Summer 2022

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RECOVERY

Sanctions

Sanctions at home and overseas
Find out about the sanctions regimes that are likely to affect insolvency work, cases with an offshore element and the impact of sanctions on asset-tracing professionals

The National Security and Investment Act 2021
Read up on the scope of the new regime for managing national security risk

More moratoria, maybe?
Has Corbin & King finally proved that the part A1 moratorium can be more than a niche tool?

An interview with… Christina Fitzgerald
R3's new president talks about expanding the profession's knowledgebase, diversity and inclusion, and the focus on regulation this year

What do you think? Readers' views are welcome. Have an opinion about a burning issue? Want to comment on articles or *RECOVERY* itself? Please contact me on **membership@r3.org.uk.**

From the editor

The conflict continues in Ukraine and governments across the world pursue the implementation of sanctions to increase the economic pressure on Russia and its allies in the hope of bringing a conclusion to hostilities.

The conflict is starting to manifest economic consequences of its own in the UK and further afield as it contributes to the spiralling cost of living, higher inflation, rising interest rates and widespread concerns of a global economic downturn.

This is a topic that we are likely to cover later in the year but, for this edition, we focus on sanctions and investigations as it is anticipated that work in this field is already on the increase and that is likely to only continue.

Fergus Randolph QC summarises sanction regimes relevant to our industry starting on page 12, various fee earners from Mourant Ozannes explore the effect of sanctions on offshore jurisdictions starting on page 14, while Laura Dymott and David Hinrichsen of FRP look at how the sanctions changes are impacting asset tracing work starting on page 16.

Jai Mudhar reviews the relevant provisions of the National Security and Investment Act 2021 and assesses their impact on our industry (pages 20–21) and Clyde & Co look at how we can use the provisions of the Economic Crime (Transparency and Enforcement) Act 2022 to our benefit on pages 24–25.

Away from sanctions, Matthew Weaver QC reviews a decision with a surprising outcome that we all need to be aware of starting on page 6. We have our first reported decision on Moratoria – Paul Keddie and Tim Bromley-White of Macfarlanes tell us more on pages 26–27. On pages 28–29 Addleshaw Goddard look at the FCA's approach to debt compromises.

Considering technology in our industry, William Minns of IP-Bid looks at the development of their sales platform on page 23. Robin Ganguly of Aon looks at the litigation funding options that you might not have considered on pages 30–31.

With the Jubilee celebrations upon us, it is only appropriate that we explore escheat and land passing to the Crown. Richard Clark at TLT updates us on that in pages 32–33. From Europe, Emmanuelle Inacio explains recent projects and collaborations that INSOL Europe have been involved in on page 35.

Lastly, congratulations to our new President, Christina Fitzgerald. Her first President's column is on page 4 and the interview with her starts on page 39.

NEIL SMYTH is a partner at Mills & Reeve and is the editor of *RECOVERY.*

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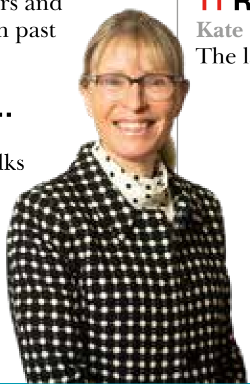

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Change at the top

Incoming president **Christina Fitzgerald** provides a preview of a busy year of new faculties, new events, new projects and a new R3.

Like many R3 presidents, I've taken the role at a challenging time for the profession and the economy. Inflation, energy and fuel costs are rising, the last of the government's Covid-19 support measures have ended, and insolvency numbers are returning to pre-pandemic levels.

These factors, along with the ongoing significant debate around insolvency regulation, means the profession and its work supporting the economy will be both even more important *and* under increased scrutiny in the weeks and months ahead.

Ensuring the profession is supported and represented during this period will make for a busy year in office, but before I talk about my plans for my presidential year, I would like to pay tribute to my predecessor, Colin Haig, for the work he has done to support R3, our members and the team throughout the most turbulent period in the Association's history.

In his two years as R3 president, Colin oversaw a transformation of the organisation that has left it leaner, more focused and better prepared for the future – whatever shape that may take.

I'm delighted that I will benefit from his experience this year when he serves as immediate past president, but before he handed over the presidential chain, he oversaw a very busy last three months in office.

Since the last issue of *RECOVERY*, R3 has held its second successful joint Fraud Conference with the Fraud Advisory Panel and INSOL Europe – its first in-person conference since 2019, its second Scotland Forum. The Training Academy has also launched a suite of new courses and held its second very successful New Professionals' Week.

While this has been going on, the Press, Policy and Public Affairs team has submitted R3's response to the government's regulation consultation, published a paper on insolvency fees and continued to give the profession a voice in Westminster, Whitehall and the media.

> **Work has already begun to develop R3's new group of faculties, with three launched in April of this year.**

Presidential priorities

So, what's on my agenda? There are a number of areas of activity I would like to make a priority during my term of office.

The first is to ensure R3 is ready and able to support the profession now and in the future – delivering on one of the key aims of the strategic plan that was launched when Duncan Swift was president in 2019.

This will involve supporting the R3 team to ensure the governance review work is completed and that every area of R3 that can be improved is improved. That way, the organisation can serve members and the profession in the future as well it has for the last 30 years.

The second is to build on the faculties project that Colin announced in the last issue, to ensure R3's community is as broad as possible – including the profession and those organisations and sectors outside it that engage with us on a regular basis.

Work has already begun to develop R3's new group of faculties, with three launched in April of this year. I'm really looking forward to working with the chairs and members of each faculty, hearing the insights they provide, and seeing how these new groups support and contribute to R3 and its work on the profession's behalf.

And my third and final priority is to build on the excellent work we've been doing with the Insolvency Service to promote diversity and inclusion within the profession.

I believe this is a really important project – for R3 and for the profession. I want to play my part in helping to ensure our profession's talent pool is as deep and broad as it possibly can be. By ensuring as many barriers to entry and progression are removed, we can help the profession to better reflect the breadth of communities and people we engage with, as well as wider society.

Conference success

One of the many high points of the president's year in office is the Annual Conference. This year's conference was the first we've held in person since November 2019, and it was great to see the profession come back together to network, catch up and hear from our excellent panel of speakers.

The highlights for me were BBC economics editor Faisal Islam's insights into the economic issues that are likely to arise over the next 12 months, and Insolvency Service chief executive Dean Beale's views on the challenges the profession will face in the short and long term.

> **This year's conference was the first we've held in person since November 2019, and it was great to see the profession come back together to network, catch up, and hear from our excellent panel of speakers.**

Thank you to the R3 team and this year's conference committee for their work in making the event such a success – you've set the bar very high for next year.

Up and coming

It's going to be a busy summer for the team at R3. The events team are well underway organising a range of regional and national events (hopefully I can attend as many of them as possible), R3's first Contentious Insolvency Forum and the President's Dinner at the Honourable Artillery Club in Moorgate, London.

Alongside this, the Press, Policy and Public Affairs team is working to give the profession a voice on a number of areas, including Companies House reform, fraud and the government's proposed regulatory reforms, while the technical team is continuing to support the profession's engagement with HMRC and has formed a new Employee Working Group, which will look to address the tensions between insolvency and employment law.

Looking at everything that's going on, I think the first three months of my presidency are going to be every bit as busy as the last three months of Colin's. ◻

CHRISTINA FITZGERALD is a partner at Edwin Coe and current president of R3.

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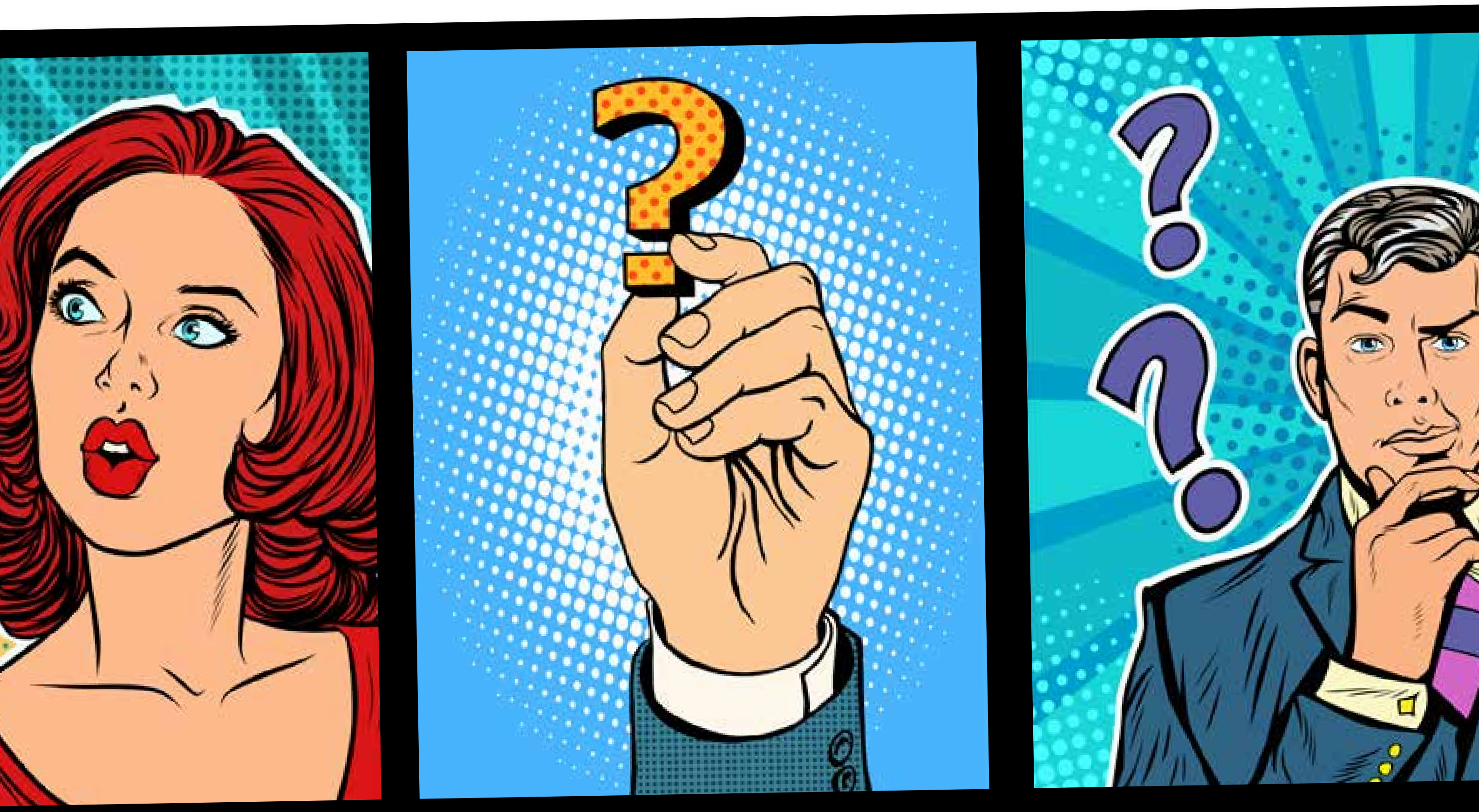


A model article muddle?

Matthew Weaver QC explores the decision in *Hashmi* v. *Lorimer-Wing & others*, which has interesting implications for the authority of sole directors under the model article regulations.

Section 20 of the Companies Act 2006 (CA2006) provides that, when a private limited company is formed, model articles of association will form the company's articles save to the extent that they are modified or excluded by bespoke articles. The form of the model articles is set out in the Companies (Model Articles) Regulations 2008 (SI 2008/3229).

In September 2009, the Department for Business, Innovation and Skills released non-statutory guidance, *Companies Act 2006 final implementation – changes to constitutional documents, including model articles: a summary of what the new approach means*, confirming that the purpose of the model articles was to allow smaller, shareholder managed companies to have simple articles to address the usual requirements of such companies.

Section 154(1) CA2006 confirms that private companies require at least one director.

The case

Hashmi v. *Lorimer-Wing & others* [2022] EWHC 191 (Ch) was a petition presented by Mr Hashmi against a fellow shareholder, Mr Lorimer-Wing, pursuant to section 994 CA2006 in which he sought an order that Mr Lorimer-Wing purchase his shares in a company, Fore Fitness Investments Holdings Limited (the company). The petition necessarily included the company as a defendant and in its defence to the petition, the company asserted claims against Mr Hashmi for breach of duty as a director, breaches of contract and/or pre-contractual misrepresentation.

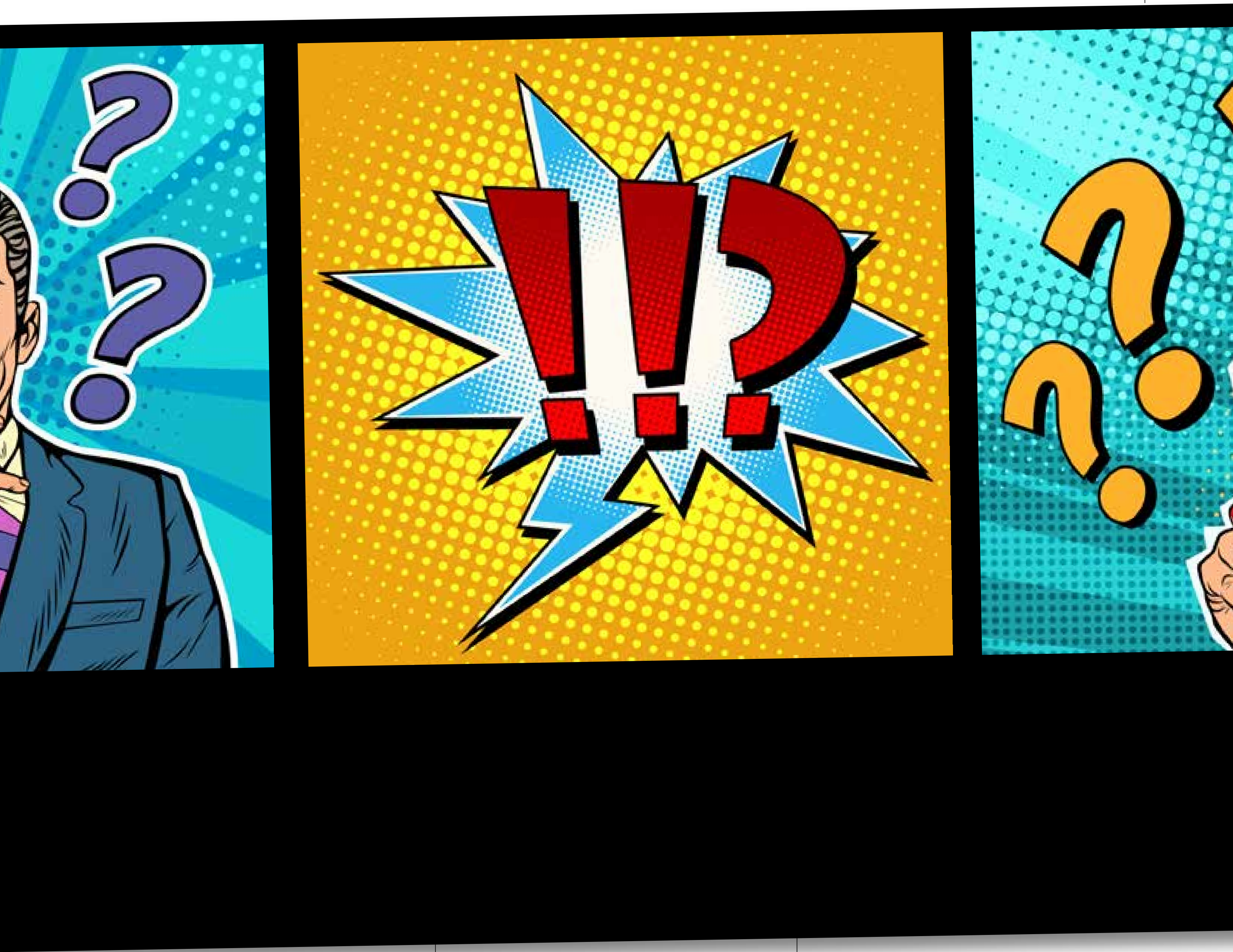
On the company's incorporation in February 2019, its sole director was Mr Lorimer-Wing. Mr Hashmi was appointed as a director in due course, along with a Mr Gilbert. The company adopted the model articles with one material amendment, article 16.

Mr Hashmi and Mr Lorimer-Wing entered into a dispute, as a result of which Mr Hashmi was removed as a director of the company. Mr Gilbert then ceased to be a director, leaving Mr Lorimer-Wing as the sole director from June 2021 onwards.

Mr Hashmi's petition was filed on 10 August 2021 and the company and Mr Lorimer-Wing filed their defences and counterclaim on 21 September 2021.

Mr Hashmi then filed an application to strike out the company's counterclaim. The principal basis of his application was, put simply, that the model articles that applied to the company (albeit as amended by a bespoke article) required there to be two directors of the company. As Mr Lorimer-Wing was the sole director at the time the counterclaim was filed, according to the articles, he did not have authority to cause the company to file its counterclaim, which was, therefore, *ultra vires*.

> **"The judge concluded that on a proper interpretation, article 16 required the company to have two directors."**



The decision

The application came before Deputy High Court Judge Farnhill who handed down judgment on 2 February 2022, acceding to Mr Hashmi's application and striking out the company's counterclaim.

The basis of the judge's decision concerned articles 7 and 11 of the model articles, together with the bespoke article drafted by the company (article 16). These articles read as follows:

7. (1) The general rule about decision-making by directors is that any decision of the directors must be either a majority decision at a meeting or a decision taken in accordance with article 8
   (2) if –
      (a) the company only has one director, and
      (b) no provision of the articles requires it to have more than one director,
   the general rule does not apply, and the director may take decisions without regard to any of the provisions of the articles relating to directors' decision-making.

11. (1) At a directors' meeting, unless a quorum is participating, no proposal is to be voted on, except a proposal to call another meeting.
   (2) The quorum for directors' meetings may be fixed from time to time by a decision of the directors, but it must never be less than two, and unless otherwise fixed it is two.
   (3) If the total number of directors for the time being is less than the quorum required, the directors must not take any decision other than a decision –
   (a) to appoint further directors, or
   (b) to call a general meeting so as to enable the shareholders to appoint further directors.

16.1 The quorum for meetings of the board shall be two directors one of whom must be an investors' director (if appointed) and one the executive (if appointed as director) unless such investors' director or executive is unable to attend a board meeting and has confirmed in writing (which may be by email) that he is satisfied that the board meeting in question is quorate without him being present.

16.2 If a quorum is not present within half an hour from the time appointed for a board meeting because the investors' director (if appointed) or executive (if appointed as director) is not present, the board meeting shall stand adjourned to the same day in the next week at the same time and place or to such other day and at such time and place as the directors may determine and if at the adjourned board meeting a quorum is not present within half an hour from the time appointed therefor because the investors' director (if appointed) or executive (if appointed as director) is not present, provided there are at least two directors present then those directors shall represent a quorum.

16.3 Model article 11.2 shall be modified accordingly.

The judge interpreted these articles as requiring a minimum of two directors at any one time. Mr Hashmi submitted that this was clear from article 16, which referred to a quorum of two, one being an investors' director and the other an executive director. As such, Mr Hashmi submitted, any decision taken by a sole director, which was not a decision to appoint further directors

or to call a general meeting to allow shareholders to appoint further directors, was *ultra vires*.

Mr Lorimer-Wing suggested that article 16 did little to add to model article 11. However, he submitted that articles 7 and 11 represented alternative options for companies. While article 11 refers to a quorum of not less than two, it did not require there to be two directors. What article 11 did was to provide for circumstances where a company has more than one director. Where, however, a company only has one director, article 7(2) applies and a sole director can make decisions without a board meeting and, therefore, without need of a quorum. Reading the articles as requiring two directors was, it was said, contrary to section 154 of CA2006, which only required there to be one director in private companies.

The judge concluded that on a proper interpretation, article 16 required the company to have two directors. This being so, article 7(2) is disapplied by 7(2)(b) on the basis that a 'provision of the articles requires it to have more than one director'. In light of that finding, the judge concluded that article 16 required at least two directors to participate in any decision to commence a counterclaim. As only one director, Mr Lorimer-Wing, had in fact taken this decision, the counterclaim was to be struck out for a lack of authority.

Consequence of the decision

Had the judge confined the basis of his conclusions on the required quorum to an interpretation of article 16 (which was, of course, a bespoke article), his decision is unlikely to have raised the interest that it has among corporate and insolvency lawyers. On the face of it, article 16 expressly requires a quorum of two directors and further defines this as being one investors' director and one executive director. The purpose of the article is plain, to ensure a balance at board level as between investors and the company and this

> **"This judgment is plainly problematic for those acting for sole director companies and in the short term, an amendment of the articles to allow for sole directors may be sensible."**

can only be done by requiring the company to have two directors.

However, the judge extended his comments to refer to article 11. In particular, he stated that *'amendment is required for the model articles to permit for a single director to run a company, but [I] consider that such amendment would need to include the deletion of model article 11(2)'*. This statement, perhaps above everything else in the judge's decision, has caused concern for corporate and insolvency lawyers given that it states that only if the model articles are amended can they apply to sole director companies.

There are, of course, numerous sole director companies in England and Wales, many of whom have adopted the model articles, often automatically under the provisions of the CA2006. If the judge is right that the model articles create a requirement for two directors, thereby rendering everything done by sole director *ultra vires*, the possible ramifications of this are obvious.

While third parties dealing with a sole director company have little to fear, given that section 40 of CA2006 protects them by providing that a director binds a company, assuming that there is good faith; the company's position is not so protected. As in this case, litigation pursued by a sole director company could be liable to be struck out but, in addition, steps taken by sole directors (such as the appointment of administrators) could be deemed *ultra vires*. Given the number of administration appointments by sole director companies over the last ten years or so, the number of potential invalid appointments could be significant.

Reason to panic?

In a word, no, albeit this decision is concerning. This judgment is plainly problematic for those acting for sole director companies and in the short term, an amendment of the articles to allow for sole directors may be sensible. However, there is a real possibility that a different court would take a different view on the effect of articles 7 and 11 of the model articles. This case was primarily decided on a bespoke article and it might be argued that the judge's comments on article 11 were obiter. Absent a bespoke article, the discussion around article 11 of the model articles is likely to be different

While the judge here correctly identified the proper basis on which to interpret articles of association (ie applying the ordinary contractual interpretation rules), the overall purpose of the articles and the surrounding circumstances at the time the document was created were not considered in any detail. The model articles are designed to be capable of application to any company without amendment (albeit amendment is permitted). As such, on the judge's expressed view as to article 11, the model articles do not appear to work as a single document. Article 7 expressly provides for what happens where the articles do not require more than one director but article 11, in the view of the judge, requires there always to be two directors, which is obviously contradictory.

The intention of Parliament in creating the model articles to simplify matters and to be suitable for smaller shareholder-managed companies also appears to have been largely ignored. Such intention could be said to be satisfied if article 11 is read as only being effective if the articles elsewhere require more than one director. If they do not, article 7 appears to disapply article 11 and all other provisions regarding decision making of directors where the company has only one director.

While the judge's decision cannot be viewed as a permanent, fatal blow to sole director authority in model article companies, it is undoubtedly a concern and may well create practical issues for directors and proposed administrators alike unless and until this issue is grappled by another court.

MATTHEW WEAVER QC is a barrister at Radcliffe Chambers.

Recent case summaries

The latest insolvency update from **Kate Rogers** and **James Fagan**.

***Karapetian* v. *Duffy & Anor* [2022] EWHC 1053 (Ch)**

Mr Arsen Karapetian, a creditor of the bankrupt, appealed under r15.35 of the Insolvency (England and Wales) Rules 2016, seeking a reversal or variation of the decision of creditors not to approve an IVA proposed by the bankrupt, Mr Rossi (the bankrupt).

Mr Karapetian was admitted to vote in the sum of £500,000, a sum due pursuant to a loan agreement with the bankrupt, however he contended that he was owed a further €1,283,847 (£1,094,166) under a personal guarantee (the personal guarantee). Had this further sum been admitted for voting purposes, the IVA would have been approved.

The nominee's firm had written to Mr Karapetian by email, giving an incorrect time for the virtual meeting of creditors, suggesting that it was 10:00 am Moscow time, when it was in fact 10:00 am London time. The link to the zoom meeting and accompanying text confirmed the correct time, however, Mr Karapetian said he did not speak English. Mr Karapetian logged onto the meeting three hours early. He could not wait for the meeting to start, so he emailed a proxy, together with loan documentation and the personal guarantee, but without explanation. An email attaching a reconciliation of sums due under the personal guarantee was stuck in his outbox and did not send.

The nominee did seek to clarify the total sum owed to Mr Karapetian during the meeting, but did not receive a response. He had no proof of debt and no informal statement of what was due and owing.

The court's task, on a challenge to the existence of a debt, is to determine whether it is proven on the balance of probabilities. For various reasons, the court did not accept that, on proper construction of the personal guarantee, the bankrupt was liable in debt to Mr Karapetian. Even if there was a liability, Mr Karapetian had not discharged the burden, as a creditor, of showing what that liability was, so that a minimum value could be ascribed to it. Further there was no evidence of loss that might sound in damages.

> **"The obligation is on the creditor to put their claim forward with appropriate supporting evidence to make out their claim."**

The provision of an incorrect meeting time was an irregularity, but it was not material. The chair of the meeting must evaluate claims *made by creditors*. The obligation is on the creditor to put their claim forward with appropriate supporting evidence to make out their claim. The email stuck in the creditor's outbox was not itself an irregularity, neither was the refusal to allow the bankrupt to pass on messages from the creditor. It was the failure to put the claim properly, not the inaccurate meeting time, that meant the €1,283,847 was not admitted for voting, therefore the application was dismissed.

***Re Changtel Solutions UK Limited (In liquidation)* [2022] EWHC 694**

Liquidators applied under s127 of the Insolvency Act 1986 for recovery of sums paid by the company, Changtel Solutions UK Limited (in liquidation), in the period between the presentation of a winding-up petition and the making of a winding-up order. The judgment concerned five payments (totalling £47,053.28) made by the company to the respondent, G4S Secure Solutions (UK) Ltd, for the provision of security services. The respondent resisted the application on several grounds including that the claim was time-barred under s9 of the Limitation Act 1980, that the court should validate the payments and/or the respondent had a change of position defence to the restitutionary claim arising out of s127.

ICC Judge Barber found against the respondent on all points, granting the application and ordering repayment. The case is of interest because it provides useful guidance on calculating limitation periods and, significantly, clarifies the availability of the change of position defence in s127 applications.

The respondent argued that the application was time-barred because it

> **"The court held that the change of position defence to a s127 application is available. However, the circumstances in which the defence can succeed are constrained."**

was issued more than six years after the company made the payments. For the purposes of calculating limitation, the judgment notes that the purpose of s127, to preserve the *pari passu* principle in a liquidation, is only brought into operation by the winding-up order. Until then the principle is only prospectively engaged. In other words, the legal consequence of the transaction at the time it was conducted depends on what happens subsequently. As a result, the cause of action under s127 is not complete until the making of the winding-up order. Therefore, time runs from the date of the winding-up order and not the date of payment and the application was not time-barred.

On the subject of change of position, the court held that the change of position defence to a s127 application is available. However, the circumstances in which the defence can succeed are constrained in the same way and for the same reasons as the exercise of the court's discretion to validate. The applicable principles governing the circumstances in which validation should be ordered are set out in *Express Electrical Distributors Ltd* v. *Beavis* [2016] 1 WLR 4783.

The respondent's evidence did not establish that it had incurred costs in connection with the security services other than in the ordinary course of things nor did it prove that the respondent had changed its position in the belief the payments were valid. Therefore, the defence failed. □

KATE ROGERS is a barrister at Radcliffe Chambers.

JAMES FAGAN is a barrister at Radcliffe Chambers.

Sanctions: the situation in the UK

Fergus Randolph QC provides an overview of sanctions regimes relevant to the UK for legal professionals.

Before Brexit, there were essentially three sanctions regimes relevant to UK legal professionals – those imposed by the UN, those by the US and those by the EU. Each regime was different and depending on the politics of the time, different countries and entities/individuals were targeted. That said, there was often a uniformity of approach, if not procedure, and it was therefore important for the UK legal professional to keep an eye on all three regimes.

Kadi changed everything

Prior to the *Kadi judgment* of the Court of Justice of the European Union,[1] challenges to individual designations were very complex – the decision-makers were given a wider margin of discretion and courts were generally unwilling to go behind designation decisions. That all changed with the *Kadi* judgment, in which the CJEU made it extremely clear that the light judicial touch that characterised the US position was not appropriate in the EU arena where fundamental rights were to be protected, and be seen to be protected. The *Kadi* judgment led to a number of successful challenges to designations, in particular in relation to Iranian sanctions.

Although UN and EU sanctions were administered in the UK by HM Treasury for many years before Brexit, the separation from the EU led to the need for the UK to establish and operate its own sanctions regime. The Office of Financial Sanctions Implementation (OFSI) was established in 2016 in order to 'provide a high quality service to the private sector, working closely with law enforcement, to help ensure that financial sanctions are properly understood, implemented and enforced.' In the run-up to Brexit, the Sanctions and Anti-Money Laundering Act 2018 [2018 Act] was passed, giving the UK the continued ability post-Brexit to implement UN sanctions regimes and to use sanctions to meet national security and foreign policy objectives.

Recent events

The invasion by Russia of Ukraine, leading to the consequential sanctions on Russian entities/individuals across the globe, has marked the first large-scale implementation of sanctions by the UK post-Brexit. That implementation has been largely carried out by iterative amendments to the Russia (Sanctions) (EU Exit) Regulations 2019 [2019 regulations]. Nearly a month after the invasion, the Economic Crime (Transparency and Enforcement) Act 2022 [2022 Act] was passed, which gave the UK government *inter alia* the power to designate entities/individuals under an urgent

procedure in addition to the existing standard procedure. The standard procedure only allowed entities/individuals to be designated if the appropriate minister had reasonable grounds to suspect that the entity/individual was an 'involved person'. An involved person is one who is or who has been involved in an activity specified in the relevant specific regulations, is owned or controlled directly by a person who is or has been so involved, is acting on behalf of or at the direction of a person who is or has been so involved or is a member of, or associated with a person who is or has been so involved – see section 11 of the 2018 Act. The alternative urgent procedure allows the relevant minister to designate an entity/individual that/who has already been designated by the US, the EU, Australia, Canada or any other country specified for this purpose in regulations made by an appropriate minister, and where that minister considers that it is in the public interest to make such a designation. The 2022 Act was passed very rapidly to combat the perceived slowness of the UK to impose sanctions on entities/individuals compared to other authorities, particular in the US and the EU. The Act also – as is clear from its title – sought to impose transparency requirements on beneficial owners, including by way of a compulsory register of overseas entities. Much legal activity since the invasion has taken place in offshore jurisdictions (see page 14 for more on the impact of sanctions in offshore jurisdictions).

> "The separation from the EU led to the need for the UK to establish and operate its own sanctions regime."

Regulations and UK persons

The 2019 regulations as amended apply extra-territorially insofar as UK persons are concerned – regulation 3(1) provides in terms that such person may contravene a relevant prohibition by conduct wholly or partly outside the UK. A 'relevant prohibition' covers those restrictions covering finance, trade (which now includes trade in services such as socia media services) and ships. The remainder of this article will concentrate on financial restrictions, which in large part, comprise asset freezes, as this is where most legal professionals have recently been impacted, either directly for clients that were the subject of asset freezes, or indirectly for clients who interacted with such designated entities/persons.

Regulation 11(1) sets out the basic principles in relation to asset freezes. It provides as follows:

'A person (P) must not deal with funds or economic resources owned, held or controlled by a designated person if P knows, or has reasonable cause to suspect, that P is dealing with such funds or economic resources.'

Regulation 11(4) defines the scope of 'deals with funds' as follows:

'For the purposes of paragraph (1) a person "deals with" funds if the person –

(a) uses, alters, moves, transfers or allows access to the funds;
(b) deals with the funds in any other way that would result in any change in volume, amount, location, ownership, possession, character or destination; or
(c) makes any other change, including portfolio management, that would enable use of the funds'

Regulation 11(5) defines the scope of 'deals with economic resources' as follows:

'For the purposes of paragraph (1) a person "deals with economic resources" if the person –

(a) exchanges the economic resources for funds, goods or services; or
(b) uses the economic resources in exchange for funds, goods or services (whether by pledging them as security or otherwise.'

Regulation 11(6) defines ownership, holding or control as follows:

'The reference in paragraph (1) to funds or economic resources that are "owned, held or controlled" by a person includes, in particular, a reference to –

(a) funds or economic resources in which the person has any legal or equitable interest, regardless of whether the interest is held jointly with any other person and regardless of whether any other person holds an interest in the funds or economic resources;
(b) any tangible property (other than real property), or bearer security, that is comprised in funds or economic resources and is in the possession of the person'

Regulation 7 defines the meaning of 'owned or controlled directly or indirectly' as follows:

'(1) A person who is not an individual (C) is "owned or controlled directly or indirectly" by another person (P) if either of the following two conditions is met (or both are met).
(2) The first condition is that P –
  (a) holds directly or indirectly more than 50% of the shares in C;
  (b) holds directly or indirectly more that 50% of the voting rights in C; or
  (c) holds the right directly or indirectly to appoint or remove a majority of the board of directors of C'
(3) Schedule 1 contains provision applying for the purpose of interpreting paragraph (2).
(4) The second condition is that it is reasonable, having regard to all the circumstances, to expect that P would (if P chose to) be able, in most cases or in significant respects, by whatever means and whether directly or indirectly, to achieve the result that affairs of C are conducted in accordance with P's wishes.

It is clear from the above that there is a large degree of subjectivity attached to the definitions, which in turn has the effect of making the task of relevant legal representatives very sensitive and complex. This is particularly concerning given the fact that breach of these provisions can give rise to criminal penalties – clients are therefore naturally anxious to ensure that the advice given is as accurate as it can be. Given the possible dire consequences of 'getting it wrong', legal advisers cannot be criticised if they take the most risk-averse approach possible.

Legal representation and payment

It should be noted that unlike the US regime, it is possible for legal representatives to be paid for legal services provided to clients who are designated. However, such payment can only be made once a relevant licence from OFSI has been obtained, unless the provisions of a general licence are applicable. OFSI licences are governed by regulation 64.

Paragraph (1) thereof provides as follows:

'The prohibitions in regulations 11 to 15 (asset freezes, etc), 16 (securities and money market instruments), 17 (loans and credit arrangements), 17A (correspondent banking relationships etc), 18 (investments in relation to non-government controlled Ukranian territory) and 18A (provision of foreign reserve and asset management services) do not apply to anything done under the authority of a licence issued by the Treasury under this paragraph.'

Insofar as concerns asset freezes, the relevant licence possibilities are set out in part 1 of schedule 5.

Paragraph 3 thereof provides that a licence can be granted for:

'Legal Services: To enable the payment of –

(a) reasonable professional fees for the provision of legal services; or
(b) reasonable expenses associated with the provision of legal services.'

It is critical therefore for legal advisers of clients who are designated to obtain a relevant licence from OFSI. Given OFSI's present heavy workload, there are delays in obtaining licences, which can cause problems in relation to the payment of work carried out prior to licences being approved. If in doubt, legal advisers should always contact OFSI and/or seek specialist legal advice. ◻

[1] Joined cases C-402/05P and C-415/05P: *Kadi* v. *Council of the EU* [ECLI:EU:C:2008:461]

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Sanctions: ripples offshore

A team of offshore lawyers explain the impact of Russian sanctions in the British crown dependencies and offshore territories.

The sanctions imposed by the European Union, the United Kingdom and the United States, among others, in the wake of Russia's unjustified invasion of Ukraine have raised a number of issues for the British crown dependencies (CDs) and overseas territories (OTs).

This article looks at the financial sanctions regimes applicable in the British Virgin Islands (BVI), the Cayman Islands, Guernsey and Jersey, and the key practical challenges currently being faced in those jurisdictions, including by IPs and those advising them. Due to the nature of business carried on in those jurisdictions, which are popular domiciles for investment funds due to their tax neutrality, the context in which issues have tended to arise are in relation to the ongoing management of investments that are subject to sanctions or in relation to distributions out of a fund which may be caught by sanctions. Issues have also arisen in relation to charging professional fees.

The financial sanctions frameworks

The financial sanctions applicable in the four jurisdictions considered by this article are broadly similar. The BVI and the Cayman Islands are OTs and Guernsey and Jersey are CDs. As such, the financial sanctions in force are essentially the same as those in force in the UK (see page 12 for more on the legal situation within the UK). The UK implements both the UN sanctions and its own financial sanctions, via a combination of primary and secondary legislation (ie statutes and statutory instruments). UK sanctions are extended to or adopted by the OTs and CDs, with certain modifications, by Overseas Territories Orders or other legislation in the CDs. In addition, the governors of the BVI and Cayman Islands, the Policy & Resources Committee in Guernsey and the Ministry of External Relations in Jersey can impose further financial sanctions under domestic legislation.

The financial sanctions in force in each of the four territories are applicable to any person (whether natural or legal) in, or carrying out activities in, that jurisdiction, and all nationals and legal persons established under the laws of that jurisdiction, irrespective of where in the world they are located, as well as to certain non-nationals ordinarily resident therein.

Although financial sanctions imposed by the EU, US and others do not have direct legal effect in the OTs or CDs, in practice they may be observed by service providers in those offshore jurisdictions.

Financial sanctions and designated persons

Financial sanctions come in many forms, with the most common types including asset freezes and restrictions on access to a variety of financial markets and services, including investment bans, restrictions on access to capital markets or international payment systems, and directions to cease banking relationships and activities. As a first step, review of restricted activity or 'sectoral sanctions' that may apply to the type of financial services or investment must be undertaken both at the time of engagement and frequently thereafter against the most current sanctions legislation.

In order to know whether a financial sanction is applicable to a particular individual or entity, daily checks need to be conducted against the consolidated sanctions list of designated persons (the consolidated list) published by HM Treasury's Office of Financial Sanctions Implementation (OFSI).[1] The consolidated list does not contain any domestic sanctions imposed in one of the offshore jurisdictions, or any listings imposed by other countries or organisations (such as the EU or the US), which need to be checked separately. The same difficulties that arise onshore in respect of reconciling this 'patchwork quilt' of financial sanctions, as well as the differing approaches taken by the EU, the UK and the US, arise in those offshore jurisdictions.

> "In order to know whether a financial sanction is applicable to a particular individual or entity, daily checks need to be conducted against the consolidated sanctions list of designated persons."

In a funds context, as the fund vehicle conducts initial and ongoing due diligence on its investors, including the identification and verification of the ultimate beneficial owners of an investor who is not a natural person, it is generally straightforward to identify whether a designated person is invested in an investment fund. Where a designated person has (as is invariably the case) invested via a separate entity or structure, the relevant sanctions regulations will set out the rules to be considered in determining whether the designated person 'owns or controls' that investment. This comes down to whether the designated person holds (directly or indirectly) more than 50% of the shares (or equivalent rights to share in profits or capital) or voting rights (or equivalent rights) in the vehicle, or whether the designated person has the right (directly or indirectly) to appoint or remove a majority of the board of directors (or equivalent management body) of the entity. An important point to note is the UK does not aggregate the ownership or controlling interests of multiple designated persons to reach the 50% or more ownership interest, unlike the EU and US Russion sanctions regimes.

So far, so good. However, the position becomes more difficult when the investor in a fund is not a designated person, but a close relative such as a spouse or child. These kinds of relationships may be identified as part of the onboarding due diligence process undertaken by investment funds, where such persons are subjected to enhanced due diligence by virtue of being treated as 'politically exposed persons', but additional checks may be necessary. The UK sanctions regulations provide that a person is owned or controlled by a designated person if it is reasonable, in all the circumstances, to expect that the designated person would be able to have that person's affairs conducted in accordance with the designated person's wishes. This is a very broad, objective test which may be difficult to apply in practice.

Asset freezes

Where an investment fund knows, or has reasonable cause to suspect, that it is in possession or control of, or is otherwise dealing with, funds or economic resources owned or controlled by a designated person, the fund must freeze those funds or economic resources and not deal with them or make them available to, or for the benefit of, the designated person (absent any exemption or licence). This is commonly referred to as an 'asset freeze' and is the main way in which offshore funds have, so far, been impacted by the recent sanctions escalation.

The acts constituting 'dealing' with an investor's interest in a fund are extensive, including (among other prohibited actions) using, altering, moving, transferring or allowing access to the interest and dealing with the interest in a way that would result in any change in its volume, amount, location, ownership or character. In practice, and in the absence of any on-point general licence or guidance, this means that a fund must not process any redemption of, or make any distributions in respect of, the frozen interest, must not accept any additional subscriptions from the designated person, and must not otherwise alter, move or allow the designated person to access or receive the benefit of the investment. Additional complexities may arise in practice, dependent upon the precise terms of an investment fund, in determining how far an 'asset freeze' may extend and what actions, such as payment of fees, may be permitted at the fund level.

The position also changes where, rather than a minority interest, a designated person owns or controls a majority interest of greater than 50% in an investment fund. Where this fact pattern exists, the entire fund vehicle will be considered to be 'owned and controlled' by the relevant designated person and will itself become a sanctioned vehicle. There must then be no 'dealings' with that entity or its assets, meaning that, for service providers such as IPs and legal counsel, no fees can be paid absent a licence, and many service providers will terminate the relationship.

> "The position becomes more difficult when the investor in a fund is not a designated person, but a close relative such as a spouse or child."

Reporting and licences

Where an investment fund and its service providers know or have reasonable cause to suspect contact with a designated person, they must also comply with their respective reporting obligations by submitting the appropriate reports to the relevant authority, as soon as is practicable. Where the circumstances warrant it, ie where there is a suspicion of criminal conduct such as an attempt to circumvent applicable financial sanctions, additional suspicious activity reporting may also be required. The governors of the BVI and Cayman Islands are the competent authorities for implementation of financial sanctions measures in those jurisdictions, though in the Cayman Islands, the power to receive sanctions reports has been delegated to the Cayman Islands Financial Reporting Authority. The Minister for External Relations in Jersey and the Policy & Resources Committee in Guernsey are the competent authorities for sanctions legislation and receiving reports in the CDs.

The competent authorities may also issue licences to allow an activity or transaction that would otherwise be prohibited by the applicable sanctions legislation. A licence may either be general or specific. Guernsey has issued several general licences in relation to the current Russian sanctions, mirroring similar general licences in the UK. While no general licences have been issued in the BVI, Cayman or Jersey, it is still early days. Governments grant general licences to permit parties a period of time to wind-up their business dealings with designated persons in an orderly manner or may permit ongoing limited activity where it is deemed beneficial overall. A party may apply for a specific licence, only applicable to them that may be granted in certain circumstances or 'derogations' set out in the applicable sanctions regulations. Usually, licences will be capable of being applied for to meet the 'basic needs' of a designated person, to enable payment of reasonable legal fees, to pay reasonable fees or service charges arising out of the holding or maintenance of frozen funds or economic resources, to implement certain pre-existing judicial decisions and/or to enable anything to be done to deal with an extraordinary situation.

Summary

The Russian invasion of Ukraine is an extraordinary situation. Sanctions legislation does not and cannot anticipate the nuances of each industry sector so, whilst the offshore investment industry is certainly responding and adjusting to the fast pace of change in this area, it is hoped that, with time, we will see some guidance, or standard practices evolve, resolving some of the practical questions and obstacles currently being seen. □

[1] The consolidated list is available here: https://www.gov.uk/government/publications/financial-sanctions-consolidated-list-of-targets.

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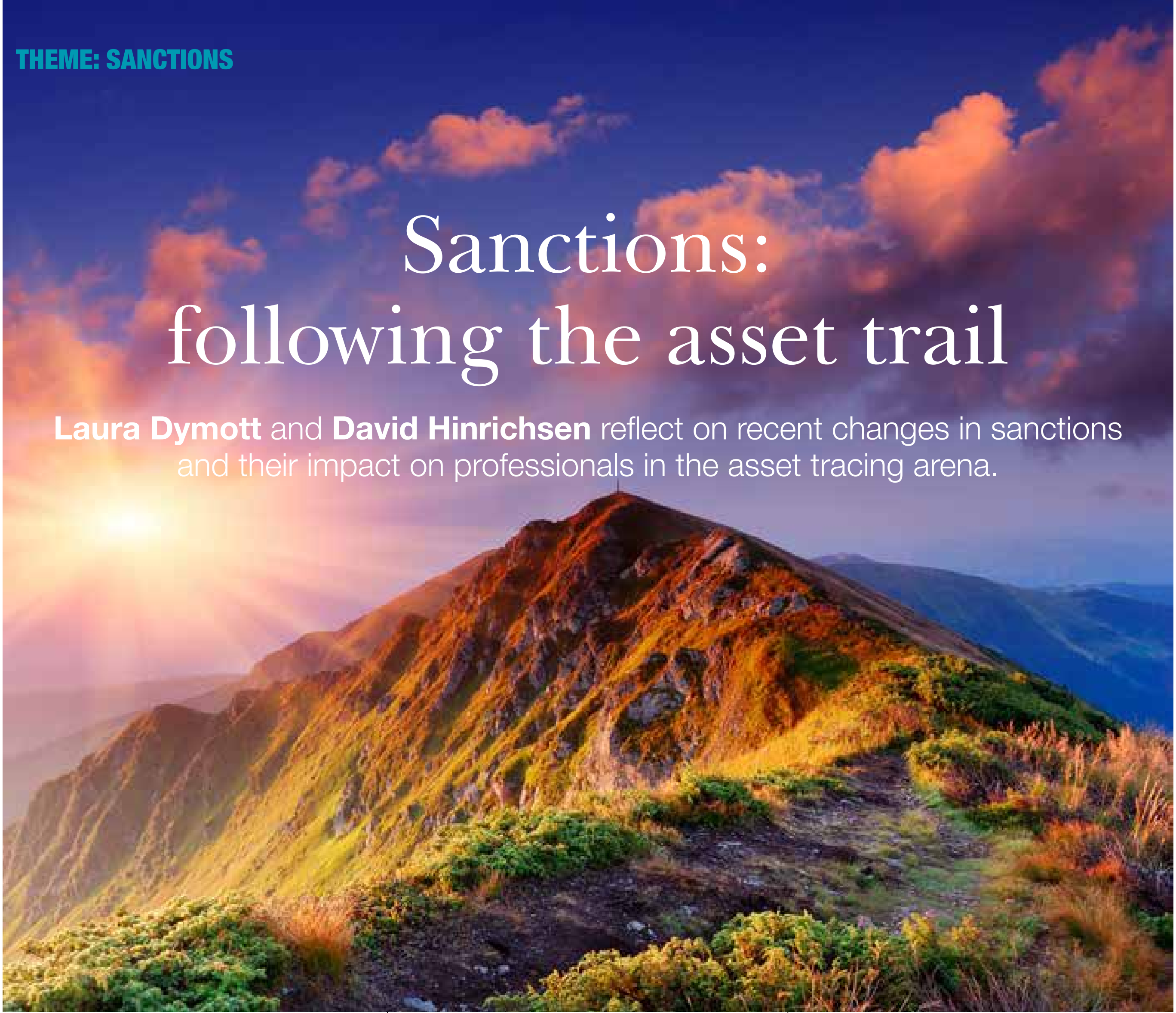

Sanctions: following the asset trail

Laura Dymott and **David Hinrichsen** reflect on recent changes in sanctions and their impact on professionals in the asset tracing arena.

The tragic events unfolding in Ukraine mark perhaps only the start of the consequences of this war. Attempts to destabilise Russia's ability to continue its invasion are demonstrated by the most significant overhaul of the sanctions regime since counter-terrorism sanctions introduced by the United Nations post 9/11.[1] Revised UK legislation under the Russia (Sanctions) (EU Exit) (Amendment) Regulations 2022 came into force on 10 February 2022 updating the original 2019 legislation that set out in detail the restrictions in relation to 'designated' or 'involved' persons regarding Russia's efforts to undermine Ukraine's sovereignty and independence.

Under the revised legislation, and in fast response to Russia's full-scale invasion, increasing numbers of Russian individuals now find their assets frozen, rights to any future financial benefit from such assets removed and are subject to travel bans (removing their right to enter the UK). This is as a result of the much wider catch-all clauses in the 2022 regulations of 'obtaining a benefit from or supporting the government of Russia'.

One of the most recent changes implemented by the UK government is to ban UK accountancy, consultancy and PR firms from providing advice to Russian businesses, which account for 10% of Russian imports in these sectors.[2] Social media and appstore companies are also required to take action to block content from RT and Sputnik to help avoid the spread of disinformation; however, lawyers are presently[3] still able to provide their services.

Impact on assets

Targeted asset freezes are a common and relatively simple form of financial sanction. They apply to named individuals and entities with the aim of restricting their access to funds and economic resources. Where assets are sanctioned, the funds and economic resources are 'frozen' immediately in the entity that is in possession or control of the asset at that time. Asset freezing does not confer a change of ownership of those assets, and it may not constitute a confiscation or transfer; however, it does restrict (ie removes) the financial benefit receivable by a sanctioned individual when that asset is sold, or during the period of ownership.[4]

While it remains to be seen what impact the increase in financial sanctions will have on the nature and outcome of the war, it is clear that the consequential media attention has provided increased public transparency over assets held by certain individuals. Where some asset and property connections may have historically been anecdotal, investigative journalists all over the world have been keen to tie together the strings from the various offshore leaks over the years with other open-source information. While this could be good news for those looking to recover assets from, and against, sanctioned individuals, it has also reinforced some of the fundamental issues asset recovery professionals commonly have regarding certain classes of assets such as trust-owned property. Assets held on trust have their beneficial use divorced from their legal ownership, raising questions as to whether a trust-owned asset can realistically be subject to successful sanction or recovery. Where legal ownership rests with independent trustees and beneficial enjoyment is purely on an arms-length basis through lease or rent, as has been alleged in the case of Alisher Usmanov, anyone looking to recover assets may face a difficult hurdle.

Utilising the available legal tools and powers of inquiry is key when looking to recover such assets. For example, if assets are being traced in an insolvency scenario, office-holders' statutory powers are wide-ranging in the context of obtaining information and can in many cases be exported internationally. The information sought can then be analysed to understand the basis of the use of a particular asset, the benefit historically gained and likely to be gained in the future, as well as the extent of any control or influence the owner or trustee has over that asset. This remains a prime opportunity for office-holders, forensic accounting professionals and investigators to work together to identify and trace assets, and assess their connection to a recovery target in order to challenge potentially artificial attempts to ringfence or shield assets from the view of creditors or as – in the current climate – government agencies. In the context of trusts, forensic analysis of trust accounts, transactional histories and communication histories between stakeholders (where available) provide a clearer picture where legal constructs may have been utilised to obfuscate the economic reality.

> **"In short, just because assets are sanctioned, it does not mean they are easier or harder to trace; this process is subject to the typical hurdles in the relevant jurisdiction relating to the ability to confirm and evidence ownership."**

Impact on ability to act

So how else do sanctions affect the ability of forensic, litigation and insolvency professionals to trace or realise assets? In short, just because assets are sanctioned, it does not mean they are easier or harder to trace; this process is subject to the typical hurdles in the relevant jurisdiction relating to the ability to confirm and evidence ownership. However, professionals continue to have an obligation to report the existence of assets likely subject to sanction to the Office of Financial Sanctions Implementation (OFSI). Additional compliance obligations also extend to the requirements under the usual anti-money laundering provisions (such as suspicious activity reports). While this obligation is always present as part of any client take-on protocol and throughout the handling of a client matter, in the context of financial sanctions, these obligations are amplified.

It is worth bearing in mind the wide-ranging application of the sanctions legislation. Among other things, any form of 'dealing with' funds, resources, securities or money market instruments of a designated person is essentially forbidden. Even in cases without an obvious sanctions impact, but with existing levels of opacity of underlying stakeholder identities and funds, this is a reminder that gaining a thorough understanding of transactional histories and connections through sound forensic examination is key to ensuring compliance and identifying potential instances of sanctions application.

Once assets are identified and traced, realising assets subject to sanctions presents an additional challenge. A licence is generally required to allow any activity prohibited by financial sanctions including the realisation of those assets, even if this is for the benefit of non-sanctioned parties, such as creditors in the event of an insolvency of a sanctioned individual or company. In the UK, this licence is obtained from the OFSI and is provided only on very specific legal grounds. Such a licence is likely required both in respect of acting in any professional capacity for clients subject to sanction or acting for a client seeking recovery of an asset now subject to sanction.

A key judgment[5] in recent weeks highlighted a BVI law firm acting for a sanctioned Russian bank in an enforcement case against a Ukrainian businessman brought before the Ukrainian invasion. While it was ruled that a licence was required under UK sanctions legislation (which is applicable in the BVI)[6] for the law firm to continue to act and receive payment from their Russian client, it was also ruled that the receivership could not be discharged without a further licence, despite the desire by the law firm to resign in the context of potential reputational damage if they continued to act. The judge ruled that the firm's duties to the court outweighed other such considerations, highlighting the complexities involved for professional services firms operating in such circumstances.

This raises the question of how the sanctions regime will affect how professional services firms acting in the Russian litigation and insolvency market may manage such cases going forwards. Multiple professional services firms already have voluntarily pulled out from Russia and confirmed they will not take on any work promoting the interests of Russia. This was before the recent ban implemented by the UK government essentially deciding how certain UK professional services firms can operate in this sector.

As demonstrated in the recent BVI ruling, firms with existing Russian clients or those looking to return to acting for Russian clients in the future under UK law will need to consider how they manage the costs of doing so from an ethical, compliance and financial perspective. Will litigation professionals who are still able to act wish to continue to represent such clients when efforts are being made to maintain professional distance?

Impact on the future

A further angle to consider is whether there could be scope in due course for Russian individuals who are subject to current sanctions to have a claim for loss and/or damage incurred as a result of the sanctions imposed in circumstances where no direct allegation of criminal activity or handling the proceeds of crime has been levied. The ethical boundary line, currently separating the desire to penalise the government of the Russian Federation and its supporters for their behaviour from the ability for legitimate Russian businesses and individuals to trade, may become blurred in due course.

Fears of repeating previous mistakes may already be playing a role in the UK government's decision-making as to which Russian entities should be subject to sanction. As a result of enforcing sanctions against Iranian Bank Mellat in 2009, the UK government was believed to have been forced to pay a settlement worth a reported £1.3bn in 2019 on the eve of a damages hearing, after the move was previously found disproportionate and unlawful; clearly this is not an error the UK government will want to repeat.[7] It remains to be seen whether the current subjects of recent sanctions would consider making similar moves to Bank Mellat in the future, especially as regards financial losses suffered; however, it is unlikely that those who have previously enjoyed decades of free and open access to the UK's economy will simply forfeit their now sanctioned assets with no consequence.

Overall, it is clear the world of asset recovery investigation and litigation is only getting more complicated as a result of an increasingly wide-ranging sanctions framework. Insolvency office-holders, forensic accountants and specialist litigation teams are experienced in maintaining and safeguarding the value of assets, particularly if an investigation is in play querying the ownership or legitimacy of such assets. Such professionals will continue to be in demand, particularly when looking to safeguard against potential fallout in years to come, and while their ability to act may be impacted by the new sanctions in place, the role of asset recovery specialists will continue to be paramount. □

[1] https://foreignpolicy.com/2012/04/23/smart-sanctions-a-short-history/

[2] https://www.icaew.com/insights/viewpoints-on-the-news/2022/may-2022/government-bans-use-of-uk-accountants-by-russian-businesses

[3] At time of writing.

[4] For example dividends generated from a company owned by the sanctioned individual.

[5] https://www.eccourts.org/jsc-vtb-bank-v-alexander-katunin-4/

[6] https://commonslibrary.parliament.uk/research-briefings/cbp-9485/

[7] https://www.theguardian.com/world/2019/jun/18/uk-settles-13bn-claim-by-iran-bank-mellat-over-trade-ban-damages-sanctions

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Restructuring Bootcamp Delegate

"I enjoyed learning from the case studies and real-life examples as it placed the statutory framework in a practical context."
Introduction to Insolvency Classroom Delegate

Offshore options for litigation

Mark Beaumont explores litigation funding where the matter may have an overseas aspect.

Given the offshore focus in this issue, I thought it might be useful to look at the use of third-party litigation funding, after-the-event (ATE) legal expenses insurance, and other risk management and financing tools in the context of insolvency disputes with an international dimension.

There are many ways such litigation can have an offshore angle: whether it's a business based offshore that's going through an insolvency or liquidation process; an individual that's attempted to put assets out of reach in overseas jurisdictions; or disputes between parties in different countries.

> **Some jurisdictions are tricker and more expensive to litigate and enforce in than others so what we know about the asset position of the defendants and where those assets are based will be important too.**

Different measures for different jurisdictions

From an underwriting perspective, the key considerations for offshore work will be similar to the factors that IPs have to weigh up before litigating: what is the value of the claim, and will the likely legal costs (or enforcement costs) be justified? Some jurisdictions are tricker and more expensive to litigate and enforce in than others so what we know about the asset position of the defendants and where those assets are based will be important too.

When it comes to retainers, there is more flexibility in some places than others. For example, in the UK and other similar jurisdictions you have various options when it comes to instructing and paying your legal team. These include various hourly rates models, including fixed fees, conditional-fee agreements (CFAs) and partial CFAs. Alternatively, you may wish to motivate your advisers in a different way, based upon the sums recovered rather than the hours worked using a damages-based agreement (DBA).

There may also be benefits in changing the retainer as the litigation develops. For example, a DBA could be used pre-issue (for example) and a different model employed as the claim develops, to try to align interests in seeking an early settlement. In my experience, far too little consideration is given on a lot of cases to retainer models and how best to get parties working together for a common goal.

In other jurisdictions you may be more restricted and must pay the lawyers on an hourly rate model only, and if there is a lack of funds in the estate it may be necessary to approach creditors and third parties to seek financing to pursue the matter through the relevant courts.

Options for creditors

Creditors can be reluctant to invest significant sums into litigation or asset recovery, and so it may be important to present them with options. We've been asked on various cases to provide examples to creditors of what the costs and returns might look like in different scenarios:

- If the creditors funded the entirety of the action, with examples of different retainer options.
- If the creditors invested a small amount upfront to attract better terms from third-party funders. What difference would this make to pricing and what share of recoveries might ultimately go to funders?
- How creditors could insure any investment they make in a case, so that should the litigation be lost they can recover some or all of their investment from a legal expenses insurer.
- What the costs of third-party funding might look like, using either a 'return on investment' approach or a 'share of damages' model.
- How an assignment model would work and how returns might compare with other options available.

> **Offshore litigation can present both a range of challenges and also opportunities through careful selection of the right legal team, retainer and funding/insurance options.**

- The different products available post-judgement to either fund enforcement actions or generate immediate cash.

Being able to present creditors with actual options from the outset allows for more informed decision making and gives the best opportunity to maximise value from potential litigation assets.

Challenges and opportunities

In summary, offshore litigation can present both a range of challenges and also opportunities through careful selection of the right legal team, retainer and funding/insurance options. By exploring a range of products and considering the potential pros and cons of the different approaches, you can pursue more opportunities to fruition.

It can be helpful to have an independent view during both the decision making and the selection process, as well as someone in your corner when it comes to discussing the key aspects of funding agreements and insurance contracts. When thinking about the right options, do consider who you are relying upon and what their interests and motivations might be: crucially, are they aligned with your own and do they actually have the knowledge and expertise that you need? ◻

MARK BEAUMONT is co-founder of Annecto Legal Ltd, a national broker of after-the-event (ATE) legal expenses insurance and a wide range of funding for litigation and arbitration claims. Annecto is happy to assist with smaller claims under £100k as well as mid-market, large-scale and complex cases. Contact Annecto Legal on 0800 612 6587 or Mark Beaumont on **mark.beaumont@annectolegal.co.uk** or 07730 217 643.

A new regime for managing national security risk

Jai Mudhar explores the National Security and Investment Act 2021 and its implications for distressed investments, restructuring and insolvency.

The National Security and Investment Act 2021 (the Act) introduced an investment screening regime to safeguard the UK's national security (the NSI regime). The UK government has the power to review and intervene in transactions that may pose a UK national security risk. The NSI regime requires mandatory, or invites voluntary, notification to the UK government's Investment Security Unit (ISU) of an acquisition of control of certain entities or assets. The ISU's review process may introduce considerable timing delays, affecting the speed at which parties can, among other activities, complete distressed sales and enforce security. Buyers, lenders, security agents and IPs should carefully consider the applicability of the NSI regime, as non-compliance with the Act may result in a void transaction and potential civil and criminal liabilities.

Overview of the NSI regime

The NSI regime applies to:

- 'notifiable acquisitions' – acquisitions where a person gains control of a qualifying entity active in one of the 17 sensitive areas of the economy (sensitive areas) by virtue of a notifiable acquisition trigger event
- 'other in-scope acquisitions' – acquisitions where a person gains control of a qualifying entity or qualifying asset by virtue of an in-scope acquisition trigger event.

What is a qualifying entity?

A qualifying entity is any entity formed or incorporated in the UK, or any foreign entity that either (i) carries on activities in the UK, or (ii) supplies goods or services to the UK.

What is a qualifying asset?

Land, tangible moveable property, or ideas, information or techniques that have commercial or other economic value (including, trade secrets, databases, source code, algorithms, formulae, designs, plans, drawings, specifications and software) in the UK, or if located outside the UK where such assets are used in connection with activities carried on in the UK or in the supply of goods or services to the UK.

What are the 17 sensitive areas?

The 17 sensitive areas are advanced materials, advanced robotics, artificial intelligence, civil nuclear, communications, computing hardware, critical suppliers to government, cryptographic authentication, data infrastructure, defence, energy, military and dual-use, quantum technologies, satellite and space technologies, suppliers to the emergency services, synthetic biology, and transport.

What are the triggers for acquisitions?

Notifiable acquisition trigger events include where a party acquires in relation to a qualifying entity:

1. more than 25%, 50% or 75% of the shares or voting rights; or
2. voting rights (alone or with others) enabling it to secure or prevent the passage of any class of resolution governing the affairs.

In-scope acquisition trigger events include the scenarios above *and* where a party acquires:

1. the ability to materially influence the policy of the qualifying entity; or
2. a right or interest enabling it to use or control a qualifying asset.

When and who should make a mandatory notification to the ISU?

The buyer of the qualifying entity must notify the ISU of a notifiable acquisition before the acquisition.

When and who should make a voluntary notification to the ISU?

The buyer, seller or qualifying entity may make a notification to the ISU before or after an other in-scope acquisition.

What are the possible outcomes following review?

The initial assessment period is 30 working days from the date of notification, after which the ISU may grant clearance or 'call-in' the transaction for further review. Where the ISU issues a call-in notice, further investigations may take 30 working days (extendable by 45 working days or longer). During this time, the ISU may issue an interim order to prevent, limit or monitor dealing with the entity or asset. After assessment, the ISU will make a final order relating to the transaction.

When can a call-in occur?

The ISU may call-in any transaction for review if a trigger event has taken place, or arrangements which if completed would result in a trigger event. Call-in may occur on notification to the ISU or independently of a notification.

What are the consequences for non-compliance?

Failure to make a mandatory notification when required will result in the transaction being automatically void. Additionally, there are potential civil and criminal liabilities of fines of up to 5% of global turnover or £10m (whichever is higher) and/or five years imprisonment.

Considerations for lenders and security agents

Acquisition financing

Lenders financing an underlying transaction must consider whether the entity or asset the transaction relates to is a qualifying entity or qualifying asset, which may require a review. While the primary notification obligation would fall on the main transaction parties, given the consequences for non-compliance with the NSI regime it would be prudent for lenders to carry out their own due diligence and consider seeking a legal opinion on the applicability of the NSI regime to the transaction.

In the event a mandatory notification obligation arises for an acquisition, lenders providing financing should consider the inclusion of protections (ie through conditions precedent, representations, undertakings and events of default clauses) in the finance documents. These protections require parties to consider the application of the Act to the transaction.

Loan agreements

Granting a loan is unlikely to pose a risk to national security. However, loans may still be scrutinised under the NSI regime where:

(a) the loan agreement provides the lender(s) with control or material influence over the borrower or the security granted by the borrower; or

(b) the borrower's activities may trigger mandatory notification or a call-in by the government.

While it is uncommon for loan agreements to give the control rights detailed in the first point above, lenders should be mindful of unintentionally triggering the NSI regime. For example, lenders may have a material influence over the policy of a qualifying entity where the borrower is distressed and has no other option but to comply with what lenders require. This acquisition of control may be subject to a call-in and a voluntary notification should be considered to mitigate the risk, particularly if the borrower operates in a sensitive area.

Security

Entering into security in which (i) shares of a qualifying entity are charged, or (ii) a qualifying asset is secured, will not usually provide lenders with absolute control or material influence over the policy of an entity at the outset and is therefore unlikely to trigger the application of the NSI regime. The security would usually need to become enforceable for the control to arise. If, however, control or material influence is expressly granted on the creation of security, notification to the ISU would be required before entry into the security document.

Enforcement of security may trigger the NSI regime where a borrower has granted security over:

i. shares of a qualifying entity operating in a sensitive area and the security becomes enforceable, a mandatory notification may be required;
ii. a qualifying asset, and the enforcement of security would entail the transfer of a right to use or control of a qualifying asset, a voluntary notification may be recommended; and
iii. shares of a qualifying entity not operating in a sensitive area and the security becomes enforceable, a voluntary notification should be considered.

Considerations for IPs

Insolvency practitioners must consider whether an action, such as a restructuring or reorganisation, distressed sale process, or their appointment as an office-holder, falls within the scope of the Act.

Appointment

The appointment of an administrator or foreign office-holder will not trigger the application of the NSI regime, as there is an express carve-out under the Act. The Act does not contain a similar express carve-out for the appointment of a liquidator or receiver. A trigger event takes place when a person gains 'control' of a qualifying entity or qualifying asset. A person gains control of a qualifying entity or qualifying asset if the person acquires a right or interest in, or in relation to, the entity and a trigger event occurs.

Before the appointment of a liquidator or receiver, it is important to assess whether a mandatory notification is required due to the company falling within a sensitive area and, if not, whether a voluntary notification would be prudent.

Insolvency sales

If an administrator, liquidator or receiver is seeking to dispose of shares or assets owned by the insolvent company, the sale may trigger the NSI regime as the Act does not contain a carve-out for the sale of a business or asset in an insolvency process. Parties contemplating such transactions should to take into account the time necessary for a review by the ISU.

A mandatory notification would likely be required where there is a share sale or debt-for-equity swap in relation to a qualifying entity operating in a sensitive area. An asset sale of a qualifying asset will not trigger a mandatory notification. Office-holders or receivers should consider the applicability of a voluntary notification. UK government guidance provides that the acquisition of assets is likely to be called-in less frequently, in comparison to the acquisitions of entities. Assets sales are most at risk of call-in if the asset is used in a sensitive area.

Implications for distressed acquisitions

The sale of a distressed company is often time sensitive; given there is no mechanism for expediting notification applications, the timing for obtaining approval may be problematic. Given the urgency with which clearance will need to be sought, it is important to ensure that all parties are aware of the ISU notification process and of the need to work together to ensure that a notification can be made as quickly as possible, notwithstanding where the responsibility of notification falls.

Conclusion

The NSI regime introduces the possibility of delays in high-risk, time-sensitive transactions. Transaction parties should consider carefully the applicability of the NSI regime to the transaction and seek to make notifications as early as possible. □

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How Recovery First can assist in the solvent closure of a law firm

David Johnstone explains how Recovery First provides services to close a law firm in an SRA-compliant and efficient fashion.

Law firm partners may make the decision to close their firm for a number of reasons, including retirement, career changes or financial difficulties. As the legal sector is closely regulated, closure of a law firm can be a particularly complex matter.

SRA compliance and an orderly closure should always be a priority to protect the interest of clients. There are many things to consider when closing a law firm, such as what will happen to staff, who will take over files and obtaining appropriate run-off cover. Due to the complexities involved with a solvent law firm closure, it is essential that the closure is planned for well in advance to prevent a disorderly closure.

The SRA has provided some guidance on ensuring an orderly closure and SRA compliance on its website at **www.sra.org.uk/solicitors/guidance/closing-down-your-practice/**.

What happens when a law firm closes?

When a firm of solicitors closes, they must notify their clients of their intention to cease trading and inform them of what will happen to their case as early as possible.

They must inform the SRA of their intention to close using a firm closure notification form as soon as possible. They should also notify their professional indemnity insurers and a number of other parties, a list of these parties can be found on the SRA website here: **www.sra.org.uk/solicitors/guidance/closing-down-your-practice/#checklist**. Firms should ensure that they have appropriate run-off cover in place to cover the costs of any claims made against the firm after they have closed.

Using Recovery First to assist closure of a firm

The Recovery First model can be used to assist closing law firms in the orderly run off of files, ensuring full SRA compliance.[1]

Our process involves discreetly selling a firm's cases to multiple purchasers on our panel of solicitors.[2] This mitigates the risks to the buying firms and results in a higher value for the work in progress (WIP) being recovered, while ensuring SRA compliance.

We also provide a complementary service for professional advisers who assist in the closure of law firms, such as advisory-only accountants and solicitors specialising in regulatory matters advising their peers.[3]

"We also provide a complementary service for professional advisers who assist in the closure of law firms, such as advisory-only accountants and solicitors specialising in regulatory matters advising their peers."

In some cases, we can facilitate a cash advance to cover administration/set-up costs. Our team manages the transfer of files from start to finish, placing case files with an approved law firm to protect the integrity of the client's case.

We are an accountancy service provider that has built specialised software and processes to liquidate the full value a law firm has locked into WIP over time. We monitor case progression and conclusion in real time and account back to our clients for the value realised on an agreed reporting period.

Selling WIP files as part of a solvent strategic exit

Recovery First assists and advises on all aspects of the WIP sale and provides guidance on the best approach that should be utilised for the run off of files. One of our most successful approaches to WIP sales is by allowing firms to exit the market on a phased basis.

Using a phased approach allows the staff in the exiting department to focus solely on the files that are capable of settlement before a target date. This is achieved by identifying files that are unlikely to settle before this target date and transferring those files to our panel of solicitors early using our usual file run-off methodology. Further reviews of files may take place throughout the process and, where appropriate, those files may be transferred to the panel at any point, with the remaining files being transferred on the target date.

Recovery First have many years of experience in advising and carrying out strategic exits from all legal markets.

Why choose Recovery First?

Recovery First offers a unique service to any law firm wishing to sell their WIP files. We provide a positive option for those wanting to exit a legal sector while remaining solvent and maintaining cash flow, or for those requiring a structured exit from the legal market.

Typically, those exiting are taken down a path of selling their WIP in bulk to a single purchaser, often at a heavy discount. At Recovery First, we offer an alternative approach to ensure you retain the value of your WIP in a fully outsourced, managed and compliant run off.

We guarantee 100% confidentiality for all clients. If you would like to find out more about Recovery First's process, please get in touch on a confidential basis direct via email **david.johnstone@recoveryfirst.co.uk**, telephone **07887796989**, or contact Sally Dunscombe at **sally.dunscombe@recoveryfirst.co.uk** or **07774 205 870**.

[1] https://www.recoveryfirst.co.uk/selling-work-in-progress-files/
[2] https://www.recoveryfirst.co.uk/panel-firms/
[3] https://www.recoveryfirst.co.uk/news/recovery-first-a-complementary-service-for-professional-advisers/

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Creating an online insolvency marketplace

William Minns marks the ten-year anniversary of IP-Bid by looking back at the site's origins and the conditions that brought it into being.

The main reasons cited why the open marketing of an insolvent company's business and assets is not always possible are the time and cost constraints that company directors and IPs have to work within. It was just over ten years ago that we set out to change this perception.

The insolvency code of ethics and SIPs 13 and 16 set out the ethical considerations and required practice for dealing with asset sales in insolvencies. These include considering potential purchasers, and sale decisions by IPs being transparent, understandable and readily identifiable to all third parties that could be affected by a sale.

The original idea for IP-Bid was to provide a quick effective route to market particularly for rapid pre-pack administration business and asset sales as going concerns. However, over the years IPs use of IP-Bid has expanded to include marketing business and asset sales in liquidations, for example where the company has ceased trading but has a customer list and order book.

Reinventing the wheel

Historically IP firms and insolvency chattel agents would attempt to reinvent the wheel when it came to marketing insolvent business and assets for sale. However, such an approach made less sense for medium and smaller business and asset sales where often it simply wasn't cost effective to attempt to reach a national audience on a very limited timescale.

We opened IP-Bid to paid postings at the end of 2009, with just 25 postings in Q1 2010. The number of postings each quarter fluctuated but gradually increased to between 30 and 40 per quarter by 2016 despite the number of administrations roughly halving. Even in the quiet market of 2022 postings are now in excess of 60 each quarter – an all-time high.

> **"Encouraging IPs to make postings was only half the battle. The other half was getting potential interested parties in insolvent business and assets to register and enter their business preferences on the website."**

Encouraging IPs to make postings was only half the battle. The other half was getting potential interested parties in insolvent business and assets to register and enter their business preferences on the website. Search engines such as Google did much of the hard work for us, drawing acquisitive businesses and individuals to the page – we listed the IP-Bid.com site with Google and tagged keywords such as 'insolvent business for sale' and 'insolvency market place'. It proved a relatively easy process, with few competitors online and a high number of search results for those keywords. This confirmed there is significant interest in acquiring businesses out of insolvencies.

Importantly, we decided not to go with passive listings. Instead, the site was designed to actively match insolvency practitioners looking to sell insolvent companies' business and assets with pre-registered, interested parties where the business and assets for sale match their specific requirements. The process works like this:

- The insolvency practitioner or their agent posts the business and assets for sale on the IP-Bid website.
- The website then generates emails that are sent to all the pre-registered interested parties whose requirements match the business and asset details that have been posted.
- Those interested parties can then submit expressions of interest, which are passed on to the insolvency practitioner or their agent.
- This is most likely used alongside all the usual sale processes that insolvency practitioners and their chattel agents already deploy.
- For a typical posting, in excess of 2,000 emails will be sent to potential interested parties and 14 expressions of interest will be emailed to the insolvency practitioner.

Pre-packs and principles

In 2014 the Graham report on 'much criticised' pre-pack administrations emphasised the need for transparency and

> **"It is obvious to me that the insolvency profession wants and needs its business and asset sales to be readily accepted and understood by all stakeholders, and open marketing and transparency are essential elements in achieving that."**

where possible improved marketing that complies with the six principles of good marketing with any deviation brought to creditors' attention. The website was specifically designed to address three of those principles: broadcast rather than narrow cast, publicise rather than simply publish and connectivity online.

Over the years there have been 2,484 business and asset postings, made on behalf of 208 licensed insolvency practitioners, shown to 7,182 unique registered interested parties with 25,665 expressions of interest made.

In the January to March 2022 quarter there were 105 postings, 77 for administrations and 28 for liquidations, which were live for an average of 27 days. Interestingly, 72 of these were posted prior to the formal insolvency appointment with the name of the company kept anonymous in 67 of those, presumably to avoid harming the business or generating negative publicity that the business was in trouble.

It is obvious to me that the insolvency profession wants and needs its business and asset sales to be readily accepted and understood by all stakeholders, and open marketing and transparency are essential elements in achieving that.

WILLIAM MINNS is CEO of IP-Bid.com Limited

Breaking open the shell: unlocking the anonymous ownership of UK assets

Tristan Cox, **Dalia Damanhouri** and **Andrew Laurie** explain how the new provisions of the Economic Crime (Transparency and Enforcement) Act 2022 *could* assist IPs with their inquiries.

When individuals being investigated by insolvency practitioners (IPs) decide to adopt an uncooperative approach to responding to questions, it can be as helpful to those that do so as it is frustrating to IPs seeking answers.

Seeking information from people who manage their affairs using complex offshore structures can lead to IPs and creditors experiencing considerable delay, particularly when trying to ascertain the ultimate beneficial ownership of UK property registered in the name of an overseas shell company.

When costs (and the risk of write-offs) increase, the prospect of recoveries can remain uncertain if answers and information are not forthcoming.

So how can a piece of legislation that was introduced in March as part of the UK's response to Russia's invasion of Ukraine assist IPs to break open the shell of anonymous property ownership?

Enacted in exceptional circumstances, the Economic Crime (Transparency and Enforcement) Act 2022 (the Act) is the fruition of the government's wider strategy to tackle illicit financial activity as developed over several years.

Taken as a whole, the measures that the Act introduces are expected to break down barriers to investigations and enhance the potential for asset recovery, with an increased risk of criminal sanction for individuals who seek to conceal their assets.

What does the Act introduce?

The key features of the Act are:

1. the creation of a register of overseas entities (ROE) to increase the transparency of who owns property in the UK;
2. the updating of the existing unexplained wealth order (UWO) regime, to assist with confiscating funds and other assets obtained unlawfully; and
3. amendments to existing legislation on UK sanctions to make prosecutions easier when sanctions are breached and to make the imposition of sanctions more straightforward.

The provisions relating sanctions have immediate effect, while the other provisions will be brought into force through regulations in the future.

Register of overseas entities

Consider a scenario where an IP has found that the trading address of an insolvent company is a UK property, owned solely by an overseas entity.

This gives rise to a number of questions: Did the property once belong to the insolvent company? Has it been transferred to the overseas entity? Is the overseas entity ultimately owned or controlled by the same person or people as the insolvent company?

In some cases, the very existence of overseas ownership can bring investigations to a halt if a letter to the entity in question goes unanswered.

Taking inquiries any further (such as proceedings under section 236 of the Insolvency Act 1986) could lead to disproportionate levels of costs being incurred, especially where there are limited known assets in the estate.

But what if the IP could simply go to the Companies House website, search for the overseas entity's name, and find out the identity of the people behind the entity within minutes?

This is what the Act intends the ROE to be: a centralised register of all overseas entities that own property in the UK, which sets out as a matter of public record the identities of the beneficial owners of those entities.

Scope of the ROE

In terms of whose details the ROE will contain, the Act defines a 'beneficial owner' as a person who:

- directly or indirectly holds over 25% of the shares or voting rights in the overseas entity;
- holds the right to appoint or remove a majority of the board of directors; or
- has the right to exercise (or actually exercises) significant influence or control over the overseas entity.

Once in force, the ROE will apply retrospectively to all property acquired since 1 January 1999 in England and Wales, and all property acquired since 8 December 2014 in Scotland.

The reporting obligations will be ongoing as, after registration, the overseas entity must either confirm the information previously provided is still accurate or provide updated information to the registrar every 12 months.

> **Taken as a whole, the measures that the Act introduces are expected to break down barriers to investigations and enhance the potential for asset recovery, with an increased risk of criminal sanction for individuals who seek to conceal their assets.**

The role of Companies House

Companies House must enter a restriction in the ROE in relation to a relevant property if it is satisfied that the overseas entity in question is the registered proprietor and became so after the respective dates for England and Wales and for Scotland, referred to above.

The restriction must prohibit the registration of any disposition unless certain circumstances apply.

How is compliance going to be policed?

Uncooperative individuals are not always known for keeping public records up to date and creating an obligation to provide information does not guarantee compliance.

The Act seeks to address this by providing that (i) a failure to register the relevant details and/or (ii) the submission of false information will both constitute criminal offences in respect of the overseas entity and every responsible officer of it. The overseas entity in question would also be prohibited from being able to buy, sell or mortgage UK property in the future.

The same criminal sanctions will apply should there be a transfer of land by an overseas entity in breach of the registration requirement.

Carve-out for transactions by IPs

Where the transfer of a property by an overseas entity would otherwise be prohibited by the Act, legislators have carved out an exception for entities where a yet-to-be-defined *specified insolvency practitioner* (in *specified circumstances*) has been appointed over the entity in question.

Future regulations will confirm (i) the relevant jurisdictions in which an IP being appointed will give the overseas entity the benefit of the exemption, and (ii) the relevant circumstances that must prevail in order for the exemption to apply.

ROE in practice

By design, the ROE has the potential to accelerate significantly investigations by an IP by unlocking information about the ultimate beneficial owner of UK assets, irrespective of the jurisdiction where the legal owner is located.

It is hoped as a matter of public policy that the increased risk of criminal liability will discourage individuals from trying to use overseas entities to conceal the identity of beneficial ownership of assets altogether.

However, certain shortcomings in the Act may be exploited by guileful individuals to deprive it of having the desired effect.

For instance, the Act leaves open the possibility of claiming that a company has no beneficial owner(s) due it not having a single person holding 25% or more of its shares. Similarly, the requirement that a property's ultimate beneficial owners be revealed does not address the potential divergence of ownership by corporate nominee or trustee, and those who ultimately benefit from it.

To close these loopholes, the Act's scope would need to be wider than the 25% threshold and would need to include the registration of anyone who has influence or control over the *property* itself, and not just over its corporate legal owner.

A further potential shortfall of the Act could be the pressure it places on Companies House to act as custodian of the ROE, without currently granting it additional powers of inquiry (such as to investigate and remove false information from the ROE).

The government published a white paper outlining plans to enhance Companies House's role and powers in February 2022, but unless and until these are enacted (a further economic crime bill is currently earmarked for the latter half of the year), the ROE may have limited use.

> **In some cases, the very existence of overseas ownership can bring investigations to a halt if a letter to the entity in question goes unanswered.**

Sanctions

The Act streamlines the process for implementing sanctions. In addition, the government can now designate an individual or entity as a sanctions target when they have already been designated as a sanctions target by the US, the EU, Australia or Canada (or any other country later specified by regulation).

Unexplained wealth orders

UWOs – court orders that require a person to provide details surrounding the nature and extent of their interest in property – are currently available in respect of politically exposed persons and persons suspected of involvement in serious crime. In both cases, there has to be reasonable grounds to suspect that their known lawful income would be insufficient to buy the relevant property.

The Act provides for a further ground, being that 'there are reasonable grounds for suspecting that the property has been obtained through unlawful conduct'.

The Act also creates a new category of person who can receive a UWO where the named respondent is not an individual. In these cases, officers of an entity that owns the property (including its director(s), manager(s) or partner(s), both in or outside the UK) may be required to provide the necessary information.

As with the ROE, the new changes are expected to be favourable to IPs and will provide a short-cut to crack down on complex structures that are intended to hide the true owner of property.

Conclusion

The Act is understood to be the first of many measures intended to target so-called 'dirty money' in the UK. Its three-pronged approach of introducing the ROE, broadening UWOs and streamlining sanctions will be welcomed by many (and some will feel that this is long overdue).

The ROE has the potential to breathe new life into IPs' inquiries when seeking information which previously may have been unattainable. However, without a sufficiently broad scope, the regime may fall short of giving the insight that it seeks to provide.

An upgrade of the powers and resources that are available to Companies House is needed more than ever if this impressive new regime can realise its full potential and finally break open the shell to reveal the secrets of property ownership in the UK. □

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More moratoria, maybe?

Tim Bromley-White and **Paul Keddie** look at the latest development in the part A1 moratorium's journey to be a major part of the insolvency toolkit.

Amid much waxing lyrical about 'rescue culture', the Corporate Insolvency and Governance Act 2020 (CIGA) introduced a new standalone moratorium procedure under part A1 of the Insolvency Act 1986. However, despite the government's expectations that the moratorium would be used over a thousand times per year, uptake has been slow. It is believed that in the nearly two years since CIGA was introduced the total number of moratoria is in the low double digits. The recent case of *Minor Hotel Group MEA DMCC* v. *Dymant* [2022] EWHC 340 (Ch) concerning the Corbin & King group is the first time the court has dealt with the part A1 moratorium and so is an opportune moment to consider whether the part A1 moratorium can be more than a niche tool.

A moratorium refresher

The part A1 moratorium's relative rarity means that it is perhaps useful to remind the readers what it is. The moratorium is a set of restrictions that provide a debtor company with breathing space from creditor actions so that it has the stability needed to implement a restructuring to rescue the company. During a moratorium creditors cannot enforce security or initiate insolvency proceedings. There is also a payment holiday for most pre-moratorium debts. However, there is no payment holiday for debts incurred during the moratorium or certain pre-moratorium debts. The latter includes the monitor's remuneration or expenses, rent accruing during the moratorium, wages, goods or services supplied during the moratorium and, crucially, debts arising from a contract involving financial services (eg loans).

> **"Despite the government's expectations that the moratorium would be used over a thousand times per year, uptake has been slow."**

The concept of a moratorium is not new to UK insolvency law. Administration and filing a notice of intention to appoint administrators creates a moratorium. There was formerly a moratorium in connection with a company voluntary arrangement (CVA) for small companies. There are, though, two distinguishing features of the part A1 moratorium. Firstly, it is not connected with any specific insolvency or restructuring procedure. It can be combined with a statutory restructuring process such as a scheme of arrangement, restructuring plan or CVA. Equally, it could also be used to implement a consensual restructuring outside of a process. Secondly, the part A1 moratorium is a 'debtor in possession' procedure, meaning the directors remain in control of the company and are not displaced by an insolvency office-holder. IPs are appointed as monitors of a moratorium but, as the name suggests, this role is about overseeing, and not controlling, the company.

If the part A1 moratorium is beneficial to debtor companies, why then has it been so little used since its introduction? In part, this is due to limits on the protection afforded by the part A1 moratorium. Significantly, there is no payment holiday for rent accrued during the moratorium and loans (even if the loan was incurred before the moratorium). There are also limitations on which companies are eligible for a part A1 moratorium. Notably, issuers or guarantors of bonds, or potentially even loan notes commonly found in private equity structures, of £10m or more, are excluded. CIGA's temporary restrictions on winding-up petitions and forfeiture and government financial support have also played their part in reducing the demand for a moratorium.

The moratorium process

The moratorium can be obtained by making an out-of-court filing (if a UK company with no outstanding winding-up petition) or by application to the court (if a UK company with an outstanding winding-up petition or an overseas company with sufficient connection to the UK). In either case, the directors will need to make a statement that, in their view the company is, or is likely to become, unable to pay its debts. The proposed monitors must state that, in their view, it is likely that a moratorium would result in the rescue of the company as a going concern.

It was a dispute over the monitor's duty to terminate under section A38 that led to the first court case on the part A1 moratorium.

There is a degree of tension between the requirements of the directors' and the monitor's statements. As the directors' statement requires confirmation that the company is in distress how can the proposed monitors get comfortable enough to accept the appointment and make their own statement? Given the nature of the process, monitors may also have to decide whether to make their statement on very short notice. Fortunately, the proposed monitors are able to rely on the information provided to them by the company (unless they have reason to doubt its accuracy) in order to give the statement. The guidance from the Insolvency Service published in Dear IP 135 is also sympathetic to the position of the proposed monitors. This advises that 'due diligence that needs to be undertaken should be proportionate to the size and circumstances of the company' and that there was no intention for the proposed monitor to conduct a full audit of the company.

At a minimum proposed monitors should obtain cash flow forecasts, run searches of the register of winding-up petitions and of the FCA's register, and check the company's main external debt (if bonds, the company may be ineligible for a part A1 moratorium). Ideally the proposed monitors would also obtain a list of creditors and financial information on a company by company rather than consolidated group basis (although if consolidated information is all that is available the monitors will be entitled to rely on it).

Once appointed a key duty of the monitor is to assess whether the company continues to comply with the conditions for the moratorium and to decide whether to terminate the moratorium under section A38 of the Insolvency Act 1986 if the monitor thinks:

(a) the moratorium is no longer likely to result in the rescue of the company as a going concern;

(b) the objective of rescuing the company as a going concern has been achieved;

(c) that the monitor's functions cannot be properly carried out due to failure of directors to provide necessary information; or

(d) the company is unable to pay (i) moratorium debts or (ii) pre-moratorium debts without a payment holiday.

This is supplemented by rule 1A.24 of the Insolvency (England and Wales) Rules 2016, which requires the monitor, when considering their duty under section A38, to disregard (i) any debts that the monitor has reasonable grounds for thinking are likely to be paid or compounded within five business days of the decision and (ii) any debts that the creditor has agreed to defer.

If a creditor, member or director of the company considers that it is being unfairly harmed by a decision of the monitor (including a decision to refuse to terminate the moratorium) they may apply to the court for relief.

It was a dispute over the monitor's duty to terminate under section A38 that led to the first court case on the part A1 moratorium. As a brief background, the Corbin & King group owns and operates a number of well known restaurants in London including the Wolseley and the Delaunay. Corbin & King owed a secured debt to Minor Hotels Group MEA DMCC (Minor), a group company of its majority shareholder, which Minor sought to enforce. The directors of certain members of the group (the moratoria companies) obtained moratoria to prevent this enforcement. The group's ultimate parent company entered into administration.

The first judicial decision on the moratorium is to be welcomed as confirming certain aspects of the moratorium's workings and perhaps giving companies more confidence in what is still a novel tool.

The monitors of the moratoria companies refused to terminate the moratoria on the basis that they thought Minor's debt (for which there was no payment holiday) would be repaid in full as a result of an offer from an investor, Knighthead. The form of that offer had evolved from a refinancing as part of an acquisition of the shares in the group to an offer to the parent's administrators to acquire the group for more than Minor's debt and then to an offer to refinance Minor's debt pending an auction run by the administrators. Crucially, the offers to the parent's administrators set a floor as any offer accepted by the administrators, if not from Knighthead, must have also resulted in the repayment of Minor's debt. Minor disagreed and applied to the court to have the moratoria for the moratoria companies terminated on the basis Minor had suffered unfair harm by the continuance of the moratorium.

Guidance from the court

The court dismissed Minor's challenge and in doing so set out useful guidance for future monitors. Firstly, the court confirmed that, as the duty to terminate is based on what the monitor 'thinks', Parliament's intention was to give a degree of latitude to monitors. A monitor's decision will only be open to challenge if it was made in bad faith or was irrational such that no reasonable monitor could have reached it. It is important, therefore, that monitors record their decisions and thought processes at the time, even if it is as simple as a daily internal email.

Secondly, although it was common ground that Minor's debt was a pre-moratorium debt without a payment holiday, there was a question over what was meant by 'unable to pay'. The court held that a 'commercially realistic' approach should be taken. Being able to pay includes having the 'immediate' prospect of receiving third-party funds or realising assets or having a co-obligor discharge the debt. 'Immediate' is a matter of commercial judgment for the monitor and, in this respect, Knighthead's refinancing offer provided the group with such an immediate prospect of being able to repay Minor. This is subject to the requirement in rule 1A.24 to disregard any debts likely to be repaid or compounded within five business days. Repayment expected later than five business days should be a matter of specific assessment by the monitor. The court will assess the monitor's decision as at the date of the hearing. Helpfully, this means the court will not reopen past decisions of the monitor if events have moved on.

Thirdly, the court retains discretion as to whether to order a termination of the moratorium on the basis of unfair harm. This will involve weighing up the harm caused to the applicant creditor by the moratorium continuing versus harm to the company caused by terminating the moratorium.

The first judicial decision on the moratorium is to be welcomed as confirming certain aspects of the moratorium's workings and perhaps giving companies more confidence in what is still a novel tool. With the lifting of the temporary restrictions on winding-up petitions and forfeiture, and a rise in the insolvency rate, there may be more of a need for the moratorium. □

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The tightrope of compliance: regulated entity compromises

Paul Fleming, **Emma Sadler** and **Steven Francis** outline the issues around the FCA's approach to debt compromises and provide practical insights for IPs.

The overriding objectives of the Financial Conduct Authority are to protect consumers and to maintain the integrity of the financial markets in the UK. The FCA recognises that a disorderly wind-down of a firm will risk undermining those objectives and there are obligations placed on regulated firms and controls available to the FCA to help prevent this from happening. It is a condition of obtaining regulated status that a firm has a robust wind-down plan in place. The FCA has produced detailed guidance in relation to its expectations on wind-down plans,[1] which covers the credibility of such a plan and its capability of implementation, with particular focus on liquidity and cash flow modelling, intra-group dependencies and wind-down trigger calibration.

However, even for those firms which have a suitable wind-down plan in place, the risk of the occurrence of an unforeseen event is ever-present, as has been seen over recent years with the impact of Financial Ombudsman Service decisions on a firm's requirement to undertake a past business review. Where regulated firms face financial (di)stress, the management must walk the tightrope of compliance with very many regulatory obligations (which will apply to the firm and in many cases to individual managers) while also being mindful of their duties to minimise loss to all creditors.

A telling example, is that FCA rules require firms to treat their customers fairly (TCF). The rule is deliberately open-text, placing the onus on a firm to establish how it informs day-to-day decisions on matters that affect customers. There are even doubts about whether TCF goes far enough, and the FCA is planning on introducing a new consumer duty to enable it to further enforce customer protections where firms seem unwilling or unable to proceed as the FCA wishes.[2] There is no FCA rule requiring firms to treat general creditors fairly but, under statutory and common law rules, firms are expected to protect all creditors' positions in times of financial distress.

> **"Where regulated firms face financial (di)stress, the management must walk the tightrope of compliance with very many regulatory obligations while also being mindful of their duties to minimise loss to all creditors."**

The restructuring framework in the UK is heralded as providing one of the most flexible systems promoting business and entrepreneurial activity but there is a tension with regulatory rules with which firms and their controlling personnel must comply. The FCA's approach to compromise of creditor claims is one such example of where this is evident.

Restructuring tools

UK company and insolvency law has within its armour a number of useful restructuring tools such as:

- Company voluntary arrangements
- Schemes of arrangement
- Restructuring plans (introduced by the Corporate Insolvency and Governance Act 2020)

CVAs are perhaps not quite so attractive for compromises of claims in relation to complex regulated firms due to the inability of a CVA to compromise secured or preferential creditor claims, necessarily resulting in the perception that the unsecured consumer is subject to more detrimental treatment than other institutional creditors.

A scheme of arrangement has been the tool of choice in the two most commonly reported attempts to effect compromises of creditor claims, being *Re Provident SPV Ltd* [2021] EWHC 2217 (Ch) and *Re ALL Scheme Ltd* [2022] EWHC 549 (Ch) and [2021] EWHC 1401(Ch) (hereafter

Amigo Loans. There is no requirement for the firm to be insolvent to implement a scheme of arrangement and it can result in the compromise of both creditor and member claims. However, where financial distress is evident, the helpful addition of the 'cross-class cram down' that comes with a restructuring plan enables the votes of those creditors who are economically unaffected by the plan to be discounted and the benefit of this should not be underestimated.

A scheme of arrangement was approved in the *Provident Finance* case. The FCA was represented at the convening hearing and then subsequently raised objections to the scheme in a letter placed before the judge. However, the FCA, ultimately, did not formally oppose the scheme on the basis that it considered there was a real and imminent prospect of insolvency if the scheme was not approved and it was intended that the entity would be wound down, thereby ensuring any 'upside' from the scheme would be for the benefit of the scheme creditors rather than the shareholders/ other stakeholders.

Conversely, the FCA did formally oppose the first *Amigo Loans* scheme on the basis there was no intention to wind down the business following the scheme (with the existing shareholders retaining their, potentially, profitable share in the business going forward). The court did not sanction the first scheme, which resulted in a second scheme (or schemes, in the alternative) being proposed. The existence of the second sanction application arguably justified the FCA's objections. The second schemes were unique in their approach. Firstly, there was a proposed compromise of the redress claims with a continuation of the business thereafter, provided certain conditions are met (one of which being the FCA's consent to Amigo restarting lending) (new business scheme). In the alternative, the second scheme would have involved the wind down of the business in a more cost-effective manner than an insolvency. The FCA did not oppose this application and the court has recently sanctioned the new business scheme following overwhelming support from Amigo's creditors.

Consultation on proposed guidance

In January 2022 the FCA launched a consultation on its proposed guidance for its approach to compromises of regulated firms.[3] This consultation closed on 1 March 2022. It is keen to ensure the restructuring tools available to regulated firms are utilised in such a way that does not undermine the FCA's objectives. The guidance focuses on those firms that are subject to redress claims that seek to compromise those liabilities but continue to trade. The FCA guidance codifies the approach it has taken in recent cases, making clear that it expects to be furnished with all relevant information to enable it to consider if it will raise an objection to the scheme or plan in either the convening or sanction hearing or (for a CVA) by bringing a challenge to court. The FCA states that it will object to the proposed compromise unless '*…it is the best proposal that the firm can make, which includes the firm providing the maximum amount of funding for the compromise so that consumers receive the greatest proportion of what is owed to them*'.

"It is the tension between the protection of consumers and maintenance of integrity in the market (whether real or perceived) and insolvency that appears to have fuelled the approach the FCA is now taking."

The FCA's proposed guidance on its approach is unsurprising given its overriding objective. However, it brings into sharp focus the tension that could exist with other statutory and common law duties for directors to minimise loss to all creditors. In all likelihood, the success of a compromise in this sector will depend on an evaluation of whether the only alternative to the compromise is insolvency.

This brings with it concerns in relation to the future of the sub-prime lending market. The apparent increase in FOS complaints in relation to such lenders is likely to lead to an increase in the implementation of redress schemes. This threatens the ability for some lenders to continue to trade, with the resulting effect that many lenders will vacate the market. With the rising number of people with poor credit ratings and the risk of them necessarily turning to illegal lending, there is a tension between maintaining integrity in the market by imposing additional regulatory obligations on lenders and encouraging sub-prime lenders to remain active.

Formulating a compromise

The ability for a firm to seek a compromise of its liabilities from such redress schemes is therefore vital to help maintain a spread of lender-offerings across the market. However, with the increasing focus of the FCA on ensuring these schemes are really producing the best result for consumers, is the regulatory burden too high?

The proposed guidance issued by the FCA provides helpful clarity on how to formulate such a scheme proposal. The guidance contains an extensive list of the minimum information the FCA would require a firm to provide to it. In practice we have seen increased sophistication in negotiations between firms and their advisers, and the FCA, and early and full engagement is essential.

Insolvency

Arguably, the FCA's hand is much weakened once IPs are appointed over a firm. While IPs must be mindful of the regulatory requirements and will work with the FCA to ensure the impact on consumers is as minimal as possible, they have their own statutory and regulatory code to comply with and ultimately they are in control of the business.

It is the tension between the protection of consumers and maintenance of integrity in the market (whether real or perceived) and insolvency that appears to have fuelled the approach the FCA is now taking. It is focusing on ensuring firms have a wind-down plan that is thought-through and capable of implementation and, with the proposed new guidance, it is ensuring regulated firms are clear as to what the FCA will expect if they seek to compromise consumer claims. The benefits that the UK company and insolvency regime provide are useful tools for entities in distress, but where this is applied to a regulated entity, the ability to avail themselves of these tools remains tempered by the need to walk the tightrope between regulatory and other statutory or common law compliance.

With the backdrop of the recent High Court sanctioning of meetings for the novel Amigo schemes, it is anticipated that, once the FCA guidance is issued (following closure of its consultation on 1 March 2022) practitioners will have increased clarity as to the stance of the FCA and hence the use of the available restructuring tools. □

[1] https://www.fca.org.uk/publication/thematic-reviews/tr22-1.pdf

[2] The aim is for final rules on the consumer duty to be confirmed by end July 2022 https://www.fca.org.uk/news/press-releases/fca-introduce-new-consumer-duty-drive-fundamental-shift-industry-mindset

[3] https://www.fca.org.uk/publication/guidance-consultation/gc22-1.pdf

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Juggling risk in litigation

Robin Ganguly explores other, less obvious but equally powerful, ways to transfer risk and enable litigation to be dealt with by estates outside of litigation funding.

The challenges that litigation can present are familiar to many IPs. At times there are insufficient funds to launch a claim. Litigation funding can unlock those claims, but the economics do not always add up, especially if claims are too small for funders or if the costs-to-claim value ratio is too tight to accommodate the funder's multiple. At other times there can be litigation against the estate, or the prospect of a judgment in favour of the estate being reversed on appeal, which hampers an IP's ability to use or distribute funds. However, the full range of potential solutions to those challenges are usually far less obvious. The litigation insurance industry is much less publicised than funding but is growing in size and sophistication and can provide ways to overcome these problems, either alone or in combination with litigation funding.

The way litigation risk is allocated among the various parties who form the disputes ecosystem is evolving rapidly. Litigation funders are increasingly looking to obtain principal protection insurance for their portfolios to de-risk and lower their cost of capital. Law firms and IPs are taking more cases 'on risk' because the market is demanding it of them and, perhaps to a lesser extent, because they are starting to see the opportunity to increase profits. Investors have a lot of appetite to apply their capital to alternative asset classes such as litigation, which can provide uncorrelated and high returns in times of market uncertainty and low interest rates.

Litigation insurance exists to meet the needs presented by all of these stakeholders, and the following products can be part of the IP's toolkit.

"The way litigation risk is allocated among the various parties who form the disputes ecosystem is evolving rapidly."

Judgment preservation insurance

This allows an IP to 'lock in' a favourable court judgment or arbitral award and, if that judgment or award is successfully appealed or set aside by the other party, the insurance will pay out to put the estate in the position it was in when it had the favourable ruling. This can allow the IP to safely use funds for other purposes or make distributions to creditors, in the knowledge that the legal outcome of the case is secure. The policy covers the legal risk of loss of the award, not the collection risk if the insured is successful in court but cannot enforce.

Judgment monetisation

Once a judgment is insured, it becomes a more concrete asset and the IP has a number of options to 'monetise' it by accelerating payment, and thereby avoid having to wait years to be able to benefit from the result. In the simplest situation, the judgment could be sold, and often for a higher amount when there is no appeal risk attached to it. However, sale of a judgment even if insured will inevitably involve a significant 'haircut' on the face amount.

IPs also have the option to monetise by retaining the insured judgment and borrowing against it. Cash can be obtained on a loan basis, secured against the insurance policy, much more cheaply than capital from litigation funders. The loan in these arrangements would typically be 'non-recourse' (like litigation funding), with the lender taking the risk of the IP not being able to collect on the judgment, provided that collection risk is low. Raising cash in this way can open up many possibilities to IPs, including being able to pay outstanding legal fees, pay for the pursuit of other litigation or make distributions to creditors.

Adverse judgment insurance

This can provide a solution where an estate is the defendant in an existing or potential claim that has a low risk of prevailing but still blocks the IP from getting on with his or her duties. For instance, there could be a trust claim over all of the funds in the estate, which causes paralysis. If insurance takes the risk on that claim, the IP can safely deal with the funds and assets in the estate. Alternatively, there may be an outstanding claim that is weak, but still prevents distributions to creditors until it is resolved. If the risk of paying out on that claim is transferred to insurers, distributions can safely be made years earlier.

WIP/contingency insurance

If an IP has a good claim but does not have the cash to pursue it and does not want to pay a litigation funder's returns, insurance can enable lawyers and the IP to take fee risk on the case with the comfort that they are not taking an all-or-nothing bet on the case winning.

Lawyers can act on the claim on a DBA (damages-based agreement) basis, under which they charge nothing upfront but take a percentage of the case recoveries. The lawyers will record their time (or work in progress/WIP) on an hourly basis as usual and, if the case loses, the insurance pays an agreed percentage of the accrued WIP. Law firms in this country are not generally accustomed or set up to take full fee risk on cases and the insurance can enable them to get comfortable taking on a case that they otherwise would not. In time, law firms are likely to use WIP insurance on a portfolio basis to grow the part of their litigation businesses that is high risk/high reward, as a complement to the part of their business that is more stable. IPs can also insure the fees they incur on litigation in the same way, to allow them to take significant reward if it succeeds, but mitigate downside if it fails.

Where litigation needs to be brought but an estate does not have cash or does not want to use its own cash, the alternative options of creditor funding, litigation funding and law firms and IPs taking fee risk can be modelled out and presented to creditors so that the best option can be chosen. If needed, cash flow can be obtained for the law firms and IP on a loan basis, secured on the insurance (in the same way as with judgment preservation insurance) or litigation funding can be used, particularly for disbursements.

After-the-event insurance

Most IPs are familiar with ATE insurance for opponent's costs; however, the possibility of using ATE to cover own costs is often overlooked. Sometimes an estate has the funds to pay lawyers and the IP on an hourly basis but there is no desire to risk wasting those costs if the case loses. In that situation, the incurred costs can be insured so that most of them are paid by an insurer if the case loses. This enables the IP to avoid giving away significant upside if the case wins, without risking returns for creditors.

"Creative and bespoke solutions are available to address litigation and contingent risks that IPs face and these solutions can optimise returns to creditors and help to streamline the winding up of estates."

Combining insurance with funding

Insurance and funding often go hand in hand. Funding and ATE for adverse costs is the most obvious combination, but insurance premia for judgment preservation insurance and adverse judgment insurance can be put up by a litigation funder if needed. Where law firms and IPs act on contingency, disbursements can be paid for with funding.

Cross-undertakings in damages

Insurance can potentially be available for cross-undertakings in damages where estates do not have funds to cover these but need to obtain injuctive relief.

In addition to pure, 'live' litigation risks, IPs are often confronted with other situations where there is another form of contingent risk that could result in liability for either the estate or the IP personally. Such risks can take the form of potential tax claims by the authorities, 'woodwork' claims being made late in the day, etc. Those claims ought not to stand in the way of distributions to creditors but where there is scope for one to arise an IP has to be cautious. Insurance for those types of risk has been used for many years but is often overlooked as a possibility.

This is the same sort of insurance that is used in M&A transactions where a buyer does not want to take on a risk and a seller wants a clean exit and does not want to reduce price or escrow cash. In that sense, M&A and insolvency have many considerations in common. Contingent risk insurance is available from the M&A insurance markets along with tax and warranties and indemnities insurance, which can also be of particular use to IPs when they are disposing of businesses and assets but are unable to vouch for what is being sold in the same way as a 'normal' seller would.

In conclusion, creative and bespoke solutions are available to address litigation and contingent risks that IPs face and these solutions can optimise returns to creditors and help to streamline the winding up of estates. □

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Death is not the end: escheat, bona vacantia and company restoration

Richard Clark grapples with Norman Conquest-era property principles to provide some clarity for liquidators.

When a lawyer tells you that a point is arcane, most people's reactions tend to be resigned dread that an impenetrable (and interminable) lecture is to follow. This, hopefully, is not that lecture. I've tried to boil it all down to a simple diagram, which you can skip to if you want the short and sweet version. If, however, you routinely deal with companies in liquidation and wonder what happens to their property both during and after the process, and why there's such an unjustifiably complicated hoo-ha about land (in particular), then read on.

The fact of the matter is that – for lack of legislative willingness to tackle a subject which has been put in the 'too difficult' box[1] – practitioners find themselves routinely having to grapple with a heady mix of Norman Conquest-era feudal principles grafted onto modern company law. It's uncomfortable territory and easy to get lost. I'm hoping that this article provides some clarity on what is involved (and why) and how to negotiate your way through the maze.

> **Generally the Crown will seek to avoid taking possession of land or exercising management powers in respect of it, in order to avoid fresh liabilities being incurred in respect of third parties and, in particular, environmental liabilities.**

What are the issues?

The issues concern what happens to a company's property both during liquidation and afterwards, when liquidation is complete and the company has been dissolved. The concepts are as follows:

1. *Disclaimer of onerous property.* A company's liquidator can disclaim onerous property during the liquidation. 'Onerous property' includes unprofitable contracts and other property that is not readily saleable or gives rise to a liability to pay money or perform other onerous obligations. This is particularly the case with real estate, where an obligation to remediate exists (such as environmental contamination or structural works).[2] Where disclaimer is exercised, that brings to an end the company's liabilities in respect of the property concerned, but *not* the rights and obligations of other persons in respect of it.[3]
2. *Bona vacantia.* When a company is dissolved, any property remaining in its possession transfers to the Crown (acting via the treasury solicitor, known as TSOL), or to the Duchy of Cornwall or Duchy of Lancaster as 'bona vacantia' (ownerless property).[4] Foreign companies that are dissolved do not fall subject to the bona vacantia provisions of the Companies Act, and so the legal position is that land of dissolved foreign companies is automatically subject to escheat, regardless of what the companies legislation of the country of incorporation might say.[5]
3. *Crown disclaimer of bona vacantia.* Where property vests as bona vacantia, the Crown may disclaim it.[6] This usually occurs, again, where the property in question gives rise to an onerous obligation. The Crown must do so within three years of becoming aware of the property vesting, and a person interested in the property can require the Crown to determine whether it will make a disclaimer, upon which the Crown has 12 months to do so. The effect of Crown disclaimer is the same as for disclaimer by liquidators – ie escheat (see below), with the seemingly paradoxical result that the Crown ends up reacquiring land of which it wanted to divest itself. [7]
4. *A note about title to real estate.* Key to what comes next (escheat) is the nature of title to real estate. Since the introduction of the Law of Property Act 1925, land can only be owned as 'freehold' or 'leasehold' (and more recently, commonhold). Norman the Conqueror decreed that all land belonged to him, because he was the king, and all title to estates derived from his ownership. What landowners are now commonly granted is not the physical land itself but a fictional 'estate' in it (much as a company is a legal fiction). That 'estate' is capable of coming to an end, usually where there is nobody left to take ownership of it, such as on intestacy or via disclaimer.
5. *Escheat.* So far as companies are concerned, escheat is what occurs to real estate (and real estate only) when either a liquidator or the Crown disclaims real estate, or a foreign company holding property in England and Wales is dissolved (subject to overseas legislation). In either case, the disclaimer brings to an end the freehold or leasehold 'estate' and the land reverts to the Crown (in this case, dealt with by the The Crown

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Estate (TCE)). While the title at the Land Registry will still appear, it will be noted as having been subject to escheat.

What happens to bona vacantia or escheat?

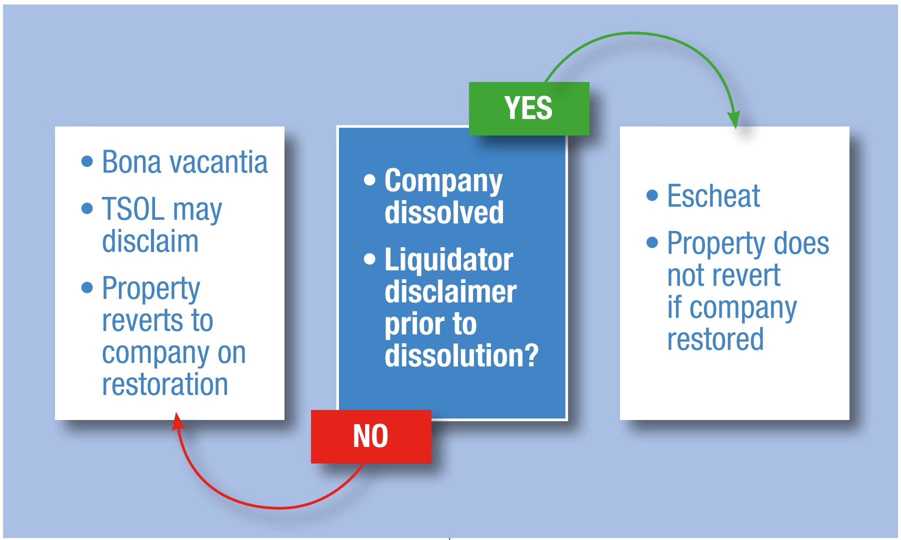
As noted above, escheat destroys the freehold or leasehold estate in land, and the land reverts to the Crown. However, it is important to note that the Crown does not 'inherit' any of the rights, obligation or liabilities of the previous owner as the freehold estate has not 'transferred' to the Crown. This becomes important in respect of the Crown's dealings, as generally the Crown will seek to avoid taking possession of land or exercising management powers in respect of it, in order to avoid fresh liabilities being incurred in respect of third parties and, in particular, environmental liabilities.

In terms of what happens next, TCE will deal with the land, subject to applications by interested parties, and the possibility of company restoration (see below). TCE will normally either sell or lease the land (if commercially viable), as the objective of TCE is to maintain and enhance the value of the estate and the return from it. The net surplus from TCE's commercial property business is passed to the Treasury.

Third-party rights and liabilities

As explained above, somewhat counterintuitively, bona vacantia and disclaimer do not bring to an end third-party rights or obligations as regards the disclaimed property. These continue unaffected. So, for example, a tenant of freehold subject to bona vacantia continues with its leasehold rights, such as the right to enfranchise or extend leases and of security of tenure.[8] Or a person holding rights of way over or a right to purchase property that has been disclaimed will continue to enjoy those rights. The end result is that third parties continue to enjoy rights and be subject to liabilities in respect of an estate in land that no longer exists (yes, really!). All of which means that TCE, although it inherits no pre-existing liabilities under the (now defunct) freehold estate, is very careful not to enter into possession or escheated land, or to exercise management powers in respect of it, where to do so might result in it incurring fresh liabilities (and environmental liability is a particular concern).

In both bona vacantia and escheat cases, persons with interests in, or liabilities in respect of, the property in question can also apply to TSOL or TCE (or via the court) to have the property vested in them.[9] This is more common with real estate, for obvious reasons. Where such an application is made, TSOL or TCE will normally look to obtain market value in exchange for the transfer. There are exceptions, and one such case is where the applicant holds a mortgage over the property, where the power of sale will be exercisable without Crown intervention.[10]



> **The end result is that third parties continue to enjoy rights and be subject to liabilities in respect of an estate in land that no longer exists (yes, really!)**

Company restoration's effect on escheat and bona vacantia

This depends on what has occurred. There are three possibilities, all of which are set out in the diagram provided above:

1. For bona vacantia that has not been disclaimed, the effect or company restoration is to restore to the company its property and the company continues in existence as if dissolution has not occurred. But if TCE has disposed of that property in the interim, that disposal will not be set aside, but instead TCE will account to the company for any proceeds received.[11]
2. For bona vacantia that has been disclaimed, the disclaimer has occurred after dissolution, and therefore is returned to the company on restoration, including any lease a company held.[12] This can be problematic, for example where defunct leases suddenly spring back into life, and it is unfortunate that the previous provisions of the Companies Act 1985 (which deemed disclaimer to have taken place immediately prior to dissolution) were not replicated.[13]
3. For property disclaimed by a liquidator during liquidation, the disclaimer will have occurred during the 'life' of the company, so on restoration there is nothing to return to it.

More thorny issues and who to contact

The above issues are not an exhaustive list. There may be situations in which direct dialogue with TCE is advisable. Among those are criminal confiscation orders involving disclaimed land, and contaminated land that has passed to TSOL or TCE, or a party which has a right or liability in respect of affected land, and seeks a vesting order as a result. Where such issues arise, it is best to contact TCE's lawyers in the first instance to see what can be done. The relevant contacts are Burges Salmon (for TCE) and Farrer & Co (for the Duchies of Lancaster and Cornwall). Both have contact sections on their websites. ◻

[1] The Law Commission last looked at escheat in March 2005 as part of the Ninth Programme of Law Reform, but it was not progressed
[2] Sections 178 – 182 Insolvency Act 1986
[3] Section 178(4)(b) Insolvency Act 1986
[4] Section 1012 Companies Act 2006
[5] *Rock Ferry Waterfront Trust* v *Penningstone Holdings Ltd* [2021] EWCA Civ 1029
[6] Section 1013 Companies Act 1986
[7] Section 1015 Companies Act 2006
[8] See for example *Fenland District Council* v *Sheppard* [2011] EWHC 2929 (Ch) and *Hunt* v *Conwy Borough Council* [2013] EWHC 1154 (Ch)
[9] Section 181 Insolvency Act 1986 and Section 1017 Companies Act 2006
[10] *Scmlla Properties Ltd* v *Gesso Properties (BVI) Ltd* [1995] BCC 793
[11] Section 1034 Companies Act 2006
[12] Re *Buzzline Coaches Ltd* [2020] EWHC 3027 and re *Fivestar Properties Ltd* [2015] EWGC 2782
[13] Section 657(2) Companies Act 1985

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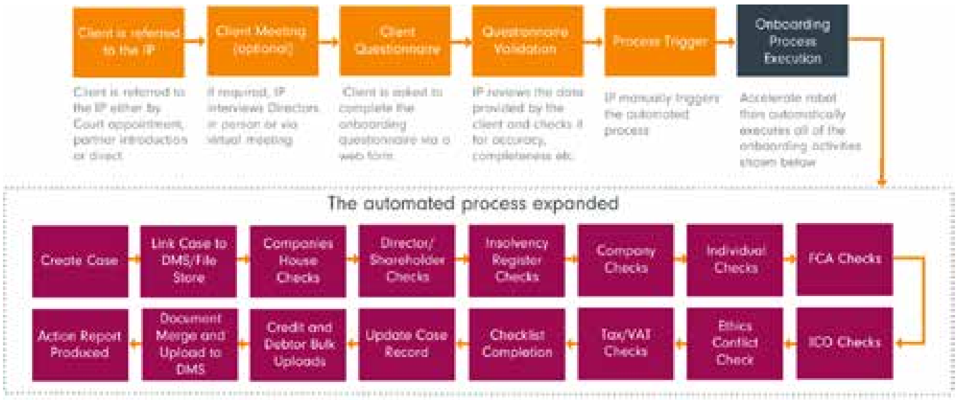
Automating the client onboarding process

Matthew Ellidge writes that you can remove up to 90% of the manual effort in pre-onboarding checks through automation.



Robotic Process Automation (RPA) has the potential to transform the insolvency industry with many practitioners and their teams intrigued by the value of automation while also questioning how it would work in the real world. Could RPA handle the level of complexity involved in gathering all the disparate information required? How could an automated process replace the numerous meetings and email exchanges usually required to start a corporate insolvency case?

Tquila Automation and Turnkey set out to solve this problem by creating an out-of-the-box solution, Accelerate, to automate the onboarding process within IPS. With the support of several IPs, the joint team mapped out the onboarding journey for a corporate insolvency case from cradle to grave. No mean feat, given the various manual pre-appointment checklists that are required on every case. Once validated, Tquila programmed the Accelerate robot to conduct each step of the process by interacting with IPS and external systems in the same manner as a human, but in a fraction of the time.

Once validated, Tquila programmed the Accelerate robot to conduct each step of the process by interacting with IPS and external systems in the same manner as a human, but in a fraction of the time.

Benefits of automating client onboarding

In corporate case onboarding, all the tasks completed by the robot are imperative from a compliance perspective. Yet, they are undeniably repetitive and are at risk of being overlooked – especially during busy times when a staff member's attention is being pulled from one case to another.

By automating this process through Accelerate, you can remove up to 90% of the manual effort, freeing up staff time to focus on case progression, rather than administrative tasks. Human error is also reduced to near zero, minimising costly redress and exposure to unnecessary risk.

How does Accelerate work for a client onboarding process?

The first step in the journey is for the case manager to send the director an online questionnaire featuring all the essential information that needs to be gathered when introduced to a client. Once the client returns a completed questionnaire, the IP receives an alert to check the information. When satisfied with the data, the case manager can trigger the Accelerate robot to begin.

The robot then creates the IPS case and links it to any document management system utilised.

It then begins performing all the required checks and collates evidence, either by taking screenshots or downloading the documents into the case file area.

Crucially, as the robot finalises these tasks, it also marks them as completed in IPS and, where applicable, attaches evidence to the record.

Next, the robot works on the pre-appointment checklists, populating them with all the essential information, enabling the case manager or IP to focus on the 'judgement-call' responses required in each checklist. It will even scan the case folder to check for a completed creditor and debtor spreadsheet and if found proceed to import the data into the case.

It then moves on to the pre-appointment document merges, such as a director questionnaire, which is emailed to the director automatically, or a letter of engagement, which can be completed and sent to the case manager for tailoring and approval.

The onboarding process is completed by producing an action report that logs every task it has conducted, which is always saved in the IPS case document area.

Value of automation

Onboarding is a common bottleneck, as practices receive numerous new instructions in a short space of time. From discussions with several firms, large and small, it's clear that even the quickest onboarding processes can take over an hour and involve many staff, often at a senior level. Accelerate reduces this time, only including staff when required, effectively removing the potential bottleneck. The Accelerate robot completes the process faster than humanly possible, with no down time providing valuable ROI for any IP. With the ability to run all day, every day without as much as a tea break!

Still have questions about the reality of automation? Contact us at enquiries@turnkey-ips.com or visit our website at www.turnkey-ips.com/accelerate to request a demo and see Accelerate in action for yourself. □

MATTHEW ELLIDGE is a former case manager and is now an IPS Product Specialist at Turnkey.

Building a stronger community

Emmanuelle Inacio reviews some of INSOL Europe's recent projects and collaborations in the field of restructuring and insolvency.

INSOL Europe is committed to communicating transparently, sharing information and delivering first-class content and lectures as well as networking opportunities. We continue to work to identify legislative change quickly and provide regular and clear legal updates to help you understand how this change affects your business and clients. Here are some of the projects we have been working on.

Information sharing

In January 2022, the joint project between LexisPSL and INSOL Europe on the *Recognition of Foreign Decisions in Different EU Countries*[1] was published. Apart from the European Insolvency Regulation, which is applicable only between EU member states, a few international instruments deal with the recognition issue connected to insolvency (and insolvency-related) judgments. Those international instruments, namely the UNCITRAL Model Laws 1997 and 2018 (for those member states that have enacted them), the Hague Convention or EU Rome I Regulation, may also be complemented by other specific private international rules. For third countries and the UK (as a consequence of Brexit), a great uncertainty remains in terms of providing the necessary authority for the recognition of such judgments. In that light, the joint project on the recognition of foreign decisions in the 27 EU countries has been designed to address those situations and provide readers with a description of each national recognition process applicable to those judgments.

The interactive *European Bank for Reconstruction and Development (EBRD) Business Reorganisation Report on insolvency and bankruptcy systems*[2] has been available for consultation since January 2022. It includes a main report and individual profiles for all 38 economies where the EBRD invests, including many European countries, thanks to INSOL Europe support and partnership over the last two years.

> “The INSOL Europe *Coffee Breaks: Connecting Minds 2022* series continues with our popular video conversation format in partnership with the EBRD.”

In February 2022, the sixth volume in the series of publications by INSOL Europe's Judicial Wing titled *COVID-19: Which practical measures adapted by the insolvency courts because of the pandemic are desirable to become permanent changes of their practice?*[3] was launched. Authored by members of the judicial wing, the information in the text shows a broad range of different approaches to deal with conditions under the pandemic: from not having specific legislation and measures at all to quite liberal legislation permitting remote hearings and extensive use of audio-visual technology by some courts.

The INSOL Europe *Coffee Breaks: Connecting Minds 2022* series[4] continues with our popular video conversation format in partnership with the EBRD. The INSOL Europe Country Coordinators share their experiences with representatives from their local associations and/or other stakeholders, highlighting challenges of the national insolvency framework to address the current crisis and other key issues in their jurisdiction. The first video for 2022 features David Sequeira Dinis (Uria Menendez) and Justice Fátima Reis Silva (Court of Appeal of Lisbon) who discuss the implementation of the EU Directive on Restructuring and Insolvency Portugal.

Return to in-person events

We are still carrying with us the images[5] and emotions of our fantastic 40th Annual Congress, which was held in the beloved city of Dublin (Ireland) from 3–6 March this year. It felt incredible to meet again in person following the Covid-imposed shelving and hibernation of our live events for more than two years. To be able to reconnect and catch up with good friends, who were so sorely missed during the dark days of the pandemic, and to reignite the passion we share for our organisation and for our industry at large was simply fabulous.

We are now most delighted to invite you to the breath-taking city of Dubrovnik (Croatia) for the 41st Annual Congress entitled 'Resilience in the face of adversity', which will take place from 6–9 October 2022 at the Hotel Rixos Premium Dubrovnik.[6]

With ancillary meetings before and after the main event, this will be the second opportunity in 2022 for our community to come together and leverage the educational and networking benefits that our delegates have come to expect – and to catch up with existing friends and make new ones.

> “As professionals within the crisis management and restructuring community, we are accustomed to approaching each new hardship as a challenge and the new crisis is no different.”

We look forward to welcoming you very warmly in this magnificent setting filled with promise.

At INSOL Europe, we are also a community. As professionals within the crisis management and restructuring community, we are accustomed to approaching each new hardship as a challenge and the new crisis is no different. We will explore new ways to connect with our colleagues around the world and be reminded of why it is so essential that we all pull together to help rebuild the global economy. We need a deeper fellowship with other insolvency professionals, we need to connect more and to facilitate discussions; to share challenges, solutions, best practices, ideas even more and to develop this thriving, robust, compelling culture. Join our community![7] □

[1] https://www.insol-europe.org/download/documents/2174
[2] https://ebrd-restructuring.com/
[3] https://www.insol-europe.org/publications/technical-series-publications
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EMMANUELLE INACIO is chief technical officer at INSOL Europe.

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Representing your views on regulation

The Press, Policy and Public Affairs team's priority in recent months has been ensuring that the profession's voice is heard on the future of insolvency regulation.

Since the government published its consultation with proposals to radically reform regulation at the end of last year, we've done a huge amount to hear our members' thoughts and to make sure that our response broadly reflects your views. We hosted meetings and webinars across all the regions and nations to ensure that we heard views from members far and wide. We also issued a survey to seek your views on specific questions and discussed the proposals line by line with our committees.

In our response, we've highlighted that our overarching concern is the lack of detail the government has provided about how each of the reforms would operate in practice. We've urged the government to publish separate and more detailed consultations on each proposal.

We've taken a position that we can't support the current proposal for a government single regulator without significant checks and balances to ensure the regulator's independence, as well as a levelling of the playing field to ensure that the Official Receiver is subject to the same regulatory framework and reporting requirements as the profession. The government also has other options it should consider more fully before setting off down this route.

Now that the consultation has closed, the government will take some time to review all the responses before it eventually brings forward legislation to enact the proposals. In the meantime, we'll continue to represent your views to try to ensure that any changes improve – rather than damage – the regulatory framework.

> **"We've taken a position that we can't support the current proposal for a government single regulator without significant checks and balances to ensure the regulator's independence."**

Focus on fraud

Another focus for the team in recent weeks has been campaigning for the government to legislate for Companies House reforms. These reforms – which include compulsory identity verification of all directors, people with significant control and those filing information on behalf of a company – will help the profession to play an even more effective role in supporting the wider fight against fraud.

It is disappointing that since the government's four consultations on Companies House reform in 2019 and 2020, aside from the publication of a white paper, few developments have taken place to advance the proposed changes. Although the government pushed an initial Economic Crime (Transparency and Enforcement) Act quickly through Parliament in the spring, Companies House reform was not included in this legislation. The government has, however, said that it will be bringing forward legislation on the reforms later this year.

In our response to the government's 2019 consultation on Companies House reforms, we made suggestions as to how these can be evolved to enable the profession to play an even greater role in tackling corporate fraud, such as through allowing IPs to access additional 'back-office' information, and making the restoration of a dissolved company an administrative process that does not require an application to court.

We'll continue to call for these amendments to be included once the new economic crime bill begins its legislative journey, and hope the government will work with us to increase the profession's role in strengthening the integrity of the UK's corporate governance framework.

Challenging myths around insolvency fees

In March we published a new report, *Insolvency fees and the cost of regulation: the detail behind the headlines*, which aims to address common misconceptions and myths about insolvency fees.

Insolvency fees are one of the most misunderstood aspects of the profession, and the report aims to show that the detail behind them often gets missed in media headlines, which can lead to an unfair perception of the profession and the work it carries out.

The paper explains that fees are linked to the range of requirements IPs must meet when fulfilling their duties as set out in legislation; that they can vary widely, depending on the size and complexity of cases; and that members of the profession are often not paid in full for their work, frequently having to write off tens of thousands from the amount that they should have been paid on a case. It also contains examples from R3 members of cases where IPs have written off a percentage of their fees.

We've promoted this resource to parliamentarians, key industry and business stakeholders and to the media, and we also hope that it might be useful for you to help explain to clients how insolvency fees are charged and regulated.

R3 in the media

Over the last few months, the team has been busy briefing journalists and responding to breaking news stories on insolvency trends and policy announcements.

Our commentary on insolvency statistics continues to be popular with national, trade and regional media, and has been quoted in stories in *The Times*, the *Financial Times*, *The Guardian* business blog, *Reuters*, *MailOnline* and *The Independent* to name just a few.

Our fees paper received coverage in the trade press while our Scottish consumer debt advice resource, *Dealing with money worries – a guide to your options* was picked up by a number of Scottish outlets.

In addition to this, R3 spokespeople have given interviews and briefings to journalists from a range of outlets that include *The Times* and *Accountancy Age* on issues including reforms to insolvency regulation, directors' responsibilities and the impact of lockdowns on insolvency levels in the travel industry. □

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An interview with… Christina Fitzgerald, current president of R3

The incoming president of R3 speaks about new faculties, diversity and inclusion, and upcoming challenges for the profession.

Christina Fitzgerald biography

- Christina was born and raised in Filey, North Yorkshire and educated at Hunmanby Hall School, where she had every intention of pursuing a career as a music teacher. Some well-placed advice from a relative in the legal profession set her on track to study law at Sheffield University.

- She moved to London in 1990 to undertake her articles and qualified at Clifford Chance as a shipping litigator, having obtained maritime law qualifications at Southampton University. It was an experience with arbitration work that set her on the path to an insolvency specialism, and she joined the newly opened Pinsent & Co office in London (which later became Pinsent Curtis) to focus on commercial litigation. She gradually became the go-to person for anything insolvency related.

- She joined Kennedys in 2000 to focus on restructuring and insolvency, later moving to work at firms Matthew Arnold & Baldwin, Shakespeare Martineau and Moon Beever. She joined Edwin Coe in 2021, where she is currently a partner.

Q You've just taken up office as the R3 president. How long have you been a member of R3 and why did you join?

A It was when I joined Kennedys in 2000 that I was encouraged by Dino Paganuzzi and John Harvey to become a member of R3 for the networking benefits, particularly the women's LASER group.

I chaired the women's London region for many years, was on the education committee and did lots of speaking on the more technical side. It was about 2014 or 2015 that I organised R3's Strictly Come Dancing to raise money for the Debbie Fund. There have been some really memorable social and professional events, such as R3's Got Talent, and the journey has been very rich.

R3 is just so important as the voice of our profession and for making sure that there's good communication between all the regions and that we're all on the same wavelength. [At the time of writing] I have only been president for a week, but we've been planning for the R3 Annual Conference, preparing for upcoming media opportunities and keeping up to date with everything that is happening.

Q For the last few years, with Brexit and the pandemic, we've said that it has been a challenging time for the profession and, by proxy, the incoming president. It feels like this year may be the one to top them all. Corporate and personal insolvencies are both on the rise – indications of an oncoming storm – and regulation is on the agenda. What does this mean for you as R3 president and the work for R3 in future?

A I think there might be an increase in insolvencies to match pre-Covid levels. I certainly suspect there will be a lot more CVLs. There are no more government measures and those that are tired of how tough things have been during the pandemic may well say, 'I'm going to call it a day for my own peace of mind'.

For the profession, the biggest upcoming event is the government's review of regulation, which could have massive implications for our industry. At R3 we see an inherent conflict if regulation is retained within the Insolvency Service. Our members on the whole said that they were in favour of a single regulator, but not one that sits within the Service. We have tried very hard to find a positive way forward and offer a solution.

"I want to use my presidency to ensure that as many people as possible, from media to parliamentarians to policymakers, understand just how valuable this work is to the wider economy."

We will be under a bright spotlight in the coming weeks and months ahead. The work that we carry out to help financially distressed businesses and individuals, as well as to support and promote the profession, will be increasingly important. I want to use my presidency to ensure that as many people as possible, from media to parliamentarians to policymakers, understand just how valuable this work is to the wider economy.

We also need to work alongside government to help support business rescue in the year ahead by encouraging directors and business owners to seek early advice, and to strengthen HMRC's approach to supporting viable restructuring proposals. We will also be urging the government to implement its planned reforms to Companies House as soon as possible. This is particularly important in light of the potential scale of Covid-related fraud and, with events in Ukraine, this is leading to a wider conversation about the integrity of the UK's corporate governance framework. We will also be engaging with the government's call for evidence due later this year in relation to the personal insolvency review.

Q You mentioned supporting distressed businesses and individuals. Is this a continuation of post-pandemic recovery?

A We introduced some of this with R3's Back to Business UK campaign, championed by people like Alison Goldthorp, Paul Zalkin and Mark Phillips QC. The campaign reached out to thousands of directors to say how important it was to get advice early on and provided a free paper to the Department of Trade and Industry. When I was at a recent IPA conference, the chief executive of the Insolvency Service, Dean Beale, said that they're going to introduce a scheme to encourage directors to take advice early on as well. We'd be happy for them to use our resources to get that advice out there.

Q Could you tell us a little bit about your priorities for the coming year? R3 has been through several stages of change recently – what does this next phase entail?

A One is communication between the regions and making sure we're on the same wavelength. Another is the implementation of the strategic plan – it's really to make sure that R3 is sleek, streamlined and commercially orientated to weather the next 30 years. We will also be working with the Insolvency Service on diversity and inclusion – we want to break down barriers to entry into the profession and progression and to make sure that the talent pool is wide and that graduates and those in education know what a great career it is.

> Now it's about getting the plan back on track and making sure we're a thriving organisation that is ready to help the profession build one community.

Q What does the D&I initiative look like?

A It's related to unconscious bias and looking at recruitment policies and mentoring for those coming up through the profession. It's also about avoiding that old saying about certain professions being 'MPS' (male, pale and stale).

R3 and the Insolvency Service have come together to form a steering group made up of people from all parts of the profession, as well as staff from the Service and R3. The four areas that the group will focus on are: entry into the profession, progression to associate level and to partner level, taking insolvency qualifications and becoming a licence-holder.

The group is looking to share best practice, start discussions about diversity and inclusion issues that firms and individuals might be facing, connect with firms and practices that have successfully addressed such issues, and improve understanding among graduates and school leavers about the profession as a potential career option.

The steering group has already started work on recruiting its first cohort of diversity and inclusion champions – people from the profession who want to help and support this project and get involved.

From my perspective, I have a lot of experience as a mentor so I'm very keen to be part of this and will work closely with the group, the Insolvency Service and Samantha Keen, president of the IPA, who is also passionate about this issue.

Q You mentioned the strategic plan, which first began back in 2019. What work is being done now on this?

A You know, in the original wording it said that our plans, objectives and activities 'will be adapted to match the world around us as time moved on'. Gosh – little did we know at the time how much was going to change! Obviously, we've been focused on adapting to providing education online, meeting virtually and not having any physical conferences, but now it's about getting the plan back on track and making sure we're a thriving organisation that is ready to help the profession build one community, have one place to learn throughout their career journey, speak with one voice, and develop and share innovative ways of supporting the UK's businesses and individuals.

Q In a recent mailshot, you mentioned the importance of developing R3's dedicated faculties to serve the profession in future. Could you tell us a little more about this?

A It works with the common theme of 'One R3'. It was Colin Haig's idea to set up the faculties to expand our membership base to a wider restructuring audience. This would also encourage collaboration with other organisations such as the IFT and TMA. Originally, we had planned to have four faculties but two have recently merged. The faculties are: public sector, special situations M&A and restructuring. If this goes to press after the Annual Conference, you may already have seen the presentations from each of the groups.

I think there's a degree of attractiveness to R3's lobbying abilities that really appeals. We have a lot of stakeholders that may need more information from, for example, a body such as Ofgem. How do IPs and lawyers get engaged in order to resolve a query correctly and quickly? Now we'll be able to feed such queries through the faculties and, if there needs to be change or reform at a higher level, R3 can facilitate the necessary conversations.

> I'm a gym bunny and have been running seven or eight miles a day since I was about 17. For me, it's my best thinking time – most people have a notepad next to the bed, but I keep mine on my jogging machine.

Q What do you do with your free time when you're not working?

A I've got a tidy garden, a home gym and a summer house in the garden with a bar and a karaoke machine in it – all of which was a godsend in lockdown for my mental health. I'm a big rugby fan and me and my husband are Harlequins season ticket holders but, really, I'm a gym bunny and have been running seven or eight miles a day since I was about 17. For me, it's my best thinking time – most people have a notepad next to the bed, but I keep mine on my jogging machine.

Q If you had not gone into the insolvency profession, what career might you have taken up?

A I won a music scholarship in my teens and I always intended to be a woodwind music teacher. I was the youngest member of the North Yorkshire County Orchestra, but that probably wouldn't have been a very reliable career. When I started getting good grades, my auntie who was a legal secretary encouraged me to study law instead. There was a time when I had aspirations to join Pan's People as well! □

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