JOINT INSOLVENCY EXAMINATION BOARD

Joint Insolvency Examination Board

Joint Insolvency Examination (Scotland) 2018

14 November 2018

PERSONAL INSOLVENCY (3.5 hours)

This exam consists of **four** questions (100 marks).

Marks breakdown

Question 1	20 marks
Question 2	20 marks
Question 3	20 marks
Question 4	40 marks

1. Please read the instructions on this page carefully before you begin your exam. If you have any questions, raise your hand and speak with the invigilator before you begin.

2. Please alert the invigilator immediately if you encounter any issues during the delivery of the exam. The invigilator cannot advise you on how to use the software. If you believe that your performance has been affected by any issues which occurred, you must request and complete a candidate incident report form at the end of the exam; this form must be submitted as part of any subsequent special consideration application.

3. Click on the **Start Exam** button to begin the exam. The exam timer will begin to count down. A warning is given five minutes before the exam ends. When the exam timer reaches zero, the exam will end. To end the exam early, press the **Finish** button.

4. You may use a pen and paper for draft workings. Any information you write on paper will not be read or marked.

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

6. Ensure that all of your responses are visible on screen and are not hidden within cells. Your answers will be presented to the examiner exactly as they appear on screen.

Question 1

You are an Authorised Insolvency Practitioner.

You have just met Mr and Mrs Mallard. During the course of the meeting Mrs Mallard explained that she had been made bankrupt on 1 June 2016 following a creditor's petition presented to the Court on 12 April 2016. Mrs Mallard stated that she had been in denial about her financial situation and as a result did not attend the Court hearing. She did not contact her Trustee, Mr Barbary, in relation to her affairs until very recently.

Mr Mallard told you that he was unaware of his wife's sequestration until last week when he received a letter from her Trustee advising him that steps must now be taken to realise their jointly owned property. Mr and Mrs Mallard are both retired and do not want to leave their home as 50% of the net proceeds of sale will not be sufficient to enable them to buy another property in the local area. Following receipt of the letter Mr Mallard contacted Mr Barbary to discuss whether a sale of the property could be avoided. Following the telephone conversation the Trustee sent Mr Mallard a calculation setting out the estimated amount required to discharge all of the sequestration costs, debts and expenses in full ("the Calculation"), as follows:

Estimate of the sum required to discharge the sequestration debts, costs and expenses of Mrs A Mallard

Assumption: all creditors will be paid by 1 February 2019

Creditors

Credit card companies	£16,059
Personal loans	£19,277
HMRC	£26,274
Total creditors	**£61,610**
Statutory interest (8% per annum for the period 12 April 2016 to 1 February 2019)	**£13,841**
Sequestration costs	
Trustee's time costs to date	£4,200
VAT on time costs to date	£840
Trustee's estimated future time costs	£3,500
VAT on estimated future time costs	£700
Estimated legal costs (realising the property)	£5,200
VAT on estimated legal costs	£1,040
Petition costs	£2,121
Outlays	£400
Statutory fees	£385
AIB Audit fees	£2,327
Total sequestration costs	**£20,713**
Total amount required	**£96,164**

Mrs Mallard confirmed to you that she is liable for the credit card debts and the personal loans included in the Calculation. She was a self-employed landscape gardener until she retired in early

2014. She is not sure if she ever advised HMRC that she had stopped working or whether she submitted a final tax return. She feels that the debt due to HMRC is significantly higher than she expected. She is not aware of any additional creditors. However, she cannot understand how debts totalling £61,610 have resulted in her Trustee calculating that £96,164 is required to discharge the costs and liabilities of the sequestration estate.

Mr Mallard is entitled to draw down a tax free lump sum of £75,000 from his pension. Mr and Mrs Mallard explained that their only assets of any value are their jointly owned property and Mr Mallard's pension and that therefore £75,000 is the maximum amount available to Mr and Mrs Mallard to avoid the sale of their home.

Before meeting you Mr and Mrs Mallard had concluded that, as they could not raise sufficient funds to pay off all of the costs, expenses and liabilities of the sequestration estate, their property would have to be sold. However a friend had advised that there may be options available to reduce the total amount payable pursuant to the Calculation and suggested that Mr and Mrs Mallard meet with an Insolvency Practitioner to take some advice.

You have agreed to review the Calculation and write a letter to Mr and Mrs Mallard advising them on the options that are available in the circumstances and how the sums payable pursuant to the Calculation could be reduced.

Requirements

Write a letter to Mr and Mrs Mallard setting out the options. The letter should detail any further information that is required and recommend a course of action.

(20 marks)

Question 2

You are an Authorised Insolvency Practitioner.

You have just had a meeting with 3 brothers, Harry, an electrician, Gary, a plumber and Barry, a plasterer who started the meeting by explaining the background to their current financial position.

When the brothers were much younger, they had purchased a derelict property for £30,000 with each brother contributing £10,000 towards the cost. The brothers had worked together to renovate the property and, when the work was completed, the property was rented out. The rental income was paid into a joint bank account and used in part to pay the expenses arising in respect of the property.

The brothers had then decided that they would allow the surplus rental income to accrue and, once sufficient funds had built up, they would use those funds to purchase another property that they would renovate and rent out. This happened, and the process was repeated with the brothers building up a portfolio of 20 properties, all of which were rented out, generating a significant profit each year.

Everything was going well until 2008 when the decision was taken to purchase an old mill building to renovate and convert into luxury flats. Rather than rent out the flats, the brothers intended to sell the flats at a profit to fund their planned early retirement.

The brothers sold 11 of the 20 rental properties in order to generate funds to put towards the development of the mill. Rouen Bank ("the Bank") agreed to lend sufficient funds to purchase the mill and cover the estimated redevelopment costs. The Bank has an all sums security over the mill building and also the 9 remaining rental properties ("the Rental Properties"), which are still owned by the brothers.

The redevelopment of the mill did not go to plan. Whilst the mill cost only £2 million to purchase, the brothers had underestimated the amount of work required to renovate and restore the building. Delays in obtaining planning permission meant that building work could not proceed as quickly as intended and, as the mill was listed, the cost of carrying out the work was significantly more than the brothers had estimated. Whilst the building work was taking place the Bank was happy to renew the brothers' facility each year. The interest accruing on the loan to the Bank was rolled up and added to the loan.

The conversion of the mill finally completed in late 2012. However, due to a decline in the property market, a sale of the flats would not have generated sufficient funds to clear the indebtedness to the Bank. The decision was therefore made to rent out the flats. The rental income has been used to make the interest payments to the Bank each quarter. The Bank was initially happy to renew the brothers' facility on the basis that only the interest accruing on the loan was paid. However, the Bank started to become concerned about its potential exposure and, when the facility was last renewed in 2017, the Bank required the brothers to start repaying capital as well as interest. The brothers have had to use all of the income generated by the Rental Properties to meet the increased repayment obligations to the Bank.

The brothers came to see you as they have just been advised by the manager with whom they deal that the Bank is unlikely to renew their facility when it expires in February 2019.

The total amount currently due to the Bank is £4.7 million. The brothers estimate that the combined value of the Rental Properties is between £750,000 and £900,000. Whilst the 12 flats in the mill were built to a very high specification, the fact that they have been rented out for the last 6 years means that the flats are now dated and the expensive initial fit out will no longer result in the projected premium being achieved upon sale. The brothers estimate that the 12 flats, if sold individually through a phased sale process, will generate in the region of £3 million. If all 12 flats are sold together, they anticipate that only £2.25 million would be achieved.

Barry has recently been through a costly divorce and has also started gambling. All of his assets have either been transferred to his former wife pursuant to a court order made in the divorce proceedings or lost through gambling. His only income comes from occasional plastering work. By contrast, Gary and Harry both have significant equity in their homes as well as each having a holiday home overseas and considerable savings and investments.

Requirements

Set out your advice to the brothers on:

(i) **the potential implications for them if the Bank facility is not renewed in February 2019; (8 marks); and**

(ii) **what options are open to them in the circumstances.**
(12 marks)

Total: (20 marks)

Question 3

You were appointed as Trustee in the sequestration of a Mr Neil Eider on 31 October 2018 following a petition by HMRC.

Mr Eider is 44 years old and is a self-employed private plastic surgeon. He had a very good income until late 2014 when the clinic from which he operated closed suddenly. Although he relocated to another clinic, this took time to arrange and resulted in clients being lost. This meant that Mr Eider was without an income for around 6 months. During this time he ran up credit card debt, utilised his overdraft, fell into arrears with his mortgage and failed to discharge his liability to HMRC.

After starting at the new clinic Mr Eider began to reduce his overdraft, credit card debt and liability to HMRC and had also reached an agreement with his mortgage company pursuant to which he could clear the arrears. However, in 2015 his wife, who does not work, announced that she wanted a divorce. Although divorce proceedings were issued by his wife in late 2015, matters became very acrimonious and it was only on 16 March 2018 that an order for financial provision was made by the Court. Pursuant to this order Mr Eider is required to:

(i) pay £3,000 per month maintenance to his former wife;

(ii) pay £2,300 a month in respect of his children's private school fees;

(iii) make a lump sum payment of £450,000 to his former wife within 12 months of the date of the order; and

(iv) pay £47,260 in respect of his former wife's costs.

Mr Eider confirmed that he is 3 months behind with the monthly maintenance but school fee payments are up to date. The lump sum payment and the costs order have not been discharged.

Mr Eider has credit card liabilities of approximately £23,000. His bank account, which was overdrawn by £9,800, was frozen by the bank following the award of sequestration. He also owes around £26,000 to HMRC in respect of unpaid income tax and national insurance.

Mr Eider's only assets comprise:

(1) a property which is registered in his sole name and is estimated to be worth £1.1 million. The property has a mortgage of £800,000 secured against it (including the arrears). The monthly mortgage repayment is £3,300; and

(2) a private pension with a fund value of around £650,000. Mr Eider currently contributes £3,000 a month into his pension. He advised that, other than a nine month period from late 2014 to mid-2015, his contributions have been at the same level for the last 15 years.

Mr Eider has a Range Rover Sport on a 3 year lease agreement pursuant to which he pays £506 a month. The agreement was entered into in November 2016.

Whilst Mr Eider's income varies, his average monthly income is £17,000.

Following a number of telephone conversations during which this information was provided, a meeting has been arranged with Mr Eider. Mr Eider wishes to understand whether:

(1) he will be required to make any payments to you from his income. Mr Eider understands that he could be asked to make a contribution but says that he does not have any surplus income available to him;

(2) he can continue residing in the property;

(3) upon receiving his discharge, he will be released from all of his liabilities; and

(4) he can retain his pension.

Requirements

In advance of your meeting, and clearly stating any assumptions you have made, prepare a note that sets out what you propose to say to Mr Eider about:

(i) his requirement to make a contribution from income; (10 marks);

(ii) his continued residence in the property; (4 marks);

(iii) his release from his liabilities (3 marks); and

(iv) his pension; (3 marks).

Total: (20 marks)

Question 4

You are an Authorised Insolvency Practitioner. You have been advising a Mr James Gadwall who was referred to you by a colleague.

Mr Gadwall is a butcher who has run his own business, Gadwall Poultry and Meats, for the last 45 years. Whilst trading has, until recently, been profitable Mr Gadwall's business has been affected by a number of factors including an increase in business rates, higher insurance premiums and also, due to his age, having to employ staff to help him in the shop.

Mr Gadwall had not previously paid much attention to his finances as there would always be sufficient funds in his business account to pay liabilities as and when they fell due. He would therefore only instruct his accountant on an annual basis to prepare accounts and to file his tax return. Mr Gadwall is concerned that his once healthy business account balance has gradually been eroded and the account is now approaching its £5,000 overdraft limit. Muscovy Bank has advised Mr Gadwall that it is not prepared to extend the overdraft limit.

Mr Gadwall is contemplating retirement and, whilst he was planning on selling the business in a few years, he does not want to continue trading if this will cause his financial position to deteriorate.

Mr Gadwall visits the local meat market every day. He has an account with a supplier (Mr Drake) who is based at the market. Between January and November each year he spends £15,000 a month on meat and poultry. In December Mr Gadwall's expenditure at the meat market triples. On average 5% of the meat and poultry that is purchased has to be destroyed as it does not sell in time. Mr Gadwall used to pay his account with the supplier in full each month. However, for the last three months he has only been able to pay £8,000. He is not sure what he will be able to pay to the supplier this month. Whilst Mr Drake has been supportive and has indicated that he will continue to supply him until the end of 2018, Mr Gadwall is concerned that the supplier may stop supplying him in the New Year if his financial position does not improve.

All sales achieve a gross profit percentage of 30%.

The business operates from a shop which costs £2,000 a quarter to rent. Business rates are £7,000 per year. Utilities cost a further £4,800 per year. Mr Gadwall works full time in the shop and draws £1,000 a month. He employs one member of staff for 30 hours a week at £9.00 an hour and another member of staff for 10 hours a week at £5.60 an hour. During December, longer opening hours mean that staffing costs increase by 50%. Other overheads generally average 10% of turnover.

Mr Gadwall has little in the way of personal assets. He lives in a rented flat above the shop and has an old van which he uses in the business and which has an estimated value of £1,500. Personal effects and items in the shop are estimated to be worth in the region of £6,000. Mr Gadwall has a savings account with Muscovy Bank which has a balance of £14,700.

In order that Mr Gadwall can gain a better understanding of his trading you have agreed to prepare an estimated profit and loss account for the year to 31 December 2018. Once this has been prepared Mr Gadwall has arranged to come to see you again in order to discuss his options.

Requirements

(i) Prepare an estimated profit and loss account for Mr Gadwall's business for the year to 31 December 2018. Set out your supporting calculations and state what assumptions you have made. Ignore VAT. (10 marks)

(ii) In advance of your meeting, prepare a note which sets out the options that are available to Mr Gadwall and the potential consequences of each option. (12 marks)

At the conclusion of your meeting with Mr Gadwall he advised you that he would go away and think about his options but you did not hear anything further from him. Three months later you are contacted by Mr Drake who was aware that you had been assisting Mr Gadwall. Mr Drake informed you that he has an expired charge for payment for sums owed to him by Mr Gadwall and had intended to petition for his sequestration. However, Mr Gadwall has died and Mr Drake is unsure how to proceed and concerned about whether it is worthwhile incurring any further cost. Mr Drake has asked whether you would act as Trustee of Mr Gadwall.

Requirements

(iii) Given your prior instruction by Mr Gadwall, explain whether or not it would be appropriate for you to accept appointment as his Trustee. (5 marks)

You have recently taken a number of appointments as Trustee where asset realisations have turned out to be insufficient to enable your remuneration to be paid. You therefore decide to try and determine whether, commercially, it would be worthwhile accepting the appointment as Mr Gadwall's Trustee.

Requirements

(iv) Explain whether or not it would be commercially worthwhile for you to accept the appointment as Mr Gadwall's Trustee; (4 marks);

(v) Having regard to the circumstances of Mr Gadwall's case, set out the sums that would be payable out of the estate ahead of any distribution to Mr Drake and other unsecured creditors; (5 marks); and

(vi) Set out the various ways in which a Trustee can be appointed both in the specific circumstances of this case and generally; (4 marks).

Total: (40 marks)