date.

We could be heroes?

By the time I had finished having these thoughts on the drivers for change, the end credits were rolling, and my single glass of red might have been replaced with its friend. What, I wondered, to make of all this? I supposed, thinking of the modern practitioner's offering – the training, flexibility of approach, and his or her profound understanding of the subject – and straining the analogy for all it was worth, that Bowie had it right when he wrote, in 1971: 'I said that time may change me, but I can't trace time'. Here is to change, I thought, and with that, drained my glass. ◻

If you have any comments relating to this article or would like the R3 SPG Committee to address any matters on your behalf, please contact Emma Hobson at R3 (**Emma.Hobson@r3.org.uk**)

SIMEON GILCHRIST is the R3 SPG chairman and a partner at Edwin Coe LLP.

Save the dates

17–18 November 2016
R3 SPG Forum
Chesford Grange Hotel, Warwick

26–28 April 2017
R3 Annual Conference
DoubleTree by Hilton, Dublin

R3 events, courses and conferences

	Date	Event	Venue
June	1	Scotland Question Time	Deloitte LLP, Glasgow
June	8	Southern Region – Thames Valley Meeting	Boyes Turner, Reading
June	9	Restructuring Day	Holiday Inn Regents Park, London
June	9	South West & Wales Black Tie Dinner	Marriott Hotel, Bristol
June	10	London & South East Ladies Afternoon Tea	The Mandarin Oriental Hotel, London
June	16	Scotland Golf Day	Renaissance Club, North Berwick
June	17	North West Ladies Lunch	The Lowry Hotel, Manchester
June	21	SPG Technical Review	Hilton Deansgate, Manchester
June	24	Yorkshire Ladies Lunch	Aspire, Leeds
July	5	Charities and Community Interest Companies	Marriott City Centre, Leeds
July	5	Partnership Insolvency	Marriott City Centre, Leeds
July	11	North West Regional Meeting & Barbeque	RSM LLP, Manchester
July	12	SPG Technical Review	Holiday Inn Bloomsbury, London
August	3	Yorkshire Women's Group Race Day	Pontefract Racecourse
August	18	Scotland Edinburgh Fringe Event	Burness Paull LLP, Edinburgh

Regional events (teal): Scotland Question Time; Southern Region – Thames Valley Meeting; South West & Wales Black Tie Dinner; London & South East Ladies Afternoon Tea; Scotland Golf Day; North West Ladies Lunch; Yorkshire Ladies Lunch; North West Regional Meeting & Barbeque; Yorkshire Women's Group Race Day; Scotland Edinburgh Fringe Event

R3 events (navy): Restructuring Day; SPG Technical Review (21 June); Charities and Community Interest Companies; Partnership Insolvency; SPG Technical Review (12 July)

For further information on R3 courses and conferences, please visit the R3 website **www.r3.org.uk**, where you can download the 2016 Spring–Summer programme.

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An interview with…

Sarah Albon

The inspector general and chief executive of The Insolvency Service speaks to *RECOVERY* about the big issues that influence the profession.

Q In what way do you think your previous work and role at The Courts and Tribunals Service prepared you for your current role, in particular the 'change management' aspect?

A My experience at the Courts and Tribunals Service (HMCTS) meant that the world of insolvency wasn't quite so alien to me. There is a lot of interaction with the courts and we still do some work with HMCTS. After working in the justice environment, The Insolvency Service felt very much like a home away from home. There is a common purpose across Whitehall at the moment and, as with other areas of government, there has been a big change focused on efficiency and digital agendas.

> It's difficult to propose major change in an organisation and not see it through.

My recent background has been in major transformational change, and that gives me a sense of how well we are set up and how things look. The Service is probably the smallest organisation I've worked with for some time in terms of the number of people and sites. Our running costs here are in the region of £100m per year; in HMCTS you could add another nought on that figure. Also, HMCTS had in excess of 600 sites; we have just 21 here. I've been to each of the offices at least twice, so this means I can get to know people and understand what's going on. There is a sense of scale, but you can also feel there is a chance to make a difference as an individual.

Q We understand that The Service has lost (or is about to lose) more of its highly experienced, long service insolvency experts as they retire or move to other parts of the Civil Service. How are you addressing this challenge?

A With any organisation you lose people all the time. It would be unhealthy if you didn't see a reasonable turnover of staff because you want to think about your talent for the future, training them up and giving them a sense that they've got somewhere to go. If they feel that all the experts at the top are planning to stay there forever, it's a difficult environment in which to develop and attract new talent. On a personal level it's really sad to see people go; even after only a year I've made friends as well as colleagues.

Q You've been in the post just over a year; what has been the main focus of your reforms and what are your targets for the rest of your term?

A There have been some real highlights and really large cases, but we've been making big changes in the way people interact with us. The Redundancy Payments Scheme (RPS) went online and we've now got 99 per cent of people making applications through that system, which is an extraordinary success.

As with all government services, what we really need to think of is the customers – individual members of the public who have lost their jobs and are seeking redundancy payments, and those who are coming into financial difficulty.

We've worked closely with the profession to put in place an online replacement for the old 'D' returns; IPs have helped us to design how we digitise director conduct reporting and how the system can continue to develop.

Another success has been the launch of online bankruptcy applications to our new Adjudicator. We took on that role from HMCTS and have had a good uptake from feedback received, although we still need to wait for a bigger volume of

> The Redundancy Payments Scheme (RPS) went online and we've now got 99 per cent of people making applications through that system, which is an extraordinary success.

cases before we can tell how it is properly working. The Adjudicator has already both approved and rejected applications and, I hope, once we start getting a volume of cases through, people will see that this is an efficient process with a proper scrutiny.

It is important for the Insolvency Service to continue to consider our customers. In our liquidator role, we must consider returns to creditors and how we can maximise them. In enforcement and disqualification, in terms of the role we play in the wider UK corporate world, we need to show how directors of insolvent companies who didn't do the right thing are not able to get away with it: that they can and will be tackled.

Q How long is a typical term?

A There is no 'fixed term' and I certainly don't have any plans to move away quickly. It's difficult to propose major change in an organisation and not see it through. We've had a positive, busy time so far and it was the agency's 25th anniversary this past year.

Q You've already mentioned a couple of digital products that The Service has introduced and it's clearly a major agenda point at the moment. How successful have these products been? And how are you dealing with the 'downtime' issue with the RPS and Insolvency Services Account systems?

A I think we have had some real success with our digital products. They've been delivered on time, on budget and they work. The 99 per cent uptake on the RPS was extraordinary – very few digital launches get that level of success. I think in this case it's because it's targeted to working people, and the population we're aiming at is more computer literate than the general population.

The thing about digital products is that you keep learning and getting feedback as they are used. We're keen to keep working with practitioners and R3 to see what works, as well as what further tweaks the profession would like made.

We've had some periods of downtime and I think in some sense that's going to become a feature of modern life. Any large organisation can have a loss of IT support – just look at the banks, for example. The key thing is that we deal with it quickly, although perhaps we need to do more to publicise the fact that applications made under the RPS are not lost if there's a short period of downtime. The application is not going in a queue to nowhere – it's not lost and we're still meeting our payment targets.

My key message is to *tell us* about any problems you are experiencing. We're keen to fix them. I'm from a background of continuous improvement and I believe complaints are really important feedback. If people don't tell you what's not right for them, you can't do anything.

Q The Kids Company liquidation was dealt with in-house by The Insolvency Service. What made it preferable for the Official Receiver to deal with this over an independent liquidator?

A The thing to remember is that we were appointed by the court. It was an incredibly high profile case, but not particularly complex. We felt that what needed to be done was within our ability. There wasn't a large group of creditors willing to say 'please can we move this case' – we would have done so if half of the creditors had asked for it. We were competent to do it, and the complexity was not around the initial investigation, but around the conduct investigation that was to come and is now ongoing.

Q There was a similar public focus on SSI Redcar and the steel industry. What were the biggest challenges for The Service over the SSI administration and why was The Service appointed?

A What was unusual in both cases was the level of profile. In both we were appointed by the courts to handle the cases. In SSI we appointed special managers and worked closely with PwC and external lawyers. Initially there was the difficult issue of the sheer costs of liquidation and the cost of continuing to buy coal and maintain the coke ovens when there were efforts to find a buyer.

This is still a highly hazardous site – it's at the top end of industrial hazard sites. Being the liquidator also means taking on the liability if anything goes wrong in terms of environmental damage and staffing. We've still got a substantial number of people keeping the site safe and there is a substantial cost in managing that close-down safely. And I think, bluntly, that there was not a firm that would take on the role of liquidator but having that special manager relationship with PwC and an external legal team was essential and has worked really well.

Q How did you deal with the public scrutiny that was focused on the number of redundancies and the actions of the redundancy payments service? How does The Service highlight its good work in general?

A IPs and the Insolvency Service get engaged in something when it's gone really horribly wrong, and there's a real human cost there, whether it's an individual's bankruptcy or a firm's insolvency with the knock-on effects that has for the individuals employed.

We do our best to support each other as I'm sure IPs do as well. Our press team use social media and press releases to highlight the success of individual cases and later this year we are organising our first annual stakeholder presentation to

> We will continue to talk the talk in Whitehall about a good quality regime and the role the profession plays in making sure there is a good insolvency regime.

showcase all our work and seek feedback. We will continue to talk within Whitehall about our good quality regime and the role the profession plays in that. I think my colleagues in the Department for Business, Innovation and Skills (BIS) and other departments understand the importance of a well-functioning insolvency regime, and the role of IPs as a key part of this, in order to make Britain a good place to do business.

It is great that R3 is playing the role of highlighting the good work of the insolvency profession. A lot of the onus will fall on the profession itself – it needs to blow its own trumpet and respond reflectively, not defensively, to criticism. »

Q How do you expect insolvency office holders to resolve the conflict between their duty to look out for creditors' interests and employees' rights to consultation on redundancy if the benefits of the former outweigh the cost of the latter?

A We published a call for evidence last year and we're thinking about what people have said to us. It is clear that people do think that there is a conflict. It's a difficult balance to strike in legislation because it's clear that when there is time to give consultation to employees you must do that, but equally you don't need to spend much time working around insolvency to see that it can be genuinely very difficult to do that on occasions.

> A lot of the onus will fall on the profession itself – it needs to blow its own trumpet and respond reflectively, not defensively, to criticism.

From the feedback, in some cases IPs fear that consultation can precipitate the insolvent outcome that everyone is trying to avoid. I absolutely get the fact that there is a real tension but at the same time there is a legal framework and we need, just as IPs do, to see what more we can do to comply. We need to make sure that the process is saying 'should I consult?', 'is there any more I can do?', rather than a default of 'well it's impossible so why should I try?'. It's an issue that we want to work on collaboratively with R3 and the profession to see what more we can do.

Q What is The Insolvency Service doing to ensure that insolvency regulation is fit for purpose in eradicating inappropriate behaviour by a minority of IPs?

A From this autumn we're no longer a direct regulator of IPs so we'll be looking much more to the Recognised Professional Bodies (RPBs) to play their role. As oversight regulator we are doing what we can in terms of transparency, we're publishing regulatory outcomes and we'll continue to undertake thematic reviews with RPBs. The common gateway has also made a difference and gives us an insight into how complaints are being managed.

We have the tools, if we need, to have more of a challenging conversation with the RPBs. The onus is on the profession to do the right thing, to put pressure on the RPBs to behave in the right way. If the majority of professionals who do behave well feel that their profession is being undermined by RPBs letting their colleagues get away with things, they should be complaining to their own professional body to take action. It's in the profession's interest for the regulatory regime to be seen to be appropriately tough to give people confidence in it.

Q What about The Service becoming a single overall regulator?

A We have additional reserved regulatory powers but it's really early days yet to say that we would or wouldn't use them. The sunset clause is over four years away, so probably about three years in, we will need to look at practice, consult and see if there are problems. From my own postbag, there seem to be fewer complaints from IPs, either individually or collectively. It was always a tiny minority of people doing anything wrong, so maybe the pressure coming from within the profession has made a difference.

Ultimately Parliament gave us those additional powers for a reason and if we really thought that there were problems that could only be addressed by using some of those more draconian powers then of course we would use them. I think it's in all of our interests to avoid that happening if at all possible.

Q What is your view of the pre-pack pool so far?

A I don't think you could say that a pre-pack is good or bad. They are a valid mechanism but potentially open to abuse. We don't oversee the pre-pack pool, but it's interesting that it hasn't had a huge take-up at the moment. Perhaps the changes to the SIP are providing transparency and giving greater confidence to creditors.

At present RPBs don't have a big enough data set to understand the impact of the pool but it's something that we'll be interested in seeing.

Q Do you think the World Bank (WB) insolvency rankings offer a fair view of how good our industry is?

A I don't know if they offer a fair view or not. The change in ranking methodology has certainly resulted in a slip in where we were rated overall, but our insolvency regime hasn't significantly changed. It could look unnecessarily defensive to start arguing about methodology.

I think our insolvency regime is well respected. I think the whole of the wider corporate edifice in the UK is well respected. The legal regime, company law, the way we do business and insolvency, play a massive part in that. That's not to say we're not interested in seeing if we could make the regime even better. We are open to improvement and climbing back up the rankings, but we'd be just as keen to see what we could do working with professionals to make the insolvency regime even better.

Q Would you welcome people from the private sector working for a period within The Insolvency Service, on either short or longer term secondments?

A We absolutely would. I think the movement between us and the profession has tended to be a bit one way, and it has mostly been the other way. We would welcome experienced professionals and we do periodically have people here on secondment.

It's healthy in an organisation to have a mixture of external talent and homegrown talent. If you become too focused on recruiting externally, it can be awkward for those who are homegrown, but equally it can be destabilising and insular to develop your own way of working and never be open to new challenges and ways of working.

> We think that the profession is extremely important to the work that we do and important to the confidence that the wider public has in the insolvency regime.

Q Is there a message you'd like to give to members of the profession reading this interview?

A We think that IPs do extremely important work that is critical to the confidence that the wider public has in the insolvency regime, which we are responsible for protecting. I think we already work well together, but being even more collaborative and having confidence in each other's distinct and important roles are important goals to me. I would welcome greater contact and feedback from IPs. ◻

MATT JUKES is publishing manager of *RECOVERY* magazine.

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