# ACCA Insolvency Newsletter

**This is the third issue of the ACCA Insolvency Newsletter, a twice yearly update for ACCA licence holders on matters of regulatory importance to them.**


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## 1. TECHNICAL GUIDANCE

### 1.1 INSOLVENCY STATISTICS

The official statistics for the first quarter of 2003 were published on 2 May. Recorded company insolvencies in England and Wales were 3,684, a decrease of 13.9% on the last quarter of 2002 and down by 8.2% on the first quarter of 2002. There were 8,103 individual insolvencies, an increase of 1.7% on the previous quarter and up 11.9% on the first quarter of 2002.

### 1.2 COURT FEES

Changes to court fees have been made under the Supreme Court Fees (Amendment) Order 2003 (SI 2003/646) and the County Court Fees (Amendments) Order 2003 (SI 2003/648). The changes came into effect on 1 April 2003. The full list of the fee changes, and a revised series of guides to court fees, can be found on the Court Service's web site, http://www.courtservice.gov.uk/using_courts/fees

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**About ACCA**

The Association of Chartered Certified Accountants (ACCA) is the largest, fastest growing, global professional accountancy body, with nearly 300,000 members and students in 160 countries.

### 1.3 TECHNICAL MANUAL

The Insolvency Service has now published its technical manual on its web-site as part of its duty to make information available to the public under the Freedom of Information Act 2000. This is a useful technical resource for practitioners, particularly in respect of bankruptcies and compulsory liquidations. It also enables practitioners to see the Insolvency Service's attitude and approach to specific issues, such as the matrimonial home and pensions. The technical manual can be accessed at http://www.insolvency.gov.uk/pubsscheme/

### 1.4 SIP 9

R3 will shortly be issuing guidance notes on "transitional provisions" relating to the introduction on SIP 9. These will include guidance on, amongst other matters, information to be provided when reporting to creditors on cases where the case was open and the basis of remuneration approved prior to 29 December 2001 and information to be provided to creditors when seeking agreement to the basis of remuneration in cases which were open prior to 29 December 2001.

There are two particular aspects of SIP 9 that have given rise to clarification being sought form the monitoring unit during monitoring visits. The first relates to the amount of information that should be provided to those responsible for agreeing an office holder's fees. The monitoring unit considers that the suggested format for production of information set out in Appendix D to the SIP, including the time and charge out summary, sets out the minimum disclosure requirements. Consequently, that minimum level of disclosure should be made in cases where the total remuneration is expected to be less than £10,000, although a breakdown of the summary is required to explain any unusual features of the case, which will be a matter for the practitioner to consider on a case by case basis. Practitioners should follow the principles relating to disclosure set out in the SIP, in particular at note 3 to Appendix D, where the expected level of remuneration exceeds £10,000.

Secondly, paragraph 3.3 of the SIP requires a practitioner to provide details of the charge out rates of all grades of staff to meetings where agreement is being sought as to the terms on which they are to be remunerated. The principles underlying the SIP are openness and transparency, so the monitoring unit considers that the practitioner should always provide

details of charge out rates irrespective of whether this is actually requested by those present at the meeting. Preferably, this information should be provided in written form rather than being presented to the meeting orally. In addition, if information relating to charge out rates is provided at the section 98 meeting in a creditors' voluntary liquidation, the monitoring unit considers that it should also be included in the rule 4.49 report issued to creditors. This is on the basis that the rule 4.49 report is a report of the proceedings of the meeting, and so should reflect both the resolutions passed at the meeting and the information provided to creditors at the meeting.

### 1.5 JOINT INSOLVENCY COMMITTEE (JIC)

The Annual Report of the JIC for 2002 is available for information on ACCA's web site - http://www.accaglobal.com/technical/digest.

# 2. Regulatory Guidance

## 2. REGULATORY GUIDANCE

### 2.1 COMMON THEMES IN MONITORING VISITS

This is the second in a continuing series of articles produced by the monitoring unit's compliance officers. It deals with issues that have arisen regularly during the monitoring visits carried out since the last insolvency newsletter. This gives practitioners an insight into changing trends in monitoring and enables those not scheduled for a monitoring visit in the near future to benefit from the main issues which emerge on visits.

**(i) Rule 4.49**

Insolvency Rule 4.49 requires the liquidator to send to creditors and contributories, within 28 days of the creditors' meeting held under s95 or s98 IA 86, a copy or summary of the statement of affairs, together with a report of the proceedings at the meeting. Where information is disclosed to creditors at the meeting, details should be included in the report to creditors in order to ensure that it accurately reflects the proceedings at the meeting.

The information most commonly omitted from these reports concerns information which is required by SIPs 8 and 9 to be provided verbally at the meeting. The omission of such information from the liquidator's reports means that creditors who did not attend the meeting do not receive the information that the SIPs require the liquidator to disclose.

SIP 8 sets out the information which should be given to the creditors at the meeting convened under section 98. It includes, amongst other matters:

1) a summary or a copy of the directors' statement of affairs;

2) details of any prior involvement with the company or its directors by the proposed liquidator;

3) a report of the shareholders' meeting, stating the date of issue of the notice of the meeting, the date and time that the meeting was held and, if it was held at short notice, the reasons for that and confirmation that the requisite consent was obtained from shareholders;

4) the date on which the directors gave instructions for the meeting of creditors to be convened and the date on which the notices were despatched;

5) the details of the costs paid by the company or on its behalf, or proposed to be paid, in connection with the preparation of the statement of affairs, the arrangements for the creditors' meeting, and any advice provided to the company or its directors since the insolvency practitioner was first consulted, indicating in all cases the name of the payee, the amount and the source of the payment;

6) a report on the company's trading history, which should include the date of its incorporation and registered number, a deficiency account and the names and qualifications of any valuer whose valuations have been relied upon for the purpose of the statement of affairs, together with the basis of that valuation;

7) an explanation of the contents of the statement of affairs; and

8) details of any transactions with connected persons or companies during the year prior to the directors' resolution that the company be wound up.

SIP 9, the revised version of which came into force on 1 January 2003, requires an insolvency practitioner to disclose sufficient information to enable those responsible for approving his/her remuneration to form a judgement as to whether the proposed fee is reasonable. This should include the charge out rates for all staff and principals likely to be involved in the case.

Any of the information disclosed under SIPs 8 or 9 at a section 98 meeting should therefore also be included in the subsequent report under rule 4.49.

**(ii) Evidence of investigation and decisions**

Most practitioners carry out detailed investigations into both asset recovery matters and into possible misconduct which could lead to proceedings under the Company Directors Disqualification Act 1986, as required by SIPs 2 and 4. A significant number of visits, however, have highlighted the need for these investigations to be specifically recorded.

SIP 2 requires the liquidator to:

1) invite creditors to bring to his/her notice any particular matters which they consider require investigation both at the section 98 meeting and in the report under rule 4.49;

2) examine the books and records of the company to ensure that any transactions with associated companies or connected persons were carried out at arm's length and to examine material transactions in detail;

3) satisfy him/herself as to the validity of any transactions with associated companies or connected persons during the period of two years prior to the resolution of the directors that the company be wound up; and

4) ascertain the location of and safeguard and list the books, records and other accounting information belonging to the company at the outset of the appointment.

These matters should be clearly evidenced on the practitioner's file and it might be logical to keep the evidence of them in a separate section of the case file, together with a detailed record of any investigation carried out under SIP 4.

SIP 4 provides that an office holder (liquidator/administrator/administrative receiver) who is required under The Insolvent Companies (Reports on Conduct of Directors) Rules 1996 to make a report to the DTI on the conduct of a director or directors is expected to base his report on information coming to light in the ordinary course of his work, including any investigation which has taken place under SIP 2. SIP 4 also requires the office holder to ensure that the basis of his opinion that a report should be submitted is properly documented. ACCA would also expect to see the reasons for any decision to submit a D2 fitted return documented on the case file. In many cases a brief file note would suffice.

ACCA encourages practitioners to use checklists to identify the key investigation and disqualification issues in particular cases in order to identify potential recoveries and whether a conduct return or a report highlighting unfit conduct is appropriate. A checklist is also a useful source of evidence for practitioners to show to the compliance officers during a monitoring visit that they have fulfilled their duties under SIPs 2 and 4.

**(iii) File evidence and structure**

There is no statutory rule or best practice guidance on the sort of filing system which is appropriate to insolvency work, other than the requirement under Scottish Law for a Sederunt Book to be maintained. ACCA expects that any system adopted should contain clear evidence of case events and the reasons for any decisions. In general, practitioners appear to follow one of two systems:

i) a single indexed filing system, based on subject categories which follow approximately the logical chronology of a case, so that, for example, all notices, minutes, proxy schedules, attendance records, and reports relating to a meeting appear in the same section. This system has the flexibility to cover both small and large cases and reduces the need for duplication. This is the monitoring unit's preferred system.

ii) a two-tier system where the practitioner keeps a permanent file (more commonly seen in, and more appropriate to, audit files) containing statutory information and key documents (often the Sederunt Book in Scotland). In addition, the practitioner keeps a working papers file, sometimes by subject but often chronological, into which other documents are placed. The disadvantage of this system is that the longer a case goes on, or the more complex the correspondence becomes, the more likely it is that documents will become difficult to retrieve, or have to be duplicated. The monitoring unit has found that this system is usually less effective in practice.

The monitoring unit considers that it is appropriate for a signed copy of most documents to be retained on file. Whilst a signed copy may be available on the Court file or at Companies House, it is preferable to have a copy readily available to deal with any disputes that might arise.

There should be evidence on file to show to whom a particular circular letter or notice has been sent. This will usually involve a list of the specific creditors, members or other third parties to whom it was sent being attached to the letter or notice. The monitoring unit does not, however, consider it sufficient to have a general list of creditors on file and just annotate the file copy of a letter with "to all creditors/members". The reason for this is because new creditors may come forward at different times during the administration of a case, such that it may not be clear which notices a particular creditor received.

In general, a streamlined filing system will ensure that documents can be readily retrieved, and anyone attempting to administer a file without prior knowledge can understand what has been dealt with and what remains outstanding. As a result, cases will be administered more efficiently, adding value to the administration and reducing the costs to both creditors and insolvency practitioners alike.

### 2.2 BRUMARK

In December 2002, ACCA issued the following guidance to members:

ACCA would normally expect that where a case is potentially in dispute, the following course of action should be taken by the practitioner:

- to ascertain from the chargeholder the reasons for his/her view that a charge may be regarded as fixed

- to advise the preferential creditors of the chargeholder's view and the reasons for it

  and

- if the view of the preferential creditors is that the charge should properly be categorised as floating, then to consider applying to the court for directions. If the practitioner concludes that such an application is not appropriate, then he/she should record the reasons for that decision.

Subsequent chargeholders may also be affected and should be consulted as appropriate.

The above guidance reflects that issued by R3 to its members in May of 2002.

It has recently come to the attention of the monitoring unit that, in cases where insolvency practitioners have been prepared to take disputed cases to court, the banks have often withdrawn "at the courthouse door". The monitoring unit will therefore expect practitioners to clearly state on their files what action they have taken in "Brumark" cases, in accordance with the guidance already issued.

## 2.3 BONDING

Regulation 12(1) of The Insolvency Practitioners Regulations 1990 (as amended) requires an insolvency practitioner to obtain a specific penalty bond for an amount not less than the value of the insolvent estate's assets as estimated in accordance with Schedule 2 of the Regulations, subject to a minimum amount of £5,000 and a maximum amount of £5m, and to forthwith increase the amount of the specific penalty bond where he/she forms the opinion that the value of the insolvent estate's assets is higher than the amount of the existing bond.

The following examples illustrate the monitoring unit's approach to two common problem areas:

i) *IVA contributions of £300 per month, equating to £3,600 per year over the course of a five year arrangement.*

The monitoring unit accepts that there is a degree of uncertainty in voluntary contributions. Consequently, it would not object to an insolvency practitioner initially obtaining a bond for the value of the first year's contributions, subject to the statutory minimum, provided that there are systems in place to monitor the arrangement's progress in relation to the bond value, such that an increased bond is obtained before the value of contributions made exceeds it. Thereafter it would be appropriate to increase the bond annually, or even to obtain a bond for the total expected contributions, given that the arrangement has survived a year. The reasons for bonding other than for the full potential value of the insolvent estate's assets in accordance with the Regulations should be clearly recorded on the file.

ii) *Total realisations to date, £125,000; total distributed to creditors or drawn in fees and expenses, £77,000.*

To comply with Regulation 12(1) the office holder should hold a bond for the full value of the assets realised - £125,000 - and not the value of the funds held.

In general, bonding errors appear to arise less often in practices which obtain a bond to the maximum of each premium band.

## 2.4 IP BANKING UPDATE

IP Banking is the Insolvency Service's new name for Central Accounting Unit. At the last meeting of the IP Banking User Group, an update was given regarding on-line access to estate accounting information.

The on-line system went 'live' in January 2003 and 450 insolvency practitioners are now using the service. Positive feedback on the system was provided at the meeting and the Insolvency Service is encouraging more practitioners to register for and use on-line access.

Those practitioners who currently use on-line access are reminded that they may use the system to print out estate account statements. Consequently, IP Banking will no longer produce automatic 6 monthly statements for practitioners using the on-line system.

## 2.5 PROTRACTED REALISATION BANKRUPTCIES

The Insolvency Service continues to appoint trustees in respect of protracted realisation bankruptcies. In such cases the debtor is usually discharged from bankruptcy. The monitoring unit has become aware that practitioners are advising debtors to propose voluntary arrangements in such circumstances with a view to binding the pre-bankruptcy creditors. Practitioners are reminded that in order to bind such creditors a voluntary arrangement can only be proposed where the debtor is an undischarged bankrupt. Consequently it is unlikely that a voluntary arrangement will be appropriate in protracted realisation appointments.

# 3. Legislation

## 3.1 MONEY LAUNDERING

The Money Laundering Regulations 2003, due to be published shortly, will implement in the UK the provisions of the EU Second Money Laundering Directive. Although insolvency work was not specifically referred to in the Directive, the UK Government decided that insolvency practitioners fall within the scope of the Directive and should therefore be covered by the UK legislation (along with, inter alia, anyone who provides accountancy services or provides tax advice). Under the Regulations, therefore, IPs who 'act as insolvency practitioners', i.e. who accept appointments under the IA 86 or the Insolvency NI Order 1990 will be specifically required to comply with prescribed new responsibilities. (For the purposes of this item the categories of person who are covered by the Regulations are referred to as 'affected persons').

At the time of writing, the implementation date for these new Regulations had yet to be fixed but was likely to be some time in September 2003.

Where the affected person's firm conducts investment business, the prescribed internal procedures should already be in place. If not, then firms will be required to establish them and ensure that adequate internal controls and training are arranged.

In summary, the new Regulations will require affected persons to do two things. Firstly, they must put in place in-house procedures designed to enable them to prevent, identify and report to the authorities any instances of money laundering that they come across. (NB the expanded definition of money laundering - see below).

The specific procedures required by the Regulations are as follows:

i) Identification procedures

An affected person is required to carry out appropriate identification procedures in respect of each instance where

- he forms, or agrees to form, a business relationship* with another party (an 'applicant for business')

- in respect of any one-off transaction he is involved in, he knows or suspects that the transaction involves money laundering, or the transaction involves the payment of 15,000 EUR (currently c£10,500) or more by or to the other party

- in respect of two or more one-off transactions, it appears to the affected person that the transactions are linked and involve payments which, in total, come to 15,000 EUR or more.

(* A business relationship is defined in the Regulations as being any arrangement for the carrying out of transactions on a regular basis where the total amount of any payments to be made by any person to any other in the course of the arrangement is not known at the outset.)

In respect of any relationships covered by the above criteria, the affected person must maintain appropriate identification procedures. These must be sufficient to cover the following matters:

- as soon as is reasonably practical after initial contact is made between the affected person and the other party, satisfactory evidence must be obtained of the person's identity

- where satisfactory evidence of identity is not able to be obtained, the relationship or transaction should not be proceeded with

- where the affected person knows or suspects that another person is involved in money laundering (and reports the matter to NCIS), he/she must comply with any directions given by NCIS in relation to the matter

- where the other party (the second party) acts or appears to act for a third person, then 'reasonable measures' must be taken to establish the identity of that third person. 'Reasonable measures' would include a written assurance from the second party to the effect that the third person's identity has been recorded by him/her, but only where the second party is regulated by an overseas regulatory authority and is based in a country whose law on money laundering is 'comparable' with EU law.

**ii) Record-keeping**

An affected person must maintain procedures for the retention of prescribed records. These records comprise

- copies of evidence of identity or information as to where this can be obtained and
- a record containing details relating to all transactions he has carried out in the course of 'relevant business'

These records must be kept for five years from the end of 'business relationships' and for five years from the date of completion of a one-off transaction (or the date of completion of the last of a series of them).

**iii) Internal Reporting**

The affected person is responsible for ensuring that his firm maintains internal reporting procedures so as to ensure that

- someone in his firm is appointed to be its money laundering reporting officer (MLRO)
- anyone in the firm who 'handles relevant business' who knows or suspects that a transaction involves money laundering reports the matter to the MLRO
- the MLRO (or some other designated person) considers any report, in the light of any additional information provided by the affected person, and considers whether it gives rise to knowledge or suspicion of money laundering.
- the MLRO reports any knowledge or suspicion of money laundering to NCIS.

The report to NCIS should be made as soon as practicable and may be made on a pro-forma form prepared by NCIS (http://www.ncis.gov.uk).

N.B. The above 'internal reporting' requirements do not apply to sole practitioners who have no employees and who do not in association with any other person.

Over and above the specific procedures set out above, affected persons must establish any other procedures of internal control and communication as may be appropriate for the purposes of forestalling and preventing money laundering.

They must also take appropriate measures to ensure that their employees are made aware of the requirements of the new regulations and of the expanded definitions of 'money laundering' contained in the Proceeds of Crime Act 2002. Specifically, affected persons are required to give their staff training in how to recognise and deal with transactions which may be related to money laundering.

Note that, under the Regulations, money laundering is now taken to encompass

- the concealment, disguising, conversion, transfer or removal from the UK of criminal property

- involvement in an arrangement in which a person knows or suspects that it facilitates the acquisition, retention, use or control of criminal property by or on behalf of another person

- the acquisition, use or possession of criminal property.

Property is criminal property if i) it constitutes or represents a person's benefit from criminal conduct or ii) the alleged offender knows or suspects that it constitutes or represents such a benefit. Criminal conduct is itself defined as any conduct which constitutes an offence in any part of the UK. Accordingly, the scope of 'money laundering' , as far as reporting responsibilities are concerned, is expanded significantly by the new Regulations. The offences now covered include the proceeds of tax evasion and benefits obtained though bribery and corruption.

Detailed guidance on compliance with the Regulations is being issued to members by ACCA separately. R3 is to consider what additional guidance may be appropriate for insolvency practitioners.

# 4. Recent Cases

## 4.1 SUMMONING OF OFFICERS UNDER S236 IA 86

Under s236 IA 86, an office holder may apply to the court to summon before it any officer of the company or other person who may be in possession of the company's property or who may have information concerning the company. In the case in question, a s236 order was granted against the directors of the company in liquidation. The judge, in granting the order, held that s235 and s236 were to be read together and that the classes of people covered by s235 - whom he called 'insiders' - were under a greater duty to assist the office holder than others. Consequently, an insider's ability to contest a s236 order was reduced, and the consideration of 'oppression' was to be put to one side. On the directors' appeal, the court held that it was not correct that, in the case of insiders, the rule against oppressive conduct was not to apply. However, any oppression might be outweighed in a particular case by the legitimate requirements of the liquidator. In this particular case, the court agreed that the circumstances justified the making of the order.

*Re RBG Resources Ltd (Shierson v Rastogi) [2003] 1 WLR 586*

## 4.2 DIRECTORS' DUTIES TO CREDITORS

The court reaffirmed that, where a company is insolvent or on the verge of insolvency, directors must consider the interests of the creditors as paramount.

The defendant company held the lease of a block of flats; the three tenants each held one share in the company. After one tenant - CGA - embarked on substantial amendments without obtaining the prior consent of the company, the company issued proceedings for forfeiture of the flat. At a subsequent board meeting of the company, the two directors present - one of whom was CGA - voted to agree to a settlement which was clearly disadvantageous to the company.

By the time of the meeting, the company had been served with a statutory demand and the directors had been clearly aware of the company's pending insolvency. The court, in hearing an application from the directors for confirmation that their decision had been valid, held that the directors should not have released the company's claim without considering the impact of this on its creditors. Further, the court could apply the test of whether 'honest and intelligent'

directors would have been capable of believing that the decision was for the benefit of creditors.

*Colin Gwyer Associates v London Wharf (Limehouse) Ltd, Chancery Division 13 December 2002*

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