JOINT INSOLVENCY EXAMINATION BOARD

Joint
Insolvency
Examination
Board

Joint Insolvency Examination

Tuesday 7 November 2017

ADMINISTRATIONS, COMPANY VOLUNTARY ARRANGEMENTS and RECEIVERSHIPS (3.5 hours)

ANSWER ALL FOUR QUESTIONS

EACH QUESTION CARRIES TWENTY-FIVE MARKS

SUBMIT ALL WORKINGS

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

Note: References to legislation are to that which was in force on 30 April 2017. References to 'the Act' are to the Insolvency Act 1986 as amended.

References to Sections, Schedules and Rules are to Sections and Schedules of the Act and to Rules of the Insolvency (England and Wales) Rules 2016.

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

1. As an insolvency manager, you have recently attended a meeting with Astralorp Limited ("the Company"), a long established business specialising in the design and manufacture of precision engineering products used within the oil and gas sector.

The Company has experienced trading difficulties as a result of its customers reducing the amount of investment in new and replacement equipment. Whilst the Company has been able to slightly reduce its cost base, it has retained staff in the hope that trading conditions will improve. As a consequence the Company has been trading at a loss for the last 18 months and has been reliant on other members of the corporate group for working capital support.

On 31 October 2017 the Company requested additional funding of £250,000 from its parent company to meet ongoing trading obligations including payroll. The Company's parent provided these funds on that day but has stated that it is unable to provide further support to the Company.

As a result of this communication the Directors have reviewed the situation and presented the following financial information to you at the meeting:

Income Statement for the 12 months to 31 October 2017

	Note	**£'000**
Revenue	1	15,000
Cost of sales - materials		(7,000)
Cost of sales - payroll	2	(5,000)
Gross profit		3,000
Overheads	3	(4,500)
Net loss		(1,500)

Statement of financial position as at 31 October 2017

	Note	**£'000**
Tangible fixed assets	4	3,000
Current assets		
Stock	4	1,000
Debtors	4	1,250
Amounts due from related parties	5	300
Cash at bank	6	50
		2,600
Creditors: amounts falling due within one year		
Trade creditors		(3,000)
Amounts due to related parties	5	(2,000)
Bank loan	7	(300)
Employee holiday pay		(60)
		(5,360)
Net current liabilities		(2,760)
Creditors: amounts falling due after one year		
Bank loan	7	(2,000)
Net defined benefit liability (pension)	8	(3,000)
		(5,000)
Net liabilities		(4,760)

Notes to the financial statements

1. Revenue has remained consistently at this level and is not expected to change over the next few years.

2. The Directors believe that immediate payroll savings of 50% can be made through an aggressive redundancy programme: however the costs of this are estimated at £1.5 million including redundancy and notice pay.

3. The Company will also make 40% of office staff redundant, saving £500,000 p.a. of overhead costs (associated termination cost £200,000) and other overhead savings of £200,000 are achievable.

4. The Directors have commissioned valuations of the assets of the Company and these valuations indicate that in a liquidation scenario realisations net of agent's costs would be as follows:

Fixed assets	60% of book value
Stock	25% of book value
Debtors	80% of book value

   The level of stock and debtors does not materially change over time and there is no need for any further investment in fixed assets.

5. The related party balances comprise:

	Owed to Company £'000	**Owed by Company £'000**
Parent company	-	(1,500)
Fellow subsidiary 1	200	(400)
Fellow subsidiary 2	100	-
Director A	-	(100)
	300	(2,000)

6. Due to intra-month cash flow movements it is necessary for the Company to retain £300,000 of working capital.

7. The bank loan is secured by a fixed charge over the fixed assets of the Company and a floating charge over the remainder. It is repayable at £300,000 p.a. capital plus interest fixed at £100,000 p.a.

8. A recent revaluation and review by the Company's defined benefit pension scheme has identified that the funding deficit has increased from that shown in the accounts and on a 'buy out' basis the liability would be c. £6.5 million. There are no active members of this scheme.

Following your discussions with the Directors they have concluded that they wish to propose a Company Voluntary Arrangement. This has been discussed with the Company's bank and they are willing to continue to provide the existing facilities on the condition that the trading assets of the Company are excluded from the arrangement, they continue to receive the agreed level of repayments and they do not participate in the CVA.

The Directors therefore wish to put forward a contribution based CVA in which the Company pays to a Supervisor 75% of its annual net profit for a 3 year period (subject to maintaining the minimum working capital requirement referred to above). Any staff to be made redundant would be paid their salaries (but not other entitlements) up to the date of termination, which would occur prior to the commencement of the CVA.

Requirements

(a) **Given these circumstances, set out the legal and best practice obligations relating to the pension scheme. (5 marks)**

(b) **Making appropriate assumptions, prepare a comparative outcome statement for inclusion within the CVA proposal clearly showing the expected return to the unsecured creditors. (20 marks)**

Total: (25 marks)

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2. Six weeks ago a principal in your firm was appointed Administrator of Orpington Limited ("the Company") by the Directors.

During the year to 30 June 2017 the Company reported a break-even trading position: however in mid-June 2017 the Company lost a large profitable contract. When the principal funder, Maran Finance Limited ("Maran"), became aware of the position they were immediately concerned since they believed that this would bring in to question the viability of the Company. However it was not until the Company missed a scheduled interest payment in late September 2017 that Maran was able to serve demand for repayment of the entire debt. This in turn led to the Directors appointing an Administrator.

Shortly following the Administrator's appointment, the Company ceased trading and all employees were made redundant. Since that date all the assets of the Company with a combined book value of £500,000 have been realised for a total of £350,000.

At a meeting of creditors a creditors' committee was duly formed and during this meeting the members of the committee expressed their concerns regarding the actions of the Directors in the lead up to the appointment of the Administrator.

You have now commenced your investigations and have identified the following information:

(i) Creditors of the Company

The creditors of the Company comprise:

Creditor	**Debt £**	**Notes**
Dorking Limited	£70,000	A Company under the control of one of the Directors
HMRC	£350,000	Comprises £200,000 VAT (2 quarters) and £150,000 PAYE/NI (3 months)
Pension scheme	£30,000	3 months' employee and employer contributions
Employees	£150,000	Total expected claims
Maran Finance Limited	£200,000	Charges dated 30 June 2017 conferring a fixed charge (chattel mortgage) over the Company's plant and equipment and a floating charge over the remaining assets of the Company
Trade creditors	£100,000	£25,000 of this at the date of the Administrator's appointment was overdue for payment with the balance not yet due
Total creditors	£900,000	

You have reviewed the historic balances as at 30 June 2017 and at this date total creditors (excluding employees) amounted to £650,000. The change in creditors comprised an increase the amounts due to HMRC and Maran Finance Limited of £250,000 and £50,000 respectively together with a decrease in amounts owed to trade creditors and Dorking Limited of £150,000 and £50,000 respectively.

(ii) Assets of the Company

A balance sheet review shows that the book value of the assets of the Company reduced by £50,000 from 30 June 2017 to the date of the Administrator's appointment. The only asset that changed materially during this period was stock.

Requirements

(a) **Set out the Administrator's key obligations in relation to investigating the affairs of the Company and explain the role of the committee in relation to this. (10 marks)**

(b) **Set out the key areas of investigation that you have identified from the information provided and where relevant provide an estimate of the quantum of any potential claim and explain the key steps you would take to pursue each matter. (15 marks)**

Total: (25 marks)

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3. You have been contacted by one of your firm's personal tax clients, Mr Barnevelder, regarding the financial position of Compine Agricultura Unipessoal Lda ("the Company"). Mr Barnevelder is the sole Director and Shareholder of the Company, which is registered in Portugal.

The Company's primary activity is the export of agricultural machinery from Portugal into the UK, where it leases several warehouses and an office to service its client base. Mr Barnevelder is a UK resident and splits his time between the two countries.

In 2016 an industrial accident caused by a faulty product resulted in a significant claim against the Company. Whilst the majority of this claim will be met by the Company's insurers, Mr Barnevelder had opted for a high excess and the Company is unable to meet this obligation.

Mr Barnevelder has concluded that he should seek to place the Company into an insolvency process and his preference is for this to be an Administration in the UK. He has approached you for advice regarding several matters:

(i) Compine Seeds Limited ("Compine Seeds")

Compine Seeds is a wholly owned English subsidiary of the Company that it acquired in 2010 for £300,000. Compine Seeds is a profitable and solvent business and its operations are kept entirely separate from those of the Company. Mr Barnevelder's brother, who works within this business, wishes to acquire this subsidiary should the Company enter into an Administration process.

(ii) Director's loan account

Mr Barnevelder received loans from the Company in 2013 and 2014 amounting to a total of £150,000 and this is shown as outstanding in the Company's accounts. Mr Barnevelder has experienced some personal financial problems of late. His only material asset is his matrimonial home that he owns jointly with his wife. This property is valued at £250,000 and is subject to a joint mortgage of £130,000 and a second charge in relation to a secured loan of £30,000 in Mr Barnevelder's sole name.

(iii) Patents

Mr Barnevelder's son, an employee of the Company, is recorded as the inventor of a European patent for a turnip harvesting trailer, one of the Company's leading products. Mr Barnevelder believes that his son is the true owner of the patent and therefore should be able to either use the patent in a new business or license it to a competitor.

Requirements

(a) Set out your key considerations as to whether you could accept the appointment as Administrator. (5 marks)

(b) Set out the key matters you would consider and information you would seek from the Company to determine whether it would be possible to appoint an Administrator in the UK. (5 marks)

(c) Assuming a UK Administrator is appointed, explain how they would approach the three matters and explain the potential methodologies they may apply to determine an appropriate realisable value. (15 marks)

Total: (25 marks)

4. You are an Authorised Insolvency Practitioner and have been engaged by Padovana Bank plc ("the Bank") in relation to their customer Shamo Limited ("the Company") following several requests by the Company for additional funding.

Your review of the Company's cash flow has identified that there will be a substantial funding requirement in excess of its overdraft facility in 3 weeks' time at which point both payroll and a quarterly rent payment will be due. The Bank has confirmed that they are not willing to provide this additional funding and therefore the Directors have decided that they will file a Notice of Intention to Appoint Administrators and have agreed with the Bank that you will be the nominated Administrator.

The Company manufactures and installs specialist hydraulic lifts for commercial and residential applications. It is currently working on two large office development projects:

Customer:	**Wilma Construction Limited**	**Gazoo Building Services Limited**
Project Name:	York Street One Project	Carlisle Business Hub
Start date:	1 April 2017	1 August 2017
Completion date:	30 March 2018	31 January 2018
Contract financial summary	£	£
Total contract value:	1,500,000	900,000
Amounts certified as at 31 October 2017:	900,000	200,000
Amounts invoiced as at 31 October 2017:	800,000	nil
Debtor outstanding:	300,000	nil

The Directors of the Company wish to buy its trade and assets through a pre-packaged sale and have stated that this would only be possible if no customer, competitor or employee becomes aware of the situation prior to completion of the deal. They believe that, should the financial difficulties become known in the market, the Company would lose all existing contracts, sub-contractors and employees.

You have received the following offer from the Directors for discussion:

Proposed terms of purchase:

- Consideration as follows:
  - Plant, machinery, equipment, computers, etc. — £25,000
  - Stock — £10,000
  - Order book — £1
  - Books and records — £1
  - Trade name — £1
  - Debtors and work in progress — 25% of current book value
  - Payment terms — equal instalments over 12 months

- Employees – a transfer of the employees to the purchaser, who will accept responsibility for the forthcoming payroll.

- Property – the acquirer requires a sub-lease of the Company's factory and offices for 18 months

The Directors are keen to move ahead and complete their acquisition as soon as possible.

Requirements

(a) Set out your obligations in relation to Statement of Insolvency Practice 16 for the period leading up to the appointment of an Administrator and explain how you would apply them in these particular circumstances. (15 marks)

(b) Explain how you would deal with the situation should the Directors refuse consent for you to market the business for sale. (5 marks)

(c) In the absence of any other offer, outline your key considerations and concerns when assessing the offer from the Directors. Where appropriate, provide alternative suggestions as to how the offer could be structured in the best interests of creditors. (5 marks)

Total: (25 marks)

Assumptions:

Ignore VAT