

JOINT INSOLVENCY EXAMINATION BOARD

*Joint
Insolvency
Examination
Board*

Joint Insolvency Examination (Scotland)

Tuesday 8 November 2011

ADMINISTRATIONS, COMPANY VOLUNTARY ARRANGEMENTS and RECEIVERSHIPS (3.5 hours)

ANSWER ALL FOUR QUESTIONS

EACH QUESTION CARRIES TWENTY-FIVE MARKS

SUBMIT ALL WORKINGS

The Examiner will take account of the way material is presented. Candidates should answer the questions set - and marks will not be awarded for extraneous material.

Note: References to legislation are to that which was in force on 30 April 2011. References to 'the Act' are to the Insolvency Act 1986 as amended.

References to Sections, Schedules and Rules are to Sections and Schedules of the Act and to Rules of the Insolvency (Scotland) Rules 1986 as amended.

References to Sections and Rules of other Acts, Regulations and Orders will mention the Act, Regulation or Order.

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1. The case manager of Bluefin Products Limited (“the Company”) recently left the practice of Jones and Carter Accounting LLP to join a competing firm of insolvency practitioners. Prior to his departure, the case manager finalised the Company’s affairs and the Administration was closed.

You have been provided with the following note prepared by the case manager prior to his departure.

Jones and Carter Accounting LLP
14 The Square
Largs
KA30 8HG

File note on Bluefin Products Limited (company number SC1234567) – In Administration

Richard Jones and Emma Carter were appointed Administrators on 13 January 2011 pursuant to Paragraph 22 of Schedule B1 to the Act.

A meeting of creditors was held on 15 February 2011 at which the Administrators’ proposals were approved. The Administrators’ proposals stated that the proposed exit route would be through dissolution and that discharge from liability pursuant to Paragraph 84 would occur 14 days from filing the notice at Companies House.

It was agreed at this meeting that the remuneration of the office holders would be a fixed fee of £35,000 plus VAT.

Company assets

Heritable property

The heritable property was initially valued at £1,250,000 by Smith & Co Chartered Surveyors (“Smith & Co”). The heritable property was subject to a standard security in favour of Skipjack Bank Limited which was owed £750,000 at the date of appointment of Administrators.

Smith & Co were instructed to market the property for sale and it was agreed that their fees would be 5% of the net proceeds.

A sale of the property was agreed (subject to contract) on 25 March 2011 at a price of £1,150,000. In early April 2011, shortly prior to completion, a competing fully funded bid at £2,250,000 was received from a local house builder. As a result the property was sold to the house builder and completion occurred on 23 May 2011.

Trade debtors

A comprehensive review of the debtors was carried out upon appointment and it was established that debts amounting to £650,000 would be collectable. A debt collection agency; Albacore Collections Limited (“Albacore”) was instructed to undertake the collection process. It was agreed that Albacore’s fees would be 5% of realisations.

The debt collection initially went according to plan, however, in April 2011 it became clear that one of the debts amounting to £150,000 would be wholly uncollectable. The remaining debts were collected as anticipated.

Sale of the business

Following the appointment of Administrators, the business was marketed for a short period. A sale of the business was concluded in January 2011 and the purchaser immediately vacated the site. The amounts realised from this disposal was as follows:

	Estimated to realise at appointment	Sale proceeds
	£	£
Stock	100,000	80,000
Plant and machinery	350,000	350,000
Goodwill	50,000	50,000

The estimated-to-realise-at-appointment figures were those provided by Smith & Co following a valuation on the day of appointment.

Residual plant and machinery

Elements of the Company's plant and machinery were excluded from the business sale since these were not required by the purchaser. Smith & Co valued these as follows:

	Estimated to realise at appointment	Sale proceeds
	£	£
Unencumbered assets	300,000	550,000

The excluded plant and machinery was sold at an auction held on 15 April 2011 and it was agreed that Smith & Co would receive a fee of 10% of the proceeds plus a buyer's premium of 10%.

In addition there were a number of items subject to a hire purchase agreement in favour of Tunny Finance Limited. The Administrators consented to the removal and disposal of these assets by Tunny Finance Limited and the associated realisation was as follows:

	Estimated to realise at appointment	Actual Sale proceeds
	£	£
Plant and machinery	250,000	250,000
Finance outstanding (Tunny Finance Limited)	450,000	n/a

Creditors

The following unsecured claims were received:

Bigeye Services Limited	£3,350,000
Atlantic Gold Limited	£2,100,000

On 12 August 2011 a successful application was made to the court enabling the Administrator to distribute the funds in hand to the unsecured, non-preferential creditors. In this respect payments were made on 26 September 2011.

Other statutory information

A D1 form was submitted on 11 May 2011.

Closure

Additional disbursements including legal costs amounted to £25,000 plus VAT.

The notice pursuant to Paragraph 84(1) was filed on 17 October 2011.

A thorough review of the case indicates that all the above matters were properly dealt with and there were no additional issues to address. However the review identified that the file did not contain the minimum information that Insolvency Practitioners are required to maintain.

Requirements

Stating appropriate assumptions, prepare a schedule summarising for this case the minimum information that Insolvency Practitioners are required to maintain.

(25 marks)

NOTES: Assume all VAT is recoverable
Assume a VAT rate of 20%
Ignore Corporation tax

2. Twisoft Limited (the "Company") is an IT software business specialising in developing applications for a major internet social networking site.

In 2002 the business acquired an office block in Inverness for £475,000. This purchase was funded in part by Bangor Bank plc (the "Bank") through a loan facility. This loan is secured by a standard security over the property and a floating charge over the Company's remaining assets. Increasing property values and a solid trading performance enabled the Company to release equity in the property over the following years to fund the growing working capital requirements of the business.

Whilst the business had historically been highly profitable, the popularity of the social networking website had significantly diminished over the last few years and during the last financial year the business reported significant losses.

Recently the directors implemented a profitability improvement plan involving a number of initiatives:

- Software development was outsourced to a lower-cost French operator. As a result, the development team in Inverness were made redundant. As part of this outsourcing agreement certain assets of the Company were loaned to the new provider.
- A significant proportion of the office space has been let to third parties generating an income of £4,000 per week.
- The non-domestic rating has been successfully challenged and as a result the Company's rates liability has reduced to the equivalent of £2,000 per week.

Despite these efforts the business has continued to incur losses.

Following a breach of the loan facility covenants, the Bank commissioned a review of the business. This review identified that the Company has in excess of £700,000 of unsecured, non-preferential creditors including HMRC, utilities, trade suppliers and customers, all of which are based in the UK. Subsequent to this review the Bank, which is the sole secured creditor, last week served demand for full repayment of the loan amounting to £2,450,000.

The Company has confirmed that it is not in a position to repay the debt and the Bank has approached your firm for advice. The following additional information has been established:

- (i) A review of the property has been undertaken and it has been identified that for tax purposes the current indexed cost of the property is £650,000. Your agents have valued the property at £2,750,000 and believe that the property could be sold at this price within 12 weeks.
- (ii) Your agents have informed you that the remaining floating charge assets have a net realisable value of £50,000 for the UK operations and £35,000 for the assets in France.

- (iii) You have identified that, due to the complexity of the lease arrangements and the continual maintenance requirements of the property, for the next 12 weeks it would be necessary to retain a number of staff. These staff members have agreed to work during that period after which they would be made redundant. The staff required consist of the following:

Title	Weekly pay	Service (years)	Age	Contribution to occupational pension
Maintenance manager	£750	4	45	5%
Tenant supervisor	£400	1	25	0%
Caretaker	£300	7	40	7.5%

The remaining staff would be made immediately redundant by the Company and it is estimated that the resulting redundancy and notice liability would be £45,000. All staff are currently paid up to date in relation to salary and holiday pay.

Requirements

- (a) **Briefly outline the formal options that the Bank has under its security arrangements to recover its debt. Summarise the comparative financial outcome for the Bank of each option. (15 marks)**
- (b) **Set out the key advantages and disadvantages to the Bank of each of its options. (10 marks)**

(25 marks)

**NOTES: Ignore office holder, realisation and legal costs
Assume a Corporation tax rate of 30%
Ignore Employer's national insurance
National Insurance Fund upper limit on the amount of a week's pay is £400**

- 3(a) Snax Biscuits Limited (the “Company”) is a long established, family-owned mass producer of white label baked biscuits for a number of supermarket chains. Just under two years ago the business lost a major contract, accounting for 40% of its turnover. Whilst the Company was able to restructure its operations, the associated costs and losses resulted in cash flow difficulties. As a result 18 months ago the Company entered into a CVA and your principal was appointed Supervisor.

Because of current issues relating to the CVA a meeting between the Supervisor and the directors was recently convened and the following matters discussed:

- (i) Due to poor trading the Company is currently two months in arrears in respect of its agreed contributions. During the meeting the directors stated that they would be unable to make the following month’s contribution.
- (ii) It was a condition of the CVA that the directors’ loan accounts would not be repaid by the Company until the CVA had successfully concluded. During the meeting the directors stated that £250,000 of the loans has been repaid.
- (iii) The terms of the CVA provided for redundant plant and machinery on the Company’s premises to be disposed of for the benefit of the CVA creditors. The CVA stated that these assets would be held on trust for the benefit of creditors and that the Company would be responsible for the sale. The directors confirmed that no action had been taken to sell these assets.
- (iv) HMRC is owed £300,000 in relation to post CVA unpaid VAT and payroll taxes. Two weeks ago HMRC carried out an attachment of the plant and machinery at the Company’s premises.
- (v) The terms of the CVA provided for the Supervisor to be remunerated on a time cost basis. The directors stated that they considered that the level of fees charged to the case so far was disproportionate and requested full details of what work had been undertaken.
- (vi) The electricity supplier, which was not subject to the CVA, is owed a significant sum and intends to disconnect supply imminently unless the current arrears are paid in full. Without power the business would immediately cease to trade and any value in the business would be irreparably damaged.

Requirements

For each matter outlined in (i) to (vi) explain what steps the Supervisor may take to deal with each situation. (15 marks)

- 3(b) Shortly following this meeting the directors contacted the Supervisor to discuss the situation further. The directors explained that whilst they believed that there was an underlying sound business the continuing viability could only be achieved through an investment of capital via a third party. They provided evidence that there was a third party equity provider willing to invest in the business on condition that it was able to make a clean break from the CVA.

Requirements

Explain generally what options could be considered to facilitate the investment and any issues likely to arise in the particular circumstances of this case. (10 marks)

(25 marks)

4. Your principal, a sole practitioner in a small firm of accountants, was appointed sole Administrator of Clowder Products Limited (the "Company") by the directors on 15 February 2011.

An extract from the statement of affairs as prepared by the directors of the Company shortly following appointment is presented below together with relevant notes.

	Estimated to realise £	Note
Assets specifically pledged		
Freehold property	350,000	(i)
Amounts due to Yoke Bank	<u>(250,000)</u>	
	100,000	
Assets not specifically pledged		
Surplus from book debts	200,000	(ii)
Stock	50,000	(iii)
Plant, equipment and motor vehicles	<u>125,000</u>	(iii)
	475,000	
Preferential creditors	<u>(50,000)</u>	
	425,000	
Unsecured creditors	<u>(1,750,000)</u>	
Deficit towards creditors	<u>(1,325,000)</u>	

(i) Freehold property

The heritable property was vacated immediately following appointment and agents were instructed to market it for sale. There has been little interest in the property and no buyer has been found. The holding costs of the property amount to £625 per week and have been paid up to date. It has been agreed that the agent's fees will be paid out of the sale proceeds at a level of 2.5% of gross realisations.

The heritable property is subject to a standard security in favour of Yoke Bank ("Yoke"). Yoke also holds a floating charge in respect of this debt covering all remaining assets of the Company.

(ii) Book debts

The book debts of the Company were validly assigned to Cover Finance Limited ("Cover") who, at appointment, was owed £450,000. The gross debts collected by Cover amounted to £650,000 and Cover deducted £50,000 costs from these proceeds before paying over the surplus to the Administrator. On 8 July 2011, at the same time the surplus was paid over, the residual debts of £50,000 were reassigned to the Company.

Following a further two months of customer negotiations a final settlement of £25,000 was agreed and paid in relation to the only collectable residual debt.

(iii) Sale of business

The business and assets of the business were sold 4 weeks after the appointment of the Administrator, realising the following:

	£
Goodwill	100,000
Stock	40,000
Plant and machinery	90,000

The consideration in relation to the Stock and Plant and machinery was payable upon completion and the goodwill payable in two equal instalments; two months and six months following completion. The legal costs associated with the sale amounted to £20,000 and were netted off the initial sale proceeds.

(iv) Costs

The basis of remuneration of the Administrator was agreed by the Creditors' Committee during the initial creditors' meeting. It was agreed that such remuneration would be based upon a fixed fee of £10,000 plus 5% of all realisations. All fees are paid up to date.

Additional legal costs of £10,000 have been incurred and paid.

In October 2011, prior to the closure of the Administration, your principal died.

Requirements

- (a) Explain what arrangements your principal should have in place to deal with the transfer of cases in the event of his death or incapacity. (5 marks)**
- (b) Outline the procedural steps that may be undertaken to deal with the transfer of this case. (10 marks)**
- (c) Prepare a final receipts and payments account for inclusion in a final report to creditors assuming closure on 14 November 2011. (10 marks)**

(25 marks)

NOTE: Ignore VAT