INSOLVENCY UPDATE

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Introduction

The last Update referred to the media frenzy about Brexit and, since then, it has become a fevered obsession for many. It is disappointing to witness the turmoil because many commentators had suggested that the North East economy was beginning to settle into a gentle upward pattern, with capital expenditure becoming more prevalent and employment opportunities increasing. Nothing stays either settled or predictable for long.

Of course, a weak Pound provides some benefit to the Aberdeen petro-economy and if the Pound reaches parity with the Dollar it may be that one will see more investment in the North Sea because of the comparative cost-effectiveness of doing so. An unexpected benefit of the chaotic Brexit situation!

The demise of the personal service company "PSC"?

There has been much comment in recent months about the change in legislation in April 2020 which is forecast to see the majority of PSCs disappear as a result of the large oil & gas companies transferring people to a staff position : like it or not.

One can understand that the risk to large operators is high if many PSCs simply fail to pay tax on earnings to HMRC and leave the operators to pay the tax bill, even when the PSC invoice had been paid gross. Other than a cash flow disadvantage to many PSCs because corporation tax will be deducted/remitted long before the normal due date for a limited company, some service providers may still wish to shelter some income at 20% and decide when it is appropriate to extract the balance of cash.

That said, recent labour party pronouncements about the wish to either remove or restrict Entrepreneur's Relief if they are in power may also suggest that a PSC's days may be numbered. After all, why would a PSC wait to see if there is a further change in legislation that would jeopardise the opportunity for income to be taxed at 10%?

Further, a solvent liquidation can often provide a helpful mechanism to deal with a large overdrawn loan account in a tax efficient way.

The Meston Reid & Co insolvency team are alert to the possibility of a rise in PSC solvent liquidations as people seek to avail themselves of the current system whilst it remains benign. We are fit to cope.

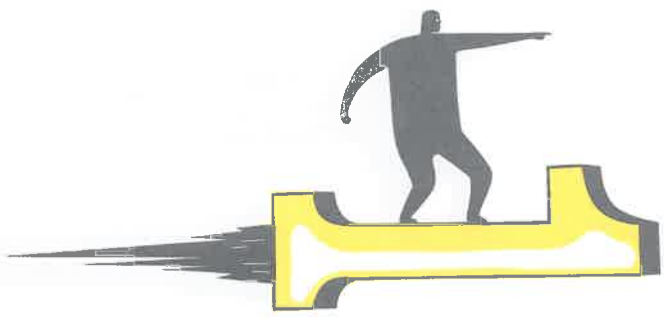
Changing the legislation to benefit HMRC

Since September 2003, HMRC have not had their previous preference for dividend purposes when a liquidator distributes the cash. However, the July 2019 draft Finance Bill sought to restore HMRC priority for certain tax debts in all formal insolvencies from April 2020. In summary, HMRC consider that Crown preference should apply to PAYE, employee national insurance and VAT. It is understood that the thinking behind the proposal is that these monies are effectively held in trust for a third party e.g. HMRC, and should have priority over unsecured creditors and, crucially, the holder of a floating charge such as a bank or invoice factor.

A supplier of cash such as a bank can turn off the supply immediately, as can the person supplying goods/services to a company. HMRC are an involuntary creditor and, unless legislation is enacted which makes taxes held on trust a personal liability of the directors, it is hard to see how HMRC can be blamed for being annoyed that a company is using "their money" to run the business rather than pay HMRC, particularly when no request is made to do so by the business.

Holders of floating charges are understandably concerned that if the proposals become law, the likely level of recovery for them will be diminished significantly. The question is whether this will lead to more aggressive monitoring from the holder of a floating charge or perhaps a more stringent attitude to lending in the first place : both stances being seen as detrimental to the ability of a business seeking working capital to run a business.

The policy analysis by the UK Government suggests a relatively small tax boost of less than £195 million per year but then again, does HMRC see itself as part of the Exchequer or merely a means of collecting cash to provide to the Chancellor and his team? A subtle difference perhaps, but important to the overall argument.



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The UK insolvency trade body R3 has mounted a campaign seeking to persuade HMRC to change their stance and time will tell how this situation will evolve.

How much do I have to pay my trustee each month?

When an individual is submitting a sequestration application to the accountant in bankruptcy "aib", one of the key issues is what should be paid as a regular contribution to the trustee. This tends to be calculated by use of the Common Financial Tool, now known as the Common Financial Statement "CFS", which is accessible by accredited money advisors and designed to reflect a typical person's lifestyle based upon whatever earnings are disclosed. For example, a person cannot advise of a net monthly salary of £2,000 and claim to pay £800 for food. This is because the CFS has trigger figures which permit a reasonable range within an expense category whilst attempting to be fair. As with the expenditure analysis contained in the sequestration application, the CFS offers an individual a wide-range of expenditure items to consider because the aib recognises that everyone has a different lifestyle and, for example, the cost of cigarettes is an allowable expense (up to a reasonable limit) because it cannot be denied that some people smoke.

The level of contribution tends to be the arithmetical difference shown on the CFS between net income and stated outgoings, unless there is an unusual reason for a different outcome. Many individuals approach the CFS on the basis that the arithmetical difference is a basis for negotiation with the aib regarding a monthly contribution, but the reality is that the aib will seek the full sum, or decline to process the application.
If the application is not processed the individual does not benefit from the protection of sequestration and remains pressured by other creditors. Thus, whilst it must be remembered that a contribution is payable for a four year period, subject to the ongoing ability to pay and changing circumstances, suitable care must be exercised when the individual is completing the CFS with the accredited money advisor e.g. Meston Reid & Co.

Keeping an eye on insolvency practitioners

As one might expect, regulation of insolvency practitioners "IPs" is fairly rigorous because of the trust reposed in them by all stakeholder groups in a distressed situation. The Government, in the form of The Insolvency Service, has issued a call for evidence which aims to gather views from all stakeholder groups on the current regulatory framework for insolvency practitioners. Currently, there are relatively few insolvency practitioners in the UK who accept appointments yet an IP licence can be obtained from :

- The Institute of Chartered Accountants of Scotland
- The Institute of Chartered Accountants in England and Wales
- The Insolvency Practitioners Association
- The Chartered Accountants of Ireland
- The Association of Chartered Certified Accountants

According to The Insolvency Service consultation document, ICAS regulates 74 appointment-taking IPs which is less than 6% of the UK total. Will the ICAS role disappear?

One of the suggestions is the creation of a single regulator which one can accept is an understandable objective from the Government's viewpoint, because it is always easier to obtain feedback from one regulator rather than five. It is not clear what the catalyst was to encourage a review, although the consultation document makes frequent reference to "a high quality service at a fair and reasonable cost". A perfectly laudable objective, but with increasing legal requirements for the IP to follow, it is difficult to undertake every task expected by stakeholder groups.

The call for evidence deadline is 4 October and if anyone wishes further information on this topic please refer to https:www.gov.uk/government/consultations/call-for-evidence-regulation-of-insolvency-practitioners-review-of-current-regulatory-landscape.

GDPR

The names and addresses contained on our Insolvency Update database are used only for this communication. If any reader wishes to be removed from such database, please e-mail ryriel@mestonreid.com .

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.

Meston Reid & Co