insolvency newsletter

ISSUE 10 – DECEMBER 2006

Contents

Editor: John Davies, Head of Business Law
e-mail: daviesj@accaglobal.com

1. Technical Update

INSOLVENCY RULES

The revised Insolvency Rules are now scheduled to come into effect in April 2008. There is to be a consultation with interested parties in mid-2007 to gauge consultees' reaction to the draft revised Rules prior to their finalisation. The current intention is that the revised Rules will feature several sections which will have common application to administration, liquidation and bankruptcy: these sections will include the relevant rules on, inter alia, meetings and remuneration.

DISCHARGE FROM BANKRUPTCY

The Insolvency Service has published the results of a survey of bankrupts concerning the effects of the discharge procedures as revised by the Enterprise Act 2002.

The survey found that 40% of bankrupts agreed that the reduction in the automatic discharge period had reduced the stigma of bankruptcy [it will be recalled that this was one of he main objectives of the reform] and 75% felt that the reduced period of bankruptcy helped to gave bankrupts a 'fresh start'. Somewhat surprisingly, only 8% of those surveyed claimed that they were aware of the reduced discharge period and were influenced by it when deciding to opt for bankruptcy rather than some other form of insolvency procedure. The survey also raised questions about whether the reduced discharge period is actually encouraging business bankrupts to go back into business - since their discharge, fewer than 5% of respondents had started trading again, obtained credit or become a company director.

The full report of the survey can be found on the Insolvency Service web site: www.insolvency.gov.uk

REVISIONS TO SIPS 2 AND 3

Statements of Insolvency Practice (SIP) 2 and 3 are currently subject to revisions. It is anticipated that the revised SIPs will be issued in January 2007 for implementation on 1 April 2007.

STATISTICS

The official third quarter 2006 insolvency statistics showed that there were 3,235 liquidations in England and Wales, a slight reduction on the figures for both the second quarter of 2006 and the third quarter of 2005. The figures for Northern Ireland showed a similar trend although in Scotland the figure for liquidations showed a rise of 17.3% on the second quarter of 2006 and a rise of 3.5% on the third quarter of 2005.

In England and Wales there were 27,644 individual insolvencies, an increase of 5.7% over the previous quarter and an increase of 55.4% on the same quarter in 2005. The figure was made up of 15,416 bankruptcies, an increase of 2.7% on the previous quarter and 26.5% up on the third quarter of 2005, and 12,228 IVAs, an increase of 9.8% on the previous quarter and 117.9% up on the third quarter of 2005.

In Scotland, there were 3,601 individual insolvencies, up 1.6% on the second quarter of 2006 and 0.2% on the third quarter of 2005. Sequestrations however showed a 17% increase over the previous quarter. In Northern Ireland, individual insolvencies actually decreased over the previous quarter but showed a 32% rise over the third quarter of 2006.

2. Regulatory Update

LIQUIDATOR'S REMUNERATION FOLLOWING ADMINISTRATION

The Regulation and Monitoring Department has encountered instances where some Insolvency Practitioners have attempted to incorporate a resolution for the approval of liquidators' remuneration on a time cost basis within the Administrators' proposals (in the event that the Administrators are appointed liquidators in any subsequent proceeding).

Members will be aware that rule 4.127 of the Insolvency Rules 1986 provides the basis for the liquidator's remuneration and for the persons who are able to make the requisite determination. It is not possible, or appropriate, for the Administrator to attempt to obtain a resolution for the basis of the liquidator's remuneration. Such a matter should be dealt with by the liquidation committee (if any), or failing that, by a meeting of the creditors properly convened for the purpose of determining the basis of the liquidator's remuneration.

CLAIMS FOR VAT REPAYMENTS

Members should be aware that HM Revenue and Customs are now only making VAT repayments in the name of the VAT registered company or trader, rather than in the name of the Insolvency Practitioner's firm. The result of this change in policy is that cases will have to remain open longer in order for the Insolvency Practitioner to finalise the VAT position and obtain any appropriate refunds.

FEES FOR TAX AND OTHER WORK

Members will be aware that where tax and other professional work is carried out by an independent third party it is usually accounted for as a disbursement. Where the work is carried out by a separate department within the Insolvency Practitioner's firm the question has been raised as to whether or not this should be treated as a Category 2 disbursement, thus requiring creditors' agreement. The principle should be that any payment between departments within the same firm should be evidenced, noted and transparent.

SECTION 283A DEADLINE IS FAST APPROACHING

Members are reminded that the three year period, in which the transitional rules relating to section 283A apply to a bankruptcy, comes to an end on 31 March 2007. Accordingly, the trustee must: realise the bankrupt's interest, apply for an order for sale, apply for a section 313 charging order, or agree with the bankrupt that he owes a specific liability to his estate with or without interest from the date of the agreement in consideration for which the interest will cease to form part of the estate by 31 March 2007; otherwise the interest will revert to the bankrupt to the detriment of the estate.

Members should also consider the possibility that any cases currently with the Official Receiver which need to be dealt with by the 31 March 2007 may not yet be distributed to practitioners on the Protracted Realisations Unit rota. If this does occur there will be a limited period of time in which to comply with the provisions of section 283A.

VOLUME IVA PROVIDERS

The expansion of volume IVA providers in the marketplace has led to debate between the Insolvency Service and the Recognised Professional Bodies on the most effective way to regulate such firms. This is a matter which has been considered at a meeting of monitors and will be discussed by the JIC in December 2006 It is an area where communication with the Volume Providers is increasingly important and it has been suggested that one or more Volume IVA Providers be invited to the Regulatory Forum to be held in

March 2007. Following on from that, the meeting of monitors will consider inviting the Volume Providers to a meeting with the monitors (similar to the Compliance Managers' meetings which were held in September 2005). ACCA will be writing to Volume Providers licensed by the ACCA in the New Year regarding the agreed monitoring process.

PROFESSIONAL INDEMNITY DISCOUNTS FOR ACCA QUALITY CHECKED

Members will be aware that ACCA has launched a new general practice quality assurance scheme, *ACCA Quality Checked (AQC)*, which replaced the Quality Checked Seal (QCS). QCS visits have taken place in the UK and Ireland for several years and have proven successful in promoting best practice procedures through a consultation process with member firms. Although best practice procedures can be applied to general practices, the QCS programme was designed to fit the UK and Ireland tax regimes and filing deadlines. It was not therefore appropriate to simply roll out the existing scheme to all disciplines. Instead, ACCA's development team has produced a new product that builds on the existing scheme but will be applicable to all disciplines worldwide.

ACCA Quality Checked is based on five principles which are supported by a set of standards. On a more detailed level, quality controls have been developed to implement the standards. Members can apply suitable quality control procedures to their practices to help provide a consistently good service to their clients, which may result in time savings from improved efficiency and could increase profitability.

To obtain *ACCA Quality Checked* a firm must demonstrate at an *ACCA Quality Checked* visit that it has achieved the standard of excellence required. The firm must demonstrate that it has applied appropriate quality assurance procedures to each area of its business, from practice management, filing and IT systems to its professional services. In addition, firms subject to statutory monitoring in respect of audit, insolvency or investment business, must have a satisfactory monitoring visit outcome before they can be awarded *ACCA Quality Checked*.

For AQS firms who obtain their professional indemnity insurance (PII) with Royal & Sun Alliance through Alexander Forbes, a discount of up to 10% can now be obtained in respect of their PII premiums.

Further information about *ACCA Quality Checked* is available on the ACCA website.

INSOLVENCY SERVICE REFERRALS TO RPBS

Members are reminded of the contents of article 6 in Dear IP 28 of November 2006, which contains a statement of Insolvency Service policy concerning cases where there is a perceived failure on the part of a practitioner to co-operate with an investigation being carried out by the Service.

The statement says that where an investigation suffers through the action or inaction of an insolvency practitioner, staff at the Service have been requested to pass details of the matter to the Insolvency Practitioner Policy section which will, in appropriate circumstances, submit a complaint to the relevant RPB.

Members (and any other person who is subject to ACCA's regulatory control) are reminded that ACCA is bound to consider any complaint alleging misconduct against them with a view to initiating an investigation into their conduct. They are also reminded that, in addition to possible disciplinary proceedings, compliance with applicable laws and regulations are taken into account in the consideration by ACCA of a licence holder's fitness and propriety for the purposes of issuing and renewing insolvency licences.

Members who are unsure of their position regarding requests for co-operation with investigations being carried out by the Insolvency service are invited to contact the ACCA Advisory Help Line on 0207 059 5720.

ACCA RULEBOOK 2007

Some changes are made to the Rulebook for 2007, although these are no way near as extensive as those made in 2006, which saw the overhaul of the Disciplinary and Appeal Regulations and the Code of Ethics and Conduct.

There are, nevertheless, some significant changes this year which have arisen as a result of:

- the move to all oral hearing for Admission and Licensing cases
- ACCA 2007 – the new ACCA Qualification.

Many of the other changes this year reflect 'improvements' on current regulations with the aim of either providing guidance where the procedure has been unclear or addressing unintended consequences. The following is a selection of the changes made.

Admissions and Licensing Committee moving to all meetings being oral hearings

One of the more significant changes this year is the move by the Admissions and Licensing Committee to hold all of its meetings as oral hearings. The Committee deals with all applications which cannot be dealt with administratively. These include applications for rule waivers, admission or re-admission to membership or the student register and for continuing membership from recently bankrupt members. It also deals with cases brought by ACCA for regulatory action following unsatisfactory monitoring visit outcomes. A large proportion of cases in this latter category have, initially, similar outcomes (i.e. a 'hot review' order is imposed on future audit work) and convening meetings to deal with these cases is an increasingly ineffective use of resources. Currently, all cases are initially put to the Admissions and Licensing Committee as paper cases. These hearings are not held in public, members or applicants are not permitted to attend.

Going forward, all cases brought before the Admissions and Licensing Committee will be heard as oral hearings. The aim of this change is to improve the effectiveness of regulatory action where regulated work is of a poor standard, and to ensure that ACCA's processes are faster and more transparent.

Bye-laws

A number of changes to the bye-laws were agreed at the 2006 AGM. The bye-laws now:

- provide for Council to set membership fees within certain limits
- create a clearer distinction in bye-law 8 between the types of conduct which will lead to the initiation of disciplinary proceedings. The change will provide for greater consistency and assist to interpret the bye-law more effectively and apply it to the conduct under consideration
- allow ACCA to fulfil its obligations under UK legislation concerning direct or indirect age discrimination.

Definitions

A review has been undertaken of the definitions used in section 2 of the Rulebook in order to eliminate variations that have crept in over the years, and where appropriate, the relevant regulations have been amended.

Global practising regulations

Following Counsel's advice, a 'for the avoidance of doubt' clause is included in the 'fit and proper person'

provisions. The amendment will allow the Admissions and Licensing Committee to take into account any matters, past or current, when determining a member's fitness to practise.

Various amendments have also been made in respect of continuity of practice. The regulations have been amended to make clear that sole practitioners operating through a limited company may not act as their company's continuity nominee and that members in firms must ensure that the continuity nominee holds an equivalent qualification and authorisation.

There are some conforming amendments to the Annexes to the Global Practising Regulations as a result of ACCA2007, the restructured Membership Regulation 3 and CIPFA's recognitions as a Recognised Qualifying Body for audit purposes.

Similarly, there are some conforming amendments to the Zimbabwe Annex to reflect the practical experience requirements for an audit qualification under ACCA2007.

In the UK Annex to the Global Practising Regulations, the regulations have been amended to make it clear that firms intending to undertake exempt regulated work must register with ACCA before doing so.

Disciplinary regulations

ACCA is mindful of the need to ensure that the disciplinary process is not unnecessarily delayed on procedural technicalities. Accordingly, the regulations have been amended, which will allow the Disciplinary Committee to determine whether a hearing should proceed where the required notice for the service of documents to a member or student has not been met. This would apply where the papers are served a day or two late, and the Committee is satisfied the member or student has been provided with the documents and has not been prejudiced in the conduct of his/her case by this delay.

The regulations have been amended to clarify that the Disciplinary Committee's power to waive fees applies to any allegation proved not simply where misconduct has been proved.

Similarly, the regulations have been amended to clarify that the ill health hearing provisions are intended to apply where the member is asking for the process to be suspended until he/she has recovered from illness.

Appeal regulations

The Appeal Regulations, which were materially revised last year, replaced the appeal by way of fresh hearing with an appeal system based on appellants showing that they have proper grounds before the appeal can proceed. The regulations have been amended to clarify that there is no longer an automatic right of appeal.

The regulations have also been clarified so that a chairman who has directed that an appeal be heard or has considered an appeal application, may sit as a member (as chair or otherwise) of the Appeal Committee which hears that appeal.

Similarly, the regulations have been amended to clarify that the Appeal Committee will only consider the grounds that appellants state in their appeal application notice, and will be entitled to consider as evidence, the reasons for the decision to grant permission.

Code of ethics and conduct

The amendments to this section deal with 'improvements' to the current code, which aim to provide guidance where the procedure has been unclear or to address unintended consequences. The following outlines the key changes to the Code of Ethics and Conduct.

Introduction
This has been amended to accommodate revised bye-law 8a(ii), as agreed at the AGM.

Descriptions of members and firms and the names of practising firms

This section has been amended to clarify that it is misleading for:

- sole practitioners to add the suffix 'and partners' to their firm's name
- firms to add the suffix 'and Associates' to their business name unless they have two or more formal associations/consultancies in existence which can be demonstrated to exist.

Professional appointments
This section now clarifies that on ceasing to hold office, members should promptly transfer books and records belonging to their former client.

Fees
This section clarifies what matters should be included in the letter of engagement in regard to fees. It also highlights ACCA's willingness to arrange the appointment of an arbitrator to resolve fee disputes, which in turn, will support the introduction of an arbitration facility as part of ACCA's conciliation service, in line with UK POB requirements.

Professional liability of accountants and auditors
As with the fees section, ACCA's willingness to arrange the appointment of an arbitrator to resolve fee and other disputes is also highlighted here.

In addition, this section clarifies that members must retain a copy of the letter of engagement which has been signed by the client.

Clients' monies and other assets
This section clarifies that members should not withhold client monies in the event of a fees dispute, i.e. both billed and unbilled fees of the firm. This section also clarifies that members should be able to demonstrate that the records maintained regarding client monies have been controlled, for example by way of regular reconciliations.

ACCA's Rulebook can be viewed on ACCA's website at www.accaglobal.com/members/professionalstandards.

NEW SENIOR COMPLIANCE OFFICER

Ashley Colombo joined the Regulation and Monitoring Department in August 2006. Ashley has worked in the insolvency profession since 1990 and passed the JIEB exams at the December 2001 sitting. It is anticipated that a third member of the insolvency compliance team will be appointed early in 2007.

3. Legislation

COMPANIES ACT 2006

The new Companies Act received the Royal Assent on 8 November and will be brought into effect in stages during 2007 and 2008. The Act consolidates the great majority of the provisions of existing companies legislation and also incorporates the provisions of the Business Names Act 1985. The result is the biggest single statute in UK legal history. The new Act abolishes the current obligations for private companies to hold AGMs and to appoint company secretaries, requires the posting only of service addresses for company directors on the public record and codifies the common law duties of directors. With regard to the latter point, directors generally will be subject to the 'objective test' of skill and care first brought in by section 214 of the Insolvency Act 1986 and, in the process of complying with their new statutory duty to promote the success of their company, will be required to 'have regard' to a number of specified factors such as the long-term consequences of decisions and the desirability of he company maintaining a reputation for high standards of business conduct. Directors who fail to comply with these statutory rules will be in breach of their duties and shareholders will have a new statutory right to bring derivative actions against their company's directors where they consider that breach has occurred. The Act also introduces a new section 176ZA into the Insolvency Act 1986 in response to the House of lords ruling in Leyland Daf. The new section provides that the expenses of a liquidation shall, where the unencumbered assets are insufficient to meet those expenses, be paid in priority to unsecured creditors, preferential creditors and the claims of floating charge holders. Regulations will be made to restrict the application of the new section to expenses authorised or approved by the holder of a floating charge, preferential creditors or the court. Where the application of the section is not so restricted, expenses will be payable by right without the need for authorisation or approval.

INSOLVENCY (AMENDMENT) RULES 2006

The above statutory instrument (SI 2006/1272) came into effect on 1 June 2006. It amends Insolvency Rule 13.12 by extending the definition of 'debt' in the context of winding up and administration so as to include civil claims against the company in respect of circumstances which existed at the time of entry into the insolvency procedure but which had not, at that stage, caused damage to the claimant and thereby provided a cause of action against the company.

The amended Rule applies to companies which enter into administration or liquidation on or after 1 June 2006, save where that procedure has been immediately preceded by another administration or liquidation. It will also apply to a company which went into administration on or after 15 September 2003 and which goes into liquidation on or after 1 June 2006.

THE ENTERPRISE ACT 2002 (DISQUALIFICATION FROM OFFICE: GENERAL) ORDER 2006

The above statutory instrument (SI 2006/1722) repeals or amends a number of statutory provisions regarding the holding by bankrupts of specified offices or positions. Certain restrictions are repealed altogether while others are amended so as to apply only to those who are subject to bankruptcy restriction orders.

NEW DEBT RELIEF PROCEDURE

The Tribunals, Courts and Enforcement Bill was introduced to the Lords on 16 November. As well as making reforms to the tribunal system and to the eligibility rules for judicial appointments, the Bill proposes two reforms of an insolvency nature.

First, the Bill introduces a new Part 7A into the Insolvency Act 1986 in order to provide for a new debt relief procedure for consumer debtors with low levels

of debt and assets. The new procedure will avoid the obligation for the debtor to petition the court for the granting of bankruptcy order, Instead, an application for a debt relief order will be made to the official receiver (through an approved intermediary – such persons are to be individuals approved for this purpose by an authority established for that purpose). The Bill includes provisions designed to safeguard against the abuse of the process; for example, the making of false representations for the purpose of obtaining a debt relief order will be a criminal offence. Discharge from the debts covered by the order will be after one year.

Second, the Bill will enable any creditor in relation to a judgement debt to apply to the High Court or County Court for information about what kind of action it would be appropriate to take to recover the debt in question.

CORPORATE MANSLAUGHTER

The Government has introduced to Parliament a bill that would create a new statutory offence of corporate manslaughter (corporate homicide in Scotland). The offence would be committed where a person to whom a corporate body owes a duty of care dies as the result of a gross breach of that duty of care and where the death can be attributed to failings in the way that the body has been organised or managed. The offence would be punishable by a fine: there would be no direct implications for individual directors or managers.

THE THIRD EU MONEY LAUNDERING DIRECTIVE

The UK is required to implement the requirements of the above into UK law by December 2007. The Directive introduces the following new provisions, inter alia:

- regulated persons are to be entitled to adopt a risk-based approach when determining the extent of the client due diligence checks they need to carry out in respect of prospective clients

- they will be required to carry out on-going identity checks during the course of the client engagement

- there will be a requirement to carry out 'enhanced client due diligence' in cases where the client is not present when the engagement is entered into and when the client is a 'politically exposed person', viz a person who has held high political or military office in another county (or who is a family member or a 'close associate' of such a person).

- Specified types of business, including company formation agencies, will have to be authorised and licensed, which procedure will involve a test of fitness and propriety.

- All regulated persons under the Directive will need to be monitored and supervised to assess their compliance with its requirements.

HM Treasury is currently preparing legislation to give effect to these changes and draft regulations are expected early in the New Year. Licensed insolvency practitioners are, of course, regulated persons for money laundering purposes under the UK's Money Laundering Regulations 2003, even though they are not as a category required to be regulated by the Directive itself. One of the issues HM Treasury has to consider, therefore, is how the new requirements regarding monitoring and supervision are to be applied to insolvency practitioners. One option would be for an assessment of members' compliance with money laundering obligations to be carried out as part of RPBs' routine inspections. Licence holders will be informed of developments in this area during the course of 2007.

4. Cases

EXPENSES IN ADMINISTRATION

Freakey v Centre Reinsurance International [2006] UKHL 45; judgment given 11 October 2006

The House of Lords has ruled that expenses incurred by an insurance company who, under the terms of the policy, were entitled to handle insurance claims of a company in administration, did not have priority under section 19(5) of the Insolvency Act 1986 over the costs of the administration, the floating charge and the unsecured creditors. The policy had stated that the insurance company concerned had, following an insolvency event which included the presentation of an insolvency petition, the exclusive right to handle claims and were entitled to reimbursement for its expenses. The House of Lords agreed with a ruling made by a lower court that the work carried out by the insurance company, while it may have been undertaken on behalf of the company, was not undertaken on behalf of the administrators and for that reason did not qualify for priority over the administration expenses.

JUST AND EQUITABLE WINDING UP

Re Portfolios of Distinction Ltd [2006] EWHC 782 (Ch)

In considering whether to order the winding up of a company under the just and equitable ground under s124 of the Insolvency Act 1986, the court should carry out a balancing exercise, having regard to all the known circumstances. The burden of proof was on the petitioner to establish on the balance of probabilities that it was just and equitable for a company to be wound up.

TECH-INS-010

ACCA
29 Lincoln's Inn Fields London WC2A 3EE United Kingdom
tel: +44 (0)20 7059 5972 fax: +44 (0)20 7059 5730 www.accaglobal.com

The Association of Chartered Certified Accountants