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**Winter 2016**

# RECOVERY


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Advice for IPs from HMRC

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To claim or not to claim against the Official Receiver and BEIS?

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# From the editor

Change is competing with new technology as the theme of this issue of *RECOVERY*. Our president, Andrew Tate, majors on change in his column on p4. He reminds us that many changes have and will come from the government, but their proposals themselves merit change. We should perhaps reflect that both appetites for change and the way to influence change are changing. In the political sphere, reasoned liberal debate and polite lobbying have been overshadowed by emotive appeals exploiting perceived injustices – and radical change has ensued.

Change surrounds the Official Receiver acting as an office-holder. Andrew refers to the Insolvency Service's policy change and to the regulatory imbalance it highlights (how regulated is the OR?). Another highlight comes from the fascinating legal update from Joseph Curl, Paul Allen and Andrew Foster on p8. *Longmeade* is a significant case on at least three counts. As well as reminding IPs that the court is not a bomb shelter and bringing clarity to liquidators' consideration of the wishes of creditors, *Longmeade*, through the analysis set out in the legal update, identifies Court of Appeal authority that the OR can be sued in relation to his acts or omissions as liquidator and that the Department for Business, Energy and Industrial Strategy would probably be liable.

Change affects the courts, as Adrian Cohen and Giles Allison explain on p13. Some of that change is technological, one aspect of which (service of documents) is explored by Gemma Kaplan on p20. Simon Edel and Olivia Lancaster's article on p22 concludes, having considered technological change in the world of insolvency, that embracing technology is a business imperative. How apposite then to read the article from Henry Page and Rachael Ellis on p24 explaining blockchains and how they work and warning of the likely disruption of the financial sector by FinTech. Might this be a stimulant for the UK economy if financial passporting rights are lost on a hard Brexit?

Change also involves our own practices. Like me, many IPs will be spending more time as advisors, helping businesses to avoid formal insolvency when it's right and feasible to do so. Alison Byrne tells her story – from Fiat 500 to formal change management techniques – on p39. As a new year approaches, we at *RECOVERY* hope that the changes it brings help all our readers to prosper.

C. Laughton

**CHRIS LAUGHTON** is editor of *RECOVERY* and a partner at Mercer & Hole.

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| SUMMER | Tax |
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| WINTER | Avoiding insolvency (turnaround) |

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Chris Laughton, Mercer & Hole



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Peter Thompson, HSBC



**Publishing manager** Matt Jukes
Tel: 01491 828939, matthew.jukes@groupgti.com

**Advertising director** Will Nevill
Tel: 01491 828920, william.nevill@groupgti.com

**Creative director** Thomas Gray

**Administration** Jack Roberts

**Printed by** Stephens & George

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www.r3.org.uk/recovery

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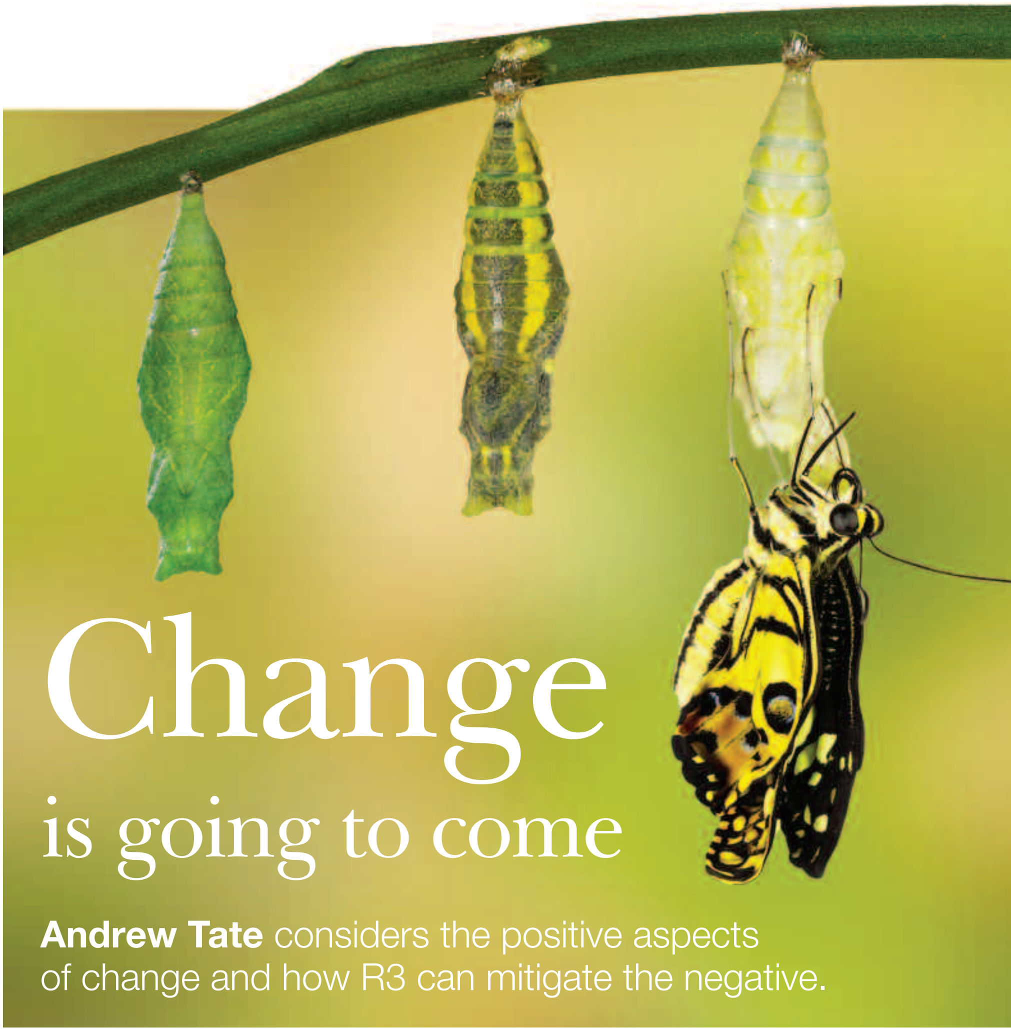

# Change is going to come

**Andrew Tate** considers the positive aspects of change and how R3 can mitigate the negative.

One of the constant themes of recent president's columns in *RECOVERY* has been change. In my short time as president, I've already written about it; my predecessors have covered it extensively, too. Change is, of course, inevitable and necessary, helping the insolvency and restructuring regime adapt and stay relevant.

This year, the modern iteration of the UK's insolvency regime turned 30. Over the past three decades, the regime has proven to be remarkably durable and successful and, importantly, adaptable to changing circumstances. Businesses have changed, creditor behaviour has changed, the types of creditor have changed, funding options have changed, other legislation has changed and, as you will see from other articles in this edition, technology has changed the insolvency and restructuring world too.

Change can mean tweaks and amendments to insolvency procedures or the responsibilities and requirements of IPs, or it can be deeper, less perceptible change; the kind of change that is gradual yet takes you far away from where you started. Changes to IPs' fees, pre-packs and creditors' meetings are examples of the former; the rise of restructuring that I've focused on as president is an example of the latter.

> “Change can be deeper, less perceptible... yet takes you far away from where you started.”

The increasing importance of restructuring work in the insolvency profession's day-to-day work is just one of a number of changes happening now that, taken together, could represent some of the most important changes to affect the insolvency and restructuring regime for a long time.

And while change can be positive, it can sometimes take us off in the wrong direction, too. R3 is there to make sure that doesn't happen.

### The importance of restructuring

Although there has been little objective analysis of the rise of restructuring – something R3 is looking to address in the coming months – there is no doubt that it is taking place. It's noticeable to those of us working on the frontline of insolvency that the type of work we are called in to do has evolved, while insolvency numbers suggest some sort of shift has occurred.

There is a sense, too, that the growth in importance of restructuring work has been positive for the economy. It has allowed more flexibility when working with struggling businesses, helped businesses seek advice sooner and may have allowed for more businesses to be rescued.

Governments internationally are now playing catch-up with developments: the UK government's recent corporate insolvency framework proposals contained several features designed to formalise restructuring work.

The intentions behind the proposed reforms are welcome and it's pleasing that the importance of restructuring could be recognised in legislation. As the business environment changes, it's crucial that the regime dealing with business distress shifts with it.

However, the proposed reforms, as set out in the government's consultation paper, are not necessarily the best way forward. Rather than formalising what works about existing restructuring efforts – flexibility and IP expertise among other things – many of the reforms ignore what we already have and introduce things that may work overseas but may not work in a UK context. One of the predominant features of the reforms is an increased role for the court in approving and overseeing procedures. While this is the sort of approach favoured in the US and other jurisdictions, it would represent a fundamental shift in how insolvency and restructuring work in the UK is carried out.

The good news is that the reforms are far from finalised and there is plenty of scope for change and improvement. The government's proposal for a business rescue moratorium, for example, is similar to an earlier proposal by R3 and there is still time to move the government's plans closer to those of the views of the restructuring professionals represented by R3.

Encouragingly, the government has indicated that it is open to further input on its proposals for a new restructuring tool and essential supplies reforms. These latter changes appear to be an extension of an earlier R3 campaign – although in this instance our proposals may have been extended a little too far.

> “Governments internationally are now playing catch-up with developments.”

As a whole, the government's reform proposals need to do more to protect both creditors and debtors. And the government should also remember that we already have an effective and flexible framework; it would be better to work with what we already have than introduce new, untested procedures.

Change happens, and change can be a good thing, but it need not be radical to make a difference. Gradual change may mean slower change, but it means change all the same – and it may be more

manageable in the long run, too.

The corporate insolvency framework reform proposals are, of course, only one of a few government-instigated changes causing consternation for the profession at the moment. The government's changes to OR fees and guidance on making secretary of state appointments could well have long-term unintended consequences. It is appropriate that, as R3 president, I reflect the concerns of the profession to the government and this is exactly what I am doing.

> Change happens, and change can be a good thing, but it need not be radical to make a difference.

R3 is continuing to discuss these changes with the Insolvency Service to ensure that the consequences are properly thought through, and we are very pleased that the Insolvency Service has committed to reviewing its revised technical guidance in the wake of pressure from R3; as IPs will have seen from Dear IP 73, the Insolvency Service will be working with R3 to put together revised guidance in time for Dear IP 74.

The changes made to the OR's guidance raised serious concerns about creditors' wishes being respected but there is also the danger that the changes could lead to a de-skilling in the insolvency profession as young insolvency professionals lose the opportunity to hone their skills. This is a real concern to senior insolvency professionals.

Regrettably, the changes published also brought into sharp focus concerns around the accountability and transparency of the system operated by the OR. As the article on the Longmeade case later in this edition of *RECOVERY* shows, ORs are capable of making occasional significant mistakes to creditors' detriment – and while IPs may make similar errors, they are subject to much, much more transparent oversight and regulation. Mistakes by IPs are apparent through the reporting and monitoring regime we are subject to and have clear consequences for those making the mistake; the lack of case reporting requirements or overall monitoring reports of the OR service means that creditors cannot know whether the work is being undertaking efficiently and diligently. IPs and ORs will undoubtedly do all their work to the best of their ability but there seems little justification for a two-tier regulatory regime, particularly given the fee changes brought in in July.

Finally, all these changes are taking place against the backdrop of 'Brexit'.

The vote to leave the EU – and the manner in which the UK eventually leaves – will mean changes to the work we take on and the way we work in future. There may be an increase in insolvencies in the near future, and it may become harder for the profession to do its job and return money to creditors when European cross-border work is needed. Ensuring the benefits of the EC Insolvency Regulation can be retained post-Brexit will be a priority for R3 and we will be looking to feed the profession's views into the government's Brexit negotiations.

### Sticking up for the profession

As well as highlighting the profession's restructuring skills set, one of the things I said I would do as president would be to stick up and fight for our profession. That objective is more important now than ever before.

Insolvency issues are never far from the news and as well as the developments detailed above, more demands for change are always likely. Just this month, a report for a parliamentary committee has called for a new look at pensions and pre-packs – just a year after the last round of pre-pack reforms were introduced.

> The vote to leave the EU... will mean changes to the work we take on and the way we work in future.

At R3, we're here to make sure that policy-makers are educated about the profession and regime, that they understand what we do, and that they understand our concerns. During the party conference season we met the new insolvency minister Margot James MP, and since then we have caught up with 14 other parliamentarians. More meetings are planned in the coming weeks, including with the shadow insolvency minister, to make sure public debate on the future of the insolvency and restructuring regime is properly informed.

The UK's insolvency and restructuring profession and regime are among the best in the world. They are flexible and effective and make an enormous contribution to our economy. Change can help cement the positions of both regime and profession, but it has to be the right kind of change. ◻

**ANDREW TATE** is president of R3 and a partner at Kreston Reeves LLP.

▶ If you are a lawyer and would like to write for Legal Q&A please contact: **matthew.jukes@groupgti.com.**

# Recent case summaries

Latest insolvency update from **Rowena Page**.

## CORPORATE INSOLVENCY

***BTI 2014 LLC* v. *Sequana SA & Ors* [2016] EWHC 1696 (Ch)**

The claimants brought a claim against the first and second defendants and the second defendant's directors (D1, D2 and 'the directors' respectively). The background was as follows:

- Based on interim accounts (which included an estimate of a future liability that the D2 was at that time liable to pay), in December 2008 the directors resolved to reduce the D2's capital and pay an interim dividend to D1 (the December dividend). A favourable solvency statement was prepared and signed by directors before this was done.
- In May 2009 the directors determined to sell D2 to a third party and resolved to pay D1 a further dividend (the May dividend). Again, a favourable solvency statement was prepared and signed.

> This decision is interesting as it is one of the first of its kind in determining that the declaration of a dividend is, or can be, a transaction at an undervalue.

- D2's actual accounts for year-end 2008 showed that it had suffered substantial losses.
- The claimants brought proceedings alleging that the reduction of capital was unlawful; the directors had acted in breach of fiduciary duty; and the December and May dividends were transactions defrauding creditors contrary to s423, Insolvency Act 1986.

It was held by Rose J that:

- The breach of fiduciary duty claims and part 23 Companies Act 2006 claims should be dismissed. The validity of a solvency statement depended simply on the directors having *actually formed* the opinions stipulated within the statement. Provided they had formed those views, the statement was valid; there was no need to show the directors had reasonable grounds for doing so. Further, the correct test under s643(1)(a) Companies Act was not whether, if calamity struck, the company *might* be unable to pay its debts, but whether the company was in fact unable to pay its debts, taking into account prospective and contingent liabilities: *BNY Corporate Trustee Services Ltd* v. *Eurosail-UK 2007-3BL plc* [2013] UKSC 28 applied.

The s423 claim should be allowed in respect of the May dividend (but not the December dividend). On the evidence, it was held that in December the directors did not have the requisite purpose to place D2's assets beyond the reach of creditors, but that they did have that purpose in May when they declared the May dividend.

This decision is interesting as it is one of the first of its kind in determining that the declaration of a dividend is, or can be, a transaction at an undervalue. The court also left open the question of whether in other circumstances a change of position defence could be advanced by a recipient of the dividend, so further argument on this point can be expected in future (*4Eng* v. *Harper* [2009] EWHC 2633 (Ch) distinguished).

## PERSONAL INSOLVENCY

***Horton (as trustee in bankruptcy of Michael Gerard Henry)* v. *Michael Gerard Henry* [2016] EWCA Civ 989**

The bankrupt (B) had one self-invested and three personal pension policies. B was entitled to draw down under the policies, but had not at the date of his bankruptcy (or thereafter) chosen to do so, living instead on the 'generosity of his wife and family'.

B's trustee in bankruptcy (TIB) sought an income payments order under s310 Insolvency Act 1986 (IA) in respect of B's pension entitlements.

Prior to the instant decision the authorities at this stage were conflicted on the question of whether an entitlement to draw down a pension fell within s310(7) IA, and/or whether it was possible to require a bankrupt to elect to draw down using the provisions of s333 IA or s363 IA.

In her leading judgment Gloster LJ held that:

- The TIB could not compel B to exercise his rights to draw down on his pensions: *'it would draw a coach and horses through the protection afforded to a bankrupt's pension rights by the Insolvency Act and pension legislation [s11 Welfare Reform and Pensions Act 1999] if a trustee were able, in effect, to require a bankrupt to make the entirety of his pension available for the satisfaction of creditors' claims…'* (at [38]).
- The fact that, prior to bankruptcy, a judgment creditor may by injunction compel a judgment debtor to elect to draw down his pension does not mean that a trustee can do the same where the debtor is in bankruptcy. Filing for bankruptcy provides relief from the ability of creditors to individually execute

> As a matter of interpretation, the *right* to draw down on a pension was not a '*payment in the nature of income*' within the meaning s310(7) IA.

upon the debtor's assets, in favour of a process of collective execution. A non-bankrupt judgment debtor is therefore in a wholly different position to a bankrupt debtor: a judgment creditor cannot have the benefits of bankruptcy without its burdens.

As a matter of interpretation, the *right* to draw down on a pension was not a *'payment in the nature of income'* within the meaning s310(7) IA. Such a construction would be wholly unrealistic: 'payment' when used in s310 *'does not mean a chose in action or a bundle of rights which, if exercised, and only then, give rise to the making of a payment'*.

The instant case provides clear guidance on the circumstances in which a bankrupt's pension rights will and will not fall within the income payments order provisions of the insolvency legislation. It is notable that the court chose to preserve the ability of judgment creditors of non-bankrupts to require them to exercise their pension rights (see *Blight* v. *Brewster* [2012] EWHC 165 (Ch)) therefore drawing a distinction between the availability of pensions assets to creditors in pre and post bankruptcy situations. ◻

**ROWENA PAGE**
is a barrister at Enterprise Chambers.

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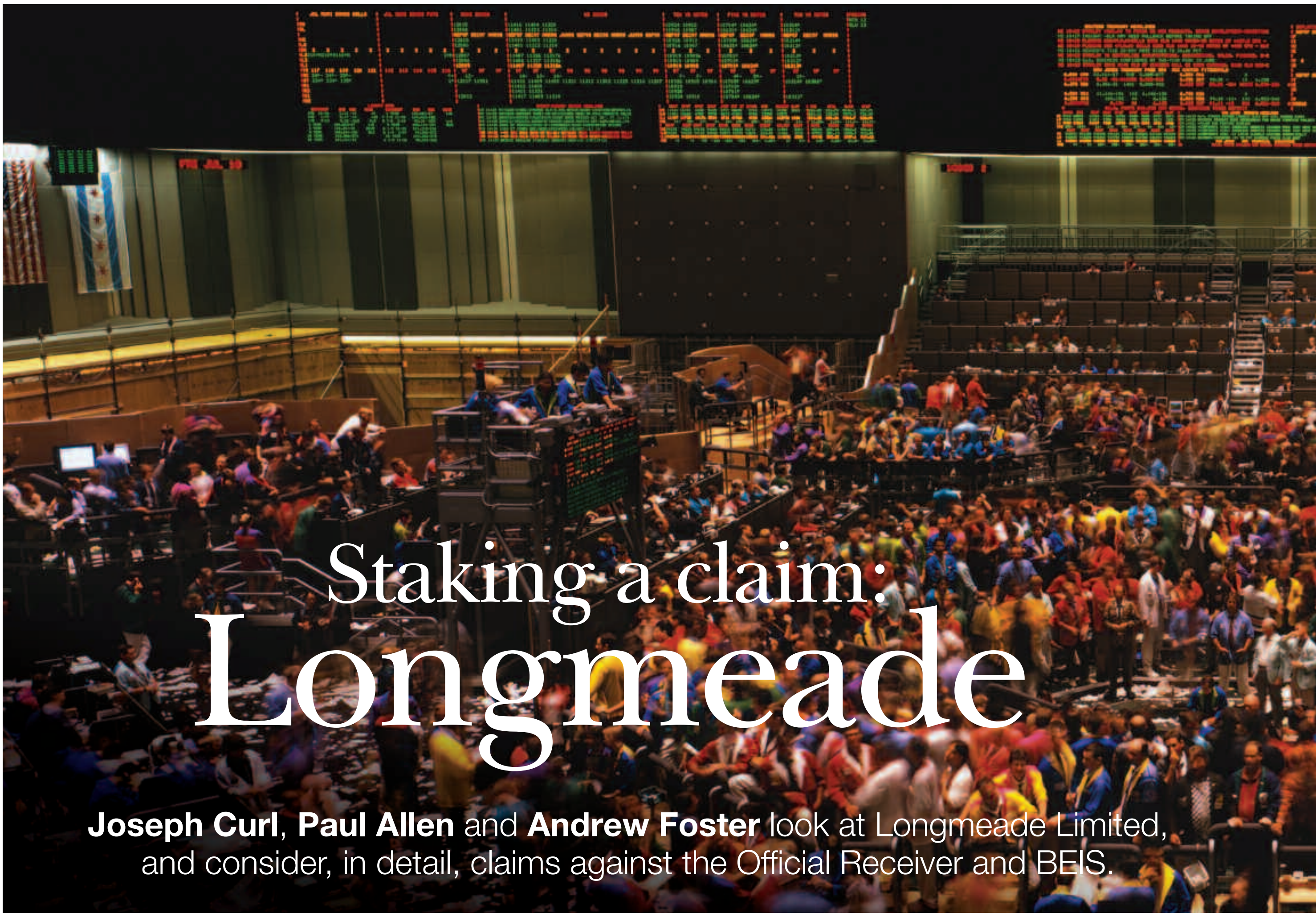

# Staking a claim: Longmeade

**Joseph Curl**, **Paul Allen** and **Andrew Foster** look at Longmeade Limited, and consider, in detail, claims against the Official Receiver and BEIS.

In *Re Longmeade Limited (in liquidation)*[1] Mr Justice Snowden gave guidance on the extent to which liquidators in a compulsory winding-up need to consult with creditors or refer to the court before commencing proceedings, following the change to section 167 of the Insolvency Act (IA) in May last year. In this article, the professionals who made the application for directions to Snowden J reflect on his Lordship's judgment but also the other aspect to the case – the ability of successor office-holders to bring claims against the Official Receiver (OR) and BIS (now BEIS) in negligence.

## Background

Longmeade Limited was a company in the Lehman Group that went into compulsory liquidation in March 2010. On its winding-up, the OR was appointed in the usual way. On the liability side of its balance sheet were nine creditors, whose debts totalled just over £93m. HMRC was the largest creditor at about 49 per cent of the amount owed by Longmeade. Next came a group of inter-company creditors controlled by Lehman Brothers Holdings Inc (LBHI) in the US, whose debts were 46 per cent of the total. There were also some debts owed to Lehman estates where office-holders from PwC had been appointed (approximately four per cent) and some very small creditors making up the remainder.

On the asset side of Longmeade's balance sheet was just one significant item: a claim in a US Lehman estate in the amount of $130m. The US Lehman estate in question was subject to a plan of reorganisation, administered by LBHI, under which substantial distributions were being made to creditors.

> **"LBHI's London agent referred the OR's office to certain tax forms that had to be completed and filed if Longmeade was to participate in each distribution."**

LBHI's London agent referred the OR's office to certain tax forms that had to be completed and filed if Longmeade was to participate in each distribution. Unfortunately, the OR's office did not file the forms and this resulted in Longmeade missing distributions in 2012, which would have amounted to around $26m.

Paul Allen and Jason Baker of FRP Advisory LLP then replaced the OR as liquidators in early 2013. Upon their appointment they ensured that subsequent dividends were paid to Longmeade and investigated whether it might be possible to recover the loss of the previous distributions from the OR. There was no prospect of playing catch-up under the plan of reorganisation as a set of forms must be filed within a particular timeframe, following which the distribution reverts irrevocably to the debtor.

## Claims against the OR

On FRP taking the case, we investigated the possibility of bringing a claim against the OR in negligence. The leading authority on the liability of the OR is *Mond* v. *Hyde*.[2] In that case, the Court of Appeal found that the OR enjoys immunity from suit for reasons of public policy in respect of statements made by him in the course of a bankruptcy (and the court would no doubt have reached the same conclusion about compulsory liquidation).

Beldam LJ gave the only reasoned judgment in *Mond* and the immunity that the court granted appears generous in its scope. In a critical passage, Beldam LJ said:

*'[t]o be afforded immunity from suit… the Official Receiver must be acting in the course of the bankruptcy proceedings and within the scope of his powers and duties…The getting in of the assets of the bankrupt's estate for the purpose of being distributed to the creditors is part of the bankruptcy proceedings…'.*[3]

However, there is older authority than *Mond*, which was not cited either in

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argument or the judgment in the latter case, and which suggests that the scope of the OR's immunity is more limited than the blanket form described by Beldam LJ. In *Re John Tweddle & Company Limited*,[4] the Court of Appeal drew a distinction between:

- the public duties of the OR that are unique to his office and that he is required to perform by statute (principally, reporting to the court); and
- the ordinary duties as liquidator that the OR may conduct because no other liquidator has been appointed.

In the case of the statutory functions that are peculiar to the OR, Falwell LJ found that the OR is performing '*… functions of a judicial character which are cast upon him, not in the liquidation of the company for the benefit of the assets, but primarily… for the protection of the public…*'.[5] His Lordship therefore held that '*… the Official Receiver is acting in a capacity which renders it impossible for any court to visit him with costs any more than it could visit the judge himself…*'.[6]

On the other hand, in relation to those functions that are common to any liquidator – whether the OR or not – Falwell LJ found that there is '*…no reason why [the OR] should not be liable to the ordinary rules which affect the liquidator in respect of costs of applications made in the capacity of liquidator…*'.[7] While the case in point related to a costs liability, the reasoning of Falwell LJ extends to other forms of liability to which a liquidator or trustee might succumb, such as a liability in negligence. The authors' views are that the reasoning in *Re John Tweddle* is correct and that the apparently unqualified statements in *Mond* should be viewed in the context of the earlier authority. According to *stare decisis*, all courts below the Supreme Court ought to be following *Re John Tweddle*, as the earlier Court of Appeal authority, and in preference to *Mond*, should there be any inconsistency between them.

> “A claim against the OR would have to be issued against an individual or individuals working for the Insolvency Service and that would be undesirable for a number of reasons.”

### Liability of BEIS

The possibility of immunity from suit is not the only obstacle for any office-holder contemplating a claim against the OR. The OR's office has no corporate personality, so the reality would be that – absent any ability to fix a government department with responsibility – a claim against the OR would have to be issued against an individual, or individuals, working for the Insolvency Service. Clearly a significant claim against individuals would be undesirable for a number of reasons. The government department with responsibility for the OR is the Department for Business, Energy and Industrial Strategy (BEIS). There are two potential routes for fixing BEIS with liability for the acts and omissions of the OR's office: vicarious and direct liability.

### Vicarious liability

The starting point for considering whether BEIS could be found to be vicariously liable on behalf of the OR is the decision in *Mond*. Having found that the OR enjoyed immunity from suit, Beldam LJ went on to decide that even if the OR had been liable to Mr Mond in negligence, the Department of Trade and Industry (DTI), as it was then, would not have borne responsibility on a vicarious basis. That was because the DTI did not exercise sufficient control over the OR to create a master/servant relationship.

However, *Mond* was a case decided under the Bankruptcy Act 1914 and Beldam LJ's reasoning focuses on the relevant parts of that statute. Notwithstanding this section of the judgment in *Mond* being cited with approval in passing in a later authority,[8] the IA contains certain provisions that go into some detail as to the relationship between » the secretary of state and the OR. Section 399(2) says:

*'The secretary of state may (subject to the approval of the Treasury as to numbers) appoint persons to the office of official receiver and a person appointed to that office:*
- *shall be paid out of money provided by Parliament such salary as the secretary of state may with the concurrence of the Treasury direct,*
- *shall hold office on such other terms and conditions as the secretary of state may with the concurrence of the Treasury direct,*
- *may be removed from office by a direction of the secretary of state.'*

Section 400(1) goes on to say that the secretary of state may confer functions on the OR from time to time and that the OR shall carry out those functions. The above provisions did not appear in the Bankruptcy Act 1914 and – it is submitted – do suggest a master/servant relationship between BEIS and the OR.[9]

> Creditor views on the prospective litigation were not unanimous and evolved with the progress of the case.

### Direct liability

Even if the position remains that BEIS is not liable for the OR on a traditional vicarious basis, a recent authority suggests that there is scope for what was BIS to assume direct liability. In *Sebry* v. *Companies House*,[10] proceedings were brought against Companies House and the Registrar of Companies for losses suffered by the director of a company that became insolvent as a result of a notice of winding-up order being incorrectly filed against it on the public register.

There is reference in the judgment in *Sebry* to argument, having taken place before Edis J concerning whether Companies House should have been sued, because it is an executive agency of BEIS with no separate corporate personality from it. An application was made by Mr Sebry to join what was BIS, but in the event there was no need for the judge to rule on the point, because the registrar accepted that he would be liable if the claim succeeded. The relevant point to take away from this is that an executive agency of BEIS, acting via the Treasury Solicitor, has sought to defend proceedings on the basis that such an agency has no separate legal personality from BEIS. As the Insolvency Service is also an executive agency of BEIS, it would have been difficult in practical terms for either of them to put forward any analysis in the Longmeade matter that was different from that adduced in *Sebry*.

### Case progression

Having conducted the above legal analysis, the writers concluded that there was a respectable case against the OR and BEIS in the Longmeade estate. As there were only nine creditors, it was not difficult to counsel them for opinion. Creditor views on the prospective litigation were not unanimous and evolved with the progress of the case. However, the very significant majority were ultimately opposed to litigation being pursued against the OR and BEIS for a variety of reasons.

HMRC's final position was that it '… *would not want to support litigation against another government department…*'. The inter-company creditors controlled by LBHI adopted a position that was described by Snowden J as one of '… *unremitting opposition…*' to the prospective litigation. They provided a selection of reasons for opposition throughout various discussions, such as concern over the merits and potential costs to the estate of the litigation, the impact on a programme of estate closure in respect of certain Lehman entities and a possible risk of bad publicity, arising from a perception of the claim being an insolvent US bank suing a UK government department. The remaining creditors' views were divergent and in one or two cases, not absolutely clear.

As the discourse with creditors continued, two material points changed. The first was that section 167 IA was modified from 26 May 2015, so that it is no longer necessary for liquidators in a compulsory winding-up to obtain committee or court sanction before proceeding with litigation. The second point was that a commercial litigation funder – Manolete Partners – offered the liquidators all-encompassing funding for the proposed claim against the OR and BEIS,[11] which meant that there was no risk to the estate and its creditors of the claim proving unsuccessful.

Notwithstanding the two material points described above, a near unanimous percentage of creditors remained opposed to litigation, with one group confirming that if the liquidators pursued the litigation, they would '… *have to consider what remedies are available to them…*'.

### Application for directions

Given the unusual circumstances, the liquidators elected to apply to court for directions. In delivering his judgment on the liquidators' application, Snowden J applied the law as it has always stood in relation to decisions of liquidators which do not require any form of sanction: the court will not interfere unless the liquidator is acting in bad faith or the decision is one that no reasonable liquidator could take. The judge went on to elaborate and said this:

*'(ii) in taking [a] decision, the liquidators should act in what they believe to be the best interests of the insolvent company and all those who have an interest in its estate;*

*(iii) the liquidators may, but are not obliged to, consult the creditors (or contributories) who have an interest in the estate;*

*(iv) the liquidators should normally give weight to the reasoned views of the majority of such creditors (or contributories), provided that they are uninfluenced by extraneous considerations;*

*(v) if all those who are interested in the insolvent estate are fully informed and are unanimously of the same view, the liquidators should ordinarily give effect to their wishes…'.*[12]

> Given the unusual circumstances, the liquidators elected to apply to court for directions.

In the instant case, Snowden J found that the views of most of the creditors could be excluded from the liquidators' deliberations, because those views were influenced by extraneous considerations, rather than considerations that related to the position of each creditor in the Longmeade estate. So, for example, HMRC's opposition to litigation was understandable, but did not relate to its position as a creditor: it related to HMRC's perfectly rational reluctance to endorse a process that might result in one pocket of the public purse paying out damages, with only part of that payment being received into the account of HMRC.

Snowden J indicated that to prevent the litigation being brought, unanimity among the creditors was required. The judge made clear that if *any* creditors were either in favour or simply neutral, it was up to the liquidators to make a commercial decision in the interests of the creditors as a whole whether to commence the claim. This was so even if the favourable or neutral creditors were only creditors for 'comparatively small amounts'. By the time that the hearing before Snowden J took place, the only Longmeade creditors that were not known to be expressly opposed to the litigation amounted to less than one per cent of the total creditor claims. Nonetheless, the judge concluded that (subject to the below) it was open to the liquidators to proceed with the claim against the OR and BEIS and that a decision to pursue the claim at no risk to the insolvent estate (with funding from Manolete) would be within the range of decisions that a reasonable liquidator could take.

### Did the claim proceed?

The reader might think that following the judgment of Snowden J the liquidators are now pursuing a claim against the OR and BEIS; in fact the claims will not be pursued.

Towards the end of his judgment, Snowden J directed the liquidators to give those creditors, whose attitude towards the prospective litigation remained unclear or not explained, a final opportunity to clarify their wishes. The result of this direction was that the proofs were assigned to LBHI and at that point all of the relevant minority creditors were opposed to the litigation. This meant that the litigation could not proceed, pursuant to the guidance of Snowden J at (v) above.

### The continuing role of creditors

It could be suggested that there is a tension in Snowden J's judgment between a liquidator having no obligation to consult with creditors to find out their views, yet simultaneously having to abide by their wishes if they are unanimously opposed to bringing litigation. It is submitted that the absence of any obligation to consult takes precedence here. The facts of the *Longmeade* case were unusual: there were only a few creditors and all of them (other than HMRC) were under the control of various office-holders. Accordingly, it was a comparatively straightforward exercise to find out their views. But in many estates, it will be an onerous task even to attempt to canvas creditor views, and frequently there will be no likelihood of 100 per cent of the creditors expressing a unanimous view, especially in opposition to the bringing of a valuable claim.

### Different tests for different office-holders?

As noted above, Snowden J applied the long-standing test for decisions of liquidators that do not require sanction. The test is often referred to as being a test of perversity. This is a welcome decision for

> **In many estates, it will be an onerous task even to attempt to canvas creditor views.**

liquidators, because it means that there is a single, clear, test giving a wide ambit of discretion.

It should be noted, however, that a different test has been applied in the case of an application against an administrator pursuant to paragraph 74 of schedule B1 to the IA. In *Re London & Westcountry Estates Ltd; Hockin* v. *Marsden*,[13] Mr Nicholas Le Poidevin QC (sitting as a deputy High Court judge) heard an application from a creditor seeking an order requiring some administrators to assign to the applicant creditor a claim vested in the company in administration, which the administrators had decided not to pursue. The deputy judge rejected a submission by the administrators that the court should only interfere with the administrators' decision not to pursue the claims if the decision were perverse. While the deputy judge acknowledged that it might be 'sensible' to have a single test applicable to all office-holders, this was precluded by the wording of paragraph 74. Instead, the test was whether 'unfair harm' had been caused to

> **Office-holders should bear in mind the general position that applications for directions should be kept to a minimum.**

the applicant's interests, which is a significantly easier hurdle for an applicant to surmount.

The decision of Mr Le Poidevin QC's decision appears to have been reached entirely by reason of the specific wording of paragraph 74, under which only creditors or members may apply. It is submitted that where office-holders reach decisions in the exercise of their discretion, the 'perversity' test will apply in all cases *unless* there is a specific control mechanism (such as paragraph 74 of schedule B1) with an expressly different wording.

### A reminder that the court is not a bomb shelter

Snowden J considered that it had been appropriate for the liquidators of Longmeade to seek reassurance from the court in light of the highly unusual circumstances of the case. Office-holders should bear in mind, however, the general position that applications for directions should be kept to a minimum. This principle was most vividly articulated by Neuberger J (as he then was) in *Re T & D Industries plc*.[14] Neuberger J emphasised that *'a person appointed to act as an administrator may be called upon to make important and urgent decisions. He has a responsible and potentially demanding role. Commercial and administrative decisions are for him, and the court is not there to act as a sort of bomb shelter for him.'*[15]

A recent example of an office-holder receiving criticism from the court for making a 'wholly misconceived' application that 'ought not to have been brought' can be found in *Re Chinn (in bankruptcy)*.[16] A trustee in bankruptcy applied to the court for directions on whether to admit, in whole or in part, a proof of debt lodged in the bankruptcy estate. The trustee was in a difficult position, because if he admitted the proof he was exposed to a hostile application by the bankrupt, whereas if he rejected it, he faced a similar application to impugn his decision by the would-be creditor. Despite these challenging features, Registrar Barber considered that such applications should be 'strongly discouraged', for they represented the 'wholesale abnegation' by the office-holder of his responsibility. It was part of an office-holder's role, the registrar held, to make hard decisions. Accordingly, office-holders should think carefully before seeking directions from the court on a matter within the ambit of their discretion. Happily, Snowden J's judgment in *Longmeade* re-emphasises, and arguably expands further, the wide extent of that discretion. ◻

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1. [2016] EWHC 356 (Ch), [2016] Bus LR 506, [2016] BPIR 666.
2. [1999] QB 1097.
3. [1999] QB 1096, 1115H-1116B.
4. [1910] 2 KB 697.
5. [1910] 2 KB 697, 707.
6. [1910] 2 KB 697, 706.
7. [1910] 2 KB 697, 706.
8. In *Re Minotaur Data Systems Ltd* [1999] 1 WLR 1129.
9. If the above analysis is not correct, it is noted that the member of staff from the OR's office who neglected to file the forms in Longmeade was not an OR or deputy but an examiner. This means that he did not hold the statutory office necessary to bring himself within the special position referred to in *Re Minotaur Data Systems Ltd* (see footnote 4 above).
10. [2016] 1 WLR 2499.
11. The funding would have covered all of the liquidators own remuneration, legal costs (both own and adverse) and other disbursements.
12. [2016] Bus LR 506, 519G-520A.
13. [2014] Bus LR 441.
14. [2000] 1 WLR 646.
15. [2000] 1 WLR 646, 657F-G.
16. [2016] BPIR 346, para. [30].

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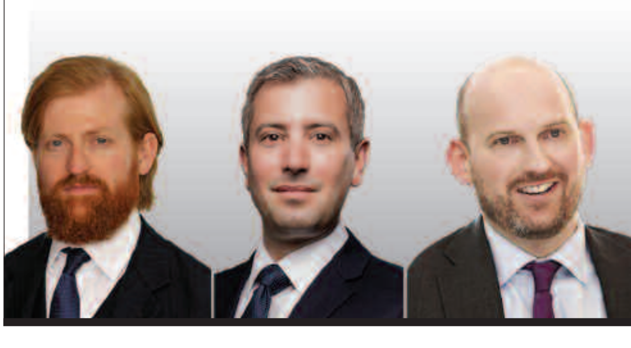

**JOSEPH CURL** (left) is a barrister at 9 Stone Buildings.

**PAUL ALLEN** (middle) is a partner at FRP Advisory LLP.

**ANDREW FOSTER** (right) is a partner at Clyde & Co LLP.

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**Contact Us**

Mark Sanderson, Managing Director
T: +44(0)7771 678571
E: Mark.Sanderson@willistowerswatson.com

Samantha Taylor, Deputy Managing Director
T: +44(0)7956 661162
E: Samantha.Taylor@willistowerswatson.com

Damien Frost, Sales Director
T: +44(0)7342 089761
E: Damien.Frost@willistowerswatson.com

Sadie Easdown, Client Service Director – North, Scotland & NI
T: +44(0)7943 825923
E: Sadie.Easdown@willistowerswatson.com

Andrew McIntosh, Client Service Director – South & Midlands
T: +44(0)7944 918542
E: Andrew.Mcintosh@willistowerswatson.com

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# Insolvency Express

## A technology revolution?

**Adrian Cohen** and **Giles Allison** look at the revolution sweeping the English insolvency courts.

Revolution is afoot in the British courts. Barely a week passes without the announcement of another new pilot scheme or initiative to speed up court procedure, or a speech by a senior judge on how to address the problem of the increasing cost of delivering justice. In July Lord Justice Briggs published the final report of his Civil Courts Structure Review, which was set up a year ago to consider judicial processes and the courts' ongoing modernisation programme. This article will consider aspects of that programme, and how technology is changing the way the courts function, and also some of Lord Justice Briggs' recommendations.

### The start of a revolution

Several different concerns are driving this programme of rapid change, and both external and internal factors have relevance. The key external factor is the government's aim to safeguard the English courts' status as the pre-eminent centre for global dispute resolution. The reliability of English law, the skill and integrity of our judges and the infrastructure provided by London's army of lawyers and other relevant professionals has maintained the English courts' position as a global hub of international litigation. But internal factors such as the cost of legal proceedings (particularly in respect of disclosure of documents), the extensive paperwork required and the length of time it can take for cases to reach a conclusion are chipping away at that position. Newer, smarter, courts around the world are now open for business and are tempting parties away from the English courts to their facilities.

> "The challenge for the UK is for its courts to remain competitive and that requires modernisation especially given the decision on the EU referendum in June."

In January 2015 Singapore's International Commercial Court was officially launched and four years earlier the Dubai International Finance Centre Courts began hearing international cases. The challenge for the UK is for its courts to remain competitive and that requires modernisation especially given the decision on the EU referendum in June. The pre-eminence of the English court will no doubt come under pressure as the terms of the exit from Europe are negotiated.

### The financial list

The physical manifestation of the modernisation of the London courts is the Rolls Building in New Fetter Lane. It provides larger courts including three 'super courts' to host multi-party disputes. Most insolvency work is now dealt with at the Rolls Building. It is also home to the new 'financial list', which was activated in October 2015. This is not a new branch or division of the courts but provides a new track for complex financial transactions, which can be heard by a group of judges who have relevant knowledge of the financial markets. The guide to the financial list states that insolvency cases» and schemes of arrangement will not normally fall within the list, but could do if the issues arising in such cases require financial market expertise or are of general market importance. If the use of schemes by financial institutions becomes more common, for example to deal with capital adequacy difficulties as was the case with the scheme involving Russian Standard Bank last year, it is possible that insolvency cases might benefit from the experience provided by the judges on the financial list.

### The Jackson reforms

The Jackson reforms of 2013 kick-started the process of procedural reform by introducing new requirements on parties to provide costs budgets and more scope for the court to adopt a stricter approach to case management and disclosure. Despite the hard fought extension to the insolvency exemption to the Jackson reforms (as a result of R3's lobbying), insolvency cases have, since April this year, been included within the scope of the reforms, which means that a success fee payable to lawyers under a conditional fee agreement and a premium payable in respect of after-the-event insurance will not be recoverable from the losing side in litigation pursuant to an adverse costs order. The requirement on litigants to prepare and file detailed costs budgets will also now apply to actions brought by office-holders by means of a Part 7 claim form (most types of debt recovery but not 'personal' causes of action such as challenges to antecedent transactions). While there are clear benefits to office-holders in being provided with budgets that are difficult to then amend (as court permission is required), the application of the Jackson reforms to insolvency litigation does add a layer of administrative work that ultimately increases costs and may well deter office-holders from commencing litigation and therefore reduce the potential recoveries for creditors.

### Pilot schemes

It is therefore to be welcomed that the courts' drive for greater efficiency and more streamlined processes has led to the introduction of several pilot schemes that effectively dis-apply the more onerous requirements of the Jackson reforms. The Shorter Trial Scheme and the Flexible Trial Scheme have both been running since October 2015. These pilots are intended to cover commercial cases that do not require extensive disclosure, witness or expert evidence. The pilots place limits on the length of pleadings, limit the granting of time extensions for compliance with court orders and apply a much stricter approach to disclosure (for example allowing parties to disclose only those documents on which they rely and those specifically requested by their opponents, which is likely to much reduce the chance of disclosure producing a 'smoking gun'). The Jackson reforms' costs management provisions do not apply

in these pilot schemes, which no doubt will incentivise parties to opt in to them. Instead, the judge will summarily assess costs after the trial. Interim applications are to be dealt with on paper or by telephone, which is a welcome and cost-effective innovation. Cases will be managed and tried by assigned judges to ensure greater continuity and efficiency.

> "The Insolvency Express Trials pilot addresses a perceived need for faster and cheaper trials and it also relieves the parties and the courts of costs management, as brought in by the Jackson Reforms."

### Insolvency Express Trials pilot

There is a pilot scheme specifically designed for insolvency cases – the Insolvency Express Trials pilot ('IET'). This started on 1 April 2016 and will operate for two years. The IET is intended to provide a streamlined procedure leading to an early determination of more straightforward applications in the Bankruptcy and Companies Courts. It addresses a perceived need for faster and cheaper trials and it also relieves the parties and the courts of costs management, as brought in by the Jackson reforms. An applicant can elect for the application to be subject to the IET scheme, although respondents can object, subject to the determination of the court, which can rule that a case is not suitable for the IET list. An example suggested by Chief Registrar Baister would be if the court suspected that an aggressive claimant was trying to rush a case through at a pace that the defendant could not keep up with.

The guidance for the scheme is set out in the civil procedure rules, at the new practice direction 51P. The scheme can be used for cases that:

- can be disposed of in no more than two days;
- require limited directions (so, for example, nothing extensive in terms of disclosure of documents or where no expert evidence is required); and
- where the costs of each party will not exceed £75,000 (excluding VAT and court fees).

Proceedings are commenced by an application notice with evidence in support, but with the notice marked as being for the IET list. The court will immediately set a date for a directions hearing, which will be no more than 45 days from the date of issue with a time estimate of 30 minutes. If the respondent objects to the use of the IET list it must file evidence of its objections no later than 14 working days before the directions hearing. At that directions hearing, the registrar will set down a timetable and list the trial for a final hearing between three and six months later. That trial date cannot be changed by

consent of the parties and an adjournment will only be granted in exceptional circumstances. The aim is for judgment to be given at the end of the trial; if judgment is reserved it should be given within four weeks of the end of the trial.

So office-holders now have routes they can use for less complex cases that relieve them of some of the burdens of standard commercial litigation. As yet there is little guidance on what work the registrars expect to be dealt with in the IET, but the scheme may be suitable for matters like an application pursuant to section 234 of the Insolvency Act for delivery up of the company's property by a third party, the rescission of winding-up orders or clear cases of misfeasance.

### Transfers to county court

A further insolvency-specific measure is the transfer of insolvency proceedings from the High Court to a specified county court hearing centre (pursuant to an amendment to rule 7.11(3) of the Insolvency Rules 1986). Applications are still issued and commenced in the High Court, but consideration will be given to whether those proceedings can be better dealt with by the county court. This is to alleviate the heavy workloads of the registrars and so ensure that applications are dealt with more quickly. The types of work that will be transferred to the county court are:

- private examinations ordered under section 236 of the Insolvency Act, or under section 366 (being the bankruptcy equivalent);
- applications to extend the term of office of administrators and;
- applications to disqualify a director.

Certain types of application must now be issued in the county court, for example an application for the restoration of a company to the register.

### A paperless route to justice?

Another important technological innovation is the introduction of electronic filing of court documents. This went live across all courts in the Rolls Building in November 2015. Its application to insolvency cases was delayed, but is now operative. Claims commenced after that date in the Chancery Division no longer have a paper court file, only an electronic one. Registered users can process documents onto the system and also access the e-file at any time of day to see what documents the other side has filed. One immediate benefit is that the deadline for filing a document on a particular day is no longer 4.30 pm, which is when the paper counters at the courts close, but 11.59 pm (assuming the relevant court order containing the obligation makes no reference to 4.30 pm). Unfortunately, as at the time of writing, this benefit is not available for insolvency proceedings – documents have to be physically provided to the court, and the court staff will then upload those documents to the e-files. The court now no longer accepts physical delivery of large witness statement and exhibits – they have to be emailed to the court as that helps the uploading process. Chief Registrar Baister has issued guidance on how e-filing should work with bankruptcy and insolvency cases. In the majority of routine cases it is expected that the court will rely on the electronic file only and not require a paper bundle. However, a paper bundle is likely to be required in cases where (i) the documentation the court needs to read is 30 pages or more, or (ii) the application is listed for more than 30 minutes.

“Chief Registrar Baister has issued guidance on how e-filing should work with bankruptcy and insolvency cases. In the majority of routine cases it is expected that the court will rely on the electronic file only and not require a paper bundle.”

### The future

So the courts are changing. Further initiatives to increase diversity on the bench and recruit judges from non-traditional (and non-barrister) backgrounds mean that the judiciary itself is changing too. Judges fresh out of law school and computers preparing lists of issues would transform how justice is delivered in the English courts. Of course the use of technology and the cutting of procedural corners are only means to an end and ultimately cases still need to be adjudicated upon. But these efforts to modernise the courts and their procedures are to be welcomed and seek to bring the courts into the 21st century. □

**ADRIAN COHEN** (left) is a partner in the restructuring and insolvency group at Clifford Chance.

**GILES ALLISON** (right) is a senior associate in the restructuring and insolvency group at Clifford Chance.

▶ **LEGAL VOICE** The nature of the advice given is general and neither *RECOVERY* nor the writer is responsible for any consequential loss arising in connection with information given in this publication.

# Legal Q&A

## Determining expenses and remuneration priorities.

**Q I am the administrator of a packaging company. I appointed a firm of valuers to provide a report on part of the business. The valuers have produced their report and are seeking payment under the contract. However, I am now unsure whether there are sufficient funds in the estate to pay their fees. Who has to pay?**

A The first thing to check is whether the valuers were engaged by the company or by you personally. As an administrator, you are the company's agent and, generally, are not personally liable for contracts made by the company in the course of its administration. Check the contract to see whether there are any clauses about whether you or the company are liable for the valuers' fees.

Assuming the company is liable, it will be important to determine the priority attaching to the fees. It is likely that the valuers' fees will have a 'super-priority' over a number of other expenses of the administration under paragraph 99(4) of schedule B1 of the Insolvency Act 1986. Paragraph 99(4) gives priority to 'any amount payable in respect of a debt or liability arising out of a contract entered into by the administrator'. This means that the valuers' fees will be payable in priority to 'the administrator's remuneration and expenses' (which are those expenses listed in rule 2.67 of the insolvency rules 1986). Note that rules 2.67(2) and (3) allow the court to re-order the priorities in rule 2.67 where the company has insufficient assets; however, it cannot amend the paragraph 99(4) priority which will likely apply to the valuers' fees.

> "The safest approach is to refuse to pay expenses where you are unsure, or seek the court's permission before making payment."

Usually, expenses incurred by an administrator can be paid during the course of the administration. However, as you are concerned about insufficient funds, you should be careful making any payments. If you continue making payments, there is a risk that you may end up with insufficient funds to pay expense claims of equal or greater priority. At the least, you should ensure that you can also pay any other 'debts or liabilities arising out of a contract entered into by the administrator', which would rank equally to the valuers' fees. The safest approach is to refuse to pay expenses where you are unsure, or seek the court's permission before making payment. Of course, the valuers' might also decide to apply to the court for payment.

There is also a risk that, where the assets of the company in administration are insufficient to meet the expenses of the administration, an administrator may face liability for a breach of his duty to creditors or misfeasance. In practice, it is very rare for this to arise. Under paragraph 74(1)(a) of schedule B1, a creditor or member of the company may apply to court claiming that the administrator has acted to unfairly to harm his interests. Alternatively, a creditor or member may allege that incurring expenses that the company cannot pay amounts to misfeasance under paragraph 75. The court will examine the administrator's conduct and may order him to contribute a sum to the company's property by way of compensation. This means you might end up having to contribute to the company due to the valuers' fees.

> Failing to meet a statutory deadline is a serious breach of the rules and in your case the court will carefully consider whether there was a good reason for this breach.

**Q I was appointed the administrator of a property investment company in September 2015. I published progress reports on 15 March 2016 (first report) and on 15 September 2016 (second report) with details of my remuneration and the expenses I incurred in the period covered by each report. On 30 September 2016, a creditor issued an application challenging the remuneration and expenses for both periods on the ground that they are excessive. Given it is more than six months since the date of my first report, is the creditor time barred from challenging the remuneration and expenses incurred in this period? How will the outcome of this application affect my future remuneration and expenses?**

A An application of this nature must be made no later than eight weeks after receipt by the creditor of the progress report in which you first reported the charging of the remuneration/expenses in question (rule 2.109(1B) of the IA 1986). Administration provides a short-term moratorium protecting the company against enforcement by creditors with an objective of rescuing the company as a going concern. In order to pursue this purpose, administrators need to know the financial position of the company, and the process of determining the quantum of remuneration and expenses needs to be resolved quickly. The policy behind the time limit is to achieve certainty as to the company's liability in this respect, subject to the limited right of challenge.

In your case, the creditor's application challenging the remuneration/expenses covered by your first report was made out of time and the challenge in respect of your second report was made in time. This then leads us to the next issue: can time be extended?

In principle, the answer is yes. The court has discretion to apply its general powers of case management so as to extend time for compliance with anything required to be done by the rules of the IA 1986 (rule 12A.55(2)). Therefore the eight-week time limit is not absolute and can be departed from depending on the facts in your particular case.

In *Re Calibre Solicitors Ltd (in administration)* [2015] BPIR 435 the court did allow an extension of time on the basis that a separate application to challenge the administrators' remuneration and expenses in respect of an earlier progress report had already been issued in time. The grounds of challenge were the same in both applications and it was decided that allowing a second application was unlikely to materially delay the resolution of the amount of the office-holder's remuneration and expenses.

That is not to say that an extension of time will always be granted where there is a separate application afoot which was issued in time. The creditor in *Re Calibre Solicitors Ltd* always intended to challenge the remuneration and expenses in the second progress report; however, it was wrongly assumed that the amounts charged in the second report could be challenged as part of its first application. The key distinction in your case is that the creditor is seeking an extension in respect of an *earlier*

> It should not be assumed that because remuneration/expenses in one progress report are challenged, the remuneration/expenses in later progress reports will also be challengeable.

progress report. Failing to meet a statutory deadline is a serious breach of the rules and in your case the court will carefully consider whether there was a good reason for this breach in deciding whether to grant an extension.

As regards your future remuneration and expenses, it should not be assumed that because remuneration/expenses in one progress report are challenged, the remuneration/expenses in later progress reports will also be challengeable. A separate application is required in respect of each progress report and the amounts claimed in later periods will need to be examined separately. However, any reasoning behind the decision of the court in respect of your first or second progress reports, which has the effect of reducing the amount you are allowed to charge, will be applied to the remuneration/expenses you are entitled to charge in later reports. □

**EDWARD GREIG** (left) is an associate at Fladgate LLP.

**PETER REYNOLDS** (right) is an associate at Fladgate LLP.

# Tech turnaround

**John Lowry** provides a unique insight into tech companies in trouble and how technology can aid the turnaround process.

After 20 years working for the great and good of the supply side and the user side of the technology industry, I spent 20 years, as a fellow of the Institute for Turnaround, in the regeneration of distressed technology businesses and businesses that can be transformed by the deployment of new technologies.

My financial literacy has come from management training in global corporations rather than formal qualification, which means that my approach to turnaround is therefore not simply financial but operational. I regard the financial restructuring mechanisms we all use as ways to stabilise businesses and buy time to determine why they became distressed, as well as to develop new operating models to deal with the shortcomings or changed circumstances that brought about their failure. It is the recreation of businesses in a form that will bring about the regeneration of stakeholder value that, for me, constitutes turnaround.

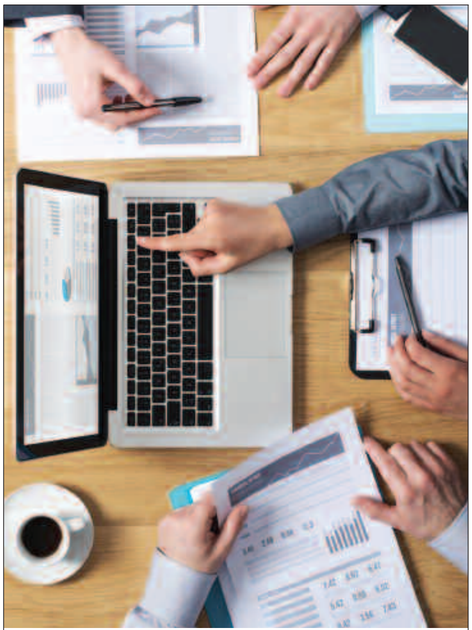
> In the fast-moving world of technology, recreation of the business model in the time bought by financial stabilisation is an exciting challenge.

In the fast-moving world of technology, recreation of the business model in the time bought by financial stabilisation is an exciting challenge.

### Buying time to regenerate

Of the common mechanisms for the financial stabilisation of businesses, some are rarely available to technology businesses and some are very fragile.

Technology businesses tend to grow quickly from humble beginnings and have little in the way of tangible capital assets that can be used in the 'time buying' process. Even companies based in this country, which are engaged in hardware manufacture, have probably outsourced manufacturing to a low-cost economy. If they do own assets abroad, they may be difficult to utilise.



The principal assets are intellectual property (IP), some of which may be well recorded and possibly even patented, but much of which is in the knowhow of key employees who will be in demand and under pressure from competitors to jump ship during unpredictable times. Fortunately the loyalty of employees of tech companies to their company's vision is often very strong. But the assets are intangible and ephemeral in fast-moving, highly competitive markets.

Debt is usually supported by intangible assets and by expectations of rapid growth from new products – the tech bubble syndrome. In times of distress, the faith of debt providers in the vision evaporates quickly and rescheduling of debt, on the promise of jam tomorrow, has a hollow ring.

The hubris of tech companies may often be the cause of their distress and therefore also offer an opportunity for cost reduction by pruning pet projects, eliminating fantasy research and selling trophy acquisitions.

Fortunately, tech companies rarely have pension funds and, if they do, they are newly created ones with relatively sensible structures. There are exceptions where a business has been spun out of a 'traditional' parent. AEA, the privatised arm of the Atomic Energy Authority, had collapsed into losses and a market cap of circa £5m whilst carrying £40m debt and a deficit of £200m (buyout value £500m) on its ex-government pension scheme. Its removal to the Pensions Protection Fund (PPF) was critical to the survival of the business, which we achieved with the loss of only four jobs out of 1,000.

### Recreating the operating model

Technology businesses usually fail for a common set of reasons: dysfunctional organisation as a result of rapid growth from 'techie'-led start up; selling a product but implementing it as a bespoke solution with resulting inappropriate licensing and support fee structure; over-ambitious and over-optimistic development plans; obsolescence through unforeseen platform shifts and disruptive technologies; technology pride – a desire to build components rather than buy tried and tested ones; market hype not matched by product functionality and value proposition; lack of sales management science and over-ambitious forecasts; lack of migration and sunset strategies for products; failure to integrate 'trophy' acquisitions; and, of course, simple lack of financial control of complex activities.

The assets around which a new operating model can be built are usually customer contracts and associated revenues, IP in its broadest sense, patents, people, brand and positioning.

> The hubris of tech companies may often be the cause of their distress and therefore also offer an opportunity for cost reduction.

Quick resolution of the above issues and rebuilding of the operating model is possible, provided you have a good understanding of all the issues. In the short term the most important issues to address are sales process, contract terms, pipeline management and prospect closure. The most critical things to get right as soon as possible are the function of product management, the crystallisation of the detailed product road map and the customer/supplier relationship between product management and product development. Understanding of the product management function is poor in the UK compared to the US, where it is understood to be of paramount

 Editor recovery@r3.org.uk | Recruitment recovery@r3.org.uk/recruitment

importance and is well catered for by a large population of competent product managers. The next thing is the technical architecture of the product and the design and development methodologies.

All this has to be done in parallel with whatever conventional cost reduction, divestment and financial restructuring is possible.

> **My rule of thumb is that if it has taken a technology business *n* months to get into difficulties, it will take *n* months to get out.**

Speed is of the essence. Products lose currency without constant R&D; technology markets reinvent themselves every two to three years; product life cycles in some sectors are down to nine months; technology leapfrogging is ever present – look at the Blackberry story, from world leading mobile device manufacturer to ceasing manufacturing and licensing its software and brand to others in the space of a few years. Transforming visions into products that have USPs, strong value propositions and barriers to entry, as well as repositioning the business in the market is a constant demand.

My rule of thumb is that if it has taken a technology business *n* months to get into difficulties, it will take *n* months to get out. If *n* is greater than 30, think long and hard before you take it on!

### Turnaround of 'non-tech' businesses via tech

Over the last decade most market sectors have been transformed, if not revolutionised, by the deployment of new technology. But there are, of course, companies (even possibly sectors) that have missed the boat. The opportunities for a tech-savvy turnaround director have increased substantially.

When I was appointed executive chairman of one of the UK's largest wholesale and distribution companies, the company had been through two debt restructurings in three years and its equity was underwater. There was overcapacity in its market that was declining by 5 per cent per annum and margins were declining. The products the company distributed were not technology products.

I found a business that had a paper catalogue of 45,000 SKUs that was published six monthly, a 'clunky' website, salesmen taking orders on paper or telephoning them in, three disconnected ERP systems (a legacy of acquisitions), ageing robotics in the warehouses and over 4,000 dealers (customers) of which many of the smaller ones were of doubtful profitability.

The company owned the biggest design studio in the north of England and while it was taking six months to introduce new products via the catalogue (unless interim product additions were issued on paper) Amazon were taking about six minutes to offer a new product on their website.

We developed a new business model and a technology strategy to underpin the business model transformation. We redeveloped the website and introduced a digital catalogue and the concept of virtual stock (in transit from manufacturers). We developed an e-commerce system and a cloud-based stockless business model for dealers. We introduced new CRM and sales pipeline management and forecasting systems. We provided the sales force with tablets giving them direct access to available and virtual stock. We deployed new warehouse automation.

In the first year revenue increased by 7 per cent and EBITDA by 37 per cent. In the following half year (until my exit) revenue was up 9 per cent and EBITDA up 64 per cent on the previous year. This was achieved while continuing significant investment in new technology and processes.

The company won a European Wholesaler of the Year award in both years and made the *Sunday Times* Top Track 250 at number 45. Equity value rose to exceed debt for the first time, we disrupted the market and acquired a major competitor adding 50 per cent to turnover.

### Cybercrime

This perspective would not be complete without a consideration of cybercrime, which is both a potential cause of business failure and a threat to business recovery.

In 2015, 90 per cent of large companies and 74 per cent of SMEs suffered a cyber attack. The total cost to UK businesses was £34bn. 34 per cent of attacks involved loss of IP. A similar number involved loss of customer or business partner information. By 2020 the global cost will be $2.1tn (£1.7tn) and the average cost per attack, $150m (£123m).

Direct costs of this magnitude and the loss of company value associated with loss of IP, customer confidence and business partner confidence, can bring a company down. And there are currently potential fines of up to 4 per cent of global revenues for loss of confidential data.

The days of attack by penetration of technical barriers, cracking of codes and decryption of messages are all but over. Cybercriminals now use sophisticated social engineering techniques on employees: phishing, befriending on social media, personal interaction and networking. Their 'holy grail' is administrator credentials with which they can make an apparently legitimate, undetectable entry to their target company. 75 per cent of attacks now involve employees of the target, mostly unwittingly. On average such penetrations are undetected for 243 days, in which time incalculable damage can be done and business partners may be penetrated too.

Employees' vulnerability to cybercriminals may be increased during a turnaround. They may be on notice of redundancy and disaffected. They may be demoralised and less diligent. They may just be confused and fearful and more vulnerable to being befriended and hoodwinked.

In a turnaround, the would-be cybercriminals are probably increased in number: competitors, business partners, the press, disgruntled shareholders and potential acquirers. Some of these may be state sponsored or ideologically motivated.

> **You can't make a plan after it happens! So one of the first actions on being appointed to recover any distressed business should be examination of the cyber attack recovery plan.**

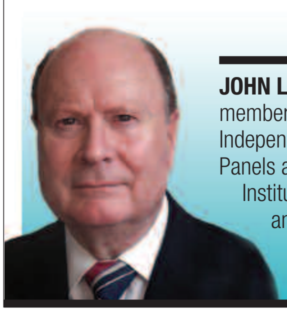
When it happens, the actions taken in the first 48 hours will be critical to the survival of the business. There are many tasks to be undertaken decisively involving technologists, the board, lawyers, shareholders, banks, regulatory authorities, employees, customers, business partners, suppliers, the press and the police.

You can't make a plan after it happens! So one of the first actions on being appointed to recover any distressed business should be examination of the cyber attack recovery plan.

### The future

It's not getting easier; technology life cycles are still shortening; deployment of new technologies is disrupting markets, disintermediating and obsolescing current business models; collaborative remote working is dispersing IP and control of information; cyber threat is increasing.

We live in interesting times for the combination of technology and turnaround.



**JOHN LOWRY** is a member of the PwC Independent Director Panels and a fellow of the Institute for Turnaround and Transformation.


# Notification – you've been served!

**Gemma Kaplan** considers how the courts allow parties to use modern technology and social media to serve court documents on obstructive defendants.

I recently went to see the comedian Seann Walsh perform at the Royal Albert Hall. 'Gone are the days when we used to go round to our friends' houses for a social visit and to catch up through conversation. A greeting would be along the lines of *"hello, how are you, how's the family?"* Now the first thing we ask when we walk through the front door is *"what's your wi-fi password"*.' said Walsh, commenting on modern technology. 'We log on to their wi-fi and check our emails and play games during conversations. You would not have taken your post to open and read at a friend's house or played board games by yourself ten years ago.' As a guilty party, I have to say he is right!

> The average person uses their smart phone for five hours a day, about a third of the time they are awake, and checks it about 85 times.

A recent study by Nottingham Trent University found that the average person uses their smart phone for five hours a day, about a third of the time they are awake, and checks it about 85 times. We live in a world obsessed with social media such as Twitter, Facebook, Instagram and LinkedIn, to name but a few popular sites.

How then has the court adapted to the rise of social media? And how has it allowed parties to use it as a means to serve documents on individuals who might otherwise have evaded personal service or been too difficult to track down? Below I take a look at the original permitted methods of service and then go on to consider recent cases and examples of how the court has allowed social media to play its part. I will refer to claimants and applicants as 'claimants' and defendants and respondents as 'defendants'.

### Service of documents under the Civil Procedure Rules 1998 (CPR)

What do lawyers mean by 'service' of documents? The simplest explanation is to consider 'service' as the steps required by the CPR to bring documents used in court proceedings to a person's attention. The service rules are mainly contained in part 6 of the CPR. Service must be made in a specified way and, if followed correctly, the defendant can suffer penalties and judicial sanction if he or she fails to respond. The claimant's solicitors are expected to serve the documents.

The permitted methods of service for a claim form are set out in CPR 6.3 and for other documents in CPR 6.20. They include personal service, using post, or another document service that provides for delivery on the next business day. You can also leave the document at a specified place and lastly, by using fax or other electronic means (email) where the defendant or his solicitors have confirmed they will accept service by fax or email, and provided the claimant with the relevant fax number and email address. Additionally, a claimant can use any alternative method permitted by court order under CPR 6.15 and 6.27, as long as it can satisfy the court that there 'is a good reason to do so'. It is these under these two rules that applications can be made for service using social media.

CPR rule 6.9 gives further guidance where the defendant has not given his address and applies where personal service or service via a solicitor does not apply. Helpfully it sets out a list of places at which a defendant (individual, corporation or partnership) can be served – generally referred to as the 'usual or last known place of address'.

> The first case in which the High Court considered the use of social media for service was in *Blaney v. Persons Unknown* (October 2009).

Of course, if a defendant has failed to confirm that he can be served by email, a claimant can make an application to the court for an order permitting service to all known email addresses for the defendant. However, you might not know of any such email addresses and the court might still not be satisfied that service has been effected even if you do. What then are the other options available to claimants?

### Examples of the court's willingness to move with the times

There are three publicised cases where English courts have been prepared to allow service via social media. There are also known but unreported cases in the county courts. However, the limited number of examples of this and the specific conditions under which these methods were accepted indicate that these practices are only acceptable as a last resort rather than as an alternative to being used with any regularity.

The first case in which the High Court considered the use of social media for service was in *Blaney* v. *Persons Unknown* (October 2009). The court granted an order for an injunction to be served against an anonymous Twitter user by sending a direct message containing a link to the injunction.

In the *Blaney* case, an unidentifiable Twitter user was impersonating Mr Donal Blaney who ran a right wing blog called 'Blaney's Blarney'. The impersonator used Mr Blaney's name, picture and a link to his blog. Mr Blaney sought an injunction against the Twitter user requiring him to cease his tweeting (in breach of intellectual property rights), preserve the account and password and identify himself. However, he struggled to serve the claim form against the wrongdoer as he did not know the individual's actual identity. The court allowed service via Twitter following an application by Mr Blaney for alternative service under CPR 6.16. In granting the order Mr Justice Lewison highlighted that doing so was owing to the difficulty faced in both locating and identifying the impersonator. Although not reported, the media coverage of the case established that the court was prepared to depart from the traditional methods of service so long as 'there were good reasons for doing so'. The factors the judge took into account in allowing service by Twitter included:

- the regularity with which the defendant used his Twitter account – as the court had to be satisfied the method would bring the injunction to the defendant's attention, and his regular use persuaded the court it would, and
- the ability in being able to monitor on Twitter whether the injunction had been received.

Facebook has also been held to be a permitted method of serving a defendant to English proceedings. In *AKO Capital LLP & another* v. *TFS Derivatives & others* [2012] the court allowed one of the claimants to serve a claim form using Facebook. This was the first time the court had permitted service using that method. The claimants were seeking reimbursement of alleged over-charged commission from their broker, TFS Derivatives. TFS disputed the claim and argued that if they were found liable then they should be able to recover some of the damages from ex-employees of AKO and TFS.

TFS applied under CPR rule 6.15 to serve the claim on one of the ex-employees via Facebook. They brought the application because they could not prove that the employee still lived at the address at which the documents were originally served. The judge approved the application because he was satisfied that TFS had shown that the Facebook account belonged to the relevant defendant by demonstrating that he was 'friends' with a number of other TFS colleagues, and that the account was active and in frequent use by showing that the defendant had accepted 'friend requests' recently.

### Trending post… bankruptcy?

Facebook has also been found to be a permitted method to serve notice of proceedings in a bankruptcy. *Re A Debtor* (No 0274 of 2010) is the first known time that the use of social media to serve proceedings has been allowed in the Bankruptcy Court. In this case, the trustee in bankruptcy had tried to effect both personal and substituted service on the bankrupt to summons him for examination under sections 366 and 367 of the Insolvency Act 1986. The debtor had been elusive and evaded service.

> "*Re A Debtor* (No 0274 of 2010) shows that, if the court is satisfied the respondent is active on the relevant social media account, it will allow both service of proceedings and notification of orders to be sent to respondents and debtors using social media."

Applying the same tests as in *Blaney* and *AKO Capital*, the judge was satisfied that the debtor was a regular user of his Facebook account and therefore granted the order which provided that:

*'by means of an email and/or posting upon the respondent's Facebook account in the following terms: "…TAKE NOTICE that on the 22 October 2014 the court made an order in connection with these proceedings which requires your personal attendance before the Judge at 42–46 London Road, Tunbridge Wells, Kent, TN1 1DP. For further details please telephone the court office on 01892 700150…'*

This is a particularly important step for trustees in bankruptcy dealing with difficult and vexatious bankrupts who fail to cooperate with either the Official Receiver or themselves. It is also useful because it shows that, if the court is satisfied the respondent is active on the relevant social media account, it will allow both service of proceedings and notification of orders to be sent to respondents and debtors using social media.

### Social media service in the foreign courts

Common law jurisdictions, particularly Australia and New Zealand, have shown a greater willingness to allow the use of social media as a mechanism for serving court documents. In addition to using direct messages on Facebook and Twitter, another example saw posting a notice to a user's Facebook page as a means of substituted service.

In the case of *Re the Irish Education Research Institute in Liquidation*, a decision of the Irish High Court in 2014, the court ordered service of proceedings via LinkedIn. The judge made an order providing for papers to be served by sending a message to the defendant detailing the case and attaching a link to the URL containing the papers. The court was satisfied that by using the technical features available on LinkedIn, the liquidator would be able to determine that the message had been delivered and read.

### Take away points

These examples show that the court will be prepared to allow service using social media in circumstances where regular methods of service are unavailable and it is reasonably expected that the alternative method will bring the court documents to the defendant's attention.

The court also takes into account the time and cost that a party would incur in trying to establish the identity and address of an anonymous defendant to be able to serve them under standard methods. In *Blaney*, the claimant would have had to obtain an order against Twitter requiring it to provide registration data. These types of orders are commonly referred to as Norwich Pharmacal orders and are obtained against a third party that has been innocently mixed up in wrongdoing, forcing the disclosure of documents or information. In the event that no meaningful (or false) data had been registered online, it may have been necessary to also seek Norwich Pharmacal relief against the relevant internet service provider.

Although more common, it is not predicted that social media will become a standard method of service any time soon. It is important to remember that it can only be used where the claimant can satisfy the court that the standard permitted methods are not available and that there are 'good reasons' to make an order under CPR rule 6.15 or 6.27. ◻

**GEMMA KAPLAN** is an associate in the restructuring team at Pinsent Masons LLP.

# Futurology in the world of insolvency – threat or opportunity?

**Simon Edel** and **Olivia Lancaster** offer their insights on how technology is shaping the profession.

Technology is a disruptive force that affects almost every industry, from artificial intelligence and robotics, to 3D printing, augmented reality, cloud computing and blockchain. The restructuring industry is no different. Change *is* coming, and it's already begun to impact on our profession!

> Data analytics allow us to capture the data in a user friendly manner and then allow the advisor to apply analytical techniques to the entirety of the data set.

Not only do we need to be familiar with the technology that is disrupting our clients' business models, but we must, as a profession, understand how such technological innovation can influence our own business practices around advising clients and in undertaking insolvency.

### Embracing futurology

Naturally, there are winners and losers with each technological leap. So how do we use technology to our advantage as restructuring advisors and create opportunities, not threats, for our industry?

There are many ways in which technology is changing and enhancing our respective business models and the way that we as a profession deliver our advice – examples include:

### Big data analytics

As a result of the digital age, more data is being produced and recorded than ever before. Big data analytics is a powerful development that blends statistics with easy-to-interpret user interfaces. Increasingly this allows an advisor to identify issues more quickly and identify strategies to impact on business performance.

As restructuring professionals our days of physically searching through volumes of documents and samples of financial information are limited. Data analytics allow us to capture raw system-generated information in a user-friendly manner and then allow the advisor to apply analytical techniques to the entirety of the data set, to form quicker and more definite conclusions on drivers of performance, and how to best influence these drivers in a turnaround situation. One example of this could be identifying specific times/dates where sales decline across a network of business points of sale. Capturing that information would require access to time stamped sales data over a significant period, for example during at least a one year period and all trading locations. That volume of data can now be captured and analysed in a short timeframe by one individual, and graphically illustrated with dynamic functionality.

Key performance indicators, once identified, can even be captured into a smartphone/tablet app – allowing clients and the advisor to pull and update a dashboard of key operating metrics in almost real time to show how the data is uploaded on systems. This may also have an informative impact on the decision to trade a business during insolvency.

> Clients are changing the way they do business and if we want to remain expert advisors to them we must continue to innovate and work creatively.

The decision to trade should be kept under constant review to ensure that creditor interests are being maintained and that a better outcome can be achieved relative to a shut down. With better and more real time data access through big data analytics, the IP will be better positioned to take decisions on specific divisions to stem losses and trade with a view to achieving a sale.

### Artificial intelligence (AI)

The commercial usage of AI is also ever evolving and has received a lot of media attention over recent months, particularly around its adoption by some leading law firms. AI is now sufficiently developed to save legal associate time by analysing hundreds of pages of complex legal documentation every minute, searching for precedent cases, or even helping to draft certain documents.

While some may perceive AI to be a threat to jobs, it can provide firms and individuals with a significant advantage. Highly skilled individuals will now be able to focus more on advisory work, review what the AI tools have provided and have more time for wider casework and clients.

**Bespoke accounting tools**

Corporate groups are increasingly multinational and complex, with business units not neatly mapping to legal entity structures. In a restructuring context is it often necessary to understand the impact of a non-core disposal – which in effect may remove business volume and balance sheet items from a range of legal entities rather

> “The proliferation of digital data has also allowed ‘e-discovery’ tools to be an essential component in building a litigation case.”

than simply being the case of selling the shares of a neatly packaged subsidiary. Tools such as EY’s CarvEx and others allow a group’s accounts to be prepared on a proforma basis quickly and in full compliance with local GAAP or IFRS standards. Proforma carveout accounting can be highly involved and take a lot of time, but with bespoke software programs such proposals can be modelled at pace and give a more informed view to the negotiation.

## Technology v. tradition

Technology will also change the way that insolvency cases are handled. The new insolvency rules even provide that creditor meetings will not need to be held in person and other means will be recognised, which may see creditor meetings in time being run by video conference and other methods. Video conferencing is by no means the end of the benefits of innovation for IPs, and a number of new developments are on the horizon, including:

- *Drone technology* will, and already is, helping to better profile large assets such as properties. Aerial inspection and surveying using remotely operated aerial vehicles can be used to either undertake a close visual inspection or topographic land survey from the air.

- *Online clearing platforms* help facilitate the sale of traditionally harder to realise assets. A good example is its use for intellectual property assets such as patents and domains via online exchanges.
- *Cloud storage* can be used to store key company documentation on insolvency cases and is able to reduce storage costs by almost 30–40 per cent, according to industry experts. The data can also be accessed instantly and create an opportunity for managing ongoing estate costs, potentially increasing the return to creditors.

An increasingly popular topic in insolvency forums currently is the rise of litigation funding. The proliferation of digital data has also allowed ‘e-discovery’ tools to be an essential component in building a litigation case. The ability to conduct file discovery scans of key storage repositories and email servers, thereby creating an inventory of interest from which to identify trends and anomalies, profiling both data and users of interest, is very powerful to assessing the merits of and progressing a litigation.

E-discovery reduces the need for hours of fact finding, working rapidly to locate key words within hard copy evidence to support a case of wrongful trading. E-discovering does not remove the need for an advisor and their team, it enhances the operations of the team to find solutions for their clients expeditiously, at a more favourable cost. This is not just a benefit to litigators due to its ability to capture, map and interrogate data – which has become increasingly important – IPs will also be able to use it for reviewing director conduct and relevant capital events for CDDA purposes.

## What’s next?

Clients are changing the way they do business and if we want to remain expert advisors to them we must continue to innovate and work creatively. We acknowledged at the beginning of this piece that technology can be disruptive. It’s important to get out ahead of this disruption. Embracing technology will inevitably lead to greater efficiencies and will allow us as practitioners to focus on advising with better facts, which can be accessed more quickly, as a consequence of this change.

> “AI is now sufficiently developed to save legal associate time by analysing hundreds of pages of complex legal documentation every minute, searching for precedent cases, or even helping to draft certain documents.”

It’s not always possible to break from tradition without the help of others. Innovation teams can be of great use to understand how technology can be adapted for business use. In London, our firm has established a workspace and cultural venue for thinkers, makers, artists and entrepreneurs. The aim is to help us and our clients navigate and take advantage of disruption, to support innovation and realise the business value of key emerging technologies. We want to be able to disrupt and challenge our own businesses before others do so. The key thing to remember is that embracing technology is not an option – it is a business imperative for both us as IPs and our clients. ◻

**SIMON EDEL** is an executive director at EY.

**OLIVIA LANCASTER** is a senior executive at EY.

# Decoding FinTech and blockchain

With the likelihood that FinTech will disrupt the financial sector, **Henry Page** and **Rachael Ellis** warn that insolvency practitioners will need to adapt to new practices.

Very simply, FinTech can be separated out into its constituent parts – finance and technology; that is to say, the use of technology within financial services and markets. Finance and technology working together is not a revolutionary concept; however, the current focus is the influence that technology is having on the financial sector and the pace of change that results.

The modern FinTech revolution includes: alternative investment platforms such as peer-to-peer lending and crowd funding; robo-advisers providing cheap investment strategies dependent upon user profiles and providing access to algorithmic investment advice; and crypto-currencies such as the Bitcoin, developed with blockchain technology to provide secure transactions.

The common theme with all these products is that they bypass the middle man and instead facilitate transactions through technology.

Inevitably there will be an effect on large swathes of the financial services industry with participants having to adopt new technology, provide something more bespoke to clients than data processing or algorithm based investment advice, or face the prospect of losing clients to cheaper, technology-focused competitors.

The pace of change being forced on the industry – under intense political pressure to create a UK FinTech 'hub' – also presents a significant challenge to both regulators and regulated businesses looking to adopt new technologies and there are critical questions being raised about how you regulate an industry that is likely to have mutated before the ink is dry on new regulations.

> "The common theme with all these products is that they bypass the middle man and instead facilitate transactions through technology."

### Examples of successful examinerships

- We encourage innovation in the interests of consumers
- We promote competition through disruptive innovation – innovation that offers new services to customers and challenges existing business models
- To do this we engage constructively with innovative businesses and seek to remove unnecessary barriers to innovation.

Source: FCA – Project Innovate: next steps (www.fca.org.uk/firms/project-innovate-innovation-hub/next-steps)

### Regulation and FinTech

The FCA's response to the rapid expansion of the FinTech sector has (encouragingly) been to actively engage with FinTech businesses, and in October 2014 the FCA launched Project Innovate, including an innovation hub, advice unit and regulatory sandbox, designed to help innovator businesses navigate their way through the regulatory regime.

Two years on, and no doubt in part thanks to the regulator's forward-thinking approach, the UK has been voted the most FinTech-friendly regime in the world. Clearly underpinning Project Innovate is that FinTech entities providing regulated products or services will need to be authorised by the FCA and comply with the FCA's handbook, a not inconsequential challenge for established entities, let alone new, innovative, evolving businesses.

Taking just the example of loan-based crowdfunding platforms (including peer-to-peer), the innovation hub points users to rules including SYSC (senior management arrangements, systems and controls); COND (threshold conditions); and APER (statements of principle and code of practice for approved persons) to name just three requirements within the FCA handbook. The modification and amendment of an existing regulatory framework provides some guidance to the developing industry but faces significant challenges as innovation outpaces regulation. Forthcoming regulations (such as MiFID II for investment firms and IDD for insurance) are yet to come into force but were drafted before the robo-advice and 'insurtech' booms began.

As FinTech becomes part of everyday consumer life, the FCA will expect firms *demonstrably* to put consumer protection at the heart of their approach. Navigating how consumers are protected and treated fairly; understanding sophisticated technology; and demystifying the regulatory regime for start-ups that may be new to the requirements, is the challenge for the regulator. FinTech propositions offer the opportunity for scalable, low-cost and compliant solutions for retail financial services. The also face the age-old challenge of not becoming mere distribution channels for sales-driven product manufacturers and service providers. Many are waiting for the 'Uber' moment when a non-financial services consumer tech brand takes on the incumbents with a truly revolutionary proposition.

While the FCA is using the innovation hub to bring FinTech products closer to the market through assessing companies, understanding risks and providing feedback prior to regulatory approval, there remains a long way to go. Alongside the innovation hub, the regulatory sandbox provides a 'safe' testing environment, which allows businesses to live-test new, innovative products, services and business models on real customers without incurring all the normal regulatory consequences of engaging in those activities.

> Inevitably there will be an effect on large swathes of the financial services industry with participants having to adopt new technology.

The FCA is currently considering approval for a number of firms including various blockchain applications that could lead the way for UK consumers using products underpinned by the technology behind the Bitcoin.

The success of the FCA's initiatives is yet to be seen but there will inevitably remain a gap between innovation and existing regulation that will provide a tight rope to be navigated by legitimate entities and an opportunity for the less well-intentioned, consumer-centric entrepreneur. Clearly over the coming years, regulation in the FinTech space will result in considerable advisory and investigatory assignments across the restructuring sector.

### A rough guide to the bitcoin blockchain:

1. A set of transactions will be bound together using an algorithm, to form a block, and linked to previously verified blocks already on the chain.
2. Participants within the blockchain known as 'miners' will use their processing power to solve the algorithm and verify the transactions, looking back to previously solved blocks, to authenticate the current block.
3. Once solved the successful miner will broadcast a 'proof of work', which other miners will verify.
4. Once verified the block is chronologically added to the chain and the updated ledger is distributed.
5. The ledger does not show details of the transactions but just a record that the transactions have happened.
6. The encryption of the block through the algorithm is known as hashing.
7. Each block will include a hash to the previous block, linking it to the chain.
8. The miners are incentivised to solve the algorithm and verify the block, in order to gain the reward of the issue of the next bitcoin.

FinTech is certainly having an impact but it is perhaps blockchain technology that may be considered the innovation likely to have the greatest impact, both within the financial sector and beyond. It is also perhaps the least understood.

## What is blockchain and how does it work?

Blockchain is the technology that underpins bitcoin. It is a secure open record of transactions that is distributed to the participants and verified through algorithms and links to previously verified transactions. In other words a secure distributed ledger.

Blockchain and bitcoin work through the verification of sets of transactions by participants within the chain, which cannot be manipulated by any single or group of participants. The verifiers, or miners, are rewarded for confirming a set of transactions, or a block, by the issue of new bitcoins or otherwise benefit from disintermediated transactions.

To use a banking analogy, a block is a bank statement and the blockchain is the record of all bitcoin transactions that have ever happened. In essence the blockchain is simply doing what traditional banks seek to achieve – to keep a secure record of who has what.

As a true blockchain is a decentralised ledger verified by participants, there is no central server or mediator to be attacked by hackers. The programming facilitates the ongoing verification process adjusting the complexity of the algorithms depending on the processing power being used to solve them. Therefore regulating the frequency with which new blocks are added to the chain and protecting against corruption. As soon as a block is verified it cannot be altered.

Clearly the programming behind blockchain is significantly more complicated than can be explained in this article, we haven't for example sought to discuss the detail behind the cryptography, security, or a theoretical 51 per cent attack here.

We would instead like to consider some of the wider implications for distributed ledger databases.

## Additional applications

As well as cryptocurrency, and uses within the financial sector such as removing the need for clearing houses and efficient payment processing, blockchain also has wider implications for non-financial markets.

The technology supporting a distributed ledger could be used for activities as diverse as recording ownership and transfer of property (potentially replacing the Land Registry), smart contracts and verification of ethical supply chains (the end of conflict diamonds?).

> Regulation in the FinTech space will result in considerable advisory and investigatory assignments across the restructuring sector.

Within the next year corporations such as Microsoft and IBM will launch blockchain-as-a-service offerings, which will again extend the use and accessibility of the technology. Separately banks are spending significant resource to harness blockchain applications to facilitate smart settlement systems and reduce the back office cost of trading.

The amount of investment in the technology and the variety of applications to which it can be applied, means blockchain will not go away.

## The effect on the recovery and restructuring profession

FinTech will disrupt the financial sector, causing change for many existing businesses and presenting opportunities for new entrants into the marketplace. As with any changing marketplace there will be a need for restructuring advice as entities grow, face increased competition and try to differentiate themselves. Advising insolvency practitioners will need to ensure that as well as considering restructuring strategies, regulatory obligations (which are unlikely to be straightforward) are properly discharged.

As the use of this technology diversifies away from FinTech, any industry associated with the gathering, recording, processing or verifying of information, is likely to see change and a requirement for professional restructuring advice. □

**HENRY PAGE** is an insolvency practitioner at Mercer & Hole.

**RACHAEL ELLIS** is an associate in RPC's regulatory team.

# Stop worrying and learn to love the future

**Mark Beaumont** writes about the slow-to-adopt approach to technology in dispute resolution, and why that needs to change.

*'Technology is the collection of techniques, skills, methods and processes used in the production of goods or services or in the accomplishment of objectives, such as scientific investigation'.* ***Wikipedia***

The focus on technology in this issue of *RECOVERY* has me considering the human problem with innovation: we are, for the most part, an inherently conservative species.

We've evolved over a long period of time in challenging environments where there are both advantages and potentially high costs to being an early adopter of new technologies. On the one hand, being at the forefront of change can bring real benefits but, on the other hand, adopting an innovative way of doing something could put you in harm's way (or at least make you look foolish!).

> Only when practitioners seek to understand all the options available to them can they weigh up the genuine pros and cons of all.

Innovation is a problem in insolvency dispute resolution because lawyers tend to be more conservative than the average person. New ideas are unlikely to be rapidly adopted by lawyers.

Do you recall the legal communities' attitude towards email in the mid-1990's? I think it's fair to say that the concept was not immediately embraced by solicitors, but as clients became more and more wedded to email, their lawyers had no choice but to eventually catch up.

### New developments

Now we see the same resistance to change when we look at other new developments, such as technology-assisted document review, the use of damages based agreements (DBAs) and utilisation of third-party litigation funding to support claims. Document review has traditionally been a big employer of junior lawyers, but as advances in communications and storage have led to ever larger amounts of data, so technology has offered solutions for managing such volumes. Maintenance of the *status quo* in this area is simply not possible and yet we still see a conservative mind set at work: how quickly are weaknesses in the new technology highlighted, while simultaneously ignoring obvious issues with the traditional model? Change will only come as clients push for more efficient and cost-effective solutions.

DBAs were introduced in 2013 as an innovation in the funding of litigation, but they have not been widely adopted – many lawyers say 'DBAs create a conflict'. This is an attractive argument for lawyers in that it's both true and it justifies a maintenance of the *status quo*. However, the inherent truth of the statement is also what undermines it. Of course DBAs create a conflict, but only because all retainer agreements create a conflict…

A retainer that pays the lawyers for every hour of work they do creates a conflict. Of course, professionalism and integrity mean that lawyers would never drag a case out or do more hours than necessary when paid in this fashion. It seems to me that this professionalism could be extended to DBAs too.

I should just say, there are arguments both for and against DBAs, but I don't buy the conflicts one for one second. Imagine we'd used contingency fees in litigation for the last two hundred years, and then Lord Justice Jackson came along and said: 'instead of aligning the interests of lawyers and their clients, we're going to move to a new system whereby clients pay their lawyers for every hour of work, whether they win, lose or draw'. I can imagine a legal community up in arms over the change. It seems to me that the real objection here is simply an aversion to any new ways of working.

### A legacy of experience

The final area we'll consider is third-party litigation funding. In the last two years we've seen multiple new providers, radical new pricing structures, far more willingness to embrace risk and generally a vast improvement in both speed of delivery and ease of working. Because much of this change has happened in a relatively short space of time, there is a legacy of experience in the market that fails to match the experience of today. This means that insolvency practitioners and their legal advisors are sometimes making choices without knowing the full range of options available to them, to the detriment of all stakeholders. Only when practitioners seek to understand all the options available to them can they weigh up the genuine pros and cons of all, and make fully informed decisions.

> Innovation is a problem in insolvency dispute resolution because lawyers tend to be more conservative than the average person.

I am of course fully aware that new ideas, ways of working and technologies always come with pros and cons. I am not disputing this. I'm simply saying that exactly the same applies to our current practices too.

Take a current hot topic in technology: driverless cars. Conversation quickly turns to 'what if they go wrong?'. That's a perfectly reasonable question, but only if we also look at what goes wrong with cars driven by people: since 1951 the number of people injured or killed on British roads is 18 million. Will driverless cars be perfect? No they won't. But that shouldn't be the question.

Let's not let perfection be the enemy of good. My hope is that the rapid advance of technology in our lifetime is matched by an open-mindedness to consider new choices alongside old choices, not on time served but purely on merit.

**MARK BEAUMONT** is co-founder of Annecto Legal Ltd, an FCA-regulated broker of after-the-event (ATE) legal expenses insurance and non-recourse litigation funding that allows meritorious insolvency claims to be pursued without cost and risk to the IP.

# Talking tax

Advice for IPs on the matter of tax avoidance.

Increasing numbers of companies and individuals are having to settle bills with HM Revenue and Customs (HMRC) because they have participated in tax avoidance schemes. The majority of those who receive tax avoidance bills contact HMRC and settle their affairs in a timely manner. However, HMRC is aware of a minority of individual and corporate users of avoidance schemes who appear able to pay, but are unwilling to do so, and are using insolvency as an exit strategy. It is therefore becoming acutely important for insolvency specialists to look at possible cases more sceptically.

> **If it sounds too good to be true, it almost certainly is.**
>
> **David Richardson, director of the counter-avoidance directorate at HMRC**

It is for this reason that HMRC has been keen to engage with R3 and the insolvency profession to ensure that where HMRC identifies the use of avoidance, it advises the IP of the presence of avoidance debt and of HMRC's interest in the insolvency process whatever it might be. Some avoidance may be disclosed by the office-holders or identified in the annual accounts. Unfortunately there are no hard and fast rules about identifying avoidance to IPs but HMRC is keen to be proactive in its engagement with the profession where it knows avoidance is present.

### Insolvency specialists at HMRC

A priority for HMRC is to ensure that those that can pay do and that insolvency isn't perceived as an easy way out. To mitigate this risk, HMRC insolvency specialists are looking carefully at companies and individuals who declare themselves insolvent where there is avoidance at play, and is challenging these arrangements if it finds assets have been hidden, or transferred before or during proceedings. HMRC specialists aim to support investigations by insolvency office-holders to assist them in recovery actions and bringing claims.

> **We're looking very carefully at instances where individuals or corporates are saying that they are insolvent.**

To support the insolvency profession in their understanding of avoidance liabilities in insolvency, HMRC specialists have been attending regional R3 events. At the recent SPG Forum in November, Paul Winterton and Ian Campbell from HMRC's counter-avoidance insolvency team gave a presentation on some of the common issues that arise in insolvency proceedings where tax avoidance is present.

Building on the SPG event, HMRC specialists and R3 are broadcasting a joint webinar on 7 February 2017 at midday. Entitled, 'An Overview of Tax Avoidance for Insolvency Practitioners', R3 strongly recommends IPs to attend. The webinar is followed by a Q&A with experts from R3 and counter-avoidance. Details on how to register and more information on the event will be circulated in due course.

### Getting out of an avoidance scheme

HMRC is always happy to help the growing number of individuals and companies who want to disentangle themselves from the increasingly fruitless practice of tax avoidance. If you know of someone in an avoidance scheme please encourage them to contact HMRC.

**Email:** exitsteam.counteravoidance@hmrc.gsi.gov.uk
**Phone:** 03000 530 435

### Progress so far

HMRC is having considerable success in tackling avoidance, for instance:

- HMRC wins around 80 per cent of avoidance cases that taxpayers push to litigation and has protected almost £1.6bn in tax since April this year through that litigation; many more scheme users choose to settle their tax bills rather than entering into lengthy and costly litigation.
- The government has strengthened HMRC's powers to tackle avoidance, bringing in a raft of legislative measures such as the introduction of accelerated payment notices. This is a key tool in HMRC's armoury against avoidance. It is a new charge which seeks to change the economics of tax avoidance by requiring those that are in a tax avoidance scheme to pay the tax up front while their case is investigated. This removes their cash flow advantage and puts them back in the same position as the majority of other taxpayers who pay first, dispute later.
- HMRC has issued more than 60,000 accelerated payment notices and collected in excess of £3bn of disputed tax since their introduction in 2014. In addition, HMRC has successfully defended the accelerated payment rules in five out of five judicial review challenges that have been heard in the courts.
- In the last two years HMRC has recovered around £3bn from settling enquiries with avoidance scheme users, in addition to the amount collected under the accelerated payments regime.

### What is tax avoidance?

- Tax avoidance involves bending the rules of the tax system to try to gain a tax advantage that Parliament never intended. It often involves contrived, artificial transactions that serve little or no purpose other than to produce this advantage. It involves trying to operate within the letter, but not the spirit, of the law.
- Most tax avoidance schemes simply do not work, and those who engage in them can find they pay more than the tax they attempted to save once HMRC has successfully challenged them.
- HMRC has new powers to stamp out avoidance and a dedicated directorate focusing on getting people to settle their avoidance schemes. This directorate is using the new powers to considerable effect and getting increasing numbers of avoidance scheme users to the point where they pay up.

**SIMON CHAPLIN** is head of insolvency for the counter-avoidance directorate at HMRC.

# Call the examiner

**Kieran Wallace** explains the court process in Ireland that oversees options to save a business.

Examinership is a process in Ireland where the court provides protection and oversight to a company to allow it, with the assistance of the appointed examiner, to explore all options to save the company's business so that it might thrive into the future.

### The examinership process explained

Examinership commences by way of an *ex parte* application and petition to the court usually by a company's directors or shareholders and, on rare occasions, a creditor. An independent expert's report is submitted along with the petition, which provides an opinion on whether the company is insolvent or likely to be insolvent, has a reasonable prospect of survival and can trade on a cash neutral basis during the examinership process.

In examinership, court protection is granted for an initial period of 70 days (which can be extended by a further 30 days at the court's discretion). During this time creditors (trade creditors, lending institutions, landlords, hire purchase and leasing companies, revenue commissioners etc) are prevented from enforcing debts or guarantees against the company. A liquidator or receiver cannot be appointed to the company. No goods of the company can be seized by creditors. No other proceedings can be taken against the company without the approval of the court.

Under the process, the management of the company remains in control. This provides the company with some breathing space to afford the examiner, working with the company's management, time to assess the company's financial position and to set about drafting a scheme of arrangement with the company's creditors. The scheme must set out the plan for the survival of the company and will likely involve the writing down of debt, staff redundancies, store closures and the disclaiming of onerous leases or contracts etc.

### Examinership success criteria

The scheme of arrangement gives a complete overview of how the company is going to be restructured, including the examiner's proposal on how to save the business. The examiner needs to demonstrate that the company has a reasonable prospect of survival after it exits the process. It is key that the scheme demonstrates to each class of creditor that the outcome of the scheme will lead to a better outcome for creditors than the company being wound up.

The approval of greater than 50 per cent in number and value of creditors of a minimum of one class of creditors is required for a scheme of arrangement to be put to the court for approval.

If, at the conclusion of the process, the court forms the view that the examiner's scheme of arrangement is fair and provides a reasonable basis for the survival of the company, it is approved. Once approved by the court, the scheme becomes binding on all creditors.

### Benefits of examinership

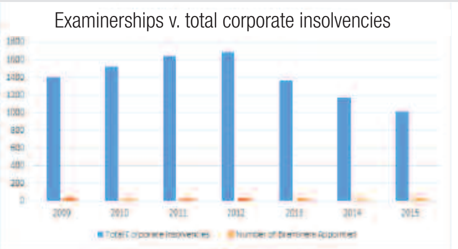
There are benefits to a number of stakeholders of a company. The examinership process is focused on saving viable businesses and the jobs they provide. The process favours consensual 'deals' with classes of creditors.

> "The examiner needs to demonstrate that the company has a reasonable prospect of survival after it exits the process."

- *If successful, the company continues as a going concern during and after examinership*
  Its directors retain control during the examinership period and it continues to trade. Court protection is granted to the company from creditor enforcement actions. The company's management are most familiar with the company and can either provide investment directly or work with a preferred investor to retain control. The company is given the opportunity to retain its customer base and existing contracts with customers/suppliers etc.
- *Repudiation of onerous contracts/leases.*
  A significant benefit of examinership for a company is the ability of the examiner to repudiate contracts, eg onerous leases/supply terms. A number of high profile examinerships have been completed successfully where the main purpose of entering examinership was to renegotiate onerous lease terms, eg upward-only rent reviews, excessive rent terms negotiated during the boom years etc, which is one of the main causes of an insolvent financial position for a company. Renegotiation of these leases with landlords to more favourable/affordable terms puts a company on a stronger footing to continue to trade successfully for the foreseeable future.
- *Restructure of subsidiary's debt by parent company*
  There have been examples of UK parent companies applying for examinership over its Irish subsidiaries to restructure debts/repudiate leases etc. In certain instances parent companies will likely have significant group debt (supply of stock, parent company loans) owed by its subsidiaries, which assists in obtaining the requisite threshold for creditor approval.

  Despite the commitment of a parent company to invest in a scheme of arrangement to restructure a subsidiary's debts, there is the possibility that another investor could come forward with an alternative investment proposal, which could result in the disposal of/loss of control over the subsidiary. The Ladbrokes case was an example of a competitor, Boylesports, wishing to obtain commercial information so it could put forward an alternative scheme of arrangement to the creditors of Ladbrokes. However, Ladbrokes eventually exited examinership and successfully remained under the control of its UK parent.
- *Significant savings for the company*
  As part of the scheme of arrangement, creditors will be expected to write off debt based on the expected return from a liquidation/receivership alternative. It is important that creditors are not unfairly prejudiced by a scheme of arrangement, ie offered a worse return than what they could expect to receive in a liquidation/receivership scenario.
- *Creditors get a higher dividend than in a liquidation scenario*
  Creditors can continue to do business with the company in future, after it exits examinership.
- *Protects employment/saves jobs*
  While some redundancies may result from examinership, the process will result in jobs being saved as opposed to the closure of the business.
- *Court protection from creditor enforcement action*
  There is an automatic stay on creditor enforcement action upon the filing of the application with court on an *ex parte* basis, and assuming there is no secured creditor opposition.
- *Low threshold for creditor approval*
  There is a low threshold for approval of greater than 50 per cent in number and


Editor recovery@r3.org.uk | Recruitment recovery@r3.org.uk/recruitment





**Statistics**
Historically the examinership process has been underused by Irish companies. The graphs demonstrate the consistent low uptake of examinerships by companies comparable with the total number of corporate insolvencies. It was hoped that the introduction of new examinership legislation, making the process more flexible and affordable for smaller companies, would lead to an increase in the number of examinerships, but the impact of the new legislation is yet to be seen.

| | Examinership | Administration |
|---|---|---|
| **Appointment** | • Only by the court after *ex parte* application by the company, its directors or creditors. | • Can be appointed without petitioning the court by a company, its directors or a floating charge holder.<br>• Creditors must petition the court for the appointment of an administrator. |
| **Entry requirements** | • Must be insolvent<br>• Company has a 'reasonable prospect of survival', confirmed by independent expert report | • Must be insolvent |
| **Executive control** | • Remains with the board of directors | • Administrator has full control |
| **Court reporting** | • Frequent as per specific timeframes | • Less frequent – status reports |
| **Length of process** | • <100 days (can be extended with court approval) | • <12 months (can be extended with court approval) |
| **Successful exit** | • Approval from 50 per cent in value and number of a minimum of one class of creditor<br>• Must obtain court approval | • Disposal of business and assets<br>• Approval by way of company voluntary arrangement (75 per cent in value)<br>• No court approval required |

value of creditors of a minimum of one class of creditors. An examiner will attempt to obtain approval from as many classes as possible to ensure a smooth exit and avoid a creditor challenge to the scheme of arrangement.

- *Quick process*
  The maximum 100 day period (extended in certain circumstances) ensures the restructuring of the company's debt in a timely manner. This can also be a disadvantage as 100 days may not be enough in complex examinerships to agree a restructuring of debt.

## Pre-negotiated schemes of arrangement

While pre-negotiated schemes of arrangement can be formed by parent companies who wish to restructure the debts of subsidiaries by applying for examinership, the court has emphasised that no matter what amount of negotiation has taken place before the examinership, it will always be the duty of an examiner to ensure the scheme of arrangement put forward for approval is the best deal available for the company and its creditors.

## 'Examinership lite'

There is a perception that examinership is an expensive court process better suited for large companies, and that it has mostly been high profile, large companies that have entered examinership in recent years.

In December 2013, the legislation was changed to accommodate the examinership process in the Circuit Court, a lower court than is normally used in examinership applications. This has become known as 'examinership lite'. It is hoped that this extension of jurisdiction will encourage insolvent small- and medium-sized companies to utilise the process to save viable businesses burdened by legacy debts.

Smaller companies are allowed to bring their examinership application in to the Circuit Court's jurisdiction if it meets at least two of the following three conditions.

- The company's balance sheet is less than €4.4 million.
- Turnover at the company is less than €8.8 million.
- The company has less than 50 employees.

As this is a recent development in company law, it remains to be seen if the process will prove successful for small to medium-sized companies.

> "An examiner will focus on saving the business and jobs. An administrator considers the survival of the company, the survival of the business and also the return to the company's creditors."

### Examples of successful examinerships

| Entity | Sector |
|---|---|
| Aer Arann (2010) | Airline |
| Four Star Pizza (2010) | Fast food |
| Eircom plc (2012) | Telecommunications |
| B&Q Ireland (2013) | Retail |
| Homebase Ireland (2013) | Retail |
| Pamela Scott (2013) | Retail |
| The Sunday Business Post (2013) | Media |
| SIAC Construction (2014) | Construction |
| Elvery's (2014) | Retail |
| Karen Millen Ireland (2014) | Retail |
| Best Menswear (2015) | Retail |
| Ladbrokes Ireland (2015) | Bookmakers |
| Mothercare Ireland (2015) | Retail |
| Petroceltic (2016) | Oil/gas exploration & production |

## Examinership v. administration – main differences

Examinership and administration are mistakenly considered the same by some. However, there are significant differences between both processes. Both processes aim to rescue insolvent struggling companies but the focus of an examiner and administrator is different.

An examiner will focus on saving the business and jobs. An administrator considers the survival of the company, the survival of the business and also the return to the company's creditors. The differences between both processes are summarised in the table above but a fundamental difference is in relation to the examiner's/administrator's involvement or control of the company during the process.

There is significant oversight by the court in an examinership but no such oversight exists in an administration.

**KIERAN WALLACE** is partner and head of restructuring at KPMG in Dublin, Ireland.

# When the well runs dry

**Alan Meek** and **Sophia Harrison** explore the decline of North Sea oil and the implications for Scottish insolvency.

It will be obvious to all that the North Sea oil industry is in dire straits. To say that oil prices have been 'declining' is putting it mildly – much like suggesting that currency markets have 'shifted a touch' since Brexit.

### The problem at a glance

In stark terms, North Sea oil has been the subject of a significant, sustained and relentless fall in price since September 2014. Last year alone, 43 per cent of the North Sea oil fields operated at a loss, the UK oil and gas sector suffered a 30 per cent drop in revenues and exploration (crucial to finding and maximising production of as much of the UK's oil and gas reserve as possible) is now at an all-time low. The downturn has come earlier and more severely than many expected and this has left the industry itself, and those dependent upon it, with little or no time to prepare or react to this decline.

> "Aberdeen was the most economically productive region in the whole of the UK. So when the downturn arrived, there was bound to be a significant fallout."

### What has been the effect?

To answer this, one need look no further than Aberdeen – a place that has been described as the Monaco of Scotland. That leap of imagination aside, Aberdeen has been a very prosperous city. This is evident from the rows of plush offices, streets full of the kind of cars only insolvency practitioners can afford to buy and ATM machines calibrated to automatically offer a minimum withdrawal of £200. Indeed outside of central London, Aberdeen was the most economically productive region in the whole of the UK. So when the downturn arrived, there was bound to be a significant fallout.

Within the North Sea oil industry itself, low oil prices have caused companies to consider the viability of their assets. Some have determined it necessary to decommission their North Sea operations without delay. Others, who wish to continue operating, are aggressively cutting costs and prioritising cost and cash liquidity to create leaner operating structures. Notably, labour costs are being slashed and capital expenditure deferred. This has meant streamlined administrative structures, seeking blanket price reductions from suppliers, renegotiating logistics contracts, optimising employment terms and arrangements, and a focus on improving invoicing strategies and the retention and collection of cash.

In isolation, most would consider these strategies prudent and sensible business practices in a declining market. Put in context though, they are being employed in an industry historically awash with cash and, in real and practical terms, these strategies have meant the direct and indirect loss of tens of thousands of jobs in Aberdeen. Investment in new oil and gas projects across the UK has also reduced from an annual average of £8bn to just £1bn. North Sea oil tax revenues have also fallen from around £2bn in the 2014/2015 financial year to an estimated £35m in the 2015/2016 financial year.

### Any white knights?

The Scottish government has expressed support for the industry. The Transition Training Fund was launched in February 2016 with a view to helping Scotland retain the considerable and extensive skills and expertise that have been developed here in the oil and gas industry. The Scottish government has provided £7m to innovation projects to help firms reduce the risks associated with research and

**The effects have gone far beyond the oil industry itself:**

- Average house prices in Aberdeen fell by 3 per cent in the year to March 2016. Average rents in the city have also fallen by 15.9 per cent over the past year.
- Mortgage arrears in Aberdeen have increased sharply and there has been a 42 per cent increase since 2010 in the number of Aberdeen mortgages being classified as high risk (ie mortgages where the total amount lent is four and a half times or more the salary of the borrower(s)).
- Hotel occupancy rates in Aberdeen have plummeted to less than 50 per cent. It has been reported that revenue has fallen to a low of £32.89 per available room.
- Local pubs, restaurants and shops have closed.
- The number of start-ups in Aberdeen fell by 16 per cent between the first quarter of 2014 and the first quarter of 2015. The comparable decrease for the whole of Scotland was 9 per cent.
- The recent borrowings of some independent exploration companies are now understood to exceed the entire value of the companies themselves.

development and has committed £1.1m to boost business resilience.

However, such financial assistance is a drop in the ocean of a multi-billion pound industry that is now sinking into decline. While the price of oil might well eventually recover, the consensus appears to be that when it does, the UK oil and gas industry will be nowhere near the size it was prior to September 2014.

> "Any IP who is tempted to dip his toes into the (freezing) waters of Scottish insolvency needs to be aware of the nuances of Scots law, the many differences between it and English law."

## Role of the insolvency profession

Put bluntly, more distressed oil and gas sector businesses will mean more restructurings and formal insolvencies. English insolvency practitioners are permitted to take corporate insolvency appointments in Scotland and may increasingly look to do so given the prevailing economic climate in Scotland's North East. However, any IP who is tempted to dip his toes into the (freezing) waters of Scottish insolvency needs to be aware of the nuances of Scots law, of the many differences between it and English law and that it will always be necessary to take Scottish legal advice throughout any appointment.

### Administrations and liquidations

The structure and appearance of administrations and liquidations in Scotland would be highly recognisable to any English IP. However, these regimes can have a varying degree of court involvement (depending on how they progress). In this regard, Scottish court procedure, which is entirely separate to English court procedure, becomes important, and Scottish legal advice must be obtained to avoid the unwary IP tumbling into any pitfalls.

While the process of going into administration is similar to that in England (either by administration order or by appointment by the holder of a floating charge/the directors or the company), Scotland has its own distinct set of administration appointment forms. Given the hard-line approach taken by courts in these cases it is advisable not to try the court's patience by attempting to file English forms in Scottish courts – it won't go down well.

It is also worth noting that there is no Official Receiver in Scotland.

There are separate Scottish provisions (ss242 and 243 of the Insolvency Act 1986) for challenging gratuitous alienations (transactions at undervalue) and unfair preference. There are also Scottish common law versions of the same remedies. So, again, similar but different.

### Receiverships

Of all the corporate insolvency regimes, receivership is the most different. Scottish receivership reaches a similar outcome to that in England, but by a very different route. Receivership and floating charges in Scotland are both wholly statutory. Like many great things in Scotland (Sir Chris Hoy, Ewan McGregor and First Minister Nicola Sturgeon) they were born in the 1970s. However, since 2003 there has been the same prohibition on the appointment of administrative receivers in Scotland as in England. Accordingly, a receivership will only be competent now in Scotland if:

- it proceeds on a floating charge that pre-dates 15 September 2003;
- it is not a receivership of the whole or substantially the whole of the assets of the company; or
- if one of the exceptions set out in sections 72A-G are applicable (which are the same as those applicable in England).

The law on receiverships is set out in ss50–71 of the Insolvency Act 1986 (and these provisions apply only in Scotland). It should be noted that the Law of Property Act 1925 does not apply in Scotland so there can be no LPA receivers or other fixed charge receivers in Scotland.

### CVAs

The Insolvency Act provisions relating to CVAs apply in Scotland as they do in England.

### And not to be forgotten…

Scottish insolvency law does not consist solely of the Insolvency Act 1986. Underpinning it are volumes of statutory instruments and rules. Importantly, Scotland has its own set of insolvency rules, the Insolvency Rules (Scotland) 1986. These address fundamental practical issues such as:

- distributions to creditors;
- treatment of secured creditors;
- treatment of expenses of the insolvency;
- calling and holding of meetings; and
- IP's remuneration.

Importantly for the English IP, many of these issues have been derived from early Scottish personal bankruptcy principles and so may diverge considerably from their English equivalents.

There are also numerous differences between Scots and English insolvency law beyond even the Act and rules, for example Scottish securities law. Fixed charges and/or equitable charges are not favoured by the Scottish courts. Indeed, anything that purports to create a fixed charge in a manner hitherto unknown to Scots law is likely to be struck down.

The law of diligence (the closest English equivalent might be freezing orders) is important too, and its application to insolvency cases is technical and uniquely Scottish.

An area that has arisen from the dead in the past few years and become relevant again in Scottish insolvencies is the law of hypothec. This is a security right, arising by operation of law, given to a landlord in an insolvency process. The security is over any moveable goods owned by the tenant on

> "It is advisable not to try the court's patience by attempting to file English forms in Scottish courts – it won't go down well."

the premises at the insolvency and the sum secured is the amount of arrears as at the point of insolvency. The hypothec ranks ahead of floating charge creditors and it seems that the banks were often unaware of this when lending. Hypothec needs to be borne in mind in all insolvency processes involving leasehold premises in Scotland.

## What next?

It seems the North Sea oil crisis will increase the work of insolvency professionals in the North East oil and gas industry and in other markets and areas of commerce. Crucially, there are issues in Scottish insolvencies unique to Scotland that cannot be overlooked. However, we have no doubt that the profession – throughout the UK – will rise to the challenges (and opportunities) that the North Sea decline brings.

**ALAN MEEK** is a partner at MacRoberts LLP.

**SOPHIA HARRISON** is an associate at MacRoberts LLP.

# Jumping fences? Recovering debt from Europe

**Jeremy Boyle** looks at two options for debt recovery that should still apply post-Brexit.

The situation is this: it's post-Brexit and you've done some work for a client in Madrid, but you are based in England. Then the client doesn't pay.

How do you recover the sum due to you under your invoice for professional accountancy services provided?

Prior to the regulations referred to below, if a small business or consumer needed to recover money from a debtor in another EU country, such recovery was difficult, time consuming and expensive. Challenges included differences in national or domestic laws, the cost of hiring legal expertise and translating documents.

Accordingly, the European Commission proposed a Europe-wide expedited regime aimed to ease the recovery of cross-border debts for both citizens and businesses.

### Jurisdiction

When dealing with cross-border debt, we always advise clients to ensure that they regularly update their terms of business. For the sake of expediency, one of the main clauses we like to see in agreements reads something along the following lines:

*'This engagement letter is governed by, and construed in accordance with, English law. The courts of England will have exclusive jurisdiction in relation to any claim, dispute or difference, concerning this engagement letter and any matter arising from it.'*

It is likely that post-Brexit the EU member states will still recognise a choice of English law. So it is perhaps of paramount importance that such a clause is inserted into your contracts sooner rather than later.

Presently, there are two useful tools in a creditor's armoury:

### European Enforcement Order (EEO)

The chances are that if you do have such a clause in your terms of business you can secure a judgment in the English court. At the very least it will encourage your debtor to engage with you in the English courts, which will mean that your debtor will probably have to appoint a solicitor to deal with the matter. Who knows, he may decide at that point that it would be more beneficial to pay your invoice rather than hire a lawyer!

If the defendant does not contest the claim or fails to appear in the proceedings after initially objecting to the claim and you obtain a judgment what next?

Member states can enforce 'uncontested' judgments under the European enforcement order regulation. A judgment is considered 'uncontested' if the judgment comes via a consent order approved by a court, or if the defendant either did not contest the claim or failed to appear in the proceedings after initially objecting to the claim. If the EEO regulation applies, a creditor may apply for an EEO certificate from the court where the judgment was entered.

> "It is likely that post-Brexit the EU member states will still recognise a choice of English law."

Once certified, the judgment is automatically enforceable in the court of any other member state as if the judgment had been made in the court of the member state.

***Example***: in 2015 we acted for an English resident in Spain who had secured a judgment in the Spanish courts against another British couple who we discovered had assets in London.

Having registered the Spanish judgment in the High Court in London, we were able to place a charging order over the judgment debtor's London property, which we found through our tracing team. The settlement of the judgment followed swiftly.

### European Payment Order (EPO)

Although a judgment on an 'uncontested' claim may be obtained as detailed above, as of 12 December 2008 use may also be made of the uniform procedure called a European order for payment process.

If a European order for payment is obtained, this order is automatically enforceable once a declaration of enforceability has been made.

An EPO is automatically enforceable in every EU country if it is uncontested by the defendant.

***Example***: by way of example, we act for condominium owners in Portugal who raise management charges against British residents owning second homes in Algarve.

Once we have details of the management charges from our Portuguese clients, we can apply for an EPO in an English county court and, once obtained, the EPO can be enforced like any other English judgment.

This could be via the enforcement officer (formerly known as the sheriff), a third party debt order, attachment of earnings order or by placing a charge over the debtor's home.

### What is the position post-Brexit?

It is unlikely that there will be an immediate change.

The UK's exit from the EU will not take place immediately. The procedure for a member state that withdraws from the EU is set out in Article 50 of the Treaty on European Union. It provides for the UK to negotiate a withdrawal agreement with the EU and for the Treaties to apply to the withdrawing state after two years, unless there is unanimous agreement to extend that period.

**JEREMY BOYLE** is a solicitor and partner at Welbeck Solicitors LLP.

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# Summertime blues

**Colin Hardman** details the complexities behind the demise of another travel group.

The Lowcostholidays Group had grown to become one of the largest sellers of package holidays and hotel accommodation worldwide, with a 500 strong workforce, annual transaction values in the region of £500m and more than three million flights arranged to destinations across the globe each year. Its abrupt collapse this summer left over 27,000 travelling holidaymakers in a panic over whether their hotel and travel arrangements would be honoured and a further 110,000 future holiday bookings at risk of being cancelled. The speed of its demise and the cross-border aspects have raised some interesting issues for the administrators at Smith & Williamson and CMB Partners and also for our legal advisors. A number of these issues could very well have had a very different conclusion in a post-Brexit world outside of the current EU insolvency regulation, if that is the type of world that Brexit will bring.

### Background

Founded in 2004, the group principally focused on selling hotel accommodation (essentially a 'bed bank') through lowcostbeds.com Limited (Beds.com) before progressing also into selling accommodation-only and package holidays through lowcostholidays Limited (Holidays Limited). Its structure morphed over the last decade and was latterly based in Spain, the UK, Switzerland and Poland. Early financial success allowed the group to roll out the business internationally and it made additional acquisitions including a transfer service business (Resorthoppa) and a high-specification software business (Intuitive), the latter being credited with assisting the group in achieving significant growth during that period.

> “Holidays Limited held all the travel agent and tour operator licences, including ATOL.”

Holidays Limited held all the travel agent and tour operator licences, including the Air Travel Organisers' Licence (ATOL). By law, every UK travel company that sells air holidays and flights is required to hold an ATOL licence. If a travel company ceases trading, the ATOL scheme protects customers who have booked holidays with that firm. The scheme is designed to reassure consumers that their money is safe, and will provide assistance in the event of a travel company's failure. Holidays Limited also provided a bond through the Irish Commission for Aviation Regulation (CAR) that enabled customers whose bookings originated in the Republic of Ireland to receive a refund in the event of the company's failure.

In 2012, to improve its liquidity position, the group sold Resorthoppa and Intuitive, which had been profitable and significantly cash generative. The following year, the group made the much publicised and controversial decision to bring its licensing arrangements under one EU licence – that of the Balearics licensing authority, Govern de les Illes Balears (CAIB). Consequently, all existing bookings with Holidays Limited were transferred to a Spanish subsidiary, Lowcostholidays Spain SL (LCH Spain SL). At the time, the Civil Aviation Authority (CAA), which was only given 48 hours' notice of the group's intentions, expressed concerns over the transfer of the licence out of ATOL protection. While the group had notified all customers with forward bookings of the transfer and had offered them a full refund, the CAA considered that the communication was unclear. The group only gave customers seven days' notice to make a decision, as the protection provided was less than that which ATOL could provide to UK customers (who constituted approximately 60 per cent of the group's bookings), despite the fact that notice may have been adhering to EU law.

> “Following the transfer of the group's business abroad to Spain and Switzerland, the group's financial performance deteriorated significantly.”

The Air Travel Insolvency Protection Advisory Committee (ATIPAC), set up by

the secretary of state for transport to support the CAA on situations such as this, voiced its disapproval in its 2013/14 annual report, raising wider concerns that other UK travel companies, particularly those operating at the cheaper end of the market, would follow suit in order to reduce their overhead base — effectively a 'race to the bottom'. The concerns of ATOL and ATIPAC were ultimately proved to be justified.

In 2013, to facilitate the group's expansion plans, a Swiss branch was also set up with the assets and business of Beds.com Ltd transferred to a new Swiss entity, lowcostbeds.com AG (Beds.com AG).

### The group's financial difficulties

Following the transfer of the group's business abroad to Spain and Switzerland, the group's financial performance deteriorated significantly. Some of the reasons given for this include:

- software difficulties;
- shorter credit terms being provided by travel industry suppliers;
- the increasing incidence of lower deposits being offered by (better funded) competitors;
- the deterioration of the group's preferred status across hotel groups, as major competitors offered significantly better (lower) credit terms;
- the increased utilisation by customers of online holiday search facilities at the expense of the more traditional (higher margin) telephone bookings;
- the escalation of terrorist incidents targeting a number of hitherto popular holiday destinations throughout 2016; and
- the Brexit decision in June 2016, which impacted bookings from exchange rate-sensitive customers and spooked investors.

### Appointment of administrators, COMI and the Swiss problem

Following unsuccessful attempts to restructure the business, the directors ultimately made the decision for the group to cease trading, making the majority of the workforce redundant and subsequently appointing me (Colin Hardman), Finbarr O'Connell and Henry Shinners of Smith & Williamson LLP together with Lane Bednash of CMB Partners as administrators over four of the UK group companies on 15 July 2016. However, the majority of customers (and indeed suppliers) had contracted with Spain SL and Beds.com AG.

On 21 July 2016 the High Court, being satisfied that Spain SL's centre of main interest (COMI) was in the UK, rather than Spain, made a UK administration order over that company and appointed the same four administrators as had been appointed in the earlier administrations. Glen Flannery, who led the Nabarro LLP team advising the administrators, commented: 'Making effective use of the European Insolvency Regulation, it was possible to anchor the group's insolvency proceedings in the UK, thereby avoiding the complication and cost of disparate proceedings across a range of jurisdictions. It would be unfortunate for future cases if we were to lose this tool as a result of Brexit.'

> "To date we have received more than 30,000 separate email communications from affected customers."

In preparing the administration order, it was decided that the administrators' objectives, functions and powers, as well as the other effects of the administration, such as the moratorium, should be recited in the administration order, to assist in getting recognition of such matters in Spain.

Glen Flannery commented that: 'This was a practical measure to assist in getting local recognition. We adopted it to useful effect in the Eurodis case and similar has been done in a series of other high-profile cases, including Nortel.'

The Spain SL administration order also included other forms of relief designed to streamline the process and minimise costs in a case with such a large and global consumer and creditor base, in particular, the use of emails for formal communication purposes.

Unfortunately, even though the Swiss registered company, Beds.com AG, also had a strong connection with the UK and could potentially have been placed into an English insolvency process using the European Insolvency Regulation or other means, Swiss law would not have » recognised the English insolvency practitioners. Therefore Beds.com AG entered into Swiss bankruptcy on 25 August 2016.

### Communication strategy

Given that there were over 250,000 customers who were either in the middle of or due to depart on holiday in the days/weeks after the administrators' appointment, it was imperative for support and information to be provided to those affected quickly, including during the hiatus period between the appointments over the UK companies and that of Spain SL, one week later.

An external call centre was set up to assist customers with their bookings and refund enquiries. In the early weeks of the administration we were dealing with thousands of enquiries from affected customers. To date we have received more than 30,000 separate email communications from affected customers.

### Supporting the customer refund process

The majority of customers were found to have valid flights that were booked and paid for but with accommodation and/or transfers unpaid. We recognised early on that a significant proportion of customers had paid all or part of their holidays via their credit or debit cards or through online payment providers and consequently had rights under statute and/or contract for compensation for non-delivered services. Customers were provided with direct access to information on the status of their bookings and also with assistance as regards the various avenues by which an application for reimbursement could be pursued (or by which a claim could be submitted in the administration).

The administrators have been working closely with the UK Card Association (UKCA), the trade body for the card payments industry in the UK representing financial institutions that act as card issuers and acquirers, to support their members in processing customer refunds. The UKCA continues to provide guidance on protections available to consumers who have purchased travel or holiday packages using a debit or credit card, in particular in respect of customers' rights to receive a chargeback for credit and debit card transactions and, for credit card purchases only, entitlement to a refund under Section 75 of the Consumer Credit Act 1974 (Section 75). We have also supported acquirer banks directly, these being the financial institutions that maintain the accounts that process credit and debit card transactions and which, ultimately, are likely to be the principal parties to reimburse customers and thus, through subrogation, become the principle creditors in the administrations.

Through our efforts and those of the UKCA and their members, and the online payment providers, a significant number of customers have already obtained refunds, largely facilitated by applications made to credit card companies under Section 75 and via debit card chargeback schemes. We currently estimate that the cumulative payments made to the group's customers by acquirer banks (and online payment providers) will exceed £125m. From our work on this case to date, it is evident that the credit card industry, with the UKCA at the helm, has developed a joined-up and effective approach to dealing with large-scale retail insolvencies like this one.

> "One complication is how to ensure that customers do not 'double dip' and get compensated for more than they are entitled to."

We have also worked alongside CAR, which held a bond that enabled customers whose booking originated in the Republic of Ireland to receive a refund, which has made substantial progress in processing many of those claims. The situation is very different as regards holidays booked in the UK and other countries. CAIB will only pay out up to the level of the bond held (which only amounts to circa €2m). Consequently, for those not covered by the credit/debit card/online payment providers or holiday insurance, they can expect only a very small recovery under the CAIB scheme and, from our experience on other travel related insolvencies, may unfortunately have to wait years before receiving any payment.

The institutions that provide refunds to customers may ultimately step into the shoes of customers, as creditors, either under the terms of the relevant merchant contracts or by subrogation. For this reason, it is anticipated that there are likely to be relatively few consumers that booked with Spain SL or Beds.com AG, who will remain as creditors.

One complication for those institutions that are liable to pay out to customers is how to ensure that customers do not 'double dip' and get compensated for more than they are entitled to. We are working with a number of these organisations to minimise the risk of this occurring as far as possible.

### Employee-related matters

Under the European Insolvency Regulation, although the law of the main insolvency proceedings governs matters arising in them, there is an exception for employment contracts. The effect of the insolvency proceedings on employment contracts and relationships is governed by the law of the member state applicable to the contract.

There has been extensive focus on employee legal matters, across various jurisdictions, ensuring that group companies were compliant with the various laws and protocols applicable to staff based in the UK, Poland and Spain.

Consequently, the staff in Poland and Spain needed to be dismissed in accordance with Polish and Spanish laws and customs (as applicable). In these jurisdictions the laws and procedures for terminating employment contracts are more onerous than in the UK and there can be adverse consequences if they are not carefully followed, eg ineffective termination of employment contracts, resulting in claims continuing to accrue against the estate and difficulties for employees accessing state guarantees.

Tracey Marsden, employment partner at Nabarro LLP, commented that: 'Cases such as this highlight the tension that can exist between discharge of functions under UK insolvency laws and compliance with local employment laws, particularly in foreign jurisdictions.'

### Conclusions

Lane Bednash has commented, on behalf of the administrators, that, 'The demise of the Lowcostholidays Group shows that whatever legislative safety nets are put in place to protect the public in this historically dangerous sector, potential cost savings will still cause travel companies to take big risks with their customers' travel arrangements. While this business failure did not result in many thousands of customers stranded abroad or at airports, it could have.'

It is clear that Brexit will add even further challenges to the risks involved in booking the ever-popular package holiday. We will all be looking with interest as to whether the cross-border insolvency regime returns to one similar to the pre-2002 landscape. One sobering thought: if the music world were to take a similar leap back in time then we can all look forward to the nauseating beats of the Ketchup Song all over again, and again…

The author would like to thank Lane Bednash, Glen Flannery and Tracey Marsden for their assistance with this article.

**COLIN HARDMAN** is a director and restructuring and recovery specialist at Smith & Williamson LLP.

# The compensation regime

**Vicky Bagnall** writes about the need for collaboration between the Insolvency Service and insolvency practitioners as office-holders.

The compensation regime followed up on the government's intention to make directors who have fallen short of acceptable standards financially accountable to creditors (where their actions have caused loss). The new powers allow the court to make a compensation order (and the secretary of state to accept a compensation undertaking – which has the same force as the order) against a director who has been disqualified following an insolvency. The compensation can then go to creditors who have suffered identifiable losses from the misconduct of that director.

> "The Insolvency Service does not intend to usurp the asset recovery role of IPs."

The proposals were enacted by the Small Business, Enterprise and Employment Act 2015 with sections 15A-15C inserted into the Company Directors Disqualification Act 1986. The provisions came into force on 1 October 2015.

Supporting secondary legislation for England and Wales, governing the practice and procedure of compensation proceedings, came into force in October 2016 and included a provision to enable the secretary of state to combine an application for a disqualification order with an application for a compensation order and to recoup costs for distribution. Scottish rules will be laid down in early 2017.

We have to act reasonably and in the interests of fairness we will tell directors at the time we inform them of our intention to seek a disqualification whether or not we will also be seeking compensation. We intend to take compensation action as soon as is practicable after, or at the same time as, applying for the disqualification.

### The role of the Insolvency Service on behalf of the secretary of state

The compensation regime will support the civil disqualification regime in cases that warrant disqualification action against the director. As with disqualification cases, we have to treat each case on its merits and consider whether:

- the conduct of the director (after 1 October 2015) caused a quantifiable loss to the creditor or a class of creditors;

- the director has made any financial contribution in recompense for his conduct;
- it is financially beneficial to creditors for us to seek compensation against the director (ie does the financial benefit outweigh the cost and legal risk involved?);
- any prosecuting authority is intending to seek a confiscation or compensation order.

Compensation can be paid to the secretary of state for specific creditors or classes or creditors, or as a contribution to the assets of the company.

For compensation orders awarded as an asset of the company, the office-holder will enforce the collection and distribution of the award, as well as our costs in the proceedings. Compensation orders awarded for the benefit of a creditor or class of creditors will be collected and distributed by the Insolvency Service on behalf of the secretary of state.

We should also note that the regime allows that where the director has signed a compensation undertaking he or she can later make an application to court to vary it, either by reducing the amount or providing for it to not have any effect.

### Collaborative working

The Insolvency Service does not intend to usurp the asset recovery role of IPs. Therefore, to enable the effective application of this new regime, a continuous dialogue between us becomes even more important – we certainly don't want to bring proceedings where the IP is already contemplating recoveries for the same misconduct. Close collaboration will assist both of us in making decisions on how to achieve the best result for creditors and avoid the risk of double recovery action at a cost to the liquidation and/or taxpayers. In deciding whether to proceed with a compensation order application we will consider whether:

- the office-holder is taking or considering taking recovery action
- the director made other financial compensation for the misconduct
- the office-holder is aware of the director's ability to pay any compensation

> "A continuous dialogue between us becomes even more important – we certainly don't want to bring proceedings where the IP is already contemplating recoveries for the same misconduct."

- the office-holder is aware of any action taken by the creditor (with powers) to pursue compensation
- there is possible or ongoing criminal action in which the prosecution might seek compensation that would financially benefit the creditors.

So we expect that in many cases, the office-holder will continue, as now, to take recovery action.

The compensation regime will help to ensure that directors are more financially accountable for the consequences of their conduct. In taking this forward we look forward to strengthening our relationship and collaboration with IPs to maximise returns for the benefit of creditors. □

**A summary of the key points of the regime are:**

- the misconduct must have occurred from 1 October 2015;
- the director(s) must be disqualified for a compensation order or undertaking to be effected;
- the loss suffered by the creditor must be attributed to the misconduct and be identifiable;
- a compensation order can be sought up to two years from the disqualification order or undertaking.

**VICKY BAGNALL** is director of investigation and enforcement services at the Insolvency Service.

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# Becoming a new kind of IP

**Alison Byrne** talks through the personal and professional events that have reshaped her practice.

In the Autumn edition of *RECOVERY*, the president of R3, Andrew Tate, outlined his belief that: 'Insolvency practitioners are about much more than just formal insolvency processes'. In his interview he emphasised: '…that R3 stands for rescue, recovery and renewal…'. The recognition of these facts, coupled with a life-changing event, had already set me down the path of investigating ways my practice could adapt to changing economic and social circumstances.

## Formal functions and Fiat 500s

In the early noughties, not a week went past without four or five enquiries resulting in at least one or two formal appointments. Conversely, with the crash in 2008, the market started to become static and by 2011/2012 I had started to notice a marked decrease in enquiries. At that stage I started to investigate where our skills sets could be redeployed or augmented to broaden our services.

At this time the communications team at R3 had done a great deal to improve the perception of IPs and improve understanding of their value and work with MPs, journalists and the general public. Despite this, an underlying guardedness towards insolvency professionals remained. I dreaded the inevitable question at a function or dinner party, *'So Alison, what do you do for a living?'*. Eyes either glazed over as I tried to explain, or people already had a preconceived idea based on the 'equation' that *business failure + insolvency practitioner = negativity*. I'd try to explain that insolvency practitioners are like doctors: they diagnose your problem and may have to give you bad news, but then they try and find the best course of treatment, which often results in survival.

I also found that as a small practice I was dealing with directors who were far more emotionally invested in their businesses. These emotions manifested themselves in their dealings with the IP; they ranged from deep despair and misery to outright aggression as you tried to plot the best route for all involved.

However, it was a 'crash' of a different nature that eventually made me re-evaluate where I wanted to go professionally. In July 2013 I had dropped my son off at school and thought I'd go for a quick run before heading into the office. With my mind on work I ran into the path of an oncoming vehicle. The accident left me with a broken neck, which, it turned out, was a lucky escape. Had the car been anything other than a Fiat 500 the outcome would have been very different. I used the recovery time to look closely at what I enjoyed and knew I had to make some changes.

## Realisation – it's rescue, recovery, renewal

Over the years that I had been running my practice, the greatest pleasure I derived was from turning things around for businesses who appeared to be, or were, in deep trouble. From building to baking, designing to driver recovery, the most rewarding work had been in helping businesses recover from dire situations and go on to thrive. While there was the same emotional investment in dealing with people in distress, I also shared their relief at seeing a path forward and elation in seeing their business, some parts of which were long standing family concerns, flourish. I still get calls from people whose business I rescued with my IP knowledge, but none from people whose businesses I'd had to close – minimising the personal impact, using exactly the same skills.

> "From building to baking, designing to driver recovery, the most rewarding work had been in helping businesses recover."

## Using hands-on skills

From early 2014 onwards, while still acting as an appointment-taking IP, I became more focused on not just advisory procedures for business recovery, but also acting in a much more hands-on manner, either shadowing CEOs and boards or providing services as the acting CEO.

One of the areas in which I have found my IP skills transferrable is the charity sector. There are new challenges in working with individuals with no commercial ability, to whom I must simplify and embed basic commercial principles. I need to temper these principles with those that underline a charity's work and the Charity Commission's guidance.

There are also differences in charity accounting and, as one would expect, a proportion of the charity's funds are ring-fenced and cannot be included in their operating funds. A further complication is the increasing number of charities with pension trust shortfalls. What came as a surprise to me was the fact that charities are often treated as a 'soft touch' and end up in arrangements that are detrimental to their work as they fail to properly scrutinise contracts and leases etc.

In one project, I was approached by the accountant of a local charity that had been running for over 20 years. As a result of a lack of management, over-generous practices and a lack of rigour, they were faced with shutting down. Stepping in as an acting CEO I implemented a full cost cutting review and recovery plan:

- undertaking three tranches of redundancies;
- renegotiating an unfavourable lease;
- shutting down loss-making parts of the charity;
- eradicating poor practices; and
- negotiating the sale of their commercial premises, which were far too big for the charity's purposes.

The charity is now in a much healthier position to continue and is planning further growth and considering options, which include merging with similar organisations. It has been enormously rewarding to take the trustees on a journey from despair to delight and watch them grow personally as the recovery took place.

This and other similar projects have highlighted skills sets I needed to acquire to augment my IP knowledge – in particular change management. It is all very well having an executive that sponsors the recovery and project management to implement the recovery plans. However, if you don't deal with the change management aspects that affect the employees, recovery plans falter or fail. Formal change management techniques and practices have been useful in allowing me to better structure and communicate recovery plans.

Throughout 2015 and 2016 this side of my business has overtaken my traditional IP work and I find myself involved with clients well before any formal procedure is required, often being retained by them to provide ongoing advice and guidance. So I like to think, in line with our president's message in the Autumn *RECOVERY*, I am becoming 'a new kind of IP'. □

**ALISON BYRNE** is the principal insolvency practitioner at Byrne Associates.

# Corporate insolvency framework review

R3 looks at the government response to major changes in corporate insolvency.

The government's summary of responses to its corporate insolvency framework review provides an insight into what we might expect to be introduced through legislation in the near future. There were 71 responses from the stakeholder community; many from the insolvency and restructuring profession but also a number from the creditor community.

The consultation set out four proposals that aim to ensure *'that the insolvency framework supports business rescue where possible, maximising returns to creditors where possible'*. The proposals are: a new business rescue moratorium, allowing companies to designate certain supplies as 'essential', which would guarantee the continuation of these supplies in case of insolvency; a new 12-month restructuring tool; and new options for rescue finance.

R3 welcomed the government's objectives but had a number of concerns around the details. We spent a lot of time during the consultation engaging with members of the profession and business community so were pleased to see that our views and concerns were shared by many others.

## What should we expect next?

Although it's still early days with the government's thinking (they have said they will maintain dialogue with stakeholders over the coming months on the proposals), there was 'broad support' for the principles behind the proposals. We should therefore expect the government to continue with its direction of travel – albeit hopefully with some revision to the current proposals before we see any legislation.

There are clearly a number of concerns that the government must address. There are fears that the proposals could undermine the UK's world-class insolvency regime unless safeguards are put in place to better protect creditors. Business bodies in particular have serious concerns, with one describing them as 'stifling' the current insolvency and restructuring system, and another saying that that they will not enhance the existing framework.

R3 hopes the government will take on board this strength of feeling and consider better safeguards.

### The moratorium

There was broad support for the business rescue moratorium. However, like R3, the majority of respondents believe that the detail of the proposal needs refining and more safeguards for creditors should be introduced.

R3 has previously called for a 21-day moratorium to be supervised by an insolvency practitioner; the government's own plans are for a three-month (extendable) moratorium to be supervised by an insolvency practitioner, accountant or lawyer. Seventy-five per cent of respondents disagreed with the government's proposed length, with the most common alternative suggestion being R3's proposed 21 days; 60 per cent of respondents agreed with R3 that the supervisor should only be an insolvency practitioner.

Given the strength of feeling, we hope the government's final proposal will follow that suggested by R3 and supported by a number of organisations.

### Essential supplies

R3 welcomed the October 2015 extension of continuity of supply rules to IT and utility contracts – it was an R3 campaign that led to these changes being introduced. Under the rules, certain 'essential' contracts (now including IT and utility supplies) cannot be unilaterally changed or cancelled simply because the customer has become insolvent.

The government's 2016 proposal is to extend these rules by allowing directors of insolvent companies to designate their own essential supplies. Over half of the respondents who commented on whether the proposal would bring about more business rescues thought it would do so. However, around 40 per cent disagreed with the proposed criteria under consideration for an essential contract as drafted and almost 70 per cent do not believe the proposed safeguards for creditors are sufficient.

It's clear that safeguards need to be tightened but there is still a lot up for debate around the criteria and scope of an 'essential supplier'.

### Restructuring tool

The government's plan for a 12-month restructuring tool would introduce a 'cram-down' mechanism and the ability to bind secured creditors in a restructuring plan; it was supported in principle by respondents. Just under half agreed with the government that the tool should be a stand-alone procedure rather than an extension of an existing procedure eg a CVA.

The majority of the respondents believe that there is sufficient protection for creditors (through the courts); R3 disagrees. R3 is concerned that the main proposed safeguard, the court, is not set up to deal with such a tool and with the courts already under significant budgetary pressures, we proposed that the tool should only be introduced alongside a new specialist insolvency court. R3 will also continue to raise concerns about the potential for the proposed tool to be abused, particularly in the SME market. This issue hasn't been picked up in the summary but we will continue to call on the government to make the tool only available to larger businesses.

### Options for rescue finance

With more than 70 per cent of respondents disagreeing with the government's proposals, it is unclear what may happen next. The government had proposed to introduce new rules to encourage rescue funding (including priority for rescue finance), but many of those who opposed the proposal agreed: that there is no shortage of rescue funding; that any changes to the 'order of priority' will impact the UK's lending environment; and that secured creditors already make funding available for viable businesses.

The government may put this particular proposal on the back burner, but the issue of rescue finance won't disappear anytime soon.

## Over the coming months

R3 welcomes the government's commitment to engage with stakeholders and looks forward to being part of that dialogue.

The UK's insolvency and restructuring regime is one of the best in the world and any new proposals must only serve to maintain or improve that status, not undermine it. We hope the government will take on board the views of all stakeholders and only introduce proposals that benefit insolvent businesses, creditors and, importantly, that are workable for the insolvency profession.

**GEORGINA WAITE** is R3's senior public affairs and policy manager.

# R3 contacts

R3, 8th Floor,
120 Aldersgate Street,
London EC1A 4JQ

T: 020 7566 4200
F: 020 7566 4224
www.r3.org.uk

## R3 Executive

**President**
Andrew Tate,
andrew.tate@krestonreeves.com

**Vice-president**
Adrian Hyde,
ahyde@cvr.global

## Administration

**Chief Executive Officer**
Graham Rumney, grumney@r3.org.uk

**Office Admin Assistant**
Bonnie Prowse, bprowse@r3.org.uk

## Smaller Practices Group; Personal Insolvency Committee; Regional Communications Committee and R3 Regional Network

**R3 Director**
Emma Hobson, ehobson@r3.org.uk

**Policy and Committee Executive**
Caitlin Powell, cpowell@r3.org.uk

## Finance

**Finance Manager**
Harvinder Kular, hkular@r3.org.uk

**Assistant Finance Manager**
Alex Coles, acoles@r3.org.uk

## Membership & Marketing

**Head of Marketing & Member Services**
Cynthia Matthews,
cmatthews@r3.org.uk

**Marketing Executives**
Fareeha Afghan, fafghan@r3.org.uk
Marek Nusl, mnusl@r3.org.uk

**Membership Officer**
Shemin Varma, svarma@r3.org.uk

**IT Manager**
Samit Vadgama, svadgama@r3.org.uk

**Membership & Marketing**
membership@r3.org.uk
020 7566 4238

## Communications, Public Affairs and Policy

**Director of Communications & Public Affairs**
Victoria Jonson, vjonson@r3.org.uk

**Senior Communications Manager**
Nick Cosgrove, ncosgrove@r3.org.uk

**Communications Officer**
Jo Tacon, jtacon@r3.org.uk

**Senior Public Affairs & Policy Manager**
Georgina Waite, gwaite@r3.org.uk

**Public Affairs & Policy Officer**
James Jeffreys, jjeffreys@r3.org.uk

## Education, Courses & Conferences

**Senior Courses & Conferences Manager**
Angela Fuller, afuller@r3.org.uk

**Courses & Conferences Organiser**
Amber Emberson, aemberson@r3.org.uk

**Courses Administrator**
Maggie Dean, mdean@r3.org.uk

**Senior Regional Events Co-ordinator**
Sara Calvert, scalvert@r3.org.uk

**Course Bookings**
courses@r3.org.uk
T: 020 7566 4234
F: 020 7566 4225

## Technical

**Technical Director**
Caroline Sumner, csumner@r3.org.uk

**Technical Officer**
Jonathan Ausena, jausena@r3.org.uk

## Committee Chairs

**Education, Courses & Conferences**
Adrian Hyde, 020 3794 8750

**General Technical Committee**
Mike Pink, 0207 311 1000

**Membership & Member Services**
Duncan Swift, 023 8033 0116

**Personal Insolvency Committee**
Stuart Frith, 0207 809 2379

**Policy Group**
Giles Frampton, 01752 690101

**Regional Communications Committee**
James Martin, 0121 543 1900

**Scottish Technical Committee**
Eileen Blackburn, 0131 225 6366

**Smaller Practices Group**
Simeon Gilchrist, 0207 691 4166

## R3 in Scotland

**Chair & Representative on the R3 Council**
Tim Cooper, 0131 222 9817

## Regional Chairs

**Eastern**
Frank Brumby, 01603 611370

**London & South East**
Nick O'Reilly, 020 7186 1144

**Midlands**
Chris Radford, 0115 983 8200

**North East**
Neil Harrold, 0191 2328345

**North West**
Richard Wolff, 0161 828 1990

**Northern Ireland**
Michael Neill, 028 9031 4466

**Southern**
Andrew Watling, 023 8033 6464

**South West & Wales**
Alan Bennett, 01392 337000

**Yorkshire**
Adrian Berry, 0113 243 9021

## Regional Representatives on the R3 Council

**Eastern**
Andrew Turner, 01502 563921

**London & South East**
Stuart Frith, 020 7329 4422

**Midlands**
James Martin, 0121 543 1900

**North East**
Kelly Jordan, 0191 211 7904

**North West**
Richard Wolff, 0161 828 1990

**Northern Ireland**
Joan Houston, 07799 581 528

**Southern**
Duncan Swift, 023 8033 0116

**South West & Wales**
Richard Clark, 0117 939 2000

**Yorkshire**
William Ballmann, 0845 437 4660

## Other Council Members

Eileen Blackburn, Alison Byrne, Frances Coulson, Matt Dunham, Christina Fitzgerald, Giles Frampton, Simeon Gilchrist, Adrian Hyde, Jamie Leader, Gareth Limb, Nick Pike, Mike Pink, Liz Pywowarczuk, Phillip Sykes, Matthew Tait, Charles Turner, Laurence Weeks, Cathryn Williams.

# R3 in Scotland celebrates at Annual Dinner

Inaugural award celebrates a member's special contribution to the profession.


**Left to right:** Chair of R3 in Scotland Tim Cooper, award-winner Roy Roxburgh and James Waterson, regional manager at Close Brothers Asset Finance

In September, members of R3 in Scotland congregated in the Grand Central Hotel in Glasgow for their third Annual Dinner. The evening, sponsored by Willis Tower Watson, Sweeney Kincaid and Insolvency Support Services, was a relatively new event in the social calendar but offered an opportunity for members to get together socially and recognise the achievements, value and contribution of the insolvency profession to Scotland.

### Seismic shifts in the markets

During the dinner, host and chair of R3 in Scotland, Tim Cooper, spoke about the changes he's seen in his 20 years in the insolvency profession and how it has adapted as the markets and economy shift.

> "It's important that we adapt to the landscape so we can continue to help companies and individuals in distress."

'Over the last two decades there have been seismic changes to the markets. The insolvency profession shifted with the economy; one recession led by industrial decline is very different to one led by a financial market crisis,' said Mr Cooper. 'It's important that we adapt to the landscape so we can continue to help companies and individuals in distress.'

Tim also spoke about changes to the insolvency regime over the last two decades, and the wealth of new tools and options available to the profession that has helped to make the UK's regime one of the best in the world today.

### A lifetime of good work

While the dinner celebrated the work of all R3 in Scotland's members, the evening was an opportunity to recognise the special contribution of one member in particular.

Roy Roxburgh was presented with the 'Inaugural R3 in Scotland Award for Lifetime Achievements and Outstanding Contribution'.

Mr Roxburgh, a recently retired partner at Maclay Murray & Spens LLP (now a consultant), is a qualified solicitor and notary public based in Aberdeen. During his career he acted as a convenor and speaker at courses for both ICAS and the Law Society of Scotland (LSS). For over 20 years he has been a member of the R3 Scottish Technical Committee, the LSS Solicitors Company and Insolvency Committee, and the LSS Accreditation Panel for Insolvency Specialisation. Since 2010 he has represented LSS on the Joint Insolvency Committee. He was the moderator of the JIEB ACVAR (Scottish) paper for two spells totalling over ten years.

Presenting him with the prize, James Waterson of Close Brothers Asset Finance, the sponsor of the award, described Roy as having: 'contributed countless hours, days and weeks over a distinguished career for the betterment of the insolvency profession and to raise ethics, standards and technical excellence. Roy is a shining example of what professionalism means, and the profession as a whole has benefited from his outstanding contribution over his career, and he continues to do so in retirement.'

Roy's fellow Scottish Technical Committee member and chair, Eileen Blackburn of French Duncan, added: 'He has always contributed to the Committee in a helpful fashion and his great wealth of knowledge and experience has furthered the work of the Committee on many occasions and accordingly the standing of R3 in the Scottish business community.'

### A bright future

Summing up another successful year for R3 in Scotland, Tim Cooper concluded: 'I have practised now in three market regions, latterly Scotland and none more so have I found such a degree of excellence, professionalism, integrity and expertise as I have here.'

With the Annual Dinner going from strength to strength and establishing itself as an important date in the profession's social diary, be sure to look out for details of next year's event. □

Save the dates
26–28 April 2017
**R3 Annual Conference**
DoubleTree by Hilton, Dublin

# R3 events, courses and conferences

## January

| Date | Event | Venue |
|---|---|---|
| 1 | **Northern Ireland Region Half-Day Conference and AGM** | The Merchant Hotel, Belfast |
| 6 | **Introductory Series, A-Z of Insolvency** | Prospero House, London |
| 6 | **Advanced Tax** | Holiday Inn Regents Park, London |
| 6 | **South West Christmas Event & AGM** | The Square Club, Bristol |
| 6 | **Southern AGM & Christmas Drinks** | RSM Restructuring Advisory LLP, Eastleigh |
| 8 | **Insolvency Day** | Gateley plc offices, Manchester |

## February

| Date | Event | Venue |
|---|---|---|
| 23 | **Asset Tracing, Fraud and Forensics** | Holiday Inn Regents Park, London |
| 28 | **London Regional Meeting** | TLT LLP, London |

Regional events (light teal): 1, 6 (South West), 6 (Southern), 28
R3 events (dark blue): 6 (Introductory Series), 6 (Advanced Tax), 8, 23

- Regional events
- R3 events

For further information on R3 courses and conferences, please visit the R3 website **www.r3.org.uk**, where you can download the 2017 Spring programme.

Alternatively, call the Courses team on 020 7566 4234 to request further details.

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An interview with...

# Judge Brian Doyle

**Matt Jukes** speaks to the president of Employment Tribunals for England and Wales to get his thoughts on how insolvency and employment law come together.

**Q These are times of great change for the legal system in England and Wales, and Employment Tribunals have not escaped changes to fees. How have you had to adapt?**

A The introduction of fees in tribunals has reduced the number of cases by about 70 per cent. The typical workload has changed quite radically and the type of cases we're hearing now are complex, higher value cases. The lower value, more straightforward cases are either not being brought forward because of fees or, if they are, they are more capable of being settled. It's been a big change and we're doing that against the background of the government's public expenditure savings and without any real prospect of replacing judges as they retire or resign.

> "An insolvency practitioner needs to stay up to date with the legislation and with the case law that emerges from it; have a good understanding of what the law requires; and take legal advice."

**Q In our summer issue we ran several articles about how employment law and insolvency law interact. There seemed to be a perception that the two areas of law have problems working together or even work at cross purposes. Do you think this is the case?**

A My view is that they are two distinct areas of law that have to interact at certain points – most notably when we're concerned with corporate rescues, transfers of undertakings or when a business fails. Where the two regimes interact, there are some difficult policy decisions to be made about which set of rights or duties is to prevail over the other. Do you say that corporate rescue is a more important policy than the employment security of a workforce? Or do you say that protecting the public interest in the insolvency fund is more important than providing financial security to employees who have been made redundant? Members of the public often assume that courts and tribunals decide what the fairest thing is to do in those circumstances, but the reality is that we're working through a framework of legislation decided by government and parliament that sets out the parameters and limits of what we can do.

**Q In certain situations an IP could now find themselves held responsible for, or in deep trouble because of, errors around the process of a collective redundancy. What steps should they take to avoid this?**

A Generally speaking, where an insolvency practitioner or an employer gets into difficulty it's because they were either unaware of the legal position or they were indifferent to it – they took a chance or a risk. The answer is that an insolvency practitioner needs to stay up to date with the legislation and with the case law that emerges from it; have a good understanding of what the law requires; and take legal advice. I understand that's a counsel of perfection. In an insolvency situation you're going to be asking: 'Do I have the funds to seek legal advice, what if I expended those funds, and does that mean there will be fewer available for the creditors?' I appreciate those tensions for IPs. If you were a going concern you'd always want to take legal advice in order to avoid being on the end of a liability judgment. But if you're dealing with an insolvent business with few and deteriorating assets, it's a very different equation.

**Q How can the insolvency profession engage more with Employment Tribunals?**

A Don't ignore Employment Tribunal correspondence, which is unfortunately what often happens. For example, if a tribunal sends a claim form to an IP, it's not helpful for an IP to write back with a letter saying: 'We intend no disrespect to the tribunal but we are not going to take part in the proceedings'. By writing to the tribunal saying you're not intending to take part, you immediately exclude yourself from the process. You're then much more likely to find that you're on the wrong end of a tribunal judgment that inevitably has to be based on the evidence that the employees give.

One additional step will put the IP in a much better position: send back a completed ET3 response form. It's a relatively straightforward form that is easy to complete. Then the IP is entitled, even »

## Judge Brian Doyle biography

- Judge Brian Doyle was appointed president of Employment Tribunals in England & Wales in 2014. He was previously the regional employment judge for the North West region.
- Immediately prior to becoming a salaried employment judge in 2000, Brian was professor of law at the University of Liverpool and he was dean of the Liverpool Law School.
- Brian is the author of a number of publications in the employment and equality law field, most notably in the area of disability discrimination law.

if they don't attend the actual hearing, to correspond with the tribunal. Completing the response form ET3 allows the IP to participate in the process. Just providing the facts as seen from the company's perspective is helpful. Otherwise we're left with the employee's ET1 claim form, which will inevitably be an incomplete picture.

**Q Are you getting more litigants in person at present as well? Doesn't that really affect a tribunal?**

A We are seeing more litigants in person. If the claimants are represented by a trade union, for example, they may have lawyers on their behalf. Those lawyers do some basic research and piece together a picture, and often that's all we're left with. It would be much better if we were presented with information from the company's side so that we could see the bigger picture. This comes back to the priorities of the IP, and they may feel that engaging is a luxury, but at least completing the ET3 response form will give you a seat at the table.

> “If a tribunal sends a claim form to an IP, it's not helpful for an IP to write back with a letter saying: ‘We intend no disrespect to the tribunal but we are not going to take part in the proceedings’.”

**Q What can Employment Tribunals do to engage more with insolvency practitioners?**

A If we can digitise our processes so that claims and responses are routinely completed online, communication is entirely electronic and, if a case comes to hearing, we receive all evidence in digital form rather than having to create paper files. The mantra now is ‘digital by design, digital by default’. If we can digitise the process we will not only save money but also save time for all concerned.

The other thing we are doing is the kind of activity I'm engaged in now: being interviewed. The discussions I've had with R3, my willingness to meet with representatives and professional bodies, not just in the insolvency world but in employment and business generally, are all part of this. The value of meeting and communicating with them is that I hope I can give them a better understanding of how the process works and what our expectations are.

**Q Meeting the stakeholders is not the norm for a senior member of the judiciary is it?**

A It hasn't been, but the senior judiciary is generally now of the view that we need to spend more time in outreach activities, explaining to users and stakeholders what it is that we do and why we do it. The view has changed particularly, but not exclusively, because of the growth of litigants in person. It's not just individuals – companies, businesses and firms are represented by a partner or a shareholder or a director and for all intents and purposes they are a litigant in person. We can't take sides, but the more we can help them to understand the process the better.

**Q How will the Courts and Tribunals Service Reform (reconfirmed by the ‘Transforming our Justice System’ proposal) change things with regard to the way the system works, and how IPs and Employment Tribunals interact?**

A It is now a six-year programme worth a billion pounds and it's all about rationalising our estate, simplifying our procedures and making better use of IT.

I'm pretty confident that we will get to a system by 2020 where Employment Tribunals won't be working with paper files. It's not just about ensuring evidence and materials are in electronic format, it's about whether we always need to hold physical face-to-face hearings.

One of the big reforms that Lord Justice Briggs is recommending is an online court for claims of up to £25,000, probably initially up to £10,000. Many Employment Tribunal claims could be dealt with via that medium. That would be suitable for the simpler cases, of which many would be insolvency and collective redundancy cases. This applies to instances where there's no real dispute of facts and it's just a question of what compensation is payable.

**Q That's quite fitting given our theme of new technology this issue, but talk of technology like that can make people nervous. It sounds like much of the interaction will be electronic. Is there any reason to think that the human element is being cut out?**

A I'm not nervous about it. We're not necessarily proposing an AI system, where cases would be decided using technology and no human hand – it's more about how the parties interact via the online court. Lawyers are still going to be needed to give initial advice, and judges and caseworkers are still going to be needed to reach decisions at points in the process.

**Q Despite the uncertainty, we have to ask how you think Brexit is likely to shake up things for Employment Tribunals, in particular regarding the relationship with insolvency practitioners?**

A Judges could be the worst possible predictors of this. We don't know what kind of Brexit we're going to experience. We have a hint with the so-called ‘Great Repeal’ bill that existing EU law will be captured into UK law at the point of Brexit and government will take its time after to decide what parts to keep or jettison.

A lot of insolvency and redundancy law is derived from European law. All we can say is that we might not experience any immediate change. For example, take the meaning of the word ‘establishment’ in collective redundancy. That is all about

> “Completing the response form ET3 allows the IP to participate in the process. Just providing the facts as seen from the company's perspective is helpful.”

how you measure whether an employer is making 20 or more employees redundant. One interpretation is that establishment is the whole of your workforce. Another is that it just refers to the workforce at a single unit. That had to be resolved in case law and we focus on the single factory or unit. You could imagine a future government saying: ‘We want to keep collective redundancy law, but we want to improve it by saying it's all of your workforce, not at individual sites’. You could also have a government that says ‘We don't see why it should take place at all; it's an impediment to the insolvency process’. It won't necessarily be Brexit that will determine change, but more likely the policy of future governments. ◻

**MATT JUKES** is publishing manager of *RECOVERY* magazine.



Editor recovery@r3.org.uk | Recruitment recovery@r3.org.uk/recruitment


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