



Corporate Turnaround and Insolvency

Focus on IPs: a summary of recent legal changes

This update focusses on a range of issues affecting IPs from the past two months, covering the consultation on fees announced in February, the HMRC announced changes to the VAT deregistration regime, when accountants may be required to produce documents under Sections 235 and 256 of the Insolvency Act, and a recent Court of Appeal decision on when a company may be considered to be insolvent for the purpose of Section 238 actions

Consultation on the regulation of Insolvency Practitioners and IPs' fees

Readers will be aware that on 17 February, the Government published a **consultation** in two parts focussing on (i) the regulation of IPs and (ii) the charging and monitoring of IPs' fees.

From a licensing point of view, the objectives appear to be to reduce the number of RPBs, to introduce common sanctions and a common complaints gateway, and to provide for oversight of RPBs by The Insolvency Service. On the last point, it is proposed that TIS would have power (amongst other things) to direct RPBs to take steps, to impose financial penalties on RPBs for failures in their functions, to publish statements censuring RPBs, and to ask the court to sanction IPs directly in appropriate circumstances.

On more concern across the industry are the proposals concerning IPs' fees (paras 88 to 129 of the consultation). The headline proposal seems to be that IPs would be prevented from charging on a time cost bases **except** where (i) there is a creditors' committee; (ii) the secured creditor will not be paid in full; or (iii), in cases concerning CVAs, IVAs and MVLs. In all other cases it is proposed that fees be charged either as a fixed fee or as a percentage of realisations. In addition, a regulatory objective proposed to ensure that IPs' fees represent value for money.

The proposals obviously present a number of serious questions and challenges and raises concerns across the entire industry.

The consultation closed on 28 March and we will report further once the Government publishes the responses and any further revised proposals.

Changes to deregistering insolvent business for VAT

On 6 April HMRC **announced** that it will extend the registration of insolvent business until after all trading has ceased and assets have been realised. IPs will have therefore to file VAT returns until trading/asset realisation ceases, although those businesses trading at revenue levels below the VAT registration threshold will still be able to apply for deregistration on that ground.

The concern from HMRC appears to be that it has received advice that deregistered business can no longer issue valid VAT invoices or reclaim input tax based on defunct VAT numbers. As a result HMRC will no longer allow early deregistration on grounds of insolvency alone.

This decision will be welcomed by fixed charge receivers in particular, who are often at the mercy of subsequently appointed liquidators maintaining VAT registrations (and on the good graces of the local HMRC office in allowing them to reclaim VAT). Whether HMRC will issue guidance on the ability of receivers to formally reclaim VAT remains to be seen.

Can accountants be required to produce documents under Sections 235 and 236 of IA 1986?

The recent High Court decision in *Re Acolisia Ltd* (10/04/2014) saw a firm of accountants being ordered to produce documents detailing its dealings with an insolvent company, where it was clear that there was relatively little information in the company's own accounting records.

Specifically, the liquidator sought information concerning various tax issues, to which the accountants responded that they had not advised on tax issues and so objected to the request under Section 235. Upon the liquidator's subsequent

application for production of the documents under Section 236, the court ruled that the information was required to hold the liquidator reconstitute a company's records, that lack of information justified the application, and that the amount of work involved was no unreasonable or oppressive.

Whilst the decision is unremarkable of itself, in light of the recent challenges in the Tchenguiz claims against the SFO and others, it should be borne in mind that this is yet another potential avenue under which insolvent entities may seek disclosure of information from their former advisers.

Point of insolvency for Section 238 actions

The recent decision in *Re Casa Estates (U) Ltd (03/04/2014)* raises a further point in relation to the Eurosail debate on balance sheet insolvency recently determined by the Supreme Court.

In this case, a Mrs Bucci (connected with Casa Estates) had been the subject of a Section 238 action to recover payments made to her by a company in liquidation. The county court judge decided that although the transactions **were** at an undervalue, the company was not cash flow insolvent until a later date when it passed the "point of no return" (a formulation later overturned in *Eurosail*). On appeal, the High Court ruled that the company was only meeting its liabilities through incurring further borrowings. As a result, there was no evidence to rebut the presumption of insolvency (as burden of proof is reversed with transactions to connected parties) or to show that the company would **ever** be able to meet its liabilities. Therefore the company was balance sheet insolvent at the time of the payments.

The Court of Appeal agreed with the High Court and said that even when applying the "cashflow" test of insolvency, it was still possible for a company to be balance sheet insolvent even whilst solvent on a cashflow basis. In any event, on any commercial view the company had been balance sheet insolvent even whilst continuing to pay its debts, and it was appropriate (in certain instances) for the court to question **how** those debts were being met.

This decision serves as a useful affirmation of *Eurosail* principles and a timely reminder that there is a presumption of insolvency where transactions at an undervalue are made in favour of connected parties.

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