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RECOVERY

Banking and finance

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Editorial

Judicial commentary on the fees and conduct of insolvency practitioners often attracts press attention, but Mr Registrar Jacques' comments on the fees application of the administrators of Super Aguri Formula 1 compare favourably with some recent examples. Awarding 95 per cent of the fees applied for in a case reported to be high profile, complex and difficult, he noted that the administration was 'properly managed by professional administrators'.

The more of us who can attract positive judicial or other comment the better. Such third-party approval is the best way to raise the perception of our industry. R3 does a great job with its PR and lobbying, but we also need to help ourselves.

It is also gratifying, and humbling, to receive praise from those less fortunate than ourselves. For instance, recently two chaps from my office came back from a job where they had had to make 20 people redundant. They told me that, after they had done it, the people thanked them for explaining things properly and acting professionally. I'm sure many of us have been in that situation too; this is how it should be.

However, many of us getting the job right and being recognised for doing so is not enough. There are still too many occasions when personal or client experience, or judicial criticism, identifies IPs who have fallen short of the standards we must demand. A remedy to that is speedy, clear and fair regulatory action not only being taken, but being seen to be taken, by a regulator that is respected by the public and independent of those it regulates.

And what of where the work is coming from? At the time of writing the construction industry continues to add to the corporate insolvency statistics, which nevertheless remain subdued. The economic consensus attributes the lower than expected levels of insolvency to low interest rates and zombie companies not being pushed over by the banks. Vernon Dennis considers these issues on page 3. At the same time HMRC, while apparently recognising the problem, continues to offer time to pay to repeat customers, as Gordon Smith explains on page 31. The restructuring and insolvency tide is turning, albeit slowly, and seems unlikely to become a flood, but it will no doubt be supported by the public sector spending less in the private sector due to the government's austerity measures. As a profession we have much to offer and we should ensure that we are being seen to do so. In some cases we will help businesses avoid disaster, but decent burials will also be required.

C. Laughton

Chris Laughton is editor of *RECOVERY* and a partner at Mercer & Hole.

The Great British insolvency conundrum

Where are all the insolvencies? Vernon Dennis thinks they may be hiding…

According to Laurence J Peter, the American management theorist, 'an economist is an expert who will know tomorrow why the things he predicted yesterday didn't happen today.'

Bearing this is mind it is with some trepidation that a mere lawyer seeks to answer the question: why, following a recession as deep as that of the Great Depression, have we not seen an exponential rise in the rate of corporate insolvencies?

The recession wasn't that bad?

The decline in GDP from Q2 2008 to Q3 2009 was sharper than in any recession suffered in the last seventy years. With an expected lag between recessionary peak and insolvency peak of 12–18 months, it appeared that 2010 would see a large rise in corporate insolvencies. Instead, comparing Q2 2009 and 2010 we have seen a fall of 19 per cent in liquidations and 24 per cent in administrations.

While GDP is the accepted economic measure of growth or decline, it does not tell the whole story. Alternative economic indicators in different recessions have been worse. In the 1980s unemployment rates and falls in household income were significantly worse, while in the early 1990s business insolvencies and repossession rates were higher. Perhaps the effects of the recent recession were not as bad as feared?

Unfortunately, for the answer does not appear this simple, the economic recovery is fragile, retail spending is falling, the UK housing market moribund, and consumer and business confidence remains low. We are not out of the woods yet.

The banks are sitting on the problems?

The credit crunch and the near implosion of the banking system brought swift and unprecedented state intervention. This action has come at a high cost, not least to the banking industry itself. Some banks are now wholly or partly state owned, all banks are subject to stricter capital requirements and regulation. Prudent banking is likely to be the new orthodoxy for some time to come.

This is shown by the low rate of mortgage acceptances and the exhortations of Vince Cable for the banks, once again, to start lending to businesses. Bank lending is, however, unlikely to return to normality until balance sheets are improved and it is those lenders most exposed to the property market who seem to be having most difficulty.

Seeking to avoid flooding the market with property, as occurred in the 1990s, banks are seeking ways to ensure bad debt is not crystallised. Where 'forced' this may include moving assets into subsidiary special purpose vehicles (SPVs), or agreeing to 'amend and extend' facilities. In general, many potential investors have waited in vain for banks to release under-performing property assets, as the banks appear to be waiting to see if the overall economic situation will improve.

> “Standard and Poor's European Leveraged Loan Index of outstanding loan maturities shows a rise from €5 billion in 2011 to €49 billion in 2015.”

One further issue on the horizon is the maturing of credit facilities that were provided pre-credit crunch. Standard and Poor's European Leveraged Loan Index of outstanding loan maturities shows a rise from €5 billion in 2011 to €49 billion in 2015. Dealing with this wall of debt will be a challenge to both lender and borrower alike.

Borrowers are avoiding the problems?

With lenders willing to amend and extend facilities, albeit at the cost of increased spreads, additional fees and improved security, many businesses are currently able to avoid issues of over gearing – for now. Allied to this, over 371,000 businesses have entered into time to pay arrangements with HMRC (delaying payment of £6.38 billion in tax).

Financial and operational restructuring is the long-term solution for many companies. Unfortunately for many, short-term survival seems to be their only aim. Planning for the future is being put on hold and opportunities to obtain the invaluable assistance of our profession are not being taken up.

Capital markets have come to the rescue?

Despite the gap left by banks, hedge funds, pension funds and sovereign wealth funds have not stepped into the breach. Instead the most marked incidence of new lines of debt funding has emanated from investor appetite for high yield bonds. The non-investment grade bond market has a chequered history; often associated with hostile take-overs and problems associated with identifying stakeholders who may prove to be disruptive on any corporate restructuring.

With the wall of debt fast approaching more companies may turn to this solution; this will improve the overall quality of the investment encouraging a different type of bondholder. 'Step-up notes', which structure interest rate rises are developing to meet short-term funding gaps and the traditional subordination of high yield bond debt to bank debt is being challenged. With greater ability to control situations of possible default bondholders may be more inclined to reach longer term collaborative solutions.

The access to this market is limited, but as with smaller companies seeking funding from asset based lenders, factors and discounters, larger companies may find that alterative sources of funding come at a cost.

Are we heading for a double dip?

The cost to UK plc of the bank crisis has been a fundamental re-evaluation of public spending. In finding £81 billion worth of cuts by 2014 over 490,000 public sector jobs will be lost. Those companies dependent on public sector contracts will undoubtedly suffer and a domino effect could endanger the growth required from the private sector, if a double-dip recession is to be avoided.

Allied to a lack of available funding business confidence is low, resulting in a paucity of new investors willing to buy businesses following reconstruction and/or from administrators. The deflationary pressures of 'why buy now when the price could be lower later' mean that lenders and other stakeholders have little desire to expose distressed assets to an already depressed market.

As a result, despite signs of economic recovery, there are clearly huge problems still remaining. These problems have not been solved, merely postponed. Surely this must mean that corporate insolvency numbers will rise? My personal opinion: I have no idea. The only thing that has been certain about the economy over the last

Vernon Dennis is a partner at Howard Kennedy.

President's column

Steven Law reviews R3's progress and indicates there will be more corporate insolvencies in 2011 according to the latest members' survey.

Six months into my role as R3 president and I feel like I am running at full speed – my R3 diary includes attending the party conferences (see report on page 40), briefing journalists, shaping consultation responses, touring the regions, attending R3 committee meetings and hosting LITE.

The need for R3 to engage with Parliament and the press remains as critical as ever. We have a new insolvency minister, Ed Davey MP, whom I met on 21 October. It was an achievement just getting a slot in his schedule but he was keen to hear R3's views on the industry and the issue of regulation. He seemed engaged and responded very well to our upcoming campaign 'Holding rescue to ransom'. In PR terms, a recent BBC Radio 4 *File on 4* piece on a perceived failure of regulation showed how we cannot let journalists form their own opinions without hearing our side.

Conservative Conference fringe event. Left to right: Stephen Alambritis (Federation of Small Businesses), Steven Law, Kamal Ahmed (business editor, *Sunday Telegraph*) and Harriett Baldwin MP.

The economic outlook as predicted by you

The impact of the recession doesn't feel quite as bad as the recessions of previous decades as corporate insolvency numbers seem to have steadied, and in fact have decreased a little over this year. However, you as R3 members are expecting increases in corporate insolvency to come through the pipeline at some point.

When we look back at 2010, it seems you thought this year could be the calm before the storm, as indicated by our latest R3 members' survey. This found that almost half (45 per cent) of you are expecting corporate insolvencies to peak in 2011. You are predicting 27,540 corporate insolvencies for 2011, which is up on the 26,196 for 2009 for England, Scotland and Wales. Given the decreases over the course of this year, an increase from 2009 to 2011 will seem even more pronounced.

Various monetary and fiscal policies have, in my view, successfully stemmed the tide of insolvencies so far. We've seen historically low interest rates keeping the costs of servicing debts relatively low; HMRC's Time to Pay scheme, giving many businesses breathing space to pay their taxes; and major creditors adopting a more supportive attitude towards struggling companies than they have previously. The banks, in particular, have demonstrated a real supportive role towards ailing businesses.

Conditions set to change

Early next year, rises in VAT will begin to hurt certain sectors and interest rates can only go one way (up!). Public sector cutbacks are likely to impact on the private sector, hitting the many businesses that grew up dependent on outsourcing contracts from local and central government, and, as the cost of servicing debt grows, creditors will begin to demand their dues. Our recent membership survey also shows that IPs feel that HMRC is starting to tighten up on Time to Pay. HMRC remind us about the criteria for their Business Payment Support Service in this issue (see article by Gordon Smith, HMRC on page 31).

> "Almost half (45 per cent) of you are expecting corporate insolvencies to peak in 2011. You are predicting 27,540 corporate insolvencies for next year."

Comprehensive Spending Review

While the focus is on public sector jobs likely to be lost, jobs in the private sector are just as much under threat. Research by R3 indicates that 200,000 small businesses in the private sector would also have to consider job cuts should their public sector contracts cease. These potential loses will come on top of the 490,000 public sector jobs likely to be lost. Since the 1990s, reliance on private sector companies has mushroomed and today a third of small businesses are reliant on public sector contracts.

Thirty per cent of small businesses say they are 'very reliant' or 'fairly reliant' on public sector contracts and ten per cent of all small businesses say they would become insolvent if they no longer had contracts to supply the public sector. We calculate that 148,000 small businesses are at risk of failure, but of course not all businesses will lose all of their public sector work. The effect on the current levels of corporate insolvency is likely to be pronounced in any case – given that business failures ran to 26,000 for the whole of 2009. Businesses with a diversified customer base will clearly be better able to weather the storm.

By the seaside

While the political parties had their conferences, nearly 150 delegates gathered for the LITE Conference in Bournemouth. Although not as warm as Portugal, the presentations were excellent. I was also delighted to see so many of you at the SPG on 4 November and to have some constructive discussion regarding the next six months. We will also be publishing minutes of council meetings in the near future on our website, in the interests of greater transparency. ☐

Steven Law is a partner at Ensors and president of R3.

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News update

New INSOL Europe president

Chris Laughton, editor of *RECOVERY*, became the new president of INSOL Europe in October. Chris is a cross-border restructuring and insolvency specialist and he will be championing the theme of communication during his term as president. He will encourage other IPs to communicate more effectively with stakeholders and the business world in order to promote a better understanding of the skills and legislation insolvency professionals bring to bear when seeking to rescue a failing business.

Support for SPG

Emma Lovell joined R3 in September as the Smaller Practices Group (SPG) Committee support executive. She will provide a range of support for the work of the SPG and for smaller firm members. Emma will be assisting with smaller firm operational practice development, addressing education and training needs and providing a specific avenue, in addition to SPG committee members, via which smaller practices can highlight issues affecting their business that require further work or support.

Having trained in the legal field in the private sector, Emma joined R3 from The Insolvency Service, where she was an insolvency examiner and more recently worked within the headquarters department that supports Official Receiver services.

New SPG chair Liz Pywowarczuk (left) with Emma Lovell, SPG Committee support executive (right), at the conference.

New reporting accounting code for banks

The UK's largest banks have agreed to a self-imposed financial reporting code in order to avoid regulators imposing their own reporting requirements in the ongoing poor financial environment. The British Bankers Association has released the new code, which commits the largest banks, including HSBC, Lloyds TSB and Barclays, to increase and enhance the standard of their financial reporting.

The Financial Services Association (FSA) became frustrated at the poor level of consistency of banks reporting to the market and, in particular, their valuation of complex financial assets. These assets have no market inputs into their value and must be measured according to an accounting model, so auditors actions have been called into question. The FSA is also seeking new powers to censure, penalise or disqualify individual auditors on the grounds that the profession failed to challenge management bias in the lead up to the banking crisis.

However, banks themselves seized the initiative by agreeing to impose their own code, meet and discuss accounting issues and promote more consistency in how they measure their financial assets. In the new code, banks promise to go beyond strict interpretation of accounting rules, provide more meaningful notes to the market and to deliver a more consistent standard.

New figures on 'Time to Pay'

On 29 October the ONS released new figures on HMRC's Business Support Payment Scheme and Time to Pay Agreements. The figures showed the number and value of Time to Pay arrangements has decreased dramatically during 2010. The number and value of arrangements granted across all tax regimes between January and September 2009 was 196,200 and £3.41 billion respectively. During the equivalent period in 2010 (up to September) 114,600 arrangements worth £1.89 billion were granted. Currently, levels in September 2010 are running at around 56 per cent in terms of numbers of arrangements and 56 per cent in terms of value in comparison to 2009 levels. The figures also show that since the scheme began in November 2008, 371,200 arrangements were granted, which were worth £6.38 billion. £5.41 billion has already been paid to HMRC from mature arrangements.

RICS launches Valuer Registration Scheme

Credit crunch losses have massively increased the number of overvaluation claims against surveyors and as a result professional indemnity insurance has become increasingly difficult to obtain. Several high-profile surveyors' firms have collapsed under the pressure and the profession's reputation has been hit.

As a result, RICS has launched the Valuer Registration Scheme to 'ensure that members adhere to, and can be monitored on, practising the standards contained in the *RICS Valuation Standards* (also known as the *Red Book*)'. In essence, the scheme will require specified information from its members to allow RICS to monitor compliance. If RICS detects anomalies it can call in surveyors' files, visit members and ultimately use the information to commence disciplinary proceedings.

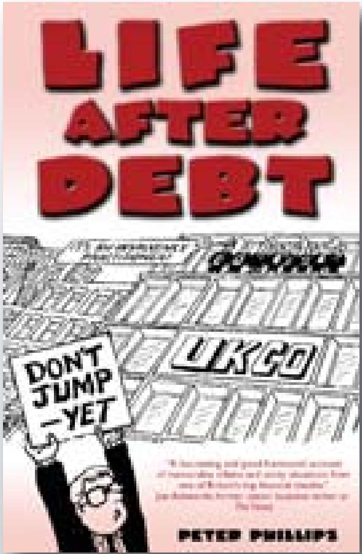
The scheme was launched formally on 20 October 2010 and members can now sign up on a voluntary basis. For members undertaking *Red Book* valuations in the UK, the scheme will become mandatory from 30 April 2011. The scheme is also being rolled out across the rest of the world on a staggered basis. Failure to register under the scheme will result in a surveyor being unable to undertake *Red Book* valuations.

Consultation on ISA facility

Liquidators in voluntary liquidations may no longer be able to bank with The Insolvency Service's Account (ISA). Following the sharp decline in the use of ISA by liquidators in these circumstances, The Insolvency Service (IS) has launched a consultation on the withdrawal of this option. The IS has provided documentation giving advanced notice of the proposed changes, which, subject to the outcome of the consultation and approval by the minister, will come into force in 2011.

UK economy grows

The UK economy grew by 0.8 per cent in Q3. This follows a 1.2 per cent rise in the second quarter and is double the 0.4 per cent expected by analysts. However, these figures come in advance of the spending cuts promised in the Comprehensive Spending Review and, with VAT due to rise in January 2011, it is debatable if such growth can be sustained.



Life After Debt

Edition: First
Author: Peter Phillips
Publisher: Matador
ISBN: 9 7818487 6526 9
Price: £12.50

Book review

In an engaging collection of anecdotes drawn from a lifetime's travails as an insolvency practitioner, Peter Phillips shows us, from the safe harbour of his very active retirement, the way the insolvency profession has evolved over the last four decades.

If the past is, as L P Hartley tells us, a foreign country, then these tales are the dispatches of a foreign correspondent. They record, in the historic cases, the characters and events of a time when the profession as it is now was still in its infancy – still recognisable, but they undoubtedly did things differently there!

The stories, mostly amusing but sometimes sobering, draw from a wide selection of the largest, most memorable and most colourful insolvencies of our time. They tell us a great deal about the remarkable versatility required of insolvency professionals and the diverse combination of skills they must bring to the rich mix of problems confronting them on a daily basis. No insolvency professional is ever bored. The endless variety of the characters, industries and situations encountered through insolvency business is powerfully attested to in this attractively quixotic miscellany.

The most appealing aspect of the book is, perhaps, that the writing reveals the author himself at every turn. Peter's innate modesty, his intense veneration for his father, his warm regard for his professional colleagues and pride in the profession he helped to shape are everywhere in evidence. The open-hearted nature of the man and, above all, his unquenchable sense of humour shout out from each page.

Mark Andrews is a partner at SNR Denton UK LLP.

In support of the Wiseman Trust

One of the ten team members from Wedlake Bell celebrates completing a 220-mile cycle ride across the Massif Central, southern France. All ten members of the Wedlake Bell team completed the trip over a three-day period at the end of September. Generously sponsored by Hilco, the team raised money on behalf of the Richard & Jack Wiseman Trust.

The Trust was founded following the tragic loss of Richard and Jack Wiseman in the summer of 1993 as a result of Twin-to-Twin Transfusion Syndrome.

This little known condition accounts for the deaths of many hundreds of identical twins in single-placenta pregnancies. For reasons unknown, the placental blood flow is irregular to the two babies, one receiving too much and the other not enough. This places both babies at extreme risk of a tragedy, both before and after the birth.

Richard, Jack and their mother were treated at Queen Charlotte's and Chelsea Hospital in London where research into the condition is at an advanced stage. This research is concerned with placental blood flow and progress is anticipated in all abnormalities of blood flow in unborn babies, whether single or twins.

Careful monitoring of a single-placenta, twin pregnancy brings great benefits. Using an ultrasound scanner, monitoring is carried out at 18 weeks into the pregnancy and every two to three weeks thereafter. For instance, when an unusual increase in the fluid surrounding the developing babies is observed and can be readily drained away, it can save as many as two out of three pregnancies from ending in tragedy.

Already research has led to a large saving of life. The aim of the Trust is to fund continuing research into the causes of the syndrome so that early diagnosis and treatment become routine with every multiple pregnancy.

Martin Arnold is a partner at Wedlake Bell LLP.

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Legal update: challenging CVAs – a growing trend?

Recent decisions on CVAs have provided administrators with useful guidance, which should help them to reduce costly court involvement in the future.

Introduction

When company voluntary arrangements (CVAs) were introduced, their key selling points were that they were flexible and that they avoided the need for court involvement in all but the most exceptional cases. Twenty-five years on, that very flexibility, and the consequent scope for innovation when preparing a CVA proposal, seem to have been driving dissenting creditors to seek (or at least threaten to seek) court involvement in an increasing number of cases.

Why are CVAs currently coming under increased scrutiny?

The underlying reasons behind this apparent increase in court involvement are not hard to identify. CVAs have, over the last few years, been used in increasingly inventive ways, as those seeking to rescue companies have attempted (as in the *JJB Sports* CVA and the failed *Stylo* CVA) to use CVAs to free a company from specific problematic liabilities (often obligations under unprofitable leases) while making clear their intention to satisfy other unsecured liabilities in full, subject to relatively minor contractual amendments.

The increased focus on using CVAs to compromise specific liabilities has led to a growing awareness that the votes of all unsecured, unconnected, creditors are given equal weighting for voting purposes, whatever the terms of the CVA. Unlike the position under a scheme of arrangement, creditors being offered a different economic deal are not put into a separate voting class, with the potential ability to veto the proposal. A creditor's rights could therefore be significantly altered by the terms of a CVA that had been approved by only those creditors who were not asked to make any significant concession or compromise. As Etherton J noted in *Prudential Assurance Co Ltd* v. *PRG Powerhouse Ltd* [2007] EWHC 1002:

> *'In effect, the votes of those unsecured creditors who stood to lose nothing from the CVA, and everything to gain from it, inevitably swamped those of the guaranteed landlords who were significantly disadvantaged by it. It is obvious from the terms of the* Cork Report *that such a result was wholly outside the contemplation and intention of the committee.'*

While this result may have been unintended, the reality is that those creditors who are being asked to make the greatest concessions could find that their opposition to a CVA proposal was mathematically irrelevant, as the CVA was likely to be approved by creditors with entirely different economic interests.

When this CVA voting structure is combined with an increased focus on the recent high-profile CVAs on compromising specific creditor claims, the possible disapplication in a CVA of the general *pari passu* principle (as considered in *HMRC* v. *Portsmouth City Football Club & Anor* [2010] EWHC 2013 (Ch)) or the potential loss of parent company guarantees (as threatened in *Mourant & Co Trustees Ltd* v. *Sixty UK Ltd* [2010] EWHC 1890 (Ch)), it is perhaps inevitable that there has been an increased focus on the circumstances in which the courts may intervene in the CVA process in order to provide creditor protection.

The role of the nominee in preventing challenges

Before looking at the role of the court, and possible grounds for challenging a CVA, it is important not to lose sight of the crucial role of the nominee in acting as a gatekeeper, preventing companies from proposing CVAs that are manifestly unfair. This point was highlighted in the *Miss Sixty* judgment, which referred to the following observations made by Warren J in *SISU Capital Fund Ltd* v. *Tucker* [2005] EWHC 2170 Ch:

'It is not for officeholders to advocate the interests of one group of creditors against another group, nor to engage in brinkmanship, or attempt to extract ransom payments…they simply put forward proposals (which, if they are acting properly, are ones which they must consider to be fair to all the creditors of the company and to the company itself). …[the responsibility of the office-holder] is to try to structure an arrangement that will be capable of achieving the necessary statutory majorities ***and will not be unfairly prejudicial to any creditor****.' [our emphasis]*

The role of the nominee (and also, if a different person, the administrator or liquidator making the proposal) should be, to borrow a phrase from the *Miss Sixty* judgment, to ensure that any manifestly unfair CVA proposals never see the light of day. Unfortunately, a small minority still slip through the net. The remainder of this article considers what happens if they do.

The statutory basis for challenging a CVA

Once approved, section 6 of the Insolvency Act 1986 (IA) provides that an aggrieved creditor can only challenge the decision to approve a CVA if:

a) the CVA *unfairly prejudices* the interests of a creditor, member or contributory of the company[1]; and/or
b) there has been some *material irregularity* at, or in relation to, either of the meetings of creditors and members.[2]

Where the court is satisfied that either of these two grounds is made out, it may revoke or suspend the approval of the CVA and/or give a direction for the summoning of a further meeting of the company's creditors to consider any revised proposal the company may make or, in a case of material irregularity, to reconsider the original CVA proposal.

Crucially, any creditor who was aware of the CVA, and who wishes to make a challenge, only has 28 days in which to do so, beginning on the day on which the chairman's report of the CVA meetings was filed at court. If a creditor misses this statutory deadline, the Insolvency Act equivalent of a 'snooze you lose' clause, it is generally too late to do anything about the CVA proposal, no matter how unfair the creditor considers it to be.

What constitutes material irregularity?

Mann J's judgment in *HMRC* v. *Portsmouth City Football Club & Anor* includes a useful summary of the current law in relation to challenging CVAs. When looking at the question of what amounts to 'material irregularity', Mann J emphasised the fact that both elements must be established – irregularity and its materiality. Any challenge on this basis will therefore fail if it can be shown that the outcome of the meeting would have been the same, even if the alleged irregularity had not occurred.
In practice, while there are other, more extravagant, grounds on which material irregularity challenges have been made (for example where creditor support was

obtained by means of secret payments or creditor claims had been fabricated) material irregularity challenges tend to fall into two broad categories.

1) The first are challenges based on the admission and valuation of claims, with the challenging creditor alleging either that the chairman incorrectly excluded or incorrectly valued their vote or that they, or others who would have opposed the CVA, did not receive proper notice of the meeting and therefore did not submit claims.

"It is, however, not enough to establish mere prejudice; the prejudice must, as noted in the *Powerhouse* judgment, be both unfair and disproportionate…"

A recurring theme in this context is that of arguments surrounding the chairman of the meeting's discretion to value contingent or unliquidated claims under insolvency rule 1.17(3), which provides that such claims 'shall be valued at £1 unless the chairman agrees to put a higher value on it.' This discretion, combined with the various potential approaches to discounting to reflect the uncertainties inherent in such claims, can often form the basis of an allegation that an opposing creditor's claim was incorrectly valued, preventing them from blocking a proposed CVA.

2) The second main area of challenge is where the alleged irregularity is the non-disclosure or inaccurate disclosure of material information, the question in such cases being whether there was a substantial chance (meaning that it was more likely than not) that creditors with that information would not have approved the proposed CVA (*Re Trident Fashions (No 2)* [2004] 2 BCLC 35). The key problem facing a creditor running a material irregularity argument on this basis is that of proving that they would not have supported the CVA (and would potentially have preferred liquidation) had they known the relevant information. In many cases, the reality is that the creditor would have been much less enthusiastic in its support, but that it would, despite this, have supported the CVA anyway, as long as it was still the best available recovery option.

While it is not unusual for an unhappy creditor to allege the occurrence of a material irregularity as part of their argument, most recent high-profile challenges to CVAs have been largely based on allegations of unfair prejudice.

What now amounts to unfair prejudice?

A creditor who is asked to accept something short of their full entitlement in the relevant circumstances will, at a basic level, always be prejudiced. It is, however, not enough to establish mere prejudice; the prejudice must, as noted in the *Powerhouse* judgment, be both unfair and disproportionate.

As identified in Mann J's summary of the current law in the *HMRC* v. *Portsmouth City Football Club & Anor*, a number of key principles have emerged from recent case law when considering what amounts to unfairness. The first two of these were specifically considered earlier this year in the *Miss Sixty* case:

- When considering whether or not any disadvantage resulting from the CVA is unfair, it is relevant to consider both vertical comparisons (comparing the CVA with the outcome of a liquidation) and horizontal comparisons (comparing the position of the dissenting creditor with other creditors).
- In relation to any horizontal comparison, the fact that creditors were treated differently is something that calls for close scrutiny, but any differential treatment does not automatically make the CVA unfair. There may well be valid economic reasons why differential treatment is necessary or desirable in order to enable the debtor to continue its business.
- When considering the results of a vertical comparison, if creditors in >>

general, or a specific class of creditors, stand to receive less in the proposed CVA than they would have done in a liquidation, the CVA is likely to be regarded as unfair: *Re T&N Ltd* [2004] EWHC 2361 (Ch).

- Any such vertical comparison cannot, however, be conducted on the basis of speculation as to what other better deals might have been available. Unless the court is satisfied that a better compromise or outcome would actually have been available, it can only compare that which was proposed with no compromise at all – *Sisu Capital* v. *Tucker* [2005] EWHC 2170.
- Any unfair prejudice must come from the terms of the CVA itself. Section 6 IA cannot be used where, for example, the unfairness complained of resulted from the misconduct of other creditors.

What is also clear from existing case law is that a CVA is not *automatically* unfair simply because a creditor or group of creditors might have been better protected by a scheme of arrangement, in which they could have voted as a class to block the scheme. Parliament has deliberately offered two different cram-down procedures and provided protection for creditors under each, giving the debtor a choice as to which to use. It is, however, difficult to see how a court would not be influenced to some extent, when considering an unfair prejudice application made by a creditor or group of creditors, if it became apparent that those making the proposal had chosen the CVA implementation option in order to deprive those creditors of the protection that would otherwise have been available to them under a scheme.

A specific type of unfairness? – guarantee stripping

The *Powerhouse* and *Miss Sixty* cases have generated considerable commentary, as in both cases it was held that a CVA could validly provide for the release of third party guarantees provided in respect of claims being compromised in the CVA. This has potentially placed the onus on any creditor losing the benefit of a guarantee to go to court, and to establish that the CVA proposal containing such guarantee stripping was disproportionately unfair to them.

While a similar guarantee-stripping outcome could be achieved under a scheme, the key difference between a scheme and the position in a CVA is that those losing the benefit of guarantees would normally be expected to be placed in a separate voting class for the purposes of approving the scheme, and would thus be able to block the scheme proposal by a simple vote, without the need for further court involvement.

The *Powerhouse* and *Miss Sixty* cases were both relatively exceptional on their facts. Each CVA was also found to have unfairly prejudiced those who stood to lose their guarantee. In *Powerhouse*, such unfairness was demonstrated by the facts that (i) landlords were not adequately compensated for the loss of their ability to claim on a guarantee provided by an apparently solvent listed entity (they received the same as those who had no guarantee), (ii) other creditors were being paid in full and (iii) the landlords were overall worse off than they would have been in a liquidation.

Similarly, in *Miss Sixty*, the CVA was found to be unfairly prejudicial as, *inter alia* (i) the CVA only imposed a compromise on four landlords, with all other creditors being paid in full, (ii) those landlords were not adequately compensated for the loss of their ability to claim on a guarantee provided by an apparently solvent parent company and (iii) another creditor in a broadly analogous position was not asked to accept any compromise.

The key point emerging from these cases is that, as pointed out by Henderson J in *Miss Sixty*, while a CVA might validly provide for guarantee stripping, there has been no reported case of a CVA fairly removing a creditor's claim against a clearly solvent guarantor. By way of contrast, in *Re Primlaks UK Ltd (No.2)* [1990] BCLC 234, a creditor who had effectively lost the benefit of a guarantee was held not to be seriously prejudiced where the guarantor had few assets.

What is the real CVA approval threshold?

Where does this leave the target voting thresholds for a CVA? It is arguable that the real CVA creditor approval threshold may actually be 75 per cent in value of the total creditors present in person or by proxy and voting, *with a clear majority of the prejudiced creditors voting in favour of the CVA*, unless those voting against include more than 50 per cent in value of the company's total unconnected creditors.

Why? Simply because, if the 75 per cent threshold is expected to be satisfied, the main focus will be on the possibility of an unfair prejudice challenge. If it can be shown that a clear majority of the prejudiced creditors (assuming that each was offered the same deal) actually supported the CVA, the prospects of a successful challenge to a CVA should recede significantly – it becomes much harder for a judge to conclude that a proposal is disproportionately unfair to a group of creditors if a clear majority of those prejudiced have already made an informed decision to support that 'unfair' CVA proposal.

What does the future hold – more or less court involvement?

The recent CVA related decisions in *Powerhouse*, *Miss Sixty* and *Portsmouth City FC* have provided useful guidance as to the approach that the courts are likely to adopt when creditors attempt to involve them in the CVA process by claiming that a CVA was unfair. It is to be hoped that clearer judicial guidance in this area, and the reminder in the *Miss Sixty* case of the duties of office-holders considering CVA proposals, will head off commercially unreasonable CVA proposals and thus reduce the amount of court involvement in CVAs going forward.

Court involvement in CVAs is something that keeps returning in different guises. The most recent is the current Insolvency Service consultation on proposals for a restructuring moratorium, which envisages a possible court hearing where a moratorium is sought in relation to a proposed CVA, attended by the company's creditors, at which the court would consider whether the CVA proposal had a reasonable prospect of being approved. Any such hearing could potentially give creditors the opportunity to involve the court at an earlier stage, and on a more extensive basis, than is currently the case. Court involvement in CVAs looks, despite the probable intentions of the Cork Committee, to be an unavoidable fact of life. ☐

> "It is arguable that the real CVA creditor approval threshold may actually be 75 per cent in value of the total creditors present in person or by proxy and voting, *with a clear majority of the prejudiced creditors voting in favour of the CVA*, unless those voting against include more than 50 per cent in value of the company's total unconnected creditors."

1 Section 6(1)(a)

2 Section 6(1)(b)

Tony Bugg (far left) and Jo Windsor (left) are partners at Linklaters LLP.

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Recent case summaries

Corporate and international insolvency update from Ben Griffiths.

Corporate insolvency

***Re Leyland Printing Co Ltd* (in administration) [2010] EWHC 2105 (Ch)**

Facts: The applicant company entered administration in 2002. Owing to the length of the administration, the claims of almost all the company's creditors became statute-barred while the company was in administration. The administrator sought directions as to whether he should accept the claims of creditors that were statute-barred.

Held: The making of an administration order under the pre-Enterprise Act 2002 regime did not stop time from running for the purposes of the Limitation Acts (see *Re Maxwell Fleet and Facilities Management Ltd* [1999] 2 BCLC 721 and *Re Cosslett (Contractors) Ltd* [2004] EWHC 658 (Ch)). A creditor whose claim is statute-barred can prove in the administration only with the consent of those creditors and members whose position would be adversely affected if his proof were to be allowed.

The position is different in the case of a liquidation. Time ceases to run upon the making of a compulsory winding-up order as liquidation involves the imposition on the available assets of the company of a statutory scheme of rateable division among the company's creditors (*Re Cases of Taff Wells Ltd* [1992] BCLC 11). In contrast, in the case of an administration under the pre-Enterprise Act regime, the administrator has no power to distribute the company's assets and thus no equivalent scheme arises.

The judge therefore directed the administrator to reject the creditors' claims. He acceded, however, to the administrator's request to be permitted, before concluding the administration, to contact all the company's shareholders and invite them to consent to the admission to proof of the statute-barred claims.

Comment: The effect of the decision in *Re Leyland Printing*, as the judge recognised, was to give an 'expected windfall' to the company's shareholders and arguably to produce 'an unfair result'. Nonetheless, the judge considered himself bound by principle and authority on the point. The court has no general power in these circumstances 'to do justice according to the merits of the case'.

In respect of post-Enterprise Act administrations, administrators do have power to distribute the company's assets. It is therefore arguable that time should cease to run for limitation purposes in such cases as it does on a winding up. However, the judge expressed no view on this issue in *Re Leyland Printing*.

Thus the safest course for creditors of any company in administration, whether under the pre- or post-Enterprise Act regime, continues to be to bring protective proceedings where their claims may become statute-barred. The permission of the administrator or the court will be required for proceedings to be instituted (eg Insolvency Act 1986, sch. B1, para. 43(6)).

International insolvency

***Rubin & Lan (Joint Receivers and Managers of The Consumers Trust)* v. *Eurofinance SA and others* [2010] EWCA Civ 895**

Facts: TCT was a trust company settled for the purpose of carrying on a sales promotion scheme in the United States. Under the scheme, participating merchants in the US would offer customers a cashable voucher promising a rebate from TCT of up to 100 per cent of the purchase price. In practice, customers had to navigate such a complex process in order to recover the rebate that few customers ever succeeded in doing so. Claims were brought against TCT in the US under consumer protection legislation.

Subsequently, proceedings in respect of TCT were instituted under Chapter 11 of the US Bankruptcy Code and the applicants were appointed as TCT's legal representatives. Proceedings were then brought by the applicants in the US Bankruptcy Court against the respondents for the recovery of monies paid to them by TCT (the US proceedings). The respondents deliberately chose not to submit to the jurisdiction of the US court or to defend the US proceedings and default judgment was entered against them (the US judgment).

The applicants, as the legal representatives of TCT, applied to the English Companies Court seeking to have (i) the US proceedings recognised as a foreign main proceeding under the UNCITRAL Model Law on Cross-Border Insolvency and (ii) the US judgment enforced against the respondents in this jurisdiction.

Held: The Court of Appeal held that the US judgment was a judgment in and for the purposes of the collective enforcement regime of the US Chapter 11 proceedings. Insolvency proceedings for the purposes of the Model Law include the mechanisms for dealing with transactions at an undervalue and preferential transactions (under IA 1986, ss 238–239), and thus the equivalent provisions under US law that allow for proceedings against third parties for the collective benefit of all the creditors of the debtor. The US proceedings were therefore to be recognised as a foreign main proceeding under Article 17 of the Model Law.

Recognition of a foreign insolvency proceeding by the English court generally carries with it the active assistance of the court, including the enforcement of judgments made in the foreign proceeding. It would not be unfair to uphold the US judgment in this case as the respondents had been aware of the claims against them and had chosen not to participate in the US proceedings. The US judgment would therefore be enforced by the English Court as a matter of common law.

Comment: As a general principle insolvency proceedings, whether personal or corporate, should be both unitary and universal (*Cambridge Gas Transportation* v. *Navigator Holdings Plc* [2007] 1 AC 508 and *Re HIH Casualty and General Insurance* [2008] 1 WLR 852). The effect of the general principle in this case was that the US proceedings were governed not by the ordinary private international law rules but instead by the *sui generis* private international law rules relating to bankruptcy. Accordingly, the US judgment could be enforced by the English court notwithstanding the fact that the respondents were not subject to the jurisdiction of the US court under ordinary private international law rules.

The Court of Appeal's decision in this case forms part of the current trend of increasing judicial co-operation and comity in cross-border insolvencies. ☐

Ben Griffiths is a barrister at Erskine Chambers.

Technical update

Moratoriums and employee consultations are discussed and R3's suggestions outlined.

Moratoriums and employee consultations are two hot topics that merit a closer look. The former seeks to strengthen our rescue culture; the latter has the potential to destroy it.

Moratoria

Recently the government consulted on a scheme to allow all companies to seek the protection of a moratorium without necessarily entering into an insolvency process. The scheme envisaged that a qualifying company could apply to the court for a moratorium of three months while it sought agreement to either enter into an informal arrangement with its creditors, or to propose a CVA or a scheme of arrangement. The moratorium would be on the public record and no action could be taken against the company without the leave of the court. It was further envisaged that the moratorium would be overseen by a monitor, who would be an IP. The monitor would have two roles: advising the court as to whether or not the company satisfied the conditions at the outset and then monitoring the company's progress.

There would be no limit to the size of the company that could apply, but certain types of companies, such as banks, would be ineligible. Two qualifying conditions were proposed:

- the company must be able to demonstrate that there is a reasonable prospect that a compromise or arrangement can be agreed with its creditors; and
- the company must be able to show that it is likely to have sufficient funds to carry on its business during the moratorium.

In its response, R3 supported the idea of the moratorium, but counselled caution regarding the role of the monitor. It would seem to be reasonable for the monitor, in effect acting as an expert witness, to advise the court as to whether or not the applicant company qualified for a moratorium. It was difficult to see, however, that a role that would involve responsibility for what was done without the power of control could be an acceptable risk for any practitioner unless the monitor had statutory protection from any liability. For this reason, R3 took the view that the monitor's role should be restricted to acting as an expert at the outset. Creditor protection during the moratorium would be achieved by the directors having a responsibility to the monitor, with sanctions for failing to do so. Creditors would also be able to go to court where it became apparent that the terms of the moratorium were being breached.

R3 also raised the issue of continuing supply under existing contract terms. Faced with a company subject to a moratorium, existing creditors alerted to the company's difficulties, if only by the very fact of the moratorium, may seek to vary their terms of supply with a view to recouping their potential or actual losses. Unchecked, this would represent a flaw in the moratorium process that *in extremis* could lead to failure. It must therefore be desirable for contract terms to be maintained. S233 of the Act provides the precedent although its existing scope appears to be too limited to deal with current complex trading arrangements.

> "R3 took the view that the monitor's role should be restricted to acting as an expert at the outset."

R3's other concerns surrounded the terms of the qualifying conditions. The first seemed to require the views of major creditors to be obtained before the moratorium was in place. R3 thought that this would remove a principal purpose of the moratorium, which is to allow the company to consult creditors without suffering a damaging response. For this reason, R3 thought that the first qualifying condition should be restricted to there being a reasonable prospect that a compromise or agreement can be formulated for presentation to creditors.

With regard to the second condition, R3 thought that as well as having sufficient funds to carry on business, a moratorium should be likely to benefit or at least not prejudice the interests of unsecured creditors as a class.

Employee consultations

Under employment rights legislation, where there are 20 or more employees at an establishment, an employer must consult with its employees when it intends to make employees redundant or otherwise vary employment contracts. Unless there are specific circumstances, a failure to consult leads to a protective award of up to 90 days' pay. An award will not be made where there are special circumstances. Case law has determined that insolvency is not a special circumstance.

In the recent case of *Mr CJ Byrne* v. *Nortel UK Limited (in administration)* the employment tribunal made it clear that consultation should be a process of ascertaining views possibly resulting in a change of plans. At paragraph 28 of the judgment:

> *'At the employee forum meeting of 18 June 2008, the purpose of the meeting was to allow the joint administrator to present and discuss the actions to be taken and to provide the employee representatives with an opportunity to raise questions. The tribunal takes the view that this was not a meaningful consultation but it was an attempt to give information to the employees through the representatives about the redundancies. This was no consultation in the sense that it had any chance [of] altering the path which the administrators had set upon.'*

A similar line was adopted in *Unite & Others* v. *Nortel Networks UK Limited (in administration)*, an industrial tribunal case in Northern Ireland. At paragraph 39 of the judgment:

> *'…the English cases stress the need for genuine consultation. In the present context, genuine consultation means consultation that fulfils all of the following requirements:*
> *1) there must be consultation when the relevant proposals are still at a formative stage*
> *2) the consultee must be provided with adequate information upon which to respond*
> *3) the consultee must be given adequate time in which to respond*
> *4) the consultor must engage in conscientious consideration of the response to consultation.'*

In some cases it is possible to imagine that the administrator might be able to consult properly but in the majority of cases funds are likely to be limited and meaningful consultation impossible. It follows that the administrator has no option but to break employment law.

The tribunal viewed such a breach seriously. At paragraph 30 of the judgment:

> *'The duty of the administrator to protect the interests of creditors has to be carried out within the law; the duty to protect creditors' interests does not give the administrator any fiat to ignore legal obligations that might impact on the financial interests of the creditors.'*

In ch7 s32 of his book, Pollard (*Corporate Insolvency: Employment and Pension Rights*) refers to various cases

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involving claims for special circumstances. Unfortunately, 'the likely futility of consultation [was] not a special circumstance' (*Iron and Steel Trades Confederation* v. *ASW Holdings PLC (in administrative receivership)*).

No consideration was given to the impossibility of consulting. The argument might run something like this: real consultation could not be undertaken because there was little or no money and redundancies were inevitable; therefore consultation could not be meaningful. This impossibility of consultation amounts to special circumstances. Absent the acceptance of this argument, or the treatment of formal insolvency proceedings as special circumstances, it seems inevitable that in many cases administrators of companies with 20 or more employees will find themselves breaking the law; a wholly unsatisfactory state of affairs.

There is clearly a tension between insolvency law and employment law that needs to be addressed, but which, to date, government seems reluctant to acknowledge. However, this tension exists not only at a UK level, but also at an EU level. The obligation to consult arises by virtue of EC directive 98/59/EC, the collective redundancy directive, which makes no express provision for insolvency. At the same time, the European Commission wants to encourage the rescue of viable businesses. See, for example, the paper on entrepreneurship referred to in this column in the summer 2008 edition of *RECOVERY*. More recently, DG Enterprise has been conducting a research project on rescue procedures as part of an EU project on financial restructuring of financially distressed firms. There are signs that the Commission is prepared to take note of issues that act as an impediment to business rescue: witness the amendments made to the acquired rights directive designed to mitigate its effects in insolvency proceedings (the implementation of which in the TUPE regulations 2006 was unfortunately rather unsatisfactory). Perhaps the conflicts caused by the consultation requirements should be drawn to the Commission's attention? ☐

> "There is clearly a tension between insolvency law and employment law that needs to be addressed, but which, to date, government seems reluctant to acknowledge. However, this tension exists not only at a UK level, but also potentially at an EU level."

Giles Frampton (pictured) is a partner at Richard J Smith & Co and John Francis is the technical director at R3.

Legal Q&A

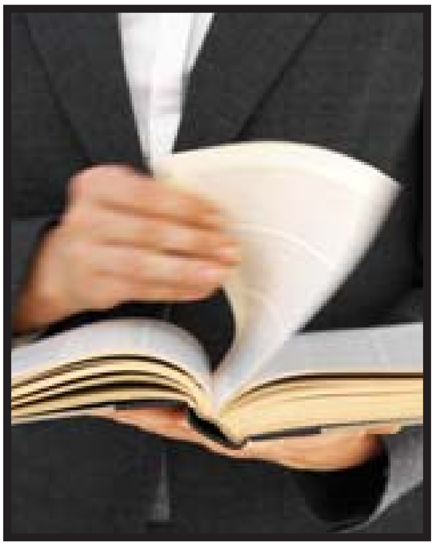
James Hyne answers your insolvency queries.

I have agreed to accept an appointment as administrator. While I am satisfied that the statutory purpose of the administration is reasonably likely to be achieved, I am aware that the company has already filed a Notice of Intention to Appoint an administrator on form 2.8B, which has elapsed as the proposed purchaser of the business has not yet been able to secure funding. Can the directors lodge a further Notice of Intention to Appoint?

The decision of the Birmingham District Registry in *Re Cornercare Limited* [2010] EWHC 393 (Ch) demonstrates that paragraph 28(2) of schedule B1 of the Insolvency Act 1986 does not prohibit the filing of further Notices of Intention to Appoint (NOITAs) under paragraph 27(1). Paragraph 28(2) sets out that an appointment may not be made under paragraph 22 after the period of ten business days beginning with the date on which the NOITA is filed under paragraph 27(1). In *Cornercare*, His Honour Judge Purle QC considered the effect of paragraph 28(2) to be that no appointment may be made after the period of ten business days had expired *in relation to that particular notice* but paragraph 28(2) does not prevent a further NOITA from being served and filed, which would consequently provide a further ten business days within which to appoint an administrator.

In *Cornercare*, the court also considered the potential for abuse in circumstances where a continuing interim moratorium is engineered by the repeated filing of NOITAs. In this circumstance, the court expressed that it had adequate powers to deal with such a situation; for example, if a creditor complains or makes representations to the court and the court considers repeated notices to be an abuse, the court may consider a variety of sanctions such as ordering the restraint of filing of further NOITAs, or even, in an extreme case, declare a specific NOITA (and the associated moratorium) to be invalid. Although the judgment did not comment on further penalties, it is feasible that the court could also make an adverse costs order (*prima facie* against the directors who lodged the various NOITAs, but possibly against any professionals who advised the directors to pursue such a strategy with no genuine intention to appoint an administrator).

In summary, if there is a genuine reason as to why an appointment of an administrator was not made pursuant to a NOITA within the prescribed time limit for doing so (and a buyer suffering genuine delays in obtaining funding was considered a legitimate reason in *Cornercare*) then a second NOITA should not be problematic. A less compelling reason, or the filing of numerous NOITAs, is far more likely to constitute an abuse.



> "If there is a genuine reason as to why an appointment of an administrator was not made pursuant to a NOITA within the prescribed time limit for doing so… then a second NOITA should not be problematic."

I am a trustee in bankruptcy who has been appointed over an individual's estate. I have become aware that a final charging order was granted by the court after the date of the presentation of a bankruptcy petition. The creditor with the benefit of the final charging order is alleging that they are secured and should be paid in priority to other unsecured creditors. Are there any grounds to challenge the final charging order?

In the recent case of *Nationwide* v. *Wright* [2009] EWCA Civ 811, the Court of Appeal restated that the date of the bankruptcy order triggered the commencement of the bankruptcy for the purposes of section 278 Insolvency Act 1986 (IA 1986) ie the date of the vesting of the debtor's assets. Under the IA 1986, dispositions between the presentation of the bankruptcy petition and subsequent bankruptcy order are not capable of being avoided under s284 IA 1986 in relation to a recipient acting in good faith, for value and without notice of the petition.

The crucial question is, therefore, whether the creditor and/or the court were aware of the impending bankruptcy petition at the time of the hearing when the charging order was made final. If the creditor is aware of the petition and a final charging order is subsequently made, the charging order is susceptible to being set aside under s284 IA 1986.

In *Nationwide*, an interim charging order was made in order to secure a judgment. Prior to the date of the hearing to make the charging order final, a bankruptcy petition was presented against the debtor. It was common ground that neither the court nor Nationwide knew of the pending petition. The judge granted the final charging order.

The debtor's trustee in bankruptcy applied to discharge both the interim and final charging orders. The trustee's application was successful at first instance. The court's reasoning was that while the charging order was properly made, it had a statutory discretion whether to permit an application to set aside the charging orders.

The Court of Appeal disagreed with this analysis; a person who deals with a party in good faith before a bankruptcy order, and who has received no notice of that petition is entitled to retain the security they have acquired. The court stated that if the creditor or judge hearing the final charging order was aware of the petition, the proper course of action would be to adjourn the final charging order hearing. In such a case, the creditor would not have had the benefit of the final charging as at the date of the bankruptcy order. ☐

James Hyne is head of Corporate Recovery & Insolvency at Charles Russell LLP.

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The Independent Commission on Banking

Tony Anderson outlines the issues relating to current banking practices and the options the Independent Commission on Banking is considering.

On 16 June 2010 the Chancellor of the Exchequer, George Osborne, announced that Sir John Vickers would be chairing the Independent Commission on Banking. While the Commission is charged with formulating policy recommendations on a number of issues, the majority of media interest has been focused on whether the retail and commercial arms of global banks should be formally separated from their investment banking arms.

Fundamental flaws in the global banking system

There has been much emotive rhetoric concerning the role that banks and shadow banks may have played in the global financial crisis, and with due reason. A combination of cheaply available debt, complex and poorly described tradable instruments and a dangerously short-term rewards culture, fuelled unprecedented levels of leverage globally. When the financial crisis occurred it exposed fundamental flaws in global banking systems and market regulations, as well as the inappropriate risk weighting of balance sheets. The tightened regulation and the capital and liquidity requirements currently being proposed globally will continue to reduce significantly the amount of debt previously available to financial institutions and their customers.

There is political mileage to be gained in such a scenario that engenders a culture of apportioning blame arbitrarily without considering the individual behaviour of the protagonists, many of whom weren't banks. For example, while banks generically have been under the microscope for their role in the crisis, little attention has been focused on their shareholders and their demands for positive short-term results. What also must be acknowledged is that none of the banks operating in the UK that went into administration operated a combined model of retail and investment banking. These banks (as well as numerous other participants including hedge funds, insurers and building societies by way of example) were allowed to participate in risky investments such as securitised US sub-prime mortgages based, in several instances, on short-term borrowing. The spiralling loss of value on these investments as the crisis continued resulted in refinancing risk and the subsequent runs suffered by some of these entities.

During the crisis it also became apparent that what became known as systemically important financial institutions (SIFIs) had been pursuing risky strategies on the assumption that, due to their size and global interconnectedness, they would be deemed 'too big to fail' by their respective states and receive the benefit of an implicit guarantee from the taxpayer, should it be required.

It was not necessarily the structure of the institutions involved but the investment activities within which they were participating that created many of the dilemmas now faced by the wider economies throughout the world. It is more constructive to consider the full list of the objectives that the Independent Commission on Banking is being asked to consider rather than solely the breaking up of the retail and investment banking model, which has garnered the most press mileage and emotional response.

The role of the Commission

The Commission's principal terms of reference require it to make recommendations promoting stability and competition in banking, while having regard to the government's wider goals of financial stability and creating an efficient, open, robust and diverse banking sector. It has been asked to pay specific attention to the potential impact of its recommendations on financial stability, lending to UK consumers and businesses and the pace of economic recovery, consumer choice, the competitiveness of the UK financial and professional services sector and the wider UK economy, and the risks to the fiscal position of the government.

In its Issues Paper, released in September 2010, the Commission acknowledged that competition and financial stability are not necessarily harmonious.

The Commission also has a number of reform options available to it relating to the structure of banks and to the structure of markets. These include in the case of banks:

- separation of retail and investment banking;
- narrow banking and limited service banking;
- limits on proprietary trading and investing;
- structural separability 'living wills' and resolutions schemes;
- contingent capital; and
- structure-related surcharges.

The initial four reform options proposed for banks are drafted with a view to either reducing the use of banks' balance sheets (including deposits on receipt) or to separate their functions. The limits on proprietary trading are similar to the Volcker Rule adopted under the US regulatory reforms in the Dodd-Frank Act. Contingent capital considers the automatic conversion of debt to capital upon the reaching of a critical point. Contingent capital instruments or 'co-cos' have already been issued by several institutions in the marketplace. Similarly, surcharges or bank levies have also been imposed.

The reform options available in the case of markets include:

- measures to reduce market concentration
- market infrastructure reform.

The struggle to ensure a level playing field

The Commission has stated that the market concentration reform could, in principle, block a merger on the grounds of market stability, even where it had been approved by the competition authorities.

Much has already been said in the press about market infrastructure proposals for securities to be traded through a central counterparty, rather than over-the-counter, with a view to reducing counterparty risk.

While it is clear that the structure of banking participants is one of the key focuses of the Commission, there are several other areas that it will be investigating. As with the regulation of any sector with global participants, the difficulty will be ensuring that, where global banks may be operating, any measures imposed by the Commission are replicated on similar terms to ensure a level playing field.

Responses to the Issues Paper were due by 15 November 2010. The Commission is due to report with its recommendations by the end of September 2011. □

Tony Anderson is a partner in the Financial Institutions Group at Pinsent Masons.

Where to go for funding?

Neal Judd sounds out banking and finance professionals on sources of funding.

The current market conditions have made it very challenging for small businesses and mid-market companies to access financing and this is likely to remain the situation in 2011. Traditional lenders, concerned at their exposure levels, are tightening their belts and their prevailing attitude to risk is putting the squeeze on firms seeking vital funding.

So where can a business owner turn to for finance at this time?

It is a sweeping generalisation to say that banks are not lending. They are still lending to their most creditworthy, established clients; and they are, of course, open to the 'right' new lending opportunities. In fact the issue, as the banks see it, is that there is much less demand for lending, 'This year market-wide demand for lending remains subdued with recent SME surveys pointing to only nine to ten per cent of businesses currently seeking finance,' according to Andy Mason, regional commercial director at HSBC.

So, if not a traditional bank, then where can a business owner go?

The independent asset finance houses (at least, those that do not have their own problems) are very much open for business, and are taking over facilities from the traditional banks. Even these independent houses, however, are being more cautious – partly spoilt for choice, but equally keen to avoid repeating past mistakes.

As Jeff Greenfield, business development director at Centric Commercial Finance explains, 'Today, companies are looking to the independent asset-based lending sector for much needed liquidity and turning to their assets to release working capital. Increasingly, these businesses are seeking access to a higher level of funds than their current traditional facilities allow, delivered with greater velocity and flexibility.'

At the core of an asset-based lending facility is invoice discounting, which provides an immediate injection of cash and ongoing working capital to create headroom for the business. Specific loan to value ratios are attributed to stock, plant and machinery, and property to create a total funding programme. With asset-based lending, additional cash-flow funding is available for those businesses with stronger profit generation.

So once a business owner has raised finance by selling on their securable assets, where else can they then turn to access further finance?

> “At the core of an asset-based lending facility is invoice discounting, which provides an immediate injection of cash and on-going working capital to create headroom for the business.”

Equity financing options

We now move away from the world of debt finance and into the sphere of equity finance. This necessitates consideration of certain fundamental issues, such as who has control of the business, and how does the equity investor make an acceptable return.

First, let's summarise the range of options available:

- friends and family
- high net worth, angel investors
- government initiated funds
- Venture Capital Trusts (VCTs)

Friends and family

Friends and family are very often a quick and easy source of finance. However, unless the business owner is lucky enough to be particularly well connected, this option tends to be limited to small amounts. There is also the problem that the investor is unlikely to properly understand the risks, nor add any commercial value to the business.

Angel investors

High net worth (HNW), or angel investors, have increasingly become a major source of finance for small businesses. HNWs are incentivised to make investments by the attractive tax benefits available, in particular, through the Enterprise Investment Scheme (EIS), which provides the investor with a range of tax benefits, including:

- an instant 20 per cent credit against their income tax for the year of, or the year preceding, the investment;
- capital gains tax rollover from gains

made in the previous three years to the date of the investment and 12 months following the investment; and
- on disposal, in the event of a gain being realised, the gain should be exempt from capital gains tax.

Relief from inheritance tax under the business property rules is also available for investors holding shares in an unlisted company, which means that the shares would not be taxed by inheritance tax on the estate of the owner, thereby saving 40 per cent tax at current rates.

It must be pointed out that there are, of course, detailed rules relating to these reliefs, for eligibility for both the investor and the business, and personal circumstances will also determine whether these reliefs apply.

> “The income tax relief available for VCTs allows 30 per cent credit against an investor's income tax for the year.”

High net worth investors are likely to be experienced in growing businesses, and have varied connections that will be beneficial to the growth of the business. However, as we are dealing with individuals, the strengths and weaknesses of each HNW investor will vary considerably.

It is imperative that a business owner takes the time to get to know their investor before consummating a transaction, properly understands their motivations, and takes detailed references, just as they would with a new employee. The Dragons' Den-style confrontation over a deal is, I'm pleased to report, not all that common in the real world, but clearly careful consideration must be taken over the legal form of the relationship and the detailed terms.

The government

The government has for a long time been active in small company investments by seeking to alleviate the equity gap that it is felt exists above the threshold of most HNW investors and below that of the institutional equity investor.

Central government has introduced and part-funded many initiatives in recent years, both regionally and nationally, to allocate capital to small, growing businesses. Most often, this is done by tendering out management of small funds to professional venture capital managers, and setting strict investment criteria to focus the funds, in particular, in terms of amounts invested per transaction.

- **Capital for Enterprise Fund**
  One recent, highly publicised initiative was the £70 million Capital for Enterprise Fund that was managed by Maven Capital Partners and Octopus Ventures. This fund was a direct response to the issues being suffered by small businesses during the credit crisis, and was aimed at businesses struggling to obtain traditional bank finance or those that were over-reliant on debt.

  This fund has now closed to new opportunities, Maven Capital Partners having invested their £35 million allocation in seventeen companies during 2009–2010. There is discussion of a repeat fund for 2010–2011 but as yet no formal announcement, so for now this option has been closed.
- **Growth funds**
  Another example of a government-initiated fund is the Catapult Growth Fund, a £30 million venture capital fund established to provide capital for expanding businesses, and funded, in part, by central government. The initial equity requirement available is between £500,000 and £2 million, available to all revenue generating businesses from early stage through to development capital, as well as transactions such as MBOs and MBIs. Their sector focus is a generalist approach, but with innovative growth sectors favoured, including technology, healthcare, medical devices, environment and support services.

  As Richard Bucknell of Catapult Venture Managers comments, 'In the absence of adequate security, lending for entrepreneurial growth businesses can be hard to come by. If there's anything the credit crunch has taught us, it must be that high leverage is not the most solid of foundations on which to grow and that longer term, committed equity could be a more appropriate solution. Refinancing of excessive bank debt, along with an injection of new money to fund growth can be the answer for established businesses that have stalled without the necessary working capital, while earlier stage enterprises can also benefit from venture capital investment where proven concepts demand additional financing to deliver on significant potential.'
- **RDA funds**
  The Regional Development Agencies (RDAs) have historically been delegated the function of managing small, local funding initiatives. With the announced demise of the RDAs across much of the country, there remains a lot of uncertainty as to what will happen to this important source of funding.

  Where monies have already been allocated to third party managers, it is likely that these allocations will be fully utilised and their management contracts honoured. A recently established government entity, Capital for Enterprise Limited, is expected to become the umbrella manager of all government funding initiatives, from the Enterprise Finance Guarantee (EFG) scheme for bank finance through to the local equity funding facilities.

Venture Capital Trusts (VCTs)

Another tax vehicle for investors, the VCT tax reliefs are similar to the EIS scheme. However, the income tax relief available is more generous, allowing a larger 30 per cent credit against an investor's income tax for the year.

Each VCT is listed and managed by a professional, FSA-registered fund manager, who receives an initial fee plus an ongoing annual fee. The manager will lay out their investment criteria in small unquoted companies to prospective investors, and market their funds to those individuals looking to allocate their annual allowance of up to £200,000 to VCT investments.

The expectations of an investor in a VCT fund, and therefore of the fund manager, are for high returns in exchange for the higher risk. The result is that the investment criteria set by VCT managers are extremely rigorous, and the restrictions placed on the business owner are often considerable.

As Ned Dorbin of Maven Capital Partners, a VCT fund manager, summarises, 'Maven's funds are looking to invest in businesses with a demonstrable track record and a credible strategy for growth.'

The VCT market has a large amount of capital at its disposal and time limits in which its investments must be made, so they are very much looking for new opportunities and actively taking stakes in high growth businesses.

As Ned explains, 'We understand that the current trading climate is difficult for many companies but we continue to be open for business to maintain our active rate of new investments.'

Future funding

The climate for funding businesses is going to remain tough for a while yet. There are clearly many sources of funds available to a business owner, but each has their strict criteria that need to be met, and most funders are spoilt for choice, so they can afford to be very selective.

It is imperative, therefore, that a business owner is properly equipped before they approach funders, of whatever form, because even a small failing in their preparation can make the difference between a successful outcome and a polite decline. ☐

Neal Judd is a director at NA Judd Corporate Finance.

What happens when a bank or building society gets into trouble?

As joint building society special administrator of Dunfermline Building Society, Mike Pink was one of the first to make use of the supplementary legislation for the Banking Act 2009.

We all saw, and still suffer from, the wave of insolvencies of financial institutions that occurred in the UK between 2007 and 2009. What lessons have been learned from that and how might the regulators tackle similar problems in the future?

Lessons learned

From the 'run' on Northern Rock in 2007, through to the bail-outs at RBS and Lloyds/HBOS in 2008, the UK authorities (the Financial Services Authority (FSA); Bank of England (BoE); and HM Treasury (HMT)) found that they lacked the tools to intervene decisively at an early stage to resolve problems at an institution. General insolvency law could only be initiated at the point of insolvency, which is often too late, and the objectives of an administrator or liquidator do not strictly accord with the authorities' desire to ensure continuity of key banking services.

Yes, the authorities could still work behind the scenes on finding a 'private sector' solution – be it a capital injection, a takeover, a merger or partial sale – or provide liquidity support either publically or confidentially. But these all take time, and may not always be viable solutions.

Confidence is a key issue. Any trouble at a financial institution that becomes public can quickly lead to that trouble being amplified: depositors will take their funds elsewhere and trading counterparties will, at the very least, demand collateral or security – if they trade at all. Liquidity and balance sheet solvency can evaporate.

The Banking Act 2009

With the objective of improving the prospects of maintaining stability and confidence in the UK financial markets, the Banking Act 2009 introduced the Special Resolution Regime (SRR) for UK incorporated deposit takers (banks, building societies and credit unions – I'll use 'bank' hereafter generically to apply to all three). This includes UK subsidiaries of foreign banks, and overseas branches of UK banks.

With new powers and responsibilities the BoE, working with the other authorities, could now act incisively before an institution becomes insolvent. These new powers are only to be used as a last resort, but enable the BoE to effect a transfer of shares, property *and* liabilities of a failing bank or building society to a (willing) third party. In practice this means it can seek to preserve the bits that it wants (eg depositors, banking services, mortgage lending, etc) as a 'good bank' by separating them from the bits that are not working (eg under-performing loans, contingent and other liabilities), which can be left behind in a 'bad bank' to be wound down or dealt with without impacting on market stability.

Two new insolvency procedures were also introduced to ensure the co-operation of the insolvency office-holders in delivering a successful resolution: the bank insolvency process (BIP) and the bank administration process (BAP). The BIP is akin to a liquidation, with the aim of a rapid payout of its creditors, while the BAP is akin to a trading administration or admin receivership if there is a business to continue.

In a resolution the BoE can transfer shares using a share transfer instrument (STI) or assets and liabilities using a property transfer instrument (PTI) to a private sector purchaser (PSP), to a bridge bank (owned by the BoE), or to temporary public ownership (TPO) (under the control of HMT), or a combination of them. The PSP option will generally be the preferred solution and the TPO option the last, as the PSP offers a market-led solution while the other two will necessarily require a further transaction in the future (eg IPO or sale).

For the resolution to result in a transfer to a PSP, the BoE will probably have held an auction of the distressed business. Any auction will be at very short notice, to a tight deadline, with limited opportunity for the bidders to conduct diligence – probably between 12 and 48 hours, maximum. The auction will be followed by the issuing of a PTI or STI. The main objective is likely to be to ensure that the depositors and other essential banking services are protected through a transfer to a 'viable' institution; whether other assets or liabilities transfer is of secondary importance. Consequently, a successful bid may involve taking on of more liabilities (eg the depositors) than assets – any shortfall being balanced by a cash 'dowry' from HMT. HMT will then have a subrogated claim against the estate of the distressed bank in place of the liabilities that were transferred by the PTI. Whether the remains of the distressed bank then go into a BAP or BIP will depend on circumstances.

The trigger for a resolution will typically be the FSA determining that the distressed bank no longer meets the 'threshold conditions' to retain its authorisation. At this point, the BoE can take action under the SRR as described above.

> "Confidence is a key issue. Any trouble at a financial institution that becomes public can quickly lead to that trouble being amplified."

Dunfermline Building Society

The resolution at Dunfermline occurred less than six weeks after the Banking Act 2009 (the Act) came into effect, and only hours after the relevant supplementary legislation was passed that extended the Act to cover building societies and Scotland! However, it demonstrated that the new SRR could work, effecting a solution without harming depositors or impacting the banking system. It is likely to be a model for future resolutions.

The Dunfermline resolution involved a partial transfer of assets and liabilities to a PSP (Nationwide Building Society) and a smaller partial transfer of other assets and liabilities to a bridge bank. The residual Society, which retained a portfolio of loans and floating rate notes as its primary assets, was placed into building society special administration (BSSA). The special administration has been used to manage the run-off or eventual sale of these remaining assets.

In effect, the BoE was able to deliver a good bank/bad bank split as described above. It avoided a cash-out of depositors and the potential 'run on the bank' scenes previously seen at Northern Rock. It avoided disruption to the payment and other banking services that the Society's customers were dependent on.

> "The resolution at Dunfermline occurred less than six weeks after the Banking Act 2009 (the Act) came into effect, and only hours after the relevant supplementary legislation was passed that extended the Act to cover building societies and Scotland!"

Future developments

The regulatory framework and political environment for the banking sector are dynamic and will continue to change, particularly as a result of international developments. Regulation has been tightened and supervision increased. Banks are required to hold more capital as a buffer against shocks and future losses. There is a requirement for each of the major banks in the UK to write their own Recovery and Resolution Plans (RRP also known as a 'living will'), that will summarise all key economic functions in the bank, how they would respond in various crisis scenarios, and how their business could be broken up into its economic functions along the lines of a resolution as described earlier.

While the Dunfermline 'model' works well for a UK domestic-only deposit-taking bank, it is less clear how a truly global and complex business such as the former Lehman Brothers would now be addressed under the Banking Act. Much thought is being put into this, with a further Treasury consultation on the special administration regime for investment firms having been issued at the end of September (note that this goes beyond just banks – Lehman Brothers in the UK was not in fact a bank). That bankruptcy has demonstrated the enormous complexity and legal uncertainties that exist in relation to property rights when dealing with trading and derivative products and client assets in a cross-border environment. Cutting through that complexity to deliver stability and avoid systemic failure is likely to prove challenging at least for the immediate future. However, there is also a Banking Commission review in progress that is looking at the structure of the banks themselves (see article by Tony Anderson on page 17). Some experts have argued that a true separation of investment banking and retail banking is essential to protect retail depositors from the risks inherent in the investment banking model. Whether this will ever happen only time will tell. In the meantime, look out for the next BIP or BAP. ☐

Acronyms at a glance

BAP	bank administration process
BIP	bank insolvency process
BSSA	building society special administration
HMT	HM Treasury
IPO	initial public offering
PSP	private sector purchaser
PTI	property transfer instrument
RRP	recovery and resolution plan (living will)
SRR	Special Resolution Regime
STI	share transfer instrument
TPO	temporary public ownership

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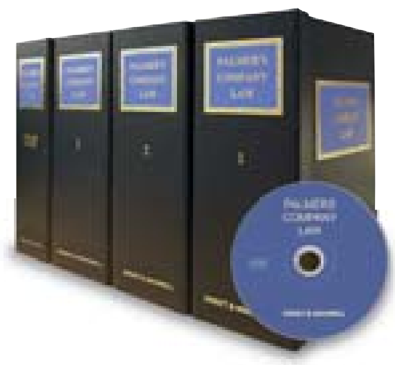


NAMA makes waves as it gets into its stride

Neil O'Keeffe sets out the progress of NAMA in acquiring the loan books from the Irish banks and the impact generally expected in Ireland and the UK.

The collapse of the Irish real estate market is now quite stark. It still reverberates beyond our domestic shores around Europe affecting sovereign debt yields, macro economic policy, and is affecting certain real estate sectors within the UK. On the ground, the Irish National Asset Management Agency (NAMA) is in the throws of acquiring the real estate loan portfolio of the Irish participating institutions and blood has only recently been spilled in the Irish courts with the first legal challenge to NAMA and NAMA's first judgment against a real estate developer.

The establishment of NAMA

NAMA was established by the Irish National Asset Management Agency Act, 2009 and commenced operations on 22 December 2009. Loan facilities of the participating institutions with an aggregate nominal book value of approximately €77 billion to €81 billion were identified as eligible assets on account of being secured by 'development land' (€49 billion) or being associated loan facilities (€28 billion) with a breakdown per institution of: Anglo Irish Bank €28.4 billion, Allied Irish Banks €24.1 billion, Bank of Ireland €15.5 billion, Irish Nationwide €8.3 billion and EBS €0.8 billion. The geographical spread of the development lands were 66.8 per cent in Ireland, 20.7 per cent in Great Britain, and 6.2 per cent in Northern Ireland with the balance spread between the United States and continental Europe.

Eligible assets

The eligible assets are to be acquired over five tranches with haircuts being applied depending on the fall in the value of secured property and any legal flaws in security. As of the end of October 2010, tranche 3 with an aggregate nominal value of €12 billion was recently transferred. NAMA has already made data available in relation to the first two tranches set out in the table.

The extent of the discounts or haircuts is quite unexpected and the reality is that where banks suffer losses on foot of loan/value haircuts applied by NAMA, the Irish state has had to make up the capital adequacy in the same banks by pumping tier 1 investments into the banks. Accordingly, over the course of the summer months the international sovereign debt markets have become increasingly concerned about the extent of Ireland's bank bailout and the lack of certainty surrounding future NAMA haircuts that would require additional capital adequacy investment. The concern prompted the Irish minister for finance to announce a number of changes to the NAMA project. Allied Irish Banks and Bank of Ireland are not now going to transfer loan facilities where the exposure to the relevant 'sponsor connection' is below €20 million (the previous threshold was €5 million), which will instead continue to be held on those banks' balance sheets. Furthermore, Nationalised Anglo Irish Bank is about to transfer all of its remaining eligible assets to NAMA in a composite valuation with detailed due diligence to occur post transfer on a clawback basis. The other participating institutions are to complete their transfers before year end. This approach is intended to give more certainty to the losses incurred by the participating institutions.

NAMA's eligible assets include loans by the participating institutions to UK businesses even if the land and property developments are solely within the UK. It is

"NAMA's eligible assets include loans by the participating institutions to UK businesses even if the land and property developments are solely within the UK."

Participating institution	Nominal value of loans acquired	Value of securities exchanged for loans	Discount	Discount %
Allied Irish Banks	€2.73 billion	€1.40 billion	€1.32 billion	48.5%
Bank of Ireland	€1.82 billion	€1.13 billion	€686 million	37.8%
EBS Building Society	€35.9 million	€19.3 million	€16.6 million	46.4%
Irish Nationwide Building Society	€591 million	€163 million	€428 million	72.4%
Anglo Irish Bank	€6.75 billion	€2.57 billion	€4.18 billion	61.9%
Total Tranche 2	€11.9 billion	€5.28 billion	€6.63 billion	55.6%
Total Tranches 1 & 2	€27.2 billion	€13 billion	€14.2 billion	52.3%

important to appreciate that the eligible assets will be assigned to NAMA based on the legal principle that a person cannot give what they do not own, *nemo dat quod non habet*, so that NAMA is in effect stepping into the shoes of participating institutions. Consequently, NAMA cannot simply set aside the terms of the underlying documentation – this is particularly so outside of the Republic of Ireland where the NAMA Act has no statutory authority. Thus the fundamental nature of the UK borrowers' financing arrangements should be unaffected.

Critical to the NAMA business plan is that the eligible assets include performing as well as non-performing loan facilities and also captures those loan facilities of associated debtors of the primary sponsor connection. In such a way, NAMA can capture the loan facilities to a particular family, their connected persons, their co-ownerships/partnerships, their special purpose vehicles and sometimes their trading entities and in doing so NAMA can take a holistic approach to each sponsor connection, reduce the risk of competing secured creditors and then extract as much value as is possible from them.

> “While social policy experts are clambering for reform of the Irish bankruptcy laws there is surely an opportunity here for insolvency practitioners in the UK.”

NAMA is being challenged

Currently in the Irish High Court, Paddy McKillen is challenging the authority of NAMA to forcibly acquire his loans from participating institutions, claiming that the reputational damage of being a NAMA 'client' will prejudice the sale and operations of his businesses and their ability to refinance elsewhere. Commentators, however, take the view that Mr. McKillen's initial contractual consent to the assignment of the loan facilities together with various constitutional provisions and indeed public policy concerns will prevent his challenge being successful.

Within two month of having their loan facilities transferred to NAMA, the various sponsor connections are required to submit detailed business plans for assessment and approval by NAMA and its external team of financial analysts. If a particular business plan is accepted then NAMA has indicated that it will restructure the facilities to reflect the business plan. If, however, no feasible business plan is forthcoming NAMA has already threatened debtors that it will move to enforce against them. On 11 October 2010, NAMA obtained its first summary (uncontested) judgment for €280 million against Landmark Enterprises Limited and for €82.5 million (aggreg) against Paddy Shovlin, Anthony Fitzpatrick and Patrick Fitzpatrick on foot of personal guarantees. Over the past year or so high-profile developers, Liam Carroll and John Fleming among others, have sought to restructure their businesses through examinership (a process similar to administration) but failed to do so and have gone into liquidation on account of the realities of the real estate markets. On that basis it would seem likely that NAMA will be faced with more enforcement than restructuring activity.

Sophisticated 'clients' of NAMA are now very conscious of the harsh bankruptcy laws for individuals here in Ireland and are running for cover by forum shopping for bankruptcy. The most obvious example of such stringent laws is the contrast between the one-year period for discharge of a bankrupt in the UK and the 12-year period in Ireland. Many well known developers now officially reside and have the centre of their operations in the UK, Switzerland or elsewhere, and only on 18 October 2010 the ex-CEO of Anglo Irish Bank, David Drumm, filed for bankruptcy in Massachusetts as opposed to Ireland. While social policy experts are clambering for reform of the Irish bankruptcy laws there is surely an opportunity here for insolvency practitioners in the UK.

If a sponsor connection has their business plan accepted by NAMA then a detailed workout will be put in place. Under the relevant legislation, NAMA can advance up to €5 billion in working capital and other facilities. NAMA has, to date, made available €40 million in working capital facilities to the sponsor connections on its loan book and the market commentators indicate that such funding has merely been made available on an asset preservation (as opposed to enhancement) basis until decisions are made on whether to approve a particular sponsor connection's business plan.

Implications for the UK

NAMA, therefore, has significant implications for any UK company or any UK associated debtor that meets the criteria of an 'eligible bank asset'. As in Ireland, until there is visibility as to how NAMA is dealing with the various sponsor connections and their secured properties, the full implications for the UK are not widely understood and significant uncertainties remain. Among all the speculation, we wait to see how aggressive NAMA will be with non-compliant debtors; how unencumbered assets will be treated in a workout; how much pain it will bear in a workout (if any); what margin will be applied by NAMA; to what extent will capital repayments have to be made at the outset; whether fees may be generated by performing debtors providing expert services to operate other assets of NAMA; how credit underwriters will perceive a NAMA credit facility; how difficult will NAMA clients find it to refinance elsewhere; as a government agency, how quickly will NAMA make decisions in a fast-changing market; how will NAMA deal with competing creditors; how will NAMA act in a syndicate with non-NAMA lenders; will REITS or other form of IPO be used to create liquidity in NAMA assets; and will NAMA sell debt-pieces to vulture funds or other institutional investors. Clarity on the situation would be extremely welcome but, like any cautious credit committee, NAMA is likely to approach each sponsor connection on a case-by-case basis.

In a research note on 13 April 2010 Capital Economics stated that it believes NAMA's impact on the British real estate market will be minimal simply because of the scale of its €20.7 billion British portfolio. Time will tell whether this view is correct. While NAMA has made assurances that it is a long-term workout vehicle, it bought the eligible assets based on long-term economic values, as opposed to current market values, and consequently NAMA already has ground to make up. Furthermore, this issue is exacerbated by the adoption of valuation dates for tranches that are some months prior to their transfer to NAMA in a falling market (eg 30 November 2009 for tranches 1 and 2 that were transferred in March 2010 and June 2010 respectively). On that basis, and bearing in mind the fiscal and political imperative for NAMA to perform quickly, it is fair to say that the more the Irish real estate market falls in value or stays somewhat illiquid then NAMA will be forced to sell its better performing assets in the UK.

Currently, there is a lot of gazing into crystal balls to assess the implications in Ireland and in the UK. What is certain, however, is that the participating institutions have now crystallised their losses on their mid- to large-cap real estate development loan books and, with that immediate objective achieved, focus will turn to the real estate developers themselves. The phoney war with developers is therefore coming to an end and no wonder people are jockeying for position. ☐

Neil O'Keeffe is a partner in the Banking and Financial Services department of LK Shields Solicitors, Dublin.

Lehman Brothers International (Europe) (in administration): client money conundrum

Unwinding Lehman Brothers International (Europe) is complex. The article explains why it is so involved and what is happening.

The collapse of Lehman Brothers sent shockwaves through the financial services sector in September 2008, sorting out the aftermath is still an on-going process.

A major issue to be resolved is the question of exactly what constitutes client money. The questions relating to client money issues are the subject of a court application by Lehman Brothers International (Europe)'s (LBIE) administrators. When the administrators were appointed in September 2008 LBIE held approximately US$2.16 billion in segregated client funds. Approximately US$1 billion of this was held with a German affiliate, which is the subject of formal insolvency proceedings in Germany. The segregated funds are also subject to competing claims from clients and affiliates who claim they should have been treated as segregated clients. The result has been the diminution and potential dilution of the segregated funds so that even clients whose money was, or should have been, segregated from LBIE's own funds will almost certainly suffer a substantial loss.

The current model, which has to be determined by the court, exists despite detailed legal and regulatory rules providing for the protection of client money, by the segregation from LBIE's own money and assets. In theory, the proper segregation of money and assets should protect clients on the basis that these segregated assets will not form part of the estate of the insolvent company; they should be easy to identify and straightforward to return to the clients. In practice, the failure by firms to properly implement segregation and reconciliation requirements, together with weaknesses in the regulatory rules and the investment firms' own internal procedures for dealing with client money often means that there would rarely be sufficient funds to fully repay clients. The recent court decisions have shown that where there is a shortfall in available funds, the courts are unlikely to order the topping up of the shortfall by ordering a transfer of the company's own house funds into the client account to satisfy segregated client claims. The theory of the protective regime and what happens in practice are worlds apart. The Lehman collapse has clearly demonstrated that it is not enough to assume that investment firms will adhere to the rules.

"The theory of the protective regime and what happens in practice are worlds apart. The Lehman collapse has clearly demonstrated that it is not enough to assume that investment firms will adhere to the rules."

The client money framework

The regulatory obligations on firms to segregate and protect client money and assets are derived at a European level from the Markets in Financial Instruments Directive (MIFID) and its implementing directive. MIFID requires firms to protect an investor's ownership rights in respect of securities and funds entrusted to the firm and keep those securities and funds separate from the firm's own securities and funds. The directive requires adequate arrangements to be made to safeguard clients' rights and detailed organisation of requirements are imposed. However, the obligation to segregate is not absolute and carve outs are provided for. Where a client transfers funds or assets to a firm, (eg as financial collateral) on terms that ownership is transferred for the purpose of securing or otherwise covering present or future, actual, contingent or prospective obligations of a client towards the firm, the funds or assets transferred do not need to be segregated.

The obligations under MIFID are enacted under the UK regulatory system in the FSA's Client Asset Sourcebook (CASS). The rules relating to client money are contained in chapter 7 of CASS.

The requirements of MIFID are also subject to local insolvency and property laws that are not harmonised at European Union level and are implemented in different ways across Europe. In the UK, MIFID requirements have been implemented through a statutory trust, so that a firm receives and holds client money as trustee. In order to comply with its obligations as trustee, a firm will hold money in a client account separate from its house accounts in which it holds its own funds. The insolvency of the investment firm will constitute a pooling event under chapter 7 of CASS so that the funds held in all of the firm's client accounts will be pooled and distributed to clients according to their client money entitlements. To the extent that there is a shortfall on available pool funds, payments to clients will be pro-rated.

Problems with the UK framework

Although the UK framework may appear rigorous, there are various complexities and uncertainties in the way in which the UK rules operate. In the event of the insolvency of the investment firm, eg LBIE, what in theory should be straightforward can in practice be complex and uncertain.

The use of the statutory trust as opposed to the simple segregation requirement gives rise to uncertainty as to both the meaning and effect of the trust and which particular funds the trust applies to. These uncertainties mean clients whose funds have not in fact been segregated can seek to assert a claim to segregated funds or to extend the trust to non-segregated funds held in the insolvent firm's house accounts. The position is further complicated by the fact that the UK rules provide investment firms with two options to comply with their obligations to protect client money: the 'normal approach' and the 'alternative approach'. Under the normal approach a firm is required to pay client money promptly, and, in any event, no later than the next business day after receipt, into a client bank account. Under the alternative approach, client money is received by a firm into its house account. A reconciliation may be performed on the next business day with any funds required to top up the client bank being transferred from the house account. Segregation under the alternative approach takes place on a net basis rather than separately in relation to each amount of client money received. A client whose funds are paid into the firm's house account under the alternative approach assumes the credit risk of the firm pending transfer of the funds into the client account.

> "The CMP is not limited to the segregated accounts, it includes client money in the firm's house accounts and it is the administrators, not the claimants, who are obliged to identify client money in the firm's house accounts."

The LBIE client money application

The administrators' application for directions on a number of issues highlighted the complexities of dealing with the repayment of client money following the insolvency of an investment firm. These issues related to: (i) identifying what money constituted the client money pool (CMP); (ii) what money the statutory trust should apply to; and (iii) who was able to share in the distribution of the CMP. Certain clients of LBIE claimed that they should be treated as segregated clients and LBIE had failed to segregate money for them. Issues arose as to whether the shortfall on LBIE's client money should be topped up with LBIE's own funds so that the segregated clients would receive back 100 per cent, or nearly 100 per cent, to the detriment of the unsegregated clients and LBIE's general unsecured creditors.

LBIE's failure to properly segregate client money had several causes including: (i) it did not segregate money for its affiliates; and (ii) routinely treated as its own money deriving from OTC derivatives transactions with its clients, regardless of the terms of business agreed with those clients.

LBIE used the alternative approach and so received client money into its house accounts, which were subject to the Lehman Group liquidity management process. Funds were swept daily from LBIE's house accounts to its parent company in the US. This sweeping of funds would likely defeat any proprietary claim to those funds by the clients from whom they were received.

The High Court found that while the trust attached to all client money from its receipt by LBIE (regardless of whether the money was properly segregated), where a client's money was not properly segregated, that money did not form part of the CMP to be distributed to clients. Although LBIE's failure to segregate effectively meant that there was a huge shortfall in the CMP, the court found that there was no obligation, either under the CASS rules or otherwise, to top up the CMP from LBIE's own funds or from identifiable client money held in LBIE's house accounts.

Given the number of parties involved and the differing arguments and positions, it was no surprise that the judgment was appealed.

The Court of Appeal judgment

The Court of Appeal was asked to consider four questions:

1) Is the CASS 7 statutory trust created on receipt of client money or its segregation?
2) Is the CMP limited only to client money in segregated accounts?
3) Do clients have the right to claim in the CMP on a claims basis or a contributions basis?
4) When does money which the firm owes to a client become client money?

The Court of Appeal judgment overturned the original judgment on two issues:

- The CMP is not limited to the segregated accounts, it includes client money in the firm's house accounts and it is the administrators, not the claimants, who are obliged to identify client money in the firm's house accounts.
- Claims against the CMP are on a claims rather than a contributions basis.

It upheld the original judgment on two other issues:

- The CASS 7 statutory trust is created on receipt of client money by LBIE, not at the point of segregation.
- Client money does not include money payable to a client by the insolvent firm but which had not been appropriated prior to administration (eg by segregation).

Three parties, including the administrators, have now sought permission to appeal directly from the Supreme Court. The administrators' concern is that the Court of Appeal's decision will require them to carry out an extensive and time consuming exercise to identify client money in LBIE's house accounts, which will significantly delay the final distribution from the CMP. They are also concerned that the obligation on them to trace identifiable client money in the house accounts to contribute to the CMP will be a complex exercise that will significantly increase the costs of the administration. They will also require further court directions before any distribution of client money can be made. If the Supreme Court grants leave to appeal a hearing is not likely until mid-2011. □

Arun Srivastava (far left) is a partner and head of the Financial Services Group at Baker & McKenzie LLP and Martin Gray (left) is a senior associate in the Restructuring & Insolvency Group at Baker & McKenzie LLP.

Court gives blessing to Halliwells' pre-packs

This high-profile case may well have implications for future funding of law firms by banks.

Pre-packs approved by court

Over the summer, the High Court gave its blessing to four pre-pack sales in the high-profile administration of Halliwells LLP (Halliwells), which became the first UK top-50 law firm to enter into insolvency. The case follows a line of authority starting with *DKLL Solicitors* (2007) EWHC 2007 (Ch) and more recently *Hellas Telecommunications (Luxembourg) II SCA* (2009) EWHC 3199 (Ch) where the courts have expressly given the administrators liberty to enter into pre-pack administration sales. These cases mark a departure from the general position of the courts, which is that the merits of a pre-pack sale are ordinarily for the administrator himself to deal with and the creditors can challenge any decision if they feel sufficiently aggrieved.

Background

Halliwells was a national law firm providing a range of legal services, with 116 partners and over 600 employees and offices in Manchester, Sheffield, Liverpool and London. Halliwells had entered into a number of property leases that had left it with onerous payment obligations to landlords. The burden of these rental payments, a fall in revenue caused by the departure of a number of partners and a drop in turnover occasioned by the economic climate left Halliwells facing insolvency. Also, in the background, was a highly controversial property transaction involving the firm's equity partners and the firm's new headquarters at Spinningfields in Manchester. The collapse into administration was even more dramatic as during the boom years the firm's rise had been meteoric, culminating in 2007 with a turnover of £82.2 million and profits per equity partner of £550,000.

By the spring and summer of 2010, however, the position was very different and on 20 July 2010, Halliwells together with Shay Bannon and Dermot Power of BDO Stoy Hayward (the proposed administrators) made an application to court for an administration order, the appointment of the proposed administrators, and for the court's approval of four pre-pack sales of parts of the business of Halliwells. A pre-pack administration of the whole business was the only alternative as the Solicitors Regulation Authority (SRA) would have ordered an intervention into the firm in the event of liquidation and the trading of such a large practice in administration was not a viable option.

The proposed administrators had quickly formed the view that Halliwells could not be rescued as a going concern and that it was not reasonably practicable to achieve the objective of a better result for Halliwells' creditors as a whole than would be likely if it were wound up without first being in administration. They concluded that the only way forward was to realise the assets of Halliwells by means of various sales in order to make a distribution to the secured creditor, the Royal Bank of Scotland plc (the bank).

> "The purchasing firms were keen to ensure that the transferring members were not at risk of bankruptcy."

The application marked the end of the marketing of Halliwells' business undertaken over the course of the previous three months. The proposed administrators quickly discovered that there were not many potential purchasers for a large national law firm. Negotiations were conducted with eight different law firms and these generated four proposed sales which, in the opinion of the proposed administrators, represented the best return available for Halliwells' creditors. The four purchasing firms were Hill Dickinson, Kennedys, Barlow Lyde & Gilbert and HBJ Gateley Waring. Hill Dickinson was to acquire the firm's Liverpool office and the non-insurance part of the Sheffield office. Kennedys was concluding a previous agreement to purchase the insurance part of Halliwells' Sheffield office. Barlow Lyde & Gilbert was picking up the insurance part of Halliwells' Manchester office, leaving HBJ Gateley Waring with the remainder of the business.

Court intervention

It was initially intended that the proposed administration would be an out-of-court appointment. Two notices of intention to appoint administrators were filed on a rolling basis to protect Halliwells' assets principally from landlords' action against the Manchester, Sheffield, Liverpool and London offices while the sale negotiations were taking place. The decision was, however, taken to apply to the High Court for an administration order because the proposed administrators wished for a court order to accept their appointment in light of the protracted nature of the negotiations, the imminent expiry of the second notice period and their wish to seek the approval of the court for what were unusual proposed sales.

Halliwells' largest single creditor was the bank, which was owed approximately £18 million, which was increasing each month. The debt was secured by way of a debenture. As the projected return from the sales of the various parts of Halliwells' business was significantly less than £18 million it was clear that, on the basis of the bank debt alone, Halliwells was also insolvent on a balance sheet basis.

Protection of members' practising certificates

As with any law firm, the members of Halliwells were also significant stakeholders. The members had nearly £13 million of capital invested in Halliwells, most of it funded through individual partnership practice loans (PPLs). The members had taken out these PPLs through various banks (the PPL providers) and Halliwells had undertaken, through the Halliwells' members' deed, to repay each member's PPL when such member ceased to be a member of Halliwells. Also, Halliwells had given direct written undertakings to the PPL providers regarding payment of the members' PPLs. Given that Halliwells was insolvent, it was unable to honour these undertakings, which would leave the members personally liable to repay their PPL providers. As law firms are essentially people businesses, the purchasing firms were keen to ensure that the transferring members were not at risk of bankruptcy because of their personal liabilities under the PPLs. This is particularly relevant for a law firm as, if a solicitor is declared bankrupt, his practising certificate is automatically suspended.

The four pre-packs

In the case of each of the four asset sale agreements, the purchase price consisted, wholly or partly, of the proceeds of Halliwells' debts and work-in-progress, which the purchasing firms would endeavour to collect and pay over to Halliwells. In the case of two of the agreements, the proceeds were to be paid in part to Halliwells, and in part into a trust over which Halliwells would be the trustee for the benefit of the PPL providers, the transferring members and the purchaser. In the case of the third, the transferring members would have the benefit of a covenant from the purchaser that the PPLs would be taken over. The reason for these arrangements was that in each of these three cases, the purchasing firms made it clear that if the deals were to proceed they wanted to ensure that the transferring members did not become bankrupt by reason of their obligations under the PPLs. The purchasers were not prepared to risk the fact that some or all of the transferring members may no longer be able to practise as solicitors.

Importantly, the bank had provided a letter confirming that it was content that part of the monies received from three of the four purchasers should be used for the purpose of repaying the PPLs of relevant transferring members and acknowledged it was driven out of necessity in order to maximise returns in the administration. The preferential creditors were to be paid in full. Further, the unsecured creditors were to receive the maximum prescribed part payment of £600,000. A key point of contention was that there were Halliwells' members (past or present) who were unsecured creditors of Halliwells and did not transfer as part of the four sales and they would remain liable under their PPLs and would therefore be at risk of bankruptcy. The court felt that the payment of monies to satisfy the PPLs of the transferring members was undoubtedly a preference and the transferring members were treated differently to the leaving members but it was a necessary evil to achieving those sales.

The judge noted the comments made by His Honour Judge Cooke in the case of *Re Kayley Vending Limited* [2009] BCC 578 that in exercising its discretion in pre-pack cases, the court must be alert to see, so far as it can, that the procedure is at least not being obviously abused to the disadvantage of creditors and for that purpose the court is likely to be assisted by the provision of (at least) the information required by SIP 16. A draft SIP 16 report was provided to the court that contained a detailed explanation of why it was not appropriate to trade Halliwells and offer the business for sale as a going concern in the administration, full details of the marketing process and a complete explanation of the terms materially affecting the consideration paid. The judge said that he was satisfied that the proposals were SIP 16 compliant and that there was no evidence of any abuse of the process and that the pre-packs were in fact the only way forward.

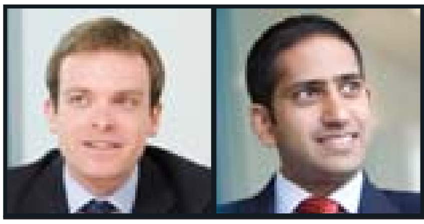
The judge made the administration order, appointed the proposed administrators as administrators and blessed the four pre-pack sales. The judge said that he recognised that his order permitted the administrators to enter into sale contracts, which required them to apply substantial amounts of the consideration received for the purpose of paying down PPL obligations ahead of the bank, and to that extent, repaying the capital of the transferring members. In all the circumstances the judge concluded that despite the unusual nature of the sale contracts they did not unnecessarily harm the interests of the creditors as a whole.

> "Lenders will obviously be concerned that members' PPLs may be paid in priority to them in the event of a pre-pack administration sale."

Conclusion

The case will provide some comfort to insolvency practitioners that in certain circumstances the courts will bless pre-pack administration sales. Although the unusual nature of the case means that it is unlikely to be seen as a departure from the court's normal approach that in the majority of cases the decision is one for the administrator and the making of an administration order should not be taken as the court's blessing of a pre-pack sale.

The case is going to have wide-ranging implications in relation to how banks fund law firms in the future and lenders will obviously be concerned that members' PPLs may be paid in priority to them in the event of a pre-pack administration sale. It will undoubtedly cause lenders to review their exposure to professional practices and one fears that Halliwells may not be the last significant law firm to be placed into administration. □



Steven Cottee (far left) is a partner and Bhaljinder Mander (left) is a senior associate in the Corporate Recovery team at Lawrence Graham LLP.

The new Bribery Act: should you care?

Richard Saunders suggests that businesses need to understand how the new Bribery Act affects their dealings with clients and put into place effective procedures.

The Act outlined

Should businesses be concerned about the stipulations as detailed in the forthcoming legislation? The short answer is yes. The Bribery Act 2010 (Act), which comes into force in April 2011 is a serious attempt by government not only to bring the law on bribery up to date but also to broaden the reach of the UK authorities over corporate activity both within the UK and abroad.

The Act is short. It has only 15 sections. Those that are of particular relevance are section 1, which deals with the offence of bribing another person; section 2, which deals with the offence of being bribed; and, most importantly from the corporate point of view, section 7, which is the offence of failing to prevent bribery. I will primarily focus upon this last section. Of particular concern for many is the thorny issue of corporate hospitality. Can that be seen as a bribe? Unfortunately the answer to this question is – it depends.

Section 7 provides that a commercial organisation (not just a company) can be guilty of an offence if any person associated with it whether in the UK or abroad (ie not only employees but also agents, consultants or subsidiaries) bribes another person intending either to obtain or retain business for the organisation or obtain an advantage in the conduct of its business. This is a strict liability offence for the organisation and the consequences can be severe. The guilty individual can receive up to ten years in prison and an organisation can received an unlimited fine and also debarment from competing for public contracts.

> "The guilty individual can receive up to ten years in prison and an organisation can received an unlimited fine and also debarment from competing for public contracts."

What are adequate procedures?

The only defence that the Act permits is if the organisation has put in place 'adequate procedures designed to prevent persons associated with the organisation from undertaking such conduct'. Thus the burning question is – what are adequate procedures? The Act is not particularly helpful on this and guidance from the Ministry of Justice was only published on 14 September 2010. This guidance sets out six broad management principles to assist organisations in deciding what procedures to put in place. They are:

1) Risk assessment – the organisation will regularly assess the nature and risks relating to bribery.
2) Top level commitment – the board or its equivalent must establish a culture within the organisation in which bribery is never acceptable.
3) Due diligence – organisations must look at any party with whom they do business.
4) Clear practical and accessible policies and procedures – these must take account of the roles of the whole of the workforce from the board down.
5) Effective implementation – this will ensure that the development of policies and procedures become embedded throughout the organisation.
6) Monitoring and review – the organisation must have in place mechanisms to ensure compliance with policies.

The problem with this is it is not a one size fits all approach. Organisations will need to communicate their policies effectively to their suppliers and agents both in the UK and abroad and seek adherence to these policies. It may well be that it becomes a contractual term that all parties must sign a declaration of anti-bribery compliance.

Payments that oil the wheels are not allowed. Such facilitation payments are, however, permitted by certain jurisdictions, including the USA, and that in itself could cause problems. It is possible that an agent abroad making such payments is not committing an offence there but the UK-based organisation could be liable. It is to be hoped that prosecutors will take a sensible view in relation to this but that cannot be guaranteed.

Anti-bribery policies and training must form part of internal structures. Companies must be flexible and active in ensuring they put into place adequate procedures and that they are adhered to by everyone it deals with.

What constitutes acceptable hospitality?

Of course one major concern is corporate hospitality. The guidance from the Ministry does not assist particularly on this issue. However, to be a bribe any such hospitality must have been given to induce that individual to perform a function improperly and there must be an intention for a financial or other advantage. Common sense, perhaps, should be the way to approach it. The higher the expenditure or the more lavish the hospitality provided, the greater the risk will be that it will be inferred to have been intended to influence the individual to perform their function improperly. It is to be hoped, however, that again the prosecuting authorities accept that corporate hospitality and promotional expenditure are a fact of everyday business life. As such, so long as the procedures are in place to ensure that all such activity is monitored and a legitimate business case for it can be provided, then one would hope that would be sufficient. However, that cannot be guaranteed.

Thus, what can we conclude? Organisations must ensure that they understand their own business and whom they deal with; and they must take active steps throughout their organisation to put into place, apply and monitor anti-bribery policies. The Act does not expect perfection. So long as procedures are in place and an organisation follows them as well as it can then that should be enough to avoid any prosecution. The problem is, that at this early stage, one simply does not know what the prosecutors will wish to do. Time alone will tell. □

Richard Saunders is a non-practising barrister at Moon Beever solicitors.

HMRC's Business Payment Support Service

Gordon Smith outlines how HMRC's Business Payment Support Service is keeping the UK in business and safeguarding the public purse.

Companies that are temporarily unable to pay their tax debts can ask HM Revenue & Customs (HMRC) for extra time to pay by contacting the Business Payment Support Service (BPSS). The BPSS can grant a 'time to pay' (TTP) arrangement to cover PAYE, National Insurance, Corporation Tax, VAT or any other HMRC taxes.

HMRC has always been able to agree time to pay. But in November 2008 it set up a new service to make TTP more accessible, and to provide viable businesses in temporary financial difficulties with a streamlined, cost-free source of help.

The starting point is that if a business is unable to pay its tax, it must be viable and able to meet its future tax obligations. Arrangements are made for the shortest period necessary to allow a business to get back up to date with its tax.

BPSS was introduced in response to the deteriorating economic conditions and HMRC has no plans to withdraw the service. It believes that the BPSS has been successful in helping businesses in genuine but temporary financial difficulty, and gets them back up to date with their taxes.

Businesses need to get in touch with HMRC before payment is due. Provided they do so, if HMRC agrees TTP, a business will not be charged late payment penalties or surcharges. It will, however, have to pay interest in the normal way.

During the first 15 months of the service alone, more than 200,000 businesses, large and small, rescheduled more than £5.2 billion in tax. The businesses spanned a wide range of industries – from retail, tourism, transport and leisure to farming, manufacturing, construction and engineering. New figures are now available on the website: http://www.statistics.gov.uk/hub/economy/government-receipts-and-expenditure/taxes-and-revenue/Business Payment Support Service.

Criteria for time to pay

In the majority of cases, HMRC aims to make a very quick decision, typically over the phone, within around ten minutes. But in making a decision, HMRC will also look at:

- the amount of money involved and the risk of not being paid;
- the timescale requested; and
- the previous compliance of the customer.

In some cases, HMRC may need to ask for more information. The longer the repayment period, the larger the risk posed to the Exchequer. All TTP arrangements should be as short as possible, typically within one to three months, but HMRC may allow businesses up to a year.

The timescale is measured from either the date the business makes a TTP request or the due date for payment – whichever is the later.

Large tax debts

The larger the debt, the larger the risk it poses to the Exchequer. For large tax debts (over £1 million) new rules came into effect in April 2010. This means that businesses with large tax debts may now be asked to provide, at their own expense, an independent business review (IBR) in support of their request to reschedule payment.

Businesses that are asked to provide an IBR must expect to pay from £10,000 for a simple review to £50,000 for a more complex case; but the cost is usually small in relation to the size and turnover of the business and the benefits that will accrue by securing HMRC's ongoing support.

Protecting the public purse

IBRs were introduced to help HMRC decide on the most suitable method of payment for each company and how best to address those businesses that are unlikely to survive even with the help of a TTP agreement. IBRs help HMRC protect the public purse to fund vital public services.

The reviews also help ensure HMRC's actions do not distort competition within the marketplace. It guards against granting extra time to pay to a business that is able to pay in full, as well as to a business that is likely to fail anyway. IBRs are not a mechanism for denying companies time to pay.

> "The IBR must be carried out by a qualified professional advisor such as an accountancy firm or an insolvency practitioner."

An IBR typically includes details on a company's current trading and financial position; profit and cash flow projections; business and financial strategies; and funding and banking arrangements.

HMRC will be looking to establish from the IBR:

- whether a business is genuinely unable to pay its tax;
- whether it is currently solvent;
- whether it is viable going forward; and
- what terms or conditions might need to be applied to any TTP arrangement.

Large tax debts account for around one in every thousand TTP requests and the detailed information in an IBR helps HMRC make an informed decision in these highly complex cases.

The review must be carried out by a qualified professional advisor such as an accountancy firm or an insolvency practitioner, and must be paid for by the business seeking extra time to pay.

Independent business reviews

Using qualified professional insolvency practitioners and accountants to review the solvency and ongoing liquidity of a business is accepted practice in the banking sector to facilitate decisions on lending or investment. And HMRC considers that TTP decisions on large debts warrant a similar review.

Fairness for the taxpayer

In view of the amounts of tax involved, HMRC needs to ensure that decisions about large TTP arrangements are supported by a comprehensive audit trail, to help guarantee better value for money and fairness for all taxpayers.

We remain committed to supporting compliant, viable businesses through periods of temporary difficulty by providing TTP arrangements under the BPSS. □

Further information

- www.hmrc.gov.uk/pbr2008/business-payment.htm
- www.hmrc.gov.uk/stats/bus_pay_sup_serv/bpss-official-stats-oct2010.pdf
- BPSS helpline: 0845 302 1435 (open from 8am to 8pm, Monday to Friday, and 8am to 4pm at weekends)

Gordon Smith is deputy director of debt management and banking at HMRC.

Re Frankice (Golders Green) Limited

A recent High Court judgment regarding the administration moratoria and gambling licences has implications for almost all licensing and regulatory decisions affecting companies in administration.

Moratoria and licences

As readers of *RECOVERY* will know, a company that enters administration gains the protection of a moratorium that provides that 'no legal process… may be instituted or proceeded with against the company or its property', without the consent of the administrator or permission of the court. Money claims are naturally caught by the moratorium, as are criminal proceedings. What was previously unclear is the extent to which the moratorium prevents other steps being taken against the company, which are not proceedings before a court or tribunal. A classic example is the review of a licence held by the company, which may be crucial to its ability to trade, and therefore to a sale as a going concern or a successful restructuring. This point came before the High Court earlier this year in *Re Frankice (Golders Green) Limited* [2010] All ER (D) 59 (May).

Re Frankice concerned three companies that were members of the Agora Group, one of the UK's largest operators of amusement arcades with around 100 trading sites. The group entered administration in December 2009, with an estimated shortfall to its creditors of £84 million. The companies were required to hold operating licences under the Gambling Act 2005, while licences were also needed for key individuals and the premises at which the licensed activities were conducted.

Suspected breaches of licence conditions

Prior to the administrations the Gambling Commission had started an investigation into suspected breaches of licence conditions by the group. Subsequently, the Commission served notices of preliminary findings that detailed a number of adverse findings, and indicated that these were sufficiently serious that the conditions for revocation of the operating licences were met. The notices stated that the fact that the licensed activities were now controlled by the administrators was likely to be a highly relevant mitigating factor, but when the administrators asked the Commission to confirm that the licences would not be revoked, it refused to limit its powers on the basis that its investigations might uncover matters that justified revocation, notwithstanding the administrators' involvement.

Review powers curtailed

The administrators applied to court for directions, and Norris J had to determine whether the convention of the Commission's regulatory panel was 'legal process', within the meaning of paragraph 43, schedule B1 Insolvency Act 1986. The administrators said that it was, and compared the review process to criminal proceedings. The Commission argued that the review was not a 'legal process' and that the procedure was simply a way of reaching an administrative decision in a fair way.

The judge found that the review of the licences was 'legal process'. He said, 'I consider that the nature of the decision which the regulatory panel is called upon to make and the circumstances in which and the procedure according to which the decision is made, fall within the description of "legal process"… There is undoubtedly a "process". It is governed by a procedure. The whole process has about it the stamp of a case being presented by the Commission, being answered by the licensee and being decided upon according to legal advice and for declared reasons by an independent and impartial regulatory panel…'

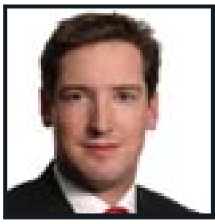
> "The law as it now stands has undoubtedly altered the balance of power between regulators and administrators, and will restrict the exercise by regulators of many of the powers that they have to perform."

As this passage shows, Norris J's decision turned on the quasi-judicial character of the review procedure itself, which leads to a reasoned judgment and is subject to a right of appeal. The judge made it clear that it was this process that was barred by the moratorium, and not the revocation of licences itself; he stated expressly that nothing in his judgment prevents the Commission suspending or revoking licences summarily, without a panel hearing, where that power arises.

This basis of the judgment on the review process itself indicates that this case has significance for almost all regulatory decisions. The elements of the review procedure that led the court to hold that it was a 'legal process' exist (as the Commission's guidance states) in order to ensure 'a fair process, which accords with the requirements of natural justice and the Human Rights Act 1998', and most bodies that exercise a comparable regulatory function have similar procedures. For example, the decision may have implications for the review of premises licences by local authorities.

Will this judgment stand?

It is unclear whether *Re Frankice* will stand if challenged in the future. At a number of points in his judgment, Norris J indicated that he had found the decision difficult, and there is reason to suspect that his conclusions were significantly guided by the effect that the revocation of the licences would have had upon the administrations, rather than pure questions of law. Nonetheless, the law as it now stands has undoubtedly altered the balance of power between regulators and administrators, and will restrict the exercise by regulators of many of the powers that they have to perform their public duties and keep businesses in check. Faced with this decision, it may be that some regulators will simply seek to change their licensing conditions to ensure that the regulatory regime is not undermined by companies going into administration. □



Jamie Leader (far left) heads the London contentious insolvency team and David Roberts (left) is an associate within the Manchester licensing team at Eversheds LLP.

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Special administration regime for investment firms

Could the special administration regime proposed by the government have implications for 'normal' administrations in the future?

The recent failure of several investment firms, and in particular the financial instability caused by the collapse of Lehman Brothers, has prompted the government to propose a special administration regime (SAR) for investment firms.

At the time of writing, the proposals are still in the form of a consultation paper. However, the paper states that it is the government's intention to introduce the new regime by 11 February 2011, as otherwise the relevant power under the Banking Act 2009 (the Banking Act) will have lapsed.

The purpose of this article is therefore to:
- explain the key features of the proposed regime; and
- highlight a few of the proposed changes that we contend could in the future be introduced for 'normal' administrations.

Why is legislation required?

The proposal recognises that the basic administration regime set out in the Insolvency Act 1986 (the Act) is not suited to the complex financing arrangements that have to be addressed by the administrator of an investment firm such as Lehman Brothers.

The government's two stated objectives in introducing the SAR are:
- to provide administrators with clarity and direction to conduct the administration, without the need to make frequent applications to the court for directions; and
- to give clients and counterparties greater confidence in the administration process, thus reducing the impact of an investment firm's insolvency on the stability of the UK financial system.

"The proposal recognises that the basic administration regime set out in the Insolvency Act 1986 (the Act) is not suited to the complex financing arrangements that have to be addressed by the administrator of an investment firm such as Lehman Brothers."

The scope of the SAR

The SAR only applies to an 'investment bank'. This term is defined under section 232 of the Banking Act as a UK incorporated institution (including UK-based partnerships and LLPs) which holds client assets and has permission under Part 4 of the Financial Services and Markets Act 2000 to carry on at least one of the regulated activities of (i) safeguarding and administering investments; (ii) dealing in investments as principal; or (iii) dealing in investments as agent.

An investment bank can be placed into special administration on one of three grounds:
- Ground A is that the investment bank is, or is likely to become, unable to pay its debts;
- Ground B is that it would be fair to put the investment bank into special administration; or
- Ground C is that it is expedient in the public interest to put the investment bank into special administration.

Proposed changes

New special administration objectives

Perhaps the most significant change contained in the proposals is the introduction of a new set of objectives specifically for the SAR. These are described as special administration objectives (SAOs) and are intended to replace the usual administration objectives found in paragraph 3 of Schedule B1 of the Act. The objectives are:
- to ensure the return of client assets as soon as reasonably practicable;
- to ensure timely engagement with market infrastructure bodies and authorities (listed below); and
- either to rescue the investment firm as a going concern or wind it up in the best interest of the creditors.

The first two objectives are noteworthy in that they expressly recognise the interests of non-creditor stakeholders in the administration process.

It is proposed that there is no pre-defined order of priority between each of the SAOs; the draft regulations expressly state that the order in which the SAOs are listed is not significant. Instead the proposals require the administrator to prioritise each objective as the administrator thinks fit in order to achieve the best result for both creditors and clients (again recognising the wider interests to be considered by an administrator under the SAR). The administrator would have to explain at the outset how he or she intends to achieve the SAOs and the FSA would have the power to direct that the administrator focus on one objective over another.

Therefore, the proposals open the possibility of a situation in which an

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administrator has to make one or more value judgements between the competing interests of different stakeholders (for example, prioritising the return of assets over maximising the return to creditors). The ability to be able to seek directions from the FSA could prove to be essential in these scenarios.

A summary of each objective is set out below:

1) **To ensure the return of client assets as soon as reasonably practicable**

To ensure the return of client assets the plan enables an administrator to set a bar date for the submission of claims to the beneficial ownership of, or security interests asserted over, client assets.

It is proposed that in setting the bar date, the administrator would have to allow a reasonable time period after notice of the bar date has been published for the calculation and submission of claims.

Where there is a shortfall in securities of a particular description held as client assets in a client omnibus account, those shortfalls will be allocated on a pro rata basis among the clients (although this will not apply to client money).

The proposals also confirm that the return of client assets would only apply after taking account of any netting off and any third-party security over the assets.

2) **To ensure timely engagement with market infrastructure bodies and authorities (Treasury, Bank of England and FSA)**

The administrator will be required to work with market infrastructure bodies to facilitate any action that the above authorities need to take in order to minimise the disruption to businesses and the markets.

The administrator will also need to facilitate the operation of the default rules of the bodies and resolve any issues that arise from the operation of those rules and facilitate the settlement or prompt cancellation of non-settled trade debts.

3) **Either to rescue the investment firm as a going concern or wind it up in the best interest of the creditors**

This objective is substantially derived from two of the objectives for a normal administration contained within Schedule B1 of the Act. The proposal also contemplates that the reference to 'wind it up' would potentially avoid the need to subsequently place the firm into liquidation.

The role of the FSA

The SAR contemplates a greater role for the FSA, particularly in relation to entry into administration and the power to direct the actions of the administrators.

Entry into the SAR will require an application to the court. The FSA's consent will be required before an investment firm can commence a normal insolvency procedure and the FSA would have the reverse power to apply to court to put a firm into a normal procedure.

As mentioned above, it is also proposed that the FSA will have the power, after consulting with the Bank of England and the Treasury, to direct administrators to prioritise the SAOs if this is in the interests of financial stability.

Administrator's liability

Although the proposals recognise that there may be an increased level of exposure and personal liability for administrators dealing with an investment firm, the proposals do not contain any further protections for administrators. On the contrary, the SAR will also allow the FSA and clients to bring an action against administrators in respect of their conduct. The stated logic for this stance is that since the SAR should enable administrators to carry out their objectives in the most efficient and timely manner, with the support of the FSA's power of direction, the government does not foresee any successful challenges to the administrators' conduct. This is one area that may be subject to comment during the consultation process and it will be interesting to review whether any changes are made in the final form of the legislation to provide further comfort to administrators operating under the new regulations.

Operational reserve

One of the most important proposals to be highlighted by the government is the requirement for investment firms to maintain an operational reserve, which aims to provide sufficient funds to cover the expenses arising upon the commencement of the administration.

Potential changes of wider interest

In addition to the above changes, which are relatively specific to the particular circumstances that arise when dealing with investment firms, the SAR also contains a few changes that could, arguably, have relevance for 'normal' administrations. Therefore, if they are adopted for SARs it may not be such a leap for these changes to be adopted for normal administrations at some point in the future.

Adoption of liquidator's powers

One of the most marked shifts contained in the proposals is the extension of certain powers currently only exercisable by a liquidator so that these could be exercised by an administrator. The explanatory notes make express reference to the ability of an administrator under the SAR to bring actions under sections 213 and 214 of the Act, but the draft legislation goes further to encompass other powers only currently exercisable by liquidators, such as disclaimer or actions against directors for misfeasance.

> "One of the most marked shifts contained in the proposals is the extension of certain powers currently only exercisable by a liquidator so that these could be exercised by an administrator."

If the proposals are adopted in their current form it would open up a debate as to whether these powers, currently reserved for liquidators, should be made available for administrators in normal administration.

Continuity of supply

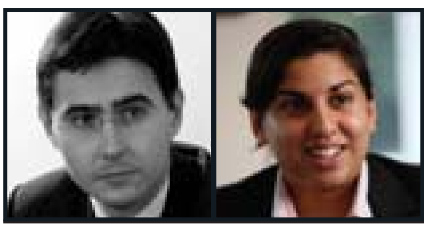
Another proposed change is the expansion of section 233 of the Act to recognise the extent to which modern companies rely not only on traditional utilities but also on IT and other key services.

Key services in this context include computer software; financial data; broadband and electronic mail; data processing and commercial bank services; all of which may be considered integral to the carrying on of business for ordinary companies and not just investment firms.

Implementation and the future

The consultation process is now over but those who wish to read the paper in full will find it available on HM Treasury's website[1]. It will be interesting to review the final form of the legislation in early 2011 and observe the extent to which some of these changes subsequently find their way into the normal administration process. ☐

[1] www.hm-treasury.gov.uk/d/consult_sar_160910.pdf



David Fletcher is a partner and Nyla Yousuf is a solicitor at Farrer & Co.

Insurance recoveries can yield substantial assets for IPs

Rob Samuel says there may be hidden gems recoverable in insurance contracts.

The recovery of outstanding insurances can be a complex process for insolvency practitioners (IPs). Not only does an insurance policy indemnify a company while actively trading, in liquidation it may provide a cash asset that can easily be overlooked. We have seen examples where companies have bought an insurance product and have not been fully aware of the coverage it provides and the possible recoveries that are due when the company fails. A thorough review of insurance coverage can produce significant financial benefits for an estate.

Upon entering receivership or liquidation a client is demoted in terms of priority by most insurance companies and brokers. Clients in liquidation are referred to as being 'in run off' with no future revenues anticipated to the insurance companies. This reduced client value manifests itself in file handling being transferred to satellite offices and service levels can be negatively impacted. Insurance brokers, despite being retained by the client, will often side with the insurers in the knowledge that the insurer will continue to be a market for the broker.

There are two main insurance recoveries relevant to IPs.

1) Outstanding claims recoverable

We have seen instances of claims being closed without payment to the client estate on the basis that they have gone into liquidation. These claims should be actively pursued since they represent considerable value to the estate. Alternatively, insurers may simply ignore correspondence from a liquidator or make a weak representation to refute a claim.

For liquidators to confront and challenge this approach, they need to have access to and knowledge of the insurance industry. IPs should be aware that once a claim has been submitted to the insurer and substantiated with evidence, the onus is on the insurer either to pay the claim or detail the basis on which the claim has been rejected or the values reduced. IPs should not be put off if there are several insurers covering the same policy since a lead insurer would have been assigned to approve all payments and it is the broker's responsibility to manage the collection process.

> "Concerns over information from the client's insurers should be raised with the FSA."

2) Return premiums recoverable

It is not only claims that are recoverable when companies go into liquidation. There are often opportunities to receive return premiums if the insurance policy is cancelled mid-term. The contract wording needs to be scrutinised and a return premium claim submitted to the insurer. Insurers' attitudes have not proved to be sympathetic on monies that are contractually due in these instances and they will make attempts to refute return premiums. Ensuring that insurers are promptly notified of the need to cancel the insurance contracts in place and asserting any rights to return premiums can lead to significant recoveries.

Some contingent insurance contracts will only come into force when a number of conditions are met. Clients pay a deposit premium upfront that might be recoverable if a company fails prior to the insurance conditions being met. The brokers should be able to identify and return these premiums, although they may be reticent to do so since they could forego a proportion of their brokerage as a result.

The introduction of a tougher regulatory regime under the Financial Service Authority (FSA) has improved the professionalism within the industry and eliminated some bad practices. If you have concerns over the information received from the client's insurers or insurance brokers, you should contact the FSA who will clarify these issues and investigate, if appropriate.

There are often hidden gems recoverable from insurance contracts. IPs should be aware of the variety of recovery means that exist and seek professional advice to identify and assist in maximising the insurance recoveries. ☐

Rob Samuel is a partner at Flag Partners.

Economic snapshot: Scotland

Does the Scottish economy's dependency on the public sector and financial services, coupled with the credit squeeze, bode ill for rapid recovery? John Hall reports.

Scotland has an enviable record in many things: from medicine to literature to its historic acumen (at least until recently) in the financial services sector. However, it is an economy that has traditionally been heavily dependent upon the public sector. This has, perhaps, made it a less dynamic, more cautious economy, which usually means that it is less susceptible to downturns in the economy (as the public sector bolsters the private sector) but slower moving in the upturn.

A triple whammy

However, with heavy cuts confirmed for the public sector, and a private sector that has been hit hard by the recession, it appears that Scotland faces the triple whammy of a less dynamic economy, a public sector about to be hit and a private sector that is still reeling from the recession.

Scotland starts from a difficult position. With personal bankruptcy rates twice those of England and Wales and a 340 per cent increase in the number of personal insolvencies over the last decade it is clear the country has been living beyond its means for some time. Numbers have begun to stabilise at an alarming 23,000 personal insolvencies per year with little sign of this number falling back. Given that just ten years ago this figure was less than 6,000 it is deeply concerning how ingrained the debt culture has become.

Dependency on the public sector

Indeed all of this has occurred before the impact of public sector cuts has been felt. In some parts of Scotland – Dumfries and Galloway, and the Highlands and Islands for example – more than 50 per cent of the population is employed in the public sector. Over the last decade the public sector has contributed 30 per cent to Scotland's GDP growth compared with 20 per cent for the rest of the UK.

Once the full impact of the Comprehensive Spending Review begins to take effect it is clear that there will be substantial parts of Scotland that will experience a significant loss of public sector jobs. There will undoubtedly be a serious impact on the local and national economies once these cuts are implemented and there is no obvious solution in place to counter this.

Drop-off in the financial services sector

The greater worry is that there is a weakened private sector that is unlikely to be able to absorb such job losses. The impact of the loss of HBOS as a Scottish headquartered bank coupled with the public ownership of the Royal Bank of Scotland has meant that Edinburgh, which once had two of the world's largest banks at the head of its renowned financial services sector, has seen an enormous drop-off in corporate activity. What was once the main driver of much of the financial growth in the wider Scottish economy has been severely curtailed and does not appear likely to recover for many years to come.

A reduction in lending

The straitened circumstances of the banks has also lead, despite their public protestations to the contrary, to a reduction in lending that is continuing to have a negative impact on Scottish businesses. In particular, SMEs report that, not only are they unable to raise additional funding, their existing lending facilities are being reduced and re-priced, which is severely hampering their activities. The result is that the private sector, which should be driving the economy out of recession, is being hampered in its growth.

The inevitable consequence of this credit squeeze is that some firms have had to close. For the last year, Scottish firms have experienced a higher level of corporate insolvency than the rest of the UK. The figures for 2010 to date indicate that this will be the highest ever year for corporate failures with a very strong upward growth over the first couple of quarters. For example, the second quarter saw an increase of 103.4 per cent compared with the same quarter in 2009. The worst hit sectors have been the usual suspects of property, construction, logistics and hospitality, but all sectors have been affected to some extent.

Even in the good times the Scottish economy has always underperformed the rest of the UK. A recent Item Club (this group uses the same model of the economy as the Treasury) report stated that growth in the Scottish economy would be 0.8 per cent compared with 1.0 per cent for the rest of the UK. The predicted loss of 30,000 public sector jobs will undoubtedly reduce this further.

> "Scottish firms have experienced a higher level of corporate insolvency than the rest of the UK."

Future possibilities

What all of this tells us is that Scotland has been too reliant on the public sector for growth, that its principal economic driver was the financial services sector, and that it has a personal debt culture that is not supportable by its income – a combination that is unlikely to produce a rapid improvement in the economy!

To try and draw some positives, while the proposed cuts in the public sector will be harsh in the short term they should, eventually, lead to a larger private sector. This will undoubtedly improve the GDP over the medium to long term and result in more dynamic economic growth for Scotland. That is the theory at least; whether this actually happens remains to be seen! Whatever the outcome it is clear that the Scottish economy of the future will have a dramatically different form from that of today. □

John Hall is founder and group development director of Invocas Group.

A snapshot of the nation's personal finances: R3 research

Can you last till the end of the month? Will Black evaluates findings on personal finance.

While most of R3's research focuses on corporate insolvency, we have commissioned a major personal debt snapshot to coincide with ever-increasing personal insolvency numbers and uncertainty over the pace of economic recovery. These findings have provided key lines to attract the interest of MPs and journalists, and have already generated press coverage in *CITY AM*, the *Daily Mail*, the *Sunday Mirror*, Sky News (online), the Press Association, Virgin Media, MSN UK and USwitch. The same report has also been sent out to all MPs.

The research revealed 40 per cent of adults in the UK are worried about their current level of debt, equating to almost 20 million individuals. Concerns over credit card debt (at 51 per cent) far outstrip worry over any other kind of debt. A third of people worried about their current debt level (32 per cent) are worried about their overdraft, and 19 per cent worry about bank loans and mortgage repayments.

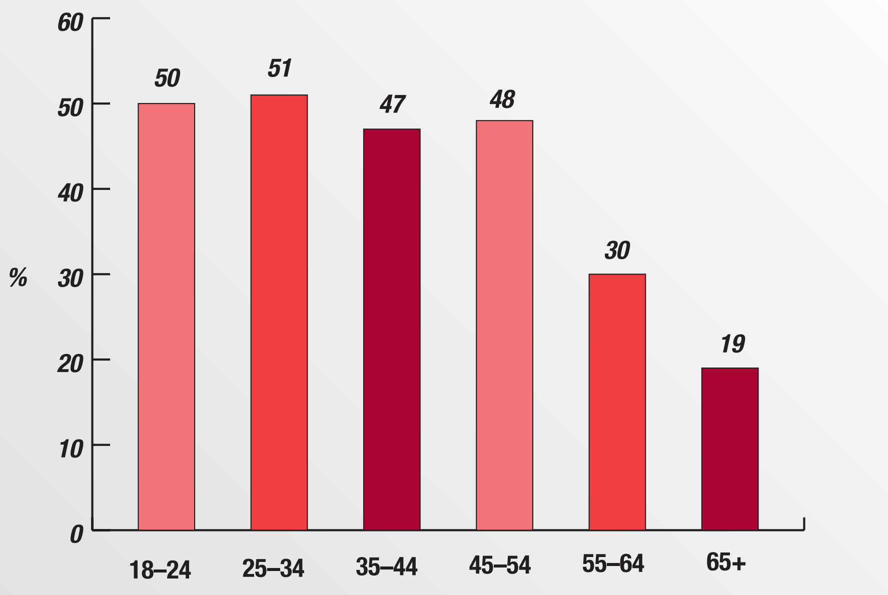
For 40 per cent of the British population getting through to 'payday' is a struggle. The money tends to run out on the twentieth day after payday. Of those who say they often or sometimes struggle to make it to payday, 35 per cent say credit card payments are at the heart of their struggle, while 25 per cent say spending on going out, or non-essentials is to blame.

Paying off bank loans, big-ticket purchases and making mortgage repayments clearly also play a significant role (between 15 per cent and 17 per cent). Recent changes – tax rises and welfare cuts – apparently affect around one in ten of those who struggle.

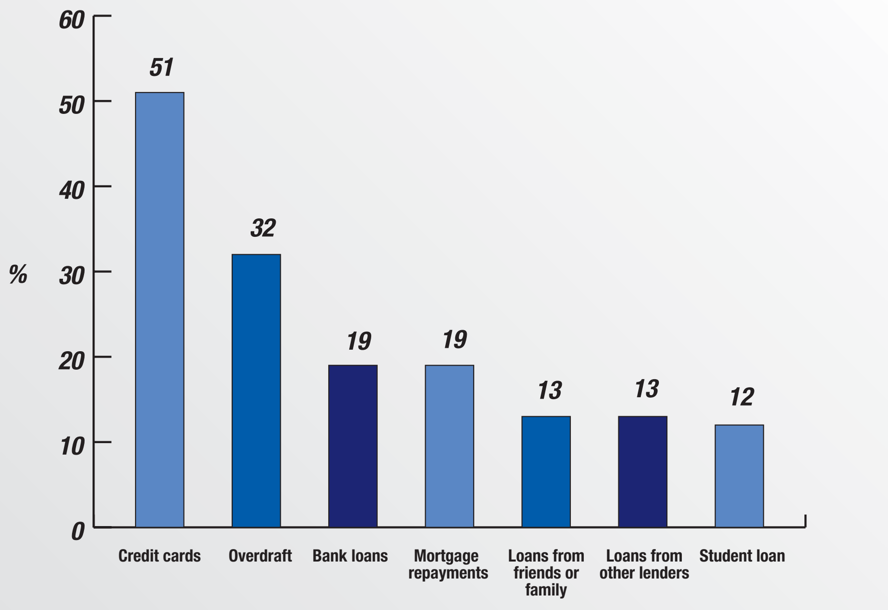
Over the course of the last decade, personal insolvencies have increased by 350 per cent and it is very worrying that over 40 per cent of the British population are struggling financially just to get through the month. This is a huge stress in itself and factors such as inflation associated with basic living costs and potential rises in interest rates will not make this monthly struggle any easier. □

Will Black is the communications manager at R3.

How many people are worried about their debts?



What kind of debts are they worried about?



Age group	Day struggle begins
18–24	19
25–34	19
35–44	19
45–54	20
55–64	21
65+	22

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R3 insider at party political conferences

Steven Law gives a round-up of R3's activities at the recent party conferences.

After an exhausting yet exciting three weeks at the party conferences I am happy to report that the experience has proved to be hectic, enlightening and, above all, successful. Travelling up and down the country to Liverpool, Manchester and Birmingham has definitely been worthwhile.

This year we succeeded in:

- holding two well attended fringe events;
- holding a series of successful meetings;
- beginning to form positive relationships with MPs with whom we have previously struggled to engage; and
- finding common ground with stakeholders such as the FSB, ABI and CAB.

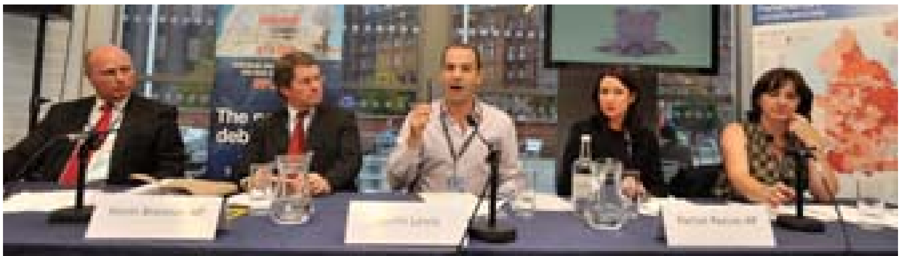
Although the Labour Party conference lacked the bustle and excitement of previous years, the culmination of the three-month leadership campaign, which saw Ed Miliband beat his older brother David, caused some excitement, if not shock for conference delegates, party members and politicians alike.

Not surprisingly the Lib Dem and Conservative conferences were upbeat. Spirits were high in the Conservative conference centre and the Lib Dems looked happy if not a little surprised at being in power. However, the combination of Tory blue and Lib Dem yellow saw some green-looking faces in Liverpool and Birmingham as the coalition presented a united front and attended each other's conferences. Key announcements about child benefits and academy schools exposed some small cracks in the coalition but, despite some serious digging, the media were unable to find any serious splits within the Lib Dem or Conservative camps.

Fringe insider

At the Labour Party conference, R3's fringe event focused on personal debt and insolvency. The event was titled 'The ticking bomb? How big is the personal debt problem and what should we do about it?' I was joined on the panel by Kevin Brennan MP (former Business, Innovation and Skills Minister) Rachel Reeves MP (who sits on the Business, Innovation and Skills Select Committee) and Teresa Perchard from CAB. Martin Lewis from MoneySaving Expert chaired the panel and conducted a lively debate focusing on the explosion of personal insolvencies over the last decade and the need to tackle the debt culture in the UK.

Our Conservative fringe event, titled 'Avoidable or a necessary evil? Does business failure matter and what should government be doing about it?' had a different tone altogether and focused on



Labour Conference fringe event. Left to right: Steven Law, Kevin Brennan MP (former Business Innovation and Skills Minister), Martin Lewis (MoneySaving Expert), Rachel Reeves MP (member of Business Innovation and Skills Select Committee), Teresa Perchard (CAB).

corporate insolvency. The event was chaired by the business editor of the *Sunday Telegraph*, Kamal Ahmed. He was joined on the panel by Harriett Baldwin MP, who enjoyed a 20-year career in banking prior to entering the House, and Stephen Alambritis from the Federation of Small Businesses. We had an interesting and well informed debate that covered topics from bank lending and corporate insolvency trends, to IPs' fees and pre-packs.

R3's meetings

At all three conferences we had excellent engagement with MPs, peers and stakeholders. The new intake of MPs were particularly keen to engage and learn about our profession and we discussed issues ranging from insolvency in the constituency to the up-coming launch of R3's corporate campaign, 'Holding rescue to ransom'. Here are some of the highlights...

At the Liberal Democrat conference in Liverpool we had an excellent meeting with Lord Oakeshott, which is crucial given that he is a key adviser to Vince Cable (Secretary of State for Business, Innovation and Skills). He was positive about R3 and would like to work closely with us in the future, especially on issues such as directors' disqualification. Similarly we had a very constructive meeting with Lorely Burt MP (chair Liberal Democrat Business Committee) who was extremely supportive and enthusiastic about our new campaign.

At the Conservative conference in Birmingham we met with George Eustice MP to discuss his Private Members' Bill on Secured Lending Reform, which proposes to make some changes to the law surrounding fixed charge receiverships. We also held a positive meeting with Lord Hodgson of Astley Abbotts who was extremely knowledgeable and interested in insolvency issues.

At the Labour Conference in Manchester a particular highlight was the meeting with Gareth Thomas MP (shadow Business, Innovation and Skills minister). We discussed with him insolvency trends and predictions, and he would like to work with R3 in his constituency to tackle debt and insolvency.

On the back of the conferences, we have also arranged several meetings with MPs over the coming weeks, including a meeting with the Small Business minister, Mark Prisk MP, and the Business, Innovation and Skills Select Committee chair, Adrian Bailey MP.

The 2010 conference season also saw great engagement with stakeholders. The British Chamber of Commerce has a shared aim with R3 in rescuing businesses and we agreed to work closely with bodies such as the Consumer Financial Education Body, the Federation of Small Businesses and the Money Advice Trust in the coming months. □

Why does R3 'do' party conferences?

- Parliamentarians can be notoriously hard to engage with. At conference they are more willing to meet in an informal environment to discuss key issues and concerns.
- A combination of fringe events and a meeting programme shows that R3 is a serious player, giving us unrivalled exposure to parliamentarians, stakeholders and key decision makers.
- Engaging with MPs is vital when so many trade bodies and other stakeholders are out in force. Not all of them share our views of the profession and it is important that we are on the pulse to counter any negative comments.
- With public sector cuts and a recent spending review it is more important than ever that we attend conference. Government can no longer justify the expenditure for expensive advisors and more and more they are looking to those at the 'coalface' to feed into policy.

Information for R3 members

For more detailed information about R3's 2010 conference activity, our wider public affairs programme or our corporate campaign 'Holding rescue to ransom' please contact Laura Harvey on 020 7566 4214 or laura.harvey@r3.org.uk

Steven Law is a partner at Ensors and president of R3.

R3 events, courses and conferences

Date	Event title	Venue
December		
2	Yorkshire Region Wine Tasting Event	Park Plaza Leeds
6	North West Regional Meeting	
7	Introductory Programme Liquidations 2	etc Venues, London
7	Introductory Programme Liquidations 2	Deloitte, Birmingham
7	Breakfast Briefing – Environmental Issues for Insolvency Practitioners	SNR Denton, London
8	North East Regional Meeting	Dickinson Dees, Newcastle
9	Introductory Programme Liquidations 2	Irwin Mitchell, Leeds
9	Southern Regional Meeting	Blake Lapthorn, Southampton
10	North East Regional Bands' Night	Centre For Life, Newcastle upon Tyne
January		
19	South West and Wales Ladies' Lunch	
27	North West Women's Group Champagne Tasting Event	Epernay Champagne Bar, Manchester
29	Yorkshire Women's Dinner and Dance	
February		
1	Introductory Programme Introduction to Insolvency	etc Venues, London
1	Introductory Programme Introduction to Insolvency	Deloitte, Birmingham
1	Introductory Programme Introduction to Insolvency	Irwin Mitchell, Leeds
10	Trading Insolvencies	Hilton, Manchester
17	Liquidations	Hilton Tower Bridge, London

For further information on R3 courses and conferences, please visit the R3 website **www.r3.org.uk**, where you can download the full 2011 programme. Alternatively, call the Courses team on 020 7566 4234 to request a programme by post.

regional events **R3 events**

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Other Council Members

John Alexander, Mark Andrews, Elizabeth Bingham, Louise Brittain, Robert Brown, Malcolm Cohen, Patrick Ellward, Antony Fanshawe, Giles Frampton, Colin Haig, Brian Hamblin, Richard Heis, Gareth Limb, Lee Manning, Jane Moriarty, Peter Sargent, Frank Simms.

R3 membership categories

We continually strive to improve benefits for all members. Membership benefits across categories include:

- A copy of *RECOVERY* every quarter
- Attendance at regional meetings
- Priority bookings for R3 courses and most of its conferences
- Technical bulletins and releases
- Access to the members' section of the R3 website
- An invitation to the R3 annual conference
- Continuing professional education at discounted rates

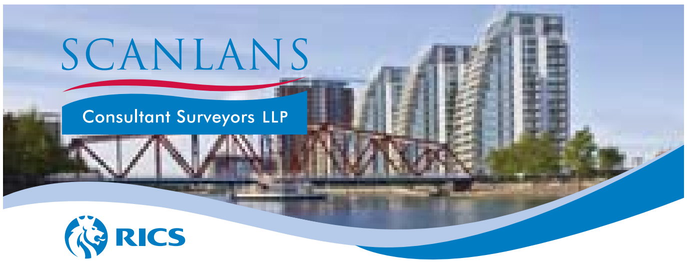
Please see below for details of the different categories of membership:

Full members are invited to contribute to the development of insolvency, business recovery and turnaround professions at both local and national levels. Benefits include: use of the designatory letters MABRP and a certificate of membership, inclusion in the *R3 Directory* and a copy of it, membership of INSOL International.

Associate members are individuals who do not meet the requirements for full membership but work significantly within the business recovery sector.

New Professional (Student) members are individuals preparing to take the examination of the Joint Insolvency Examination Board (JIEB) or Certificate of Proficiency in Insolvency (CPI). Pass students of these exams are eligible to apply for full R3 membership.

New Professional (Networking) members are individuals who have recently joined their firm, and/or are new to the business recovery sector and wish to network with R3 members. This category receives electronic copies only via access to the R3 website.



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Inserts: Jordan Publishing, Peter Phillips

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Wanted

Interview with Neville Kahn

The ICAEW has recently set up a new insolvency group. Neville Kahn, the chair of the group, answers questions from the insolvency community.

Why was the insolvency group set up at the ICAEW?

The main aim of the group is to support insolvency practitioners (IPs) throughout their careers to encourage best practice in this field. As the UK's largest regulator of IPs, the ICAEW is well positioned to offer the very best in up-to-date information, technical guidance, thought leadership and advice.

Although ICAEW has long supported IPs, it recognised the need to provide more effective support for members and licence holders working in this important sector. The launch of the group will help to achieve this by bringing together all ICAEW's insolvency activity under one umbrella to achieve a more streamlined service.

What are the aims and objectives of the group?

We aim to:

- Advocate effectively on behalf of IPs and address issues that may impact the sector.
- Provide a powerful voice, particularly with government, the media and key insolvency bodies.
- Develop effective support for IPs at every stage of their career, from those who are training to experienced professionals.
- Develop a leadership role, ahead of other regulators, and develop the next generation of IPs.

Neville Kahn, global head of reorganisation services, Deloitte.

> "There's no common membership between the committees as none of the volunteers who are members of the insolvency group committee are also members of regulatory or disciplinary committees."

Why is the group needed and what will it do for IPs?

The insolvency group will encourage best practice by providing members with a range of services including thought leadership, representation and regulatory and technical support.

Those who join the group will gain access to a wide range of opportunities designed specifically to help them remain at the forefront of their field. They will receive an e-mail newsletter with regulatory updates, links to helpsheets, and news and views on issues affecting the insolvency profession.

In addition, they will be able to attend free seminars and other events to meet and exchange ideas, extend and refresh technical knowledge and hear from leading experts in insolvency.

How will it link in with the existing regulatory committees at ICAEW?

The group will work with existing committees at ICAEW drawing on their collective experience to help shape the debate on issues affecting the sector.

As the UK's largest regulator of insolvency practitioners, ICAEW has the ability to act as a powerful advocate on issues affecting insolvency practitioners.

There's no common membership between the committees as none of the volunteers who are members of the insolvency group committee are also members of regulatory or disciplinary committees. ICAEW governance processes require that there is no overlap.

But one of the main aims of the group is to provide support for insolvency practitioners. So feedback from the regulatory and disciplinary committees and from ICAEW staff involved in regulation and monitoring will highlight areas where guidance is needed or where IPs need a gentle reminder about existing requirements. Our regional insolvency events, which are part of the group offering, also give us the opportunity to share feedback from monitoring visits with IPs. The group's newsletter, *Insolvency News* will continue to include 'need to know' content on legislative and regulatory subjects as well as 'nice to know' content too.

There are also strong links with ICAEW's insolvency committee (which is not a regulatory committee) chaired by Tony Lomas of PricewaterhouseCoopers. It's the insolvency committee that responds to consultations on insolvency matters on behalf of ICAEW, so the insolvency group will be sharing their views with this committee too.

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Does the group plan to be involved in other IP-focused activities?

Yes, specific IP-focused activities include:

Offering representation and advocacy

- The committee will act as an advocate for group subscribers, co-ordinating responses on issues that affect the work of insolvency practitioners.
- It will channel members' views into the committee's response to policy and legislative change.
- The group has and will continue to develop strong working relationships with key insolvency organisations.
- The committee is representative of the profession as a whole and includes insolvency practitioners from small, medium-sized and large firms.

Providing information and advice

- The insolvency group will provide helpsheets and checklists with practical advice on topics including cold case file reviews, internal controls and systems and technical help.
- It will issue regular newsletters with news, opinion pieces and sector commentaries, legislation changes, best practice and methodology.
- There will be webinars on topical subjects delivered via our online community *TalkInsolvency*. Over the next few months we'll be repeating the presentations from our regional roadshows as webinars.
- It will offer e-library resources including journals, briefings and articles on key topics including debt recovery and managing creditors plus catalogues of reading materials.
- It will give information on the latest regulatory changes and compliance updates at a new annual conference to be held in Spring 2011, and through regional events.
- It will provide free access to Lawrence Graham's out of hours emergency helpline.
- It will also provide e-mail access to an expert panel for technical enquiries.

Hosting seminars and events

- The group will offer members and their staff free access to regional insolvency events.
- Next year ICAEW will be holding roadshows for those who have recently taken a licence from ICAEW and those who have recently passed their JIEB.
- It will also give group members discounted rates at ICAEW's annual insolvency conference.

Building networks and contacts

- Members will be able to meet fellow insolvency practitioners and experts in the sector and develop their network of contacts at regional events and conferences.
- They will also be able to participate in *TalkInsolvency* where they can share experience with peers, hear about recent insolvency cases and learn from our expert bloggers about the key issues affecting insolvency professionals.

> "The group will work closely with R3 and other insolvency bodies for the mutual benefit of insolvency practitioners ensuring its member's views are appropriately represented."

As the ICAEW is a regulator of IPs, won't that function risk corruption if it has, or appears to have, other relationships with its licence holders?

No. ICAEW's approach to insolvency regulation, including licensing, monitoring and guiding practitioners, reflects its determination to make sure that the public interest is taken fully into account.

The many measures it has in place to uphold the ethical and professional standards of the insolvency profession are designed to ensure accountability, transparency, consistency and independence.

The ICAEW already has other relationships with its licence holders – the majority of its insolvency practitioners are ICAEW members, though ICAEW is increasingly licensing non-members. And this is a model that we're well used to operating, providing both regulation and support. ICAEW is a regulator for audit and investment business and we also have an audit faculty and a financial services faculty, so a dual role isn't a new thing for ICAEW.

Committee members of the insolvency group

Neville Kahn, Deloitte (chair)
Angela Swarbrick, Ernst & Young
Tyrone Courtman, Cooper Parry
Barrie Harding, Barrie Harding & Co
Diane Hill, CLB Coopers
Guy Hollander, Mazars LLP
Jeremy Knight, Jeremy Knight & Co
Ellie McKinnon, DFD
Kevin Murphy, Chantrey Vellacott DFK LLP
Jacqueline Parsons, Dodd & Co
Nick Pike, Lawrence Graham LLP
Steve Quick, Baker Tilly
Steven Ross, RSM Tenon Recovery
Kevin Wall, Zolfo Cooper
Jeremy Willmont, Moore Stephens

How will the group relate to R3?

The group will work closely with R3 and other insolvency bodies for the mutual benefit of insolvency practitioners, ensuring its members' views are appropriately represented.

How will the group be funded and resourced?

ICAEW insolvency licence holders will automatically become members at no extra cost. ICAEW Certificate in Insolvency students and those who register with ICAEW to sit the JIEB also get free membership of the insolvency group.

For ICAEW members who take their licence elsewhere and non-members who we don't license there will be a charge to join the group. To join the insolvency group visit **icaew.com/insolvencygroup**.

The group is led by a committee of volunteers comprising a cross-section of the IP community. ☐

Sarah Houghton is the publishing manager of *RECOVERY*.