

## Statement of Insolvency Practice 2

### A liquidator's investigation into the affairs of an insolvent company

#### Introduction

1. This statement of insolvency practice is one of a series issued by the Council of the Society with a view to harmonising the approach of members to questions of insolvency practice. It should be read in conjunction with the Explanatory Foreword to the Statements of Insolvency Practice and Insolvency Reminders issued in June 1996.

2. The statement has been prepared for the sole use of members in connection with liquidations of companies registered in England and Wales. Members are reminded that SPI Statements of Insolvency Practice are for the purpose of guidance only and may not be relied upon as definitive statements. No liability attaches to the Council or anyone involved in the preparation or publication of Statements of Insolvency Practice.

3. This statement deals with the duty of a liquidator to investigate the affairs of the insolvent company. The purpose of an investigation is to determine the property (as defined in section 436 of the Insolvency Act 1986) and liabilities of the company and to identify any actions which could lead to the recovery of funds. The standard of investigation set out in this statement should be applied in every case, and creditors should be confident that the investigating duty has been carried out. The extent of any further investigation beyond that set out in this statement will depend upon the assessment, if necessary with legal advice, of the benefit to the insolvent estate. Where a liquidation committee has been appointed the liquidator should normally consult the committee on any matter which might warrant such further investigation so that the committee's views can be obtained in the light of the potential costs and the benefits which might accrue to creditors.

4. The result of the liquidator's investigations will also impact on the discharge of his duties under the Company Directors Disqualification Act 1986.

5. The liquidator should normally commence investigations at the start of the liquidation but investigations may be carried out at any time. When considering his investigation a voluntary liquidator should have regard to the appropriateness of any extensive investigation prior to the hearing by the court of any winding-up petition presented against the company.

#### Best Practice

##### Report to creditors

6. At the initial creditors' meeting and in the subsequent report to creditors the liquidator should invite creditors to bring to his notice any particular matters which they consider require investigation. In a compulsory winding up the official receiver will usually make such an invitation.

##### Liquidation committee

7. The liquidator should also specifically invite members of the liquidation committee to bring to his attention any matters requiring investigation. A copy of this statement of insolvency practice should be made available to liquidation committee members.

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8. The liquidator should advise the liquidation committee of any decision to bring or defend any action or other legal proceedings in the name of and on behalf of the company which may be appropriate following the outcome of his investigation work, and in the case of a compulsory winding up should obtain the necessary sanction.

### **Questioning directors and other key personnel**

9. At the outset of the winding up, the liquidator should normally arrange to make enquiries of the officers of the company and other senior officials as to the company's affairs, including the reasons for failure and the location of its records and property. The liquidator should consider carefully which individuals are relevant to his investigation having regard to the information which he believes they may have. The individuals who may be relevant will normally include:

- (a) all directors (by whatever name called), including directors who held office during the three years prior to the liquidation;
- (b) the company secretary;
- (c) other senior officials and employees,

but may also include others from among the persons listed in section 235(3) of the Insolvency Act 1986. Members may find it useful to issue questionnaires to obtain factual information.

### **Statutory books and minutes**

10. The statutory books of the company, including the minute book, should be examined and compared with a search obtained from the Companies Registration Office. Particular attention should be given to the identity of directors who held office during the three years prior to the liquidation.

### **Validity of charges**

11. Details of all security held by banks and other parties should be obtained and the liquidator should check registration and consider the possible invalidity of any charge. Where liquidation follows receivership, the validity of the receiver's appointment should also be confirmed.

### **Records**

12. At the outset of his appointment the liquidator should ascertain the location and safeguard and list the books, records and other accounting information belonging to the company.

13. The records of the company (including, inter alia, bank statements) covering the period since the date of the last audited or filed accounts, or if none since the incorporation of the company, should be examined to ensure that changes in the financial position of the company can be accounted for.

### **Trading**

14. Consideration should be given to the preparation of trading and profit and loss accounts in any case where there is a material difference between the deficiency disclosed in the statement of affairs and the last audited or filed accounts, or, if none, since the last management accounts or since the incorporation of the company, after taking into account matters such

as writing down asset values. In considering the advisability of preparing trading and profit and loss accounts regard should be had to the likely costs which would be incurred and the benefits which might accrue to creditors from carrying out such an exercise.

### **Comparison of assets with last audited or filed accounts**

15. For the purposes of discovery of company property, the statement of affairs should be compared with the last audited or filed accounts. The liquidator should satisfy himself that material movements in fixed and current assets can be properly explained.

### **Transactions with associated companies or connected persons**

16. The books and records of the company should be examined to ensure that any transactions with associated companies or connected persons (as defined in sections 435 and 249 respectively of the Insolvency Act 1986) were carried out at arm's length and material transactions should be examined in detail. Particular attention should be paid to transactions involving directors, including any reduction in loan accounts, overdrafts or other debts supported by personal guarantees.

17. The liquidator should also satisfy himself as to the validity of any transactions (other than in the ordinary course of business) between the company and any company of which it is an associate during the period of two years prior to the resolution of the directors that the company be wound up. He should similarly satisfy himself in relation to any transactions with any one or more of its directors or any other associate of him or them during the same period. In addition, the liquidator should have special regard to any information supplied by creditors or others which concern transactions between directors and associated companies or connected parties.

## **General**

### **Rights of action**

18. The liquidator's investigation into the affairs of the company should aim to identify any rights of action which the company or the liquidator may have against third parties, and attention is drawn in particular to the following provisions:

#### **Insolvency Act 1986**

<i>Section 76</i>	Redemption or purchase of own shares
<i>Section 127</i>	Avoidance of property dispositions etc.
<i>Section 128</i>	Avoidance of attachments etc.
<i>Sections 150 and 165</i>	Uncalled capital
<i>Section 212</i>	Misfeasance and misapplication etc. of property
<i>Sections 213 and 215</i>	Fraudulent trading
<i>Sections 214 and 215</i>	Wrongful trading
<i>Section 238</i>	Transactions at an undervalue
<i>Section 239</i>	Preferences
<i>Section 244</i>	Extortionate credit transactions
<i>Section 245</i>	Avoidance of floating charges
<i>Section 423</i>	Transactions defrauding creditors

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### **Companies Act 1985**

<i>Sections 135 to 141</i>	Unauthorised reduction of capital
<i>Sections 151 to 181</i>	Unlawful assistance/redemption in the purchase of own shares
<i>Section 277</i>	Unlawful distributions to members
<i>Sections 320 to 322B</i>	Unlawful property transactions
<i>Sections 330 to 341</i>	Unlawful loans

### **Criminal offences**

**19.** If in the course of the winding up it should come to the notice of the liquidator that any past or present officer (or member) of the company may have been guilty of any offence in relation to the company for which he is criminally liable, then in a compulsory winding up the liquidator should report the matter to the official receiver. In a voluntary winding up the liquidator's duty is to report the matter to the Director of Public Prosecutions (Insolvency Act 1986, section 218).

**20.** In the case of a voluntary liquidation, the liquidator must report to the Secretary of State on the conduct of any past or present director where it appears to him that the conduct of that director makes him unfit to be concerned in the management of a company (Company Directors Disqualification Act 1986, section 7).

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