ACCA Insolvency Newsletter

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

1 TECHNICAL GUIDANCE

1.1 SIP 9 – CLARIFICATION

Section 4 of the current SIP 9 deals with the provision of information to creditors after the basis of remuneration has been approved. The interaction between various sections of the SIP and Appendix D means that there are different interpretations with regard to the level of information that needs to be provided to creditors when an office holder reports to them on the quantum of remuneration drawn after the basis of their remuneration has been approved. ACCA has sought clarification on this issue from R3 and now considers that the following is the correct interpretation on the disclosure provisions.

- Where the total fees are expected to be less than £10,000 then, in general, the practitioner need only provide the information set out at paragraph 4.1, namely details of the time spent, charge-out value to date, and any material changes in the rates charged in reports to creditors. If, however, there are any

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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.

unusual features to the case then practitioners should also provide a summary in the format set out in Appendix D (or something similar).

- Where the total fees are expected to be between £10,000 and £50,000 then, in general, the summary in the format set out in Appendix D (or something similar) should be sufficient.

- Where the total fees are expected to be in excess of £50,000 then, in general, a summary providing a more detailed breakdown than that contained in the format set out in Appendix D (or similar) will be required.

When providing information to creditors, practitioners should always bear in mind that creditors have the right to challenge the level of the office holder's remuneration and hence provide them with sufficient information to enable them to decide whether to exercise those rights. Consequently, practitioners may wish to consider issuing a summary in all cases, even where the expected level of fees is less than £10,000.

Please note that with regard to the disclosure provisions applicable to cases where total fees are expected to be less than £10,000, this is a different interpretation of the disclosure provisions of SIP 9 from that which the monitoring unit was indicating to practitioners during monitoring visits that took place in late 2002 and in the early part of 2003.

1.2 INSOLVENCY STATISTICS

The third quarter statistics for 2003, published on 7 November, revealed a drop in the number of corporate insolvencies. There were 3,398 company insolvencies in England and Wales during the period, a decrease of 11.2% on the second quarter and a fall of 12.5% on the third quarter of 2002.

However, the rate of individual insolvencies increased. There were 9,094 individual insolvencies, an increase of 4.1% on the previous quarter and an increase of 16.9% on the third quarter of 2002.

1.3 EC PROJECT – INSOLVENCY

Following the Lisbon meeting of the European Council in 2000, the European Commission initiated a benchmarking project on 'Restructuring, Bankruptcy and a Fresh Start'. The project was undertaken by an 'expert group' comprised of Government representatives from all member states, chaired by the Commission. The group has now published its final report.

The report takes the form of a comparative analysis of the legal provision and social and business attitudes to insolvency across the EU. The report makes a number of recommendations for future action, which are directed to the Commission. These recommendations are largely consistent with the reforms made by the UK Government under the Enterprise Act 2002. They include the following.

- Businesses should have access to external advice at an early stage so as to enable early recognition of financial difficulties and the initiation of remedial measures.
- Training courses for new entrepreneurs and business advisers should be provided.
- Rescue and restructuring procedures should be simplified and made cheaper.
- The 'unnecessary' effects of bankruptcy should be reduced or removed.
- Early discharge from debts should be available, on certain conditions.
- A fresh start for entrepreneurs who failed through no fault of their own should be promoted.

The full report can be found on the EC website at http://europa.eu.int/comm/enterprise/entrepreneurship/support_measures/failure_bankruptcy/index.htm

2. Regulatory Guidance

2 REGULATORY GUIDANCE

2.1 PROXIES

The incorrect use of proxies is often encountered during monitoring visits. This item looks at some of the main statutory provisions and offers practical advice for preventing common pitfalls.

Under IR 8.6(1) a proxy holder is not permitted to vote in favour of any resolution which would directly or indirectly put him, or any associate of his, in a position to receive any remuneration out of the insolvent estate, unless the proxy specifically directs him to vote in that way. Where such instructions are included, the proxy will be a 'special proxy'. Where no instructions are given, the proxy is a 'general proxy'.

IR 8.6(2) makes clear that IR 8.6 applies to any person acting as chairman of a meeting and using proxies in that capacity under IR 8.3; and in its application to him the proxy-holder is deemed an associate of his. IR 8.3(3) states that where the responsible insolvency practitioner holds proxies to be used by him as chairman of a meeting, and some other person acts as chairman, the other person may use the insolvency practitioner's proxies as if he were himself proxy-holder.

Consequently, IRs 8.6(2) and 8.3(3) prevent an insolvency practitioner from requesting a non-associate of his to chair a meeting and vote in favour of any resolution which would directly or indirectly put the insolvency practitioner, or any other associate of the chairman, in a position to receive any remuneration out of the insolvent estate, unless the proxy specifically directed the acting chairman to vote in that way.

In the most simple terms, therefore, an insolvency practitioner acting as chairman can only vote in favour of his own appointment to office and matters relating to his remuneration if he holds a special proxy. A general proxy can never be used by an insolvency practitioner acting as chairman to vote in this way.

Advancing the argument that, as chairman holding a general proxy, the insolvency practitioner (or other acting chairman) has exercised his discretion to vote in favour of a resolution that

places him, or an associate, in a position to receive remuneration simply does not work. The Rules are very clear and there is no inherent discretion in these circumstances.

In the case of voluntary arrangements, insolvency practitioners often quote IRs 1.15 and 5.16, which state that the chairman is prohibited from using a proxy to vote to increase or reduce the amount of remuneration or expenses of the nominee or supervisor of the proposed arrangement, unless the proxy specifically directs him to vote in that way. A chairman holding a general proxy cannot vote in this way, but a chairman holding a special proxy can, provided there are specific instructions in the proxy for the chairman to vote on remuneration.

IRs 1.15 and 5.16 and 8.6 are not mutually exclusive. Consequently, insolvency practitioners involved in voluntary arrangements must be aware of the restrictions imposed by IR 8.6 when chairing meetings.

In practice, the incorrect use of proxies will only cause problems if a resolution would not have been passed but for the inclusion of the invalid vote. An insolvency practitioner may find that a resolution approving the basis of his remuneration and category 2 disbursements, as defined in the revised SIP 9, is invalid and, consequently, that he has drawn unauthorised remuneration. This constitutes a serious breach and will be viewed as such by the monitoring unit.

It's not all bad news, however, as there are several steps that can be taken to alleviate potential problems arising. IR 8.2 and SIP 10 make clear that proxy forms cannot be pre-completed before despatch with any information except the title of the proceedings. The monitoring unit would, however, have no objection to instructions being given to those appointing proxies, provided the wording used did not infringe the rules against improper inducement or solicitation. In particular, proxy forms should specify the resolutions being sought at a meeting, together with 'for/against' voting options, and the creditor (or member) may be asked to delete the inappropriate voting option to make their voting instructions clear in view of the provisions of IR 8.6. Instructions may also be given to ensure that a proxy-holder is nominated, otherwise the proxy will be invalid.

A proxy schedule, recording the validity of votes, should be compiled as soon as proxies are received. Instructions as to how the vote on a general proxy is to be cast can then be sought

from the creditor (or member). These should be either endorsed on the proxy form itself by the creditor (or member), or given by them in writing prior to the meeting. Written instructions should be retained with the proxy. On no account should the insolvency practitioner, his staff, or the acting chairman amend a proxy, even where the creditor (or member) has sanctioned this course of action.

2.2 BONDING

A serious issue that is often found during monitoring visits is under-bonding, both where the bond is set at a level less than the value of the insolvent estate's assets and also, more seriously, where the level of the bond is for less than the value of funds received to date. This latter situation may arise, for example, as a result of the incorrect initial valuation of the insolvent estate's assets, or as a result of new assets coming to light, or as a result of realisations exceeding expectations.

In simple terms, when determining whether the current level of a bond is sufficient, the monitoring unit compares the value of funds received by the insolvency practitioner in his capacity as office holder with the amount of the bond. The monitoring unit considers that the value of funds received includes any interest earned on estate funds held in the estate account or the ISA. The monitoring unit also considers that it is not appropriate to exclude from the calculation any distributions already made or office holder's fees paid.

In order to minimise the risk of under-bonding the monitoring unit recommends that practitioners have in place a system to review the level of bonds, both as part of the routine case review process, and also whenever a significant realisation is received to the estate account.

Putting a review system in place should not, however, detract from the underlying requirement under Regulation 12(1) of The Insolvency Practitioners Regulations 1990 (as amended) whereby a practitioner is required to have in place a specific penalty bond for an amount not less than the value of the insolvent estate's assets 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.

Where a practitioner decides to bond for an amount less than the amount of the insolvent estate's assets disclosed in the statement of affairs, or notified by the Official Receiver in respect of compulsory liquidations and bankruptcies where there is no statement of affairs, then he/she should make a file note to record the reasons for that decision and for setting the bond at the particular level chosen.

2.3 REGULATION 17 CASE RECORDS

The Regulation 17 Case Records form a useful source of information for the monitoring unit during monitoring visits. They can also be a useful means of assisting insolvency practitioners in the control of their cases. However, the monitoring unit frequently encounters problems with the completeness and accuracy of information contained in Case Records.

Practitioners are reminded that they should record in the Case Record the information specified in Schedule 3 to the Regulations forthwith upon the occurrence of the event concerned. With regard to accuracy, the most common errors found are:

- where practitioners use the IPS Turnkey system, the date of commencement of the insolvency proceedings is incorrectly shown as the date of the first meeting with the directors

- the commencement date in compulsory liquidations is incorrectly shown as the winding up order date rather than the date of presentation of the winding up petition

  and

- the first general meeting of creditors convened by the insolvency practitioner acting as trustee or liquidator in compulsory liquidations is incorrectly recorded as the 'first' meeting of creditors.

2.4 SIP 2

Practitioners are reminded that an insolvency practitioner's duties to investigate the affairs of an insolvent company under SIP 2 apply both to companies in creditors' voluntary liquidation and also to those in compulsory liquidation. Whilst the Official Receiver also has a duty to investigate in compulsory liquidations, and is responsible for submitting a return/report on the conduct of the directors, the liquidator must still make his/her own enquires in order to comply with SIP 2. However, the insolvency practitioner should make as much use of the Official Receiver's investigations as possible. Information about potential antecedent recoveries should be included in the hand-over papers provided by the Official Receiver, but insolvency practitioners may consider it appropriate to make appropriate enquiries about such matters at hand-over.

2.5 WHAT IS THE TIMESCALE FOR DISCHARGING A STATUTORY DUTY 'FORTHWITH'?

An office holder may be required to discharge a statutory obligation, such as giving notice, forthwith. 'Forthwith', however, is defined neither in the Insolvency Act 1986, as amended, nor the Insolvency Rules 1986. Consequently, there has been varying opinion and practice as to the timescale for the performance of the particular statutory duty. From a regulator's perspective, what exactly is the anticipated timescale for discharging a specific statutory obligation 'forthwith'?

The Compact Oxford English Dictionary defines 'forthwith' as 'without delay'. Halsbury's Laws of England reports that there appears to be no material difference between "immediately" and 'forthwith'. It further states that a provision that something must be done "forthwith" or 'immediately' means that it must be done as soon as possible in the circumstances, taking into account the nature of the act to be done. The meaning of 'forthwith' has also been subjected to judicial consideration over the years, but none of the more recent cases appear to relate directly to insolvency.

The monitoring unit considers that 'forthwith' means without unjustified delay. It does not mean within a specified timescale such as 7 or 14 days, or at the convenience of the officeholder, taking into account other commitments or workload.

Examples of statutory duties that must be discharged forthwith are set out below. References to a section number or rule are to the Insolvency Act 1986, as amended and the Insolvency Rules 1986, respectively.

- Regulations 5 (compulsory winding up) and 20 (bankruptcy) of the Insolvency Regulations 1994 impose a duty to remit funds forthwith to the Insolvency Services Account where £5,000 or more is received.

- Regulation 17 of the Insolvency Practitioners Regulations 1990 imposes a duty to maintain a case record for each insolvency appointment, and to make the appropriate entry into the record forthwith upon the occurrence of any recordable event, as specified in schedule 3 to the Regulations.

- IR 4.106(4) imposes a duty to give notice of appointment as liquidator in a compulsory winding up to the Registrar of Companies forthwith.

- Section 171(5) and IR 4.142(5) impose a duty on a liquidator appointed to a company in a members' voluntary winding up to give notice of resignation as liquidator forthwith to the Registrar of Companies.

- IRs 4.138(2) (compulsory liquidation) and 6.146(2) (bankruptcy) impose a duty to file proofs of debt forthwith in court when the administration of the estate is for practical purposes complete.

- Section 46(1) imposes a duty on an administrative receiver to send notice of his/her appointment to the company and to publish notice of the appointment forthwith.

Practitioners are reminded that the monitoring unit expects these duties, along with any other statutory duties that are required to be discharged forthwith, to be discharged 'without delay'. Although the facts of the case and associated circumstances will be taken into account when assessing compliance it is anticipated that exceptional circumstances preventing a statutory duty being discharged forthwith will be encountered only rarely. Practitioners must, therefore, anticipate any circumstances that may affect their ability to comply with forthcoming statutory duties. This will include absences from the office due to work commitments, or holidays. In

such cases the monitoring unit will expect the practitioner to have prepared in advance to avoid any delay occurring.

Further guidance on this topic may be obtained from ACCA's monitoring unit.

2.6 TRAINING

During monitoring visits the compliance officers are occasionally asked why ACCA does not provide technical insolvency training for the insolvency practitioners it licences. The answer to this lies in the structure of the profession and the existence of R3.

When R3 (SPI as it was then called) was set up with the assistance of the Recognised Professional Bodies (RPBs), memoranda of understanding were entered into between R3 and each of the RPBs. As part of these memoranda it was agreed that R3 would provide 'technical' training and support for its members, and that the RPBs would not compete with R3 by running such courses of their own. It is for this reason that ACCA does not provide technical insolvency training courses for insolvency practitioners.

ACCA has, however, run occasional events dealing with regulatory issues relating to insolvency, and ACCA is arranging two such events in 2004. These events will take place in London in the Spring, and the Midlands/North in the Autumn. Full details of these events will be provided to insolvency practitioners nearer the time, but they will be an opportunity for ACCA to explain its approach to insolvency regulation, and in particular to monitoring and complaints handling.

2.7 NATWEST CLIENTS' MONIES SERVICE

NatWest offers an online clients' account service called the 'Clients' Monies Service' (CMS). This involves a central hub account and separate accounts for each client (estate for insolvency practitioners). Since this is an online account there is only one cheque book, for the hub account, and funds are transferred to/from that account from/to the separate estate accounts as funds are paid/received.

ACCA is satisfied that the CMS service complies with the requirements of SIP 11 with regard to the need for separate estate accounts that are clients' accounts. However, there is a potential issue relating to interest earned on the estate accounts that causes the monitoring unit concern. The rate of interest earned on the estate accounts is that applicable to the aggregate balance of funds held in all the estate accounts, rather than that applicable to the amount held in each separate account. This aggregation of balances is only notional and for interest purposes only, and is a direct result of the 'hub' structure of the CMS service. However, the CMS service is not designed specifically for insolvency practitioners and consequently the account holder can elect as to whether all, some, or none of the additional interest earned by virtue of the aggregation of balances is passed on to the separate estate accounts. Since these accounts contain estate funds and are clearly trust accounts, an insolvency practitioner using the CMS service must ensure that all the additional interest is credited to the separate estate accounts.

Consequently, where a practitioner uses the CMS service the monitoring unit will, as a matter of routine, require the practitioner to obtain written confirmation from NatWest that all interest earned is credited to the separate estate accounts.

2.8 SIP 9 – TRANSITIONAL ARRANGEMENTS

Practitioners are reminded of the advice regarding transitional arrangements for the revised SIP 9 which was circulated in October. This advises that, in respect of cases which commenced before 31 December 2002 (i.e. before the revised SIP 9 came into effect), any reports issued or resolutions taken after that date should comply with the new SIP. However, where any analysis or disclosure required for such a report or resolution relates to a period prior to 31 December 2002, it should comply with the new SIP as far as the available records reasonably allow.

3. Legislation

3 LEGISLATION

3.1 MONEY LAUNDERING

The new money laundering regulations, which were originally scheduled to come into effect in June 2003, have been subjected to repeated delays. On 23 October, Parliament was informed that the regulations would appear 'shortly'. Subsequently, on 30 October, the Treasury announced that there had been a further delay in preparing the regulations - no indication was given of the likely publication date but it is considered that the regulations will not now come into effect until February 2004 at the earliest. It will be recalled that R3 is considering additional, specific guidance for insolvency practitioners over and above the interim guidance which has already been prepared by CCAB. The guidance issued by ACCA is available in Fact Sheets 85 and 86, both of which are available via the ACCA website (www.accaglobal.com/practicechannel/publications).

3.2 ENTERPRISE ACT 2002

Members will be aware that the corporate insolvency-related provisions of the Enterprise Act 2002 came into effect on 15 September 2003. Part X of the Enterprise Act, which contains the new provisions relating to personal insolvency, will come into effect on 1 April 2004. Substantial consequential changes to the Insolvency Rules are made by The Insolvency (Amendment) Rules 2003 (SI2003/1730). As with the primary legislation, the changes to the Rules dealing with 'corporate' provisions came into effect on 15 September 2003; the changes to the 'personal' provisions will take effect on 1 April 2004.

Members are reminded that, consequent to the coming into force of the 'corporate' provisions, the Insolvency Service is undertaking a project to ascertain whether the new 'prescribed part' rules, which are designed to ensure that the benefit of the abolition of Crown preference flows to unsecured creditors, are appropriately framed so as to bring about the desired outcome. Practitioners are encouraged to take part in this project by filling in a simple form in respect of formal insolvency appointments which they have taken on on or after 1 April 2003. The form can be downloaded from the Insolvency Service website (www.insolvency.gov.uk).

3.3 COMPANY LAW REFORM

The DTI has announced that the long-expected Company Law Reform Bill will not now form part of the package of measures to be announced in the Queen's Speech on 26 November. There will still be a limited Companies Bill in the next session but this will not be the comprehensive reform exercise envisaged by the Company Law Review project or by the DTI's White Paper of July 2002. The fully reformed Companies Act is not now expected to come into effect until 2008.

Separately from the above, the Government has now completed its consultation exercise on the future of the small company audit exemption threshold. The Government was expected to announce that it had decided to increase the existing turnover threshold of £1 million to the maximum level now permissible under EU law (c£5.6 million). ACCA's response to the consultation argued that the DTI's case for such a major increase in the threshold was not proven. It pointed to the fact that 93% of all the complaints received by Companies House regarding the quality of published accounts relate to unaudited accounts; it suggested that the proposal would have major implications for the detection of fraud and money laundering; and argued that the prospective benefits to small companies in terms of cost savings had been seriously exaggerated. The government announced on November 19 that it was to go ahead with its original proposal to raise the threshold to £5.6 million.

3.4 PENSIONS REFORM

Among the other measures expected to feature in the Queen's Speech is a new Pensions Bill. The Bill will bring in a requirement that solvent employers who want to wind up their schemes be made liable for the full costs (as opposed the immediate cash value) of buying out members' benefits. This reform is in response to the highly-publicised recent cases where solvent schemes have been wound up to the detriment of active and deferred scheme members.

The Bill will also amend the priority order in which the assets of a pension scheme are distributed. At present, after meeting scheme expenses and debts to third parties, pensioners have claim on the scheme's assets before non-pensioners; all those employees still working, irrespective of length of scheme membership, are treated broadly the same. The amended order will therefore aim to improve the position of active and deferred scheme members.

4. Recent Cases

4 CASES

4.1 USE OF S236 IA 86 IN CONNECTION WITH DISQUALIFICATION PROCEEDINGS

Official Receiver v Wadge Rapps & Hunt (Re Pantmaenog Timber Co), [2003] UKHL 49

The House of Lords has allowed an appeal by the Official Receiver against the dismissal of an earlier appeal against a ruling that the purpose of s236 IA 86 was to assist the liquidator of a company in carrying out his functions as liquidator and did not extend to helping him in situations where his sole purpose in searching for information was in connection with bringing disqualification proceedings against the company's former directors.

The Lords of Appeal held that s236 contained no express limitation on the purposes for which it might be invoked. Further, the functions of the office holder included the making of a report to the Secretary of State where he was in possession of information which led him to the conclusion that the conditions for disqualification were satisfied. A narrow interpretation of s236, which confined its scope to information which the office holder needed to get in the property of the company, would not be in the public interest and would increase the risk that wrong doers would go unpunished.

4.2 RIGHT OF ACTION IN BANKRUPTCY

Mulkerrins v PricewaterhouseCoopers, [2003] UKHL 41

A bankrupt claimed damages from her professional advisers (PwC) for having negligently failed to protect her from her bankruptcy. The question on which the House of Lords was asked to rule concerned whether the right of action vested in the bankrupt or her trustee for the benefit of her creditors. The Court of Appeal had allowed PwC's appeal against the ruling of a district judge that the right of action vested in the bankrupt and not the trustee, a ruling against which the trustee himself had not appealed.

The Lords agreed that PwC had no right of action in this matter, which was an issue solely between the trustee and the bankrupt. In the absence of any appeal by the trustee, the trustee and creditors were bound by the order. The bankrupt was therefore free to continue with her action against PwC.

While not seeking to rule on the merits of the earlier order, Lord Millett commented that the debtor has been 'shamefully ill-served by her professional advisers, by the law of insolvency and by the civil justice system'.

4.3 DUTIES OF RECEIVERS

Silven Properties Ltd v Royal Bank of Scotland, The Times, 27 October 2003

Receivers appointed by a bank to sell properties owned by borrowers were under no duty to take steps to increase the market value of properties by obtaining planning permissions or seeking tenants for the properties which were to be sold.

The borrowers had contended that the receivers were under a duty to take such steps in order to obtain the best sale price possible.

The Court of Appeal, dismissing an appeal by the borrowers against an earlier ruling, accepted that the receivers owed a fiduciary duty of care to the bank and the borrowers. However, the actual scope of this duty would depend on and reflect the special nature of the relationship between the bank, the borrowers and the receivers arising from the terms of the charges and appointments. Those conditions would preclude any automatic assumption by, or imposition on, the receiver of the obligation to take the pre-marketing steps which the borrowers felt were appropriate. The receivers were at all times free, as was the bank, to halt those steps and to exercise the right to proceed with an immediate sale of the charged properties.

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