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BLOG ENTRIES

23 AUGUST 2012 TO 10 OCTOBER 2012

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1. Changes to Money Laundering Regulations 2007 – planned for 1 October 2012 (23 August 2012)

In July 2012, the Government published its response to the 2011 consultation on proposed changes to the Money Laundering Regulations 2007 ("MLR07") – see http://www.hm-treasury.gov.uk/press_61_12.htm. I describe below the aspects of the response that in my view may affect IPs (and some that more directly impact the RPBs), although it should be noted that there are other changes to the MLR07 (and please note the end of "About" for the basis of any of my comments made on this blog).

Reliance

The MLR07 allow businesses to rely on customer due diligence ("CDD", i.e. identity checks) carried out by certain regulated third parties, provided certain conditions are met. The reliance conditions have always appeared to me to be almost as onerous to the newly instructed regulated business as those required simply to conduct CDD via the new client direct (see paragraph 5.33 et seq of the CCAB Anti-Money Laundering Guidance, available on www.ccab.org.uk). However, in some insolvency circumstances, I can see that it would be useful to rely on the CDD of the client's bankers, solicitors, accountants or a previously-instructed IP who either was involved in the pre-insolvency period or who was a previous office-holder. Nevertheless, I get the feeling that few IPs use the reliance provisions and I doubt that the subtle distinction between which regulated businesses/persons can be relied upon is well-known either.

The MLR07 separate Supervisors into Part 1 and Part 2 – businesses/persons who are supervised by Part 1 bodies can be relied upon but those supervised by Part 2 bodies cannot. This has resulted in a peculiar situation – and in my view an unfair distinction – that, for example, a successor IP can rely on checks made by an ICAEW-licensed IP but not by an IPA-licensed IP. I am pleased that the Government plans to correct this position.

In its response, the Government has stated that "based on recent and continuing work with Supervisors, it is considered that they are discharging their role satisfactorily and that the proposed change [in removing the distinction between Part 1 and Part 2 Supervisors] is advisable" (paragraph 2.21). It also acknowledges (2.23) that "while liability remains with the business placing reliance, some businesses may be reluctant to take advantage of this provision". Whilst this may suggest that there is some acceptance that use of the reliance provisions will not be widespread, given the Government's emphasis on saving costs (it is noted that the Impact Assessment accompanying this response states that there is "agreement that the change will save both businesses' and customers' time" (page 13), something that personally I would dispute for regulated businesses given the conditions attached to the reliance provisions) and not making consumers' lives unnecessarily burdensome, I would not be surprised if there is more emphasis put on using reliance more in the future.

The draft Money Laundering (Amendment) Regulations 2012, which are proposed to take effect on 1 October 2012, will replace the schedule of Part 1 and 2 professional Supervisor bodies with a single list.

Information Gateway between Supervisors

The draft Regulations introduce an information gateway between Supervisors "for purposes connected with the effective exercise of the functions of either supervisory authority".

The insolvency RPBs long ago signed up to a Memorandum of Understanding with the Insolvency Service that in some respects meets a similar purpose in the regulation of IPs. For example, it is usual practice for an RPB to provide regulatory information to another RPB where an IP seeks to move his/her licence. Clearly, this makes good sense for effective regulation and thus it makes sense to me to extend such information-sharing to regulated businesses'/persons' track records on MLR07 compliance.

One issue that bothers me a little is how this new MLR provision will interact with the Freedom of Information Act ("FoIA"). Whilst this is not an issue when information is shared between RPBs as they are not public bodies under the FoIA, many of the MLR07 Supervisors are public bodies, thus there may be a possibility of regulatory information becoming more widely disseminated. However, perhaps some might consider this a positive!

Records on Beneficial Owners' Identity Checks

This was not a subject of the consultation, but in my view the proposed change makes perfect sense and I would not be surprised if the omission of this matter from the MLR07 has passed most people by, as it had me.

Regulation 19(2)(a) of the MLR07 requires the retention of a copy of, or references to, the evidence of customers' identities obtained but not that for beneficial owners. The draft 2012 Regulations, to take effect from 1 October 2012, widen this requirement to retaining records on the checks made on the identities of beneficial owners (although peculiarly the current wording of the draft Regulations is "or", not "and"). I suspect that many IPs' systems incorporate the retention of such records anyway, but it might be worth checking this out.

Consultation Proposals Abandoned

I was heavily involved in drafting the IPA's response to the consultation, so I was interested to read about the proposals that, post consultation, the Government has decided not to pursue.

The Government had contemplated removing the criminal sanctions attached to some of the MLR07 breaches. It has decided not to do so as the consultation responses highlighted a number of risks in dropping the sanctions. In response to the Law Society's comments that the current threat of criminal sanctions burden legitimate businesses due to the procedural/administrative nature of the MLR07 requirements and because criminal breaches may occur through inadvertent mistakes (paragraph 2.9), the Government highlights that the Crown Prosecution Service has made it clear that "it is not in the public interest to prosecute employees of regulated businesses for minor, procedural or accidental regulatory failures" (paragraph 2.12). However, I suspect that this is cold comfort for businesses and individuals who are nervous about falling foul of the MLR07 requirements particularly those carrying a threat of criminal action.

Another proposal was to exempt very small businesses, the suggestion being those that turn over less than Euros15,000 pa, from some of the MLR07 requirements. Some consultation responses suggested that criminals may target small businesses – and certainly the risk would be greater if they were to be made exempt from some MLR07 requirements. The proposal has been dropped because the Government acknowledges that there is no correlation between the size of a business and the money laundering risk it represents. Paradoxically it seems to me, the Government response follows this with the words: "Supervisors are encouraged to ensure that the risk-based approach translates into effective, differential treatment in terms of the burden of requirements and, where possible, the fee levied". I understand that some non-insolvency Supervisors already operate tiered

fees for members, but given that most, if not all, of the MLR monitoring carried out by the RPBs/Insolvency Service sits alongside monitoring IPs' compliance generally, I suspect it is unlikely that small IP practices will see a drop in fees in response to the Government's encouragement.

2. Can a successor office-holder rely on the previous office-holder's fee resolution? (24 August 2012)

I was asked this question informally by an IP and I hope that she will not mind me using it as an illustration of how I hope this blog content will develop. I invite any IP or others working in the UK insolvency industry to send to me queries (at insolvencyoracle@pobox.com) on technical, ethical or SIP matters (but please bear in mind that I'm not a solicitor!) and I will provide my thoughts, confidentially if you would prefer, but I am a great believer in sharing information, so I'm hoping to post the results (avoiding any hint of the identity of the enquirer, of course) on this blog. The usual caveats apply: these are purely my own views and are not to be relied upon.

So to the query: a liquidator, IP1, is replaced by IP2. Can IP2 draw his fees on the basis of a resolution put forward by IP1 whilst he was in office and approved by creditors before IP2 came on the scene?

Cases after 6 April 2010

The answer appears simple for cases that commenced after 6 April 2010 (having regard, of course, to the effects of the transitional provisions): R4.131B of the IR86 states that "if a new liquidator is appointed in place of another, any determination, resolution or court order in effect under the preceding provisions of this Section of the Chapter immediately before the former liquidator ceased to hold office continues to apply in respect of the remuneration of the new liquidator until a further determination, resolution or court order is made in accordance with those provisions". There are similar rules for some other insolvency types – R2.109B for Administrations and R6.142B for Bankruptcies – but, as to be expected, there are no such provisions for VAs or Receiverships.

Cases before 6 April 2010

There are no statutory provisions to deal with this matter for cases pre-April 2010, so I would suggest that the answer lies in the wording of the original resolution. If the resolution is of the usual style, "remuneration shall be fixed by reference to time properly given by the liquidator and his staff…", then it would seem to me that the actual identity of the liquidator does not come into the equation, although of course the thoughts of the creditors when they considered the resolution would be concentrated on IP1. I believe that this resolution technically would apply also to IP2's remuneration on his succession. The matter would be different, however, if the original resolution specifically referred to IP1 (and/or his firm, if that is different from IP2's).

There is an ethical angle here too, however. Given that the creditors approved the original resolution on the basis of the charge-out rates of IP1 and his staff, some may question the ethics of IP2 relying on such a resolution to draw fees at significantly higher charge-out rates. SIP9 (paragraph 16) does provide that creditors be informed of changes in charge-out rates when reporting routinely, but it would seem to me fairer to creditors to explain to them up-front, when the change in office-holder has taken place, that IP2 is relying on the original fees resolution and providing details of his and his staff's charge-out rates. Personally, I do

not believe that it would be necessary to seek a new resolution to approve IP2's time costs if different charge-out rates apply, but this may be a method of heading off future challenges or complaints.

3. What Should an Administrator do if his proposals are rejected by creditors? (27 August 2012)

Lavin & Ors v Swindell [2102] EWHC 2398 (Ch) (23 August 2012)

http://www.bailii.org/ew/cases/EWHC/Ch/2012/2398.html

The Administrator did not call a meeting to consider his proposals, as he envisaged there would be insufficient funds for a dividend to unsecured creditors. Some creditors requisitioned a meeting at which a majority of creditors voted to reject the Administrator's proposals. They also voted that the Administrator should immediately petition for the compulsory winding up of the company, however the Administrator did not accept this modification to the proposals citing that there were insufficient funds to cover the petition costs. The proceedings were commenced by a creditor in order to compel the Administrator to apply for the compulsory winding up.

Behrens J considered the notes in Lightman & Moss' the Law of Administrators and Receivers and Sealy & Milman's Annotated Guide to the Insolvency Legislation on Paragraph 55 of Schedule B1 of the IA86. Lightman & Moss suggest that "the administrator is under specific duties to seek directions from or the permission of the court… where he finds that his proposals, or any revisions to them, are not approved at a creditors' meeting", whereas Sealy & Milman suggest that "although the administrator is required to report the failure to gain approval to the court, it does not appear essential that he should seek any ruling from the court: in particular, if revised proposals are not approved, he is surely free to continue to act under the original proposals or to draw up a new set of revised proposals and summon a further creditors' meeting".

Behrens J preferred Lightman & Moss' views: "Whilst it is true that paragraph 55 does not expressly require the Administrator to bring the matter before the Court, to my mind the language of paragraph 55(2) contemplates that there will be a hearing and indeed necessarily implies that there must be a hearing. There can only be such a hearing if an application is made. That application must ordinarily be made by the Administrator. If, as here, the Administrator does not make the application, I see no reason why it should not be made by a creditor… If, therefore, the proposals are rejected by the creditors it is difficult to see how the Administrator can manage the Company's affairs in accordance with paragraph 68 without making an application to Court" (paragraphs 64 & 66). Behrens J did suggest that the situation might not be quite so dire in the event that ***revised*** proposals are rejected, as the Administrator can still manage the company's affairs in line with the original proposals.

Behrens J concluded that the court had the power, not only to direct the Administrator to present a winding up petition, but also to wind up a company without a petition, but this step should be taken only in an exceptional case. In this case, the judge was persuaded that there were pre-Administration events that required investigation – with the consequence that it was not absolutely certain that there was no possibility of a recovery for unsecured creditors – and that had not been investigated by the Administrator. He was satisfied that, if a petition were presented, a winding up order would result and he considered that there was a degree of urgency. Consequently, his decision was that the Administrator's appointment be terminated with immediate effect and a compulsory winding up order be made.

4. When does an Administration convert to a CVL under Paragraph 83? The Globespan appeal (30 August 2012)

Cartwright & Anor v The Registrar of Companies [2012] EWCA Civ 1159 (24 August 2012)

http://www.bailii.org/ew/cases/EWCA/Civ/2012/1159.html

Summary

Many readers will be aware of the court decision leading to this appeal: Briggs J decided that the date of conversion from Administration to CVL is the date the Paragraph 83 notice is ***received*** by the Registrar of Companies ("RoC"). This appeal considered the RoC's contention that the conversion date is the date the notice is ***registered*** by it. In short, the court of appeal agreed with the RoC and it considered the vital question arising from this conclusion: what happens if the notice is ***received*** by the RoC whilst the Administrator is in office, but is only ***registered*** after the Administrator's term of office has ended, e.g. by effluxion of time per Para 76(1)? The court decided that there is generally an automatic extension of the Administrator's appointment to cover this period (provided the notice is duly filed).

The dates in this case

The Administration began on 17 December 2009. On 13 December 2010, the Administrators signed a Para 83 notice, which was received by the RoC on 14 December 2010. The RoC rejected it because it did not contain the Liquidators' addresses, albeit that it contained the Administrators', which were the same. After some toing and froing, the RoC finally registered a Para 83 notice (the third one submitted to them) on 4 February 2011, i.e. long after the anniversary of the Administration.

Why the court decided that the conversion date is the date of registration

Lady Justice Arden provided eight reasons for this decision (paragraph 41 et seq.). In my view, the most persuasive arguments lie in the wording of Paragraph 83(4) and (6). Para 83(4) states that "On receipt of a notice under sub-paragraph (3), the registrar shall register it", indicating that receipt and registration are two different events. Para 83(6) states that "On registration of a notice under sub-paragraph (3), the appointment of an administrator in respect of the company shall cease to have effect and the company shall be wound up as if a resolution for the voluntary winding up under section 84 were passed on the day on which the notice is registered". Taken together, I can see why the judge concluded that the date of registration is the conversion date and the judge noted that "the most natural meaning to give it [the word "registration"] is the completion of the steps which the registrar needs to take to make the information in the notice available as part of Globespan's file at Companies House" (paragraph 43).

In this case, because of all the toing and froing of Para 83 notices, this conclusion led to an interesting result: the Administration moved to CVL on 4 February 2011, almost two months after the anniversary of the Administration. Fortunately for the Administrators, as Briggs J had already decided that the first Para 83 notice was valid notwithstanding the absence of the Liquidators' addresses and the RoC had not sought to contest this, the appeal court concluded that "in registering the third conversion notice, the registrar was in fact fulfilling his obligation to register the first conversion notice. That conversion notice was executed and filed when the administrators were still in office" (paragraph 52). Thus, it was irrelevant in this case that the third notice was sent by the IPs to the RoC long after the anniversary had

passed. I suspect that the situation would have been quite different had there been a real deficiency in the first notice, as this would have meant that any subsequently correct notice would have been filed after Para 76(1) had taken effect to end the Administrators' appointment.

What is the status of the Administrators between the filing and the registration date?

As mentioned above, the first Para 83 notice was received by the RoC on 14 December 2010; the anniversary of the Administration was 17 December 2010; and the court decided that the move from Administration to CVL occurred on 4 February 2011. No extension to the Administration was sought under the Act's provisions, so the question arises: did the Administrators' appointment end some two months before the company moved to CVL?

Lady Justice Arden decided that "the administrator's term of office is in general automatically extended if a conversion notice under paragraph 83 is duly filed" (paragraph 58) and she provided five reasons for this judgment. Personally, I like the judge's argument that the Act provides for the Administrators to file a Para 83 notice at any time whilst they are in office, i.e. right up to the point when the Administration is about to end (although personally I would still be very nervous about leaving the Para 83 notice to the last minute), but Parliament's clear intention was to provide a seamless transition between Administration and CVL. Thus, it would make no sense to require Administrators to seek extensions to Administrations to cover the interregnum from the RoC's receipt of the notice to the point that it is registered.

Interestingly, the judge stated "on the evidence that [registration of the notice] would normally have happened within about 3 days of 14 December 2010 [the date the notice was received by the RoC]" (paragraph 32). I have not been at the front-end of filing documents with the RoC for a long time now, but I am surprised to see such a short timescale evidenced as normal – things must have improved a great deal since my days! Fortunately, in view of the judge's reasonings, it would seem to me that the length of this time between receiving and registering the notice is immaterial. Paragraph 64 of the judgment simply states: "an administrator's term of office is by implication from the words of paragraph 83(6) extended by filing a conversion notice from the date on which it would otherwise expire by effluxion of time until paragraph 83(6) comes into effect on registration of the conversion notice" (although, quite rightly the judge points out that this is subject to the provisions of Paragraphs 87 to 89, i.e. if the Administrator were to die, cease to be qualified etc., during this interregnum).

23 September 2012: Companies House has lodged a statement following the appeal decision explaining the consequences for filing. The statement can be accessed at: http://www.companieshouse.gov.uk/about/miscellaneous/insolvencyCourtOfAppealJudgement

5. BIS Measures to Enhance Consumer Protection – summer consultations (6 September 2012)

Insolvency-specific case law has been quiet over the last couple of weeks, so I've taken a closer look at some summer publications that touch on insolvency matters.

I will start by apologising for the fact that likely this post will create more confusion than clarity!

Over the summer, BIS issued a consultation (plus impact assessments) on the Consumer Rights Directive, "Enhancing consumer confidence by modernising consumer law" (http://www.bis.gov.uk/Consultations/consultation-implementation-consumer-rights-directive), closing date 1 November 2012, and a standalone impact assessment, "Enhanced suspension of consumer credit licences" (http://www.bis.gov.uk/assets/biscore/consumer-issues/docs/e/12-987-enhanced-suspension-of-consumer-credit-licences-impact), which explores the "preferred option" of introducing a change via the Financial Services Bill plus an OFT consultation in September 2012 on draft guidance. I read these documents whilst keeping in mind the question, what impact, if any, might these proposals have on IPs? I have to say that I discovered that this was a tricky question to answer given the plethora of existing regulations! There is a further BIS consultation, "Enhancing consumer confidence by clarifying consumer law" (http://www.bis.gov.uk/Consultations/consultation-rationalising-modernising-consumer-law?cat=open), closing date 5 October 2012. I have not reviewed this one, although it does encompass proposed changes to the Unfair Terms in Consumer Contracts Regulations 1999, so there may be some impact for IPs – and presumably, if there is, the OFT will revise its debt management guidance accordingly.

Consumer Rights Directive

The Consumer Rights Directive ("CRD") was agreed by EU Member States in October 2011 and this BIS consultation explains how it is proposed the Directive will be reflected in UK statute. The focus of the Directive includes on transparency of information, particularly pre-contractual information, cancellation rights, and express consents for payments.

Readers will be aware that the OFT has issued guidance on how it expects consumer credit licence-holders who provide debt advice and debt management services (which, by the OFT's definition, includes those who advise and assist debtors with IVAs and Trust Deeds) to demonstrate their fitness to hold a licence. The OFT's debt management (and credit repair services) guidance ("DMG" http://www.oft.gov.uk/shared_oft/business_leaflets/credit_licences/oft366rev.pdf), thus describes expected standards in relation to some areas that are likely to be impacted by the implementation of the CRD.

However, the CRD does not apply to "financial services", which are defined as "any service of a banking, credit, insurance, personal pension, investment or payment nature" (Art 2(12)), and BIS' CRD consultation states that "The Financial Services (Distance Marketing) Regulations 2004 will remain in force, offering consumer protection for financial services sold at a distance. There are also additional protections through FSA rules, under the Financial Services and Markets Act 2000, offering protection for certain off-premises sales as well as on-premises sales" (footnote on page 28).

But are the provision of IVAs and Trust Deeds caught by this "financial services" exemption? To my mind, helping debtors avail themselves of statutory insolvency processes does not fit exactly the CRD definition (which is the same as the definition in the Financial Services (Distance Marketing) Regulations 2004). However the OFT DMG states: "In the OFT's view, a licensee who provides debt management services or credit information services will be providing financial services and those that do so at a distance should comply with the Financial Services (Distance Marketing) Regulations 2004" (paragraph B.8). It is noteworthy that the OFT's previous DMG (issued September 2008) referred to the Consumer Protection (Distance Selling) Regulations 2000 as setting down the requirements for providers of debt management services, but this does not appear in the current DMG. Presumably therefore, the OFT had reconsidered its views on which regulations apply sometime before the current DMG was issued in March 2012.

If the OFT's (current) view is correct, then it would seem to me that very little UK statute arising from the CRD will impact IPs – it is anticipated that the Consumer Protection from Unfair Trading Regulations 2008 and the Provision of Services Regulations 2009 will continue in force – and thus we can rest easy that the outcome of this consultation will not alter IPs' pre-Nominee/Trustee engagement with debtors (although the Cancellation of Contracts made in a Consumer's Home or Place of Work etc. Regulations 2008 and the Consumer Protection (Distance Selling) Regulations 2000 will be revoked and replaced). But can we..?

Then again, should we be concerned even if the CRD does stray into IPs' work? In my view, much of the proposals seem common-sense, concerning the provision of thorough information to consumers about the service to be provided, charges to be made, cancellation rights, etc. Thus, implementation of the CRD may require IPs to revisit, and probably lengthen, their engagement letters and terms and conditions – and some provisions may prove cumbersome to translate in relation to the provision of IVAs or Trust Deeds – although much of the principles of transparency, fairness etc., seem to be covered already by the OFT DMG and related regulations.

In researching this matter, I got to the bottom of one significant change in the OFT DMGs that arose due to the OFT's shift away from the Consumer Protection (Distance Selling) Regulations 2000 to the Financial Services (Distance Marketing) Regulations 2004. The Distance Selling Regs 2000 require only a 7 working day cooling-off period, but the Financial Services Regs 2004 require 14 calendar days (and the on-consumer-site Regs require 7 calendar days). Thankfully (in the interests of consistency at least), the CRD consultation proposes to change the cooling-off period for both off- and on-site sales to 14 calendar days, which would bring it in line with the selling of financial services.

Enhanced Suspension of Consumer Credit Licences

At present, when the OFT considers a consumer credit licence-holder is unfit, the licence remains in effect until all rights of appeal have been exhausted. The appeal process can take up to two years, during which time a licence-holder may continue to trade uninterrupted. Although it is expected that the new Financial Conduct Authority will take over credit regulation from the OFT in April 2014, the BIS select committee and others have called for more immediate changes. Thus, it is proposed that with effect from spring 2013 the OFT will have to power to suspend immediately a business' consumer credit licence where the OFT considers that there is a risk of serious consumer detriment.

Although this change is clearly welcome given the worrying companies that pop up from time to time, I have been aware of "minded to revoke" notices issued by the OFT in the past on businesses whose practices, in my mind, should not be fatal (they are either easily rectified or in fact defensible). It seems to me that the OFT has only really been aware of IVAs and Trust Deeds in the past four years or so and its knowledge still seems somewhat patchy (perhaps not helped by the regular rotation of staff to different positions in the department). The Impact Assessment states that the new power would only be used against businesses that cause significant and ongoing harm to consumers and it defines consumer detriment as including "being sold inappropriate or more expensive credit products due to poor or misleading customer advice, provision of incomplete or incorrect customer information, harassment of customers, delays in providing refunds, deducting additional fees without informing the customer etc." (paragraph 33).

Although I take some comfort in the Impact Assessment's statement that "the OFT is in close contact with firms under investigation and the firms have the opportunity to explain their behaviour etc and alter it if required" (paragraph 32), and thus perhaps the "minded to

revoke" process or something similar may still be used to persuade firms to fix deficiencies or to convince the OFT that in fact they are compliant, clearly the impact on a business of an immediate licence suspension would be enormous. Therefore, I hope that the OFT remains – and perhaps becomes more – open to engagement with licence-holders who are endeavouring to be compliant, some of whom may have suffered temporary lapses in performance or who may hold a different opinion, for example, on what constitutes correct or complete information.

6. Two case summaries – COMI and a rejected Administration Order application (7 September 2012)

Sparkasse Hilden Ratingen Velbert v Horst Konrad Benk & The Official Receiver (29 August 2012)

http://www.bailii.org/ew/cases/EWHC/Ch/2012/2432.html

I confess that COMI cases have always left me cold, but I have tried to extract some interest from this case that appeared to me to follow principles set down in earlier cases, which Purle J usefully summarises.

In short, the court decided that the debtor's COMI was, at all material times, Germany – the debtor purported to trade as a photographer in England (he had practised as a notary in Germany), albeit that he did not own a camera and the judge stated that the main purpose for taking golfing tours was recreation, not photography; the judge also commented that the photography business was not at the root of the insolvency, which was caused by his previous German business activities – with the consequence that the Bankruptcy Order was annulled. However, what I found interesting was that the debtor's original bankruptcy petition was opposed by the OR – in fact, it was a second petition, as the first Order was annulled on the application of the OR on the grounds that the debtor had provided false information – but that opposition, and a later appeal, failed. This annulment application was brought by the German Bank, owed some Euros3 million, which contended that the debtor did no more than create the illusion of an English COMI. It is clear that this time the court was provided with far more evidence and, whilst it is a shame that the OR's earlier objections were unsuccessful, it is comforting to note that at least the OR remains alert to potential abuses. It was also interesting to note that, in this case, the bankruptcy was discharged automatically on 17 June 2011, but notwithstanding this, as S282(3) provides, the Order was annulled.

UK Steelfixers Limited (23 July 2012)

http://www.bailii.org/ew/cases/EWHC/Ch/2012/2409.html

A bit of an old case this one that I'd not covered before, as I don't think it generates any new thoughts, but perhaps it provides a warning for IPs (or more correctly of course, directors) seeking certain Administration Orders.

The application was sought on the grounds that there was likely to be a better result for creditors than liquidation. There was a proposed pre-pack to a company owned and controlled by an employee, Mr Harrison, and there was also an extant HMRC winding-up petition.

Purle J was "not at all happy with the history of this company" (paragraph 2). It seems that Harrison's company had already stepped well into the frame – Harrison's company's bank account had been used to receive the main customer's payments and to discharge company debts including wages, the argument being that there was a risk the main contract would be lost, if this were not done. "Another construction that can be put on what happened is that Mr Morrison and Mr Harrison effectively put the prepack in place before the administration occurred, thus pre-empting the court's decision" (paragraph 3).

Purle J commented on the proposed administrator's "very full witness statement containing all the SIP16 material" and that the proposed administrator had "reached the conclusion, no doubt genuinely, that almost any sale is better than a liquidation because the goodwill will in his professional judgment realise nothing on a liquidation, especially as the relationship between the main customer and Mr Harrison's company is already in place" (paragraph 5). However, it seems that Purle J was sceptical about the £5,000 round sum paid to Harrison during the post-petition period and wished to see that, and other post-petition transactions and activity, investigated. "Proper consideration of those transactions may also reveal that the company's goodwill has already been arrogated in whole or in part to Mr Harrison or his company, giving rise to a claim for payment or compensation for that goodwill" (paragraph 6). Despite commenting that "there is evidence of the usual quality that the result of an administration will be better than a liquidation" (paragraph 7), the judge concluded that, in the interests of conducting such investigations, a winding-up order be made that day.

7. The AiB/Scottish Government's report on Responses to the Bankruptcy Law Reform Consultation (13 September 2012)

Summary

The AiB/SG's consultation, which closed on 18 May 2012, raised questions on every aspect of Scottish personal insolvency – DAS, PTDs, SEQs, LILAs, and even suggested introducing a whole host of other "products" – as well as exploring the AiB's current and prospective roles in administering and supervising insolvencies. The report on the consultation responses was published on 28 August 2012 and can be accessed at: http://www.aib.gov.uk/news/releases/2012/08/bankruptcy-law-reform-consultation-summary-responses

The summary of the opening Summary alone lists 65 conclusions (pages 5 to 7), but I have attempted to list the most significant below (my comments added in parenthesis). I should mention that I have only ever come across Scottish insolvency in my role at the IPA, so, although I have been closely involved with Scottish IPs in drafting consultation responses (although not for this one) and I have reviewed Scottish cases as part of the monitoring function, I have no front-line experience of administering them.

- Money advice to be made compulsory prior to accessing any form of statutory debt relief, although not to be provided by the AiB
- Support to have one Common Financial Tool, preferably a Scottish-specific one, against which all debtors will be measured, irrespective of the insolvency process being contemplated
- Allow assessed contributions to be deducted directly from an individual's wages
- "Support to introduce a moratorium period of 6 weeks in statutory debt relief products, these to be displayed in a public register" (this seems to be directed at bankruptcy, so that the debtor can intimate an intention to apply, as is currently available in DAS)

- "DAS should not be the default option where an individual can pay their debts in 8 years, although there was support for a shorter period" (it seems the majority who responded to the question, "how long should it be?", answered 6 years. However, the table suggests that "majority" is only 12 out of a total of 129; 89 answered "N/A", so presumably many of those would not wish to see ***any*** defined timescale where DAS is the default option – seemingly this was not picked up by the AiB.)
- "Composition in DAS should be available, after the programme has run for 12 years and 70% of the debt has been paid" (although not in the summary, the report indicates that a strong majority would like creditors to have to consent to the composition, with some suggestion being that this is sought after DAS has run successfully for a number of years)
- Support for a minimum debt level of £10,000 for entry into a PTD
- Support for a minimum dividend in PTDs (see my comments below)
- There should not be a fixed term for completion of a PTD
- The current process of deemed consent and current thresholds in PTDs should continue
- "Support for the removal of Apparent Insolvency as criteria in debtor applications" (the report adds: "if mandatory advice is adopted as a precursor to bankruptcy")
- The minimum debt level for debtor's bankruptcy should increase to £3,000
- Support for a "No Income" product for individuals on state benefits who have up to £10,000 of debt and up to £2,000 of assets
- Other products, e.g. "Low Income Product", "High Value Product", not required
- Support for a new Business DAS for sole traders and partnerships
- Support for discharge to be linked to a bankrupt individual's co-operation with their trustee
- Where an individual cannot be located their discharge should be deferred indefinitely
- AiB should have the power to defer discharge rather than refer the case to a sheriff
- Support for debts that were incurred within 12 weeks of a debtor application or the granting of a trust deed should be excluded from discharge
- Child maintenance arrears and credit union debts should continue to be discharged in bankruptcy and PTDs
- Creditors should have to submit a claim within 120 days (the report adds "… of notification of an individual's bankruptcy", although the consultation question suggested this statutory timescale for all processes and this had strong support from respondents)
- Support for the recall of bankruptcy process to be clarified and that the final interlocutor should be withheld until all funds have been distributed
- The current prescribed rate of interest should be retained and all post-procedure interest and charges be frozen
- Support for the debtor's discharge to be linked to the date of award
- Payment holidays of up to 6 months should be available in all statutory debt relief products and the period of time added onto the length of the product before discharge is granted
- AiB should have the power to make orders for some bankruptcy processes and a separate independent panel should be used to review complex or disputed decisions
- AiB should not have a more proactive role in supervising debt relief products
- An AiB panel should not determine an appropriate course of action where a trustee has not followed an AiB direction (see my comments below)
- Support for a Memorandum of Understanding between the UK Insolvency Service and RPBs to be redrafted to allow information on regulatory activity related to Scottish cases to be issued to AiB
- "There should be an office of the Official Receiver in Scotland and this role should be carried out by AiB" (i.e. to act as liquidator of last resort)

The timescales for changes are, understandably, vague, given the vast range of proposals that will affect primary and secondary legislation as well as AiB Guidance Notes and the development of other projects, such as the proposed Scottish common financial tool. Whilst the report states that, after a series of stakeholder workshops, it is hoped that the SG will be in a more informed position to issue an official response, the AiB's website states that the SG's response is expected to be published in October 2012.

My thoughts on the report – the methodology

What struck me was the AiB's methodology in considering, not only the numbers of responses by individuals, but also those by organisations only. The cynic in me senses that the AiB may have been somewhat selective in this consideration.

For example, Q15.1b asks: "If the AiB should continue to act as trustee, should she act only as trustee of last resort?" (page 87). 49 individuals answered "yes" and 44 answered "no", but when responses only from organisations are considered, this becomes 29 "yes" against 39 "no". The summary to this section states: "Whilst the majority of respondents believed that AiB should continue to act as trustee of last resort, when the figure for organisations only was examined, this showed that AiB should continue to act as trustee in all cases where appointed" and this conclusion seems to have drifted into the opening summary. However, on other occasions, an "organisations only" majority does not seem to have influenced the outcome. For example, Q15.4 asks: "Where the AiB makes a direction which is not adhered to by the trustee, should an AiB panel decide on an appropriate course of action?" (page 89). Although more "organisations only" answered "yes" than "no", fewer individuals answered "yes" than "no" and the individuals' voices seem to have taken precedence in the conclusions (albeit that the comment from Nolans Solicitors suggests that some "no" respondents may feel that someone ***other*** than an AiB panel, e.g. the IP's regulator, should decide – something again not picked up by the AiB).

Perhaps I should not be too selective myself however, as sometimes this selective process seems to lead to positive outcomes. For example, Q15.3 asks: "Should AiB have a more proactive role in the supervision of all debt relief products?" (page 89). Although more "organisations only" answered "yes" than "no", fewer individuals answered "yes" than "no" and the individuals' voices seem to have taken precedence in the conclusions.

Given that IPs are perhaps more accustomed to writing as individuals than the other categories of respondents, it is not surprising that this selective approach, putting greater emphasis on "organisations only" responses, sometimes swings the outcome away from what I suspect are the IPs' preferences. 20 of the 37 IP responses were from individuals, whereas all the creditor responses were from organisations and only 7 of the 27 advice sector responses were from individuals (and 13 in the "other" category). There may be some merit in giving less weight to some individual responses (which some may be inclined to put in the "green ink brigade" category), but given that the vast majority of IPs operate in an "organisation" and many manage that organisation, this broad-brush distinction seems grossly unfair to me.

My thoughts on the report – the detail

Although there are many quoted responses that are extremely sensible suggestions, of which I hope the AiB will take notice and incorporate in future plans, some response quotes raised my hackles. For example, there seems to be a perception that, if a PTD only produces a 50% dividend, this means that a large proportion (would some incorrectly assume 50%?) of the funds ingathered fall into the hands of the IP (see, for example, Grampian Credit Union's comment on page 32). Putting aside all the non-IP costs that need

to be discharged, the percentage dividend of course bears no resemblance to the ***amount*** of the funds paid as a dividend. For example, if £10,000 is distributed to creditors with claims of £200,000, this is only a 5% dividend, but if the same sum is distributed to creditors with claims of £20,000, it is a 50% dividend (perhaps a comparison of extremes, but I'm sure you get the point). Thus it is nonsensical to assume that a PTD paying out a low dividend is automatically disadvantageous to creditors; surely the crux of the matter is: would the outcome be any better (not forgetting the impacts on the debtor) via any other process? It seems to me that the only real way of exploring whether PTDs can become more beneficial to creditors is to consider carefully whether the costs in the process can be reduced, although the outcome of the AiB/SG's earlier consultation on "Protected Trust Deed – Improving the Process" suggests to me that the process will become ***more*** costly with more reporting and other burdens laid at the IP's door.

It is therefore extremely frustrating that the outcome of the consultation, that "the majority of respondents either suggested 10p in the pound or that no minimum amount should be specified" (page 33), has been interpreted by the AiB as "support for a minimum dividend on PTDs" (summary on page 5).

I was surprised at the majority (albeit not a large one) supporting the idea that a debtor's discharge from bankruptcy be deferred indefinitely where he/she cannot be located. I would concur with ICAS' comment (page 63) that "just because an individual cannot be located does not indicate that he would not co-operate. Consideration has to be given to whether the Trustee has been able to deal with the estate effectively for the benefit of the creditors. Each case has to be considered on its own merits". Hopefully, reasonableness will prevail if/when this provision makes it to statute.

I also find the idea that debts incurred prior to bankruptcy (the apparent preferred period being 12 weeks) should be excluded from discharge a novel one, particularly in comparison with E&W bankruptcy legislation (putting aside transactions such as preferences). I will be interested to see how this is described in draft legislation, as the report suggests there is support for the exclusion of only some debts, such as those relating to non-essential items or where the debtor had knowledge that they would probably not be paid – this may generate some work for the lawyers and courts, I would suggest.

Speaking from my perspective of having worked at an RPB, I struggle with the arguments the AiB puts forward for engaging in an information gateway with the RPBs and the UK Insolvency Service. The AiB seems to want to know what disciplinary actions the RPB may be in the process of taking against IPs. No information gateway will assist the AiB to learn of actions-in-process (and even if she knew, what would this indicate about the IP's conduct until the issue had been decided?), but only of settled sanctions, which in most cases are in the public domain (and if any are not, it is very likely that the Insolvency Service's/JIC's work in ensuring consistency of the publicity of disciplinary outcomes will bring these into line). It is certainly the case that currently the AiB's and the RPBs' activities in supervising/regulating IPs occur in isolation from each other – and I believe that it is unhelpful when the AiB receives and investigates complaints (with no reference to the RPB) that are more suited to investigation by the IP's licensing/authorising body – but in my mind that is an inevitable outcome of the seeming overlap of responsibilities of the different bodies.

There are far too many details in the report to cover here and it is perhaps not sensible to spend too much energy in contemplating the proposed changes at this moment. I am sure that many of you, like me, will be interested in seeing how the results of this consultation are reflected in future stages.

8. Lean Pickings from recent High court decisions (3 October 2012)

My lack of blog postings has been bugging me over the past couple of weeks, but I regret that, despite my best efforts, I have failed to spot any earth-shattering news (for which we should be grateful, I guess).

Over the past weeks, I have made my personal submission to the Government's Red Tape Challenge on insolvency (but I did not think that readers would be interested in that) and I have been exploring the thorny issues of PPI claims in IVAs, but every time I look at the issues, more questions pop up. Nevertheless, I hope to post something on this subject shortly.

I have also been reviewing the High Court decisions as they have been released, but in my view there have been few of any particular interest to insolvency practitioners. For the more curious amongst you, here are my lean pickings:

- Both ***Odyssey*** and ***Ross River*** consider directors' pre-liquidation duties.
- ***Clyde & Co*** considers whether LLP members can be employees.
- ***Tinseltime*** considers solicitors' liabilities to non-party costs orders in some CFA situations.

Odyssey Entertainment Limited v Kamp & Ors (09/08/12)

http://www.bailii.org/ew/cases/EWHC/Ch/2012/2316.html

The court found that a director ("D1") had broken his duty of good faith under S172 of the CA 2006 towards the company (now in liquidation) ("C"): "In a nutshell, I find that (1) by 4.1.09, D1 had decided that C would not provide him with the route to a capital profit which he had hoped for and that he would have better prospects in that respect working on his own account; (2) thereafter, D1 influenced the board's stage by stage decision making process which led to the winding down of C's business, the termination or surrender of its contracted rights, and the liquidation of C; (3) over the period 4.1.09 to 31.8.09, D1 misled C's board as to his own true intentions and kept secret the work he undertook on his own account as a film sales agent, whilst still a director and an employee of C, as part of his plan to bring those intentions to fruition. In so doing, D1 continued to mislead C's board (and therefore C) as to C's true viability and prospects; (4) had C's board not been misled by D1, C's board would probably not have made the decisions that it did leading to its winding up on 9.9.09; and, (5) in consequence, D1 and/or D2 and/or D3 as a result of D1′s efforts secured sales agent's rights in films that (a) would otherwise probably not have reverted to the rights owner in the case of film rights already under contract to C and (b) would otherwise probably have been acquired by C in the case of other films on which D1 had been working while a director of C" (paragraph 204).

The only point of interest I gleaned was the comment of HHJ Simon Barker QC on the position of the co-directors: "What emerged from both the written evidence and the cross-examination of [the co-directors] is that they all deferred to D1′s long experience and expertise as a film sales agent (the expert witnesses were agreed that D1 is a leading individual UK film sales agent) for guidance as to C's sales prospects and, more generally, the market for independent sales agencies. In so doing, they were not simply accepting whatever D1 might say in disregard of their own powers of thought nor were they in dereliction of their duties as directors. Rather, they were giving due weight to the one of their number who could speak with particular authority on the general market for sales agents and the specific position of C" (paragraph 94).

Ross River Limited & Anor v Waverley Commercial Limited & Ors (06/09/12)

http://www.bailii.org/ew/cases/EWHC/Ch/2012/2487.html

The main issue before the court was the possible liability of a director (Mr Barnett) to pay a sum to RossRiver by way of equitable compensation for alleged breaches of fiduciary duties that he owed to RossRiver. Amongst the considerations was whether the director should have wound up the company ("WCL") earlier and before WCL had used its assets (including revenues from a joint venture with Ross River) to defend an action brought by Ross River for payment of monies due under the joint venture agreement.

Morgan J concluded that RossRiver had failed to prove entitlement to equitable compensation from the director. In so doing, he seems to have put some weight behind the director's consultation at an early stage with accountants, who reflected on the option of liquidation: "Mr Barnett did take advice on whether WCL should be wound up or, possibly, whether it was in Mr Barnett's separate interests for WCL to be wound up. There is no evidence as to the advice which Mr Barnett received. In these circumstances, I consider that I ought not to decide that it was a breach by WCL or by Mr Barnett of a fiduciary duty owed to Ross River to omit to take steps to wind up WCL in early 2009" (paragraph 74), although the fact that the allegation was not pleaded nor put to the director when cross-examined may have had something to do with the judge's decision.

Morgan J also commented: "On the face of it, WCL was entitled to defend itself and to use its own assets to do so, even though the use of those assets might produce the result that it used up all of its available funds and ended up being unable to pay any sum found to be due to RossRiver… In my judgment, both WCL and Mr Barnett were real and substantial defendants. Both were entitled to defend the claims brought against them without there being a breach of fiduciary duty owed to RossRiver. The fiduciary duties which, in my earlier judgment, I found to exist do not go so far as to restrict either WCL or Mr Barnett from putting forward their chosen stance in litigation brought by RossRiver against them. It would be a very onerous fiduciary duty which prevented a party to adversarial litigation from defending itself" (paragraphs 67 and 69).

Clyde & Co LLP & Anor v Bates Van Winkelhof (26/09/12)

http://www.bailii.org/ew/cases/EWCA/Civ/2012/1207.html

The main question before the court was: can a member of an LLP be a worker within the meaning of S230 of the Employment Rights Act 1996?

Whilst "workers" have limited rights under the ERA and do not extend to the rights to insolvency qualifying liabilities (as far as I can see) as is the case for "employees", Elias LJ did include consideration of an LLP member's rights as an employee also. He commented: "I would be minded to hold [and he did so conclude in paragraph 74] that the member of an LLP would not by virtue of that status alone constitute either an employee or a worker. Whether the member could enter into some separate employment relationship with the partnership, rather in the manner that a company director can do, would be a different question. There would be no employment status arising out of the simple status of member of the firm" (paragraph 73).

Tinseltime Limited v Roberts & Ors (28/09/12)

http://www.bailii.org/ew/cases/EWHC/TCC/2012/2628.html

This is one more for insolvency solicitors than practitioners: does a solicitor who takes on a case for an impecunious claimant under a conditional fee agreement (CFA) where there is no after the event (ATE) insurance policy in place, and who also agrees to fund the disbursements necessary to allow the case to proceed, thereby constitute himself a non-party funder and render himself liable to a non-party costs order in the same way as if he was a commercial non-party litigation funder?

Solicitors who are alert to this issue will have been watching the progress of an appeal on another case, ***Flatman v Germany & Ors*** ([2011] EWHC 2945 (QB)), in relation to which the Law Society asked to intervene. The judge, HHJ Stephen Davies, and the parties in this case did not find compelling reasons to wait for the outcome of that appeal (expected in December 2012). Although it seems possible that the appeal may proceed on grounds different to those already advanced, it is interesting that HHJ Davies, after acknowledging that there may be particular aspects of the other case that led Eady J to allow the appeal, stated that "if however Eady J was holding that it would be sufficient to make a non-party costs order that the solicitor was acting under a CFA without there being an ATE policy in place under which he agreed to fund the disbursements because the client was unable to do so and in order to ensure that the client could bring his claim, then I respectfully disagree with him. I consider that something more is required to justify the making of such an order, in circumstances where it is perfectly proper for the solicitor to agree to fund the disbursements under a CFA, even if he may be taken to know that unless he agrees to do so the claim cannot proceed" (paragraph 60).

On the facts of this case, HHJ Davies concluded: that there was nothing in the evidence indicating that the solicitor (Mr Edmonson) viewed the case as a business proposition under which he could receive a substantial fee; rather, that the solicitor had failed to understand how complex and costly the case might be; that in no way can it be considered that the solicitor controlled the litigation; and that "finally, but extremely significantly in my judgment, when I come to consider the overall justice of the matter, this is a case where there is contemporaneous evidence that Mr Edmondson was not motivated solely by financial self-interest in taking on this case, but with the laudable aim of providing access to justice to Tinseltime… Mr Edmondson was prepared to provide that assistance, where other solicitors were not. He may well have been naive as matters turned out, and Mr Ridgway may well not have been deserving of the assistance which Mr Edmondson provided. But that does not detract from the fact that Mr Edmondson cannot in my judgment be criticised, let alone made personally liable for costs, for taking on a case on a basis permitted by the law in order to ensure that Tinseltime was able to present what Mr Ridgway clearly believed was a genuine claim to the court" (paragraph 67).

Earlier in the judgement, HHJ Davies had stated: "So far as I am aware there are no reported cases in which a solicitor acting under a CFA has had a non-party costs order made against him on the basis of control, but I can see how there might be circumstances where the court was able to conclude that the solicitor's desire to achieve a successful outcome had caused him to in effect take over the running of the litigation for his own ends, and that this would justify the making of a non-party costs order against him. One example might be where the damages claimed were, or had become, modest in comparison to the costs already incurred, so that the client had for all practical purposes lost any real interest in the pursuit of the proceedings but the solicitor was wedded to pursuing them to recover his costs" (paragraph 58).

9. Mis-sold PPI claims in IVAs (8 October 2012)

In its August 2012 newsletter, the IPA referred to a number of questions on the subject of mis-sold PPI policies, which, having spoken to a few IPs, only scratch the surface of the PPI refund minefield.

As with the Paymex VAT decision, the absence of guidance from the RPBs/Insolvency Service (I appreciate that the Service has published something on PPI refunds in bankruptcy, but again that does not really begin to get to grips with the issues) will only lead, at best, to each IP seeking his/her own independent legal advice, or at worst, it may mean that some IPs fail to face the issues head-on, prepared to face (or perhaps oblivious to) the risks of challenge down the line.

I sense that the regulators have a difficult job, however, as of course many issues in IVAs turn on their particular terms and thus any guidance either will have to cover a variety of situations or will be so generic as to be well-nigh useless. However, I do not believe that this means that it is futile or unnecessary to point out the pitfalls or questions that each IP should be asking him/herself. Of course, I come at this from a purely theoretical perspective and thus I am grateful to the IPs, particularly Sue Clay and Melanie Giles, who have helped me to appreciate the practical issues and get me up to speed with what is going on out there.

What are PPI refunds – assets, windfalls or after-acquired assets?

The Insolvency Service takes the view that a PPI claim is a bankruptcy asset (http://www.bis.gov.uk/insolvency/personal-insolvency/ppi-mis-selling-claims-and-bankruptcy), however CCCSVA suggests it is caught by the windfall clause in their IVA Proposals (http://moneyaware.co.uk/2012/05/can-i-reclaim-ppi-while-on-an-iva/) – and well it might be, as IVA Proposals* can define terms as the drafter sees fit and can "deem" one thing to be another. This demonstrates the need to scrutinise the terms of each IVA Proposal (or at least each template used by the IP) to see where a PPI claim falls and thus whether it is caught by the terms of the IVA.

Proposal definitions aside, my instinct is to consider the PPI claim to be an asset, but it does not necessarily follow that it is due to be paid into the Arrangement. This will depend on the wording of the Proposal. Does the Proposal provide that all assets, apart from those expressly excluded, are available for the Arrangement? Or does the Proposal define included assets as those specified, resulting in any others (including any undisclosed) being excluded?

Could the PPI claim be an after-acquired asset? The Protocol Standard Terms & Conditions ("STC") define "after-acquired assets" as "any asset, windfall or inheritance with a value of more than £500, other than excluded assets that you acquire or receive between the date the arrangement starts and the date it ends or is completed, if this asset could have been an asset of the arrangement had it belonged to or been vested in you at the start of the arrangement" (R3's STC use similar wording at clause 27). ***Could*** the PPI claim have been an asset at the start of the arrangement or ***was*** it an asset at that time? My instinct is that the PPI claim existed at the start of the IVA; I do not believe that the asset was created when it was established that the policy was mis-sold, but the asset was created when mis-selling of the policy took place. In that event, it would not be an after-acquired asset. However, I am no lawyer, so I would welcome an authoritative answer.

Is the Supervisor obliged to pursue a PPI refund?

If it is an asset caught in the IVA, then I believe the Supervisor is so obliged (subject to the usual commercial question of whether the realisation will exceed the allowable costs to recover). However, what if it is likely that the creditor will seek to set off the claim against an existing debt? Ah, the thorny problem of set-off! Let me start with the definitions in widely-used STCs.

Set-off and the Protocol STC

Clause 17(6) of the Protocol STC states: "where any creditor agrees, for whatever reason, to make a repayment to the debtor during the continuance of the arrangement, then that payment shall be used solely in reduction of that creditor's claim in the first instance. If such repayment results in the creditor's claim being entirely extinguished (after the application of set off) any surplus will be treated as an after acquired asset and offered to the Supervisor for the benefit of the arrangement". I understand that proceeds of PPI claims can comprise: (i) return of premium paid; (ii) historic interest on the premium paid; and (iii) compensatory interest/payment. Are the proceeds of a PPI claim a "repayment"? To my mind, something can only be a *re*payment, if it were paid over (or charged to an account) in the first place. If this is the case, then I suggest that it follows that only the return of the premium and any interest paid is a "repayment" and thus available under the Protocol STC to the creditor for set-off. I do not believe that the creditor can claim – at least not under the Protocol STC – to set off any compensatory payment against any monies owed to it.

Set-off and the R3 STC

Interestingly, R3 STC's clause 79 is comparable to the Protocol STC's clause 17(6), but it restricts set-off only for repayments due to HMRC. Thus, that clause is not relevant for PPI claims. However, R3's STC apply S324 of the Insolvency Act 1986 to IVAs at clause 7. It appears to me that this clause gives creditors a strong argument for setting off PPI refunds against any outstanding IVA debt, although the application of, and case law surrounding, the statutory set-off rules make me sufficiently nervous to suggest a "seek legal advice" approach.

What if it is likely that there will be no surplus after set-off?

Even if set-off is likely, I struggle to see how a Supervisor can adjudicate on claims without taking the possibility of mis-sold PPI into consideration. Of course, not all PPI policies have been mis-sold and I believe it would be professional of an IP to make enquiries of the debtor and take a balanced and reasonable view on the evidence as to whether the policy was mis-sold and thus whether it would be time well-spent to pursue a claim.

Does the IP need to go through the process of lodging a complaint with the PPI provider to agree the claim? If the Supervisor is satisfied that the PPI adjustment will not generate an actual realisation for the IVA, might it be possible for the Supervisor simply to adjudicate on the claim, take account of the apparent mis-sold PPI policy, admit only the remainder of the claim, and deal with any appeal from the creditor in the usual manner? That might be a risky approach and I appreciate that the calculation of a PPI refund is complex, but the alternative approach – incurring costs to agree a PPI refund that generates no real cash for the estate – seems to me to give rise to other considerations.

Adjudicating claims is a clear responsibility of Supervisors and other insolvency office-holders where a dividend is intended. It is generally acceptable to incur costs, payable from the insolvent estate, in this exercise. True, discharging costs of the adjudication process will

reduce the “pot” available for dividend, but it likely will also reduce the total creditors’ claims ranking for dividend and, more importantly I think, it results in a fair dividend. I understand that some PPI refunds can be substantial sums, so the resultant percentage charge of any claims management company in pursuing large claims will be significant and payable in full from the IVA funds. Whilst I do not believe that this downside calls into question the appropriateness of properly adjudicating claims, I suspect that it may create a perception with some that IVA funds are being used unnecessarily. I believe therefore that IPs would be wise to reflect on the Insolvency Ethics Code’s principles on obtaining specialist advice and services (paragraphs 53 to 56) and they may want to add some explanation to reports of the justification for such costs.

What happens to the tax liability arising from the interest payment?

If the PPI refund includes compensatory interest, this may give rise to a tax liability, depending on whether the PPI provider has deducted tax and/or depending on whether the debtor is a basic or higher rate tax-payer.

The Protocol STC cover “tax liabilities arising on realisations” at clause 28 (and R3 STC’s clause 82 has similar wording): “if you have taxation liabilities arising on the sale or other realisation of any asset subject to the arrangement, you must meet them out of the proceeds of that sale, as far as those proceeds are sufficient”. The STC refer to proceeds of ***sale***, which seems to me to be a drafting error (it is obvious what scenarios the drafter had in mind) – whether this can be relied upon to enable the Supervisor to pass to the debtor sufficient funds to discharge the tax liability on the compensatory interest, I cannot say, but I get the sense that the major creditors/agents in consumer IVAs are taking a fair and reasonable approach to PPI refunds, so I would be surprised if they would challenge this… but I think it would be very useful to IPs in general if they issued something in writing on this.

However, as I see it, it is likely that the compensatory interest will fall into two categories: interest relating to the period pre-IVA and that post-IVA. Therefore, I would have thought that a portion of the tax liability arising from the compensatory interest is likely to fall as HMRC’s claim in the IVA (note: Protocol and R3 STCs include in HMRC’s IVA claim the tax relating to the tax year in which the IVA was approved). But does clause 28 override this so that ***all*** the tax liability, pre- and post-IVA, is discharged from the realisation? It seems so to me (provided the drafting error is not fatal).

I would hope that a sense of fairness would prevail so that, whatever happens, the debtor is not left with a tax liability (and for that matter, the charges of any claims management company, provided the debtor has not seriously gone out on a limb) to be paid outside of the Arrangement where the benefit of the PPI refund has been passed on solely to the IVA.

Could the debtor or IP (as advising member) be considered at fault for not disclosing the PPI claim as an asset in the Proposal?

Before the mis-sold PPI story broke, I do not believe that anyone could be blamed for assuming that PPI premiums had been charged appropriately. However, I would hope that IPs are now wise to the situation and take the possibility of mis-sold PPI policies into consideration when advising debtors and preparing IVA documents.

How far does a debtor/IP need to go in establishing a claim at this stage? SIP3 paragraph 4(b) states that “the member should take steps to satisfy himself that the value of the assets is appropriately reflected in the statement of affairs. Where the value of an asset is material to the outcome of the arrangement consideration should be given to obtaining corroborative evidence as to its value”. Of course, the application of SIPs rests with the IP’s authorising

body, but I suggest that we have all lived with the concept of estimated asset realisations for long enough to be able to provide sufficient information in Statements of Affairs or similar to enable readers to understand the position reasonably.

Conclusion

I should reiterate that the above are my own opinions, albeit that I have been helped in reasoning on this by a number of IPs. Therefore, readers should not rely on any of the above, but should consider seeking their own legal advice. However, I do hope that this helps to highlight some of the issues and perhaps move the arguments on.

Although it would be a challenge for the regulators/R3 to issue guidance on this topic, the Paymex VAT decision experience proves that it can work, but that it is really only useful if the guidance is issued quickly.

In the meantime, IPs will have to make their own decisions. I have heard stories of debtors handing over surprise cheques to Supervisors, having pursued a PPI refund on their own. I believe that this does not mean that Supervisors need not check that the monies are due to the IVA – if it is not an included asset, then the debtor could use it to propose a full and final settlement variation – nor should they disregard the effects of any recovery costs or tax liability arising for the debtor. Ethically, IPs should act with integrity and professionalism, but they will also wish to act prudently to avoid complaints or challenges down the line.

I now wonder whether this has been of any help at all! My aim is simply to attempt to move the story along a little – it is clear that there are still many uncertainties – and I hope that I have not written anything misleading; I will attempt to keep my ear to the ground and report any updates/changes. If anyone would like to email to me their thoughts (rather than make them public here), please feel free at insolvencyoracle@pobox.com.

* "Proposal" in this article may include any terms and conditions associated with the Proposal.

10. Government issues response to Bankruptcy Petition Reform consultation (10 October 2012)

"The Government has decided to take forward changes just to the process for dealing with debtor bankruptcy applications and has today included the measure as a proposed new clause in the Enterprise and Regulatory Reform Bill. Instead of applying to the court for a bankruptcy order, individuals will instead make a bankruptcy application to an Adjudicator, which would be a new office based within the Insolvency Service." (Jo Swinson MP, 9 October 2012)

The full response is available at:
http://www.bis.gov.uk/insolvency/Consultations/petition%20reform.