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CHARTERED ACCOUNTANTS

INSOLVENCY UPDATE

Introduction

Recent statistics from the registrar of companies show a 6% increase in the number of corporate insolvencies across Scotland and it is perhaps a reflection of this trend that the MR&Co insolvency team receive regular requests for advice regarding turnaround strategies and cash flow management. This may well indicate that business owners are keen to save their company if possible rather than allow it to fail. An encouraging sign for the economy.

Director disqualification : hard to believe!

A company in England called Exotic Global Limited "Exotic" was subject to liquidation in 2015. The liquidator's report resulted in The Insolvency Service "TIS" taking steps to disqualify the sole director Mr Al-Safee. As a result of the process, the court decided that a higher period of disqualification is warranted if a director pursues a defence which is patently untrue. In this case, TIS had sought a ten year period of disqualification, partly because the sole director had barely engaged either with the liquidator or with TIS in their subsequent investigation into his conduct. Further, the lack of accounting records meant that, inter alia, some questions could not be answered e.g. :

1. Why Exotic had not accounted for VAT on 14 expensive cars that had been imported.
2. If the 14 vehicles had been sold by Exotic or another entity, and on what basis.
3. How Exotic had accounted for the disposal of a further 45 cars and 2 cherished number plates.

A key part of the sole director's defence was his assertion that his passport had been stolen and he was the subject of identity theft. This was a curious stance because when he appeared in court, the liquidator identified the sole director as the person who had instructed him to liquidate the company. Equally oddly, the sole director declined to be cross-examined in court.

Unsurprisingly, the court found that the sole director was lying, had been involved with Exotic and further, that his lies could be construed as an attempt to pervert the course of justice. At a subsequent Hearing which the sole director declined to attend, he was disqualified from acting as director for a total period of 13 years.

General Data Protection Regulations "GDPR"

The various insolvency bodies have been asked to clarify various issues relating to GDPR when an insolvency practitioner becomes involved. For example, what sort of warranties might be appropriate if a company is liquidated and the liquidator wishes to sell a mail order activity as soon as possible? Immediately after appointment, issues might arise such as :

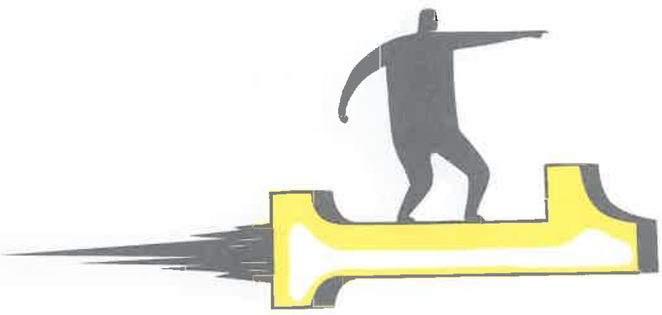
- what steps might be required if the liquidator wishes to continue trading?
- how does he respond to a subject access request from an employee?
- what happens if company mobiles/laptops are lost either just before or just after appointment?
- who is responsible if the company is penalised by the information commission officer?

In addition to GDPR, a business has to comply with a plethora of legislation such as the money laundering regulations, health & safety issues, employment law and environmental concerns. It is fair to say that any insolvency practitioner appointed to deal with a failed business cannot hope to deliver a perfect solution because, by the very nature of the fact that the business has run out of cash, it is not unreasonable to suppose that adherence to all regulations/laws has been somewhat lax and considered low priority.

Clearly, the use of checklists, legislation updates and experience will all play their part in the liquidator trying to exercise appropriate control in the short-term and the general view is that GDPR will simply impose an additional layer of cost to the average insolvency process without a commensurate benefit to all stakeholder groups. Time will tell.

Competition, but on a level playing field

Whilst it must be acknowledged that competition is healthy in terms of promoting efficiency and effectiveness at a fair price, many licensed insolvency practitioners "IPs" find that it can be difficult to work in an arena where some competitors are unregulated. Unregulated operators will often secure work by quoting low fees (typically paid in advance by service users with little opportunity to complain at a later date!) which annoys IPs across the UK because the strict legal and



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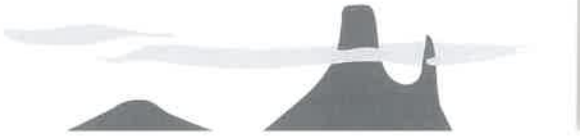

regulatory framework applicable to them requires a high degree of skill, experience and diligence. Complaining about an unregulated advisor can be seen as sour grapes but the reality is that if something goes wrong, who is prepared to correct the problem?

IPs are often heard to comment about the frustration of unlicensed advisors who offer solutions that are simply not available and further, seek fees and personal guarantees to cover all sorts of costs that are unnecessary.

When financial difficulties emerge and, for example, court recovery action is taken by creditors, unregulated advisors often seize the opportunity to send a letter to worried directors suggesting that they should be wary of any advice from a licensed IP, that the IP only acts for the creditors, or that a route is available to allow a business to continue trading with the same assets yet write-off all debts without any repercussions. False promises. The lesson is simply that if someone turns to an unregulated advisor and things go wrong, remember the old adage of " you get what you pay for ".

The role of the responsible director

In 2017, ICAS produced a guide for directors of private companies in order to help identify key statutory duties and responsibilities, together with the expectations of a director and non-executive director from both the board and shareholders. The vast majority of companies operate in a perfectly normal and successful manner, but it is quite understandable that every director might not have the same level of training and experience. The ICAS guide includes information about how to deal with situations where one is presented with bribery, corruption or ethical issues, the difference between statutory and operational duties, and looks at some difficulties which can emerge if a business is facing challenging times e.g. wrongful trading, misconduct, disqualification and where to seek advice.

Being a director can be a most rewarding and satisfying experience but, for smaller companies with perhaps only one or two directors, life can be lonely at the top which means that practical and independent guidance is always welcome.

The full publication can be accessed at www.icas.com, and typing "Guidance for Directors of Private Companies" in the search section.

Well worth a read.

Equity release time bomb?

A recent media article suggested that a negative equity time bomb is unlikely to create a problem for British banks as baby boomers unlock unprecedented sums of cash from their homes in equity release schemes at ever-younger ages. The article indicates that borrowers aged between 55 and 64 comprised nearly 15% of the mortgage market, double the level in 2015.

Traditionally, such loans were given to pensioners to help fund retirement costs on the basis that the house would be sold at date of death in order to repay the borrowing, but working-age households have now become major borrowers, with about £900 million of equity being released from UK homes each quarter.

Further, research by Moody's suggests that nearly one in five mortgages are interest-only. This creates the worry that any decline in property values, which could happen if interest rates increase and/or borrowing becomes more difficult, will generate negative equity for people who have reached an age where it will be almost impossible to create further income to deal with the problem.

You scratch my back and ....

The insolvency code of ethics makes it perfectly clear that it is inappropriate to pay for an insolvency introduction. Thus, any licensed IP who becomes involved in this activity should be reported to his licensing body. Various methods of rewarding an introducer of business have been seen by the MR&Co insolvency team over the years : some more creative than others.

For the avoidance of doubt, it is perfectly permissible to pay an introducing accountant to complete a set of accounts or a tax return in order to finalise a financial position as at date of liquidation because that will invariably prove to be a cheaper way of achieving such result and hence enhancing dividend prospects for the general body of creditors. Paying an introductory fee, howsoever disguised, is wrong and MR&Co does not condone such activity.

Conclusion

This Update is provided for general interest purposes and does not purport to offer definitive advice. Please contact either Michael J M Reid (reidm@mestonreid.com or Michelle Byrne (byrnem@mestonreid.com) if you wish to discuss anything raised herein.

Thank you for taking the time to read this Update and feel free to pass it to anyone who you think might be interested in reading it.

If you wish to be removed from the Update mailing list, please contact us at (ryriel@mestonreid.com).

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